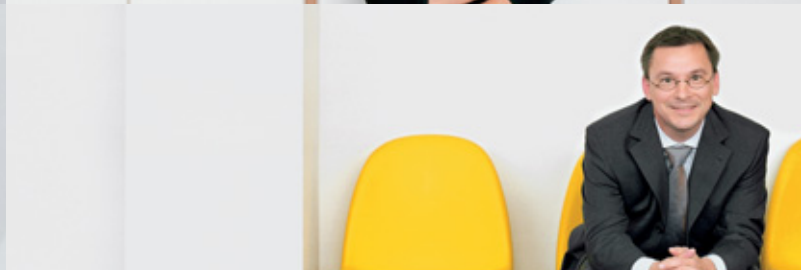


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LANXESS AG BALANCE SHEET

	Note	Dec. 31, 2004	Dec. 31, 2005
€ '000			
ASSETS			
Non-current assets	[8]		
Intangible assets			
Acquired concessions, industrial property rights, similar rights and assets, and licenses thereunder		0	29
Property, plant and equipment			
Furniture, fixtures and other equipment		23	17
Financial assets			
Investments in subsidiaries	[9]	738,839	738,839
Other loans		70	42
		738,932	738,927
Current assets			
Receivables and other assets			
Receivables from subsidiaries	[10]	283,136	1,193,153
Other assets	[11]	14,315	25,115
		297,451	1,218,268
Liquid assets		50	60,259
		297,501	1,278,527
Prepaid expenses		2,045	917
Total assets		1,038,478	2,018,371
STOCKHOLDERS' EQUITY AND LIABILITIES			
Stockholders' equity	[12]		
Capital stock		73,034	84,621
Capital reserves		763,267	804,777
Balance sheet profit (2004: balance sheet loss)		(1,738)	0
		834,563	889,398
Provisions			
Provisions for pensions and other post-employment benefits	[13]	2,757	6,713
Other provisions	[14]	1,158	10,931
		3,915	17,644
Liabilities			
Liabilities to banks	[15]	0	155,817
Trade payables	[16]	0	2,470
Payables to subsidiaries	[17]	0	946,167
Other liabilities	[18]	200,000	6,875
		200,000	1,111,329
Total stockholders' equity and liabilities		1,038,478	2,018,371
Contingent liabilities from guarantees	[19]	0	535,370

LANXESS AG INCOME STATEMENT

	Note	2004	2005
€ '000			
Sales	[1]	4,787	33,589
Cost of sales	[2]	(4,787)	(33,589)
Gross profit		0	0
General administration expenses		0	(6,232)
Other operating income		0	1,855
Other operating expenses		(34)	(1,916)
Operating result		(34)	(6,293)
Income (loss) from investments in affiliated companies – net		0	(118,365)
Interest income (expense) – net	[3]	(1,874)	2,379
Other financial income and expenses – net	[4]	172	(33,760)
Financial result		(1,702)	(149,746)
Loss before income taxes/net loss		(1,736)	(156,039)
Loss carried forward from previous year		(2)	(1,738)
Withdrawal from capital reserves		0	157,777
Balance sheet profit (2004: balance sheet loss)		(1,738)	0

NOTES TO THE FINANCIAL STATEMENTS OF LANXESS AKTIENGESELLSCHAFT, LEVERKUSEN, FOR FISCAL 2005

General Under the Spin-Off and Acquisition Agreement notarized on September 22, 2004, Bayer AG, as the transferring entity, transferred all the shares of LANXESS Deutschland GmbH and other portions of its assets and liabilities to LANXESS AG, as the acquiring entity, by means of a spin-off pursuant to Article 123 paragraph 2 No. 1 of the German Transformation Act (UmwG). The spin-off was based on the closing balance sheet of Bayer AG as of June 30, 2004. The assets and liabilities transferred were valued at the net carrying amounts recorded by the transferring entity. As far as the relationship between Bayer AG and LANXESS AG is concerned, the transfer took place with economic effect from July 1, 2004. As of that date, all business relating to the assets of Bayer AG to be spun-off was deemed to be undertaken for the account of LANXESS AG.

The Spin-Off and Acquisition Agreement between Bayer AG and LANXESS AG, which formed the basis for this transaction, was approved by a stockholders' meeting of Bayer AG on November 17, 2004 and by a stockholders' meeting of LANXESS AG on December 21, 2004. The spin-off took effect when it was entered in the Commercial Register for Bayer AG on January 28, 2005. On this date, 73,034,192 no-par bearer shares in LANXESS AG were issued to the stockholders of Bayer AG, bringing to an end Bayer AG's majority ownership of LANXESS AG.

The income statement for 2004 thus reflects the business activities from July 1, 2004. Accordingly, the income statement for fiscal 2005 is not comparable with that for 2004.

The Board of Management and Supervisory Board have issued a Declaration of Compliance with the German Corporate Governance Code pursuant to Article 161 of the German Stock Corporation Act (AktG). This declaration has been made available to the stockholders and the English version can be viewed at any time at www.lanxess.com, Investor Relations, Corporate Governance.

Accounting Policies The financial statements of LANXESS AG are prepared in accordance with the provisions of the German Commercial Code (HGB) and the Stock Corporation Act (AktG) applicable to large stock corporations.

To enhance clarity, certain items in the income statement and balance sheet are combined, as explained in the Notes.

The income statement is drawn up by the cost-of-sales method.

Financial income and expenses whose disclosure is not covered by a mandatory item are stated under other financial income or expenses.

LANXESS AG prepared consolidated financial statements for the LANXESS Group as of December 31, 2005. The recognition and valuation principles used in those statements are at variance with German GAAP in the following material respects:

- Goodwill is not amortized. Instead it is tested for impairment at least once a year if it relates to a business combination effected on or after March 31, 2004.
- Financial instruments are measured at fair value.
- Foreign currency receivables and payables are translated at the respective closing rates on the reporting date, the resulting differences being recognized in income.
- Pension provisions are computed by the projected unit credit method, taking into account future increases in remuneration and pensions.
- Provisions are only recorded for liabilities to third parties.
- Other provisions are not recorded if the probability of utilization is less than 50%.
- Deferred taxes are recognized using the balance sheet liability method, including recognition of deferred taxes on loss carryforwards where utilization of the loss carryforwards is sufficiently probable.

Recognition and Valuation Principles Intangible assets that have been acquired are recognized at cost and amortized on a straight-line basis over their estimated useful lives.

Property, plant and equipment is carried at the cost of acquisition. Assets subject to depletion are depreciated. Write-downs are made for any declines in value that go beyond the depletion reflected in depreciation and are expected to be permanent. Low-value assets are fully depreciated in the year of acquisition. Where permitted under the tax laws, depreciation is made by the declining-balance method at the highest rates possible, switching to the straight-line method as soon as this leads to higher depreciation. Useful lives of intangible assets, property, plant and equipment:

Software licenses	3 to 4 years
Computer equipment	3 to 4 years
Furniture and fixtures	4 to 10 years

Investments in affiliated companies are recognized at cost of acquisition.

Loans receivable that are interest-free or bear low rates of interest are carried at present value; other loans receivable are carried at nominal value.

Receivables and other assets are stated at nominal value, less any necessary write-downs.

Provisions for pensions and other post-employment benefits are computed by the actuarial method set out in Article 6a of the German Income Tax Act (EstG) using the mortality tables according to K. Heubeck 2005 G and a discount rate of 6%.

Other provisions are established to cover all foreseeable risks and uncertain liabilities, based on reasonable estimates of such commitments as of the closing date.

Liabilities are stated at nominal value.

Income and expenses are accrued in the fiscal year.

Foreign currency receivables and payables are translated at the rates at which they were initially recorded or at the current year's closing rates, whichever yields the lower amounts for receivables or the higher amounts for payables. Foreign currency receivables and payables that are hedged are translated at the rates applicable on the recording dates or at the hedged rates.

Contingent liabilities arising from sureties and debt guarantees are shown at the amounts equivalent to the loans or commitments actually outstanding on the reporting date.

Notes to the Income Statement

(1) Sales Sales revenues total €33,589,000 (2004: €4,787,000) and relate entirely to services provided to LANXESS Deutschland GmbH in Germany.

(2) Cost of sales The cost of sales totaling €33,589,000 (2004: €4,787,000) comprises expenses relating to the services provided, mainly personnel and general administration expenses.

(3) Interest income (expense) – net

Interest income (expense) – net	2004	2005
€ '000		
Other interest and similar income		
from third parties	94	1,136
from subsidiaries	2,207	36,617
	2,301	37,753
Interest and similar expenses		
to third parties	4,175	19,931
to subsidiaries	0	15,443
	4,175	35,374
Interest income (expense) – net	(1,874)	2,379

(4) Other financial income (expenses) – net

Other financial income (expenses) – net	2004	2005
€ '000		
Other financial expenses		
Expenses for commodity swaps	0	16,295
Exchange losses	15,578	152,591
Miscellaneous other financial expenses	116	38,666
	15,694	207,552
Other financial income		
Income from commodity swaps	0	16,295
Exchange gains	15,866	157,175
Miscellaneous other financial income	0	322
	15,866	173,792
	172	(33,760)

Miscellaneous other financial expenses include the costs for the early repurchase and resale of the mandatory convertible bond and commission expenses for guarantees provided to subsidiaries. Miscellaneous other financial income contains commission payments for guarantees granted by subsidiaries.

(5) Personnel expenses

Personnel expenses	2004	2005
€ '000		
Wages and salaries	3,359	17,012
Social expenses for pensions and other benefits	1,124	3,626
of which for pensions	[737]	[2,568]
	4,483	20,638

(6) Number of employees

Number of employees	Average 2005	Closing date Dec. 31, 2004	Closing date Dec. 31, 2005
General administration	102	98	106

(7) Audit fees The following fees for the services of the auditors PricewaterhouseCoopers Aktiengesellschaft, Wirtschaftsprüfungsgesellschaft, were recorded as expenses in fiscal 2005:

Audit fees	2005
€ '000	
Financial statements auditing	413
Audit-related services and other audit work	597
	1,010

Notes to the Balance Sheet

(8) Non-current assets A breakdown of non-current assets and the changes in them during the year is shown in the statement of changes in non-current assets.

(9) Overview of shareholdings pursuant to Article 285 paragraph 11 German Commercial Code

Overview of shareholdings pursuant to Article 285 paragraph 11 German Commercial Code			
Company Name and Place of Business	Interest in %	Equity as of Dec. 31, 2005 € '000	Net income (loss) 2005 € '000
LANXESS Deutschland GmbH Leverkusen, Germany	100.0	1,253,862	0*

* A profit transfer agreement exists with LANXESS Deutschland GmbH, Leverkusen, Germany.

(10) Receivables from subsidiaries Receivables from Group companies totaling €1,193,153,000 (2004: €283,136,000) comprise short-term loans receivable, including accrued interest, and receivables from financial transactions.

All receivables are due within one year.

(11) Other assets Other assets of €25,115,000 (2004: €14,315,000) mainly comprise claims for sales tax refunds for December 2005 (€16,019,000) and option premiums paid (€6,012,000). Of the latter amount, €2,368,000 (2004: €0) relates to options with remaining terms exceeding one year.

(12) Stockholders' equity The stockholders' equity changed as follows in 2005:

Stockholders' equity					
€ '000	Dec. 31, 2004	Contributions from the exercise of the convertible bond	Net loss for the year	Withdrawal from capital reserves	Dec. 31, 2005
Capital stock	73,034	11,587			84,621
Capital reserves	763,267	199,287		157,777	804,777
Balance sheet loss	1,738		156,039	(157,777)	0
	834,563	210,874	156,039	0	889,398

The capital stock of LANXESS AG is divided into 84,620,670 no-par bearer shares of a single class.

At the Extraordinary Stockholders' Meeting of LANXESS AG on September 15, 2004 the Management Board was authorized until August 30, 2009 to increase the company's capital stock, with the approval of the Supervisory Board, by issuing new no-par

shares against cash or non-cash contributions by a total of €36,517,096 on one or more occasions (authorized capital). This resolution on authorized capital was entered in the Commercial Register on February 25, 2005. Stockholders essentially have to be granted subscription rights to any authorized capital issued. However, with the approval of the Supervisory Board, the Management Board is authorized to exclude subscription rights for stockholders in certain circumstances.

The Annual Stockholders' Meeting on June 16, 2005 authorized an increase of up to €20,000,000 in the capital stock. This conditional capital increase was used to grant shares to holders of the convertible bond issued by LANXESS AG under a resolution adopted at the Stockholders' Meeting of September 15, 2004. The holders of the convertible bond exercised their conversion rights on July 20, 2005 and received 11,586,478 no-par bearer shares. The new shares were issued at a price of €18.20 per share. They are entitled to any dividend payments from January 1, 2005. Accordingly, the capital stock increased by €11,586,478 from €73,034,192 to €84,620,670 and the capital reserves increased by €199,287,421 to €962,553,629. The capital increase was entered in the Commercial Register on February 2, 2006 following notification by the Board of Management pursuant to the provisions of the German Stock Corporation Act. The purpose of the contingent capital was extinguished upon exercise of the subscription rights relating to all convertible bonds.

€157,777,000 was withdrawn from capital reserves to offset the net loss for the year and the loss carried forward from the previous year.

(13) Provisions for pensions and other post-employment benefits Pension provisions relate to pension obligations for present employees and commitments under early retirement programs.

(14) Other provisions The other provisions are established for vacation and overtime credits, the part-time working program for older employees, long-service anniversaries, bonuses and other uncertain liabilities.

(15) Liabilities to banks Liabilities to banks total €155,817,000 (2004: €0) and include €125,685,000 in short-term borrowings and €30,132,000 for a promissory loan; both amounts include accrued interest.

Of these liabilities, an amount of €125,817,000 is due in 2006 and an amount of €30,000,000 is due in 2012.

(16) Trade payables All trade payables are to third parties and mature within one year.

(17) Payables to subsidiaries Payables to subsidiaries amounting to €946,167,000 (2004: €0) mainly comprise short-term loans, including accrued interest, and receivables relating to financial transactions. Also reflected here is the liability relating to the assumption of the loss at LANXESS Deutschland GmbH (€118,365,000).

All payables are due within one year.

(18) Liabilities

Liabilities	Dec. 31, 2004	Dec. 31, 2005
€ '000		
Option premiums received	0	6,012
Tax liabilities	0	308
Liabilities for social expenses	0	442
Others	200,000	113
	200,000	6,875

Of the total amount, €4,507,000 is due in 2006. Option premiums totaling €2,368,000 relate to options with remaining terms exceeding one year but not exceeding five years.

(19) Contingent liabilities Under Article 133 paragraphs 1 and 3 of the German Transformation Act (UmwG), LANXESS AG is jointly and severally liable for obligations of Bayer AG incurred prior to the spin-off on January 28, 2005 if they are due within five years from the announcement of the entry of the spin-off in the Commercial Register for Bayer AG and the resulting claims against LANXESS are lodged in the correct legal form. The Spin-Off and Acquisition Agreement of September 22, 2004 specifies that LANXESS AG and Bayer AG shall each release the other party from all legally determined liability for obligations that the respective other party assumed as principal debtor under that Agreement. Further, in a master agreement concluded on the same date, LANXESS AG and Bayer AG agreed upon further arrangements on the general allocation of liability and on the allocation of specific liability of either party vis-à-vis the other party

for environmental contamination, antitrust violations and product liability in the relationship between them.

LANXESS AG has given the following guarantees to its subsidiaries:

Guarantees to subsidiaries	
€ '000	
to banks	25,114
to suppliers	10,256
to holders of the bond issued by LANXESS Finance B.V.	500,000
	535,370

(20) Other financial commitments Bayer AG offered stock incentive programs to all employees in the years 2000 to 2004. These comprised different offers for different employee groups. Participants in these programs have the opportunity to receive free Bayer AG shares over a period of up to ten years if they made an initial personal investment in the stock. The allocation of free shares to senior executives depends not only on retention periods but also on internal and external performance criteria which, if achieved, would trigger the corresponding financial commitments. Under the Spin-Off and Acquisition Agreement, such commitments relating to employees transferred to LANXESS AG in accordance with Article 613a paragraph 1 of the German Civil Code (BGB) were assigned to LANXESS AG.

Other Information

(21) Derivative financial instruments The notional value of financial derivatives contracts concluded with external counterparties was €1,611.9 million on December 31, 2005 (2004: €185.6 million). Opposite derivatives contracts with a notional value of €1,088.0 million (2004: €0 million) were concluded with Group companies. The notional value of derivative financial instruments totaled €2,699.9 million (2004: €185.6 million) on the closing date and comprised the following:

Derivative financial instruments	Dec. 31, 2004			Dec. 31, 2005		
	Notional value	Fair value	Carrying amount	Notional value	Fair value	Carrying amount
€ '000						
Forward rate contracts						
positive fair values	185,565	4,435	0	792,191	20,622	0
negative fair values	0	0	0	1,148,382	29,313	1,682
	185,565	4,435	0	1,940,573	(8,691)	(1,682)
Currency option contracts						
positive fair values	0	0	0	290,555	5,245	6,012
negative fair values	0	0	0	290,555	5,245	6,012
	0	0	0	581,110	0	0
Commodity contracts						
positive fair values	0	0	0	89,099	19,827	0
negative fair values	0	0	0	89,099	19,827	0
	0	0	0	178,198	0	0
	185,565	4,435	0	2,699,881	(8,691)	(1,682)

The notional value of forward rate contracts totaling €708,303,000 includes instruments with fair values of €20,263,000 passed through to other Group companies.

The currency option and commodity contracts concluded with external counterparties for the first time in 2005 were passed through to other Group companies via back-to-back transactions.

The fair values of forward contracts are derived from their trading or listed prices using the "forward method". Currency options are valued using an asset pricing model based on that of Black & Scholes. The fair values of commodity swaps are also derived from their trading or listed prices by the "forward method". If no market price is available, the value is determined using capital market pricing models.

Wherever possible, derivative financial instruments are valued in closed positions with the corresponding underlyings, so no valuation results had to be recognized. Option premiums paid and received totaled €6,012,000 and are recognized in other assets and other liabilities respectively as accounting units at cost of acquisition. Negative fair values totaling €1,682,000 relating to the remaining derivatives are reflected in miscellaneous provisions.

Total remuneration of the Board of Management and the Supervisory Board, advances and loans

In fiscal 2005 the members of the Supervisory Board received fixed remuneration totaling €580,403 from the company. There were no loans or advances to members of the Board of Management or the Supervisory Board on December 31, 2005 nor had any other financial commitments been entered into for these individuals.

Remuneration of the Board of Management in Fiscal 2005

€ '000	Fixed salary	Fringe benefits	Bonus	Total
Dr. Axel C. Heitmann	592	46	820	1,458
Dr. Ulrich Koemm	469	22	643	1,134
Dr. Martin Wienkenhöver	393	29	396	818
Matthias Zachert	400	20	403	823
Total	1,854	117	2,262	4,233

Corporate Officers

Supervisory Board Members of the Supervisory Board hold or held offices as members of the supervisory board or a comparable supervising body of the corporations listed (as of February 28, 2006 or the date on which they ceased to be members of the Supervisory Board of LANXESS AG):

The following gentlemen were members of the Supervisory Board until January 28, 2005:

Klaus Kühn Chairman of the Supervisory Board
Mathematics graduate, Chief Financial Officer of Bayer AG

Dr. Roland Hartwig
Attorney at Law, Head of Legal and Patents at Bayer AG

Johannes Dietsch
Industrial business manager, Head of Finance at Bayer AG

The following gentlemen were appointed to the Supervisory Board effective January 29, 2005:

Dr. Rolf Stomberg Chairman of the Supervisory Board
Chairman of the Board of Directors of Management Consulting Group plc, London

Further positions:

- Member of the Supervisory Board of LANXESS Deutschland GmbH, Leverkusen
- 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, U.K.
- Member of the Board of Directors of Smith & Nephew plc, London, U.K.
- Member of the Supervisory Board of Reed Elsevier NV, Amsterdam, Netherlands
- Member of the Supervisory Board of TNT Post Group NV, Amsterdam, Netherlands

Dr. Friedrich Janssen Member of the Executive Board of E.ON Ruhrgas AG, Essen

Further positions:

- Member of the Supervisory Board of LANXESS Deutschland GmbH, Leverkusen
- Member of the Supervisory Board of Gerling Versicherungs-Beteiligungs AG, Cologne
- Member of the Supervisory Board of HDI Rechtschutz Versicherung AG, Hanover
- Member of the Supervisory Board of STEAG AG, Essen

- Further positions on the Supervisory Boards of subsidiaries of E.ON Ruhrgas AG, Essen
- Member of the Advisory Board of HDI Haftpflichtverband des Deutschen Industrie Versicherungsverein auf Gegenseitigkeit, Hanover

Rainer Laufs Self-employed consultant

Further positions:

- Member of the Supervisory Board of LANXESS Deutschland GmbH, Leverkusen
- Chairman of the Supervisory Board of WCM Beteiligungs- und Grundbesitz AG, Frankfurt am Main
- Member of the Supervisory Board of Klöckner Werke AG, Duisburg

Following completion of the statutory status procedure, the following gentlemen have been members of the Supervisory Board as stockholder representatives since March 10, 2005:

Dr. Jürgen F. Kammer Chairman of the Supervisory Board of Süd-Chemie AG, Munich

Further positions:

- Member of the Supervisory Board of LANXESS Deutschland GmbH, Leverkusen
- Member of the Supervisory Board of Villeroy & Boch AG, Mettlach
- Member of the Supervisory Board of Wittelsbacher Ausgleichsfonds, Munich

Robert J. Koehler Chairman of the Management Board of SGL Carbon AG, Wiesbaden

Further positions:

- Member of the Supervisory Board of LANXESS Deutschland GmbH, Leverkusen
- Chairman of the Supervisory Board of Benteler AG, Paderborn
- Member of the Supervisory Board of Pfeleiderer AG, Neumarkt
- Member of the Supervisory Board of AXA Versicherung AG, Cologne
- Member of the Supervisory Board of Heidelberger Druckmaschinen AG, Heidelberg

Lutz Lingnau Business administrator

Further positions:

- Member of the Supervisory Board of LANXESS Deutschland GmbH, Leverkusen
- Member of the Supervisory Board of Sirna Therapeutics Inc., San Francisco, U.S.A.
- Chairman of the Board of Directors of Medrad Inc., Indianola, Pennsylvania, U.S.A.
- Chairman of the Board of Directors of Intendis Inc., Montville, New Jersey, U.S.A.

Prof. h.c. (CHN) Dr. Ulrich Middelmann Vice Chairman of the Executive Board of ThyssenKrupp AG, Duisburg/Essen

Further positions:

- Member of the Supervisory Board of LANXESS Deutschland GmbH, Leverkusen
- Member of the Supervisory Board of RAG AG, Essen
- Chairman of the Advisory Board of Hoberg & Driesch GmbH, Düsseldorf
- Member of the Supervisory Board of E.ON Ruhrgas AG, Essen
- Further positions on the Supervisory Boards of subsidiaries of ThyssenKrupp AG, Duisburg/Essen

Dr. Sieghardt Rometsch Chairman of the Supervisory Board of HSBC Trinkaus & Burkhardt KGaA, Düsseldorf

Further positions:

- Member of the Supervisory Board of LANXESS Deutschland GmbH, Leverkusen
- Chairman of the Supervisory Board of APCOA Parking AG, Stuttgart
- Chairman of the Supervisory Board of Düsseldorf University Hospital, Düsseldorf
- Member of the Board of HSBC Private Banking Holdings (Suisse) SA, Geneva, Switzerland
- Member of the Supervisory Board of HSBC Bank Polska S.A., Warsaw, Poland
- Chairman of the Advisory Board of Management Partner GmbH, Stuttgart

The following employee representatives were appointed to the Supervisory Board by a decision of Cologne Local Court on March 14, 2005:

Gisela Seidel Chemical laboratory assistant

Further positions:

- Member of the Supervisory Board of LANXESS Deutschland GmbH, Leverkusen

Wolfgang Blossy District Secretary of the German Mine, Chemical and Power Workers' Union, Cologne

Further positions:

- Member of the Supervisory Board of LANXESS Deutschland GmbH, Leverkusen
- Vice Chairman of the Supervisory Board of Stora Enso Beteiligungen GmbH, Düsseldorf

Werner Czaplík Reprographics specialist

Further positions:

- Member of the Supervisory Board of LANXESS Deutschland GmbH, Leverkusen

Ralf Deitz Vice Chairman of the Supervisory Board

Chemical production technician

Further positions:

- Member of the Supervisory Board of LANXESS Deutschland GmbH, Leverkusen

Dr. Rudolf Fauss Chemistry graduate

Further positions:

- Member of the Supervisory Board of LANXESS Deutschland GmbH, Leverkusen

Ulrich Freese Vice Chairman of the German Mine, Chemical and Power Workers' Union

Further positions:

- Member of the Supervisory Board of LANXESS Deutschland GmbH, Leverkusen
- Vice Chairman of the Supervisory Board of Vattenfall Europe Mining AG, Berlin
- Vice Chairman of the Supervisory Board of RAG Immobilien AG, Essen
- Vice Chairman of the Supervisory Board of Deutsche Montan Technologie, Essen
- Vice Chairman of the Supervisory Board of GSB – Gesellschaft zur Sicherung von Bergmannswohnungen mbH, Essen
- Vice Chairman of the Supervisory Board of Wohnbau Westfalen GmbH, Dortmund
- Vice Chairman of the Supervisory Board of Wohnungsbaugesellschaft für das Rheinische Braunkohlerevier GmbH/GSG Wohnbau Braunkohle GmbH, Cologne

Rainer Hippler Chemical production technician

Further positions:

- Member of the Supervisory Board of LANXESS Deutschland GmbH, Leverkusen
- Member of the Supervisory Board of RheinChemie Rheinau GmbH, Mannheim

Hans-Jürgen Schicker Fitter

Further positions:

- Member of the Supervisory Board of LANXESS Deutschland GmbH, Leverkusen

Board of Management In 2005 the members of the Board of Management were:

Dr. Axel C. Heitmann Chairman of the Board of Management

Further positions:

- Chairman of the Board of LANXESS Chemical (Shanghai) Co. Ltd., China

Dr. Ulrich Koemm Member of the Board of Management

Further positions:

- Member of the Board of LANXESS Ind. de Produtos Quimicos, Brazil
- Director of the Board of LANXESS K.K., Japan
- Chairman of the Board of LANXESS, S.A. de C.V., Mexico
- Chairman of the Board of LANXESS International SA, Switzerland
- Chairman of the Supervisory Board of Dorlastan & Monofil GmbH, Dormagen

Dr. Martin Wienkenhöver

Member of the Board of Management and Industrial Relations Director

Further positions:

- Chairman of the Board of LANXESS Yaxing Chemical (Weifang), China
- Director of the Board of LANXESS Chemical (Shanghai) Co. Ltd., China
- Chairman of the Board of LANXESS HONG KONG LIMITED, Hong Kong
- Chairman of the Board of LANXESS India Private Limited, India
- Chairman of the Board of LANXESS S.r.l., Italy
- Chairman of the Board of LANXESS B.V., Netherlands
- Director of the Board of Sybron Chemicals Ind. Nederland B.V., Netherlands
- Director of the Board of Sybron Chemicals Holding B.V., Netherlands
- Chairman of the Board of LANXESS Pte. Ltd., Singapore
- Member of the Board of Chrome Int. South Africa (Pty) Ltd., South Africa
- Chairman of the Board of LANXESS Corporation, U.S.A.
- Chairman of the Supervisory Board of RheinChemie Rheinau GmbH, Mannheim
- Chairman of the Board of LANXESS Holding Hispania, S.L., Spain
- Chairman of the Board of LANXESS Chemicals S.L., Spain

Matthias Zachert

Member of the Board of Management, Chief Financial Officer

Further positions:

- Member of the Board of LANXESS K.K., Japan
- Member of the Board of LANXESS Corporation, U.S.A.
- Chairman of the Board of LANXESS N.V., Belgium
- Chairman of the Board of LANXESS S.A.S., France

Leverkusen, March 21, 2006

LANXESS Aktiengesellschaft, Leverkusen,

Dr. Axel C. Heitmann

Dr. Ulrich Koemm

Dr. Martin Wienkenhöver

Matthias Zachert

CHANGES IN NON-CURRENT ASSETS OF LANXESS AG

€'000	Gross carrying amounts				Amortization/depreciation and write-downs		Net carrying amounts	
	Jan. 1, 2005	Acquisitions	Retirements	Dec. 31, 2005	Accumulated Dec. 31, 2005	2005	Dec. 31, 2004	Dec. 31, 2005
Intangible assets								
Software licenses	0	35	0	35	6	6	0	29
	0	35	0	35	6	6	0	29
Property, plant and equipment								
Furniture and fixtures	29	0	0	29	12	6	23	17
	29	0	0	29	12	6	23	17
Financial assets								
Investments in subsidiaries	738,839	0	0	738,839	0	0	738,839	738,839
Other loans	70	0	28	42	0	0	70	42
	738,909	0	28	738,881	0	0	738,909	738,881
Total non-current assets	738,938	35	28	738,945	18	12	738,932	738,927

MANAGEMENT REPORT OF LANXESS AG FOR FISCAL 2005

Acquisition of the LANXESS Business Area from Bayer AG

Under the Spin-Off and Acquisition Agreement notarized on September 22, 2004, Bayer AG, as the transferring entity, transferred all the shares of LANXESS Deutschland AG and other portions of its assets and liabilities to LANXESS AG, as the acquiring entity, by means of a spin-off. Prior to this transaction, the chemicals activities and significant parts of the polymers activities of Bayer AG had been grouped at LANXESS Deutschland GmbH either directly or through subsidiaries. The Spin-Off and Acquisition Agreement was approved at a Stockholders' Meeting of Bayer AG on November 17, 2004 and a Stockholders' Meeting of LANXESS AG on December 21, 2004. The spin-off became effective when it was entered in the Commercial Register for Bayer AG on January 28, 2005.

LANXESS AG basically operates as a management holding company for LANXESS Deutschland GmbH, a wholly owned subsidiary with which it has a profit-and-loss transfer agreement. LANXESS Deutschland GmbH has subsidiaries in Germany and other countries. The economic performance of LANXESS AG thus depends essentially on that of the operating companies in the LANXESS Group and on the development of the chemical industry.

Sales and Earnings Performance

The spin-off of the assets and liabilities allocated to the LANXESS Group to LANXESS AG and the associated commencement of its operation as a group management company in early 2005 led to a fundamental shift in the amounts and the structure of its sales, operating result and financial result. The earnings of LANXESS AG are chiefly dependent on the profit-and-loss transfer agreement with LANXESS Deutschland GmbH, which holds all shares in its subsidiaries and thus bundles all operational business. The earnings performance of LANXESS Deutschland GmbH in 2005 was hampered by a number of one-time effects such as restructuring charges and expenses relating to antitrust proceedings. The establishment of a new financing structure also led to considerable one-time expenses.

The sales revenues of €33,589,000 reflected in the income statement (2004: €4,787,000) relate to services provided for LANXESS Deutschland GmbH. After deducting the cost of sales, which mainly comprises personnel and general administration expenses, the gross profit was around break-even point.

The remaining general administration expenses of €6,232,000 principally comprise the costs of business activities not directly related to services provided for the Group. Including other oper-

ating income of €1,855,000 and other operating expenses of €1,916,000, the company reported an operating loss of €6,293,000 (2004: €34,000).

The financial result, which comprises the balances of income and losses from investments in affiliated companies, interest income and expense, and other financial income and expenses, was negative at €149,746,000. Since the company recorded net interest income of €2,379,000 (2004: interest expense of €1,874,000), the negative financial result was attributable to the assumption of the loss of €118,365,000 reported by LANXESS Deutschland GmbH and the negative balance of other financial income and expenses, which amounted to €33,760,000 (2004: positive balance of €172,000). The negative balance for 2005 mainly comprises exchange gains of €4,585,000, offset by expenses of €34,942,000 for establishment of the new financing structure.

LANXESS AG thus reported a pre-tax loss of €156,039,000 (2004: €1,736,000). After factoring in the loss of €1,738,000 carried forward from the previous year, €157,777,000 was withdrawn from capital reserves to offset the balance sheet loss.

Asset and Capital Structure

LANXESS AG only commenced operation as a Group management company when the spin-off was entered in the Commercial Register in January 2005. Consequently, the balance sheet as of December 31, 2005 is not comparable to the balance sheet for the previous year.

In view of its function as a financial holding company, the balance sheet of LANXESS AG is dominated by financial assets and by receivables and payables to subsidiaries.

Total assets were €2,018,371,000 as of December 31, 2005. This was €979,893,000 (94.4%) higher than at year-end 2004.

Non-current assets amounted to €738,927,000, which was 36.6% of total assets. Financial assets include the interest in LANXESS Deutschland GmbH totaling €738,839,000.

Current assets account for €1,278,527,000 (63.4%) of total assets. Receivables from subsidiaries accounted for 59.1% of total assets and relate to financial transactions and short-term loans. Liquid assets were 3.0% of total assets. LANXESS AG also has agreed credit lines of €1,250,000,000 under a multi-currency syndicated revolving credit facility granted by a consortium of international banks.

Stockholders' equity is €889,398,000 and equity coverage of total assets is 44.1%. The €54,835,000 rise in the stockholders' equity of LANXESS AG comprises a contribution of €210,874,000 from the shares issued out of contingent capital in July 2005 upon the conversion of the mandatory convertible bond, less the net loss of €156,039,000. The net loss and the loss of €1,738,000 carried forward from the previous year were covered by a withdrawal from capital reserves. Equity coverage of non-current assets was 120.4%.

Liabilities on December 31, 2005 amounted to €1,128,973,000, which was 55.9% of total stockholders' equity and liabilities. Provisions of €17,644,000, amounting to 0.9% of total stockholders' equity and liabilities, are mainly for employee pensions and other commitments.

The liabilities totaling €1,111,329,000 comprise 55.1% of total stockholders' equity and liabilities. Of this 7.7%, or €155,817,000, consists of liabilities to banks, including non-current liabilities of €30,000,000. Payables to subsidiaries are the main source of financing – amounting to €946,167,000 or 46.9% of total stockholders' equity and liabilities.

Employees During 2005 the number of employees increased by eight to a total of 106 (2004: 98). The company's average headcount in 2005 was 102 (2004: 49). Personnel expenses came to €20,638,000 (2004: €4,483,000).

Risk Report

Risk management Risk management is important for LANXESS AG and the LANXESS Group (LANXESS) because business activity necessarily entails risks as well as opportunities. Success is significantly dependent on identifying both opportunities and risks and actively managing them. Effective risk management is therefore a core element in ensuring the company's long-term future and continued successful development.

LANXESS's risk management approach is based on clearly defined business processes, the precise assignment of responsibilities throughout the organization and appropriate reporting systems that ensure the timely provision of the information required for decision-making to the Board of Management and other management levels. LANXESS views risk management as an integral part of corporate controlling. Risk management is incorporated into business processes primarily through the

company's organizational structure, its planning, reporting and communication systems, and a body of detailed management regulations and technical standards. Various committees and other bodies discuss and monitor opportunities and risks.

At LANXESS, the business units each conduct their own operations, for which they have global profit responsibility. Group functions support the business units by providing financial, legal, technical and other centralized services. Complementing this global alignment of the business units and group functions, the country organizations ensure the required proximity to markets and the necessary organizational infrastructure. In line with this division of duties, LANXESS has assigned responsibility, i.e. defined the risk owners, for the following:

- risk identification and analysis
- risk prevention (measures taken to avoid, minimize or diversify risk)
- risk monitoring (watching for early warning signs) and
- risk migration (measures to minimize damage upon occurrence of a risk event)

Risk transfer transactions (hedging transactions or insurance) are entered into and managed centrally at LANXESS via the Treasury Department.

In connection with the decentralized organization of its risk management, LANXESS has established a central risk database to which the risk owners contribute structured data about the risks identified. To this end, risk categories have been defined, along with parameters for probabilities of occurrence and damage levels. The central risk database therefore provides a complete overview of LANXESS's risk profile. The Management Board receives a report on any material changes to this risk database every six months. There is also provision for immediate internal reporting on specific risk issues such as significant corporate compliance violations. In 2005 there was no cause for immediate reporting of this kind on significant risks at LANXESS. In addition to the standard risk reporting system required by the German Law on Corporate Control and Transparency (KonTraG), LANXESS has a hierarchical communication system for appraising potential opportunities and risks and making them known to the Management Board. To supplement the central risk database, those risks and opportunities considered relatively likely to materialize are presented as worst-case/best-case scenarios in the context of corporate planning.

LANXESS's risk management principles are laid down in a Group directive. Risk management also includes obtaining extensive legal advice concerning business transactions and obligating employees through the corporate compliance code to observe the law and act responsibly.

Monitoring of risk management and of LANXESS's internal control system (ICS) by means of process-independent testing is part of the risk management system. Within the Group, the Internal Auditing group function is tasked with overseeing both the functionality of the internal control and monitoring system and compliance with organizational safeguards. In addition, the risk management system is evaluated by the auditor as part of the audit of the annual financial statements.

LANXESS has acknowledged that managing the company necessarily involves managing risk. Steps have been taken to ensure that potential risks or opportunities relevant to the attainment of corporate goals are fully identified and quantified at an early stage. Preventive measures and safeguards minimize the probability that risks will materialize and limit their potentially adverse effects. The management of opportunities and risks is one of LANXESS'S goals and therefore constitutes an integral part of decision-making processes.

Risks affecting future development

Market risks LANXESS is exposed to the general economic and political opportunities and risks in the countries and regions in which its companies operate. As a chemical enterprise, LANXESS is subject to the risks typical of this industry sector. The volatility and cyclicality of the global chemical and polymer markets and their dependence on developments in customer industries harbor opportunities and risks with respect to LANXESS's business volume. LANXESS anticipates that future growth will come from a continuing increase in demand on Asian markets, particularly in China. If the general business environment in this region should deteriorate due to economic or other factors, one of LANXESS's key growth drivers could be weakened or eliminated.

LANXESS's risk profile is influenced by structural changes in markets, such as the entry of new suppliers, particularly those based in emerging economies; the migration of customers to countries with lower costs; and product substitution or market consolidation trends of the kind already occurring in some sectors, particularly rubber. LANXESS counters such trends by restructuring operations to achieve a sharper focus and arrive at a product

portfolio with which it can operate successfully for the long term. At the same time, LANXESS systematically manages costs.

On the procurement side, the principal risk lies in the volatility of raw material and energy prices. LANXESS mitigates this type of procurement risk by entering into long-term supply contracts for most raw materials and agreeing price escalation clauses with customers. To guard against possible supply bottlenecks due to factors such as the failure of an upstream operation at a networked site, LANXESS pursues an appropriate inventory strategy and lines up alternative sources of supply.

Foreign exchange risks Changes in the euro exchange rate, particularly against the U.S. dollar, can affect LANXESS's results. Such risks are documented, monitored and managed centrally. This enables LANXESS to offset the various foreign exchange effects of procurement and sales activities, and the foreign currency balances of the individual LANXESS companies, against one another. The goal is to hedge the residual amounts with derivative financial instruments. LANXESS only hedges foreign currency items that have arisen from underlying business or are considered highly likely to arise. Long-term changes in currency parities can negatively or positively affect competitiveness in relation to suppliers outside the euro zone.

Interest rate and credit risks The risk of interest rate changes is centrally managed by the Treasury Department. The majority of the company's debt was raised at fixed terms. Possible interest rate shifts in the coming years will therefore only have a limited effect on LANXESS. The Treasury Department also verifies customers' creditworthiness in close cooperation with our sales departments to minimize the default risk.

Derivative financial instruments LANXESS AG uses derivative financial instruments to hedge against the three risk factors outlined above, especially foreign exchange risk. These are mainly over-the-counter (OTC) instruments, particularly forward contracts and currency options. In these transactions, LANXESS AG acts as the counterparty entering into external contracts to hedge foreign exchange positions of its own or on behalf of Group companies. All transactions are executed with banks of high credit standing. The instruments are employed according to uniform guidelines and are subject to strict internal controls. Their use is generally confined to the hedging of the operating business and of the related investments and financing transactions. In the commodities field, derivative transactions are also carried out on behalf of Group companies to hedge against market prices of utili-

ties. The main objective in using derivative financial instruments is to smooth out fluctuations in cash flows and earnings associated with changes in exchange rates and market prices. Where transactions are undertaken on behalf of Group companies, back-to-back contracts are entered into within the Group to pass them through to the respective company.

Legal risks Companies in the LANXESS Group are parties to various litigations. The outcome of individual proceedings cannot be predicted with assurance due to the uncertainties always associated with legal disputes. To the extent necessary in the light of the known circumstances in each case, LANXESS has set up risk provisions for the event of an unfavorable outcome of such proceedings.

Taking into account existing provisions and insurance, along with the agreements reached with third parties on liability risks from legal disputes, the company currently estimates that none of these proceedings will materially affect the future earnings of the LANXESS Group. The risk level could be heightened, however, by certain antitrust proceedings brought by regulatory authorities or civil courts in the United States, Canada and Europe with respect to the business activities of Bayer AG that have been transferred to LANXESS AG or its present subsidiaries.

As part of the spin-off, the activities of Bayer AG's former Rubber Business Group were transferred to the LANXESS Group. Investigations by the antitrust authorities and several private class-action and individual suits are or were pending in connection with various products that are or were attributable to these business activities. LANXESS AG and Bayer AG have agreed on specific rules with regard to such investigations, actions and suits. With regard to all liabilities arising out of, or in connection with, proceedings that had at least been initiated prior to July 1, 2004, LANXESS AG has to bear 30% of all such liabilities vis-à-vis Bayer AG, and Bayer AG has to bear 70% of all such liabilities vis-à-vis LANXESS AG. LANXESS AG's liability is, however, limited to a maximum amount of €100 million plus possible defense costs and proportionate reimbursement of additional taxes that may be payable if the tax deductibility of expenses is restricted. Current estimates indicate that in 2005 and 2006 will make total payments equal to the €100 million maximum.

Production and environmental risks Although LANXESS applies high technical and safety standards to the construction, operation and maintenance of production facilities, interruptions in operations, including those due to external factors, such as

natural disasters or terrorism, cannot be ruled out. These can lead to explosions, the release of materials hazardous to health, or accidents in which people, property, or the environment are harmed. In addition to systematically monitoring compliance with quality standards aimed at avoiding such stoppages or accidents, LANXESS is also insured against the resulting damage to the extent usual in the industry.

Possible tightening of safety, quality and environmental regulations or standards can lead to additional costs and liability that are beyond the control of LANXESS. Particularly noteworthy in this regard is the planned implementation of the E.U. regulation on the registration, evaluation, authorization and restriction of chemical substances (REACH). In addition to direct costs that could arise due to additional measures necessary to comply with these standards, market structures could change to LANXESS's disadvantage as a result of a shift by suppliers and customers to regions outside Europe.

LANXESS is responsible for numerous sites and landfills in which chemicals have been produced or stored for periods that in some cases exceed 140 years. The possibility cannot be ruled out that pollution occurred during this time that has not been discovered to date. LANXESS is committed to the Responsible Care initiative and actively pursues environmental management. This includes constant monitoring and testing of the soil, groundwater and air. Sufficient provisions have been set up within the scope permitted by law for necessary containment or remediation measures in areas with identified contamination.

LANXESS's product portfolio includes substances that are classified as hazardous to health. In order to prevent possible harm to health, LANXESS systematically tests the properties of its products and draws its customers' attention to the risks associated with their use. Moreover, adequate product liability insurance has been arranged.

Other risks In the course of the spin-off from Bayer, LANXESS acquired structures and circumstances that will in future be subject to assessment by the tax authorities. Even though LANXESS believes that all circumstances have been reported correctly and in compliance with the law, the possibility cannot be ruled out that the tax authorities may come to a different conclusion in individual cases.

The provision of correct information at the correct time to the correct addressee is one of LANXESS's success factors. LANXESS is dependent on its integrated IT systems to manage this information. In order to ensure constant availability of its data, LANXESS maintains data back-up systems, mirrored databases, anti-virus and access restriction systems, along with other state-of-the-art security and monitoring tools.

LANXESS plans to continue with its restructuring and its realignment toward strategic core businesses. The success of the associated investments and divestments is naturally subject to forecasting risk, which LANXESS counters by carefully and systematically processing key decision-making information. Moreover, industrial action resulting from disputes about the implementation of restructuring measures or in connection with negotiations concerning future collective bargaining agreements cannot be ruled out.

Overall risk Based on an overall evaluation of risk management information, LANXESS has not identified any sufficiently likely risks or risk combinations that would jeopardize the continued existence of LANXESS.

Outlook In 2006, assuming business conditions remain stable for the chemical industry, LANXESS expects a further year-on-year rise in Group EBITDA pre exceptionals. With consistent application of the "price before volume" strategy, the company assumes that sales in continuing business activities will grow only moderately, but that the EBITDA margin pre exceptionals will rise significantly to between 9% and 10%, based on 2004 sales.

In performing its tasks as a management holding company, LANXESS AG expects to incur about the same level of costs as in 2005. Earnings should improve due to the absence of one-time charges for the new financing structure. Apart from this, the earnings position of LANXESS AG will be dominated by interest income/expense and income/losses from investments in affiliated companies. If profitability in the Group improves as expected, higher dividend payments by Group companies should enable LANXESS AG to report clearly positive net earnings.

Based on the above expectations regarding business performance, the Management Board and Supervisory Board are examining the possibility of a dividend payment for 2006 to reward the confidence and support of LANXESS stockholders over the medium term.

Subsequent events No events of material significance have occurred since the end of the 2005 fiscal year.

Concluding statement to the Dependency Report pursuant to Article 312 of the German Stock Corporation Act (AktG)

Until January 28, 2005, LANXESS AG was a company controlled by Bayer AG. During this period it did not have a domination agreement with Bayer AG, nor a profit transfer agreement, nor a domination and profit transfer agreement. Since the spin-off of the LANXESS business area from Bayer AG to LANXESS AG became effective, in consideration for which shares in LANXESS AG were issued to stockholders' of Bayer AG on January 28, 2005, LANXESS AG has no longer been controlled by Bayer AG.

The report prepared on its relationship to affiliated companies for the period January 1 to January 28, 2005 in compliance with Article 312 of the German Stock Corporation Act (AktG), concludes with the following statement:

"Our company received appropriate consideration for each of the transactions set out in this report. In the period from January 1 to January 28, 2005, there were no reportable instances in which the company adopted, or refrained from adopting, measures at the request or in the interests of the controlling company or a company affiliated with the controlling company."

AUDITOR'S REPORT

We have audited the annual financial statements, comprising the balance sheet, the income statement and the notes to the financial statements, together with the bookkeeping system, and the management report of LANXESS Aktiengesellschaft, Leverkusen, for the business year from January 1 to December 31, 2005. 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 Managing Directors. Our responsibility is to express an opinion on the annual financial statements, together with the bookkeeping system, and the management report based on our audit.

We conducted our audit of the annual financial statements in accordance with Article 317 HGB ("Handelsgesetzbuch": German Commercial Code) and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (Institute of Public Auditors in Germany – IDW). Those standards require that we 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 as to 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 Board of Managing Directors, as well as evaluating the overall presentation of the annual financial statements and management report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

In our opinion based on the findings of our audit, the annual financial statements comply with the legal requirements and 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. The management report is consistent with the annual financial statements and as a whole provides a suitable view of the Company's position and suitably presents the opportunities and risks of future development.

Cologne, March 22, 2006

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