

Management Report

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Important Disclaimer

Markets and Competitive Position

This report contains information, statistical data and predictions about our markets and our competitive position. We have not verified the accuracy of those statistical data or predictions contained in this report that were taken or derived from industry publications, public documents of our competitors or other external sources. We believe that the information presented in this report provides fair and adequate estimates of the size of our markets and fairly reflects our competitive position within these markets. However, our internal estimates have not been verified by an external expert, and we cannot guarantee that a third party using different methods to assemble, analyze or compute market data would obtain or generate the same results. In addition, our competitors may define our and their markets differently than we do.

Forward-Looking Statements

This report contains “forward-looking statements” regarding our assumptions, projections, expectations, intentions or beliefs about future events. We caution you that these statements may and often do vary from actual results and the differences between these statements and actual results can be material. Accordingly, we cannot assure you that actual results will not differ materially from those expressed or implied by the forward-looking statements. These forward-looking statements include, among others, statements concerning our financial position and results, business strategy, plans and objectives of management for future operations, including development plans and objectives relating to our business. Some, but not all, of the factors that could cause actual results to differ materially from those expressed or implied in any forward-looking statement include: the current financial crisis; our exposure to currency exchange rate fluctuations; changes in the market prices or availability of raw materials; changes in

the political, social, trade, monetary, fiscal, taxation and environmental policies of governments, agencies and similar organizations in geographic areas where we operate; the impact of increasingly stringent environmental laws and their enforcement by the relevant authorities; changes in the competitive and regulatory framework in which we operate, in particular increased competition in the specialty chemicals industry; the consolidation of our customers or the loss of key customers; our ability to implement our business strategies, including our ability to maximize production yields and lower production costs; potential environmental or product liability claims, costs, liabilities or other obligations; the impact of legislative changes and fluctuations in the equity markets on the development of our pension and retirement obligations; changes in our relationships with workers’ councils and unions; challenges to, losses of or infringements on our intellectual property rights; difficulties we may encounter in implementing our new IT systems or in updating our current IT systems; changes in our insurance coverage; acts of terrorism generally, and particularly in the countries in which we operate; our ability to claim tax losses; general economic and business conditions, including any decline in financial or equity markets; our high leverage and our ability to generate sufficient cash to service our debt; the risks associated with our structure and our indebtedness; our ability to borrow additional funds and access capital markets; our ability to repurchase or settle the Senior Secured Floating Rate Loans and Notes, Senior Subordinated Notes and PIK (Payment-In-Kind) Loans upon a change of control; and other factors beyond our control.

Forward-looking statements speak only as of the date of this report. We expressly disclaim any obligation or undertaking to release, publicly or otherwise, any updates or revisions to any forward-looking statement contained in this report to reflect any change in our expectations or any change in events, conditions, assumptions or circumstances on which any such statement is based, unless so required by applicable law.

Management's Discussion and Analysis

Our Business

Cognis¹⁾ is a global supplier of innovative specialty chemicals and nutritional ingredients, with a deep understanding of our customers' markets and consumer demands and a particular focus on the wellness and sustainability trends. Our portfolio comprises complete solutions and concepts, including ready-to-market products and marketing claims that directly meet consumer demands, giving our customers that paramount competitive edge.

Leading positions in attractive growing markets

We have identified two megatrends, wellness and sustainability, placing them at the very heart of our strategy. Our focus on the relevant segments helps our customers to achieve above-average growth in new but also in established markets.

Customers' desire for natural-source products enhancing wellness and convenience has grown due to heightened focus on health and beauty. Customers are also becoming more environmentally aware and therefore demand products that meet the standards of increased environmental regulations, have an improved performance and are cost efficient. We are positioned to continue benefiting from this trend, given our natural oil-based products.

Having previously been part of an international brand manufacturer, Cognis knows the requirements and mechanisms that prevail in the consumer goods markets. Our role is that of a partner to our customers, supporting them in the development and marketing of new and successful concepts and integrated solutions. As a provider of comprehensive concepts and integrated solutions, we are much more than a raw material supplier.

Accordingly, wellness means for us the development of effective concepts to pro-actively improve physical and spiritual well-being. This is expressed through our "Feelosophy" concept, which refers to the creation of a holistic well-being experience (comprising the components Perception, Feel, Effect and Usage) for consumers derived from the application of personal care and home care products as well as functional food and dietary supplements with orientation to central market demands.

Through our developments, we are able to support our customers in finding an early and effective response to changing market demands and regulatory requirements. With marketing messages and performance promises that are also scientifically verifiable, we provide our customers with competitive advantages that really can make a difference in their markets.

We employ some 5,900 people in our continuing operations and operate production sites and service centers in around 30 countries.

In 2008, we generated sales²⁾ of €3,001 million, EBITDA of €328 million and Adjusted EBITDA³⁾ of €351 million in our continuing operations.⁴⁾

Our focus on our Strategic Business Units ("SBUs") Care Chemicals, Nutrition & Health and Functional Products is a direct consequence of our alignment to the wellness and sustainability trends. It is here that our greatest innovative strengths lie and where the greatest growth potential for our company exists.

Care Chemicals

Cognis is a globally leading supplier of innovative, environmentally sound products and formulations for the personal care and home care markets as well as for industrial and institutional cleaning. Based on a keen awareness of the latest local and global trends, we offer winning solutions and ready-to-market concepts for cosmetics, toiletries, detergents, and household cleaners precisely in tune with contemporary consumer demands for well-being, convenience and sustainability.

Nutrition & Health

The wellness-driven market demands solutions that contribute to health and an overall sense of well-being. Using natural-source ingredients and applying extensive nutrition expertise, we develop forward-looking products, formulations and concepts for foods, beverages, functional food and dietary supplements. The bioactive and non-active ingredients of our Nutrition & Health SBU deliver real health, quality and convenience benefits—from cholesterol reduction and weight management to effective drug delivery and extended shelf life.

¹⁾ "Cognis" refers to Cognis GmbH and its consolidated direct and indirect subsidiaries.

²⁾ Due to our intention to sell our former SBUs Pulcra Chemicals and Oleochemicals as well as the Thai Fatty Alcohols business, we classified all assets and liabilities of these businesses as "held for sale". The results of all three businesses are classified as discontinued operations. Sales is defined as follows: Net Sales of Cognis' continuing operations (Care Chemicals, Nutrition & Health and Functional Products as well as Other Activities) reflect sales to third parties (Net External Sales) and to the discontinued operations but exclude sales for internal deliveries between Care Chemicals, Nutrition & Health and Functional Products.

³⁾ We use Adjusted EBITDA as our key performance indicator of operating results. Adjusted EBITDA is calculated by deducting certain income and gains and by adding certain expenses and losses from or to EBITDA that we believe are not indicative of Cognis' underlying operating performance. These items include significant gains and losses realized on the disposals of fixed assets, investments or businesses, restructuring expenses and other exceptional items which, in our opinion, are not indicative of our fundamental operating performance. In addition, you should not infer from our presentation of Adjusted EBITDA that our future results will be unaffected by unusual or non-recurring items. Adjusted EBITDA, as an analytical measure, is subject to all of the limitations applicable to EBITDA.

⁴⁾ For more details concerning the definition of EBITDA and Adjusted EBITDA, please refer to "Financial Highlights and Operating Results—EBIT, EBITDA and Adjusted EBITDA".

Functional Products

Today's industries are increasingly responding to the demand for sustainable practices and environmentally friendly products. We use our extensive chemical expertise to create specific solutions for a wide spectrum of industrial sectors—from polymers, coatings and inks, lubricants to crop protection and mining. Our ingredients and formulations deliver a superior performance profile combined with outstanding application reliability and user safety.

Divestment of non-core businesses

Cognis Oleochemicals is a major producer of natural-based oleochemical products and was a 50:50 joint venture between Sime Darby Plantation Sdn. Bhd. (until 2006: Golden Hope) and Cognis. We sold our 50 percent stake to PTT Chemical International Private Ltd. on November 24, 2008 after relevant regulatory approvals were obtained. By selling our stake to a well known partner we ensure a stable supply of our oleochemical basestocks is secured, as we intend to continue sourcing products from Oleochemicals.

Thai Fatty Alcohols Company Ltd. was a 50:50 joint venture between Cognis and Thai Oleochemicals Company Ltd., a subsidiary of PTT Chemicals Public Company Limited. The joint venture was founded in 2006 for the production and marketing of fatty alcohols. On November 14, 2008 we sold our 50 percent stake to Thai Oleochemicals Company Ltd.

Pulcra Chemicals, which supplies process chemicals to the textile and leather industries, was previously the Process Chemicals SBU of Cognis. On October 31, 2008 we sold Pulcra Chemicals to Germany-based Fashion Chemicals GmbH & Co. KG. Fashion Chemicals is backed by the Pulcra Chemicals management and other stakeholders including leading tanneries and leather manufacturers.

Financial Highlights and Operating Results

Overview of 2008

The year 2008 was marked by high raw material prices, a sudden sharp global economic downturn at the year-end and as we expected, additional capacities in Asia which increased competition further in the fatty alcohols market.

In such an unpredictable environment, we grew our business increasing sales to €3,001 million by firmly positioning Cognis on the wellness and sustainability trends. Overall, we were mostly successful in reflecting increased raw material prices in higher selling prices in spite of an extremely competitive environment. As a result, we increased our sales despite the loss of some volumes.

Raw material prices were so volatile during the year that we could not compensate the entire cost increase as quickly as we needed to. The loss in margins resulting from higher raw material prices and energy costs was almost compensated by a cost optimization program targeting processing and Selling, General and Administration ("SG&A") costs but without compromising our Research & Development ("R&D") activities. Despite the sharp increase in raw material prices, the global economic slowdown at the end of the year and unfavorable development of foreign exchange rates, our Adjusted EBITDA for continuing operations is €351 million in 2008 compared to €360 million in 2007. However, on an organic basis, i.e. without the translation effects from foreign exchange rates and disposal effects, Adjusted EBITDA remained stable at €359 million.

In terms of cash generation, we have generated sufficient cash from our operations in 2008 to cover investments in working capital, capital expenditure, restructuring activities and to service our interest payments. As a result, the disposal proceeds amounting to €131 million received for the divestments of our discontinued operations remained unutilized. Consequently, our cash and cash equivalents at the end of this year increased substantially to €226 million compared to December 31, 2007. This healthy cash position together with an undrawn revolving credit facility of €221 million provides Cognis with sufficient liquidity, stability and flexibility in terms of investing in our business, especially in these times of economic uncertainty.

Divestment of Pulcra Chemicals, Oleochemicals and Thai Fatty Alcohols

On November 24, 2008, we sold our 50 percent stake in the Oleochemicals joint venture to PTT Chemical International Private Ltd.

Further, we sold our 50 percent stake in Thai Fatty Alcohols Company Ltd. on November 14, 2008.

We also sold our Pulcra Chemicals subsidiary to Germany-based Fashion Chemicals GmbH & Co. KG on October 31, 2008.

The core SBUs, namely Care Chemicals, Nutrition & Health and Functional Products, together with Other Activities Continuing are defined as continuing operations under IFRS 5. Due to our intention to sell our former Business Units Pulcra Chemicals and Oleochemicals, we classified all assets and liabilities of these businesses as “held for sale” as of June 30, 2008. The assets and liabilities of Thai Fatty Alcohols were classified as held for sale as of September 30, 2008. The results of all three businesses are classified as discontinued operations. All three businesses were sold prior to the year-end. As such discontinued operations only include amounts and results up to the month of the respective divestments.

Consequently, the Management’s Discussion and Analysis is focused on continuing businesses with restated and comparable prior-year figures. The cash flow statement still includes cash flows from discontinued operations but operating, investing and financing cash flows relating to discontinued operations are separately disclosed.

For more details concerning these transactions, please refer to the section “Management’s Discussion and Analysis—Strategic Business Units and Segment Results”.

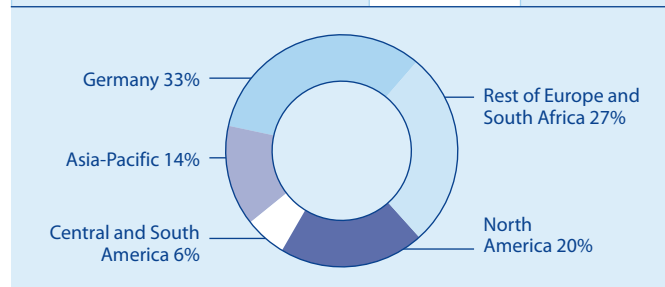
Results from Continuing Operations		
€ millions	Continuing Operations	
	2008	2007
Net sales	3,001	2,844
Operating profit (EBIT)	192	186
EBITDA	328	323
Adjusted EBITDA	351	360
Adjusted EBITDA margin	11.7%	12.7%
Net profit/(loss)	(49)	(105)

Organic sales growth of 9.2%

Cognis’ 2008 sales of €3,001 million were €157 million or 5.5%⁵⁾ higher than in 2007. On an organic⁶⁾ basis, i.e. excluding foreign currency⁷⁾ effects and the effects of acquisitions and divestments, sales growth amounted to €261 million or 9.2% despite losses in volumes. All SBUs contributed to the organic sales growth:

- Care Chemicals increased sales by 9.8%, reflecting strong growth of our Care Performance Ingredients (“CPI”) and Care Surfactants and Fatty Alcohols (“CSA”) business segments. While Primary Surfactants achieved higher growth, sales of Fatty Alcohols were lower than prior year
- Nutrition & Health reported sales growth of 6.3% mainly driven by branded ingredients and Food Technology. To a large extent, Vitamin E contributed to the sales growth due to strong demand
- Functional Products’ sales increased by 10.3%. Key drivers of this growth were strong worldwide demand for environmentally friendly agricultural solutions and for synthetic lubricants used in industrial applications and automotive applications

Sales by Company Jurisdiction—Continuing Operations		
€ millions	Continuing Operations	
	2008	2007
Germany	1,003	901
Rest of Europe and South Africa	803	834
North America	590	572
Central and South America	197	163
Asia-Pacific	408	374
Total	3,001	2,844



On a regional⁸⁾ basis, we achieved strong sales growth of +20.9% in Central and South America⁹⁾, +11.3% in Germany, +9.2% in Asia-Pacific¹⁰⁾ and +3.1% in North America¹¹⁾. The Rest of Europe¹²⁾ reported slightly lower sales with –3.7%.

⁵⁾ Percentages are calculated based on the exact underlying figures.

⁶⁾ We refer to the change from the prior period excluding foreign currency effects and excluding the effects of acquisitions and divestments as “organic growth”. From an SBU perspective, the change from the prior period excludes foreign currency effects, the effects of acquisitions and divestments and inter-SBU transfers.

⁷⁾ When discussing our results of operations, we often express a number as “excluding foreign currency effects”. This phrase means that the current and comparative figures of Cognis’ constituent legal entities have been translated into euros using the same foreign exchange rates. We have not adjusted for transaction gains and losses, which may arise when a company earns revenues or incurs costs in a currency that is not its functional currency. The transaction gains and losses represent the changes in value, resulting from changes in exchange rates, of these transactions as measured in the functional currency.

⁸⁾ We define our regions according to the location of the selling legal entity. For example, products manufactured by a European legal entity and exported to the USA are considered to generate European sales and earnings.

⁹⁾ Comprises Central America and South America, including Colombia but excluding Mexico.

¹⁰⁾ Comprises Asia and Australia but excludes Turkey.

¹¹⁾ Comprises USA, Canada and Mexico but excludes Colombia.

¹²⁾ Comprises Europe, including Turkey and South Africa.

Adjusted EBITDA remained stable on an organic basis while EBIT increased

In 2008, Cognis reported an Adjusted EBITDA of €351 million, –€9 million or –2.6% lower than in 2007. On an organic basis, Adjusted EBITDA remained stable (–0.3%). The stable earnings were aided by the strong growth by our AgroSolutions business within Functional Products and of our CPI business within Care Chemicals. We supported our bottom line with careful cost management, however without compromising R&D activities. In this way, we were able to compensate for challenging market conditions and increased raw materials costs particularly in our Care Surfactants and Fatty Alcohols segment, as well as in the Functional Products Polymers, Coatings & Inks segment.

EBIT¹³⁾ increased due to lower restructuring charges.

Net Loss decreased

Net loss of continuing operations of –€49 million in 2008 decreased by +€56 million from a net loss of –€105 million in 2007. This was primarily due to lower income taxes (+€53 million) and a higher EBIT (+€6 million) slightly offset by a higher net financial result (–€3 million). Income taxes in 2008 were lower than in 2007 as prior year includes –€53 million deferred tax expenses incurred when deferred tax assets were revalued following the corporate tax reform in Germany.

The higher net financial result in 2008 was mainly due to higher other financial items (–€4 million) whereas net interest expense remained almost constant. Other financial items in 2008 mainly comprised losses on interest derivatives of –€23 million (2007: gains of +€10 million) caused by the development of underlying market values and higher foreign exchange losses of –€11 million (2007: gains of +€16 million). The higher net foreign exchange losses were mainly due to the strengthening of the US dollar compared to the euro and the resulting effect on our US dollar-borrowings compared to a weak US dollar in 2007.

These factors were almost offset by lower other financial expenses (+€56 million) in 2008. Prior year includes financing fees (+€57 million) related to the Senior Facilities and Second Lien Obligations that were written off once these financing arrangements were terminated and replaced by new facilities (for details on the new facilities, see section “Management’s Discussion and Analysis—Financial Position, Liquidity and Capital Resources—Net Debt and Liquidity”).

Events after balance sheet date

Sale of Botanicals Extracts Business

Cognis intends to sell its Botanicals Extracts business. The Botanicals Extracts business focuses on the production of botanical extracts for pharmaceuticals and dietary supplements and cosmetics, and operates two production sites in Spain. This business is currently part of Cognis’ Nutrition & Health SBU, and generated net sales of €9 million in 2007. Assets amounting to €1 million were reclassified as assets held for sale and presented in other current assets.

Debt Buy Back

As of December 31, 2008, we have purchased PIK Loans amounting to a face value of €3 million in an open-market transaction. As of February 18, 2009, the face value of PIK Loans purchased amounted to €47.5 million.

EBIT, EBITDA and Adjusted EBITDA

We define EBITDA as net income excluding income taxes, net financial result and amortization and depreciation. Our EBITDA figures are not necessarily comparable to other companies’ EBITDA disclosure, as each is calculated in its own way and must be read in conjunction with the explanations that accompany it. EBITDA has limitations as an analytical tool, and you should not consider it in isolation, as a measure of cash available to us to invest at our discretion or as a substitute for an analysis of our results as reported under IFRS.

¹³⁾ “EBIT” refers to net profit excluding financial result, taxes on income and minority interests.

Continuing Operations

We derive EBIT and EBITDA from net profit/(loss) for our continuing operations as follows:

€ millions	Continuing Operations	
	2008	2007
Net profit/(loss)¹⁾	(63)	(120)
Net profit/(loss) from discontinued operations ¹⁾	(14)	(15)
Net profit/(loss) from continuing operations	(49)	(105)
Income taxes	29	82
Net financial result	212	209
Operating profit (EBIT)	192	186
Amortization and depreciation	136	137
EBITDA	328	323

¹⁾ 2008 figures include Pulcra Chemicals, Oleochemicals and Thai Fatty Alcohols up to the month of the respective divestments.

The following table shows Adjusted EBITDA as derived from our EBITDA by excluding restructuring charges and other exceptional items:

€ millions	Continuing Operations	
	2008	2007
EBITDA	328	323
Restructuring charges ¹⁾	22	40
Other exceptional items ¹⁾	1	(3)
Adjusted EBITDA	351	360

¹⁾ Excluding depreciation and amortization.

Restructuring charges and other exceptional items—Continuing Operations

Restructuring charges excluding depreciation and amortization of €22 million in 2008 (2007: €40 million) essentially relate to severance pay, early retirement schemes, pre-retirement part-time employment programs and other process- and cost-optimization programs including Global IT Optimization and measures aimed at improving efficiency and reducing operating costs.

Other exceptional items comprise other income, expenses, gains and losses which, in our judgment, do not reflect normal business operations and include separation costs and sundry exceptional items. Other exceptional items generally result from losses (2008) or gains (2007) from disposals of assets.

Discontinued Operations

We derive EBIT and EBITDA from net profit/(loss) for our discontinued operations as follows:

€ millions	Discontinued Operations	
	2008 ¹⁾	2007
Net profit/(loss)	(63)	(120)
Net profit/(loss) from continuing operations	(49)	(105)
Net profit/(loss) from discontinued operations	(14)	(15)
(Gain)/Loss on disposals	19	–
Net profit/(loss) for the period up to disposal date²⁾	5	(15)
Income taxes	4	5
Net financial result	3	9
Operating profit (EBIT)	12	(1)
Amortization and depreciation	10	38
EBITDA	22	37

¹⁾ 2008 figures include Pulcra Chemicals, Oleochemicals and Thai Fatty Alcohols up to the month of the respective divestments.

²⁾ Oleochemicals was disposed on Nov. 24, 2008, Thai Fatty Alcohols on Nov. 14, 2008 and Pulcra Chemicals on Oct. 31, 2008.

The following table shows Adjusted EBITDA as derived from our EBITDA by excluding restructuring charges and other exceptional items:

€ millions	Discontinued Operations	
	2008 ²⁾	2007
EBITDA	22	37
Restructuring charges ¹⁾	1	6
Other exceptional items ¹⁾	9	7
Adjusted EBITDA	32	50

¹⁾ Excluding depreciation and amortization.

²⁾ 2008 figures include Pulcra Chemicals, Oleochemicals and Thai Fatty Alcohols up to the month of the respective divestments

Restructuring charges and other exceptional items—Discontinued Operations

Restructuring charges excluding depreciation and amortization were €1 million in 2008 (2007: €6 million) and mainly reflect various local restructuring measures.

Other exceptional items amounted to €9 million in 2008 (2007: €7 million). Other exceptional items in 2008 essentially relate to impairments of assets of Pulcra Chemicals which are not cash effective and as such not included in the cash flow.

Strategic Business Units and Segment Results

Overview of our Business Structure

We manage our business through our core Strategic Business Units ("SBUs") of Care Chemicals, Nutrition & Health and Functional Products. Our focus on these SBUs is a direct consequence of our alignment to the wellness and sustainability trends. Certain secondary activities are reported under Other Activities Continuing.

The core SBUs together with Other Activities Continuing are defined as continuing operations under IFRS 5. Due to our intention to sell our former Business Units Pulcra Chemicals and Oleochemicals as well as the Thai Fatty Alcohols business, we classified all assets and liabilities of these businesses as "held for sale". The results of all three businesses are classified as discontinued operations. All

three businesses were sold prior to the year-end, as such assets and liabilities "held for sale" and discontinued operations only include amounts and results up to the month of the respective divestments.

Restatement of Prior-Year Figures

For comparability, we have changed the prior-year figures in this report to take into account the changes described above. The prior-year figures therefore, differ from the figures published in 2007. SBU last twelve months figures and commentaries are based on the amended prior-year figures.

Continuing Operations

The sales revenue of our continuing businesses for 2008, and for the comparative prior period were as follows:

€ millions	Continuing Operations			
	2008	% of total	2007 ²⁾	% of total
Net sales¹⁾				
Care Chemicals	1,684	56.1%	1,572	55.3%
Nutrition & Health	346	11.5%	332	11.7%
Functional Products	948	31.6%	908	31.9%
Other Activities Continuing	23	0.8%	32	1.1%
Total continuing operations	3,001	100.0%	2,844	100.0%

¹⁾ Including sales to Cognis' discontinued operations but excluding internal deliveries within Cognis' continuing operations.

²⁾ The 2007 figures have been changed to reflect continuing operations following the classification of Pulcra Chemicals, Oleochemicals and Thai Fatty Alcohols as discontinued operations which were subsequently sold prior to December 31, 2008.

The results of the individual businesses are discussed below.

Care Chemicals

Care Chemicals is a leading international supplier of products and formulations in the personal care and home care segments. With a clear focus on the worldwide wellness market, we offer active ingredients and technologies for enhanced application benefits and improved sensory performance. For the cosmetic, body care, laundry and household cleaner industries, we deliver innovative formulation competence and market-ready concepts geared to fulfilling consumer needs and providing them with an all-round well-being experience. With our profound knowledge of local and global market trends, we are able to generate new ideas, providing solutions that create competitive advantages for our partners and customers.

With the "Feelosophy" concept, Care Chemicals offers wellness-driven concepts and solutions that focus on primary consumer demands, and above all on the four key dimensions of a holistic product experience: Perception, Feel, Effect and Usage. These dimensions emphasize our key competencies, namely formulation technology and performance expertise, the use of natural raw materials and active ingredients, and our comprehensive understanding of marketing techniques and consumer preferences across all our markets.

In 2008, Care Chemicals generated sales of €1,684 million, representing 56.1% of our Group continuing sales.

Acquisitions, divestments and changes in structure

There were no acquisitions, divestments or changes in structure in 2008 and 2007.

Business Development in 2008

In 2008, Care Chemicals reported net sales of €1,684 million, an increase of €112 million or 7.1% compared to €1,572 million in 2007. On an organic basis, sales growth amounted to €154 million or 9.8%. This development was mainly supported by strong growth of our Care Performance Ingredients ("CPI") and Primary Surfactants business segments while sales of Fatty Alcohols were lower than prior year.

We experienced double-digit growth rates in the entire CPI product portfolio in Asia-Pacific, Latin America and North America. Within the premium and high added-value product portfolio segment, Europe achieved growth rates ahead of GDP. In both segments, the continued focus on the "Green Chemistry" market where Care Chemicals offers our Green Chemical Solutions™ drove the sales growth in 2008. Care Chemicals achieved this growth in a year marked by very volatile raw material prices as such the increase was necessary to compensate for increases in raw material prices and sustain margins.

The Care Surfactants and Fatty Alcohols business faced a challenging environment in 2008. Primary Surfactants recorded strong sales growth in 2008 compared to 2007, with double-digit growth rates in Asia-Pacific and in the Mercosur region. However, the Fatty Alcohols business was affected by new capacities from Asia which influenced selling prices in the market. Selling prices were increased to cover higher raw material prices but because lower volumes were sold, sales of Fatty Alcohols were below prior year.

Nutrition & Health

Our Nutrition & Health SBU is also focused on the wellness trend and is a leading supplier in various fields of food technology and dietary supplements. The Food Technology business involves the production and global supply of emulsifiers, whisking and whipping agents, enzymes, fats and powders into the various sales channels of the nutrition business. Nutrition & Health also produces and markets a broad range of ingredients, some of which are scientifically substantiated for the functional food and the dietary supplements markets and include phytosterols (plant sterols), conjugated linoleic acids ("CLA"), vitamin E and other natural-source products such as carotenoids and plant extracts. In addition, Nutrition & Health produces and sells a wide range of excipients and carriers based on natural raw materials for the pharmaceutical and life-science industries.

In 2008, Nutrition & Health generated sales of €346 million, representing 11.5% of our Group continuing sales.

Acquisitions, divestments and changes in structure

On February 29, 2008, Cognis acquired an interest of 12% in the natural product specialist InterMed Discovery GmbH. This cooperation with InterMed Discovery allows Cognis to discover and develop innovative products for the life-science industry and therefore tremendously enhances Nutrition & Health's R&D capabilities.

Besides the above, there were no acquisitions, divestments or changes in structure in 2008.

In June 2007, Cognis acquired certain patents, know-how and equipment related to the production of natural beta-carotene in Australia.

Business Development in 2008

In 2008, Nutrition & Health increased net sales by €14 million or 4.4% to €346 million compared to €332 million in 2007. On an organic basis, net sales grew by €21 million or 6.3% mainly driven by Vitamin E, Food Technology, Omega-3 and Sterols.

Natural-based Vitamin E showed excellent growth rates in 2008, especially in North America but also in Asia-Pacific. Vitamin E in 2008 benefited from higher demand led by the global trend toward production based on natural ingredients and away from production favoring synthetic ingredients.

The Food Technology business achieved an increase in sales compared to 2007 as a result of strong market penetration in the baked goods and dessert business segments, and also from higher selling prices in response to an increase in raw material prices.

Pharma & Health as well as Omega-3 achieved solid growth in 2008. The Pharma & Health business continued to benefit by complying with quality standards for pharma-grade specialties. Tonalin® CLA sales were generally affected by pending regulatory approvals. Our Sterols business increased slightly compared to 2007 driven mostly by demand from growth markets such as Asia-Pacific and Latin America.

Taking the regional perspective, we achieved moderate sales growth in Europe primarily driven by increased sales of Omega-3 and Food Ingredients, strong growth in North America and doubledigit growth in Asia-Pacific. A switch to direct selling in Latin America two years ago resulted in the doubling of sales in the region in 2008 compared to 2007.

Functional Products

The Functional Products SBU provides chemical solutions designed to enhance the performance and cost efficiency of our customers' products and formulations. The products and technical expertise of Functional Products are used by customers across the polymers, coatings and inks ("PCI"), synthetic lubricants, agriculture and mining sectors. The key expertise of Functional Products lies in its know-how in the chemistry of surfaces combined with its tradition in and focus on developing ecologically sound solutions.

In 2008, Functional Products generated sales of €948 million, representing 31.6% of our Group continuing sales.

Acquisitions, divestments and changes in structure

On July 10, 2008, we sold our Functional Products' isostearic acid business.

Besides the above, there were no acquisitions, divestments or changes in structure in 2008.

In November 2007, the G-Cure® business was sold. The G-Cure® business consists of acrylic polyol-based resins for the industrial coatings industry and was part of the PCI business segment in the USA.

Business Development in 2008

Functional Products' 2008 net sales increased by €40 million or 4.4% to €948 million from €908 million in 2007. Organic sales growth amounted to €94 million or 10.3%. All business segments contributed to the sales growth which was mainly driven by strong worldwide demand for environmentally friendly agricultural solutions and for synthetic lubricants used in industrial and automotive applications.

Sales of the PCI business grew mainly in South America driven by growth of the Coatings Additives products range. Sales in North America and Europe were negatively affected by the slow-down in the US housing sector and the global automotive sector.

The Synthetic Lubricants business expanded sales worldwide, driven by strong demand for ester products used in various industrial markets and also growth in compounded lubricants in the emerging markets and in Europe. In Asia, our business with refrigeration lubes for compressors continued to expand.

In the AgroSolutions business, Functional Products experienced strong worldwide growth in 2008. This was due to the combination of strong demand from key accounts and also favorable market conditions for farmers such as good crop prices and favorable weather.

Sales of the Mining Technology business continued to grow compared to 2007, mainly because of a higher number of new copper-producing installations coming on stream in 2008. We achieved sales growth despite a weaker US dollar and a rapid decline in copper prices in the second half of 2008.

Other Activities Continuing

Net sales of Other Activities include contract manufacturing activities with third parties and other secondary activities. In addition, the results of Other Activities also include other divisional costs of Pulcra Chemicals and Oleochemicals. Other divisional costs comprise remaining administrative and technical service costs formerly allocated to Oleochemicals and Pulcra Chemicals.

Business Development in 2008

Other Activities' 2008 net sales were –€9 million lower than in 2007 mainly due to the termination of agency and distribution agreements between Cognis entities and Oleochemicals entities for the sale of Oleochemicals products. Second, we reclassified contract manufacturing activities conducted for Pulcra Chemicals from Other Activities to the originating SBUs.

Discontinued Operations

The sales revenue of our discontinued operations for 2008, and for the comparative prior periods were as follows:

€ millions	Discontinued Operations			
	2008 ⁴⁾	% of total	2007 ⁵⁾	% of total
Net sales				
Pulcra Chemicals ¹⁾	190	20.5%	245	25.2%
Oleochemicals ²⁾	734	79.2%	729	74.8%
Other Activities Discontinued ³⁾	3	0.3%	–	0.0%
Total discontinued operations	927	100.0%	974	100.0%

¹⁾ Including sales to Cognis' continuing operations and Oleochemicals but excluding internal deliveries within Pulcra Chemicals.

²⁾ Including sales to Cognis' continuing operations and Pulcra Chemicals but excluding internal deliveries within Oleochemicals.

³⁾ Including sales to Cognis' continuing operations but excluding internal deliveries within Other Activities Discontinued.

⁴⁾ 2008 only includes figures of discontinued operations up to the month of the respective divestments.

⁵⁾ 2007 figures have been changed to reflect changes in the business structure as described earlier and the classification of results per IFRS 5.

The results of the individual businesses are discussed below.

Pulcra Chemicals

Pulcra Chemicals, which supplies process chemicals to the textile and leather industries, was previously the Process Chemicals Strategic Business Unit ("SBU") of Cognis. The SBU was carved out into separate legal entities on July 1, 2007, and renamed Pulcra Chemicals.

Divestment of the Pulcra Chemicals business

On October 31, 2008, we sold Pulcra Chemicals, to Fashion Chemicals GmbH & Co. KG ("Fashion Chemicals"). Fashion Chemicals is backed by the Pulcra Chemicals management and other stakeholders including leading tanneries and leather manufacturers. The closing of the transaction follows the signing of an agreement on July 14, 2008 to sell Pulcra Chemicals and regulatory approvals obtained from the relevant authorities. The cash proceeds from this transaction amount to about €23 million.

Business Development in 2008

The business development of Pulcra Chemicals in 2008 is not directly comparable to the business development in 2007. 2008 only includes figures of Pulcra Chemicals up to the date of deconsolidation, i.e. October 31, 2008.

However, during the period prior to deconsolidation, Pulcra Chemicals experienced lower sales in 2008 as a result of lower volumes in both, the Leather Technology and Textile Technology business segments due to an unfavorable market environment.

Oleochemicals

Oleochemicals is a leading producer of natural-based oleochemicals especially fatty acids, fatty acid esters and glycerine.

Divestment of the Oleochemicals business

On July 23, 2008, we signed an agreement to sell our 50 percent stake in the Oleochemicals joint venture to PTT Chemical International Private Ltd. The closing of the transaction took place on November 24, 2008 after relevant regulatory approvals were obtained. The cash proceeds from this transaction amount to about €104 million.

By selling our stake to well a known partner we ensure a stable supply of our oleochemical basestocks is secured, as we are intending to continue sourcing products from Oleochemicals.

Business Development in 2008

The business development of Oleochemicals in 2008 is not directly comparable to the business development in 2007. 2008 only includes figures of Oleochemicals up to the date of deconsolidation, i.e. November 24, 2008.

During the period prior to deconsolidation, Oleochemicals experienced higher sales driven by higher Glycerin prices.

Other Activities Discontinued

On November 14, 2008 we sold our 50 percent stake in the Thai Fatty Alcohols Company Ltd. joint venture, to Thai Oleochemicals Company Ltd., a subsidiary of PTT Chemicals Public Company Limited. The joint venture was founded in 2006 for the production and marketing of fatty alcohols.

Research & Development and Technical Service

Research & Development and Technical Service Expenditure			
€ millions	Continuing Operations		As Published
	2008	2007 ¹⁾	2007 ²⁾
Research and development expense	85	81	91
Less: Amortization included in R&D expense	(34)	(33)	(35)
Add: Capitalization of development costs	10	8	8
Total research & development expenditure	61	56	64
Add: Technical service costs	25	26	33
Total	86	82	97

¹⁾ 2007 figures have been restated to exclude discontinued operations.

²⁾ As published previous year.

Continuing Operations

Care Chemicals

Demand for green and sustainable products and concepts is ever increasing. We have gained a broad experience in providing exactly the right solutions in response, using renewable resources such as plant oils, carbohydrates and proteins to develop appropriate concepts for the personal care and home care markets. To strengthen our key competences in this area, we joined an industrial platform called "BioHub" with the aim of exploring the potential of using specialty carbohydrates as raw materials. The use of renewable resources is one important component of sustainable development, which we want to address in a broader sense. Therefore, we have defined measures that allow us to align our development activities to the twenty-four principles of "Green Chemistry" and "Green Engineering". These measures will also be used as a guideline for future R&D of new products and processes.

Our approach to product development is holistic, taking into account not only the "green" aspects of products and concepts, but also the need for exceptional product performance in all aspects relevant for the consumer. This is evident in new surfactants and waxes from our Plantapon® and Euperlan® lines which are based on plant oils, carbohydrates and hydroxy acids. They generated high interest in the market place and demand for these products is clearly increasing.

In the area of Polymers we have also launched new products in 2008 for various applications such as a new Polyquart® type for the treatment of hard surfaces in the Home Care segment, as well as new stabilizers and rheology modifiers for personal care formulations. Cosmedia® SP, an emulsifying polymer and one of the pioneer products in our polymer pipeline, received the Cognis Innovation Award for 2008.

As for formulation technology, we have developed new application concepts for dispersions by adjusting and controlling a defined distribution of the particle size. We have also developed new types of nano-emulsions that extend our formulation capabilities beyond the established PIT (phase inversion technology).

In the field of anti-aging active ingredients, we continued the development of oligopeptides with specific anti-aging properties and claims and launched a third product out of this series, namely Skinasensyl® in the market. The oligopeptide Dermican™ launched in 2006, also received the Cognis Innovation Award for 2008.

Nutrition & Health

Nutrition & Health's research and development driven by the needs of our customers activity focuses strongly on customer-oriented product development and technical services characterized by tailor-made formulations and close relationships with key accounts.

To safeguard our innovation pipeline and foster our R&D capabilities, we have started an exclusive and globally unique partnership with InterMed Discovery, the worldwide leading library of pure natural product compounds. Our partnership with InterMed Discovery facilitated several projects in offering novel ingredients on weight management and cardiovascular diseases to our customers worldwide. This partnership provides a sound basis for a continuous market launch of innovative exclusive active ingredients for Functional Food.

Further, we were successful in enhancing and improving our strong innovation capabilities by setting up new scientific platforms for “Brain Health” and “Beauty From Within” to serve the wellness megatrend.

We were successful in gaining further scientific evidence on the efficacy and safety of Tonalin® CLA (conjugated linoleic acid). As a consequence, we received the final FDA-GRAS (US Food and Drug Administration—Generally Recognized As Safe) approval for Tonalin® in the US. In addition, we achieved TGA (Therapeutic Goods Administration) approval in Australia for Vegapure®, our sterol esters product range.

Our portfolio also includes the Omevital™ Omega-3 products. Research and Development for these products concentrate on offering high quality solutions with excellent sensory qualities to the functional food and beverage markets. One remarkable milestone was the development of a high-quality Omega-3 powder for our customers.

Research within our PharmaLine® product range is aimed at achieving a continuous improvement in the purity and process integrity of our products. We completed the USP (United States Pharmacopeia) monograph for our Chitosan® product, and developed a water soluble form of vitamin E called TPGS (d-alpha Tocopheryl-Polyethylenglycolsuccinat).

The R&D activities of Nutrition & Health are also aimed at continuous process and cost improvements. We achieve these improvements by maintaining high quality, standardized but carefully controlled raw materials and finished products.

Functional Products

Public awareness of environmental impacts of hazardous chemicals supports Functional Products’ drive towards green, environmentally friendly, label-free and zero VOC (“Volatile Organic Compound”) products in the segments of Coatings, E/P (Emulsion Polymerization) Surfactants, Lubricants and Agrochemicals.

In 2008, Functional Products’ AgroSolutions team won the gold prize at the Cognis Innovation Award for its high performance adjuvant against Asian Rust. Customer specific innovation projects resulted in significant growth in AgroSolutions for 2008. In line with this, a new generation of sugar based surfactants for glyphosate, the biggest active ingredient in the agricultural market was launched in the market.

In the area of Synthetic Lubricants, Cognis was nominated for the European Frost & Sullivan award for Biolubricants with the ProEco™ HE 801 Biohydraulic fluid. Successful development and market penetration in the area of transportation lubes allowed a major OEM (Original Equipment Manufacturer) Truck manufacturer to completely switch to fuel efficient axle lubes based on Cognis’ technology.

In Coatings, Dehydran SE -1, the first of a series of new defoamers was launched in 2008 and delivers better performance combined with zero VOC to the market. The Loxanol EFC (Emission Free Coalescent) was extended by new developments to meet market requirements of renewable coalescent additives.

Functional Products formed a Global Technology Council designed to enhance the efficient leveraging of its R&D capabilities and know-how across all regions and to ensure a strong link between R&D investment and the businesses’ strategic focus areas for growth.

Patents

In 2008, Cognis filed some 75 new patent applications and was granted 65 patents by the European, US and German patent offices.

Discontinued Operations

The R&D activities of Oleochemicals, Pulcra Chemicals and Thai Fatty Alcohols have been separated from Cognis’ R&D activities after the sale of all three businesses in 2008. As such, the R&D activities are focused on their specific business needs.

Employees

Workforce by function at balance sheet date				
Number	Year ended December 31,	Continuing Operations		As Published
		2008	2007 ¹⁾	2007 ²⁾
Production		3,220	3,249	4,145
Research & Development		439	429	705
Sales & Marketing		626	634	879
Supply Chain/Purchasing		642	637	768
Administration		953	1,060	1,088
Total		5,880	6,009	7,585

¹⁾ 2007 has been restated to exclude the headcount of discontinued operations.

²⁾ As published previous year.

The number of employees at December 31, 2008 was 5,880, a decrease of –1,705 compared to 7,585 employees at December 31, 2007. The decrease of –1,705 employees includes 1,576 employees related to our discontinued operations which were sold before the year-end.

On a comparable continuing basis, Cognis' number of employees worldwide, excluding trainees, apprentices and interns, amounted to 5,880 at December 31, 2008, a decrease of –129 compared to 6,009 at December 31, 2007. The decrease was mainly the result of a restructuring program and, to a lesser extent, a more restrictive and controlled hiring policy.

In the functional breakdown, the number of employees in Administration decreased by –107, in Production by –29 and in Sales & Marketing by –8, whereas the number of employees in Research & Development increased by +10 and in Supply Chain/Purchasing by +5.

From a regional perspective, headcount in Germany decreased by –5 and in the rest of Europe including South Africa by –89. In NAFTA, the number of employees fell by –35. The number of employees in Central and South America as well as Asia-Pacific remained stable.

In 2008, the number of trainees, apprentices and interns was 164, representing a decrease of –24 from 188 in 2007. Including trainees, apprentices and interns, the total number of employees at December 31, 2008 was 6,044 compared to 6,197 at December 31, 2007.

Capital Expenditures

Capital expenditures by region		
€ millions	2008	2007
Germany ¹⁾	52	51
Rest of Europe ¹⁾	25	23
North America ¹⁾	15	22
Central and South America ¹⁾	3	2
Asia-Pacific ¹⁾	4	3
Total capital expenditures continuing operations ¹⁾	99	101
Total capital expenditures discontinued operations ²⁾	12	31
Total capital expenditures²⁾	111	132

¹⁾ 2007 has been restated to exclude capital expenditures of discontinued operations.

²⁾ 2008 figures include Pulcra Chemicals, Oleochemicals and Thai Fatty Alcohols up to the month of classification as assets held for sale.

Our capital expenditures for tangible and intangible assets in 2008 of continuing and discontinued operations together amounted to €111 million, a decrease of €21 million compared to 2007. Capital expenditures in 2008 include €12 million for discontinued operations.

On a comparable continuing basis, capital expenditures decreased by €2 million from €101 million in 2007 to €99 million in 2008. The decrease was mainly due to lower investments in North America, where in 2007 major capital expenditure related to Functional Products' manufacturing in Cincinnati was undertaken. In 2008, we invested a significant amount in growth projects at Care Chemicals, Nutrition & Health and Functional Products. Investments also focused on cost improvement and replacement activities in all businesses.

Continuing Operations

Significant capital expenditures in 2008 for our continuing operations:

- In our largest production site in Düsseldorf (Germany), we initiated, continued or completed growth projects to support the core businesses of Care Chemicals and Functional Products; we also continued projects to optimize costs
- We introduced a new in-house hardware and software solution to manage our central finished goods warehouse
- In our Illertissen plant in Germany, we completed a project started in 2007 and assigned to the Nutrition & Health SBU to increase production capacities for sterol esters
- In France, we completed projects for insourcing our filling activities and the establishment of a new warehouse to improve our supply chain. The lease expenses for this warehouse were capitalized in line with IFRIC 4 (embedded leases) and recognized as finance leases
- We also started a new project to modernize and expand facilities for Care Chemicals' active ingredients business in our competence center in Nancy (France)
- In our site in Kankakee (USA), we completed a project to debottle-neck and modernize our sulfation facilities in order to follow the trend toward higher active sulfates based on SO₃ technology; we also completed projects for the purpose of conforming with local environmental protection standards (MON) in all our US sites

Discontinued Operations

Capital expenditures of discontinued operations decreased by €19 million from €31 million in 2007 to €12 million in 2008 mainly because capital expenditures in 2008 only include expenditures till date of classification as assets held for sale. From that date till the date of divestment a further €10 million in capital expenditure was incurred.

Financial Position, Liquidity and Capital Resources

€ millions	As of December 31,	Continuing Operations		As Published
		2008	2007 ⁴⁾	2007 ⁵⁾
Total assets		2,085	2,078	2,505
Trade working capital ¹⁾		595	544	745
Equity ²⁾		(812)	(716)	(716)
Pension provisions		405	399	435
Nominal net debt ³⁾		1,829	1,922	1,979

¹⁾ Trade working capital consists of trade receivables and inventories, net of trade payables.

²⁾ Equity attributable to the Group's equity holders.

³⁾ Excludes pension provisions, deferred financing fees and accrued interest.

⁴⁾ 2007 has been restated to exclude assets and liabilities of discontinued operations.

⁵⁾ Prior period represents Group figures including discontinued operations in accordance with IFRS 5.

Total assets

Total assets decreased by –€420 million from €2,505 million at December 31, 2007 to €2,085 million at December 31, 2008. This was mainly due to the divestment of our discontinued operations prior to year-end.

On a comparable continuing basis, total assets increased by +€7 million from €2,078 million as of December 31, 2007 to €2,085 million as of December 31, 2008.

This is mainly due to higher cash and cash equivalents (+€117 million) as a result of divestment proceeds from the sales of our discontinued operations and increased inventories (+€9 million) reflecting higher prices for raw materials in the first half of the year.

These factors were partially offset by lower fixed assets (–€62 million) and the repayment of the loan provided to Cognis Holding GmbH (–€32 million). The loan was provided to Cognis Holding GmbH to pay for withholding taxes due on the capital distribution in connection with the Refinancing Transaction in 2007. Cognis Holding GmbH repaid the loan in 1H/2008 upon receiving the refund of the withholding taxes. Further, a decrease in trade receivables (–€20 million) due to lower sales in November and December 2008 compared to 2007 as well as better collection, plus decreased derivative financial instruments (–€3 million) and lower other assets (–€3 million) further offset the increase in total assets.

Trade Working Capital				
€ millions	As of December 31,	Continuing Operations		As Published
		2008 ¹⁾	2007 ^{1) 2)}	2007 ^{3) 4)}
Net sales (YTD)/net external sales (YTD)		3,001	2,844	3,518
Trade receivables		423	443	566
% Annualized sales		14.1%	15.6%	16.1%
Inventories		408	399	526
% Annualized sales		13.6%	14.0%	15.0%
Trade payables		(236)	(298)	(347)
% Annualized sales		-7.9%	-10.5%	-9.9%
Trade working capital		595	544	745
% Annualized sales		19.8%	19.1%	21.2%

¹⁾ % Annualized sales are based on net sales of continuing operations.

²⁾ 2007 has been restated to exclude assets and liabilities of discontinued operations.

³⁾ Prior period represents Group figures including discontinued operations in accordance with IFRS 5 as stated in the Consolidated Financial Statements.

⁴⁾ % Annualized sales are based on net external sales of the Group prior to application of IFRS 5.

December 31, 2008 versus December 31, 2007

Trade working capital decreased by –€150 million from €745 million as of December 31, 2007 to €595 million as of December 31, 2008. This is mainly because of the absence of trade working capital related to discontinued operations which were divested prior to year-end.

On a comparable continuing basis, trade working capital increased by +€51 million to €595 million as of December 31, 2008 from €544 million as of December 31, 2007.

Adjusted for currency effects, trade working capital increased by +€68 million between December 31, 2007 and December 31, 2008. This increase is mainly due to lower trade payables because of destocking activities and lower volumes produced in the light of the global economic situation. However, we also recorded higher inventory values as prices for raw materials increased in the first half of the year. Lower payables and, to a lesser extent, higher inventories contributed to the increase in trade working capital. The decrease in trade receivables as a result of lower sales in November and December 2008 compared to 2007 partially mitigated this increase.

We purchase and hold inventory including lauric oils on the basis of a strategic procurement program. The objective of this program is to optimize our lauric oil feedstock by purchasing based on our expectations of overall market supply, demand and pricing. Our lauric oil stocks decreased by –€11 million from December 31, 2007 to December 31, 2008, mainly due to lower volumes resulting from decreased inventory days.

From an absolute increase of +€51 million, excluding foreign exchange effects of +€17 million and decreased stocks of lauric oils of +€11 million, trade working capital increased by +€79 million.

Equity

Our Equity attributable to the Group's equity holders decreased by –€96 million to negative €812 million at December 31, 2008 from negative €716 million at December 31, 2007. The decrease was mainly due to a net loss for the period excluding minority interests of –€70 million, negative foreign currency translation losses (including IAS 21 reserve) of –€28 million and a capital contribution of –€2 million to Cognis Beteiligungs-GmbH, our immediate parent company. Cognis Beteiligungs-GmbH used the dividends for payment of real estate taxes resulting from the Refinancing Transaction. These effects were mitigated by gains from cash flow hedges amounted to +€4 million recognized directly in equity.

Pensions

€ millions	As of December 31,	Continuing Operations		As Published
		2008	2007	2007
Provisions for pensions and similar obligations at January 1		399	407	444
Current service cost		13	14	16
Operating actuarial losses		2	1	1
Pension costs		15	15	17
Other costs for obligations similar to pensions		(3)	(3)	(3)
Pension costs included in EBITDA		12	12	14
Interest expense		38	38	40
Expected return on plan assets		(19)	(20)	(21)
Financial actuarial losses		2	4	4
Net interest expense		21	22	23
Total cost of pension and similar obligations		33	34	37
Cash utilized		(29)	(36)	(40)
Cash payments to beneficiaries		(26)	(26)	(27)
Contributions to plan assets		(3)	(10)	(13)
Other movements		–	–	1
Translation differences		2	(6)	(7)
Provisions for pensions and similar obligations at December 31		405	399	435
thereof discontinued operations				36

We offer our employees various defined benefit retirement plans around the world. In 2008, we made cash payments related to pensions of €29 million (2007: €36 million) in both retirement benefits and contributions to plan assets of continuing operations.

Also, pension costs of €12 million (2007: €12 million) are included in EBITDA.

€ millions	As of December 31,	Continuing Operations		As Published
		2008	2007	2007
Present value of unfunded defined benefit obligations		401	418	452
Present value of funded defined benefit obligations		262	273	299
Fair value of plan assets		(174)	(252)	(274)
		489	439	477
Unrecognized actuarial (losses)/gains		(95)	(52)	(55)
Unrecognized past service (costs)/gains		11	12	13
Provisions for pensions and similar obligations—continuing operations		405	399	
Provisions for pensions and similar obligations—discontinued operations		–	36 ¹⁾	
Provisions for pensions and similar obligations		405	435	435

¹⁾ Defined benefit obligation amounted to €60 million, plan assets to –€22 million and unrecognized actuarial losses to –€2 million.

%	2008	2007	2008	2007
	Germany		USA	
Discount rate	6.1	5.4	6.4	6.0
Future salary increase (in USA, including benefit increase)	2.5	2.5	4.5	4.5
Future benefits increase	1.0–1.75	1.0–1.5	–	–
Medical Cost Trend	–	–	8.5	9.0
Expected return on plan assets	–	–	8.25	8.5
Actual return on plan assets	–	–	–28.0	9.3

Pension provisions of continuing operations in 2008 increased by +€6 million to €405 million reflecting cash paid to beneficiaries (–€26 million) and to plan assets (–€3 million) compensated for by pension costs (+€33 million) and foreign currency effects (+€2 million). There was no significant release of provisions included in pension costs in 2008.

Net Debt and Liquidity

Our nominal net debt, translated at foreign exchange rates in effect on the balance sheet dates, has developed as follows:

€ millions	As of December 31,	Continuing Operations		As Published
		2008	2007 ³⁾	2007 ⁴⁾
Senior Subordinated Notes ¹⁾		345	345	345
Senior Secured Floating Rate Notes ¹⁾		821	809	809
Senior Secured Floating Rate Loans ¹⁾		821	809	809
Finance lease obligations		37	30	30
Oleochemicals borrowings		–	–	69
Other bank debts		31	38	49
Total debt		2,055	2,031	2,111
Cash and cash equivalents		(226)	(109)	(132)
Net debt of Cognis GmbH		1,829	1,922	1,979
PIK Loans of Cognis Holding GmbH ²⁾		434	385	385
Cash and cash equivalents of Cognis Holding GmbH		(1)	(1)	(1)
Net debt of Cognis Holding GmbH		433	384	384
Net debt of Cognis Holding GmbH Group		2,262	2,306	2,363

¹⁾ Excludes deferred financing fees and accrued interest.

²⁾ Excludes deferred financing fees and includes accrued interest.

³⁾ 2007 has been restated to exclude assets and liabilities of discontinued operations.

⁴⁾ Prior period represents Group figures including discontinued operations in accordance with IFRS 5.

December 31, 2008 versus December 31, 2007

The change of Cognis' net debt from December 31, 2007 to December 31, 2008 includes the reduction in net debt related to our discontinued operations which we divested prior to year-end.

Net debt decreased by €150 million from December 31, 2007 to December 31, 2008. Net debt as of December 31, 2007 includes those of discontinued operations amounting to €57 million¹⁴⁾.

On a comparable continuing basis, net debt decreased by €93 million because of the following:

- Cash generated before debt borrowing and repayments as of December 31, 2008, resulting in an inflow of €131 million for continuing operations which mirrors cash proceeds received from the divestment of our discontinued operations amounting to €131 million; this inflow effectively reduced net debt

- The strengthening of the US dollar compared to the euro between December 31, 2007 and December 31, 2008 of around 5% (USD from 1.4721 to 1.3917), resulting in a non-cash foreign exchange loss of €23 million; this increased the euro carrying value of the US dollar debt
- Finance lease obligations increased by €7 million due to a new logistics agreement for a new warehouse whereas other bank debt decreased by €7 million due to lower local borrowings. Both factors roughly offset each other

¹⁴⁾ €57 million represents €69 million Oleochemicals borrowings, €5 million local Oleochemicals borrowings included in other bank debt, €3 million local Pulcra Chemicals borrowings also included in other bank debt, €3 million local borrowings of Thai Fatty Alcohols included in other bank debt and cash and cash equivalents of all three operations together of €23 million as of December 31, 2007.

The PIK Loan is not included in the net debt of Cognis GmbH and is neither guaranteed by any of the constituent entities nor secured by any assets of the Cognis GmbH Group. The increase of €49 million in the PIK Loan from December 31, 2007 to December 31, 2008 was a result of €38 million interest capitalized during the year and €11 million in accrued interest included in the PIK Loan.

As of December 31, 2008, we have purchased PIK Loans amounting to a face value of €3 million in an open-market transaction. As of February 18, 2009, the face value of PIK Loans purchased amounted to €47.5 million.

Covenants

The loan agreements and the notes indentures contain covenants that limit, among other things, the ability of Cognis GmbH and certain subsidiaries to

- incur additional indebtedness;
- make certain restricted payments;
- transfer or sell assets;
- enter into transactions with affiliates;
- create certain liens;
- create restrictions on the ability of certain subsidiaries to pay dividends or other payments;
- issue guarantees of indebtedness by certain subsidiaries;
- enter into sale and leaseback transactions;
- merge, consolidate, amalgamate or combine with other entities.

Each of the covenants is subject to a number of important exceptions and qualifications.

Throughout 2008, Cognis GmbH and Cognis Holding GmbH were fully compliant with the various financing agreements in place.

Net debt is reconciled to balance sheet borrowings in the following table:

€ millions	Continuing Operations		As Published
	2008	2007 ²⁾	2007 ³⁾
Net debt	1,829	1,922	1,979
Accrued interest ¹⁾	8	9	10
Deferred financing fees	(47)	(54)	(54)
Cash and cash equivalents	226	109	132
Borrowings	2,016	1,986	2,067
Thereof current	35	36	73
Thereof non-current	1,981	1,950	1,994

¹⁾ On Senior Subordinated Notes and Senior Secured Floating Rate Notes and Loans.

²⁾ 2007 has been restated to exclude assets and liabilities of discontinued operations.

³⁾ Prior period represents Group figures including discontinued operations in accordance with IFRS 5.

Cognis Holding GmbH, Cognis GmbH, their affiliates or other related parties may or may not opportunistically purchase debt in one or a series of open-market transactions from time to time. We refer to the PIK loan purchases as reported in the section above.

Liquidity

As of December 31, 2008, cash and cash equivalents amounted to €226 million including cash proceeds from the divestment of discontinued operations. Further, as of December 31, 2008, there is an undrawn Revolving Credit Facility available of €250 million less €29 million utilized for ancillary facilities and letters of credit.

Off-Balance-Sheet Arrangements

For contingent liabilities and other financial commitments, refer to Note 30 of the Notes to the Consolidated Financial Statement.

Net Cash Flow			
€ millions	Year ended December 31,	2008⁵⁾	2007
Adjusted EBITDA continuing operations		351	360
Adjusted EBITDA discontinued operations		32	50
Cash restructuring expense ¹⁾		(25)	(37)
Other exceptional items ²⁾		(2)	(5)
Change in trade working capital ^{3),4)}		(49)	(65)
Change in other working capital ⁴⁾		(11)	(21)
Income taxes paid		(32)	(31)
(Gains)/losses on disposal and other adjustments		–	(6)
Cash flow from operating activities		264	245
(including cash flow from discontinued operating activities)		36	12
Capital expenditures		(111)	(132)
Other investing cash flows		128	11
Cash flow from investing activities		17	(121)
(including cash flow from discontinued investing activities)		(22)	(32)
Free Cash Flow		281	124
(including free cash flow from discontinued activities)		14	(20)
Cash interest		(143)	(142)
Capital repayments and distributions		(2)	(358)
Pension payments net of service cost		(19)	(26)
Derivatives, FX gains/(losses) and other		21	(95)
Cash flow before debt borrowing/(repayment)		138	(497)
(including cash flow before debt borrowing/(repayment) from discontinued financing activities)		7	(24)
Net debt borrowing/(repayment)		11	396
Net cash flow		149	(101)
(including net cash flow from discontinued activities)		29	(17)

¹⁾ Restructuring cash-out excluding restructuring capital expenditure.

²⁾ Excluding depreciation and amortization.

³⁾ Cash change in trade receivables, inventories and trade payables.

⁴⁾ Excluding change in restructuring provisions.

⁵⁾ 2008 includes figures of discontinued operations up to the month of divestment.

The 2008 figures include cash flows of the divested operations prior to their divestment. These activities were divested in the course of Q4/2008.

Cash flows from operating activities

The 2008 cash flow from operating activities of €264 million (including operating cash flow from discontinued operations of +€36 million) was +€19 million higher than in 2007. The cashflow is not directly comparable as cashflows of discontinued operations are only included until the divestment date. The following factors mainly contributed to the increase in operating cash inflow:

- The lower cash outflow in change in trade working capital (comprising trade and other working capital together) was mainly driven by a lower change in inventories, and improved collection of trade receivables which more than compensated for higher payments of trade payables
- Lower non-recurring items (comprising cash restructuring expenses and other exceptional items) of +€15 million mainly because of lower restructuring expenses
- Lower cash out from (gains)/losses on disposal and other adjustments of +€6 million.

The lower combined Adjusted EBITDA of –€27 million (including –€18 million from discontinued operations) partially offset the factors above.

Cash flows from investing activities

The 2008 cash inflows of +€17 million from investing activities (including cash flows related to discontinued operations of –€22 million) were influenced by the following factors:

- Capital expenditures of –€111 million in 2008 were +€21 million lower than in 2007; included in capital expenditure of –€111 million is –€22 million related to discontinued operations; on a comparable continuing basis, capital expenditure of –€89 million in 2008 was +€13 million lower than in 2007.
- Other investing cash inflows of +€128 million in 2008 mainly relate to disposal proceeds of discontinued operations amounting to +€131 million which were divested in Q4/2008; these proceeds were slightly offset by an outflow mainly related to the acquisition of an interest in the natural product specialist InterMed Discovery GmbH, Dortmund, Germany.

Cash flows from financing activities

Cash outflow before debt borrowing and repayment includes the following:

- Cash interest of –€143 million in 2008 including interest payments of –€53 million on Senior Secured Floating Rate Notes, –€53 million on Senior Secured Floating Rate Loans, –€33 million on Senior Subordinated Notes and –€3 million interest payments related to discontinued operations prior to their divestment
- Capital repayments and distributions including –€2 million dividends paid to Cognis Beteiligungs-GmbH. Our immediate parent company Cognis Beteiligungs-GmbH used the dividends for payment of real estate taxes resulting from the Refinancing Transaction
- Pension payments net of service cost of –€19 million were +€7 million lower than in 2007 as no contributions were made to Cognis' US pension plan assets in 2008
- Derivatives, FX gains/(losses) and other of +€21 million mainly include the repayment of a €32 million loan provided to Cognis Holding GmbH, our former immediate parent company in 1H/2007. The loan was provided to Cognis Holding GmbH to pay for withholding taxes due on the capital distribution. Cognis Holding GmbH repaid the loan in 1H/2008 upon receiving the refund of the withholding taxes.

Foreign exchange losses net of currency derivative settlements partly offset the €32 million inflow

- Net debt borrowing/(repayment) of +€11 million relating to local borrowings drawn by various affiliates.

Reconciliation of Restructuring Costs to Cash Restructuring Expenses			
€ millions	As of December 31,	2008	2007
Restructuring costs ¹⁾		27	49
Less: Depreciation and amortization ¹⁾		(5)	(9)
Less: Additions to restructuring provisions ¹⁾		(16)	(22)
Add: Restructuring provisions released ¹⁾		1	–
Add: Use of restructuring provisions ¹⁾		17	12
Total cash restructuring expenses of continuing operations		24	30
Total cash restructuring expenses of discontinued operations ²⁾		1	7
Total cash restructuring expenses²⁾		25	37

¹⁾ 2007 figures have been restated to exclude discontinued operations.

²⁾ 2008 only includes figures of discontinued operations up to the month of the respective divestments.

Cognis has implemented, and continues to implement, various restructuring initiatives in order to streamline processes and reduce costs.

Certain Factors Affecting Our Business

Our net assets, financial position and results of operations in the consolidated financial statements have been affected by a number of factors, including the effects of the acquisition of Cognis in 2001, industry trends, exchange rate fluctuations, the cost of raw materials, acquisitions and divestments, business realignment and cost reduction programs.

Effects of the Acquisition

As a result of the acquisition of Cognis on November 30, 2001, and other subsequent acquisitions, the assets and liabilities of the acquired entities were recognized at their fair values on the acquisition date. We refer to the difference between the book value immediately prior to the acquisition and the fair value recognized upon acquisition as “step-up”.

The depreciation and amortization related to the step-up of the carrying values of the assets (excluding goodwill) and liabilities as a result of the buy-out of Cognis and other acquisitions increased the depreciation and amortization expense of our continuing operations, including minor impairment losses, in 2008 by €37 million (2007: €38 million).

Exchange Rate Fluctuations

The translation effect¹⁵⁾ on our Adjusted EBITDA resulting from the weakening of the US dollar and other non-euro currencies against the euro in 2008, as compared to 2007, was -€6 million and mostly influenced our Care Chemicals and Functional Products SBUs.

The transaction effect¹⁶⁾ on our Adjusted EBITDA is not directly quantifiable.

Acquisitions and Divestments

On November 24, 2008 we sold our 50 percent stake in the Oleochemicals joint venture to PTT Chemical International Private Ltd. The closing of the transaction follows the signing of an agreement on July 23, 2008 to sell Oleochemicals and regulatory approvals obtained from the relevant authorities. For details concerning the business performance and the results, please refer to the section “Management’s Discussion and Analysis—Strategic Business Units and Segment Results”.

On November 14, 2008 we sold our 50 percent stake in the Thai Fatty Alcohols Company Ltd. joint venture, to Thai Oleochemicals Company Ltd., a subsidiary of PTT Chemicals Public Company Limited. The impact of the sale on the Group’s results is not material.

On October 31, 2008 we sold Pulcra Chemicals to Germany-based Fashion Chemicals GmbH & Co. KG. The closing of the transaction follows the signing of an agreement on July 14, 2008 to sell Pulcra Chemicals and regulatory approvals obtained from the relevant authorities. For more details concerning this transaction, please refer to the section “Management’s Discussion and Analysis—Strategic Business Units and Segment Results”.

For details concerning the divestment of discontinued operations, refer to “Management’s Discussion and Analysis—EBIT, EBITDA and Adjusted EBITDA: Discontinued Operations”, “Consolidated Financial Statements—Group Segment Reporting” and “Notes to the Consolidated Financial Statements—Note 20”.

On July 10, 2008 we sold our Functional Products’ Isostearic Acid business.

On February 29, 2008 Cognis acquired an interest of 12% in the natural product specialist InterMed Discovery GmbH. This cooperation with InterMed Discovery allows Cognis to discover and develop innovative products for the life-science industry and therefore tremendously enhances Nutrition & Health’s R&D capabilities. On December 12, 2008 Cognis participated in a capital increase of InterMed Discovery GmbH in order to maintain its original shareholding stake.

In November 2007, the G-Cure® business was sold. The business consists of acrylic polyol-based resins for the industrial coatings industry and was part of the PCI business segment of our Functional Products SBU in the USA. G-Cure® products are sold primarily into the heavy- and light-duty industrial maintenance and automotive refinish markets.

In June 2007, Cognis acquired certain patents, know-how and equipment related to the production of natural beta-carotene in Australia.

In February 2007, Cognis Oleochemicals (Malaysia) Sdn. Bhd. (“COM”) paid an additional purchase price of €8 million due to a settlement agreement and the achievement of certain targets as agreed in the share purchase agreement related to the sale of the Oleochemicals business to COM, our 50:50 Malaysian joint venture.

¹⁵⁾ Our financial results are impacted by both translation and transaction currency effects resulting from changes in currency exchange rates. Translation currency effects occur when the financial results of our subsidiaries outside the euro region, as measured in their non-euro, local currencies, are translated into euros using the exchange rate prevailing during the relevant period. Consequently, the results of these subsidiaries as expressed in euros for different periods have been translated using different exchange rates.

¹⁶⁾ Transaction currency effects occur when one of our subsidiaries incurs costs or earns revenues in a currency different from its functional currency. Since transactions in foreign currencies are generally translated into the functional currency using the exchange rates in effect when the transactions occur, changes in exchange rates affect the measurement of foreign currency revenues and costs in the functional currency, and so influence the profitability of the subsidiary and thereby Cognis.

Raw Materials¹⁷⁾

Cognis is exposed to commodity price risks relating to raw materials, which comprise the majority of our cost of sales. We purchase raw materials from a variety of sources and, in certain cases, enter into long-term purchase contracts. Our target is to immediately pass through increases in levels of raw material prices. Nevertheless, in some cases our selling prices and our margins can suffer from volatility and temporary strength in raw materials.

Natural oils and fats represent a substantial portion of our total raw material purchases of about 30% in 2008 (2007: 29%). The single most significant raw material we use is natural lauric oils, particularly palm kernel and coconut oil, which represented about 27% (2007: 26%) of our raw material purchases in 2008. We also use a broad range of petrochemical derivatives of about 40% (2007: 42%), most significantly ethylene oxide of about 12% (2007: 12%). Other Raw Materials (inorganics and other natural based raw materials) represented about 30% (2007: 29%) of total raw material purchases in 2008.

The availability and price of these raw materials may be affected by increased market demand, new regulations, production capacity in the market, interruptions in supply, and other market conditions. Our exposure to raw materials and other input prices is partially mitigated by our high degree of vertical integration into specialty products. The benefits of this integration include the ability to spread margin fluctuations over various production stages, high plant utilization rates, the efficient use of by-products, shared infrastructure and transportation costs as well as shared customer services.

Natural renewable oils and fats

Cognis uses about half a million metric tons of natural vegetable oils globally. The most important component of our oils and fats requirement is lauric oils, namely palm kernel and coconut oil, which are near substitutes for each other. Unlike petrochemical raw materials, lauric oils are derived from renewable and biodegradable resources. We also use other vegetable oils to a lesser extent.

Prices of lauric oils have been particularly volatile and unpredictable in the past, due to adverse climatic conditions, natural disasters, regional political events, strong growth in Asia and other factors. Lauric oils accounted for about 27% of our total raw material purchases in 2008 (2007: 26%).

The market price of lauric oils is denominated in US dollars. Market prices of these oils have increased strongly in 2008. In US dollars, lauric oils increased on average about 30% in 2008 versus 2007, and in euros the increase was about 20%. The first half of 2008 was dominated by an exceptional global price increase for all commodities which came to a sudden stop in July. Prices reversed and collapsed in the second half of 2008 as a result of the global financial situation and the macro economic uncertainties.

In 2008, we purchased €393 million (2007: €327 million) of lauric oils. This increase from 2007 to 2008 is mainly a result of higher lauric oil prices in 2008. Lauric oils are only available through over-the-counter (OTC) and cash market contracts, whereas only palm and soy bean oil are traded on futures exchanges. We also purchased €42 million of non-lauric vegetable oils in 2008 (2007: €39 million).

Petrochemical derivatives and Other Raw Materials

We purchased €574 million (2007: €534 million) of a wide variety of petrochemical raw materials in 2008, the most significant being €173 million (2007: €152 million) of ethylene oxide and €30 million (2007: €31 million) of acrylates. Additionally, we purchased alkyl-benzenes, propylene oxide, ethanol amines and ethylene amines.

In 2008, we also purchased €439 million (2007: €372 million) of Other Raw Materials, thereof €152 million (2007: €146 million) of inorganic raw materials like sodium carbonate or sodium hydroxide as well as €287 million (2007: €226 million) of other natural based raw materials like tall oil fatty acids and dextrose.

Overall, prices of our petrochemical derivatives and Other Raw Materials increased by about 17% in 2008 compared to 2007 due to a strong increase of crude oil and natural gas prices as well as a globally strong economy in the first half of 2008.

Energy

In 2008, we purchased about €109 million (2007: €97 million) of energy, primarily in the form of electricity, steam and natural gas. The increase from 2007 to 2008 is caused by greatly increased energy prices partly compensated by decreased consumption due to optimization initiatives and lower production volumes.

¹⁷⁾ The prior-year figures have been amended to reflect the continuing operations only.

Risk Management

In a changing market environment, Cognis continuously adapts processes and organization to ensure business success.

Management System

Cognis regularly undertakes risk management procedures with the aim of identifying and quantifying risk exposure. We constantly review the level of entrepreneurial risk tolerated so that our risk management systems are able to respond effectively.

Our main business processes "Management", "Market Management", "Innovation", "Supply Chain Management" and "Supporting Processes" are described in our global "Corporate Integrated Manual", and in additional guidelines and procedures, providing a comprehensive overview of Cognis' process landscape and strategies.

Efficient corporate management mainly hinges on transparent site management systems and internal/external auditing. Our worldwide management system is mainly based on the quality and environmental standards ISO 9001 and ISO 14001.

There are additionally certifications at defined sites based on customer or legal requirements such as ISO TS 16949 (automotive standard) in the USA, GMP Pharma IPEC Compliance in Düsseldorf, Spain, Australia, Thailand and the USA, Responsible Care in Germany and Brazil, OHSAS 18001 (work safety) in Spain, Italy, Australia, Thailand, Brazil and Indonesia, ISO 22000 (food standard) in Germany, Certified Kosher Production in Germany, the USA, and France, and SA 8000 (social accountability) in Brazil, Mexico and China.

Entrepreneurial Risks

Cognis operates in competitive markets. If we do not continue to maintain our leading market positions by constantly developing innovative products and responding effectively to the demand of consumers and customers, we may lose focus and this could adversely affect our net assets, financial position and results of operations. Further, markets can change, for example as a result of the financial crisis, and may have a negative effect on our business.

Our business units compete across global markets, and are constantly strengthening their focus on the wellness and sustainability trends. Our business may be adversely affected if we do not:

- continue to develop highly innovative products that satisfy customer needs and preferences
- continue to develop new technology or enhance existing technology that helps product development or provides cost or other advantages over our competitors
- continue to attract and retain skilled employees who are vital to achieving these objectives

Because we are subject to price competition, we must also continue to satisfy these objectives while maintaining a competitive cost base.

We conduct customer surveys on a regular basis to meet customer expectations, improve complaint management and to enhance supply quality. We also conduct supplier audits and assessments on a regular basis to improve supplier qualifications, for example through a better understanding about what kind of quality, safety and environment requirements have to be met to satisfy our customers.

In 2008, we received many important awards from customers as well as from local authorities. Examples include: Pemenang Safety Award for Cognis Indonesia; Cognis USA was honored for safety activities by the Ohio Chemistry Technology Council and the Mauldin Plant in USA was recognized for Safety Compliance and Cognis Düsseldorf (our biggest site worldwide) received an internal 'Zero Accident' award for one year without accidents.

The price volatility of certain raw materials Cognis uses could adversely affect our net assets, financial position and results of operations.

Cognis is exposed to commodity price risks relating to raw materials which account for the largest portion of our cost of sales. We purchase natural oils and fats, petrochemicals and other raw materials from a variety of sources and in certain cases enter into long-term purchase contracts. Our raw materials inventory is managed based on expectations of price and availability. The availability and price of raw materials may be affected by increased market demand, new regulations, production capacity in the markets, interruptions in production by suppliers, price speculations of market participants and other market conditions.

Cognis' diverse portfolio of value-added products provides some ability to pass on higher input prices to our customers, depending on market conditions. There may be times when we are not able to recover increases in the cost of raw materials for some products due to weakness in demand for such products or the actions of our competitors. This could adversely affect our net assets, financial position and results of operations.

Operational Risks

The occurrence of significant operational problems could have an adverse effect on Cognis' net assets, financial position and results of operations.

Our revenues are dependent on the continued operation of various manufacturing facilities. Operational risks include among others: failure to comply with relevant regulations and standards and to maintain necessary permits and approvals; raw material supply disruptions; labor force shortages or work stoppages; any disruption caused by third parties.

While we maintain insurance at levels that we regard as economically appropriate, some operational risks could result in losses and liabilities stemming from limited insurance coverage, or in uninsured losses or liabilities. The occurrence of major operational problems resulting from the above or other events may have an adverse effect on the net assets, financial position and results of operations of a particular manufacturing facility, or concerning certain of these risks, the net assets, financial position and results of operations.

Violations of environmental, health and safety and other laws, regulations and standards could limit our operations, expose us to liability, increase our costs and have an adverse effect on our net assets, financial position and results of operations.

As a major employer, chemicals producer and provider of substances used internally and externally by consumers, Cognis' key operational risks are in the areas of occupational safety, employment standards, production safety, environmental protection and product safety. Along with ensuring compliance with numerous national and international regulations and standards, we maintain strict safety, health, environmental protection and quality control programs to monitor and control these operational risks. These programs are designed and monitored by our Corporate Operations teams in accordance with our corporate standards.

In 2007, the EU enacted a legislative framework known as REACH (Registration, Evaluation & Authorization of Chemicals) requiring companies to register any substance equal to or exceeding one metric ton per year that they import or produce. Therefore, chemical companies such as Cognis are required to comply with REACH requirements in their capacity both as a manufacturer and as a downstream user of substances.

As many of our manufacturing facilities have a long operating history, sometimes predating Cognis' ownership, we may be liable for legacy contamination of soil and groundwater, irrespective of causation, negligence or knowledge. Our policy on safety, health and environmental standards and procedures, as well as

our central oversight seek, at minimum, to mitigate risk and ensure compliance with the laws and regulations in the jurisdictions in which we operate.

We have established provisions related to future environmental, health and safety liabilities where these are not covered by contractual indemnities from third parties, where expenditure is probable and where the cost can be estimated within a reasonable range of outcomes. However, such liabilities are essentially difficult to predict and to quantify. Existing provisions could therefore be insufficient to cover these liabilities, and costs incurred in meeting such obligations could have an adverse effect on our net assets, financial position and results of operations.

The well-being of our employees, and occupational, plant and environmental safety are given permanently high priority at Cognis. Measures implemented resulted not only in the absence of fatal incidents but also in a very low incidence rate¹⁸⁾ of 0.5 in 2008 (2007: 0.5). We are, however, aware that there is a constant need for communication, training and accident analysis to improve the safety process, and particularly to keep the incidence rate as low as possible—even and especially at those sites with records of more than three years without any accidents causing lost time.

Loss of a considerable number of key employees could adversely affect Cognis' net assets, financial position and results of operations.

We rely on important employees such as senior business managers and technical experts whose knowledge is critical to our success. Although we have procedures in place to identify and retain key employees, events beyond our control may lead to loss of such personnel. Where this happens, there are processes designed to enable the transfer of knowledge from such key employees. However, failure to transfer such knowledge prior to the loss of important employees and an inability to replace such key employees on time could have an adverse effect on our net assets, financial position and results of operations.

Financial and Other Risks

Cognis' key financial risks derive from exposure to changes in foreign exchange rates and interest rates, and the risk of insufficient liquidity (cash resources).

Changes in foreign exchange rates can affect Cognis. We are exposed to transaction currency effects. On the one hand, we buy a significant portion of our raw materials in Germany and other regions in US dollars while having sales in euro or other non-US dollar currencies. On the other hand, we generate a portion of our sales in US dollars or other non-euro currencies while having a part

¹⁸⁾ The incidence rate relates to a method of computing accident experience, established under the Occupational Safety and Health Act (OSHA), whereby the number of incidents causing days away from work, death, restricted work activity, and work-related illness is calculated. The total of lost time incidents per 200,000 worked hours equals the incidence rate.

of our production and cost base in Germany and other euro region countries. Cognis controls this risk by hedging the forthcoming years' expected foreign currency exposures using derivative financial instruments such as forward contracts and options.

Second, we have major operations in non-euro jurisdictions, most significantly in the USA, Latin America and Asia. The financial positions and results of these operations are translated into euros using prevailing exchange rates. As such, the financial positions and results of these foreign operations—as expressed in euros—are affected by changes in exchange rates. This “translation risk” is controlled by the currency composition of our financial debt, so that foreign currency earnings and cash flows service debt denominated in the same foreign currencies. While this means of controlling translation risk protects our ability to service our debts and the relationship between earnings and cash flows to indebtedness, it does not reduce the impact of changes in foreign exchange rates on operational earnings figures (such as EBITDA and EBIT) or on operating cash flows as expressed in euros. We monitor the currency composition of operating earnings, operating cash flows and indebtedness on an ongoing basis, and can synthetically adjust the currency composition of our debts using derivative financial instruments, particularly cross-currency swaps.

Third, if the US dollar remains weak for a considerable time in future, barriers to entry may weaken and cheaper imports may be facilitated in businesses where this was previously not possible due to prohibitive transportation costs.

Concerning interest rate risk, we are exposed to changes in interest rates because €1,641 million of Cognis' debts¹⁹⁾ bears interest at variable exchange rates (Euribor in the case of euro-denominated debt, US-Libor in the case of US dollar-denominated debt). Increases in these interest rates result in increased interest expense and increased interest payments (while decreases in interest rates result in the opposite). We control these interest rate risks through the use of derivative financial instruments, specifically interest rate swaps and options. The application of these instruments economically converts interest on hedged portions of variable-interest debt from floating interest to fixed interest or interest variable only within a defined range. As of December 31, 2008, about 76% of our variable-interest debt was hedged in this way.

Credit risk is the risk of loss arising from a customer's or counterparty's inability to meet its obligations. Given our business structure, we are primarily exposed to credit risk with respect to our trade and other receivables.

Our client base is broad and well diversified, with customers in various consumer and industrial product end markets. Many of our

customers are perceived to be leading companies in their respective market segments.

We use a combination of external and internal ratings as a means of continuously monitoring our credit risk exposures. External rating analyses are carried out by reputable agencies, while our internal ratings are based on experiences gained with existing customers relating to their payment behavior and default rates, combined with a range of soft facts. We aggregate this information to measure and evaluate the credit risk within our portfolios. To the extent possible and where reasonable, we insure certain portions of accounts receivable against insolvency risk.

Significant cash outflows result from the funding of business operations including working capital such as trade receivables and inventories, from investments in production facilities, from servicing pensions and other post-employment benefit obligations and, especially, from making interest payments and principal repayments on our debts. In order to fund these cash outflows, we must either have sufficient liquid funds from operating activities or available lines of credit. The risk that we are unable to meet a payment obligation is mitigated by a significant undrawn and available debt facility, particularly a Revolving Credit Facility (availability of €250 million less €29 million utilized for ancillary facilities and letters of credit as of December 31, 2008). This source of funding, however, is subject to various conditions and restrictions such as a financial maintenance covenant and conditions and restrictions concerning the purpose for which the funds can be drawn. Consequently, this source of funding may not be available in full or immediately.

Cognis has certain legal commitments relating to pension funds and pension schemes. This could have an adverse effect on our net assets, financial position and results of operations.

Cognis provides retirement benefits in certain countries (mainly Germany and the USA) for our former and current employees through a variety of defined benefit and defined contribution schemes.

The following factors could all serve to increase or decrease the pension fund deficit:

- Future investment returns on plan assets that are below expectation
- Changes in actuarial assumptions including mortality of participating members
- Higher rates of inflation and/or falling bond return rates used to discount the defined benefit obligations

Increased future funding contributions (e.g. as a result of the current financial crisis) may have an adverse effect on Cognis' net assets, financial position and results of operations.

¹⁹⁾ Excluding bank overdrafts, local loans and finance lease obligations.

Outlook

We overcame the challenges we faced in 2008 by already having the right strategies in place which enabled us to respond immediately with appropriate measures. A modest sales growth, a stable Adjusted EBITDA and a healthy cash flow rounded up 2008. By successfully divesting our discontinued operations, we reduced our exposure to the cyclical trends of these commodity businesses prior to an intensified weakening of the global economy. Furthermore, the cash proceeds of the divestment provide us with sufficient financial flexibility to continue developing our core businesses.

An economic environment which deteriorated rapidly in 2008 caused volumes to decrease in all our segments. However, we are strongly diversified in end markets and have high exposure to consumer markets such as the personal care, home care and nutrition markets. Therefore, the loss in volumes experienced especially at the end of 2008 could be partly considered as the outcome of destocking activities of our customers. Looking forward to 2009 and the first two months of the year, the economic environment remains depressed. We are still experiencing and forecast for the rest of 2009, a decrease in volumes in most of our business segments and especially in Europe.

In such an environment, we expect our sales for 2009 to decrease due to lower volumes. Our margins and our earnings are expected to be influenced not only by the development of the global economic environment but also the following opportunities and risks:

- We expect the trend towards “green” solutions in the personal care, home care and industrial as well as institutional segments to continue offering us opportunities for growth
- The prices of both natural raw materials especially vegetable oils and lauric oils as well as petrochemical raw materials, could continue to remain highly volatile. Accordingly, impacts on our earnings, both positive and negative, depend on when and how we are able to reflect raw material prices in our selling prices
- The volatility of the US Dollar against the Euro poses both a transaction and a translation risk as well as opportunities for our business

To counterbalance these uncertainties, we plan on extending our cost optimization programs. Programs in 2009 will continue to focus on streamlining both SG&A costs, and manufacturing processes globally. Our restructuring plans may include introducing short-time work in Germany. Although we will take every measure necessary to continue enhancing our business and maintain our profitability, globally deteriorating economic conditions prevent us from providing a robust forecast of our sales and earnings for 2009 and 2010.

In terms of cash generation, we expect to generate higher operating cash flows on the assumption that raw material prices will not increase sharply and therefore result in lower trade working capital, and hence a cash inflow in 2009. Financing cash flows are expected to be affected by higher contributions to pension plan assets. Altogether we expect our net cash flow in 2009 to be positive.

Due to the extent of the ongoing global economic uncertainty and volatility, forecasting 2009 and 2010 is extremely difficult. We will constantly monitor the global economic development to launch appropriate measures whenever necessary. We expect our healthy cash position of €226 million as at December 31, 2008 and further liquidity of €221 million available through our revolving credit facility to provide us enough financial flexibility to overcome our challenges and pursue strategies to maintain the profitability of our business.