

# Contents

Page

<b>31</b>	<b>Important Disclaimer</b>
31	Markets and Competitive Position
31	Forward-Looking Statements
<b>32</b>	<b>Management's Discussion and Analysis</b>
32	Financial Highlights and Operating Results
35	Strategic Business Units and Segment Results
40	Research & Development and Technical Service
42	Employees
42	Capital Expenditures
43	Financial Position, Liquidity and Capital Resources
51	Certain Factors Affecting our Business
53	Risk Management
57	Outlook

# 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: 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 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

## Financial Highlights and Operating Results

### Overview of 2007

We are pleased to report that 2007 was a good year for Cognis. Organic sales growth of the Group increased by 6.5% whereas Adjusted EBITDA rose by 4.4%. We achieved our strong results despite various exceptional challenges in 2007 such as record high raw material prices and a weak US dollar. Our strategic focus on the Wellness, Sustainability and Green trends remains strong and continues to add value to our business, as demonstrated by the strong results of our core SBUs such as Care Chemicals and Functional Products.

The main highlights of our cash flows in 2007 include an exceptional investment in working capital due to steep raw material prices which reduced our operating cash flow by €59 million. On the other hand, we also implemented a successful refinancing that has effectively eliminated capital repayments.

### Results and Cash Generation from Operations

€ millions	2007	2006
Sales	3,518	3,372
Operating profit (EBIT)	185	206
EBITDA	360	365
Adjusted EBITDA	410	394
Adjusted EBITDA margin	11.7%	11.7%
Net profit before special items	30	2
Net profit/(loss)	(120)	2
Operating cash flow	245	304

### Organic sales growth of 6.5% in 2007

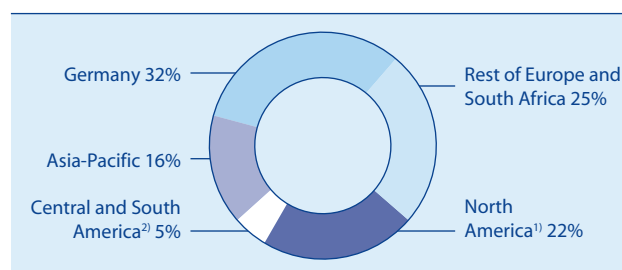
Cognis' 2007 sales of €3,518 million were €146 million or 4.3% higher than in 2006. On an organic basis, i.e. excluding foreign currency effects and the effects of acquisitions and divestments, sales growth amounted to €220 million or 6.5%. All core SBUs contributed to the organic sales growth. Oleochemicals also reported an increase whereas Pulcra Chemicals recorded a decrease in sales:

- Care Chemicals increased sales by 7.9%, reflecting growth of both its Care Performance Ingredients business and its Care Surfactants segment

- Nutrition & Health reported sales growth of 3.9%, mainly driven by our business segments of Food Ingredients, Pharma & Health and Omega-3
- Functional Products' sales increased by 8.1%. All segments profited from volume increases mainly due to strong worldwide demand in the agricultural and synthetic lubricants segments
- Pulcra Chemicals reported decreased sales of -2.5%. Pulcra Chemicals successfully continued its previous growth strategy in both the Textile Technology and Leather Technology segments in China. However, due to adverse market conditions in both industries, lower volumes were sold in all other regions
- Oleochemicals reported an increase in sales of 11.0%, mainly reflecting higher sales performance of the Fatty Acids/ Glycerin business. Plastics Technology and the Azelaic Acids and Pelargonic Acids businesses also contributed to sales growth in 2007

### Sales by company jurisdiction

€ millions	2007	2006
Germany	1,126	1,034
Rest of Europe and South Africa	890	899
North America <sup>1)</sup>	766	798
Central and South America <sup>2)</sup>	189	163
Asia-Pacific	547	478
<b>Total</b>	<b>3,518</b>	<b>3,372</b>



<sup>1)</sup> North America including Mexico and excluding Colombia.

<sup>2)</sup> Central and South America excluding Mexico and including Colombia.

On a regional<sup>1)</sup> basis, we achieved solid sales growth of +14.6% in Asia-Pacific<sup>2)</sup>, +16.1% in Central and South America<sup>3)</sup> and strong growth of +8.9% in Germany. The Rest of Europe<sup>4)</sup> reported slightly lower sales with –1.1%. The decrease of –4.0% in North America<sup>5)</sup> was mostly the result of currency translation issues arising from the weak US dollar.

#### Adjusted EBITDA increased by 4.4% on an organic basis compared to 2006

Cognis reported an Adjusted EBITDA of €410 million in 2007, €16 million or 4.0% higher than in 2006. On an organic basis, Adjusted EBITDA grew by €17 million or 4.4%. This rise reflects our strategic focus on Wellness and Sustainability which is linked to growing demand for “green” chemical solutions. Further, successful cost management and the balancing of historically high raw material prices in our selling prices both contributed to the higher Adjusted EBITDA performance.

#### Net loss reflects special items

Net profit of +€2 million in 2006 decreased by –€122 million to a net loss of –€120 million in 2007. This was primarily due to a higher net financial result (–€55 million), higher income taxes (–€46 million) and a lower EBIT<sup>6)</sup> (–€21 million).

The net financial result mainly includes –€57 million financing fees related to the Senior Facilities and Second Lien Obligations that were written off as these financing arrangements were terminated and replaced by new facilities (for details on the new facilities see section “Financial position, Liquidity and Capital Resources—Net Debt”). Also included in net financial result is a net interest expense of –€173 million, partially offset by income from interest derivatives of €10 million. Foreign exchange gains were €6 million net of the effects of foreign currency derivatives.

Income taxes include €53 million deferred tax expenses mainly incurred when deferred tax assets were revalued following the corporate tax reform in Germany. A further €6 million in taxes relates to current tax expenses arising from a higher taxable income.

The reduction in EBIT of –€21 million was mainly the result of higher restructuring charges and fair value adjustments. Restructuring charges and fair value adjustments amounting to €40 million were due to measures aimed at improving efficiency, reducing operating costs and enhancing our business structure following the carve-out of Pulcra Chemicals and Oleochemicals.

#### Net profit before special items

Net profit adjusted by special items of €150 million amounts to €30 million. The special items relate to:

- €57 million financing fees written off related to the previous financing arrangements that were terminated and replaced by new facilities of the May 2007 Refinancing Transaction
- €53 million deferred tax expenses resulting from the revaluation of deferred tax assets following the corporate tax reform in Germany
- Restructuring charges and fair value adjustments amounting to €40 million following the carve-out of Pulcra Chemicals and Oleochemicals

#### Carve-out of Process Chemicals to create Pulcra Chemicals in July 2007

Effective July 1, 2007, we carved out our Process Chemicals SBU. This now trades within the Cognis Group under the new name of Pulcra Chemicals. For more details concerning this carve-out, please refer to “Strategic Business Units and Segment Results—Pulcra Chemicals”.

#### 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.

We derive EBIT and EBITDA from net profit/(loss) as follows:

€ millions	2007	2006
<b>Net profit/(loss)</b>	<b>(120)</b>	<b>2</b>
Income taxes	86	40
Net financial result	219	164
<b>Operating profit (EBIT)</b>	<b>185</b>	<b>206</b>
Amortization and depreciation	175	159
<b>EBITDA</b>	<b>360</b>	<b>365</b>

<sup>1)</sup> 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.

<sup>2)</sup> Comprises Asia and Australia but excludes Turkey.

<sup>3)</sup> Comprises Central America and South America, including Colombia but excluding Mexico.

<sup>4)</sup> Comprises Europe, including Turkey and South Africa.

<sup>5)</sup> Comprises USA, Canada and Mexico but excludes Colombia.

<sup>6)</sup> “EBIT” refers to net profit excluding financial result, taxes on income and minority interests.

In 2007, income taxes of €86 million included –€53 million in deferred tax expenses mainly incurred when deferred tax assets were revalued under the corporate tax reform in Germany. A further €6 million taxes relate to current tax expenses arising from a higher taxable income.

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.

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

€ millions	2007	2006
<b>EBITDA</b>	<b>360</b>	<b>365</b>
<b>Restructuring charges<sup>1)</sup></b>	45	35
<b>Other exceptional items<sup>1)</sup></b>		
Separation costs	1	3
Release of pension provisions	–	(16)
Sundry exceptional items	4	7
Total other exceptional items	5	(6)
<b>Adjusted EBITDA</b>	<b>410</b>	<b>394</b>

<sup>1)</sup> Excluding depreciation and amortization.

Restructuring charges excluding depreciation and amortization of €45 million in 2007 (2006: €35 million) essentially relate to severance pay, early retirement schemes, pre-retirement part-time employment programs and other process and cost optimization programs. In 2007, other process and cost optimization programs included Global IT Optimization, and expenses incurred in separating Process Chemicals into a stand-alone unit. In 2006, restructuring charges also included our efficiency program in the USA, and expenses related to the Oleochemicals carve-out.

Other exceptional items comprise other income, expenses, gains and losses which in our judgement, do not reflect normal business operations and include separation costs, release of pension provisions, and sundry exceptional items:

- Separation costs comprise the costs of establishing our own stand-alone organization, particularly IT systems, subsequent to the separation from our former owner Henkel. The separation projects have reached the end of their life-cycles. However, a few remaining IT systems are still linked to Henkel. The costs in 2007 relate to the separation of some of these remaining systems
- Release of pension provisions included in 2006 relates to a one-time past service gain recognized in Q2/2006 due to changes made to the German pension scheme. The changes involve measures taken to counter factors that are expected to increase the future cost of financing pension obligations. Also included in 2006 and recognized in Q4/2006 is a one-time gain resulting from the curtailment of certain future retirement benefits in the USA
- Sundry exceptional items mainly relate to costs resulting from certain corporate consultancy fees and expenses. Also included in 2007 are one-time expenses related to environmental and legal provisions as well as exceptional advisory costs. Exceptional items also include a gain recognized on the disposal of the G-Cure® business which roughly offset certain fair value adjustments related to Pulcra Chemicals. 2006 includes a non-recurring gain from disposal of land in the USA recognized in Q4/2006

## Strategic Business Units and Segment Results

We manage our business through core SBUs (Strategic Business Units) of Care Chemicals, Nutrition & Health and Functional Products which are aligned to our strategic focus on the Wellness and Sustainability trends. The former Strategic Business Units Oleochemicals and Process Chemicals (now renamed Pulcra Chemicals) are pursuing their own strategies as independent entities. Having adopted appropriately revised business models, they are better positioned to succeed in their markets. Certain intra-Group (and hence inter-SBU) transfers, as well as contract manufacturing and other secondary activities, are included in "Other Activities".

### Changes in structure

Effective January 1, 2006, we changed the composition of our SBUs to reflect the transfer, in February 2006, of the Oleochemicals and Plastics Technology businesses to Cognis Oleochemicals (Malaysia) Sdn. Bhd. (COM), our existing 50:50 Malaysian joint venture with Golden Hope Plantations Berhad, Malaysia (Golden Hope).

The 2006 figures have been changed to reflect the amended transfer pricing agreements between intercompany affiliates in place from January 1, 2007. The impact of this restatement on the SBU results is in general not material.

The sales revenue of our businesses for 2007, and for the comparative prior period were as follows:

€ millions	2007	% of total	2006	% of total
<b>Sales Revenue</b>				
Care Chemicals	1,447	41.1%	1,356	40.2%
Nutrition & Health	331	9.4%	316	9.4%
Functional Products	874	24.9%	841	25.0%
Pulcra Chemicals	246	7.0%	258	7.6%
Oleochemicals	599	17.0%	553	16.4%
Other Activities	21	0.6%	48	1.4%
<b>Total net external sales</b>	<b>3,518</b>	<b>100.0%</b>	<b>3,372</b>	<b>100.0%</b>

### Care Chemicals

Care Chemicals is a leading international supplier of products and formulations in the home care and personal 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, our Care Chemicals unit delivers 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 competences, namely formulation technology and performance expertise, the use of raw natural materials and active ingredients, and our comprehensive understanding of marketing techniques and consumer preferences across all our markets.

In 2007, Care Chemicals generated sales of €1,447 million, representing 41.1% of our Group sales.

### Acquisitions, divestments and changes in structure

In March 2006, Care Chemicals broadened its product portfolio in the rapidly growing specialty polymers sector through the Group's acquisition of CRL (Cosmetic Rheologies Ltd., UK). CRL's business promises an innovative pipeline of products, and strong synergies with Care Chemicals' key accounts.

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

### Business development in 2007

2007 net external sales of our Care Chemicals SBU increased by €91 million or 6.7% to €1,447 million, compared to €1,356 million in 2006. Organic sales growth amounted to €107 million or +7.9%. Asia-Pacific posted the strongest growth with a substantial double-digit increase in sales. Care Chemicals in Europe achieved significant growth rates above GDP, contributing considerably to our success in 2007. North America generated sales growth in line with GDP, while South America's sales growth was substantially ahead of GDP.

Care Chemicals experienced significant sales and margin growth driven by marketing activities focused on specific fields such as the rapidly growing "Green Chemistry" market where Care Chemicals offers Green Chemical Solutions™ adapted to customer needs. Further, Care Chemicals gained market share within the fast growing Asian region supported by excellent business expertise. However, along with our competitors we faced soaring cost increases for major raw materials.

Sales of the Care Performance Ingredients ("CPI") segment grew in line with the SBU's overall growth rate in Europe, whereas CPI recorded the strongest growth in the Asia-Pacific region. CPI's sales growth was mainly driven by volume increases in key emerging markets in China, Korea, Thailand and Argentina.

The business of Care Surfactants Alcohols ("CSA") including Primary Surfactants and Fatty Alcohols strongly underpinned its number one market position in this field. While all regions contributed to the growth achieved, a significant portion of the improvement occurred not only in fast-growing emerging markets such as Asia and Latin America, but also in the European market, which tends typically to exhibit only moderate growth.

## 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, 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 2007, Nutrition & Health generated sales of €331 million, representing 9.4% of our Group sales.

### Acquisitions, divestments and changes in structure

In June 2006, Cognis acquired the Norwegian producer of high-quality Omega-3 fish oils, Napro Pharma AS, which broadens the Nutrition & Health product portfolio for Dietary Supplements and Functional Food applications.

In 2007, Cognis acquired certain patents, know-how and equipment related to the production of natural beta-carotene in Australia. Besides the above, there were no acquisitions, divestments or changes in structure in 2007.

### Business development in 2007

2007 net external sales of our Nutrition & Health SBU increased by €15 million or 4.7% to €331 million, compared to €316 million in 2006. On an organic basis, net external sales grew by €13 million or 3.9%, driven mainly by our business segments Food Ingredients, Pharma & Health and Omega-3.

Pharma & Health and Omega-3 showed strong growth in 2007, particularly in Europe. The Pharma & Health business continues to benefit from the trend of complying with quality

standards and offers growth opportunities for pharma-grade specialties. Further, Nutrition & Health successfully integrated the 2006 Napro Pharma acquisition, supporting sales growth with Omega-3 products sold to the dietary market. Tonalin® CLA sales decreased slightly versus 2006 due to still pending regulatory approvals in Europe. Our Sterols business did not grow as in previous years due to lower demand in Europe. The positive development in North America in the pharma sector and higher sales in Australia were not enough to compensate the lower sales performance in Europe.

The Food Technology business experienced an increase in sales compared to 2006 as a result of strong market penetration in the baked goods and dessert segments. Sales of our natural-based Vitamin E business increased slightly compared to 2006.

On a regional perspective, we achieved moderate sales growth in Europe due primarily to increased sales of Omega-3 and Food Ingredients. Strong sales growth in North America was mainly due to higher sales of Sterols to the pharmaceutical market, Tonalin® CLA in the dietary market and increased sales in our Pharma business. In Asia-Pacific, we achieved significant double-digit growth compared to 2006, mainly due to increased sales of Sterols, beta-carotene and Tonalin® CLA.

## Functional Products

The Functional Products SBU provides chemical products and 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"), lubricants, agriculture and mining industries. The key expertise of Functional Products lies in its know-how in chemistry of surfaces combined with its tradition in and focus on developing ecologically sound solutions.

In 2007, Functional Products generated sales of €874 million, representing 24.9% of our Group sales.

### Acquisitions, divestments and changes in structure

In November 2007, the G-Cure® business<sup>7)</sup> was sold.

Besides the above, there were no acquisitions or other changes in structure in 2007.

### Business development in 2007

The 2007 net external sales of Functional Products increased by €33 million or 4.0% from €841 million in 2006 to €874 million. Organic sales growth amounted to €68 million or 8.1%. All business segments contributed to the sales growth, which was due particularly to strong worldwide demand in the agriculture business and for lubricant applications used in refrigeration compressors and for other industrial uses.

Sales of the PCI (Polymers, Coatings and Inks) business grew mainly in Asia and South America, while sales in North America were negatively impacted by the slowdown in the housing market there. Sales in Europe were slightly above the 2006 level.

The Synthetic Lubricants business expanded its sales in Europe and Asia. Sales of compounded lubricants in the USA remained stable versus 2006, indicating a performance level better than the overall market considering that truck build numbers fell below 2006. In North America, Europe and Central and South America, Functional Products further strengthened ties to major international key accounts and continued to grow with existing as well as with new products.

In the AgroSolutions business, Functional Products experienced significantly higher sales compared to 2006. This was mainly due to strong worldwide demand from key accounts. Weather conditions and increased demand for agricultural produce were supportive to demand. In Europe, Functional

Products achieved higher sales of green solvents and surfactants. In Brazil, sales for additives more than doubled and in the North America region, Functional Products benefited mainly from growth with surfactants.

Helped by continuing high demand for base metals, sales of our Mining Technology business continued to grow. This was despite the fact that in 2007 a lower number of new copper-producing installations went on stream requiring initial fills of solvent extraction chemicals. The Mining Technology business has successfully maintained its position as a global leader in this area.

### Pulcra Chemicals

Pulcra Chemicals manufactures a wide range of chemicals for the fiber, textile and leather industries. The business offers high-performance process auxiliaries and system solutions for spinners, weavers and leather goods manufacturers, by focusing on production and processing techniques that improve efficiency and reduce costs for the customer. Pulcra Chemicals supplies textile auxiliaries through its Textile Technology segment and specialty chemicals for the leather industry through its Leather Technology segment. Both segments are expected to benefit from increased demand for natural-based and environmentally friendly products.

In 2007, Pulcra Chemicals generated sales of €246 million, representing 7.0% of our Group sales.

### Acquisitions, divestments and changes in structure

Effective July 1, 2007, our Process Chemicals SBU trades within the Cognis Group under the new name of Pulcra Chemicals. To form Pulcra Chemicals, the Process Chemicals SBU was carved out into ten separate legal entities. This carve-out represents a decisive step toward ensuring long-term competitiveness and further enhancing product and service quality.

Besides this, there were no other acquisitions, divestments or other changes in structure in 2007.

<sup>7)</sup> 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. G-Cure® products are sold primarily to the heavy- and light-duty industrial maintenance and automotive refinishing markets.

### **Business development in 2007**

Pulcra Chemicals' 2007 net external sales of €246 million decreased by –€12 million or –4.7% compared to 2006 and by –€6 million or –2.5% on an organic basis. Pulcra Chemicals successfully continued its previous growth strategy in both segments within China. However, due to adverse market conditions in both the textiles and leather industries elsewhere, lower volumes were sold in all other regions.

### **Oleochemicals**

Oleochemicals consists of Fatty Acids, Glycerin, Oilfield Chemicals, Plastics Technology, Azelaic Acid and Pelargonic Acid products, and also Fatty Alcohols within Malaysia. The new structure was put in place on January 1, 2006, following formation of the global joint venture in Malaysia, Cognis Oleochemicals (Malaysia) Sdn. Bhd. (COM).

In 2007, Oleochemicals generated sales of €599 million, representing 17.0% of our Group sales.

### **Acquisitions, divestments and changes in structure**

Oleochemicals headquartered in Malaysia is operated as a 50:50 global joint venture that became effective with the transfer of the global Oleochemicals and Plastics Technology businesses to our Malaysian joint venture in February 2006. The business structure changed effective January 1, 2006, as follows:

- Oleochemicals includes the Plastics Technology business (previously included in the Process Chemicals SBU), the Azelaic Acid and Pelargonic Acid business (previously part of Functional Products), the results of fatty alcohol production in Malaysia (previously part of Care Chemicals) and the results of trading Cognis products in Malaysia (previously included in the results of the originating SBUs)

- Oleochemicals excludes the Silicates business and the opportunistic trading of lauric oils, which is now included in Care Chemicals. Oleochemicals also sells other SBU products which are now reported under Oleochemicals

Following the carve-out of these businesses, new supply agreements govern the transfer of goods and services between the COM sub-group and other entities within the Cognis Group ("Cognis entities"), from which Pulcra Chemicals entities are excluded.

In February 2007, COM paid an additional purchase price of €8 million due to a settlement agreement and the achievement of certain targets as stipulated in the share purchase agreement.

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

### **Business development in 2007**

In 2007, net external sales of Oleochemicals increased by +€46 million or +8.3%, from €553 million in 2006 to €599 million, and on an organic basis by +€61 million or +11.0% mainly because of higher volumes sold in Asia-Pacific and Europe. This increase was combined with higher glycerin prices driven by strong demand and the unexpected delay in bio-diesel operations which resulted in supply shortfalls. Higher selling prices as a result of pass-through of raw material price increase likewise contributed to sales growth.

## Research & Development and Technical Service

### Research & Development and Technical Service Expenditure

€ millions	2007	2006
Research and development expense	91	94
Less: Amortization included in R&D expense	(35)	(36)
Add: Capitalization of development costs	8	6
<b>Total research &amp; development expenditure</b>	<b>64</b>	<b>64</b>
Add: Technical service costs	33	31
<b>Total</b>	<b>97</b>	<b>95</b>

### Care Chemicals

The demand for “green” solutions in the personal and home care as well as the industrial and institutional (“I&I”) segments is growing rapidly, as customers are increasingly concerned with the environmental and safety impact of the products they buy. They look for claims and labels containing words such as “green”, “organic”, “natural” or “ecological” and similar. Manufacturers intending to develop products in line with this global “Green Chemistry” trend can choose from a range of appropriate ingredients from Care Chemicals. We conduct extensive research on such ingredients which not only include plant-derived oils and fats but also plant proteins and carbohydrates. We expect this line of research to enable us to increase the proportion of natural raw materials in future products.

Our R&D processes are made even more efficient through alliances with external research institutions and start-up companies. For example, through such an alliance, we made significant progress in increasing our technical competence in the area of specialty polymers. Correspondingly, new R&D projects were launched in this field and form the basis of future polymer product launches. In another area, namely of Specialty Surfactants, we continued the successful development of tailor-made additives for automatic dishwashing detergents. One of these products, from the Dehypon® series, received the Cognis Innovation Award of 2007. We developed a new emollient in line with our “Feelosophy” concept that promises a unique feel with enhanced sensory perception in skin care

applications. As for active ingredients, we have successfully launched Dermican® onto the market. Dermican® is the first product from a series that contains specific claims related to anti-aging and results from research into various types of oligopeptides with a defined molecular structure. Our range of products was extended in July 2007, when we took over all activities related to the Skintex® business. Skintex® is based on micro-encapsulation technology as used in various products. We have focused our R&D activities on optimizing and scaling-up this technology in products such as Skintex® Supercool and Skintex® MR11, which has a mosquito repellent finish that is approved by the US Environmental Protection Agency (“US EPA”).

Our core competences include the close relationship with our customers and our excellent technical customer support. To ensure that high standards are maintained, we have enhanced our application technology network worldwide with clearly defined roles and responsibilities assigned to both our regional and our global activities. We are convinced that with such a set-up, customer needs will be addressed quickly and competently and that research and development will be effectively focused on the midterm market.

### Nutrition & Health

Nutrition & Health’s research and development activities concentrate strongly on customer-focused product development and technical services characterized by tailor-made formulations and close relationships with key accounts. Using this approach, we have developed solutions founded on scientific studies as well as human clinical studies for products such as Tonalin® conjugated linoleic acid (CLA) and Xangold® lutein esters.

In addition to outcomes recommended by these studies, some of our products also require regulatory clearance. In China, we were the first company to receive clearance for our Vegapure® sterol esters, which enables us to promote the properties of Vegapure® in our Chinese customers’ food products. Also, regulatory clearance for Tonalin® in Korea is paving the way for a wider distribution. We are aiming further for our Tonalin® range of products by extending an existing GRAS-approval [Generally Recognized As Safe (“GRAS”)] to an FDA-GRAS approval with the US Food and Drug Administration (US FDA). Applications are also pending in Australia and New Zealand as is Novel Food Certification in Europe.

We were very successful in enhancing and improving our Vegapure® product range. For our innovation, we received the prestigious Dan'Innov Innovation Award 2007 from Danone, underlining that Cognis is capable of supplying tailor-made and commercially successful applications of sterol esters.

Our portfolio also includes 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. New excipients for the PharmaLine® product range have likewise been developed for use in various pharmaceutical applications.

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

### **Functional Products**

"Where Ecology Meets Performance" serves to summarize the R&D focus of Functional Products. Product development not only aims at steady improvement of performance characteristics, but also requires alignment toward sustainable ecological benchmarks. The basis of these standards is the use of renewable raw materials and the environmental safety of products. By following this global trend, Functional Products creates an essential added value for its products and strengthens its market position.

A special highlight for 2007 was the winning by a team from Ireland and the USA of the Cognis Gold Award for Innovation. The team developed a new approach for copper recovery which reduces acid consumption and environmental risks.

In AgroSolutions, two special eco-friendly adjuvants of the Agnique® product group serve to enhance the performance of plant protection products. They are based on modified vegetable oils and exhibit a favorable toxicological and ecotoxicological profile. And a range of green solvents was also launched as environmentally benign substitutes for petrochemical substances.

A promising development in the Synthetic Lubricants segment is the development of the first CFC(chlorofluorocarbon)-free compressor lubricants both for refrigeration and air conditioning applications, which are in line with principles of environmental protection. The main advantage of the product series is the active contribution to ozone layer protection and lower energy consumption.

We continue to focus on the development of green additives and components for water-based paints and coatings, adding new innovations to the group of new product developments incorporating both enhanced performance and ecological benefits.

### **Pulcra Chemicals**

In line with its service-oriented business model, Pulcra Chemicals' development activities concentrate on product modifications and on the development of new products, driven by product cost optimization, meeting customer specific technical requirements and enhancing product performance.

Using this approach, a series of new products was introduced. In the Textile Technology business, such products include finishes for technical fibers, detergents, enzymes, stabilizers and sequestering agents for the pretreatment of textiles, as well as softeners based on amino-functional silicones, fluoropolymers and polyurethanes for the finishing of textiles. In the Leather Technology business, products developed include new fat liquoring agents and polyurethanes used in the finishing of leather.

### **Oleochemicals**

Oleochemicals focuses its activities mainly on meeting customer needs related to application technology and technical services.

Oleochemicals focuses its R&D activities on the revision and modification of existing products and the development of new products, as well as measures related to optimizing costs. For example, they have developed new applications related to agents used in the bio-plastic processing of plastic additives.

Activities related to the Oilfield Chemicals business concentrated on improving customized solutions for environmentally friendly emulsifiers and drilling fluid systems.

### **Patents**

In 2007, Cognis filed about 100 new patent applications and was granted the same number of patents by the European, US and German patent offices.

## Employees

Between December 31, 2006 and December 31, 2007, Cognis' number of employees worldwide, excluding trainees, apprentices and interns decreased by –134 employees from 7,719 to 7,585. This was mainly the result of restructuring programs and, to a lesser extent, a more restrictive and controlled hiring process.

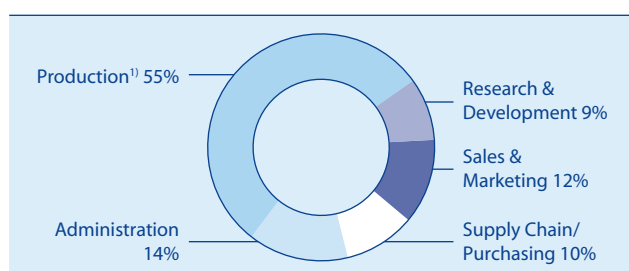
In the functional breakdown, the number of employees in Production decreased by –73, in Sales & Marketing by –38 and in Research & Development by –34.

From a regional perspective, headcount in Germany decreased by –8 and in the rest of Europe including South Africa by –57. In NAFTA, the number of employees fell by –48. There was an increase of 1 in Mercosur and a reduction of –22 in Asia-Pacific.

In 2007, the number of trainees, apprentices and interns was 188, representing a decrease of –10 from 198 in 2006. Including trainees, apprentices and interns, the total number of employees in 2007 was 7,773 compared to 7,917 in 2006.

### Workforce by function at balance sheet date

Number	2007	2006
Production <sup>1)</sup>	4,145	4,218
Research & Development	705	739
Sales & Marketing	879	917
Supply Chain/Purchasing	768	766
Administration	1,088	1,079
<b>Total</b>	<b>7,585</b>	<b>7,719</b>



<sup>1)</sup> Reporting of Cognis' headcount is affected by the strike in the US in 2005. In 2006, we excluded 123 strikers and included 229 additional workers. In 2007, we excluded 52 strikers and included 229 additional workers.

## Capital Expenditures

Our capital expenditures in 2007 amounted to €132 million, an increase of €32 million compared to 2006. The following two factors contributed primarily to this increase:

- Higher investments in growth projects, mainly in Germany, the USA and Asia, to provide additional capacities
- As expected delays in 2006 causing a spill-over effect in 2007

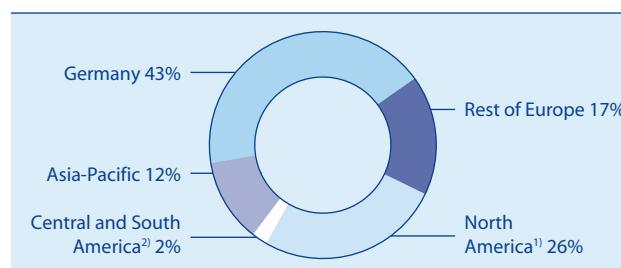
We invested a significant amount in growth projects at Care Chemicals, Nutrition & Health and Functional Products. In addition, we invested in the Oleochemicals business. Our investments were focused not only on growth projects but also on cost improvement and replacement activities in all businesses.

Significant capital expenditures in 2007:

- In our largest production site in Düsseldorf (Germany), we initiated growth projects and energy saving projects. Growth investments were made to support the core businesses of Care Chemicals and Functional Products
- We completed a project in our plant in Illertissen (Germany) for our Nutrition & Health SBU to support the strategic growth of our sterol esters business

### Capital expenditures by region

€ millions	2007	2006
Germany	57	33
Rest of Europe	23	17
North America <sup>1)</sup>	34	27
Central and South America <sup>2)</sup>	2	2
Asia-Pacific	16	21
<b>Total</b>	<b>132</b>	<b>100</b>



<sup>1)</sup> Including Mexico and excluding Colombia.

<sup>2)</sup> Excluding Mexico and including Colombia.

- We continued to debottleneck, modernize and improve the efficiency and yields of our production in the largest US site in Cincinnati and in Mauldin (USA) which we started in 2006 and successfully completed in 2007
- We started another investment in 2007 in our plant in Cincinnati to reduce VOC (Volatile Organic Compound) emissions
- Furthermore, we continued to improve the supply of steam in Cincinnati by replacing two worn-out 30-year-old coal-fired boilers with four new, modern units operating on the basis of multiple liquid and gaseous fuels including production residues and landfill gas
- We continued to invest in the construction of a new plant in our joint venture of Thai Fatty Alcohols together with our joint venture partner, Thai Olefins. The construction of the new plant producing refined fatty alcohols started in 2006. Start-up is scheduled for the second quarter of 2008
- Oleochemicals also started a project to increase methyl ester capacities in Malaysia. The aim is to add new higher-margin products to the Oleochemicals portfolio. This project is scheduled to continue into 2008

## Financial Position, Liquidity and Capital Resources

€ millions	As of December 31,	2007	2006
Total assets		2,505	2,640
Trade working capital <sup>1)</sup>		745	699
Equity		(610)	(120)
Pension provisions		435	444
Nominal net debt <sup>2)</sup>		1,979	1,530

<sup>1)</sup> Trade working capital consists of trade receivables and inventories, net of trade payables.

<sup>2)</sup> Excludes pension provisions, deferred financing fees and accrued interest.

### Total assets

The decrease in total assets by –€135 million, from €2,640 million at December 31, 2006, to €2,505 million at December 31, 2007, was mainly a result of the following:

- Negative foreign exchange effects: most significantly, the weakening of the US dollar relative to the euro to USD:EUR 1.4721 at December 31, 2007, from USD:EUR 1.3170 at December 31, 2006, decreased total assets by –€62 million; excluding this effect, total assets decreased by –€73 million
- Liquid funds decreased by –€101 million, as a result of lower cash generated from operations, mainly due to costs related to the Refinancing Transaction
- Trade working capital increased by +€46 million. Adjusted for foreign currency effects, trade working capital increased by +€67 million
- Capital expenditures of €132 million (2006: €100 million) on fixed assets were exceeded by the combination of net disposals of €6 million and amortization and depreciation of €175 million. Amortization and depreciation includes impairment charges of €23 million and amortization of €41 million of step-up<sup>8)</sup>

<sup>8)</sup> 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".

**Trade Working Capital**

€ millions	As of December 31,	2007	2006
Annual net external sales		3,518	3,372
Trade receivables		566	537
% Annualized sales		16.1%	15.9%
Inventories		526	495
% Annualized sales		15.0%	14.7%
Trade payables		(347)	(333)
% Annualized sales		-9.9%	-9.9%
<b>Trade working capital</b>		<b>745</b>	<b>699</b>
% Annualized sales		21.2%	20.7%

Our trade working capital increased by +€46 million, from €699 million at December 31, 2006 to €745 million at December 31, 2007.

Foreign currency effects, particularly from the weakening of the US dollar by around 12% against the euro, impacted the balance sheet values of trade working capital, causing a foreign exchange effect of +€21 million. Excluding foreign exchange influences, trade working capital increased by +€67 million between December 31, 2006 and December 31, 2007. This was mainly because of increased trade receivables, reflecting the higher sales performance and higher inventories arising from increased prices for raw materials, especially lauric oils. Trade payables increased slightly as more volumes were purchased, reflecting a higher level of business activity and higher petrochemical prices.

We purchase and hold inventory including lauric oils according to 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 stocks of lauric oils increased by +€8 million between December 31, 2006 and December 31, 2007, mainly due to higher prices.

From an absolute increase of +€46 million, excluding foreign exchange effects of +€21 million and increasing stocks of lauric oils of -€8 million, trade working capital increased by +€59 million.

**Equity**

Equity decreased to negative €610 million as of December 31, 2007 from negative €120 million as of December 31, 2006. This decrease of -€490 million is mainly due to a capital distribution made in May 2007 to our former immediate parent company, Cognis Holding GmbH, amounting to -€357 million. The capital distribution was applied by Cognis Holding GmbH to redeem a portion of its PIK Notes in May 2007. Equity was also reduced by a net loss for the period amounting to -€120 million, and net losses on cash flow hedges of -€7 million. The net loss of -€120 million includes the write-off of -€57 million in deferred financing fees relating to our former Senior Facilities and Second Lien Obligations in Q2/2007 as well as -€53 million in non-cash tax expenses arising from the revaluation of deferred tax assets and liabilities of our German subsidiaries in Q3/2007. Net loss also includes restructuring charges and fair value adjustments amounting to €40 million related to measures aimed at improving efficiency, reducing operating costs and enhancing our business structure following the carve-out of Pulcra Chemicals and Oleochemicals.

## Pensions

€ millions	2007	2006
<b>Provisions for pensions and similar obligations at January 1</b>	<b>444</b>	<b>464</b>
Current service cost	16	18
Operating actuarial losses	1	–
Pension costs	17	18
Other costs for obligations similar to pensions	(3)	(18)
<b>Total pension costs included in EBITDA</b>	<b>14</b>	<b>–</b>
Interest expense	40	41
Expected return on plan assets	(21)	(21)
Financial actuarial losses	4	8
<b>Net interest expense</b>	<b>23</b>	<b>28</b>
<b>Total cost of pensions and similar obligations</b>	<b>37</b>	<b>28</b>
Cash utilized <sup>1)</sup>	(40)	(41)
Other movements	1	2
Translation differences	(7)	(9)
<b>Provisions for pensions and similar obligations at December 31</b>	<b>435</b>	<b>444</b>

<sup>1)</sup> Cash utilized includes both cash payments to beneficiaries and contributions to plan assets.

We offer our employees various defined benefit retirement plans around the world. In 2007, we made cash payments related to pensions of €40 million (2006: €41 million) in both retirement benefits and contributions to plan assets. Our cash contribution to the US plan assets amounted to €8 million in 2007 (2006: €8 million).

Also, pension costs of €14 million (2006: nil) are included in EBITDA. In 2006, besides the €18 million current service

cost, pension costs also included a –€12 million one-time past-service gain resulting from changes made to German pension plans, a –€4 million one-time gain resulting from the curtailment of certain future retirement benefits in the USA, and other recurring past-service gains of –€2 million mainly in the USA.

€ millions	As of December 31,	2007	2006
Present value of unfunded defined benefit obligations		452	510
Present value of funded defined benefit obligations		299	326
Fair value of plan assets		(274)	(281)
		<b>477</b>	<b>555</b>
Unrecognized actuarial (losses)/gains		(55)	(128)
Unrecognized past service (costs)/gains		13	17
<b>Provisions for pensions and similar obligations</b>		<b>435</b>	<b>444</b>

%	2007	2006	2007	2006
	Germany		USA	
Discount rate	5.4	4.6	6.0	5.75
Future salary increase (in the USA, including benefits increase)	2.5	2.5	4.5	4.5
Future benefits increase	1.0–1.5	1.0–1.5	–	–
Medical cost trend	–	–	9.0	10.0
Expected return on plan assets	–	–	8.5	8.5
Actual return on plan assets	–	–	9.3	11.4

Pension provisions in 2007 decreased by –€9 million to €435 million, mainly due to foreign currency effects (–€7 million), cash paid to beneficiaries (–€27 million) and plan assets (–€13 million). These reducing effects

compensated for pension costs of (+€37 million) and other movements (+€1 million). There was no significant release of provisions included in pension costs in 2007.

## Net Debt

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,	2007	2006
Senior Facility Loans <sup>1)</sup>		–	898
Second Lien Loans <sup>1)</sup>		–	157
Second Lien Notes <sup>1)</sup>		–	235
Senior Notes <sup>1)</sup>		345	345
Senior Secured Floating Rate Notes <sup>1)</sup>		809	–
Senior Secured Floating Rate Loans <sup>1)</sup>		809	–
Finance lease obligations		30	33
Oleochemicals borrowings		69	69
Other bank debts		49	26
<b>Total debt</b>		<b>2,111</b>	<b>1,763</b>
Cash and cash equivalents		(132)	(233)
<b>Net debt of Cognis GmbH</b>		<b>1,979</b>	<b>1,530</b>
PIK Notes of Cognis Holding GmbH <sup>2)</sup>		–	663
PIK Loans of Cognis Holding GmbH <sup>2)</sup>		385	–
Cash and cash equivalents of Cognis Holding GmbH		(1)	(1)
<b>Net debt of Cognis Holding GmbH</b>		<b>384</b>	<b>662</b>
<b>Net debt of Cognis Holding GmbH Group</b>		<b>2,363</b>	<b>2,192</b>

<sup>1)</sup> Excludes deferred financing fees and accrued interest.

<sup>2)</sup> Excludes deferred financing fees and includes accrued interest.

The change in Cognis' financial structure from December 31, 2006, to December 31, 2007 reflects the Refinancing Transaction in May 2007 and materially comprises the transactions as described below:

### The Refinancing Transaction in May 2007

On May 16, 2007, Cognis GmbH issued €1,653 million of Floating Rate Senior Secured Notes and Loans due September 15, 2013 ("Senior Secured Debt"). The proceeds from the Senior Secured Debt were used to repay all amounts outstanding under our existing Senior Facilities Agreement (€887 million) and Second Lien Loans (€154 million), and to redeem all of our Second Lien Notes (€235 million).

The proceeds were also used to distribute €357 million to our former immediate parent company, Cognis Holding GmbH. Withholding tax of €32 million was due on this capital distribution and was paid by Cognis GmbH on behalf of Cognis Holding GmbH. The withholding taxes are expected to be refunded by the tax authorities in 2008, upon which Cognis Holding GmbH will repay Cognis GmbH in full.

Cognis Holding GmbH used the payment from Cognis GmbH to redeem €350 million (including accrued interest) of their outstanding Floating Rate Senior PIK (Payment-In-Kind) Notes due 2015 ("PIK Notes"). Related redemption fees amounting to €7 million were also paid from the proceeds.

In addition, Cognis GmbH entered into a new Revolving Credit Facility of up to €250 million.

The original indenture agreement of the 9.5% Senior Notes dated May 13, 2004 was amended by a supplemental indenture agreement dated May 1, 2007. Cognis GmbH solicited and received the required consent from related Note holders to execute the supplemental indenture agreement.

The new Senior Secured Debt bears interest on a quarterly basis, based on Euribor plus 2% for euro debt and US-Libor plus 2% for US dollar debt. Both Loans and Notes mature on September 15, 2013.

In connection with the Refinancing Transaction in May 2007, we incurred –€50 million fees and expenses. Settlements on interest derivatives related to the previous and new financing arrangements were minimal as we were generally able to use previous derivative arrangements to reflect the new refinancing structure.

In connection with the Refinancing Transaction, we implemented a corporate reorganization. Among other things, Cognis Deutschland GmbH & Co. KG ("Cognis KG") ceased to exist and its assets were collapsed into Cognis GmbH. In addition, Cognis Holding GmbH, the issuer of the PIK Notes, contributed all of its interest in Cognis GmbH to a newly created wholly owned subsidiary, Cognis Beteiligungs-GmbH. In turn, Cognis Beteiligungs-GmbH, our new immediate parent company, pledged all of the shares of Cognis GmbH to the holders of the new Senior Secured Debt and the Revolving Credit Facility as security.

#### Redemption of remaining PIK Notes of Cognis Holding GmbH in June 2007

On June 12, 2007 the remaining part of the PIK Notes amounting to about €348 million (including accrued interest) was fully replaced by a new €362 million PIK Loan due 2015. The new PIK Loan bears interest currently based on three months Euribor plus 7%.

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. As of December 31, 2007, the PIK Loan amounted to €385 million including capitalized interest of €13 million and accrued interest of €10 million.

Throughout 2007, 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	As of December 31,	2007	2006
<b>Net debt</b>		<b>1,979</b>	<b>1,530</b>
Accrued interest <sup>1)</sup>		10	12
Deferred financing fees		(54)	(71)
Cash and cash equivalents		132	233
<b>Borrowings</b>		<b>2,067</b>	<b>1,704</b>
Thereof current		73	129
Thereof non-current		1,994	1,575

<sup>1)</sup> On Senior Facilities Loans, Second Lien Notes and Loans, Senior Notes and Senior Secured Floating Rate Notes and Loans.

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.

#### Off-Balance-Sheet Arrangements

Guarantees and warranties issued were nil as of December 31, 2007 (2006: nil).

## Net Cash Flow

€ millions	2007	2006
Adjusted EBITDA	410	394
Cash restructuring expense <sup>1)</sup>	(37)	(36)
Other exceptional items <sup>2)</sup>	(5)	6
Change in trade working capital <sup>3), 4)</sup>	(65)	(19)
Change in other working capital <sup>4)</sup>	(21)	4
Income taxes paid	(31)	(42)
(Gains)/losses on disposal and other adjustments	(6)	(3)
<b>Cash flow from operating activities</b>	<b>245</b>	<b>304</b>
Capital expenditures	(132)	(100)
Other investing cash flows	11	(36)
<b>Cash flow from investing activities</b>	<b>(121)</b>	<b>(136)</b>
<b>Free Cash Flow</b>	<b>124</b>	<b>168</b>
Cash interest <sup>5)</sup>	(142)	(121)
Capital contributions <sup>5)</sup>	–	40
Capital repayments and distributions <sup>5)</sup>	(358)	(1)
Pension payments net of service cost <sup>5)</sup>	(26)	(41)
Derivatives, FX gains/(losses) and other <sup>5)</sup>	(95)	(24)
<b>Cash flow before debt borrowing/(repayment)</b>	<b>(497)</b>	<b>21</b>
Net debt borrowing/(repayment) <sup>5)</sup>	396	101
<b>Net cash flow</b>	<b>(101)</b>	<b>122</b>

<sup>1)</sup> Restructuring cash-out excluding restructuring capital expenditure.

<sup>2)</sup> Excluding depreciation and amortization.

<sup>3)</sup> Cash change in trade receivables, inventories and trade payables.

<sup>4)</sup> Excluding change in restructuring provisions.

<sup>5)</sup> Part of financing cash flows.

### Cash flows from operating activities

At €245 million, our cash flow from operating activities in 2007 was –€59 million lower than in 2006. This was a result of the following factors:

- Lower other exceptional items of –€11 million. In 2007, exceptional items included one-time expenses related to environmental and legal provisions as well as exceptional advisory costs. Exceptional items also include a gain recognized on the disposal of the G-Cure® business which roughly offset certain fair value adjustments related to Pulcra Chemicals. In 2006, exceptional items included a one-time non-cash pension gain
- An investment of trade working capital of –€65 million that was –€46 million higher than in 2006. This was primarily due to a steep increase in inventory values arising from sharp price increases for raw materials, increased receivables also reflecting those same price increases and growth of our business as well as a lower increase in trade payables
- Cash flows from other working capital decreased to an outflow of –€21 million from an inflow of €4 million, for three main reasons: first, higher payments for employee bonuses were made in 2007 compared to 2006; second, VAT receivables were higher in 2007; third, deferred payments were made in Q4/2007 related to the Napro Pharma acquisition in 2006
- Higher (gains)/losses on disposal and other adjustments of –€3 million, mainly due to the reversal of the exceptional gain on the disposal of the G-Cure® business

These cash outflows were somewhat mitigated by a higher Adjusted EBITDA of +€16 million in 2007 and lower income taxes paid of +€11 million due to tax refunds in 2007 and correspondingly lower advance tax payments. Income taxes paid in 2006 include a one-time tax payment related to prior years.

### Cash flows from investing activities

In 2007, total cash outflows from investing activities amounted to –€121 million, +€15 million less than in 2006. This was mainly the result of the following countervailing effects:

- Our capital expenditures of –€132 million increased by –€32 million due to higher investments in growth projects in Germany, the USA and Asia, and a delay in projects in 2006 causing a spill-over effect in 2007
- 2007 other investing cash flows include a cash inflow reflecting the disposal proceeds of our G-Cure® business and land sales in the USA. Also included in other investing cash flows are certain patents, know-how and equipment

related to the production of natural beta-carotene in Australia acquired by Cognis in 2007. In 2006, the acquisitions of Cosmetic Rheologies Ltd., UK and Napro Pharma AS mainly contributed to the cash outflow under other investing activities

### Cash flows from financing activities

Cash flows from financing activities in 2007 include items related to the Refinancing Transaction completed in May 2007. This Refinancing Transaction involved the drawing of the new Senior Secured Debt to repay all outstanding principal and interest payments due on our previous financing arrangements, and the partial redemption of the PIK Notes of Cognis Holding GmbH, formerly our immediate parent company.

- Cash interest of –€142 million in 2007 includes interest payments made/income received as follows:
  - Interest payments on our new financing arrangements amounted to –€32 million on Senior Secured Floating Rate Notes and –€33 million on Senior Secured Floating Rate Loans
  - Interest payments on our previous financing arrangements were –€12 million for the Second Lien Notes, –€7 million on Second Lien Loans and –€26 million on Senior Facility Loans
  - We paid –€33 million in interest on the Senior Notes and –€3 million on the Oleochemicals borrowings. We also retained +€4 million net of interest income in various affiliates

The increase in cash interest in 2007 was due to higher debt after the Refinancing Transaction in May 2007. However, interest payments were partially mitigated by lower interest margins of the new financing structure.

- Capital contributions in 2007 were €40 million lower compared to prior year as 2006 includes the cash capital contribution from Golden Hope of €40 million resulting from the Oleochemicals transaction in February 2006
- Capital repayments and distributions were –€358 million in 2007. This relates to a distribution to Cognis Holding GmbH for partial redemption of their PIK Notes of €350 million and the associated redemption fees of 2% or €7 million. In addition, we paid €1 million dividends to minority shareholders of our Oleochemicals Joint Venture in Malaysia

- Pension payments net of service cost of –€26 million in 2007 reflect normal cash payments of €27 million to beneficiaries and €13 million in contributions to plan assets. Net service costs amounted to €14 million. In 2006, this item also included the reversal of the non-cash pension gain described under operating cash flows
- Derivatives, FX gains/(losses) and other of –€95 million resulted as follows:
  - A loan of –€32 million was provided to Cognis Holding GmbH in connection with a withholding tax payment resulting from the capital distribution. Cognis Holding GmbH expects a refund of these taxes in 2008 and will then repay the loan
  - Payments of fees and expenses of –€50 million related to the Refinancing Transaction in May 2007
  - Settlement on interest derivatives of +€3 million which offset commitment fees of –€3 million on undrawn facilities
  - Foreign exchange losses net of currency derivatives of –€13 million
- Net debt borrowing/(repayment)<sup>9)</sup> of €396 million in 2007 resulted as follows:
  - The issuance and draw-down of Senior Secured Floating Rate Notes of +€826.4 million in May 2007 (€610 million and US\$293 million)
  - The issuance and draw-down of Senior Secured Floating Rate Loans of +€826.4 million in May 2007 (€610 million and US\$293 million)
  - The repayment of Senior Facility Loans of –€887 million, Second Lien Loans of –€154 million and Second Lien Notes of –€235 million in May 2007
  - The draw-down of other local borrowings of +€19 million in various affiliates

In 2006, the following transactions were recorded:

- Related to the previous financing arrangement, €100 million of Senior Loan Facility D was drawn, –€50 million of Senior Facility A was voluntarily repaid and –€20 million was a scheduled repayment
- Further included in net debt borrowing/(repayment) in 2006 is the €69 million debt drawn by COM

## 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 our depreciation and amortization expense, including minor impairment losses, in 2007 by €41 million (2006: €46 million).

### Exchange Rate Fluctuations

The translation effect<sup>10)</sup> on our Adjusted EBITDA resulting from the weakening of the US dollar and other non-euro currencies against the euro in 2007, as compared to 2006, was –€4 million and mostly influenced our Functional Products and Care Chemicals SBUs.

The transaction effect<sup>11)</sup> on our Adjusted EBITDA is not directly quantifiable.

### Acquisitions and Divestments

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.

<sup>9)</sup> Debt draw downs and repayments in foreign currencies are translated into euros at actual rates on the date of the transaction.

<sup>10)</sup> 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.

<sup>11)</sup> 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.

In 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.

In June 2006, Cognis acquired the Norwegian producer of high-quality Omega-3 fish oils, Napro Pharma AS, which broadens the Nutrition & Health product portfolio for Dietary Supplements and in Functional Food applications.

In April 2006, the investment in Desbas Deri Sebest, Turkey, was sold. The contribution of this investment to total assets and liabilities and consolidated profit and loss was not material.

In March 2006, Care Chemicals broadened its product portfolio in the rapidly growing specialty polymers sector by the Group's acquisition of CRL (Cosmetic Rheologies Ltd., UK). CRL's business promises an innovative pipeline of products, and strong synergies with Care Chemicals' key accounts.

### Raw Materials

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 (about 39% in 2007). The single most significant raw material we use is natural lauric oils, particularly palm kernel and coconut oil, which represented about 25% of our raw material purchases in 2007. We also use a broad range of petrochemical derivatives (about 38%), most significantly ethylene oxide (about 10%). Raw materials other than petrochemical derivatives and natural oils and fats ("Other Raw Materials") represented about 23% of total raw material purchases in 2007.

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 service.

### Natural renewable oils and fats

Cognis uses about one million metric tons of oils and fats globally. The largest 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 animal fats and other vegetable oils. We are a major global consumer in most of these product categories.

Prices of lauric oils have been particularly volatile and unpredictable in the past due to adverse climatic conditions, natural disasters, regional political events and other factors.

The market price of lauric oils is denominated in US dollars. Market prices have increased strongly in 2007. In US dollars we observed on average a lauric oils increase of 50.7% in 2007 versus 2006, and in euros the increase was 36.3%.

In 2007, we purchased €383 million (2006: €248 million) of lauric oils. This increase from 2006 to 2007 is mainly a result of higher lauric oil prices in 2007. We purchase lauric oils centrally for the Group excluding Oleochemicals. Natural oils and fats are commodities that are traded globally on market exchanges. Standard exchange-traded futures contracts on the products we use are not available, and so we manage commodity price risk through a mix of spot and forward buying in the relevant cash markets.

We also use animal fats, such as tallow, primarily in the USA, and non-lauric vegetable oils. We purchased €141 million (2006: €106 million) of animal fats and €90 million (2006: €68 million<sup>12)</sup>) of non-lauric vegetable oils in 2007.

The overall increase of purchases of natural renewable oils and fats from 2006 to 2007 is mainly due to higher prices in 2007 for reasons explained above.

### Petrochemical derivatives and Other Raw Materials

We purchased €593 million (2006: €569 million<sup>13)</sup>) of a wide variety of petrochemical raw materials in 2007, the most significant being €151 million (2006: €154 million) of

<sup>12)</sup> The prior-year figure has been amended to reflect additional vegetable oils not included in 2006.

<sup>13)</sup> Due to shifts in petrochemical derivatives categories, prior-year figures for "petrochemical derivatives and other non-petrol-based chemicals" have been amended to comply with the current presentation.

ethylene oxide and €34 million (2006: €38 million) of acrylates. Additionally, we purchase LAB (linear alkyl benzene), soda ash, TOFA (tall oil fatty acids), propylene oxide and ethylene amines.

In 2007, we also purchased €354 million (2006: €343 million<sup>14)</sup>) of Other Raw Materials.

Overall, prices of our petrochemical derivatives and Other Raw Materials increased by 4.3% in 2007 compared to 2006.

### Energy

In 2007, we purchased about €134 million (2006: €149 million) of energy, primarily in the form of electricity, coal, steam and natural gas.

### Restructuring Programs

€ millions	As of December 31,	2007	2006
Restructuring expenses		54	35
Less: Depreciation and amortization		(8)	-
Less: Additions to restructuring provisions		(23)	(24)
Add: Restructuring provisions released		1	1
Add: Use of restructuring provisions		13	24
<b>Cash restructuring expenses</b>		<b>37</b>	<b>36</b>

Cognis has implemented, and continues to implement, various restructuring initiatives in order to streamline processes and reduce costs. In 2007, we spent €37 million (2006: €36 million) of cash on restructuring.

## Risk Management

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

### Management System

Cognis regularly undertakes comprehensive 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 rational and transparent management systems. Our management system is 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, Germany, OHSAS 18001 (work safety) in Spain, Italy and Indonesia, or SA 8000 (social accountability) in Brazil 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 sub-prime 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

<sup>14)</sup> Due to shifts in petrochemical derivatives categories, prior-year figures for "petrochemical derivatives and other non-petrol-based chemicals" have been amended to comply with the current presentation.

- 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 quality requirements have to be met to satisfy our customers.

In 2007, we received many important awards from customers as well as from local authorities. Examples include: Gruenau Illertissen, Germany, received an "Ökoprofit" award from local authorities, Cognis Thai received an award as "Excellent Vendor of the Year" from Colgate Palmolive in Thailand, Cognis Indonesia received a "Zero Accident" award by the Indonesian Government, Nutrition & Health received an innovation award from Danone called "Dan'Innov 2007" and for the Tonalin® brand development a "Frost & Sullivan" award. Care Chemicals received eight international marketing communication awards for their advertising of "Feelosophy" and Cognis received an international award and three Mercury awards for the annual and sustainability report.

**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.

The new EU legislative framework known as REACH (Registration, Evaluation & Authorization of Chemicals) means that companies will be obliged to register any substance that they import or produce in quantities of one metric ton per year or more. Therefore, chemical companies such as Cognis are affected by REACH in their capacity both as a manufacturer and as a downstream user of substances.

We participated in national and international committees, meetings and workshops, enabling us to secure information as to the forthcoming developments. Our team has introduced a range of measures to ensure that we are well prepared for the new regulations. These include identifying all substances that

are relevant for the process of pre-registration, modifying IT systems and obtaining detailed information such as how and under what conditions Cognis products are used further down the value chain, and what sort of safety information already exists on the many and varied substances in question. We are also holding regular meetings with our business partners and customers, who will be similarly affected by REACH, in order to ensure that the extra costs and work load involved are kept to a minimum.

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 critical or fatal incidents but also in a very low incidence rate<sup>15)</sup> of 0.5 in 2007 (2006: 0.4). 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 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 on three counts. First, we are exposed to "transaction risk" when products manufactured in one currency region are exported to another currency region. Our main transaction risk results from net exports from the euro region into the US dollar region (including the USA and much of Asia). 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.

<sup>15)</sup> 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 recordable injuries and illnesses per 100 employees equals the incidence rate.

Concerning interest rate risk, we are exposed to changes in interest rates because €1,618 million of Cognis' debts<sup>16)</sup> bear 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 swaps and collars. 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, 2007, about 76% of our variable-interest debt was hedged in this way.

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 €30 million utilized for ancillary facilities and letters of credit as of December 31, 2007). This source of funding, however, is subject to various conditions and restrictions, including concerning the purpose for which the funds have been drawn, so that 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 scheme 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 may result in an adverse effect on Cognis' net assets, financial position and results of operations.

---

<sup>16)</sup> Excluding bank overdrafts, local loans and finance lease obligations.

## Outlook

We proved our ability to take on market-driven challenges in 2007, having worked constantly in previous years on optimizing our operations. Our results demonstrate that our strategy in being committed to the Wellness, Sustainability and now Green Chemistry trends enhances the value of the Group.

We expect to grow our business both in 2008 and 2009 through increasing sales volumes, and selling price increases to counter rising material costs. As such, sales growth is forecast in line with previous years.

An analysis of specific issues in our businesses is as follows:

- Care Chemicals is expected to lead the Group's sales growth with its innovative specialty products by focusing on the Wellness and "Green Chemistry" trends. Care Chemicals' growth globally is estimated at a high single digit. End consumers are becoming more and more environmentally conscious, so we expect to grow slightly above GDP in the European cosmetic, toiletry and household markets, where Care Chemicals is already the market leader. Elsewhere, we expect growth in line with GDP in the NAFTA and Mercosur regions, whereas double-digit growth is forecast for certain product lines in Asia-Pacific. On the downside, we expect a more intense fatty alcohols market as additional South-East Asian capacities have already become operational and have entered European markets, causing pressure on our selling prices
- Nutrition & Health is forecast to achieve strong sales growth with its broad portfolio. Not only the businesses of Pharma, Omega-3 and CLA are expected to bring in higher sales, but growth is also expected in more stable product lines such as Carotenoids, Food Technology and Botanicals. World-wide Nutrition & Health sales are estimated to grow in the mid single-digit range. The businesses of Pharma and CLA are expected to benefit from, firstly, increasing awareness for excipient applications for the Pharma segment, and secondly, from regulatory approvals that allow us to market CLA products with stronger claims. We also expect Omega-3 to continue achieving excellent growth rates, especially with new applications for the Functional Foods market. The more stable product lines are expected to benefit from tighter cost control and improved manufacturing processes, while mostly growing in line with regional GDP. In terms of potential risks specific to Nutrition & Health, growth in the Sterols market may be less dynamic than it was in the past, due to increased competition between end-consumer producers.

Also, regulatory bodies could potentially require applications for the marketing of product claims in regions such as Asia-Pacific and Latin America, thereby slowing down the overall growth that we have forecast

- We expect Functional Products to increase its sales mostly in line with regional GDP growth, resulting in a corresponding increase in its worldwide sales. We expect above-GDP growth in the Mining business as new copper installations are forecast to become operational. In other businesses such as Synthetic Lubricants, we aim to maintain our high market share and expand further in Asia, enabled by a shift in industry trends that favor our environmentally friendly lubricants. The business of AgroSolutions grew strongly in 2007, facilitated by record demand for vegetable oils. In 2008 and 2009, we are planning to grow on a more moderate level as we expect market factors driving the demand of vegetable oils to be volatile. Demand for AgroSolutions is also dependent on weather conditions. In the Polymers, Coatings and Inks ("PCI") segment, sales are expected to be maintained at regional GDP levels. We expect to compensate the slowdown in the US housing and construction sector by growth in emerging markets in Asia, Eastern Europe and Mercosur. Considering business specific risks, a further weakening of the US dollar exposes Functional Products particularly to both translation risk and transaction risk, as manufacturing costs of certain products are based on euros while revenues are generated in US dollars and/or currencies that are strongly correlated to the US dollar
- Pulcra Chemicals will concentrate on consolidating its activities under a stand-alone model after the carve-out in 2007. The new stand-alone business will continue the previously successful strategy of growing strongly in key regions such as China, the Indian Sub-continent and Latin America while maintaining market shares in mature markets. Textile Technology is expected to benefit from higher volumes sold in the emerging markets. Leather Technology is also expected to generate higher growth in key countries such as China, India, Pakistan and Brazil to compensate lower growth in European markets. Pulcra Chemicals will continue to optimize its business model, especially its administrative processes to improve its competitiveness against mid-scale Textile and Leather chemical producers. As for business-specific risks, Pulcra Chemicals' growth may not meet expectations if the level of growth in key regions is not sufficient to compensate challenges in mature markets

- Oleochemicals is forecast to grow sales in all its businesses above regional GDP. The Fatty Acids/Glycerin business is expected to profit from increased demand for glycerin. Due to the uncertainty in the bio-diesel market, a lower global supply of glycerin is expected to increase selling prices. The current level of crude oil prices is anticipated to drive further offshore exploration and drilling activities, thereby increasing demand for Oilfield Chemicals' products. Considering business specific risk, the Malaysian Fatty Alcohols market is expected to remain challenging due to increased global supply. Further, Oleochemicals may not grow as anticipated if glycerin prices do not increase as much as expected

In general, Cognis is exposed to the following opportunities and risks:

- We expect the trend toward "green" solutions in the personal care, home care and the industrial and institutional segments to continue offering us many opportunities to meet our growth targets
- The prices of both natural raw materials, especially vegetable oils, lauric oils and milk derivatives, 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 weakness of the US dollar poses both a transaction and a translation risk for our business
- Further, if the US dollar remains weak for a considerable period of time in future, barriers to entry may weaken and cheaper imports may be facilitated in businesses and regions where this was previously not possible due to prohibitive transportation costs
- Economic conditions globally are currently uncertain, driven by a potential slowing-down of the largest economy in the world, the USA. This could potentially affect our business in that we may only be able to sell a smaller number of volumes than anticipated, thereby resulting in lower growth than planned

- Petrochemical prices also influence our energy costs. Despite a reduced consumption of energy facilitated by improvements in manufacturing processes, energy costs may rise if petrochemical prices increase more than expected

We expect our Adjusted EBITDA to grow in both years mostly in line with sales, driven primarily by increased volumes of our innovative products and gains in market share in emerging markets. In order to meet our profit targets, we expect increases in selling prices to reflect higher material costs. To counter the potentially adverse effects, we will continue to optimize our cost base, especially SG&A expenses, as well as improve our manufacturing processes even further.

In terms of our cash generating ability, we expect improvements in both 2008 and 2009, especially since the Refinancing Transaction in 2007 has released us from regular capital repayments. Our operating cash flows are expected to increase in line with our profit-generating ability. Investment in working capital is expected to be less than in 2007, if raw materials and so inventories remain at around 2007 levels. We are also looking for further ways to optimize our working capital level. Capital expenditures are forecast to decrease in 2008 as a result of higher investments in 2007. As our new financing arrangements do not require capital repayments, our financing cash flows will increase compared to previous years, assuming stable pension payments. Our pension payments are expected to be stable provided that Plan Assets do not deteriorate substantially in value, for example, as a result of the sub-prime crisis in the USA. We also expect a €32 million withholding tax refund in 2008 related to our Refinancing Transaction in 2007.