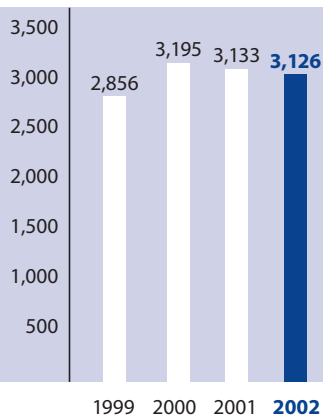


Management Report

- 37 Cognis Group posts steady sales performance
- 38 Increase in recurring EBITDA
- 38 EBIT and net earnings reflect Cognis Group purchase and initiated restructuring measures
- 39 Significant increase in cash flow
- 40 Currency effects main factor in decrease of total assets
- 41 Number of employees slightly reduced
Capital expenditure geared to enhancing production efficiency
- 42 Focusing on quality and environmental management
- 43 Research & Technology aligned to key areas
- 44 Oleochemicals increases market share and benefits from rise in demand for environmentally friendly drilling additives
- 45 Care Chemicals continues growth in care specialties sector
- 46 Nutrition & Health implements strategic restructuring and gains from strong demand for sterols
Functional Products extends competence in surface chemistry and profits from increased demand for environmentally friendly chemicals
- 47 Process Chemicals expands market position in textile technology sector
- 48 Key business risks and risk management
- 49 Significant events after the balance sheet date
- 50 Outlook for 2003

Sales (€ million)



Sales by Strategic Business Unit

€ million	2001	2002
Total	3,133	3,126
Oleochemicals	1,071	1,042
Care Chemicals	544	554
Nutrition & Health	262	276
Functional Products	690	684
Process Chemicals	509	497
Other Activities	57	73

1. Cognis Group posts steady sales performance

In the twelve months under review, the Cognis Group generated sales of € 3,126 million, thus closely matching the level of the previous year (€ 3,133 million) despite the difficult economic environment. Indeed, after adjusting for foreign exchange effects, the sales figure showed an increase of 2.2%. While positive growth was registered in the first half of the year, sales fell in the second half compared with the prior-year period due in particular to the weaker US dollar and unfavorable world economic developments. Against this difficult macro-economic background, Cognis succeeded in underlining its competitiveness through a further increase in sales volumes, albeit with average selling prices just short of the figures for the previous year.

Performance at the strategic business units was mixed. At +5.2%, Nutrition & Health showed the strongest growth (€ 276 million), with Care Chemicals (€ 554 million) also succeeding in implementing its growth strategy, posting an increase in sales of 1.9% as compared with the previous year. Oleochemicals (€ 1,042 million), Functional Products (€ 684 million) and Process Chemicals (€ 497 million) were unable to repeat the level of the previous year, due in large part to cyclical and foreign exchange factors. Sales in Other Activities rose to € 73 million as the result of, first, increased service activities and, second, an improvement in Fragrances sales of 28.1%

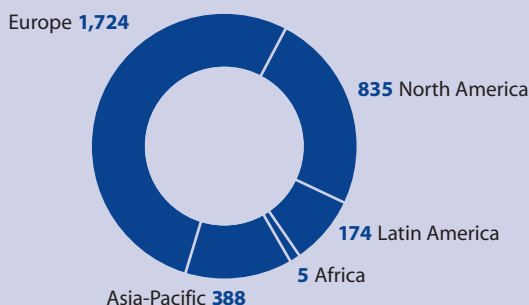
In Europe, Cognis increased sales by 3.1% compared with the prior-year figure, with our affiliated companies in Germany, Ireland and Turkey performing particularly well. North America posted lower sales (-5.0%) due to foreign exchange factors emanating from the weakness of the US dollar. After adjusting for these currency effects, however, the region's sales matched the previous year. Performance in Latin America was affected not only by the changes in the foreign exchange rates but also the economic decline suffered by Brazil and Argentina. Sales in this region fell 6.2% from the level for the previous year. In Asia-Pacific, the sales figure was almost identical to that of the prior period in spite of unfavorable currency effects. Denominated in local currencies, Cognis sales in Asia-Pacific showed an increase of 3.7%.

Acquisitions and divestments had virtually no effect on sales revenue. Laboratorios Dr. Vinyals S.A., taken over in mid 2001, Biosoph Laboratories S.A.S., acquired at the end of 2001, and the phosphonates business divested in December 2001 had a net effect on sales of the Cognis Group in 2002 of 0.1% in comparison with the previous year.

Sales by region

€ million	2001	2002
Total	3,133	3,126
Europe	1,672	1,724
North America	879	835
Latin America	186	174
Africa	5	5
Asia-Pacific	391	388

Sales by region in 2002 (€ million)



2. Increase in recurring EBITDA

In 2002, the Cognis Group generated earnings before interest, tax, depreciation, amortization and exceptional items (recurring EBITDA) amounting to € 393 million (2001: € 382 million). The change in foreign exchange rates that occurred in relation to the previous year had a negative effect on this figure amounting to € 8 million. The EBITDA return on sales rose from 12.2% to 12.6%.

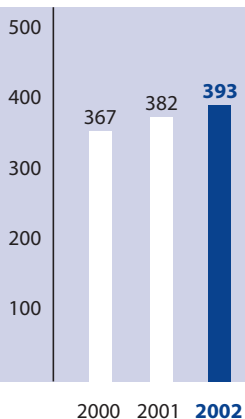
This highly encouraging earnings performance under difficult economic conditions resulted from improvements at Care Chemicals, Process Chemicals, Nutrition & Health and Functional Products. These were achieved through a combination of increased sales and the implementation of efficiency-enhancing measures. Oleochemicals was unable to repeat its EBITDA figure of the previous year. In its Basic Oleochemicals sub-segment, lower market demand emanating from cyclical influences led to a fall in average market prices. In view of the numerous negative external factors that prevailed, Cognis regards its overall EBITDA performance as further validation of its business strategy.

3. EBIT and net earnings reflect Cognis Group purchase and initiated restructuring measures

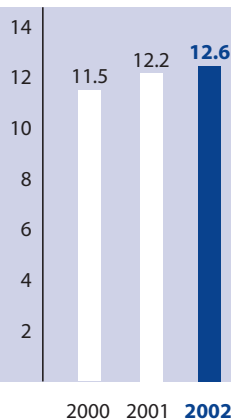
The EBIT figure for fiscal 2002 amounted to € 142 million. The scheduled goodwill amortization arising from the purchase of the Cognis Group, and depreciation and amortization taken on value increases in the other fixed assets in line with purchase accounting practice, led to a lower EBIT figure than in the previous year. The net effect of a number of extraordinary factors also had a reducing influence on EBIT for fiscal 2002. These exceptional items included, on the positive side, gains from restructuring our post-retirement healthcare plan in the USA (€ 15 million), and, on the negative side, restructuring charges of € 41 million, charges arising particularly in the functional sphere in respect of the ongoing process of separating from Henkel (€ 7 million), and other exceptional charges (€ 5 million) that are further explained in the Notes to the Consolidated Financial Statements.

In the course of the year under review, Cognis instituted a number of restructuring projects and these have also, in some cases, now been carried through. This led to restructuring charges totaling € 41 million. Of this figure, € 24 million was attributable to restructuring measures implemented in the USA, including a general reduction in personnel levels and closure of the production facilities at Hoboken and Lock Haven. The early retirement and pre-retirement part-time employment plan in Germany accounted for a further € 5 million. In Australia, we closed down the production site at Broadmeadows (€ 4 million). The restructuring of two operations in France led to redundancy payments amounting to € 2 million. The planned closure of the Kepec production site in Germany accounted for € 1 million. Restructuring charges in other countries amounted to a further € 5 million.

Recurring EBITDA in € million



Return on sales (%)



Condensed cash flow statement

€ million	2001	2002
Cash flow	251	327
Cash flows from operating activities	234	367
Cash flows from investing activities	-94	-85
Cash flows from financing activities	-96	-179
Cash flows from purchase of Group	135	0
Increase in cash and cash equivalents	179	102

The net financing costs line showed an increase in the net expense from € 54 million to € 183 million. This reflects the high level of debt and its effect over an entire fiscal year that resulted from the leveraged buy-out of the Cognis Group as at November 30, 2001. The interest expense increased from € 87 million in 2001 to € 156 million in 2002.

Earnings before tax was a negative € 41 million. While in the previous year there was a tax charge of € 58 million, in fiscal 2002 we recorded net tax proceeds of € 17 million. This resulted from a current tax charge of € 30 million and a deferred tax income of € 47 million. The tax rate was 42% (2001: 48%).

This net loss of € 41 million posted by the Cognis Group for fiscal 2002 is higher than the figure for the preceding year due essentially to an increase in interest expenses and higher levels of scheduled depreciation and amortization arising from the purchase of the Cognis Group.

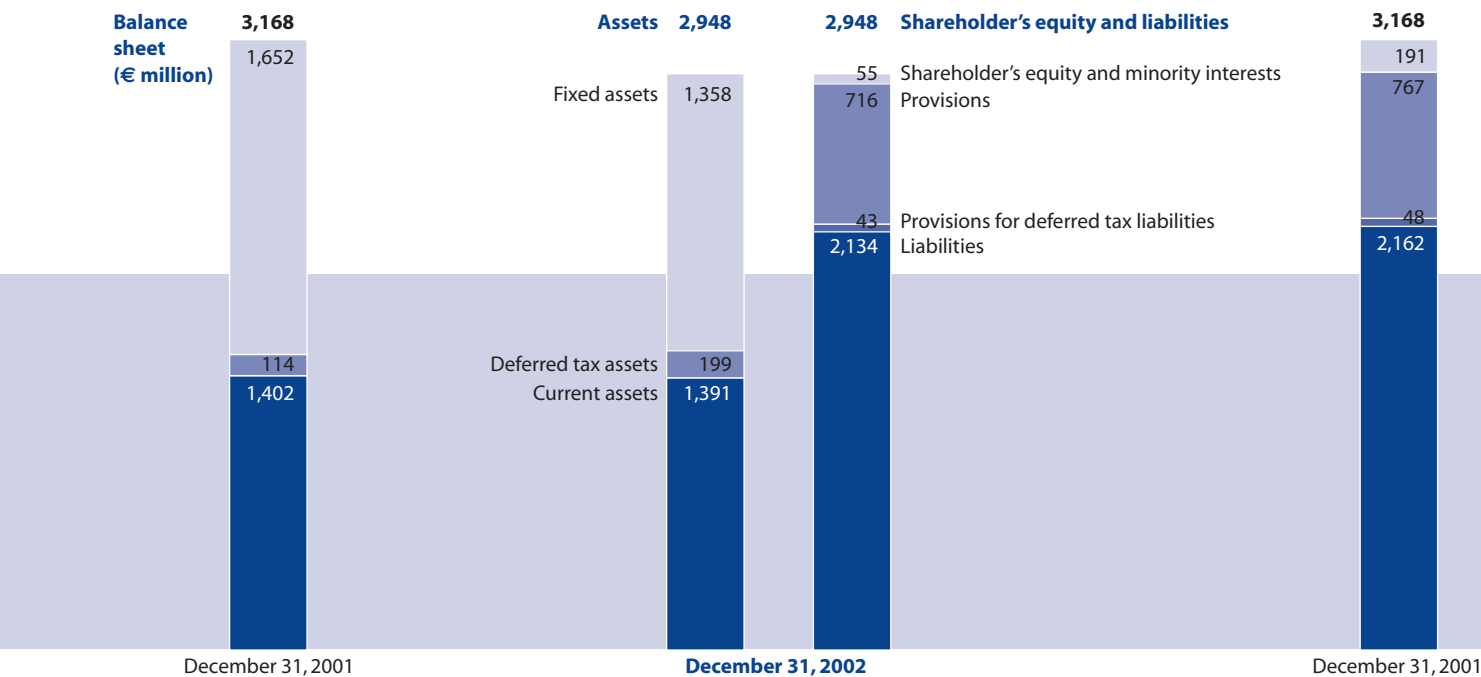
4. Significant increase in cash flow

Cognis was able to increase its cash flow from operating activities significantly in the year under review, from € 234 million to € 367 million. The main contributory factors here were an increase in topline cash flow and a reduction in net working capital.

The net outflow of funds from investing activities decreased from € 94 million to € 85 million. In the previous year, this figure included a gain of € 29 million from disposals of participations. Investments in intangible assets and in property, plant and equipment decreased from € 117 million in 2001 to € 98 million in 2002. In 2001, the take-over of a site in the USA had increased capital expenditure in property, plant and equipment by € 8 million. In addition, the initial benefits from focusing our investment activities in line with our World Class Manufacturing Program began to take effect. In 2002, payments received of € 13 million were recorded in conjunction with the purchase of the Cognis Group. We also increased our share in the affiliated company PT Cognis Indonesia, which resulted in payments out of € 2 million.

The negative cash flow from financing activities increased from € 96 million in 2001 to € 179 million in 2002. Here, an improvement in interest received from cash and cash equivalents invested was offset by significantly higher interest payments. These latter are due to the fact that the new financing structure was not put in place until December 1 in the previous year.

Cash flows from operating activities, investing activities, financing activities and the purchase of the Cognis Group resulted overall in an increase in cash and cash equivalents of € 102 million.



5. Currency effects main factor in decrease of total assets

The balance sheet total of the Cognis Group fell in 2002, due primarily to foreign exchange effects, from € 3,168 million to € 2,948 million. The fixed assets total decreased from € 1,652 million to € 1,358 million. Aside from the currency-related changes, this was also due to the significant increase in scheduled depreciation arising from the purchase of the Cognis Group. In addition, the measurement of our assets and liabilities was modified as a result of subsequent revaluations, as was the purchase price of the Cognis Group. This led to a downward adjustment of € 82 million in the fair value of goodwill and a write-up of € 3 million on other current assets, producing a net reducing effect of € 79 million on the value of fixed assets. Capital expenditure on fixed assets decreased from € 117 million in 2001 to € 98 million in 2002.

Deferred tax assets increased as a result of subsequent revaluations within the framework of the purchase of the Cognis Group, tax carry-forwards, and changes in the fair values of our derivative financial instruments. Cognis succeeded in appreciably reducing the funds tied up in trade accounts receivable and inventories

by strengthening its focus on working capital management. In the event, the figure for trade accounts receivable and inventories including foreign exchange effects decreased by a total of € 110 million. Cash and cash equivalents rose in fiscal 2002 by € 102 million.

On the liabilities side, there was a decrease of € 136 million in shareholder's equity including minority interests as a result of the net loss for the year amounting to € 41 million, the negative changes in the fair values of our derivatives (€ 24 million), and foreign currency translation losses (€ 71 million).

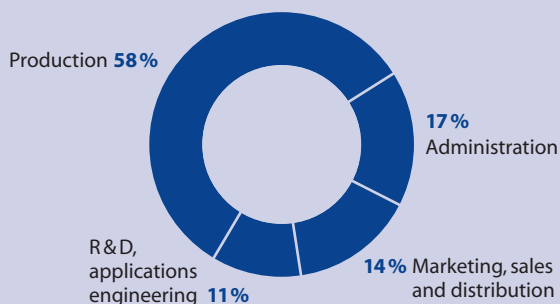
The provisions for pensions and similar obligations decreased as a result of foreign exchange effects, the restructuring of the post-retirement health care plan in the USA, and subsequent revaluations in association with the purchase of the Cognis Group.

Borrowings decreased by € 21 million. A reduction in bank loans of € 65 million was offset by an increase in borrowings from Henkel KGaA and Cognis Holding Luxembourg resulting from additional accrued interest. Loans used to finance the purchase price decreased by a total of € 73 million, of which € 25 million was attributable to redemption payments and € 48 million to changes in foreign exchange rates.

Trade accounts payable decreased by € 33 million, primarily as a result of foreign exchange effects and items contained in the prior-year figure relating to services in connection with the purchase of Cognis Group.

Changes in the Group and acquisitions only had a minor influence on the balance sheet total. Biosoph Laboratories S.A.S., accounted for in the previous year as a participation, was integrated within Cognis France S.A. in the course of fiscal 2002, while our stake in the affiliate Anticor (France) was divested.

Workforce structure



6. Number of employees slightly reduced

At December 31, 2002, the workforce of the Cognis Group worldwide numbered 8,946 employees (core workforce excluding apprentices, trainees and internees). Compared with the closure date of the previous year, this represents a decrease of 119 employees.

The number of employees in Europe increased slightly as Cognis took over further finance, IT and purchasing management functions from Henkel. With the commencement of local production, there were also new hires in Poland, while the sale of our stake in Anticor, France, had a decreasing effect on overall workforce numbers.

In North America, Cognis cut a further 64 jobs as its restructuring program, initiated in 2001, continued through the year under review.

The core workforce in Latin America decreased by 102 employees. This resulted both from the restructuring of production in Brazil, and from the transfer of employees from Cognis Mexicana to Henkel Mexicana. Previously, Cognis Mexicana had been performing administrative services on behalf of Henkel.

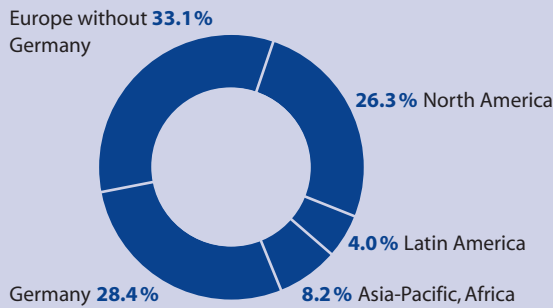
In Asia-Pacific, the number of employees fell by 51. This is predominantly due to the closure of the Broadmeadows site in Australia and the introduction of a new security management approach in Indonesia in which services are being outsourced to a greater extent than was previously the case.

7. Capital expenditure geared to enhancing production efficiency

Expenditure on property, plant and equipment in 2002 was aligned to our World Class Manufacturing Program and the associated worldwide plant distribution concept. This involves the establishment of regional production networks to secure close proximity to our markets and the dedication of facilities to certain technologies to increase manufacturing efficiency. Examples of the implementation of this approach in 2002 include the concentration of sulfosuccinate production in Germany and the pooling of our defoamer activities in Spain. As a result of these relocations, Cognis has been able to dispense with two sites in Taiwan and Australia and also a production plant in Germany. This concentration of our production capabilities has resulted in a decrease in the outflow of funds from investing activities. Capital expenditure on property, plant and equipment in 2002 amounted to €97 million compared with €116 million in the previous year.

These capital expenditures were primarily aligned to those areas into which the Cognis Group intends to expand. In France, for example, capacity for the production of phytosterols was increased in order to support growth at our Nutrition & Health segment. These sterol esters are active dietary ingredients and owing to their cholesterol-reducing effect, they are taking on a key role in the growth market for functional foods as well as opening up new prospects in the pharmaceuticals sector. With the commissioning of a

Capital expenditure by region



new plant in France for the production of UV-curing agents for the coatings and inks industry, Cognis now has the most advanced environmentally compatible manufacturing facility of this type in the world. And a new production capability for defoamers was taken on stream in the USA. With our innovative and patented defoamer technology generating unique product properties, this investment can be expected to drive further growth at our Coatings & Inks subsegment. Production expansion activities were also geared toward supporting and extending the strong market positions of the Cognis Group in its existing fields of business. The modernization of a fractionating plant in France, for example, will provide additional manufacturing capacities for long-chain and high-purity alcohols to support our business activities in these attractive markets. Meanwhile, the Synlubes subsegment will profit from the commissioning of a new reactor in Germany for the production of fatty acid esters. This not only provides for an increase in capacity but will also bring cost advantages. The installation of new plant based on advanced technology in our hydrogenation facilities in Germany has resulted in significantly increased throughputs, so supporting growth in the fatty alcohols segment.

8. Focusing on quality and environmental management

The process of global certification to ISO 9001/14001, started in previous years, was successfully continued in 2002. Our sites in France (Meaux), Ireland, Japan, Indonesia, Canada, Mexico and China were all registered to ISO 14001 for the first time.

Further focal points in this respect involved worldwide product harmonization, the establishment of GMP standards for cosmetic basestocks and dietary supplements, and the expansion of our Pharmaline activities, all in response to the requirements of our international customers.

GMP standards are geared toward consumer protection. Aside from the requirement for comprehensive production documentation – to ensure full traceability back to the raw material and the effective implementation of product recall actions should this be necessary – GMP standards also require the institution of preventive measures for avoiding cross contamination, micro-biological contamination and labeling errors.

Further progress was also achieved in certification procedures relating to the occupational safety of our employees and environmental and community safety. For example, Cognis Thailand has become our first affiliate to successfully complete the certification procedure leading to registration according to the internationally recognized safety standard OHSAS 18001. In order to satisfy more effectively the increasing requirements of our customers, Cognis has restructured its SHEQ management system (Safety, Health, Environment, Quality). The new organization now has a regional structure comparable with that on the production side. The SHEQ regional managers will, in collaboration with the corporate level, be harmonizing the standards applied in the various regions and exchanging worldwide best practice solutions.

Expenditure on R & D / Technical Service

€ million	2001	2002
Research and development	73	76
Technical Service	44	40
Total	117	116

9. Research and Technology aligned to key areas

Research and development costs at Cognis rose from € 73 million in 2001 to € 76 million in 2002. This corresponds to a ratio of 2.4% of sales (2001: 2.3%). The adjustment to the fair values of our intangible assets within the framework of the purchase of the Cognis Group led to an increase in amortization of € 7 million in respect of our research and development investment. Conversely, the effect of foreign exchange rates reduced expenditure by € 3 million. Further savings were achieved within the framework of the R&D Efficiency Program (€ 1 million).

Operating on the basis of measurable targets and a continuous review process, the Research & Technology division supports growth at Cognis through

- the development and provision of new, innovative and highly profitable products and concepts that focus on the strategic growth areas of Cognis,
- support in the optimization of manufacturing costs,
- a continuous process of technology exchange between Cognis business units,
- the implementation of concepts designed to reduce the time to market of new products.

Within this framework, our R&D activities have been concentrated in our research centers of Düsseldorf, North America (Cincinnati, USA), South America (Jacarei, Brazil), Southern Europe (Ponthierry, France and Barcelona, Spain) and LS Nancy (Pulnoy, France), the latter as a specialized facility for the development of active substances for skin and hair care.

The individual requirements of the various strategic business units were applied to define and specify the future portfolio of Cognis Corporate Research & Technology. The activities of Research and Technology have thus been refocused on ten central areas

- Products and concepts for Personal Care,
- products and concepts for Home Care,
- products and concepts for Nutrition & Health,
- sustainable solutions for Functional Products and Process Chemicals,
- new oleochemical derivatives,
- formulation concepts and delivery systems,
- product properties with screening and performance verification,
- bioconversion,
- technologies for the purification of high-quality products,
- optimization of production processes.

In 2002, Cognis conferred for the second time innovation awards on three selected teams of employees from Germany, the USA and France. A total of 25 projects from five countries were short-listed for this second competition in which a total of 126 employees participated. The Gold Award for Innovation went to a German-American group. This team succeeded in extending the properties of conventional wet wipes through the incorporation of a care component. For a long time, the wet wipes available on the world's markets have used a primarily surfactant-based formulation that can lead to dryness of the skin. The Cognis employees in this case utilized their know-how in relation to lotions, developing a special care formulation that allowed problem-free impregnation of the wipes without adversely affecting their cleaning effect.

Oleochemicals: Sales

€ million	2001	2002
Total	1,071	1,042
Basic Oleochemicals	553	521
Primary Surfactants	423	406
Other ⁽¹⁾	95	115

⁽¹⁾ The reporting unit Other includes the Silicates business, our Oilfield Chemicals operation and the other activities of Oleochemicals

This innovation illustrates particularly well the technological leadership of Cognis in the care chemicals market. The Silver Award for Innovation went to an American-German team. The successful project in this case involved the utilization of a star-shaped molecular structure in order to prevent the formation of foam in coatings and inks and facilitating the manufacture of environmentally friendly products using the associated defoamers. Based on the principles of the concept, the product has been given the brand name "FoamStar". The team succeeded in fundamentally changing and improving conventional defoamer technology which, for the last approx. 30 years, has been based on the use of mineral oil and silicone. The patented technology relating to the newly developed molecule will strengthen the position of Cognis in the Coatings & Inks market. The Bronze Award for Innovation was conferred on a German-French team. This group developed a diesel additive on the basis of a new, patented ethoxylation technology that helps to significantly reduce pollution from environmentally harmful sulfur oxides (SO_x). These new products, which Cognis is distributing under the brand name "Eumulgin", and the innovative process developed for their manufacture have enabled Cognis to further expand and consolidate its market leadership in the area of diesel fuel additives.

10. Oleochemicals increases market share and benefits from rise in demand for environmentally friendly drilling additives

Our Oleochemicals strategic business unit generated sales of € 1,042 million in 2002. This figure represents the aggregated revenues from the activities of our Primary Surfactants, Basic Oleochemicals, Oilfield Chemicals and Silicates businesses.

The decline in sales compared with the previous year of 2.7% essentially resulted from unfavorable foreign exchange developments in relation to the euro. While the subsegments Basic Oleochemicals and Primary Surfactants were unable quite to repeat the excellent performance of the previous year, Cognis succeeded in significantly increasing sales in oilfield chemicals despite the negative influence on product demand caused by two tornadoes in the Gulf of Mexico. In the regional analysis, Europe was able to maintain its 2001 level while sales in the other regions fell below the prior-year figures.

Care Chemicals: Sales

€ million	2001	2002
Total	544	554
Care Specialties	241	253
Specialty Surfactants	303	301

The sales performance at Basic Oleochemicals (€ 521 million) was adversely affected by foreign exchange fluctuations and a general softening of market prices resulting from the cyclical downturn in the world economy and especially that of North America. In the Primary Surfactants subsegment (€ 406 million), the decrease in sales resulting from currency and pricing effects was partially offset by increases in volume, particularly in North America. In Thailand, Cognis took a new reactor on stream around mid 2002, resulting in a significant increase in capacity in Asia. Cognis generated sales from Other Activities amounting to € 115 million. The increase in sales of 21% is essentially due to the business performance of our Oilfield Chemicals unit. Here, the success of focusing on drilling additives was further enhanced by the general trend toward environmentally friendly, petrochemical-free basestocks. In addition, Cognis profited in the USA from its successful registration with the Environmental Protection Agency (EPA) providing a further competitive advantage in the marketplace. Business performance in relation to silicates remained stable in fiscal 2002.

11. Care Chemicals continues growth in care specialties sector

In a difficult market environment, Care Chemicals succeeded in increasing sales from € 544 million in the previous year to € 554 million, even though a product line sold toward the end of 2001 no longer contributed to the revenue generated in fiscal 2002. Following the change in the organizational structure at Cognis effective January 1, 2001, the Care Chemicals strategic business unit now comprises the subsegments Care Specialties and Specialty Surfactants.

Through the further successful expansion of our care specialties business, sales at the Care Chemicals SBU rose overall by 1.9%. The product portfolio of Care Specialties was supplemented through the incorporation of a line of botanic extracts and the production of face masks from the marine-derived raw material chitosan. Specialty Surfactants repeated the good business performance of the previous year. After adjusting for foreign exchange effects and the sale of a product line toward the end of 2001, the recurring sales figure actually shows a significant increase. Our co-surfactants business, and particularly APG sales, were particular contributory factors in this respect. Sales in relation to products launched onto the market within the last three years were also successfully increased.

In the regional breakdown, Europe and Asia-Pacific contributed to the positive performance posted by Care Chemicals, due in particular to above-average business growth in Turkey, Thailand, Indonesia and Taiwan. Turkey's recovery from its currency and economic crisis of the preceding year was particularly noticeable, added to which Cognis was able to further expand its share of the national market. Exports to the Middle East also increased. Sales in North and Latin America remained below the level of the previous year due exclusively to currency effects.

Nutrition & Health: Sales

€ million	2001	2002
Total	262	276
Food Technology	116	116
Sterols, Vitamin E, Carotenoids, Botanic Extracts	141	156
Other	5	4

12. Nutrition & Health implements strategic restructuring and gains from strong demand for sterols

The sales performance of our Nutrition & Health strategic business unit confirmed the validity of the strategic realignment undertaken in 2002. This SBU is primarily responsible for the activities of Cognis in relation to dietary supplements and food technology. In future, the dynamic market sectors of functional foods and pharmaceutical ingredients will also be more intensively developed, as will certain specialty fields such as animal nutrition. An exclusive license agreement signed in 2002 relating to the production and sale of CLA from 2003 opens up further promising prospects for Cognis. CLA (conjugated linoleic acids) are used in dietary foods and functional foods and contribute, for example, to reducing body weight.

Sales at Nutrition & Health rose from € 262 million in 2001 to € 276 million in 2002 (+5.2%). If the exchange rates had remained stable, the growth figure would have been 7.2%. This is the strongest percentage growth of all the strategic business units at Cognis. The demand for sterols was particularly encouraging. In regional terms, this is reflected by a disproportionately high rate of sales growth in Europe and, denominated in the local currency, North America.

In the Food Technology subsegment, sales rose by 0.4%. Encouraging performance in our European business was largely offset by a downturn in exports to Latin America, with the weakness of the economies of Argentina and Brazil having a particularly adverse effect.

Sterol sales increased significantly compared with the previous year as a result both of the full utilization of existing capacities and the commissioning of a new production plant in France. The development of this product line illustrates the dynamic growth of the market for functional food. Sterol esters are, for example, used in cholesterol-reducing margarines. Sales in vitamin E were unable to match the level of the previous year due to adverse price developments. Through the introduction of a natural vitamin E in the European market, however, Cognis was able to extend its quality leadership in natural vitamin E products. Sales generated by the Carotenoids subsegment were slightly above the level of the previous year.

Functional Products: Sales

€ million	2001	2002
Total	690	684
Coatings&Inks	315	319
Synlubes, AgroSolutions	248	255
Other ⁽¹⁾	127	110

⁽¹⁾ The reporting unit Other includes the product groups Performance Monomers and Mining Technology and also the other activities of Functional Products

13. Functional Products extends competence in surface chemistry and profits from increased demand for environmentally friendly chemicals

The newly formed strategic business unit Functional Products comprises the subsegments Coatings&Inks, Synlubes, AgroSolutions, Performance Monomers and Mining Technology. In this SBU, Cognis pools and utilizes its core competencies in surface chemistry and the application of environmentally friendly chemicals so that it may offer innovative concepts and formulations to its customers in the individual industrial market segments.

With a sales figure of € 684 million, Functional Products was almost able to repeat the performance of the previous year despite the continuing economic weakness of the more important industrial markets. Denominated in local currencies, it achieved a growth of 2.6%. This reflects in particular the excellent performance at Coatings&Inks, Synlubes and AgroSolutions. Mining Technology was unable to quite match the good result of the previous year, while Performance Monomers suffered from the economic situation in North America. Coatings&Inks was able to compensate for the weakness of the North American market through the introduction of new products, particularly in the coating additives sector. It was onto this market that, for example, our new "FoamStar" defoamer technology was launched in 2002. Business in Japan and China was also successfully expanded.

Building on the technological competence of Cognis, Synlubes further expanded its market share in the fields of transportation and refrigeration in North America. AgroSolutions also increased its market share, particularly in relation to major customers. The ongoing development of our systems business, e.g. through the introduction of our Quality Trait Analysis (QTA) service, further strengthened Cognis' standing in the AgroSolutions sector. The successful integration of the Biosoph operation in France likewise boosted the sales figure.

Mining Technology consolidated its position in the marketplace. Developments at the Performance Monomers product group, which primarily concentrates on the North American market, fell below expectations.

In regional terms, Cognis was able to significantly increase its business volumes in Europe (+5.5%), especially in France, Spain and Turkey. In France, the acquisition of Biosoph – completed toward the end of 2001 – had a positive effect on sales. Spain profited from strong demand for photomers (Coatings&Inks) and also from the success of an advertising campaign in the AgroSolutions sphere. In North America, sales in local currency were just below the level of the previous year. In Latin America, Functional Products achieved an encouraging growth in sales despite the economic weakness of Argentina and Brazil. Sales in Asia-Pacific rose particularly sharply in percentage terms.

14. Process Chemicals expands market position in textile technology sector

The strategic business unit Process Chemicals provides the textiles and leather processing industries and also the plastics sector with specialty products and system solutions covering the entire production process.

In fiscal 2002, sales of € 497 million were generated through these businesses. This corresponds to a decline in respect of the prior-year figure of 2.4%, primarily due to foreign exchange effects.

In the year under review, Plastics Technology posted sales of € 162 million (-2.3%). Denominated in local currencies, however, sales fell by just 0.3%. Overall, these results reflect the difficult economic environment in which our end-customer industries, and particularly the construction, automotive and packaging sectors, are operating. Through further gains in market share,

Process Chemicals: Sales

€ million	2001	2002
Total	509	497
Plastics Technology	166	162
Textile Technology	263	262
Other ⁽¹⁾	80	73

⁽¹⁾ The reporting unit Other comprises Leather Technology and the other activities of Process Chemicals

Cognis was nevertheless able to significantly increase sales with lubricants, particularly for the PVC industry. However, sales of stabilizers fell below the prior-year figure. The price reduction in lead stabilizers was only partially offset by growth in calcium-zinc stabilizers. Sales at the Textile Technology subsegment remained stable at the level of the previous year despite the negative effect of foreign exchange rate fluctuations. Outstanding performance in Turkey compensated for the downturn in Germany within the European region. In North America, we gained market share and increased sales under conditions of weak demand. This achievement was due to the further expansion of our systems business and the introduction of new products. In Japan we succeeded in winning customers from a former competitor in the printing sector, with sales increasing significantly as a result. In Latin America, the weakness of demand in Mexico and Argentina was only partially offset by high percentage growth in Columbia. Sales under the Other heading fell by € 7 million. While business at Leather Technology remained stable at the level of the previous year despite the weakness of demand worldwide, sales from other activities decreased owing to a reduction in contract manufacturing volumes.

In the regional analysis, sales in Europe and Latin America were particularly down on the figures for the previous year. North America remained stable at the prior-year level, with a significant improvement being achieved when measured in local currency. Cognis likewise posted an encouraging increase in sales in Asia.

15. Key business risks and risk management

In conducting international business in the field of specialty chemicals, the companies of the Cognis Group are exposed to a number of risks that are inseparably related to their entrepreneurial activities. The Cognis Group has implemented an internal monitoring and control system in keeping the provisions of KonTraG – § 91 (2) AktG [German Law on Corporate Governance and Transparency]. The purpose of this system is to ensure the timely identification of economic difficulties and commercial problems so as to minimize the ensuing effects and secure the ongoing viability of the Group. A detailed reporting system in the individual companies and also at Group level, and the activities of the Internal Auditing department support management in recognizing risks at an early stage and in instigating the appropriate responses. Cognis counters operational risks through a raft of measures. In the procurement field, we alleviate the effects arising from fluctuating raw material prices, particularly for coconut and palm kernel oils, through a strategic procurement management approach that, using flexible purchasing strategies and forward contracts, optimizes cost and enables sudden volatilities in the market to be smoothed out. On the production side, where we are reliant on highly complex manufacturing processes and production facilities, we counter the attendant risks by applying appropriate

safety standards, performing regular maintenance, and ensuring the high qualification of our employees. A healthy mix of major international clients and local customers characterizes our market structure. This enables us to avoid the potentially critical effects that can emanate from the loss of individual accounts. Revenues originating from the supply of products and services to Henkel, our largest single customer, are below 10% of total sales. Moreover, these activities are secured in part by long-term agreements. We hedge financial risks through prudent interest rate, currency and cash management practices. The loans granted within the framework of the senior facilities agreement give rise to variable interest charges linked to developments in LIBOR (for our US dollar loans) and EURIBOR (for our euro loans). The interest rate risks arising from this situation have been extensively hedged through the use of interest rate swaps, caps and floors. In addition, currency risks are hedged through the use of financial instruments. The management of derivatives is the responsibility of our central Treasury department. Affiliated companies likewise enter into forward contracts, with the central Treasury department usually acting as the counterparty. The identifiable risks have been adequately accounted for by appropriate provisions. No risks came to light in the year under review which – either individually or in the context of the overall level of exposure – could endanger the continued existence of the Company as a going concern.

16. Significant events after the balance sheet date

In February 2003, Cognis signed an agreement on the acquisition of the activities of Laporte Performance Chemicals in a transaction that is still awaiting approval from the local anti-trust authorities. The acquisition involves two sites with production and development in Great Britain plus several distribution companies. Laporte Performance Chemicals has a workforce of 220 employees and in 2001 generated sales of £64 million (approx. € 100 million). The Laporte Performance Chemicals activities offer an excellent fit with the product range of Cognis in its Functional Products SBU. One of the key advantages of the acquisition was that it would complement and extend our platform for ecologically sustainable chemistry and thus enable us to develop new growth markets. The license agreement signed in August 2002 with Natural ASA, a Norwegian research and development company, came into force in February 2003. It relates to the production and marketing of conjugated linoleic acids (CLA) which are used in diet foods and functional foods.

In February 2003, Cognis signed an agreement enabling it to purchase the shares in the French company Protina Lactovit S.A., which specializes in the production of flavorings for, in particular, the meat processing industry.

17. Outlook for 2003

In the year under review, the advantages inherent in Cognis' balanced portfolio with its numerous market segments and regional activities were significantly underlined. Despite a difficult economic environment, Cognis managed to maintain its sales at a stable level while once again increasing its recurring EBITDA figure. The Group also succeeded in expanding its market share and further consolidating its market position in numerous sectors.

With their outstanding market positions, we expect our strategic business units again to perform well in 2003. The results of the optimization programs initiated in fiscal 2002 will provide further support in this endeavor. The alignment of the portfolio to the megatrends that fall under the headings of "Wellness" and "Sustainability" will enable Cognis to achieve lasting growth. The need to be able to offer environmentally compatible products and systems is continuously increasing in line with growing consumer awareness of environmental issues. With our natural-source raw

materials, we are exceptionally well placed to meet this challenge and satisfy the associated requirements. We anticipate being able to report positive developments in both sales and operating profit in 2003. However, this expectation is based on the assumption that the economic environment will recover from the level of activity that prevailed during the second half of 2002. We expect the gross domestic product of Europe to grow by around 1%. At 2%, GDP growth in the USA is expected to be higher than in Europe. These forecasts in turn assume that the current geopolitical crises (such as the Iraq conflict, increasing oil prices, potential terrorist attacks) will ease or at least not become significantly heightened. In view of the international alignment of Cognis, developments in foreign exchange rates are also of great significance. On the procurement side, we have assumed that market prices for, in particular, lauric oils will not significantly increase compared with average level that prevailed in the fourth quarter of 2002.