degussa.

creating essentials

Annual Report 2005

Preprint

Degussa ● Annual Report 2005 – Preprint

our business ● our values

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Key Figures

in € million	2001 [1]	2002 [1]	2003	2004	**2005**
Sales	11,862	11,765	11,081	10,740	11,752
EBITDA	1,858	1,747	1,630	1,583	1,585
EBITDA margin	15.7 %	14.8 %	14.7 %	14.7 %	13.5 %
EBIT	988	936	892	931	940
ROCE [2]	9.3 %	8.5 %	9.2 %	9.4 %	9.8 %
Group net income after minority interests	421	227	– 261	298	– 491
Earnings per share in €	2.05	1.10	– 1.27	1.45	– 2.39
Dividend per share in €	1.10	1.10	1.10	1.10	0.00 [3]
Total assets	18,127	15,185	14,042	13,633	13,498
Equity ratio	33 %	37 %	33 %	34 %	31 %
Capital expenditures [4]	1,269	1,001	778	722	814
Depreciation [4]	868	829	915	661	643
Employees as of December 31	53,378	47,623	45,348	45,139	45,553

[1] In accordance with US GAAP.
[2] Return on capital employed.
[3] Proposed.
[4] Intangible assets, property, plant and equipment.

Since January 1, 2004 the consolidated financial statements for the Degussa Group have been prepared in accordance with the International Financial Reporting Standards (IFRS). The figures for 2003 have been restated.

The Food Ingredients activities are classified as discontinued operations since an agreement has been signed on the divestment of these activties and the income statement and profitability indicators for 2005 and 2004 have been adjusted accordingly.

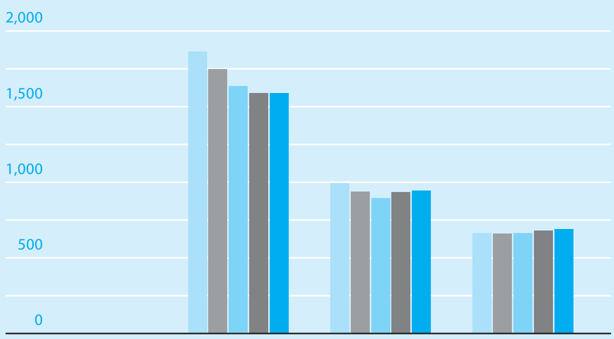
Degussa stock

ISIN	DE 0005421903
Bloomberg ticker symbol	DGX GR
Reuters ticker symbol	DGXG.DE
No. of shares	205,623,590
Market capitalization at year end 2005	€8,811 million
XETRA closing price at year end	€42.85
Dividend per share	€0.00 [1]
Dividend yield	0 %

[1] Proposed.

Operating performance

in € million



	EBITDA	EBIT	Operating result
2001	1,858	988	659
2002	1,747	936	655
2003	1,630	892	660
2004	1,583	931	674
2005	1,585	940	683

Highlights 2001–2006

February 9, 2001
"New" Degussa: The new Degussa AG, formed from Degussa-Hüls AG and SKW Trostberg AG, is entered in the Commercial Register.

February 12, 2001
Stock market listing: Trading in the new Degussa shares starts.

March 2001
Start of divestment program: Many non-core activities are divested over the next four years as Degussa shifts its focus to specialty chemicals. Total proceeds of over €4 billion are well above expectations.

October 2001
Corporate culture: "Vision, Mission, Guiding Principles" adopted.

June 24, 2002
Takeover bid: RAG makes a voluntary public offer for shares in Degussa AG.

September 23, 2002
New index: Degussa shares are transferred from the DAX to the M-DAX as the takeover bid is expected to reduce the free float.

January 20, 2003
Focus on China: Establishment of Degussa (China) Co. Ltd., a holding company based in Beijing.

February 14, 2003
Transfer of shares: RAG acquires a 46.48 percent stake in Degussa.

March 6, 2003
Degussa Foundation starts work. It pools the company's support for cultural and scientific projects.

June 1, 2003
Additional post: Professor Utz-Hellmuth Felcht, Chairman of Degussa's Board of Management, is given a seat on RAG's Board of Management.

November 24, 2003
Successful bond issue: Degussa raises the issue volume of its first bond from €1.0 billion to €1.25 billion in response to high demand.

April 13, 2004
Compliance: Degussa adopts Global Code of Conduct.

April 23, 2004
Growth in China: New R&D center opens in Shanghai. In May a cooperation agreement is signed with Jida New Materials, Changchun, on the joint development, production and marketing of high-temperature polymers for automotive and aviation engineering.

June 2004
New majority shareholder: RAG raises its stake in Degussa to 50.1 percent as planned.

September 16, 2004
Corporate history: US historian Peter Hayes publishes "Degussa in the Third Reich. From Collaboration to Complicity".

October 24, 2004
New source of funding: Degussa launches Euro Commercial Paper (ECP) program with nominal value of €750 million, giving it access to the short-term institutional debt market.

December 2004
Production in China: Construction of production plants for colorants and polyester starts at the Shanghai multi-user site. Start-up is scheduled for early 2006. The multi-user site will be used by various business units.

January 2005
Aid: Degussa and its employees donate around €850,000 to tsunami victims in South Asia.

Moving ahead in China: Establishment of a joint venture with Shandong Cathay Lineng Biotechnology. Plans to build a production plant for L-lysine in Jining with capacity of 40,000 metric tons p.a.

February 2005
Investment approved: Capacity at the carbon blacks facility in Paulinia, Brazil, is to be raised to 100,000 metric tons p.a.

Disposal: The nucleic acids group Proligo is sold to the life-science company Sigma-Aldrich Corporation, St. Louis, Missouri, USA.

March 2005
New program: Board of Management announces "Degussa 2008" program. The aim is to meet long-term financial goals, pave the way for growth, raise competitiveness and strengthen market leadership.

Research: Process Intensification Project House is set up in Hanau-Wolfgang to work on new process strategies and reactor concepts. Aim: more flexible production facilities for specialty chemicals.

High demand: Expansion of production capacity for superabsorbents and acrylic acid in Krefeld at a cost of around €40 million. Followed in April by expansion of capacity at Greensboro, USA.

April 2005
Focus on the future: Nanotronics Science-to-Business Center opens in Marl. Purpose: To develop systems solutions based on nano-scale materials for electronics applications. Total R&D expenses: €50 million.

June 2005
Approval: Construction of a new isophorone production line in Herne, which is scheduled to come on stream in 2007.

Expansion: Following acquisition of all remaining shares in CYRO Industries, Rockaway, USA, methylmethacrylate capacity in Fortier, USA, is to be raised by 20,000 metric tons to 480,000 metric tons.

August 2005
Commitment: About 600 young people start vocational training courses at Degussa. Trainees account for 7.7 percent of the payroll, well above the average for the German chemical industry.

September 9, 2005
Divestment: Sale of the Food Ingredients Business Unit to Cargill, Minneapolis, USA, for €540 million is agreed.

October 2005
Impairment charge: Degussa takes an impairment write-down of €836 million on its fine chemicals activities due to unsatisfactory business trends and poor earnings prospects.

Real estate management: Deutsche Immobilien Chancen AG and Morgan Stanley Real Estate Funds acquire Degussa's former headquarters building in Frankfurt.

Disposal: US metallurgy company ESM is sold to the financial investor Platinum Equity, Los Angeles, for US$ 55 million.

Project completed: The world's largest methionine facility comes on stream in Antwerp. Construction cost €300 million and was Degussa's biggest ever single investment.

December 2005
Growth market: Degussa and Forhouse Corporation, Taiwan, set up a joint venture to produce optical quality polymethylmethacrylate (PMMA) molding compounds for flat screens.

Start-up: JIDA Degussa starts production of high-temperature polymers in China. JIDA is a joint venture of Degussa and Jilin University.

Announcement: RAG plans to acquire the remaining shares in Degussa AG, including the 42.86 percent held by E.ON. It is making a public offer for the free float.

January 1, 2006
Leaner structures: Divisional management structure is abolished. Business units are reduced from 20 to 17, reporting directly to the Board of Management. Degussa's Board of Management is increased to six members.

White biotechnology: Bio Science-to-Business Center is established in Marl to develop biotechnological products on the basis of natural raw materials. Total R&D expenses: €50 million. Sixty research scientists.

February 2006
Negotiations: The Board of Management decides to start negotiations on divesting the activities grouped in the Construction Chemicals segment.

Recommendation: The Board of Management and Supervisory Board recommend that shareholders should accept RAG's offer and tender their shares for sale.

Market position strengthened: Acquisition of the superabsorbents business of Dow Chemical, Midland, USA, including production facilities in Rheinmünster/Baden-Baden, Germany, and toll manufacturing agreement with Dow's Midland facility.

Dear Shareholders,

During the past year we have taken a number of key steps to pave the way for the future development of the Degussa Group:

- We have streamlined our organizational structure and now manage our activities with a stronger focus on their growth potential.
- The "Degussa 2008" strategy program has been rolled out Group-wide.
- We took an impairment write-down on the fine chemicals activities and are working hard to realign these activities.

These decisions are a logical continuation of our policy of profitable growth. We are convinced that they will give Degussa a successful future.

Another major step in our future alignment came in December 2005 when our majority shareholder, RAG Aktiengesellschaft, announced that it planned to acquire all remaining shares in Degussa. It therefore made a public offer for the free float in January 2006 and intends to acquire all shares in Degussa currently held by E.ON AG.

Now I would like to single out some of the key developments in 2005:

At the start of the year we projected that Degussa would report a slight improvement in sales and EBIT. We achieved that: sales grew by 9 percent and EBIT increased by 1 percent.

Following a further deterioration in business conditions in the fine chemicals sector, we took an impairment charge of €836 million on these activities in the fall. As a result, the Group made a net loss of €491 million. We will therefore be recommending to the Supervisory Board and Annual Shareholders' Meeting that there should be no dividend payment for 2005.

We have a clear strategy showing how we intend to develop the fine chemicals business through restructuring and capital expenditures. The impairment charge was important to prepare the ground for this.

Nearly five years after the formation of the present Degussa Group, we reviewed our management structures and business portfolio. The principal outcome of this "Strategy & Organization" project was a switch to a more systematic focus on growth potential in the management of our operations, accompanied by the introduction of far leaner management structures. This will speed up decision-making processes and improve our flexibility in the marketplace. As a global specialty chemicals company, our basic philosophy of decentralization remains a key success factor.

We have thus done all the groundwork for the successful implementation of the "Degussa 2008" performance enhancement program, which is designed to raise EBIT by €300 million within the next three years. That is vital to ensure we achieve our ambitious profitability and growth targets. After all, sustained profitable growth is Degussa's central goal.

We optimized our portfolio further in 2005. That included signing an agreement to divest the Food Ingredients activities. At the same time, we stepped up our focus on promising future technologies and growth regions. For example, we acquired the remaining stake in the US company CYRO as a basis for further global expansion of our methacrylate specialties business. We also strengthened our position in high-performance polymers through JIDA Degussa High Performance Polymers, a new joint venture in China.

Research and development are fundamental for profitable growth at Degussa. Products and technologies developed in the past five years account for about 20 percent of sales. Our new Nanotronics and Bio Science-to-Business Centers bring together innovation and a strong customer orientation which should raise the pace of development from the initial idea to market success. Overall, we are investing €100 million in these projects at our Marl site. That represents a clear commitment to Germany as a center for research.

In all our efforts to make Degussa even more profitable, we make sure we do not lose sight of our social responsibility. We therefore remain firmly committed to vocational training: In 2005 Degussa took on 582 trainees, more than 50 percent above the sector average.

Management development is another area where we are proving successful. In a survey of career opportunities for managers at European companies published last September, we ranked among the top ten. That is evidence that we are well-placed in the competition to attract the best future managers.

Our international vacation exchange program for employees' children proved very popular. 175 young people were given an opportunity to spend up to three weeks at each others' homes, for example in Australia, Brazil, China, South Africa and the USA. Many companies have already expressed an interest in following our example and offering similar exchange programs.

To sum up: Degussa is built on firm foundations and has a stable and attractive portfolio of businesses that command above-average margins. Our financial structure is sound. In recent years we have made enormous progress and positioned the company for the future.

Professor Utz-Hellmuth Felcht

That has been achieved through the combined efforts of our employees, managers and representatives of the workforce. We would not be where we are today without the commitment and professionalism they have demonstrated, especially in the face of constant change. For that they earn my heartfelt thanks.

RAG's intention of taking over Degussa endorses our corporate strategy. We welcome the fact that it will continue to support us in the value-driven development of the Degussa Group in the future.

Yours,

Professor Utz-Hellmuth Felcht
Chairman of the Board of Management

Profile of Degussa

Degussa is a multinational company systematically aligned to profitable specialty chemicals. Its hallmarks are reliability, excellence, innovation and intelligent linking of knowledge. These qualities are expressed in its corporate slogan, “creating essentials”, which pinpoints its role as the originator of value-added products and systems solutions that play a crucial role in the success of its customers’ end-products. Degussa is a fast, flexible organization with flat management structures and does everything it can to make sure it is close to its markets and customers.

2006: A systematic focus on growth In the past few years, Degussa has established itself firmly as the leading specialty chemicals company by refocusing its portfolio, restructuring and strengthening its core businesses. To meet its ambitious financial targets, it has continuously adjusted its corporate strategy, its portfolio and organizational structures. In future, Degussa will be concentrating even more closely on sustained profitable growth and has streamlined its organizational structure accordingly. That gives it an even leaner and more customer-focused position on the world’s specialty chemicals markets. The new corporate strategy and organizational structure pave the way for the success of the “Degussa 2008” strategy program.

Extended management board In future, Degussa’s Board of Management will play a far stronger operational role. It has therefore been increased from four to six members with the appointment of two new members: Dr. Bernhard Hofmann, who headed the Fine & Industrial Chemicals Division until the end of 2005, and Dr. Manfred Spindler, who previously headed the Specialty Polymers Division.

Effective January 1, 2006 the five operational divisions were eliminated as a management level and the business units now report directly to the Board of Management. They are supported by service units which are run on commercial lines and therefore compete with external service providers. The Corporate Center in Düsseldorf, Germany, is responsible for strategic management of the Group. The new structure strengthens Degussa’s philosophy of decentralization, speeds up decision-making processes and increases flexibility in the market.

The number of business units has been reduced from twenty to seventeen. Similar activities have been combined so they can withstand global competition and make better use of growth opportunities.

Four reporting segments in future From 2006, Degussa’s external reporting will center on four reporting segments: Technology Specialties, Construction Chemicals, Consumer Solutions and Specialty Materials. Each segment bundles activities with similar business models and strategic success factors. However, unlike the former divisions, they are not organizational entities with their own structures.

The Technology Specialties reporting segment comprises the business units whose products are based on specialist technologies successfully developed by Degussa over decades. These include synthetic building blocks for the pharmaceuticals industry and catalysts for the production of biodiesel. Moreover, through its expertise in the physical chemistry of particle technology Degussa has achieved a leading position in rubber reinforcement and polishing processes for optical data media.

The Construction Chemicals reporting segment comprises chemical systems and formulations for customers in the construction

Pooling the activities into 17 business units

Old divisions	Old business units	Pooling/ reallocated	Business units from Jan. 1, 2006	Reporting segments from Jan. 1, 2006
Construction Chemicals	Admixture Systems Europe		Admixture Systems Europe	Construction Chemicals
	Admixture Systems North America		Admixture Systems North America	
	Admixture Systems Asia/Pacific		Admixture Systems Asia/Pacific	
	Construction Systems Europe		Construction Systems Europe	
	Construction Systems Americas		Construction Systems Americas	
Fine & Industrial Chemicals	Building Blocks	Active Oxygen	Building Blocks	Technology Specialties
	Exclusive Synthesis & Catalysts		Exclusive Synthesis & Catalysts	
	Peroxygen Chemicals	Initiators	Aerosil & Silanes	
	C_4-Chemistry	Hydrogen Cyanide	Advanced Fillers & Pigments	
	Feed Additives		C_4-Chemistry	
Performance Materials	Superabsorber		Feed Additives	Consumer Solutions
	Care Specialties	Pooling	Superabsorber	
	Oligomers & Silicones		Care & Surface Specialties	
Coatings & Advanced Fillers	Coatings & Colorants	Coating & Ink Additives	Coatings & Colorants	Specialty Materials
	Aerosil & Silanes			
	Advanced Fillers & Pigments			
Specialty Polymers	High Performance Polymers			
	Specialty Acrylics	Films & Foams	High Performance Polymers	
	Methacrylates		Specialty Acrylics	
	Advanced Polymer Shapes	Pooling	Methacrylates	

☐ Pooling applies. ☐ Pooling does not apply.

As of January 1, 2006.

industry. As the global market leader, Degussa can build on its strong distribution network and enormous expertise in applications development.

The Consumer Solutions reporting segment groups together those businesses in which Degussa is a global supplier of customized ingredients for the manufacture of consumer products and materials. Through development alliances, Degussa works closely with leading producers of end-products.

The Specialty Materials reporting segment comprises high-performance materials which rank among the market leaders as a result of Degussa's superior materials, processing and applications expertise. Many of the products are manufactured from methylmethacrylate (MMA) in a closely integrated production network which generates competitive advantages, enabling these units to systematically tap into the market for specialty applications such as pharmaceutical polymers and optical electronics.

Board of Management

Dr. Thomas Schoeneberg
Studied law and politics in Berlin and Hamburg, obtaining his doctorate in 1974. Became a substitute member of the Board of Management of PreussenElektra AG in 1986 and a full member in 1988. Member of the Board of Management of Degussa-Hüls AG from 2000 and Degussa AG since 2001. Labor Director. Other responsibilities include personnel and social policy, environment, health, safety and quality, legal affairs and insurance.

Dr. Alfred Oberholz
Studied chemistry at RWTH Aachen, obtaining his doctorate in 1980. Appointed substitute member of the Board of Management of Hüls AG in 1996 and a full member in 1998. Member of the Board of Management of Degussa-Hüls AG from 1999 and of Degussa AG since 2001. Responsibilities include innovation and technology management, mergers & acquisitions and IT strategy.

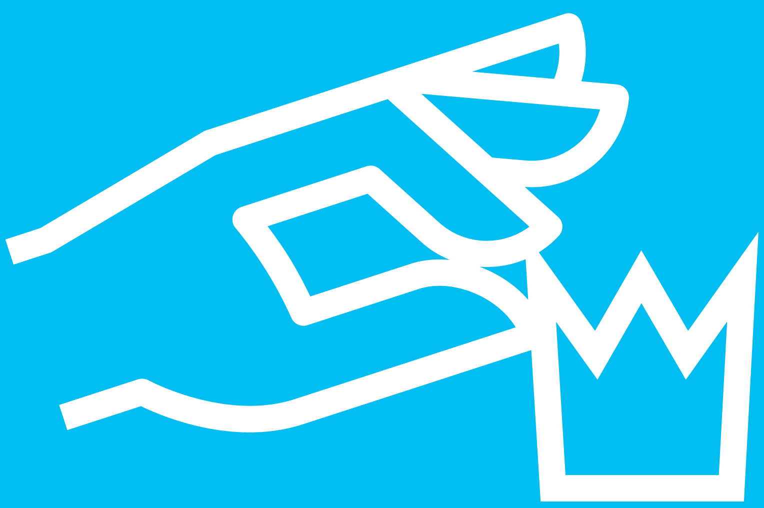
Dr. Bernhard Hofmann
Studied chemistry in Giessen, obtaining his doctorate in 1979. Worked for Hoechst AG from 1979 to 1998, became Managing Director and CEO of Vinnolit GmbH & Co. KG in 1998 and a division head at Degussa AG in 2001. Member of the Board of Management of Degussa AG since 2006. Responsibilities include the operating business of the Technology Specialties and Construction Chemicals reporting segments.

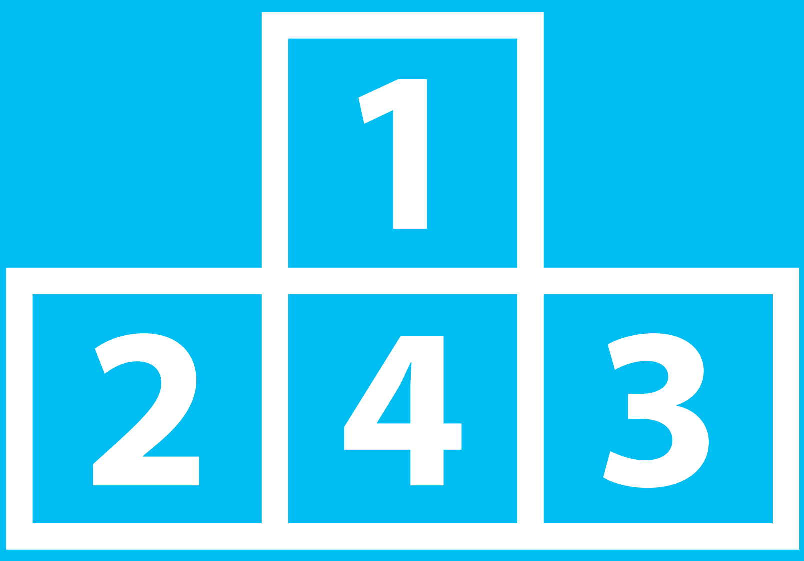
Dr. Manfred Spindler
Studied chemistry in Bonn, obtaining his doctorate in 1977 and has worked for Degussa since then. Member of the Board of Management of the former Degussa AG from 1997, Member of the Board of Management of Degussa-Hüls AG from 1999, division head since 2001 and member of the Board of Management of the present Degussa AG since 2006. Responsibilities include the operating business of the Consumer Solutions and Specialty Materials reporting segments.

Heinz-Joachim Wagner
Graduated in business administration from Frankfurt university in 1974 and has worked for Degussa since then. Appointed to the Board of Management of the former Degussa AG in 1996. Member of the Board of Management of Degussa-Hüls AG from 1999 and of the present Degussa AG since 2001. Responsibilities include finance, controlling, accounting and taxes.

Professor Utz-Hellmuth Felcht
Studied chemistry in Mainz and Saarbrücken, obtaining his doctorate in 1976. Member of the Board of Management of Hoechst AG from 1991, Chairman of the Board of Management of SKW Trostberg AG from 1998 and of Degussa-Hüls AG from 2000. Chairman of the Board of Management of Degussa AG since 2001. Responsibilities include strategy, communication and managerial staff. Member of the Board of Management of RAG AG since June 1, 2003.

Degussa 2008





Degussa Phase Two

The "Degussa 2008" strategy program introduced at the start of 2005 symbolizes an end and a new beginning. It marks the end of Phase One in the shaping of the new Degussa Group and the start of Phase Two in the ongoing development of the company. The aim is to achieve sustained profitable growth.

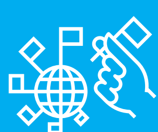
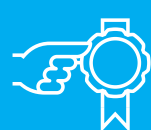
Just four years after its formation, the new Degussa Group had successfully completed its start-up phase. A good deal had been achieved in this relatively short period, including an ambitious divestment program to streamline the company's portfolio and focus its activities on specialty chemicals. Degussa is now positioned as a competitive company aligned to the market. It is the leading specialty chemicals company and ranks first, second or third on the global market in 85 percent of the fields in which it operates.

Raising performance and earning power By the start of 2005 the time had come to open a new chapter in the company's comparatively short history. Dedicated to ongoing development, its twin goals are to ensure sustained profitable growth and raise profitability. To achieve this, the "Degussa 2008" strategy program was introduced to complement other restructuring projects. Having established a completely new company within four years, the aim is to complete the next phase of development in a second four-year period, in other words, by 2008

However, "Degussa 2008" does not mean reinventing the company. It builds on established projects and initiatives. New focuses have been set to strengthen the company's performance and raise profitability substantially.

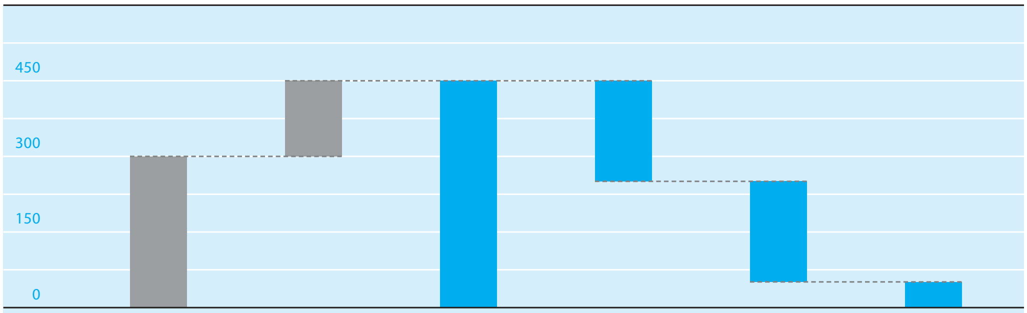
Phase Two is underpinned by quantitative targets. The aim is to raise EBIT by €300 million by 2008. To ensure that this target is achieved, the goals for individual projects come to €450 million. The additional

Sub-projects of Degussa 2008

▶ Solutions to Customers	▶ Make China Happen ▶ Explore Eastern Europe	▶ Site Excellence	▶ Human Excellence
			

€150 million is a sort of safety margin. After all, experience shows that not all ideas and initiatives can be achieved in full. Besides, market competition means that some cost savings have to be passed on to customers.

Projects aim to raise EBIT by €450 million to make sure the target of €300 million is achieved



	Target improvement in EBIT	Safety margin	Total EBIT impact	Solutions to Customers	Site Excellence	Optimization of support functions
in € million	300	150	450	200	200	50

A program based on four elements The four elements of the program are closely linked to Degussa's strategic goals and backed up by quantitative targets.

Solutions to Customers centers on securing Degussa's market leadership by installing best-in-class marketing, sales and innovation processes. The aim is to raise EBIT by €200 million.

Make China Happen/Explore Eastern Europe is geared to making even more systematic use of the opportunities in new growth markets. The goal is to identify additional growth projects for every business unit and create the necessary structures to support them. Degussa wants to increase sales substantially in both regions and leverage additional earnings potential for the period after 2008.

Site Excellence aims to ensure top-class production to maintain the company's competitive edge. That involves improving the performance of all sites and optimizing the site network. The target is to raise productivity 1.5 percentage points faster than competitors every year and increase earnings by €200 million. At the same time, savings of €50 million are targeted for the procurement of technical goods and services.

Human Excellence is designed to ensure that Degussa employs skilled and motivated staff at all levels and to position it as one of the world's most attractive employers. An integrated performance management system helps managers set clear targets and expectations, analyze potential and identify further training requirements. It also enables them to take transparent decisions and assess their implications.

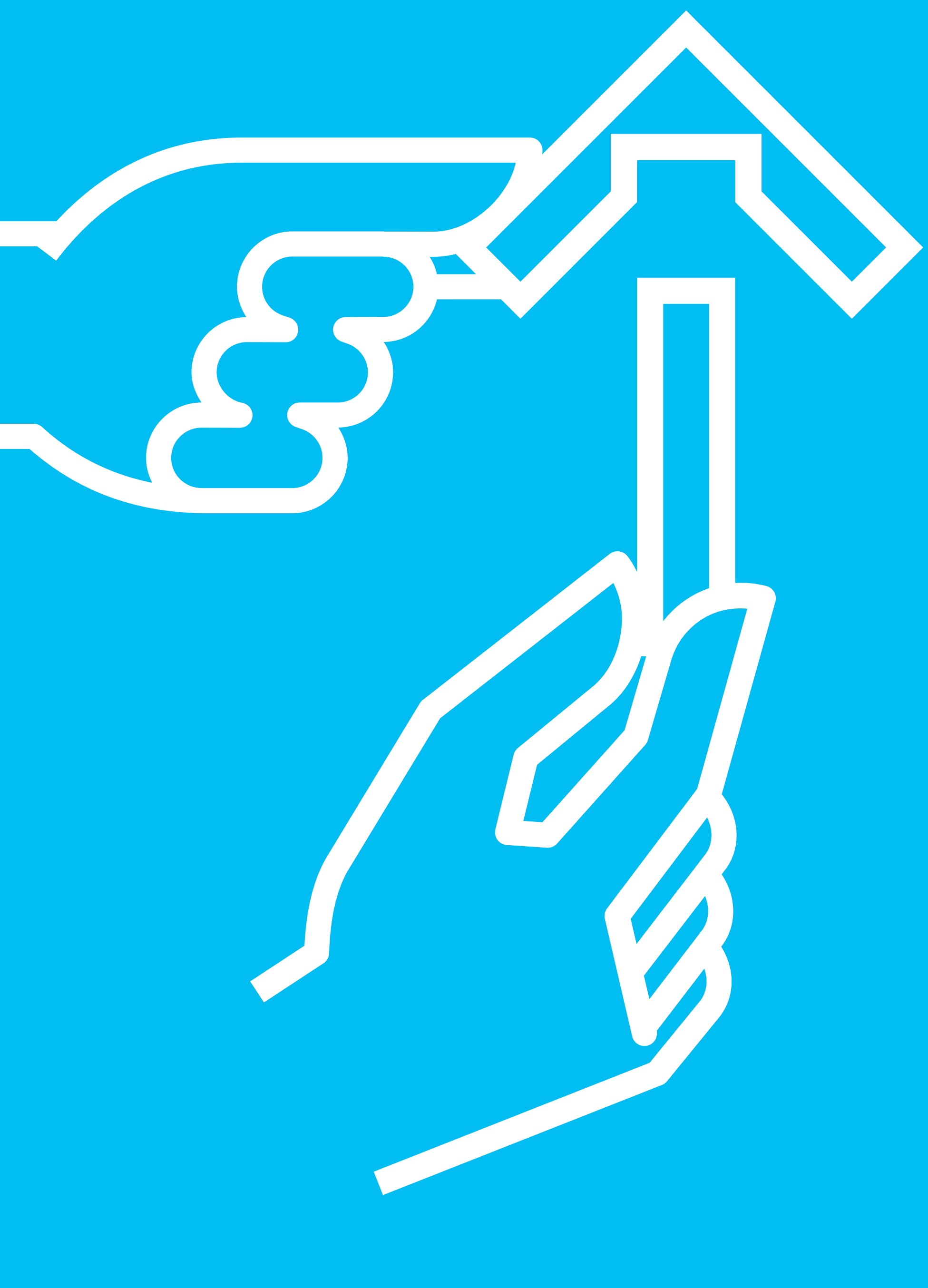
Another goal of Human Excellence is to optimize support functions at the Corporate Sector and service units. This should leverage savings of €50 million to help Degussa achieve its EBIT target.

Central coordination and transparency Since Degussa 2008 is such a wide-ranging program, central coordination and maximum transparency play a vital role in meeting the targets. They ensure the processes slot together, sub-projects benefit from one another and employees are actively involved. A "Program Office" has therefore been set up to track the progress of the program as a whole across the various units. The "IMPACT" controlling tool is used to coordinate the processes: Information on every step is entered in "IMPACT", with details of milestones and responsibilities. This facilitates tracking of the process and its outcomes so those responsible can take timely action to steer it in the right direction where necessary.

All projects within the Degussa 2008 program are divided into three phases: the initial phase, project phase and implementation phase. In the initial phase, which ran until May 2005, project teams defined the scope, procedure and timeline for the various projects. At the same time, initial analyses were performed and specific targets were set. The project phase started in June 2005 and is expected to run until mid-2006. The main aim is to develop tools and strategies and adapt them to the four central elements of the program. They will then be put into practice in the implementation phase.

This performance enhancement program is known as "Degussa 2008" because the objective is to achieve the targets set by 2008. However, the ongoing development of the company will not be completed then. Degussa will continue its strategy of profitable growth as a dynamic, ongoing process. Specific projects and focuses are outlined in more detail on the following pages.

Solutions to Customers



Service customer's needs

Degussa launches a new product. Customers are queuing up to buy it. After all, they have waited long enough for it to come onto the market! That is the dream of every salesperson.

However, reality is quite different: Customers no longer buy a single product or service. They buy a function, which essentially means they buy a solution to a specific problem. The principle can best be illustrated by a simple example: If holes were on sale, no-one would need to buy a drill!

"Everyone is talking about solutions, but hardly anyone talks about how to find them," says Dr. Claus Rettig, who is in charge of the Solutions to Customers project. "However, these days solutions are the key to acquiring customers. To make sure Degussa meets its profitability targets, the Solutions to Customers team has been looking at precisely how we can find solutions for our customers." The project team has defined three key processes where Degussa can improve: marketing, sales and innovation (MSI). Specialists have identified room for improvement in almost all areas. Although all business units have marketing, sales and innovation processes, they vary significantly. That needs to change. Uniform standards are now being defined for the entire company. Moreover, an individual timetable has been agreed with every business unit, showing how it can exploit its potential. The project team is also building up a database of best practices drawn from within the Degussa Group and encouraging the business units to share their knowledge with each other.

The Feed Additives Business Unit makes extremely high demands on marketing, sales and innovation. "We are one of the world's largest producers of amino acids for animal feeds," explains Dr. Mark Redshaw, who is responsible for implementing the "Account Management" project as part of the Solutions to Customers initiative in his business unit. "We have first-class products manufactured using state-of-the-art technology. But that is not enough to retain customers and gain new business." The business unit was therefore one of the first to supplement its broad product range by offering customers services to back up their development processes. AMINOLab® is part of that offer. Every day this unique analytical laboratory run by the Feed Additives Business Unit analyzes the amino acid content of raw materials and feed formulations from all over the world. As a

Targets for 2008

- Step up the development of innovative products and services
- Improve identification and understanding of market requirements and customers' needs
- Improve selling and product positioning skills
- Contribute €200 million to improving EBIT

Action

- Introduce mandatory standards for best-in-class marketing, sales and innovation (MSI) processes in every business unit
- The business units must translate their timelines into specific tasks for employees in order to exploit market potential to the full
- MSI Academy to secure the sustainability of best-in-class processes

Achieved in 2005

- MSI Academy established; concept and program for 2006 approved by the Board of Management
- Business units have defined details of all projects to raise earnings and paved the way to track their progress

result it now has the world's largest analytical database, which can be used to help customers enhance their feed formulations. That reduces raw material requirements and cuts costs. It also ensures that the animals metabolize their food better.

Proximity to customers is still essential to develop custom-tailored solutions. To ensure a strong local presence, Feed Additives has therefore established four regional platforms: Europe/Middle East/Africa, Latin America, North America, Asia/Pacific. Excellent customer management can also help secure competitive advantages. For example, through their close links to a major customer, the business unit's sales and marketing specialists heard that the company was planning a complete change in its production process. "The customer saw us as a strategic partner, not simply a supplier, so we were involved in the plans for the new facility from an early stage," explains Mark Redshaw. By working together they were able to optimize the entire supply chain from the production facility to the customer's manufacturing process. That included optimizing both the supply form of Degussa's products and ordering and call-off procedures. Both sides therefore benefited from the project.

Tripartite talks Degussa's subsidiary RohMax is the established market leader in additives for multi-grade hydraulic fluids, which assure the performance of hydraulic systems in bulldozers, wheel loaders and creeper tractors at all temperatures, reduce wear and tear and minimize energy consumption. "We are the market leader and have been operating in this sector for more than 50 years," says Doug Placek, product manager for hydraulic products at RohMax. "Currently, only about 15 percent of hydraulic fluids are formulated for use in low-temperature environments where our additives are needed. We are working hard to increase that percentage by demonstrating that our additives improve the performance of hydraulic fluids at high operating temperatures as well."

Machine owners simply follow the manufacturer's instructions, which were written back in the days when it was not known that hydraulic fluid selection could reduce energy costs. Moreover, back then environmental impact was not an issue for either manufacturers or users. Soaring fuel prices and the debate about CO_2 emissions from construction vehicles prompted RohMax to team up with oil producers to show OEMs how the problem could be solved: by using high-performance multi-grade fluids that cut the CO_2 emissions from off-road vehicles and save fuel. Since the response from customers was positive, Degussa's subsidiary has pressed ahead with development work. It is already becoming clear that the new maximum efficiency hydraulic fluid (MEHF) can cut fuel consumption and reduce emissions in the double-digit percentage range. RohMax is currently working with major global OEMs to obtain formal approval for this new development. Another genuine example of solving customers' problems.

Doug Placek raises awareness of the benefits of Degussa's hydraulic fluid additives.

Degussa MSI Academy As these examples show, future-oriented innovations are normally the product of a combination of factors—from technical and applications expertise to an in-depth knowledge of customers and markets.

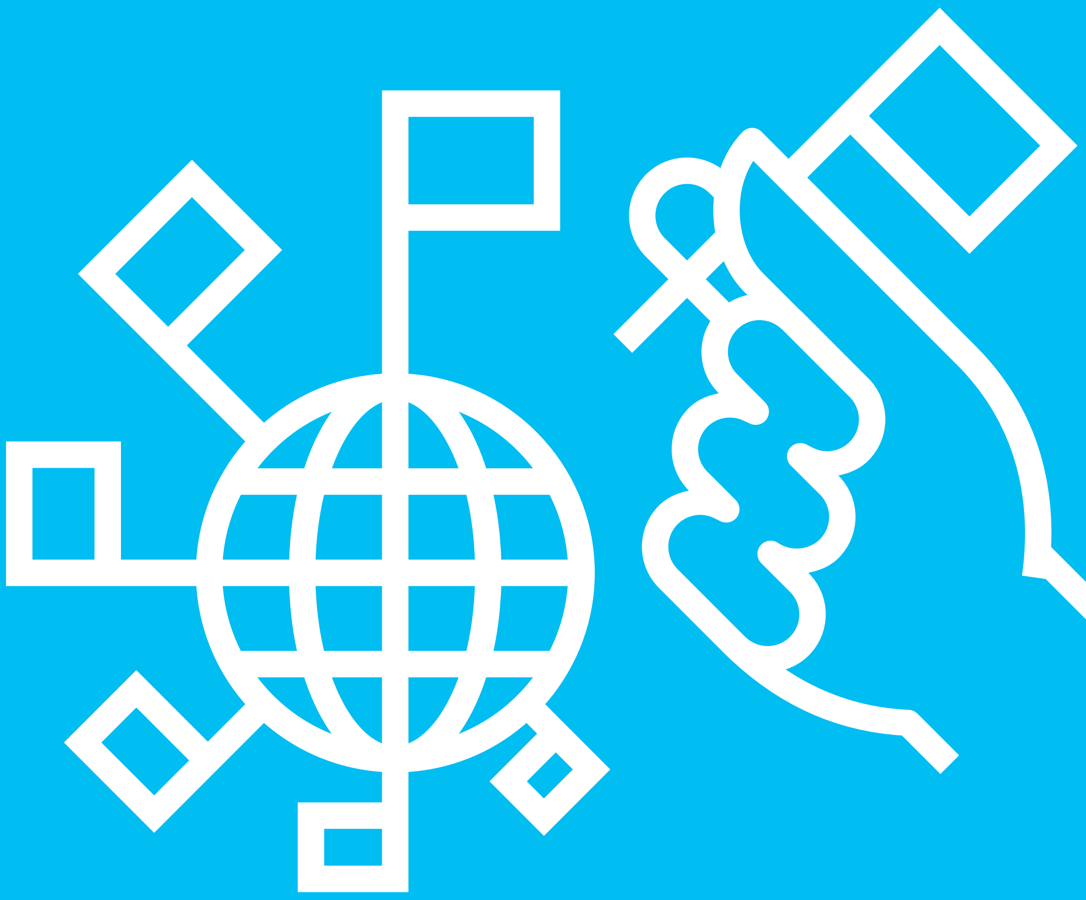
In January 2006 Degussa established an in-house training institute for marketing, sales and innovation—the MSI Academy—to support specific projects. This is a virtual organization so it has no premises of its own and no full-time instructors. Projects may be Group-wide or geared specifically to the needs of a single business unit. The basic philosophy is to provide practical experience for practical use.

The MSI Academy is therefore run by the business units, which nominate particularly experienced staff as instructors. The topics for 2006 have been set in conjunction with the business units. The Academy will start by offering five modules: Market and Customer Knowledge, Customer Planning and Customer Management, Pricing, Innovation Management, and Employee Development and Advancement. To ensure that they have a practical bias, the modules comprise a mixture of workshops, on-the-job training and coaching.

The MSI Academy thus enables the business units to develop competencies tailored specifically to their needs and ensure that they are applied systematically. It sees itself as Degussa's platform for excellence in marketing, sales and innovation and thus makes a special contribution to raising standards within the business units.

The concept was piloted by RohMax and the Feed Additives Business Unit. In view of its resounding success, all business units have expressed an interest in helping to shape the modules and utilizing the Academy for their own projects.

Make China Happen / Explore Eastern Europe



Looking East

China has become a major focus of world interest: It has over 1.3 billion inhabitants, its economy grew by nearly ten percent in 2005 and it is the world's fourth largest economy, ranking behind the USA, Japan and Germany.

Make China Happen China is already the largest market for some products such as cell phones and Chinese companies are forcing their way onto the global market in areas such as electronics. By 2010 China will be the world's most important market for chemical products. Forecasts anticipate that in ten years time about seven hundred million Chinese citizens will have annual incomes of over US$ 10,000, enabling them to enjoy a consumer-oriented—i.e. western—lifestyle. China is thus poised to become an even bigger market than Europe and North America together. Since specialty chemicals are used in many products that improve the quality of life, China's more affluent citizens will be indirect customers for many Degussa products.

Targets for 2008

- Triple sales in China to €900 million
- Generate 5 percent of Group sales in Eastern Europe

Action

- Intensive recruitment and training of staff in China
- Establish strategic alliances with companies in China
- Step up collaboration with Chinese universities
- Expand knowledge of the Eastern European market
- Increase use of raw material sources and production opportunities in Eastern Europe
- Increase the focus on Russia

Achieved in 2005

- Eight new companies established in China
- First global chemical company operating in China to obtain import and distribution permits
- Cooperation with Jilin University in Shanghai on the development and production of high-temperature polymers
- Degussa positioned clearly in Eastern Europe
- Eastern Europe firmly established in the awareness of marketing managers

That explains Degussa's ambitious growth targets for China up to 2008. Regional President Eric Baden explains: "We aim to roughly triple sales from around €320 million at present to €900 million. Investment of around €100 million a year is planned as part of the "Make China Happen" project, which comprises thirty-five initiatives, including takeovers and joint ventures. About half a dozen of these were completed in 2005.

Well-trained staff are essential to put these plans into effect. Recruiting, training and retaining suitable employees are therefore key tasks in China, especially as the Chinese tend to change jobs fast and frequently. What is more, vocational training is normally extremely theoretical. That is where the Degussa Training Center comes in: In fall 2005 Degussa set up its own training facility for thirty-six students in cooperation with the state-run Shanghai Petrochemical Academy.

"Our class trains production workers. This type of training is not very common in China," explains class tutor Song Rong. At the end of the two-year course, the trainees will have reached the same standard as their counterparts in Germany. "Instruction has a strong practical bias. The training facility is reserved for our exclusive use and enables trainees to build on what they learn," explains Song Rong. Her job includes training the teachers, who need an introduction to what are for them very unusual teaching methods.

Li Min is learning practical skills at Degussa's new training center in Shanghai.

Degussa expects the training center to pay off by reducing the familiarization period needed for new employees and thus raising efficiency. "Above all, we are securing the staff our business units need for growth," explains Matthias Speth, vice president human resources at Degussa China. Degussa has the privilege of being able to offer trainees a job at the end of their training course. That gives it an advantage over other chemical companies in China when it comes to recruiting good staff. Degussa's ambitious plans also influence the trainees' choice of employer, as 19-year-old Li Min explains: "I think it is important to get a job at a company like Degussa with an international reputation and a strong presence in China." If the training center is successful, this type of practical training will be extended to administrative courses.

Explore Eastern Europe News and information on China already play a dominant role in the media. However, another enormous market is emerging far less quietly but no less dynamically in Eastern Europe. This development was triggered by the collapse of the Soviet Union in 1991, accelerating the western focus of the former COMECON states. The political and economic opening of these countries is demonstrated by the fact that a total of eight Eastern European states joined the EU in 2004 and by the anticipated accession of Romania and Bulgaria in 2007/2008.

Degussa already has more than twenty subsidiaries in these countries. Last year it doubled production at a carbon black facility in Poland. In response to the steadily rising demand from tire manufacturers in Eastern Europe, there are plans to raise capacity further in the next few years. In 2004 a facility to manufacture PLEXIGLAS® sheeting came into operation in Russia, Degussa acquired a producer of essential amino acids in Hungary and capacity for L-threonine in the Slovak Republic was expanded. And yet, the company intends to step up its presence in Eastern Europe still further. The aim of the Explore Eastern Europe project is to make sure this happens quickly and efficiently. It is a step that pleases Dr. Roman Odvarko, who has worked for the Degussa Group in Eastern Europe for more than fifteen years and was appointed as the Group's regional president three years ago.

Dr. Odvarko, Degussa has twenty subsidiaries in Eastern Europe and the region generated sales of €414 million in 2005. Surely the Group's presence in Eastern Europe is already sufficient? *Not at all! Eastern Europe is right on our doorstep. That means we can generate good results rapidly with relatively few resources. In 2005 our region reported sales of over €400 million. So far we have been successful because a few foresighted managers within the company believed in the region. Building on this initial phase, we now plan to pool and coordinate the interests of Degussa's business units as coherently as possible to increase our market muscle.*

Degussa followed its customers to Eastern Europe very early on and has now established a good position at over twenty sites. However, we still see plenty of scope for development in this region and Degussa should be able to participate in this even more strongly than in the past.

What exactly do you understand by Explore Eastern Europe? *The aim is to generate at least 5 percent of Group sales in this region by 2008. To do that we need access to all relevant information on our business and have to process it correctly. We are therefore setting up cross-border market intelligence units.*

To enable us to operate more effectively and flexibly, we will also be adapting our structures in Eastern Europe to respond to the new challenges. In our view, it is particularly important to ensure that the business units collaborate with each other and share their knowledge. We are also working on new alliances, for example in research, procurement and production. Degussa is not yet well-known in Eastern Europe as the world's leading producer of specialty chemicals and an attractive employer. To change that we are working on our public image. That is another key success factor.

Roman Odvarko sees enormous growth potential in Eastern Europe.

What is your outlook for economic development in Eastern Europe? *According to current market data, Eastern Europe should report above-average growth in the next few years. In fact, with domestic demand picking up, we expect growth to be slightly higher than in 2005. In Poland, the Czech Republic and Russia, which are particularly important markets for us, annual GDP growth forecasts are between 4 percent and 6 percent. GDP growth rates in the new EU accession states Romania and Bulgaria are also attractive at over 6 percent, although the reference base is relatively low.*

What are the next steps? *Now that Degussa's Board of Management has approved the project team's concept, we will be setting up an Eastern Europe Council as a forum for use by all business units. We will be selecting and training employees for the market intelligence units as quickly as possible. The Coatings Council Eastern Europe, which has been set up by six business units to gain access to the market, will be starting work on schedule. And then there are a whole range of other initiatives developed by the business units and the Explore Eastern Europe team. These will be implemented step by step to achieve our ambitious targets. It is up to us to make sure we utilize the opportunities in Eastern Europe!*

Site Excellence

An all-round view

The Site Excellence program has clear objectives. It aims to raise the productivity of Degussa's nearly 220 sites worldwide and improve earnings by €200 million a year. To achieve these ambitious goals, about a hundred people are working on Site Excellence projects, around forty of them full-time.

The team members have developed an extensive concept comprising a whole package of measures to raise earnings. They are conducting site diagnoses, building a Site Excellence Academy, reviewing the structures of multi-user sites and discussing the criteria for tomorrow's production networks.

During 2005 the team's activities were mainly visible through the site diagnoses. These involve external experts examining processes at individual sites and developing new ideas on how to structure them more efficiently in consultation with the management. The first site to be examined in this way was the facility operated by Degussa's subsidiary Para-Chemie in Gramatneusiedl, Austria.

48-hour site diagnosis

The outsiders' view: identifying potential The 48-hour site diagnosis was developed by the Site Excellent Expert Team in spring 2005. It takes its name from the fact that Degussa's specialists spend two days analyzing each site locally. This special form of diagnosis was piloted at the sites in Essen, Germany, and Slovenská L'upča, Slovak Republic. It was first used seriously at Gramatneusiedl, Austria. This site, which belongs to the Advanced Polymer Shapes Business Unit, is located just a few kilometers south of Vienna and has around 220 employees, making it one of the biggest employers in the region. It manufactures specialties such as PLEXIGLAS SOUNDSTOP® sheets for transparent noise barriers and PARAPAN® for high-quality furniture fronts.

"There was an awareness that cost structures and workflows needed to be altered," remembers Reiner Meiners, site diagnosis team leader in Gramatneusiedl. "However, change is almost always painful so we were not exactly welcomed with open arms." Dr. Hans-Jürgen Kress, project manager for the entire Site Excellence project, understands the skepticism: "That is precisely why we do not go out to sites armed with ready-made concepts that have to be implemented come what may. We arrive with a team of experienced specialists and discuss production processes and workflows with the site

Targets for 2008

- Increase earnings by €200 million by 2008
- Annual productivity growth 1.5 percentage points ahead of our competitors
- Position all sites optimally to secure their long-term competitiveness

Action

- Optimize all sites
- Develop site networks for the future
- Improve procurement
- Develop structures and management models for multi-user sites

Achieved in 2005

- Individual plans agreed with all business units and site services
- Establishment of intranet sites with best practice examples
- Site diagnoses at 21 sites, leading to agreed improvements totaling €40 million
- Initial projects have started on the basis of the recommendations derived from the site diagnoses


Hans-Jürgen Kress and Reiner Meiners build on constructive dialogue with managers.

management. That enables us to identify potential, come up with recommendations and offer our assistance in implementing them. It is up to the site to decide what—if anything—is actually changed."

Although the tool is called a 48-hour diagnosis, a good deal of preparatory work has to be done beforehand. The first step is for the experts to get an overview of local conditions. The team therefore met with the head of the business unit and the site manager in July 2005 to define the exact content and procedure for the on-site diagnosis. After this preliminary discussion, the team had just four weeks to analyze all relevant data on the site and draw up a schedule for interviewing managers there. An extensive checklist is used to identify and analyze potential. However, it is not used in the same form every time. "Every unit is different," explains Meiners, "and we would not do justice to the individual sites if we were to consider them all identically. The strength of our diagnosis is that it combines the experience of team members in production optimization and business process modeling."

One of the basic principles—possibly the most important one in the experts' view—is that the site management must be prepared to engage in constructive dialogue. "No-one in Gramatneusiedl blocked us out," recalls Meiners. "We quickly entered into open and constructive talks with the managers."

On-site diagnosis means working almost around the clock. Following the interviews with the site managers, the team members went back to their hotel, discussed the findings of the first day until nearly midnight and then documented them. The presentation of the results started the following day and ended with another overnight evaluation. The experts were therefore able to present a provisional report immediately after the two-day diagnosis. Evaluating, documenting and discussing the potential identified is one of the key success factors of this tool. In Gramatneusiedl the focus was on total costs of €17 million and the impressive result was savings potential of €3.1 million.

The insiders' view: creating value "Everyone here was skeptical to some extent," says Gerald Molnar, site manager at Gramatneusiedl. In principle, the entire management was positive about the upcoming diagnosis, but evidently people had mixed feelings. In fact, the management had been trying for some time to raise productivity so some managers were at a loss to see what else could be done.

"That skepticism has given way to a basic openness to input from the Group," reports Dr. Klaus Dorn, managing director of Para-Chemie. Degussa's site diagnosis specialists were particularly effective at building confidence. Dorn talks about very constructive discussions. The diagnosis showed that the site was on the right track. Work had already started on about half of the projects where savings potential was identified. The remainder were a direct result of the diagnosis. "In some areas, we could not see the wood for the trees," admits Robert Grimus, who heads the waterbath plant. "The diagnosis showed us the real situation. We found the suggestions from outside extremely helpful." Site Excellence has injected new impetus into the site's efforts to improve performance.

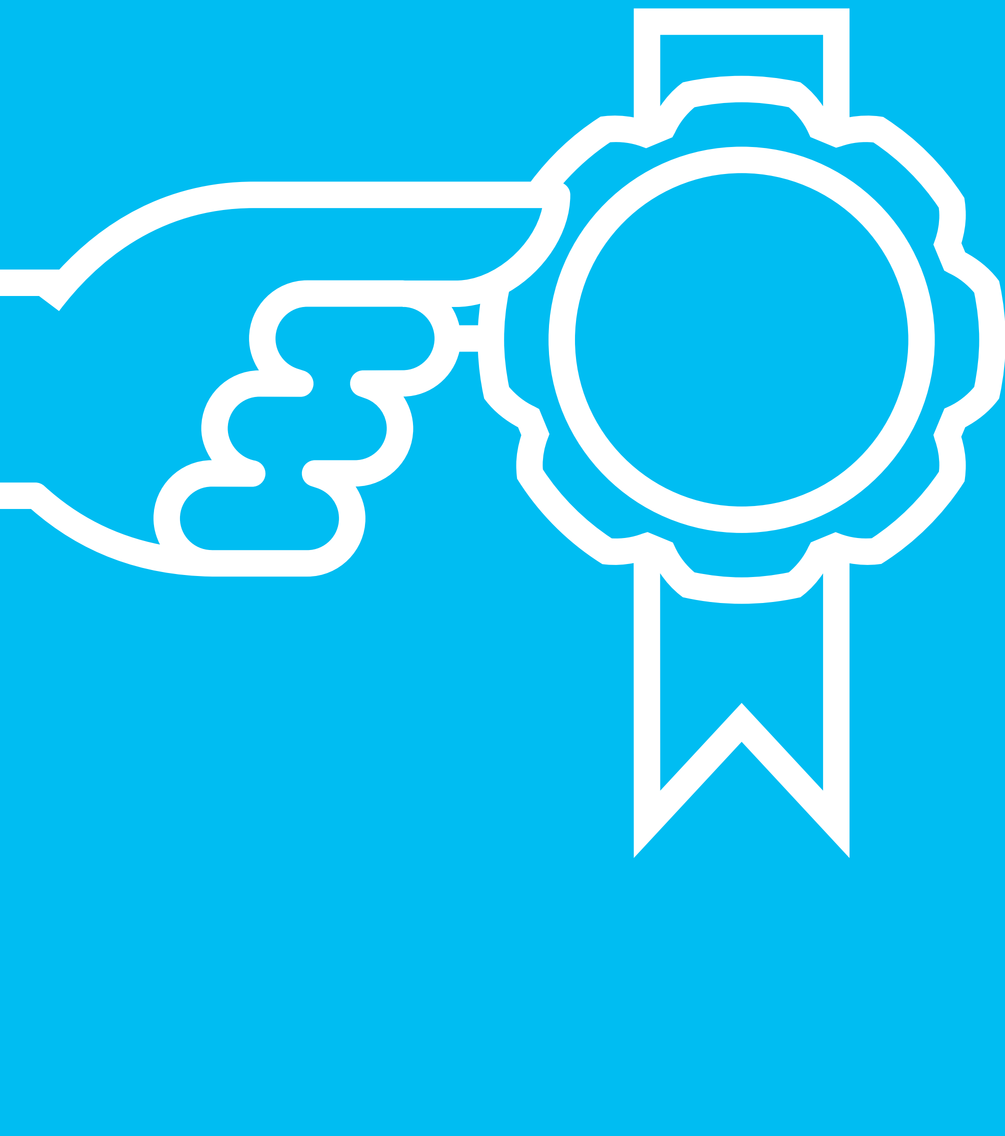
That "impetus" is worth around €3 million. The bulk of the savings will come from the technical department, with scope to reduce costs by €1 million identified in maintenance alone. For example, an accurate analysis of operating faults should help identify weaknesses more quickly and prevent stoppages. More effective work planning, coupled with better trained staff, reduces overtime requirements. Moreover, in future overhauls will be scheduled to coincide with product changeovers on individual production lines. That means production will only be halted in parts of the facility, which is far less costly than the previous practice of shutting down all plants at once.

However, altering technical workflows is not the only source of savings as the managers at Gramatneusiedl are aware: In the face of tougher competition, downsizing may be the only way to ensure the survival of a facility. Necessary personnel adjustments are therefore announced openly. The aim is to reduce costs without cutting staff numbers wherever possible, for example through more intelligent production planning, better management of contractors and training staff so they can be deployed more flexibly. That should cut out some of the 3,300 hours overtime worked at the site every year. The management would like to reduce overtime to 1,600 hours, which would be equivalent to saving one full-time job—without having to dismiss anyone.

Gerald Molnar expects smarter production planning to cut costs at the Gramatneusiedl site.

The management also uses unconventional methods to improve cost awareness. A "virtual currency" consisting of pizzas, hamburgers and cars is used to show employees what their actions actually cost: "Sometimes employees have a very lax attitude to costs at work," explains one manager. Translating costs into everyday objects they can relate to greatly increases cost-awareness. For example, one liter of a raw material used in the production of transparent sheeting costs the same as a liter of gasoline, while a special clip used in the manufacturing process costs the equivalent of two hamburgers. Since introducing this system most employees have been far more careful with tools and have handled raw materials less wastefully. That is a simple but smart way to cut costs.

Human Excellence



Looking Ahead

The objective of the Human Excellence program is to ensure that all positions in the company are filled with motivated staff with the right qualifications and interpersonal skills. In short: it is about making sure the right employees are employed in the right jobs.

The integrated performance management system helps managers define targets and expectations clearly and analyze potential and further training requirements. It also enables them to take transparent decisions and assess their implications. The overriding aim is to make Degussa one of the world's most attractive employers.

Management by objectives, performance-oriented pay, bonus systems, development and advancement through continuous skills enhancement for all employees are human resources projects introduced at Degussa to improve the development of its staff. "Human Excellence is not just another project," comments project manager Professor Herbert Klenk. "The company already has all the tools required for excellent human resources work. All that is needed is to link them better and go on developing them—and, of course, ensure they are more widely used."

Human Excellence has a clearly defined timeline. The analysis of the present situation was completed at the end of 2005. A group of managers from the business and service units and the Corporate Center examined how to improve the performance of human resources management. The outcome will be set out in a series of performance enhancement measures beginning in February 2006. The implementation phase is scheduled to start in May 2006. As a first step, a performance management system is being developed and introduced for executives. It will then

Targets for 2008

- Introduce an integrated system for recruiting staff, analyzing potential, performance management, employee development and remuneration
- Systematically apply performance management tools for executives
- Anchor performance orientation and systematic leadership as part of Degussa's corporate culture
- Achieve savings for €50 million

Action

- Analyze, coordinate and improve tools and processes to raise performance
- Empower managers to utilize these tools more consistently
- Raise performance orientation and motivation by improving communication between employees and supervisors and stepping up feedback
- Cascade the performance management system down through the company

Achieved by end-2005

- Common understanding of performance as a result of success and achievement
- Extensive analysis of performance enhancement tools used at Degussa to identify the need for action


Peter Weber and …


… Georg Wall make sure Technical Services runs smoothly.

be adapted for other management levels and finally rolled out to all employees. Consistent performance management at all levels will pave the way for an improvement in Degussa's management culture and performance.

Discussing performance Management culture was the focus of a series of workshops organized for all supervisory staff at Degussa's site in Wesseling, Germany. The workshops gave about two hundred participants, including Peter Weber and Georg Wall, an opportunity to practice ways of improving employee appraisals.

Peter Weber's new job was anything but easy. A plant utilities electrician by trade, he spent four years studying at evening school to qualify as an electronics technician and in July 2005 he took the next step up the career ladder when he became a foreman at the Wesseling site. Suddenly, he found himself responsible for about thirty employees. That was a new and challenging task, especially as some of them were his former supervisors. His first real test came after only a few months in the job: At the start of 2006 he was expected to conduct appraisals with employees as a basis for their further development.

Fortunately, he was well-prepared for his new task. In addition to his specialist training, Degussa had given him the tools he needed for his new personnel management tasks. One was a workshop on "Communication and Feedback" at the Wesseling site. "That really helped," he says looking back, "because it was very practical."

Practical training included role play exercises that enabled the participants to try out various situations with the aid of two external facilitators. Each participant was expected to play the part of supervisor and employee alternately. "At first it was a bit odd, but after a sluggish start, we had some very lively discussions. It was fun provoking managers and trying to test their reactions."

Changing places: Peter Weber and Georg Wall enhanced their appraisal skills through role play.

About a dozen present and future managers and supervisors attended the workshop where the practical exercises enabled them to gain new insights and perspectives for use in appraisal interviews. Since the participants came from a variety of different areas—logistics, human resources, manufacturing and maintenance—the role play involved a range of experience and different backgrounds.

Georg Wall is a good example. He has worked at the site since 1996 and currently heads Technical Services, which includes the Central Workshops and management of contractors at the Wesseling site. He is in charge of seventy employees and is Peter Weber's direct supervisor. In fact, he had already appraised him many times. "As a supervisor, it is important to make my expectations clear to employees," commented Georg Wall after the workshop. "That was not something I was so clearly aware of in the past so maybe that was a problem." The workshop has helped him eliminate this shortcoming.

Through the different perspectives offered by role play he discovered how to help his employees direct their professional focus. He also learnt why conflicts cannot always be resolved by finding a consensus. "The facilitator interrupted the role play at times and said: Stop, you can only go this far and no further. Cooperative management stops here."

The process initiated by the "Communication and Feedback" workshop is continuing. "The workshop was not the end of the line for us. We have already arranged additional meetings to follow up on our case studies," says Wall. This sort of training is very useful as Peter Weber and Georg Wall demonstrate. Incidentally, Weber has now successfully completed his first round of appraisals.

Leading market positions

Product	Application	Global market position	Capacity in metric tons p.a.
1-butene	Co-monomer for polyolefins	1	200,000
Acrylic glass	Construction industry, illuminated signboards, aviation/aerospace applications	1	150,000
Amphoteric surfactants	Shampoos, shower gels	1	1)
Ceramides, phytosphingosines	Cosmetics	1	1)
Colorants (pigment dispersions)	Decorative and industrial colorants	1	1)
Construction products	Systems for construction, repair and renovation (e.g. concrete admixtures, construction and oilfield polymers, sports and industrial flooring, coatings, facades, paints, EIFS [exterior insulation and finish systems], building systems and expansion joints); underground construction	1	1)
Cyanuric chloride	Crop protection and industrial applications (e.g. optical brighteners)	1	115,000
DL-methionine	Animal nutrition	1	350,000
Fat chemistry, quaternary derivatives	Fabric softeners	1	1)
Fumed silicas and fumed metal oxides	Silicon rubber, paints and coatings, adhesives, sealants, plastics, pharmaceuticals, cosmetics, high-temperature insulation, electronics	1	350,000
Precipitated silicas	Reinforcement of rubber, consumer products	1	
Heterogeneous, homogeneous and bio-catalysts	Life sciences and fine chemicals	1	1)
Organosilanes, chlorosilanes	Rubber, silicon rubber, paints and coatings, adhesives, sealants, building protection materials, pharmaceuticals cosmetics, optical fibers	1	200,000
Persalts	Bleaching agents for laundry and automatic dishwasher detergents	1	1)
Persulfates	Polymerization initiation, electronics, cosmetics, disinfection	1	over 30,000
Polyamide 12	High-performance polymer applications (e.g. automotive industry, medicine, sport)	1	1)
Polyester resins	Can and coil coating	1	24,000

Product	Application	Global market position	Capacity in metric tons p.a.
Sodium cyanide	Extraction of gold	1	100,000
Thermoplastic and reactive methacrylate resins	Binders for paints and coatings	1	1)
Exclusive synthesis of fine chemicals	Pharmaceutical and agrochemical intermediates and active ingredients	1–2	1)
Fine chemical intermediates and active ingredients, e.g. alcoholates, malonic esters, amino acids, orthoesters, peptides, NCN chemistry	Technologies, starting products und services for agrochemicals, pharmaceuticals and non-life-science applications	1–2	*
Organically modified silicones	Additives for polyurethane foams, coatings and inks, cosmetics; radiation-cured separation coatings	1–2	80,000
Superabsorbents	Diapers, feminine hygiene products, incontinence products	1–2	300,000
Carbon blacks	Tires, rubber goods, pigments	2	1,400,000
Hydrogen peroxide	Bleaching of paper and textiles, oxidant for the chemical industry	2	550,000
Isononanol	Plasticizers	2	340,000
Matting agents	Additives for the coatings and printing inks industry	2	1)
Methylmethacrylate (MMA)	Dispersions, lacquers, additives, adhesives, optical lenses	2	480,000
Oil additives	Viscosity index improvers	2	1)
Pharmaceutical polymers	Coatings for drugs	2	1)
Polymethylmethacrylate (PMMA)	Engineering polymers for the automotive industry and the electrical/electronics industry, special medical technology applications	2	180,000
Polyurethane crosslinkers	UV-stable polyurethane coatings	2	1)
Threonine	Animal nutrition	2	30,000
Peroxide-based initiators	Polymers (e.g. polypropylene and polyethylene)	2–3	1)
Professional skin protection	Skin protection products to prevent occupational skin diseases	2–3	1)

1) No data available.
December 31, 2005

Degussa stock

DAX gained more than 27 percent in 2005—Degussa shares rose to the highest level since 2001 2005 was a good year on the stock market, with the whole of Europe and not just Germany basking in a rosy glow. It was also an exciting year dominated by elections in Germany, a rising number of initial public offerings and the European Central Bank's first interest-rate rise in five years.

In Germany, the DAX index advanced more than 27 percent, ending the year at its highest level since early 2002, while the mid-caps represented on the M-DAX index posted an average gain of more than a third. German stocks thus moved ahead for the third consecutive year. Although the EuroStoxx 50 and most other share indices in the euro zone were unable to top the DAX performance, they gained an average of 20 percent over the year. Even the terrorist attacks in London, record oil prices, hurricanes Katrina and Rita and the squabbling about a European Constitution were unable to halt the clear upward trend.

The German market traded uneventfully in the first few months of the year with the DAX remaining within a relatively narrow band of 4,200 to 4,400 points until the end of May. Events on the political stage then roused it from its lethargy: the announcement of an early general election in Germany sent share prices soaring.

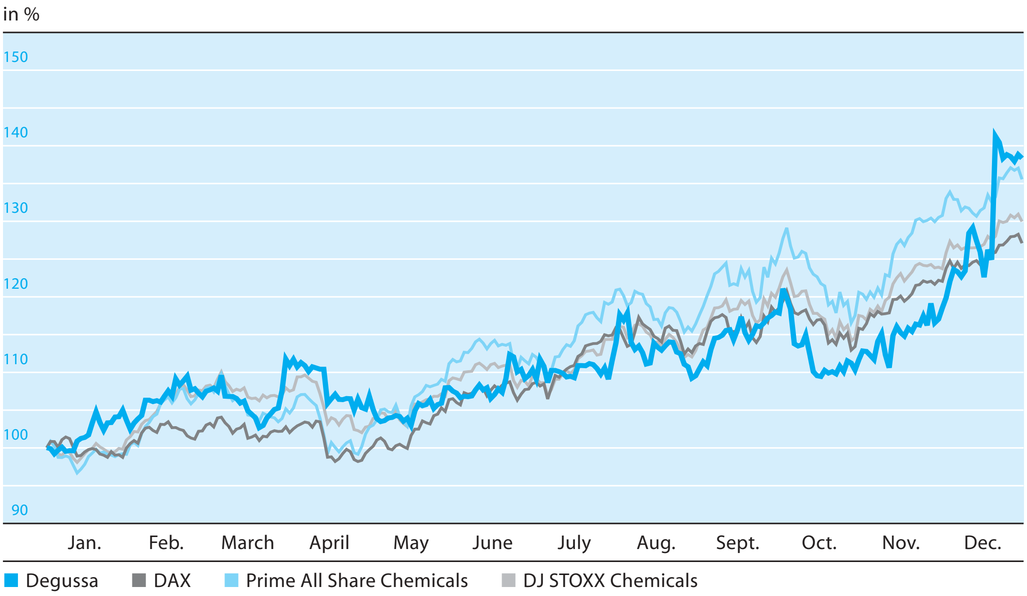
In the first half of the year, market sentiment was held back mainly by rising raw material prices. A slight drop in oil prices after the summer highs also boosted German shares.

Key data on Degussa stock

ISIN						**DE 0005421903**
Securities identification no. (WKN)						**542 190**
Bloomberg ticker symbol						**DGX GR**
Reuters ticker symbol						**DGXG.DE**
		2001	2002	2003	2004	**2005**
Average daily trading volume (XETRA)	Shares	344,115	542,104	86,094	24,258	**42,459**
No. of shares		205,623,590	205,623,590	205,623,590	205,623,590	**205,623,590**
Capital stock	€	205,623,590	205,623,590	205,623,590	205,623,590	**205,623,590**
Market capitalization at year end (XETRA)	€	5,808 million	4,935 million	5,700 million	6,370 million	**8,811 million**
Highest share price (XETRA)	€	39.60	37.67	29.47	32.98	**44.50**
Lowest share price (XETRA)	€	20.20	24.00	20.62	24.70	**30.50**
Year-end price (XETRA)	€	28.25	24.00	27.72	30.98	**42.85**
Average price for the year (XETRA)	€	30.14	31.56	25.17	29.24	**34.39**
Earnings per share [1]	€	2.05	1.10	– 0.77	1.45	**– 2.39**
Dividend per share	€	1.10	1.10	1.10	1.10	**0.00** [2]
Cash flow per share [1] [3]	€	7.28	6.95	6.42	5.42	**5.23**
Equity per share [1]	€	28.74	27.62	24.40	22.76	**20.36**
Price/earnings ratio [1] [4]		9.1	21.8	–	21.4	**–**
Dividend yield [4]	%	3.9	4.6	4.0 [3]	3.55	**0.0**

[1] 2003–2005 as per IFRS; 2001–2002 as per US-GAAP.
[2] Proposed.
[3] Funds from operations.
[4] Based on the XETRA closing price at year end.

Relative performance of Degussa stock in 2005



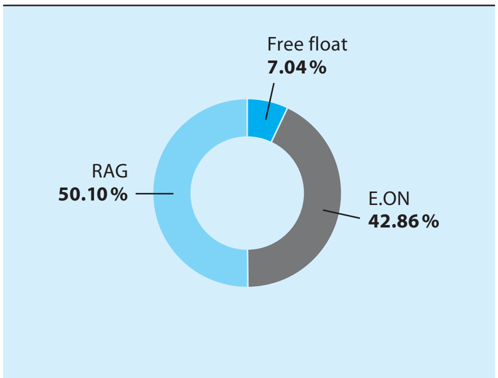
Moreover, export-oriented companies in the euro zone benefited from the weakening of the euro, which slipped more than 10 percent against the US dollar during the year, thus increasing their competitiveness.

RAG announced plans to take over Degussa

Degussa's share price rose in the first half of the year, continuing the rally that started in the second half of 2004, then traded sideways at around €34 per share in the summer. From September, it resumed its upward trend, rising to over €36.

In October it came under pressure from the high impairment charge for the fine chemicals activities and expectations that the Group would report a loss at year end. Since the Degussa Group reported a net loss of €491 million, the Board of Management has decided to recommend to the Annual Shareholders' Meeting on May 29, 2006 that the company should not pay a dividend for 2005.

Degussa's present shareholder structure



In mid-December Degussa's majority shareholder, RAG Aktiengesellschaft, announced that it intended to acquire all remaining shares in Degussa. It is offering a price of €42 per share for the free float. Rumors in the press pushed the share price up to €44.50 before the announcement and the stock has been trading slightly above the offer price since then. It closed the year at almost €43.

Comparison of the performance of Degussa stock

	Year-end 2005	Year-end 2004	Change in %
Year-end price (XETRA) in €	**42.85**	30.98	38
DAX	**5,408**	4,256	27
M-DAX	**7,312**	5,376	36
Prime All Share Chemicals	**697**	514	36
Dow Jones STOXX Chemicals	**339**	261	30

Since the free float is just 7.04 percent and average daily trading volume is therefore only around 42,000 shares, institutional investors have shown little interest in Degussa. Private German investors therefore remained the largest group of investors in 2005. A small proportion of shares were held by employees and German investment funds.

Despite this, capital market communication remains very important to Degussa. Alongside a large number of one-on-one meetings with investors and financial analysts, the management and investor relations team attended the following investment conferences in 2005:

- **January 12:** Dresdner Kleinwort Wasserstein, German Investment Seminar, New York
- **June 1:** Deutsche Bank, German Corporate Conference, Frankfurt am Main
- **June 21:** Sal.Oppenheim, European Chemicals Conference, Zurich
- **September 28:** HypoVereinsbank, German Investment Conference, Munich

During the year, financial analysts were invited to in-depth presentations of the Specialty Polymers and Coatings & Advanced Fillers Divisions. These one-day meetings gave them an opportunity to gain a more detailed insight into the business units in these divisions and talk to the managers in charge.

Assuming RAG acquires all remaining Degussa shares in the course of 2006, we will discontinue our investor relations activities. Until then, we will continue our policy of timely and open communication with the capital market and uphold our high standards of reporting and information.

Financial diary 2006

March 3, 2006:	Financial Press Conference (Düsseldorf)
May 9, 2006:	Interim Report January–March 2006
May 29, 2006:	Annual Shareholders' Meeting
August 8, 2006:	Interim Report January–June 2006
November 8, 2006:	Interim Report January–September 2006 and Fall Press Conference (Düsseldorf)

Management Report

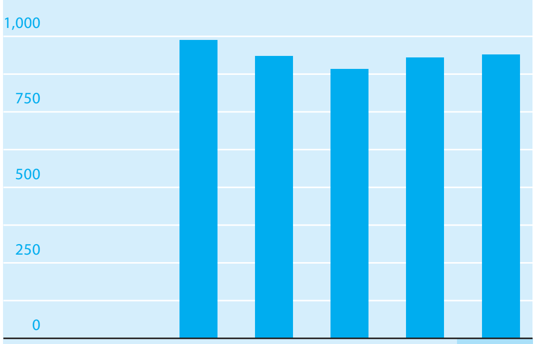
Global expansion of business
Performance and business conditions

Overview

Year-on-year improvement in sales and EBIT After a sluggish start to the year, business operations picked up perceptibly during 2005. Overall, sales advanced 9 percent to €11.8 billion, boosted by higher volumes and significant price increases. However, earnings were impacted by the substantial rise in energy and raw material costs, which could not be recouped entirely by raising prices. Thanks to higher volume sales and cost reductions, EBIT[a] rose 1 percent to €940 million.

EBIT[1]

in € million



	2001	2002	2003	2004	**2005**
	988	936	892	931	**940**

[1] Data for 2001–2003 include operations subsequently divested.

The operating result[b] also rose 1 percent to €683 million. The non-operating loss of €982 million mainly comprises an impairment charge of €836 million on the fine chemicals activities. As a result, income before income taxes for the continuing operations was minus €299 million, well below the previous year's profit of €591 million.

Group net income after minority interests was also far lower than in the previous year, showing a loss of €491 million. The Board of Management and Supervisory Board will be recommending to the Annual Shareholders' Meeting that there should be no dividend payment for 2005.

The impairment charge also caused a deterioration in Degussa's key financial ratios. Nevertheless, the company still has a sound financial basis: All dynamic financial indicators were above the internal targets. Funds from operations[c] and net financial debt were essentially unchanged year-on-year at €1.1 billion and €2.2 billion respectively.

[a] EBIT = Earnings before interest, taxes and non-operating items.

[b] Earnings before taxes and non-operating items.

[c] Funds from operations = Net income adjusted for the non-operating result after taxes, after-tax income from discontinued operations and depreciation.

Reconciliation from EBIT to Group net income

in € million		2005	2004	Change in %
	EBIT	**940**	**931**	**1**
–	Net interest income	– 104	– 102	
–	Interest expense for pension provisions	– 153	– 155	
=	**Operating result**	**683**	**674**	**1**
–	Non-operating result	– 982	– 83	
=	**Income before income taxes from continuing operations**	**– 299**	**591**	**–**
–	Income before income taxes from discontinued operations	10	– 88	
=	**Group net income before income taxes**	**– 289**	**503**	**–**
–	Income taxes	– 190	– 194	
=	**Group net income**	**– 479**	**309**	**–**
–	Minority interests	– 12	– 11	
=	**Share of net income attributable to shareholders of Degussa AG**	**– 491**	**298**	**–**
	Earnings per share in €	– 2.39	1.45	–

Forecast basically met For 2005 we forecast a slight rise in sales year-on-year, accompanied by a slight improvement in EBIT. Sales rose 9 percent and thus exceeded our target, whereas the 1 percent increase in EBIT was at the lower end of our expectations. The price rises originally envisaged for the fourth quarter were achieved slightly earlier.

As budgeted, the net interest position was in line with the previous year. We did not expect the sum of the non-operating result and income from discontinued operations to be so negative. However, the impairment charge on the fine chemicals activities meant that the non-operating result for 2005 was far worse than originally anticipated. As a consequence, income before income taxes, Group net income and earnings per share fell well short of expectations.

We forecast that the return on capital employed (ROCE) would be on a par with the cost of capital. ROCE was 9.8 percent and thus above the cost of capital, which was originally 11 percent but was adjusted to 9 percent during the year as a result of market conditions. Value creation—defined as the difference between ROCE and cost of capital—amounts to €77 million.

Following due consideration of all relevant circumstances the Board of Management decided on February 6, 2006 to enter into negotiations on divesting the construction chemicals activities. Having evaluated all offers received, it decided on February 14, 2006 that it would initially only pursue negotiations with BASF. The aim of both companies is to reach an agreement on the deal as soon as possible. The information on the strategy and future development of the company in this report is based on the current organizational structure of the Degussa Group, which includes the construction chemicals activities. The impact of the possible divestment of these activities is outlined in the section on material changes since the end of the fiscal year.

Economic background

Steady growth in the world economy The global economic upswing continued in fiscal 2005 but the growth rate was one percentage point lower than in 2004 at 4.2 percent. However, the massive rise in the price of crude oil and severe natural disasters in Asia and the USA did not cause a significant drop in economic activity, indicating that the world economy is in good shape. Sustained price stability in the main industrialized countries is central to this favorable overall trend.

As in 2004, global growth was driven by the USA and the emerging economies of China, India and Russia. The Japanese economy continued to pick up but economic growth in the European Union (EU) lagged well below the momentum in other regions. This was chiefly due to low growth rates of just 0.9-1.7 percent in the EU's largest economies: Germany, France and the UK.

In Germany, the year-on-year growth rate declined to just 0.9 percent, mainly as a result of the massive rise in oil prices. At the same time, domestic investment remained cautious. Consequently, the labor market did not receive any sustained impetus from this front and consumer spending slipped further in the face of the unsatisfactory employment situation. Once again, Germany was only able to post a positive growth rate because its export surplus increased further. The country therefore remains the world's top exporter, confirming the international competitiveness of the German economy.

Exports are expected to remain stable at a high level in 2006, strengthening capital spending in Germany and giving a slight boost to domestic demand. The growth rate should therefore increase somewhat to around 1.7 percent. At the same time, there should be a slight decline in the unemployment rate.

Like Germany, most other countries in the euro zone only benefited marginally from the sustained growth in the world economy. The euro zone grew by 1.6 percent, 0.2 percentage points less than in 2004. This was due to higher energy prices and weaker consumer spending. This trend affected all EU countries with the exception of the new member states: All of these countries—apart from Malta—posted above-average growth rates. In the UK, growth declined 1.5 percentage points to 1.7 percent in 2005.

Perceptible growth is expected in 2006, especially in the euro zone. Growth forecasts are 2.2 percent for the euro zone and 4.4 percent for the new EU member states, giving a total growth forecast of 2.1 percent for the EU.

Growth in Russia was again above the average for the world economy at 6.1 percent in 2005. Nevertheless, that represents a reduction of 1.1 percentage points despite favorable energy price trends. Structurally, inadequate investment in infrastructure, high inflation and increasing state intervention to deal with shortcomings in the business world could mar growth prospects in the future. That is borne out by the forecasts for 2006, which suggest that the growth rate will drop to 5.7 percent.

The US economy again proved exceptionally robust in 2005, driven principally by sustained high consumer spending, and grew by 3.6 percent. That was only 0.6 percentage points less than in 2004 despite the significant rise in energy prices and the considerable damage caused by hurricanes. Continued high capital spending, good capacity utilization and the labor market situation suggest that the upward trend will continue. However, the high current account deficit and signs of inflation could act as negative triggers, prompting the Fed to raise interest rates more sharply than it has done to date. Overall, there is likely to be some dampening of consumer spending, which accounts for about two-thirds of US GDP. The rise in the US dollar, combined with a renewed increase in energy prices, could exert further downward pressure on domestic consumption. In all, the economy is expected to post further growth of 3.4 percent in 2006.

In 2005 Japan benefited from far more favorable export conditions, supported by demand from the growing Southeast Asian region and the far more upbeat domestic economy. The unemployment rate declined and wages rose. Growth was 2.3 percent, just 0.4 percentage points off the previous year's level. In 2006 the country is expected to grow by at least 2 percent and by 2.5 percent if conditions prove more favorable.

As in previous years, China and India were the main driving forces behind global growth. Both countries outpaced the average growth rates, with China growing by 9.9 percent and India by 7.1 percent. China thus became the fourth largest economy in the world. Both China and India will continue to expand rapidly and should soon catch up with the established economies. For example, China is now the world's third largest exporter, behind Germany and the USA. China and India are both expected to hold growth at last year's level in 2006.

By contrast, Brazil, another important emerging market, only grew by 3.2 percent in 2005. Although economic momentum declined throughout Latin America, the sustained upward trend remained intact. In 2006 the Brazilian economy is expected to expand by 3.7 percent.

Upswing in the chemical industry The upswing in the global economy spread to the German chemical industry with a time lag of about one year. Accompanied by higher raw material and energy prices, output increased 6 percent in 2005 and total sales rose by 7 percent to around €152 billion. Exports were the main driver, advancing nearly 8 percent to almost €82 billion. Above all, deliveries to EU states, Japan and other Asian countries increased by as much as 24 percent. By contrast, exports to the USA declined by 1 percent. Domestic demand also improved due to strong export demand in other sectors, raising sales on the home market by 6 percent to just over €70 billion. Upstream activities such as inorganic commodity chemicals and petrochemicals grew by between 5 and 15 percent and thus benefited more than those further along the chain. Fine and specialty chemicals did worst, as evidenced by their growth rate of just 0.5 percent.

The outlook for 2006 is good as well. Production and sales should continue to rise and employment is expected to pick up after years of consolidation.

The chemical industry in the EU raised output by 2.8 percent and thus fell short of the global average of 3.7 percent. Output in the United States was far weaker than in the EU, posting an increase of just 0.6 percent. By contrast, the chemical industry in the Asia Pacific region and Latin America reported above-average growth rates of around 7 percent. In the Middle East and Africa, output of chemicals also increased by more than 7 percent. The positive underlying trend is expected to continue in 2006.

Degussa benefited from the sound worldwide economic trend, which enabled it to increase volume sales in all regions. Nevertheless, its performance was held back by the rise in energy and raw material costs. Its broad customer base, regional diversification and the wide-ranging applications of the products in its portfolio reduce exposure to cyclical fluctuations. Consequently, it may benefit less clearly from phases of economic upswing than some more narrowly aligned chemical companies. Conversely, it is less sensitive to downswings.

Business activities

A clear strategy Degussa is a multinational corporation consistently aligned to high-margin specialty chemicals. The restructuring of 2001–2004 following the merger of Degussa-Hüls and SKW Trostberg has been successfully completed and the company is well-positioned today. Size is one of the main competitive factors in the chemical industry. Degussa is the world's leading specialty chemicals company and ranks among the top ten chemicals corporations. In periods of rapid structural change and pronounced cyclical trends, its stable, diversified portfolio is a key success factor. Moreover, Degussa stands out from its competitors in the global marketplace through its clear profile as a specialty chemicals company. Since February 2001 operations with sales of over €6 billion have been divested. The proceeds have been used to lastingly strengthen its core operations and reduce debt.

Building on these sound foundations, Degussa is now concentrating on achieving ambitious growth and profitability targets. Its goal is not simply to be a specialty chemicals company, but to rank among the best. That is the purpose of the "Degussa 2008"[a] strategy program introduced in 2005. The objective is clearly defined: By 2008 at the latest Degussa aims to raise EBIT by €300 million compared with 2004.

[a] See pages 8–11

New organizational structure Effective January 1, 2006, two new members were appointed to the Board of Management, bringing the total complement to six. At the same time the second management tier (division heads) was abolished. Degussa also restructured its operating business as of January 1, 2006[a]. However, the segment reporting and management discussion and analysis in this Annual Report are based on the structure in place until December 31, 2005. Since the start of 2006 operations have been grouped in seventeen business units which are assigned to four reporting segments: Technology Specialties, Construction Chemicals, Consumer Solutions and Specialty Materials. The reporting segments reflect Degussa's strong competence platforms and bundle activities with comparable business models and strategic success factors. The significance of the business units is expressed in Degussa's management philosophy: "as decentralized as possible, as centralized as necessary." In line with this, the business units act as entrepreneurs within the enterprise. They report directly to the Board of Management and are supported by service units which are also run on commercial lines. The Corporate Center in Düsseldorf, Germany, is responsible for strategic management of the Group.

[a] Organizational chart see page 5

[b] Market positions see pages 28–29

An overview of the members of the Board of Management and Supervisory Board is given on pages 155–160 of this Annual Report. A description of the remuneration system for the Board of Management is contained in the Corporate Governance Report on page 150 of this Annual Report. A breakdown of the individual remuneration of members of the Board of Management can be found in Note 32 to the consolidated financial statements.

Degussa AG, Düsseldorf, Germany, is the listed parent company of the Degussa Group. The majority shareholders on the reporting date were RAG AG, Essen, Germany (50.10 percent), and E.ON AG, Düsseldorf, Germany (42.86 percent). The free float comprised the remaining 7.04 percent. In December 2005 RAG announced that it intended to take over Degussa entirely and that it would be making a voluntary public offer for the free float in January 2006.

Market leadership Degussa's aim is to position its products among the market leaders. In other words, it aims to rank among the top three suppliers[b] worldwide in all areas of business. Today, 85 percent of sales are generated by operations that are already positioned at the forefront of their market segments. Products that have not yet achieved market leadership are examined to see whether this can be achieved and if so, when. The business is then managed accordingly or divested in the medium term. In 2005 Degussa expanded its market position further as a result of higher demand and selective capacity expansions.

A global presence Degussa operates production facilities in fifty countries. The largest sites such as Marl, Wesseling and Rheinfelden in Germany, Antwerp in Belgium and Mobile in the USA have integrated production structures used by several business units. That means, for example, that by-products or waste from one production process can be used as a starting material for a different product. The business units can also use the site energy supply and infrastructure cost-efficiently. For technical or logistics reasons, some production facilities are located close to our customers or even on their sites. There are also many smaller sites around the world that are only used by one business unit.

Major production sites by region

Germany	18
Other European countries	47
North America	33
South America	5
Asia, Africa, Oceania	27

Effective procurement Most products and services are purchased via the internal procurement service. Its customers are the Group's operating units. In 2005, Europe and North America accounted for the bulk of procurement; the highest growth was in Asia.

While most procurement is centralized, a small proportion is handled directly by individual business units. The focus is on long-term agreements to secure the supply of key raw materials. In addition, the feasibility of in-house production is examined.

In future, Degussa will be stepping up its focus on renewable resources. The aim is to raise the proportion of sales generated with products produced from renewable resources from 5 percent at present to 10 percent in five years time.

Optimization of the business portfolio We continued to optimize our business portfolio in fiscal 2005 to concentrate on specialty chemicals. The following activities were divested:

Divestments in 2005

Activity	Month	Sales in 2004[1)]
Fruit Systems	February	64
Proligo	April	28
Food Ingredients[2)]	September[3)]	449
ESM	December	112

[1)] In € million.
[2)] Excluding Fruit Systems.
[3)] Divestment not yet completed.

The divestment of the Food Ingredients activities had not been completed at year end as the European antitrust authorities had not given their approval. These activities are reported as discontinued operations. The activities of Proligo and ESM, which were reported as discontinued operations in 2004, were divested in 2005. The earnings impact is reflected in the corresponding income statement items. Details are given in Note 6 to the financial statements. When calculating the key financial indicators used for corporate management purposes, discontinued operations are stripped out of the balance sheet.

We expect to sign an agreement on the divestment of the Water Chemicals activities in the first half of 2006. The assets and liabilities of these activities are classified as held for sale. In 2004 the Fruit Systems activities were classified as held for sale.

Alongside a number of smaller acquisitions, Degussa acquired all remaining shares in its former joint venture, CYRO. Details are given in Note 5 to the financial statements. CYRO has been fully consolidated since June 1, 2005.

Research and development[a)] stepped up

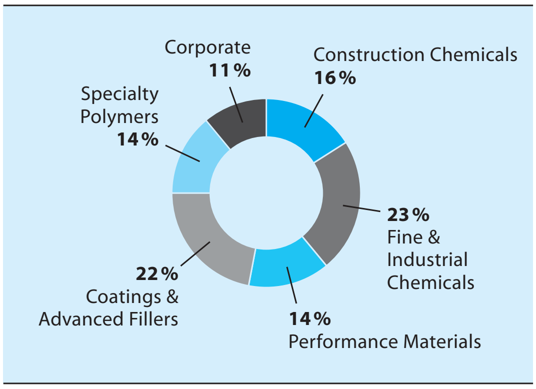
[a)] Further details see pages 65–66

Research and innovation are particularly important elements in Degussa's strategy of profitable growth. Developing intelligent products and solutions is vital to differentiate the company from competitors in the global marketplace. Innovative products and custom-tailored systems solutions are an essential way of creating value for customers.

In 2005 Degussa increased spending on research and development (R&D) by 10 percent to €350 million. Due to the strong sales growth, R&D expenses accounted for 3.0 percent of sales, as in the previous year. The aim is to increase this in the medium term. Worldwide more than 2,900 R&D staff were employed at over 40 research facilities in 2005.

In addition to in-house R&D, Degussa has numerous research alliances with universities to give it rapid access to basic knowledge. This cooperation network has been expanded through new contacts in two growth regions: China and Russia. Overall, some €6 million was invested in alliances with universities and other institutes in 2005.

R&D expenses by division



Products and technologies developed in the past five years account for about 20 percent of sales. Every euro spent on research generates sales of about €1 p.a. through new products. Pioneering approaches to research alliances are used to combine innovation with a strong customer focus. That raises the pace of development from the initial idea to market success.

Degussa submitted patent applications for about 350 new discoveries in 2005. In all it has around 20,000 patents and pending patents and about 10,000 registered trademarks and pending registrations.

Group exceeded its ROCE target Financially, Degussa is managed on the basis of a system of integrated, value-oriented performance indicators. The central performance yardstick is return on capital employed (ROCE). This shows the extent to which the company earns a return on the capital it invests. The benchmark for Degussa is the cost of capital. If ROCE is above the cost of capital, the company creates value. This is shown as an absolute figure. These indicators are used to assess the past and planned performance of individual activities and the Group as a whole.

Degussa constantly reviews the assumptions used to calculate its cost of capital and adjusts the calculation to take into account sustained changes in interest rates, market risks and effective tax rates. In 2005, other long-term interest-bearing provisions were included in the capital base for the first time alongside pension provisions. This increased the proportion of debt-like capital. The weighted average cost of capital (WACC) was 9.0 percent before taxes in 2005.

Key data on R&D at Degussa [1)]

		2001	2002	2003	2004	**2005**
R&D expenses	in € million	380	362	331	319	350
Sales to R&D ratio	in %	3.2	3.1	3.1	3.0	3.0
R&D employees	approx.	3,300	3,250	3,100	2,800	2,900

[1)] Data for 2001–2003 include operations subsequently divested.

Cost of capital

	2005	2004
Risk-free interest rate	4.3%	5.0%
Market premium	4.0%	5.0%
Beta factor	0.9	0.9
Cost of equity after taxes	**7.9%**	**9.5%**
Cost of debt before taxes	4.2%	5.4%
Income taxes[1)]	– 1.6%	– 2.2%
Cost of debt after taxes	**2.6%**	**3.2%**
Equity weighting	52.0%	54.0%
Debt weighting	48.0%	46.0%
Cost of capital after taxes	**5.4%**	**6.6%**
Tax rate	39.5%	40.0%
Cost of capital before taxes	**9.0%**	**11.0%**

[1)] Tax deductibility of interest on debt is included in the cost of capital here.

In addition to this minimum return, Degussa aims to create additional value. That secures the long-term future of the company, increases the value of investors' capital and safeguards the jobs and incomes of employees. The organizational structures of the Group and performance-related remuneration are geared to this system of targets and management. This ensures that measures taken by the operating units that create value and foster profitable growth are encouraged and rewarded. Similarly, businesses that destroy value over the long term are divested.

In 2005 ROCE was 9.8 percent and thus well above the cost of capital before taxes. Value added came to €77 million. The change in the method used to calculate capital employed (long-term interest-bearing provisions are no longer deducted) resulted in a rise in capital employed and a decline in ROCE. Compared with the restated figures for the previous year, Degussa's profitability improved. Alongside the slight rise in EBIT to €940 million, the chief factor here was the reduction capital employed.

Capital employed and ROCE

	in € million	2005	2004
	EBIT	**940**	**931**
	Intangible assets	2,872	3,314
+	Property, plant and equipment/investment property	4,741	4,632
+	Investments in associated companies	286	328
+	Inventories	1,470	1,422
+	Trade accounts receivable	1,880	1,775
+	Other non-interest-bearing assets	1,240	1,226
–	Non-interest-bearing provisions	– 1,540	– 1,493
–	Trade accounts payable	– 951	– 856
–	Other non-interest-bearing liabilities	– 359	– 360
–	Liabilities held for sale	– 15	– 96
=	**Capital employed** [1)]	**9,624**	**9,892**
	ROCE (EBIT/capital employed)	**9.8 %**	**9.4 %**

[1)] Annual averages.

Individual ROCE targets for the operating units are derived from the Group's cost of capital. To ensure that the overall target for the Group is met, the operating units have to generate a return above the Group target as they also have to cover the costs and capital employed allocated to Corporate. The Construction Chemicals, Performance Materials, Coatings & Advanced Fillers and Specialty Polymers Divisions met the minimum return requirements set for them in 2005 while Fine & Industrial Chemicals fell short of its target.

ROCE by division

in %	2005	2004
Construction Chemicals	15.9	15.1
Fine & Industrial Chemicals	9.6	11.4
Performance Materials	15.5	17.2
Coatings & Advanced Fillers	17.3	20.7
Specialty Polymers	19.2	18.3
Total divisions	**14.7**	**15.9**
Degussa (including Services and Corporate)	**9.8**	**9.4**

EBITDA margin declined slightly Another key management yardstick is the EBITDA margin (EBITDA as a proportion of sales). Since it is a relative figure, it provides a key basis for comparing cost structures and earnings power with internal and external businesses. Depreciation and amortization are not included in EBITDA, so the EBITDA margin can be taken as an approximation of the return on sales-based cash flows.

The EBITDA margin of 13.5 percent reported for 2005 is derived from virtually unchanged EBITDA (€1.6 billion) and far higher sales. Accordingly, it was below the year-back figure of 14.7 percent. This downtrend was reflected in all divisions. Construction Chemicals was only marginally below the year-back figure. Fine & Industrial Chemicals posted the strongest decline. This was attributable to high raw material prices, which it was unable to recoup fully through price rises.

EBITDA margin by division

in %	**2005**	2004
Construction Chemicals	13.7	14.0
Fine & Industrial Chemicals	11.6	14.4
Performance Materials	13.2	15.3
Coatings & Advanced Fillers	18.4	20.9
Specialty Polymers	16.4	17.6
Total divisions	**14.4**	**16.4**
Degussa (including Services & Corporate)	**13.5**	**14.7**

Ambitious targets

Strategic objectives:

- Degussa aims to achieve organic growth of 5 percent p.a. (before currency effects). This should be driven by innovation and, above all, by the fast-growing Asian and Eastern European regions.
- To achieve this, the percentage of business ranked among the market leaders is to be raised to close to 100 percent, but without jeopardizing the Group's profitability targets and sound financial profile.
- Active portfolio management is the key to this. Optimizing the business portfolio is an ongoing process of adaptation to changing business conditions.

Financial targets:

- We want to achieve our ambitious profitability targets. The goal is for ROCE to be at least two percentage points above the cost of capital, which is currently 9 percent, and we intend to raise EBIT by €300 million by 2008 (reference base: 2004).
- We aim to achieve a sustained improvement in cash flows through our focused investment policy and working capital management.
- We aim to maintain our sound credit profile. All strategic actions are therefore focused clearly on sustained achievement of our profitability targets and maintaining our good credit standing.

Earnings position

Degussa Group

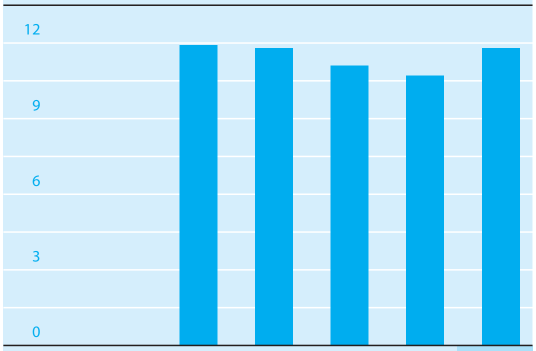
Higher sales Group sales rose 9 percent to €11.8 billion on the back of a 4 percentage point rise in volumes. The 4 percent rise in selling prices is the net effect of price increases, partly to pass on higher raw material costs, and price reductions due to the tough competitive environment in some markets. The change in the scope of consolidation mainly relates to the consolidation of US company CYRO from June 1, 2005.

Change in sales in 2005

Volumes	+ 4%
Prices	+ 4%
Consolidated companies	+ 1%
Exchange rates	0%
Total	**+ 9%**

Sales [1)]

in € billion



	2001	2002	2003	2004	**2005**
	11.9	11.8	11.1	10.7	**11.8**

1) Data for 2001–2003 include operations subsequently divested.

Hike in raw material costs The cost of sales increased 12 percent to €8.4 billion, mainly as a result of the substantial rise in energy and raw material prices. Electricity and gas cost 12 percent more than in the previous year. Our internal raw material cost index, which shows the change in the price of major raw materials used by Degussa, rose by an annual average of 18 percent. For example, there were high double-digit rises in the price of key raw materials such as C_4 crack, carbon black feedstock, propylene and acetone.

Selling expenses increased 7 percent to €1,605 million in line with the planned expansion of business, especially in high-growth markets. R&D expenses rose 10 percent to €350 million, reflecting the goal of raising the company's innovative strength. Thanks to successful cost-cutting programs, general administrative expenses were reduced by 2 percent to €553 million. Other operating income totaled €533 million (2004: €394 million) and included, among other things, the proceeds from the sale of Degussa's premises in Frankfurt and the release of unused provisions. Income and expense relating to exchange rate movements are shown in other operating income and expense without netting. As a result of wider fluctuations in exchange rates, both items increased by about €100 million year-on-year. Other operating expenses came to €631 million (2004: €405 million). The largest single items here were relocation expenses in Frankfurt, the restructuring of the fine chemicals activities and the "Degussa 2008" strategy program.

Impairment charge for fine chemicals impacted Group net income The €867 million in write-downs relate mainly to the impairment charge for the fine chemicals activities. This was necessitated by a deterioration in market prospects, accompanied by considerable overcapacity in the industry and increasing competitive pressure, especially from Asian competitors. Three business units were affected: Building Blocks, Exclusive Synthesis & Catalysts and Peroxygen Chemicals. A total impairment charge of €836 million was made on goodwill and assets. As a result of this, the Group reported an operating loss of €86 million, well below the operating profit of €821 million reported for the previous year. The financial result improved to minus €213 million thanks to a higher contribution from investments recognized at equity.

Extract from the Group income statement

in € million	**2005**	2004
Net sales	**11,752**	**10,740**
Cost of sales	– 8,365	– 7,449
Gross profit on sales	**3,387**	**3,291**
Selling expenses	– 1,605	– 1,500
R&D expenses	– 350	– 319
General administrative expenses	– 553	– 565
Other operating income	533	394
Other operating expenses	– 631	– 405
Impairment write-downs on long-term assets	– 867	– 75
Income from operations	**– 86**	**821**
Financial income	– 213	– 230
Income before income taxes from continuing operations	**– 299**	**591**
Income before income taxes from discontinued operations	10	– 88
Group net income before income taxes	**– 289**	**503**
Income taxes	– 190	– 194
Group net income	**– 479**	**309**
Minority interests	– 12	– 11
Group net income after minority interests	**– 491**	**298**

Income before income taxes for the continuing operations was minus €299 million, down substantially from the previous year's profit of €591 million.

The income before income taxes of €10 million reported for the discontinued operations contains the operating results of Food Ingredients, ESM and Proligo, which totaled €25 million, and expenses of €15 million relating principally to the disposal of Proligo and ESM. The previous year's operating loss of €88 million comprised the results of the three discontinued businesses totaling minus €16 million, minus €72 million relating to the disposal of the metallurgical activities, which were sold in 2004, and expenses for operations divested in previous years. Group income before income taxes contracted from €503 million in 2004 to a loss of €289 million in 2005. Since impairment write-downs on goodwill totaling €712 million are not tax-deductible, income tax expense of €190 million was incurred. The Group made a net loss after minority interests of €491 million in 2005, compared with a net profit of €298 million in 2004.

Key performance data[1]

		2001	2002	2003	2004	**2005**
Sales	in € million	11,862	11,765	11,081	10,740	11,752
Gross trading margin[2]	in %	27	30	29	31	29
EBITDA	in € million	1,858	1,747	1,630	1,583	1,585
EBITDA margin	in %	15.7	14.8	14.7	14.7	13.5
EBIT	in € million	988	936	892	931	940
Return on sales[3]	in %	8.3	8.0	8.0	8.7	8.0
Group income before income taxes	in € million	766	329	– 248	503	– 289
Group net income after minority interests	in € million	421	227	– 261	298	– 491
Earnings per share	in €	2.05	1.10	– 1.27	1.45	– 2.39

[1] Data for 2001–2003 include operations subsequently divested.
[2] (Sales less production costs)/sales.
[3] EBIT/sales.

Degussa AG

Net income impacted by write-downs The annual financial statements of Degussa AG are prepared in accordance with German accounting standards. A brief overview of the income statement and balance sheet is shown here. The complete financial statements of Degussa AG are available on request.

Earnings at Degussa AG, the parent company of the Degussa Group, were impacted by far higher raw material and energy costs and, above all, write-downs of €1.1 billion on financial assets. These mainly relate to the equity interest in the former British fine chemicals group Laporte, which was acquired in 2001 and was made necessary by the impairment charge on the Degussa Group's fine chemicals activities. As a consequence, Degussa AG reported a loss of €1,021 million, which was offset against capital reserves. The Board of Management and Supervisory Board will be recommending to the Annual Shareholders' Meeting that there should be no dividend payment for 2005. In 2004 Degussa AG made a profit of €295 million which was used to pay a dividend of €1.10 per share.

Total assets of Degussa AG were down €1.2 billion at €11.6 billion, mainly as a result of the write-down. Receivables, especially receivables from associated companies, declined by €1.8 billion because two companies founded for purpose of acquiring Laporte were merged into Degussa AG. The addition of the stake in Laporte to financial assets more than offset the effect of the write-downs so financial assets increased by €0.7 billion.

Income statement for Degussa AG

in € million	2005	2004
Net sales	**3,561**	**3,374**
Cost of sales	– 3,003	– 2,649
Gross profit on sales	**558**	**725**
Marketing, R&D and administrative expenses	– 873	– 721
Other operating income/expenses	– 27	35
Operating result	**– 342**	**39**
Financial income/expense	– 693	298
Extraordinary income/expense	0	– 7
Income before income taxes	**– 1,035**	**330**
Income taxes	14	– 35
Net income	**– 1,021**	**295**
Transfers to revenue reserves		– 69
Set-off against capital reserve	1,021	
Profit available for distribution	**0**	**226**

Balance sheet for Degussa AG

in € million	Dec. 31, 2005	Dec. 31, 2004
Intangible assets	53	64
Property, plant and equipment	860	921
Financial assets	6,363	5,631
Non-current assets	**7,276**	**6,616**
Inventories	321	326
Receivables	3,998	5,819
Liquid assets	9	7
Current assets	**4,328**	**6,152**
Total assets	**11,604**	**12,768**
Shareholders' equity	2,739	3,986
Provisions	2,552	2,389
Liabilities	6,313	6,393
Shareholders' equity and total liabilities	**11,604**	**12,768**

Divisions

Sales and EBIT

	Sales	Sales	Change	EBIT	EBIT	Change
in € million	**2005**	2004	in %	**2005**	2004	in %
Construction Chemicals	1,968	1,788	10	223	201	11
Fine & Industrial Chemicals	3,282	3,038	8	212	263	– 19
Performance Materials	1,761	1,598	10	156	166	– 6
Coatings & Advanced Fillers	2,279	2,190	4	289	330	– 12
Specialty Polymers	1,688	1,420	19	194	178	9
Divisions	**10,978**	**10,034**	**9**	**1,074**	**1,138**	**– 6**
Services	740	667	11	60	46	31
Corporate	34	39	– 12	– 194	– 253	23
Degussa	**11,752**	**10,740**	**9**	**940**	**931**	**1**

A full breakdown by segment is given in the notes to the consolidated financial statements on page 96.

Construction Chemicals Division

The Construction Chemicals Division comprises the admixture systems and construction systems activities and is the global market and technology leader in its field. It develops, manufactures and markets system solutions that are designed to make construction projects safer, more economical, more environmentally friendly and more aesthetically pleasing. The products and technologies marketed by Admixture Systems improve the workability of cement and optimize its properties. The products marketed by Construction Systems are used for waterproofing, insulation, repair and protection of buildings and to enhance their appearance.

Improvement in earnings Far higher volumes enabled the Construction Chemicals Division to lift sales 10 percent to €1,968 million. Good growth rates were reported in all regions, especially Asia/Pacific, Latin America, the Middle East and Eastern Europe as a result of booming demand in the construction sector and innovative products. EBIT rose 11 percent to €223 million. In most cases, higher material costs were more than offset by higher volume sales. ROCE increased to 15.9 percent as a result of the improvement in EBIT. The EBITDA margin slipped slightly year-on-year to 13.7 percent.

Capital expenditures Capital expenditures for intangible assets, property, plant and equipment were virtually unchanged year-on-year at €51 million and exceeded depreciation, which came to €47 million. A new production facility for innovative polymers came on stream in Shanghai in November 2005. It is the fifth plant of its type and produces key components for high-performance hyperplasticized concrete. Construction Chemicals hopes that this plant will enable it to benefit from the rapid growth in Asia and especially China. At the same time, it is continuing to expand its global market leadership. To secure further profitable growth, capital expenditure programs totaling over €30 million were initiated for Construction Systems. These include further expansion of powder production capacity in Western and Eastern Europe and the United States and Canada over the next three years.

Research & development Every year more than a hundred new developments are added to this division's portfolio of around 40,000 products. In 2005, R&D spending came to 2.8 percent of sales. Admixture Systems introduced new product variants in Europe and a range of products adapted to regional conditions was launched in China. A concrete admixture that completely eliminates the growth of micro-organisms on concrete surfaces was introduced in North America. Rheofit® 4 Value is a new concept for producers of concrete products such as pavers, concrete pipes and roof tiles. It is designed to raise the quality of products and make production more economical. A new thin spray-on liner (TSL) and a range of new form release

Construction Chemicals at a glance

in € million	2005	2004	Change in %
Sales	1,968	1,788	10
EBITDA	269	251	8
EBIT	223	201	11
Capital expenditures [1)]	51	52	– 2
Depreciation [1)]	47	49	– 4
Capital employed (annual average)	1,401	1,332	5
ROCE in %	15.9	15.1	–
EBITDA margin in %	13.7	14.0	–
Employees as of December 31	7,685	7,388	4

[1)] Intangible assets, property, plant and equipment.

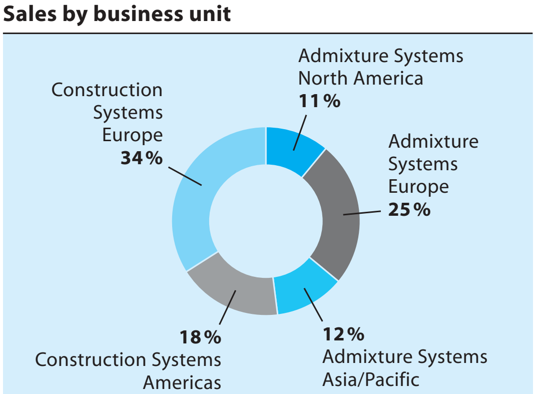
agents for sprayed concrete are ready for commercialization for mining applications.

Construction Systems successfully developed further specialties for the building trade. It launched PCI Nanofug®, the first universal flexible grout that is suitable for all types of ceramic tiles, offering users clear benefits. PCI Carralight®, a flexible mortar for natural stone, was added to the range of light mortars. Due to its innovative low-density technology, 15 kg of PCI Carralight® are equivalent to 25 kg of a conventional product.

Admixture Systems North America High demand from the North American construction industry lifted sales 11 percent to €225 million. EBIT improved considerably thanks to strong growth in volumes following the introduction of new products and technologies and successful efforts to raise efficiency.

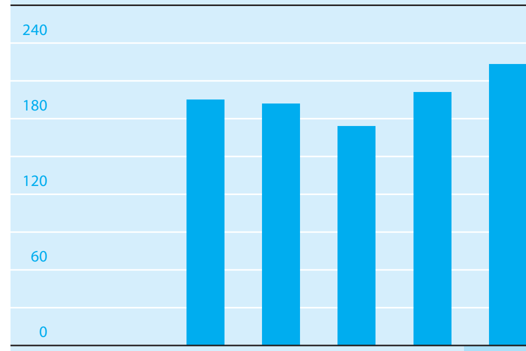
Admixture Systems Europe Despite tough economic conditions in some areas, sales increased 14 percent to €491 million in the wake of high demand. EBIT was considerably higher. Business trends were particularly good in Northern and Eastern Europe, Spain and the Middle East.

Sales by business unit



EBIT: Construction Chemicals

in € million



2001	2002	2003	2004	**2005**
195	192	174	201	**223**

Admixture Systems Asia/Pacific Despite downturns in the more mature markets, sales grew 6 percent to €234 million, mainly because of buoyant growth in the ASEAN/Pacific region. EBIT was above the previous year's level. Clear growth was registered in China. Adapting products to regional requirements has paved the way for this business unit to participate in the promising development of the Chinese construction industry.

Construction Systems Americas Business trends were held back by higher raw material costs, especially at the start of the year, as these could not be passed on to customers in full through higher prices. Nevertheless, increased volumes lifted sales 16 percent to €351 million. EBIT was also up year-on-year. The organizational structure was streamlined further to increase the efficiency of business processes.

Construction Systems Europe High demand lifted sales 6 percent year-on-year to €667 million. Significant growth was reported in Spain, Belgium and France, but sales in Germany only increased slightly. EBIT remained below the previous year's level due to higher raw material costs and increased costs for expansion of the sales network.

Fine & Industrial Chemicals Division

This division groups together most of Degussa's core competencies in organic chemicals. Its five business units rank among the world leaders in agrochemicals, pharmaceutical intermediates, catalysis, C_4 products, environment-friendly bleaching chemicals and feed additives. This division markets a wide array of advanced key technologies.

Higher demand Driven by good volume trends, sales advanced 8 percent to €3,282 million. Earnings were adversely affected by a sharp rise in raw material costs and erosion of selling prices in some areas. EBIT therefore slipped 19 percent to €212 million. The impairment write-down on the fine chemicals activities of the Building Blocks, Exclusive Synthesis & Catalysts and Peroxygen Chemicals Business Units is recognized in the Group's non-operating result so it did not impact EBIT. However, capital employed dropped to €2.2 billion as a direct result of the impairment charge. ROCE slipped to 9.6 percent, mirroring the reduction in EBIT, and the EBITDA margin retreated to 11.6 percent.

Capital expenditures Capital expenditures decreased slightly to €245 million but were well above depreciation, which came to €170 million. The biggest single project is the construction of the fourth DL-methionine plant in Antwerp, Belgium, most of which has now come into service. Since market conditions for methionine are unsatisfactory at present, the Feed Additives Business Unit has reduced annual capacity at this plant from the original level of 150,000 metric tons to 120,000 metric tons. Planned capital spending, including spending on capacity for starting products, will therefore be considerably below the budget of €350 million. A facility to produce the feed additive L-lysine with full backward integration, including a capability to process corn, is under construction in Jining, China. Production capacity will initially be 40,000 metric tons p.a. The C_4-Chemistry Business Unit completed conversion of the MTBE plant in Marl, Germany, to ETBE. Annual capacity for this bioethanol-based anti-knock agent for fuel is 250,000 metric tons. In Barra do Riacho, Brazil, the Peroxygen Chemicals Business Unit has started to expand the production facility for hydrogen peroxide for bleaching to 70,000 metric tons p.a.

Research & development Fine & Industrial Chemicals invested 2.5 percent of sales in R&D. Biocatalysts based on "designer cells" for a wide range of applications are the central focus of a new technology platform that won Degussa's internal Innovation Award in 2005. This provides easy access to high-quality precursors, especially for the pharmaceuticals industry. DegussaHeadwaters, a joint venture established by Degussa and the U.S. company Headwaters, has successfully integrated direct synthesis of hydrogen peroxide into a pilot facility that uses

Fine & Industrial Chemicals at a glance

in € million	2005	2004	Change in %
Sales	3,282	3,038	8
EBITDA	380	439	– 13
EBIT	212	263	– 19
Capital expenditures [1)]	245	263	– 7
Depreciation [1)]	170	188	– 10
Capital employed (annual average)	2,203	2,307	– 5
ROCE in %	9.6	11.4	–
EBITDA margin in %	11.6	14.4	–
Employees as of December 31	8,761	8,181	7

1) Intangible assets, property, plant and equipment.

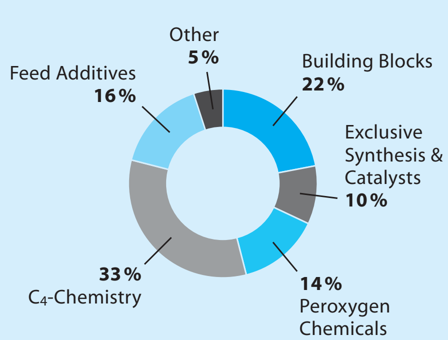
the Degussa/Uhde process to produce propylene oxide (PO). This technology is expected to be commercialized from 2007.

The changeover from MTBE to ETBE in the C_4-Chemistry Business Unit is linked to the use of bioethanol. Because of the ultra-high purity requirements, this represents a highly sensitive change to the entire C_4 hydrocarbon treatment process and is unique. A number of patents have been submitted to protect this technological edge. Work in the Feed Additives Business Unit focused on innovative product modifications. New catalysts facilitate energy-saving, environmentally friendly methods of producing the intermediates acrolein and methylmercaptan. Renewable resources like sugar are becoming valuable starting products, complementing conventional petrochemical feedstocks.

Building Blocks Sales were on a par with 2004 at €714 million but EBIT was significantly lower. The restructuring drive was unable to offset the persistent erosion of margins. In the agrochemicals segment in particular, margins were also impacted by rising raw material and energy costs.

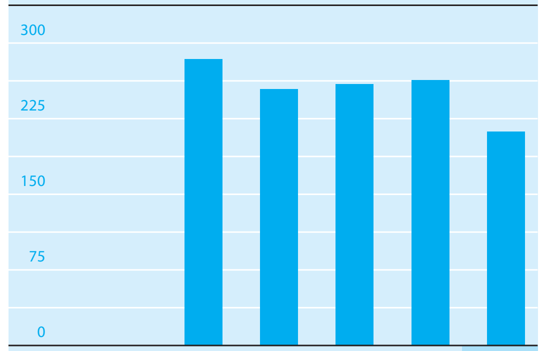
Exclusive Synthesis & Catalysts Lower volumes and prices brought sales down 3 percent to €335 million. Income from the divestment of the BDF[a] business to Victrex plc, UK, offset the decline in operating income, so EBIT was higher than in the previous year.

Sales by business unit



EBIT: Fine & Industrial Chemicals

in € million



	2001	2002	2003	2004	**2005**
	284	254	259	263	**212**

Peroxygen Chemicals Sales were unchanged year-on-year at €464 million. EBIT declined. The increased cost of energy adversely impacted active oxygen products and the earnings situation for initiators remains difficult. Further restructuring has been introduced to safeguard business.

C_4-Chemistry Demand remained high and prices were increased to reflect the rise in raw material costs, lifting sales 28 percent to €1,071 million. Cost savings were another factor behind the significant rise in EBIT.

Feed Additives A sharp drop in prices pushed sales down 2 percent to €518 million despite a considerable rise in demand. Earnings were additionally impacted by the massive rise in the cost of raw materials, especially propylene. EBIT was therefore a good deal lower than in 2004.

In response to the worsening market conditions for methionine, the old 80,000 metric ton production plant for DL-methionine in Antwerp, Belgium, will be taken out of service temporarily when the new, more cost-effective facility comes on stream. It will be modernized but only be reactivated in response to rising demand.

[a] BDF is a starting product for the production of the high-performance polymer PEEK.

Performance Materials Division

This division's main customers are manufacturers of consumer goods. Its products are used in cosmetics and skincare products, shampoos, cremes, detergents and diapers. Its knowledge of applied interfacial chemistry and polymer chemistry is also used for industrial applications. For example, its products are used to stabilize polyurethane foam and give coatings and colorants the right consistency.

The Food Ingredients activities were reclassified as discontinued operations following the signing of a contract of sale and the previous year's figures have been restated accordingly. The Water Chemicals activities are classified as assets held for sale; sales and earnings relating to these operations are still assigned to the Performance Materials Division.

Higher sales Increased volumes and higher selling prices lifted sales 10 percent to €1,761 million. As a result of the massive rise in raw material costs, EBIT came to €156 million, falling slightly short of the €166 million reported in 2004. ROCE slipped considerably to 15.5 percent owing to lower earnings and higher capital employed. The EBITDA margin dropped from 15.3 percent to 13.2 percent.

Capital expenditures Capital expenditures on intangible assets, property, plant and equipment declined year-on-year to €87 million. That was slightly above depreciation (€80 million). The Oligomers & Silicones Business Unit completed capacity expansion at the silicones plant in Essen, Germany, and started up a new polyether plant. In response to high demand, the Superabsorber Business Unit reactivated the production facility in Greensboro, USA, which had been mothballed in 2001. This business unit is expanding production capacity for superabsorbers in Krefeld, Germany, and for the raw material, acrylic acid, in Marl, Germany. Start-up of both plants is planned for this year.

Research & development The Performance Materials Division spent 2.8 percent of sales on R&D. In the adult hygiene segment, improved superabsorbers were used for a new generation of products with maximum fluid retention, making an essential contribution to improving the quality of life for users. Enzyme-catalyzed synthesis is a focus of research in the Care Specialties segment. The production of cosmetic ester oils (emollients), which are used for example in skincare products, has already been established on an industrial scale. This enzymatic process has clear ecological benefits compared with conventional methods of catalysis. Above all, it cuts both energy requirements and carbon dioxide emissions by over 60 percent. ISOLAN® GPS, a new high-molecular-weight emulsifier, has been successfully developed and commercialized. It stabilizes the interface between water and cosmetic oils and bonds the two phases in cremes and lotions. This facilitates the production of extremely stable, pourable water-in-oil

Performance Materials at a glance

in € million	**2005**	2004	Change in %
Sales	1,761	1,598	10
EBITDA	233	244	– 5
EBIT	156	166	– 6
Capital expenditures [1]	87	93	– 6
Depreciation [1]	80	79	1
Capital employed (annual average)	1,007	964	4
ROCE in %	15.5	17.2	–
EBITDA margin in %	13.2	15.3	–
Employees as of December 31	3,838	3,743	3

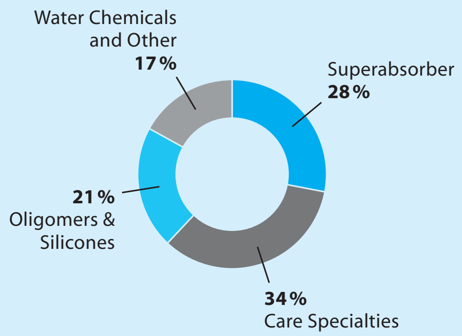
[1] Intangible assets, property, plant and equipment.

emulsions that make the skin feel softer than ever. Based on fatty acids and polyglycerin, ISOLAN® GPS is manufactured entirely from renewable raw materials.

Dispersing agents are indispensable in the production of coatings and colorants. They ensure that pigments and fillers are blended properly and have a major influence on the appearance and service properties of the final coating. The Oligomers & Silicones Business Unit has now developed a new patented class of wetting and dispersing additives allowing more economical production of general-purpose pigment concentrates. Degussa is the first company to use the styrene oxide monomer in bulk synthesis, giving it access to an especially elegant and flexible reaction route.

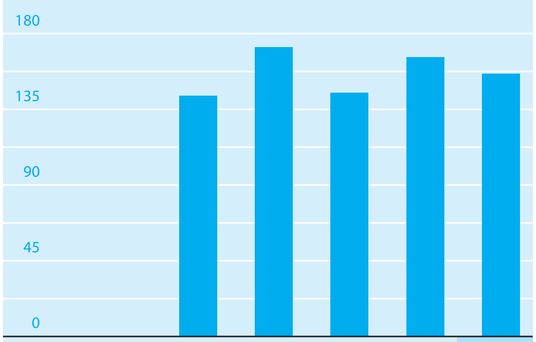
Superabsorber High demand kept the Superabsorber Business Unit's facilities operating at full capacity—including the reactivated plant. However, price increases only partly compensated for the hike in the cost of raw materials, especially propylene. This business unit raised sales 14 percent to €492 million. EBIT was down considerably year-on-year due to the sharp increase in raw material costs. Other adverse factors were production stoppages and higher energy and logistics costs following the two hurricanes in the USA.

Sales by business unit



EBIT: Performance Materials

in € million



2001	2002	2003	2004	**2005**
143	172	145	166	**156**

Care Specialties Higher volumes raised sales 8 percent to €599 million. This was accompanied by an improvement in EBIT. Contributory factors, apart from higher volumes, included perceptible cost savings resulting from a restructuring project in the USA to align production processes and capacity to future market conditions. However, the substantial rises in the price of some raw materials and energy costs could only be passed on to customers in part and then only with a time lag.

Oligomers & Silicones Sales were up 1 percent year-on-year at €366 million. Higher revenues were generated in Europe and Asia but sales declined in North America. A deterioration in the product and region mix and higher fixed costs depressed EBIT year-on-year.

Water Chemicals Sales advanced significantly to €204 million thanks to an increase in market share. Higher raw material costs could not be passed on to customers in full. The increase in EBIT was mainly attributable to higher sales volumes.

Coatings & Advanced Fillers Division

The core competencies of the Coatings & Advanced Fillers Division comprise selective modification of product properties, for example, altering surfaces or giving products a specific consistency. Although customers come from all sectors, its operations are focused primarily on the coatings, printing ink, plastics and rubber industries. Its products are frequently used in autos: in high-gloss coatings with good abrasion and scratch resistance, tires with optimum rolling resistance and high-quality interior trims. As a specialist in surface chemistry and physics, this division is in great demand as a partner to the cosmetics industry.

Impacted by higher raw material and energy costs Although volumes hardly changed, sales increased 4 percent to €2,279 million, partly because prices were increased to recoup some of the rise in raw material and energy prices. However, market conditions meant that prices could not be raised everywhere and at times price rises were only possible with a considerable delay, putting substantial pressure on earnings. EBIT slipped 12 percent to €289 million. The increase in capital employed to €1.7 billion was partly attributable to higher raw material prices, which caused higher inventories and accounts receivable. The decline in operating earnings is reflected in the profitability ratios: ROCE dropped to 17.3 percent and the EBITDA margin decreased to 18.4 percent.

Capital expenditures Capital expenditures rose 22 percent to €169 million and were well above depreciation, which totaled €130 million. In Herne, Germany, the Coatings & Colorants Business Unit started up a production plant for VESTANAT® $H_{12}MDI$ using the patented urea process developed by Degussa. This diisocyanate is a key building block for light- and weather-resistant coatings. An extended portfolio of high-quality starting products can now be offered for major applications such as aqueous polyurethane dispersions and thermoplastic polyurethanes. The expanded capacity for the adhesive raw material VESTOPLAST® in Marl, Germany, also came on stream. Around 75,000 metric tons p.a. of this product are now manufactured on four production lines. Construction work on the two production plants for colorants and polyester in Shanghai, China, has now virtually been completed and start-up is planned for the first half of 2006. Work has commenced on a major new project in Herne, Germany: Production capacity for isophorone and its derivatives is being expanded. Capital expenditures for this project are in the double-digit millions range and completion is scheduled for 2007. The Advanced Fillers & Pigments Business Unit is investing in carbon black facilities in the growing Chinese, Brazilian and Korean markets. The third expansion phase in Qingdao, China, will raise capacity by 50 percent. The new capacity is expected to come on stream in the first half of 2006. The fourth expansion phase is already being planned.

Coatings & Advanced Fillers at a glance

in € million	2005	2004	Change in %
Sales	2,279	2,190	4
EBITDA	419	458	– 9
EBIT	289	330	– 12
Capital expenditures [1)]	169	138	22
Depreciation [1)]	130	127	2
Capital employed (annual average)	1,666	1,595	4
ROCE in %	17.3	20.7	–
EBITDA margin in %	18.4	20.9	–
Employees as of December 31	6,219	6,373	– 2

[1)] Intangible assets, property, plant and equipment.

Research & development The Coatings & Advanced Fillers Division spends 3.4 percent of sales on R&D. The Aerosil & Silanes Business Unit has developed a low-cost production process for sol-gel precision glass for which it received the Degussa Innovation Award in 2005. Instead of grinding and polishing glass pieces, a new wet chemical route has been developed. An AEROSIL® dispersion in a mold solidifies to a gel which is then made into high-purity glass. This allows AEROSIL® fumed silica to be used in glass production for the first time and processed into complicated, high-purity glass bodies. Typical applications are high-tech sectors such as semiconductor components, optics, optical fibers, illuminants and optoelectronics.

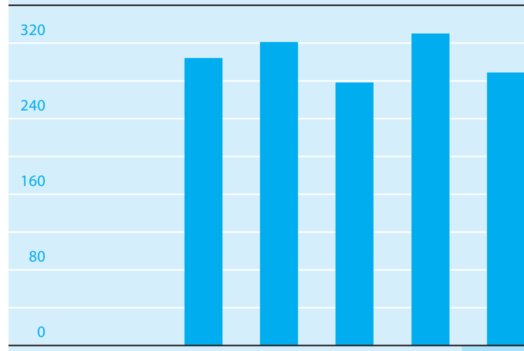
To meet rising demand from the tire industry for high-quality tires for both autos and trucks, the Advanced Fillers & Pigments Business Unit has developed new carbon blacks, performance silicas and rubber silanes. Special products have been introduced to keep auto tires running after a puncture and reduce the rolling resistance of truck tires, thus cutting fuel consumption and extending their service life.

Coatings & Colorants This business unit raised sales 6 percent to €739 million. However, EBIT fell slightly short of the previous year's level. Despite a series of price rises, it was unable to offset the effect of the massive increase in raw material costs although high capacity utilization at production facilities cushioned the impact to some extent.

Aerosil & Silanes Sales increased 5 percent to €502 million on the back of a significant hike in volume sales. Nevertheless, volume growth was not sufficient to counteract the impact of higher raw material and energy costs so EBIT decreased slightly year-on-year.

EBIT: Coatings & Advanced Fillers

in € million

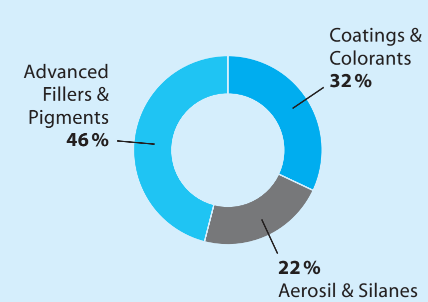


2001	2002	2003	2004	**2005**
304	327	278	330	**289**

Degussa plans to expand its portfolio to include polycrystalline silicon, the starting material for the photovoltaics industry, in order to secure its long-term market position in chlorosilanes. The joint venture (Degussa's stake: 51 percent) with SolarWorld AG will produce and market polycrystalline silicon from silanes, which are a silicon compound. SolarWorld uses this solar silicon to manufacture solar cells. A production plant for more than 800 metric tons p.a. of this product is to be erected at Degussa's Rheinfelden site in Germany. This facility will be operated by Degussa. At the same time, capacity for trichlorosilane and monosilane—precursors for solar silicon—is to be raised.

Advanced Fillers & Pigments Sales rose 2 percent to €1,038 million. EBIT was down substantially year-on-year. Business was held back by a cyclical dip in demand for some product lines and more intensive competition. The impact of sharply increased raw material prices was cushioned to some extent by raising prices.

Sales by business unit



our values
55

Specialty Polymers Division

This division bundles market, technology and applications expertise in the field of high-performance plastics and functional polymers. The business units cover the whole value chain from monomers to engineering polymers. Products are supplied to a wide variety of sectors from sports and leisure to autos and road transport, electronics and communications systems. The division works closely with the Functional Polymers Project House on inter-disciplinary projects.

Improved earnings 2005 was a very successful year: Sales rose 19 percent to €1,688 million, with 11 percentage points of this coming from the first-time consolidation of CYRO. The strong rise in raw material costs could only be recouped to a limited extent. However, cost savings coupled with expansion of business enabled the division to grow EBIT 9 percent to €194 million. Thanks to the good operating result, ROCE increased to 19.2 percent. The EBITDA margin dropped to 16.4 percent.

Capital expenditures Capital spending on intangible assets, property, plant and equipment increased 29 percent to €88 million and thus exceeded depreciation, which amounted to €82 million. The Advanced Polymer Shapes Business Unit is building an extrusion plant for thin films used to protect the surface of Blu-ray® discs. The cost of this facility, which is being constructed in Darmstadt, Germany, is in the double-digit million range. Start-up is scheduled for summer 2006. The Specialty Acrylics Business Unit is building a new oil additives plant in Singapore. Due for completion in 2007, this investment is also in the double-digit millions range.

Research & development Specialty Polymers allocated 2.8 percent of sales to R&D. The High Performance Polymers Business Unit developed high-viscosity, extrusion molding compounds with high melt stiffness based on polyamide 12 (VESTAMID®) for use in high-volume pipes for offshore oil exploration. Since it has exceeded the specifications set by the industry, this has opened up a completely new area of application with enormous potential. In the automotive industry, lightweight construction and the replacement of metal components are becoming more and more important. In response to this trend, film systems for in-mold laminating and foaming processes have been developed in close collaboration with customers to replace painted metal bodywork. The Specialty Acrylics Business Unit has developed oil additives that improve the lubricants in automatic drives and raise the fuel efficiency of motor oils. In the field of pharmaceutical polymers, a nano-structured component system comprising an active substance plus Eudragit was unveiled as the successful outcome of work on drug delivery systems in collaboration with global pharmaceuticals companies. Two clinical studies at our Indian site support the promising concept of the

Specialty Polymers at a glance

in € million	**2005**	2004	Change in %
Sales	1,688	1,420	19
EBITDA	277	250	11
EBIT	194	178	9
Capital expenditures [1)]	88	68	29
Depreciation [1)]	82	72	14
Capital employed (annual average)	1,009	975	3
ROCE in %	19.2	18.3	–
EBITDA margin in %	16.4	17.6	–
Employees as of December 31	4,284	3,632	18

[1)] Intangible assets, property, plant and equipment.

EUDRAMODE™ active ingredient diffusion and release platform.

The Advanced Polymer Shapes Business Unit has developed a high-performance transparent cover film for Blu-ray® discs. Blu-ray® discs can hold up to 25 Gigabytes of information. That is five times more than present DVDs. This enormous storage volume relies on wafer-thin films that meet extremely stringent requirements to protect the data from dirt and scratches as it is stored very close to the surface of the disc.

High Performance Polymers Higher demand lifted sales 7 percent to €288 million. In China, this business unit registered double-digit growth. Systematic cost management cushioned the impact of the sharp hike in energy and raw material costs and EBIT improved.

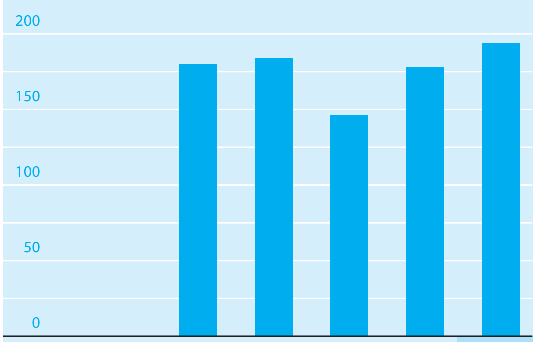
In June 2005 this business unit founded the JIDA Degussa joint venture with Jilin University in China to produce polyetherether ketone (PEEK) and polyether sulfone (PES). This extends its range of attractive high-performance polymers for applications where extremely high mechanical, thermal and chemical specifications have to be met. Markets for these products are automotive engineering, electronics and, above all, the aviation and aerospace sectors. The joint venture started production in December 2005.

Specialty Acrylics As a result of good volume trends and higher prices sales increased 9 percent to €501 million. Asia was the main source of this high growth. However, EBIT was affected by the massive rise in raw material costs and posted a slight decline year-on-year.

Methacrylates This business unit raised sales 33 percent to €493 million. The strong growth was attributable to the consolidation of CYRO and very dynamic market trends, especially in NAFTA. EBIT also improved.

EBIT: Specialty Polymers

in € million

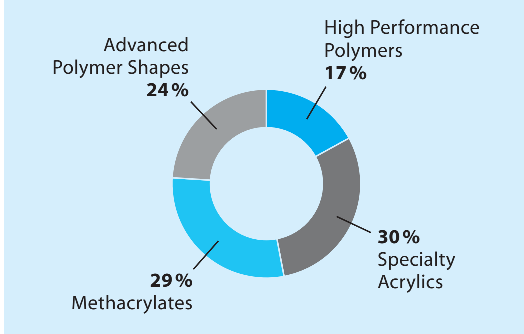


2001	2002	2003	2004	2005
180	184	146	178	**194**

In Asia, booming demand for LCD flat panel displays generated strong growth in applications for molding compounds. In December 2005 an agreement was therefore signed with the Taiwanese company Forhouse to build a PMMA plant in Taiwan. Forhouse will use the molding compounds produced there to manufacture lighting modules for LCD displays. In addition, an integrated world-scale facility for the production of methylmethacrylate and its derivatives is to be built in China. Completion is scheduled for 2008/2009.

Advanced Polymer Shapes Sales surged 27 percent to €406 million due to far higher volume sales and the consolidation of CYRO. The appreciable rise in the cost of raw materials and energy, coupled with lower demand for noise protection products in Asia, pushed EBIT down below the previous year's level.

Sales by business unit



Service units

Customer-oriented services Ten site service units and six multi-site service units support the business units in all tasks not directly related to their operating business. These internal service providers compete directly with external suppliers. They also market their services to companies outside the Degussa Group, mainly companies with facilities at our industry parks.

Services at a glance

in € million	2005	2004	Change in %
Sales	740	667	11
EBITDA	138	122	13
EBIT	60	46	31
Capital expenditures [1]	138	95	45
Depreciation [1]	72	76	– 5
Capital employed (annual average)	474	484	– 2
Employees as of December 31	12,090	12,387	– 2

[1] Intangible assets, property, plant and equipment.

Sales and earnings up substantially year-on-year
The sales reported by the service units increased 11 percent to €740 million. EBIT was 31 percent higher at €60 million, mainly due to an improved performance by Infracor GmbH, Marl, Germany.

Corporate at a glance

in € million	2005	2004	Change in %
Sales	34	39	– 13
EBITDA	– 131	– 181	28
EBIT	– 194	– 253	23
Capital expenditures [1]	36	13	177
Depreciation [1]	62	70	– 11
Capital employed (annual average)	1,864	2,235	– 17
Employees as of December 31	684	566	21

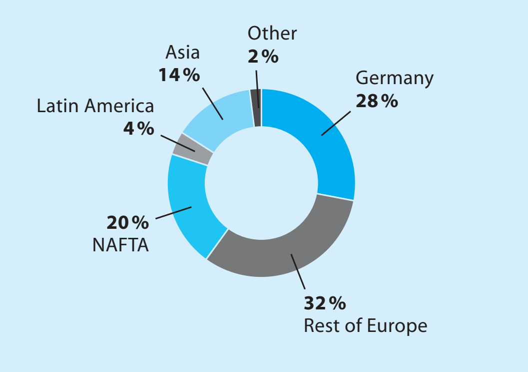
[1] Intangible assets, property, plant and equipment.

Corporate Corporate comprises costs for the Corporate Center and strategic research, including early-stage business. It also contains depreciation of purchase price adjustments on intangible assets under the purchase price accounting method prescribed by IFRS. EBIT improved to minus €194 million. The Corporate Center accounted for minus €89 million of this.

Regions

Increased demand worldwide We operate worldwide: 72 percent of sales are generated outside Germany. In Germany we raised sales 7 percent to €3,269 million. The Fine & Industrial Chemicals and Specialty Polymers Divisions and Services reported far higher sales than in the previous year. In the other European countries sales advanced 8 percent to €3,793 million. The main sales drivers here were the Construction Chemicals, Fine & Industrial Chemicals, Performance Materials and Specialty Polymers Divisions. We have stepped up our activities in Eastern Europe as we registered a clear increase in demand for our products in this region. We have 20 sites there. In Kaba, Hungary, we started up an L-threonine facility with annual production capacity of 10,000 metric tons and there are plans to raise total capacity to 30,000 metric tons. Our goal is to generate 5 percent of Group sales in Eastern Europe by 2008[a]. Sales rose 14 percent to €2,370 million in North America (NAFTA). The consolidation of CYRO made a major contribution to this. A substantial increase in sales was also reported by the Construction Chemicals, Performance Materials and Specialty Polymers Divisions. In Latin America all divisions increased business substantially and sales grew 20 percent to €413 million.

Sales by region[1]



[1] By point of sale.

Planned expansion in Asia Business trends were also good in Asia. Sales advanced 9 percent to €1,626 million with all divisions contributing to the improvement. In response to this high growth, Degussa is expanding its activities in Asia. Production capacity for pigment blacks in South Korea has been raised and work on the multi-user site[b] in Shanghai, China, is proceeding well. The first production facilities there will come on stream in the first half of 2006. Other projects in China are expansion of production capacity for carbon blacks in Qingdao and construction of an L-lysine plant in Jining. In addition, two new joint ventures have been established for agrochemicals and high-performance polymers. The aim is to virtually triple sales in China from around €320 million at present to €900 million by 2008[c].

[a] See page 17

[b] A production site that can be used by a number of business units.

[c] See page 17

Financial condition

Financial position

Financing policy Degussa AG is the financial hub of the Degussa Group. It is responsible for raising funds via the credit and debt capital markets and for ensuring the liquidity of the Group. The credit profile of Degussa AG and its capital market instruments are rated by Moody's Investors Service and Standard & Poor's.

Group companies obtain the funding they need from Degussa AG, which also manages their liquidity back-up. This reduces the cost of borrowing and allows advantageous cash management within the Group. At the same time, it avoids structural subordination for lenders.

Financial risk management In the course of its business, Degussa is exposed to currency and interest rate risks. Financial derivatives are used to reduce these risks. A full overview of the company's hedging targets and strategy of hedging currency and interest-rate risks is given in Note 28 to the consolidated financial statements.

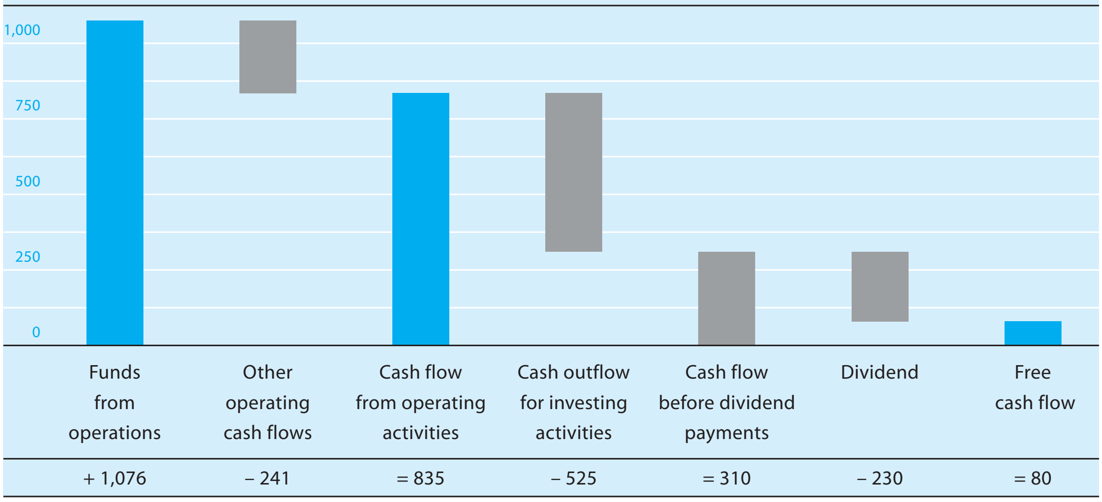
Group companies are required to channel their hedging activities through Degussa AG, which acts as the counterparty for all Group hedging contracts. It nets corresponding counter-risks and aggregates risk positions which are then hedged in full on the financial market as macro-hedges, enabling it to achieve economies of scale. Hedges channeled through Degussa AG that qualify for hedge accounting under IFRS are placed on the external financial market as micro hedges. Details of the financial derivatives used can be found in Note 28 to the financial statements.

Funds from operations unchanged In line with the slight rise in EBIT, funds from operations totaled €1,076 million and were thus virtually unchanged year-on-year (€1,075 million). By contrast, net cash provided by operating activities proved disappointing, dropping 24 percent year-on-year to €835 million (2004: €1,101 million). Reasons included the €123 million rise in net working capital and outflows for non-operating expenses. Far higher proceeds from the sale of noncurrent assets resulted in a free cash flow of €80 million after covering all investment spending and the dividend payment for 2004.

A balanced capital structure As a result of the impairment charge on the fine chemicals activities and the resultant net loss, the financial and capital structure worsened considerably compared with the previous year. Total assets

Cash flow

in € million

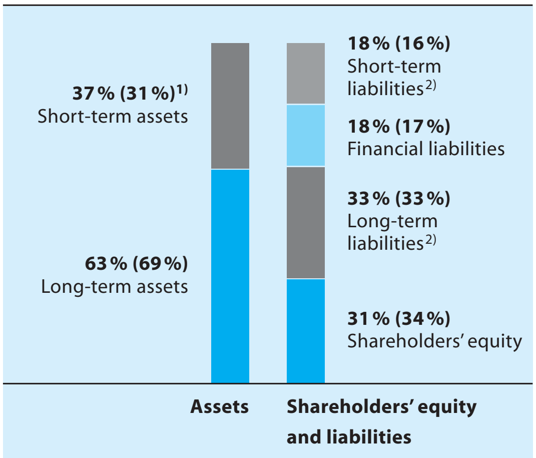


were almost unchanged at €13.5 billion (2004: €13.6 billion) but the equity ratio dropped more than three percentage points to 31.0 percent (2004: 34.3 percent). Net financial debt[a] was €2,162 million and thus virtually unchanged year-on-year (2004: €2,156 million).

Gearing (the ratio of net financial debt to equity) increased to 51.6 percent (2004: 46.1 percent) as a result of the reduction in shareholders' equity, while leverage (the ratio of net financial debt to equity plus net financial debt) increased from 31.5 percent to 34.1 percent.

Good financial ratios The financial structure of the Degussa Group is managed predominantly via dynamic financial ratios. The most important of these are shown in the table.

Financial structure as of December 31, 2005



[1)] Prior-year figures in brackets.
[2)] Excluding financial liabilities.

[a)] Net financial debt is derived from financial liabilities, marketable securities and other liquid assets.

Dynamic financial ratios

	2005	2004	Target
Funds from operations/net financial debt	49.8 %	49.9 %	> 40 %
EBITDA/net interest	15.2	15.5	> 10.0
Net financial debt/EBITDA	1.4	1.4	< 1.5

The ratio of funds from operations to net financial debt shows what proportion of net financial debt is covered by funds generated by operating business in a given period. Interest coverage (EBITDA/net interest position) shows the number of times EBITDA covers net interest expense. The dynamic debt ratio (net financial debt/EBITDA) shows the theoretical number of reporting periods required for EBITDA to repay net debt.

These financial ratios are the key factors used in medium-term planning and corporate strategy, alongside growth and profitability targets. Despite the net loss and the decline in net cash provided by operating activities, all targets set for the financial ratios were exceeded in 2005.

Rating review On the reporting date, Degussa's credit ratings (Moody's: Baa1, P-2; Standard & Poor's BBB+, A-2) had been placed on credit watch negative. Standard & Poor's (S&P) announced that it would be reviewing the rating in October 2005 when the impairment charge was taken on the fine chemicals activities. In December 2005, when RAG announced that it intended to take over Degussa entirely, S&P issued a statement that a downgrade of several rating steps was possible. On January 27, 2006 S&P downgraded Degussa's ratings to BBB and A-3 and retained it on credit watch negative. RAG's plans also prompted Moody's to place Degussa on credit watch negative.

Sound financing structure The main component of Group financing is the €1.25 billion corporate bond issued by Degussa AG at the end of 2003, which matures in December 2013. For short-term funding requirements the Group uses a €750 million Euro Commercial Paper program or money market transactions through committed credit lines.

Degussa has systematically diversified its sources of funding in recent years. At year-end 2005 61 percent of financial debt was owed to the debt capital markets and 39 percent came from the credit markets. The average remaining term of financial liabilities is 5.1 years (2004: 5.8 years). The average interest rate on financial debt, including financial derivatives, is 3.8 percent (2004: 3.7 percent).

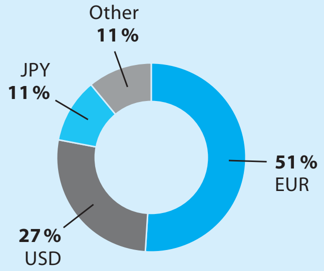
The table gives an overview of the average interest duration of our financial liabilities at year-end 2005.

Interest duration

	Percentage
< 6 months	67
6–12 months	2
1–3 years	3
3–5 years	3
5–7 years	1
7–10 years	24
> 10 years	0
Total	**100**

Wherever feasible, investments are financed in the local currency. The chart gives an overview of Degussa's financial liabilities by currency at year-end 2005, taking into account financial hedges.

Financial liabilities by currency



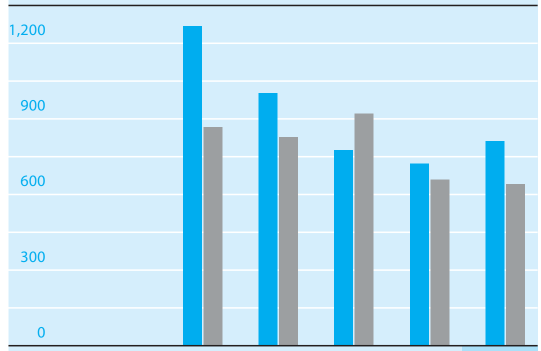
Liquidity assured Degussa AG has extensive credit lines to secure its liquidity. A central element is the syndicated credit facility for €2.0 billion renegotiated in April 2005, which runs until April 2010. €475 million of this had been drawn on December 31, 2005. Overall, Degussa AG has committed credit lines of €2.4 billion, €0.6 billion of which had been drawn at year end.

Capital expenditures[a]

Capital expenditure and depreciation policy
Capital expenditures are geared to expanding our good market position in our main areas of activity and driving forward businesses where we can achieve market leadership. A distinction is made between capital expenditures to expand capacity and market position, raise efficiency and replace existing facilities and for environmental protection and R&D. The first three categories are expected to meet demanding return targets. The objective is to finance investments out of cash flow. In view of Degussa's growth strategy, capital expenditures will be slightly higher than depreciation in the coming years.

Capital expenditures and depreciation

in € million



	2001	2002	2003	2004	**2005**
Capital expenditures	1,269	1,001	778	722	**814**
Depreciation	868	829	922	661	**643**

[a] Capital expenditures see also pages 48–57

Intangible assets, property, plant and equipment are depreciated over their useful lives using the straight-line method. Write-downs are made when the carrying amount of assets exceeds their actual value. For futher details see Note 2 to the consolidated financial statements.

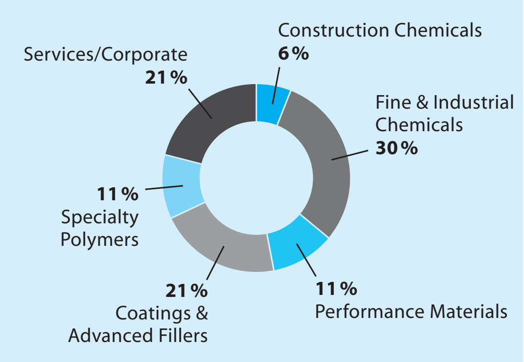
Major projects completed or virtually completed in 2005

Business unit	Location	Project
C_4-Chemistry	Marl, Germany	Conversion of MTBE plants to ETBE (completed)
Feed Additives	Antwerp, Belgium	Expansion of capacity for methionine
	Jining, China	Expansion of capacity for lysine
Superabsorber	Greensboro, USA	Reactivation of superabsorbers plant (completed)
	Krefeld and Marl, Germany	Expansion of capacity for superabsorbers and acrylic acid
Oligomers & Silicones	Essen, Germany	Expansion of capacity at the silicones plant (completed)
		New polyether plant (completed)
Coatings & Colorants	Herne, Germany	New production plant for the isocyanate H_{12} MDI
	Marl, Germany	Expansion of capacity for amorphous polyalpha olefins (completed)
	Shanghai, China	New production plants for colorants and polyester
Advanced Fillers & Pigments	Yosu, South Korea	Capacity expansion of pigment blacks
Corporate	Shanghai, China	Infrastructure and land rights for multi-user site

Capital expenditures up on the previous year
Capital spending on intangible assets, property, plant and equipment increased by €92 million to €814 million. We thus remained within our capital expenditure budget of €850 million. Depreciation declined slightly to €643 million (2004: €661 million).

The main focus of capital expenditures was once again on expanding our market leadership. 65 percent of capital expenditures were for production facilities, 32 percent for general facilities and infrastructure and 3 percent for research and development facilities. The majority of large individual investment projects were in Germany. 47 percent of capital expenditures for intangible assets, property, plant and equipment was allocated to locations outside Germany.

Capital expenditures by division



Higher investment in financial assets €170 million was invested in financial assets, compared to €32 million in 2004. This figure principally includes the acquisition of the remaining 50 percent stake in CYRO in North America and the establishment of two joint ventures in China.

Asset structure

Total assets down slightly year-on-year Degussa's total assets decreased by €0.1 billion to €13.5 billion. Within long-term assets, intangible assets declined by €0.9 billion to €2.5 billion, chiefly as a result of the impairment write-down on the fine chemicals activities. At the same time, property, plant and equipment rose €0.2 billion to €4.9 billion due to capital expenditures and the consolidation of CYRO. Overall, long-term assets were €0.9 billion lower than in the previous year at €8.5 billion. They thus accounted for 63 percent of total assets in 2005 compared with 69 percent in 2004.

Short-term assets increased by €0.8 billion to €5.0 billion. Inventories rose 5 percent to €1.6 billion due to higher raw material costs. Trade accounts receivable were €0.1 billion higher than in 2004 at €2.0 billion as a result of higher selling prices. Discontinued operations/assets held for sale increased to €0.7 billion. This item contains the Food Ingredients business (€0.6 billion) and the Water Chemicals activities (€0.1 billion).

Off-balance-sheet items Most intangible assets created by the company were capitalized at the time of the mergers of Degussa, Goldschmidt, Hüls and SKW Trostberg which were eventually combined to form the present Degussa Group. As a result, Degussa currently has no material intangible assets that are not included in its balance sheet.

The sale of Degussa's premises in Frankfurt has led to a shift from company-owned assets to leased assets. Further details of leasing agreements can be found in Note 27 to the consolidated financial statements.

Selective use is made of off-balance-sheet financing instruments (e.g. operating leases) on a very limited scale only.

General statement on the company's business condition The sound underlying demand trend is not reflected in the income statement owing to the sharp rise in raw material and energy costs. Nevertheless, the Group managed to raise sales and EBIT further in fiscal 2005. The impairment write-down led to a net loss and a deterioration in Degussa's capital structure. Nevertheless, Degussa still has good operational earnings power, a sound financial base and a good credit profile.

Strategic research

Technologies for the future Creavis is the umbrella for the Group's strategic research activities, which span all business units. It focuses on the rapid development of new areas of business, from basic research to the production of complete systems for end-users. The innovation process ranges from identifying tomorrow's technologies and attractive business opportunities to developing the technology needed to implement promising ideas and commercializing new products and technologies through internal start-ups. Project houses and science-to-business centers within Creavis generate innovative technology platforms and products for new business.

Nanotronics Science-to-Business Center The Nanotronics Science-to-Business Center opened in April 2005 after a construction period of just nine months. It is dedicated to developing systems solutions based on nano materials for the electronics industry. Applications include printable electronics, affordable displays and mobile energy systems. The nanotronics projects receive funding from the Federal State of North Rhine-Westphalia and are co-financed by the European Union.

Bio Science-to-Business Center A new Bio Science-to-Business Center is currently being erected in Marl, Germany. It is scheduled to start operating in 2006. Around sixty Degussa scientists will work in the center's state-of-the-art laboratories and pilot facilities alongside cooperation partners from universities and industry on the development of new biotechnological products and processes based on natural raw materials. Degussa has gained key expertise in bio processes in recent years, for example through its Biotechnology and ProFerm Project Houses. Building on this, it now aims to develop highly efficient processes using renewable raw materials rather than fossil-based resources.

The second major focus of innovation comprises bioactive products, for example, novel systems for the effective transportation of active ingredients in medicines and cosmetic substances. Over the next five years Degussa will be investing €50 million in the Bio Science-to-Business Center. The Federal State of North Rhine-Westphalia also plans to provide funding for the activities of this center, with the European Union as co-financer. The objective of the center is to strengthen Degussa's position in the field of "white biotechnology".

Functional Polymers Project House These days, surface modification and interfacial chemistry are key technologies for the development of new functional materials. By using nano-scale fillers, materials can be given combinations of properties that cannot be achieved using conventional technology. Potential applications range from engineering plastics with significantly better mechanical properties, for example, improved rigidity combined with better breaking resistance, to construction materials with lower temperature-sensitivity.

Proferm Project House This project house focuses on the development and optimization of fermentative processes for various product lines. For example, for the Exclusive Synthesis & Catalysts Business Unit it has developed and successfully tested new fermentative processes for the production of prolin and tryptophan, two important amino acids used in pharmaceuticals. For the Care Specialties Business Unit it has developed special microorganisms with the capability to produce a new active substance for use in cosmetic formulations. This project house is also working on low-cost sources of sugar. As part of this work, a project has been established with various Brazilian research institutes on the utilization of waste from the production of sugarcane.

Process Intensification Project House Degussa has defined two production-oriented areas of focus for process intensification: catalytic systems and functional dispersions. During its first year, this project house developed highly active catalysts. Used in conjunction with new reactor systems, these generate a substantial improvement in the cost-efficiency of selected production processes. Mini-emulsion technology has paved the way for the production of functional dispersions that should open up new industrial applications in the field of adhesives.

Internal start-up: Ceramic Membranes Degussa sees itself as a systems supplier of lithium ion batteries based on safe new components and materials. The ceramic separator SEPARION® has already been launched on the market as a pioneering product. In October 2005 a production facility with capacity of 3 million m^2 came on stream as scheduled. Moreover, Degussa has set up a joint venture with the Japanese company ENAX, Tokyo, in the extremely attractive field of materials for lithium ion batteries. ENAX is the technology donor for the joint venture and a future research partner. Through this joint venture, Degussa has acquired an exclusive worldwide license to manufacture advanced electrodes for high-volume lithium ion batteries.

Internal start-up: Degussa Homogeneous Catalysts In 2005 Degussa Homogeneous Catalysts produced and marketed ligands and catalysts on a commercial scale. Through collaboration with the Leibniz Institute for Organic Catalysis in Rostock, Germany, the range of reactions catalyzed with cataCXium® A has been increased considerably. In a single step in very mild conditions, aromatic aldehydes, valuable starting products for example for pharmaceutical active ingredients, can be obtained from simple halogen aromatics. In view of its significant benefits, this technology has already been scaled up successfully for industrial use by the Exclusive Synthesis & Catalysts Business Unit.

Employees[a)]

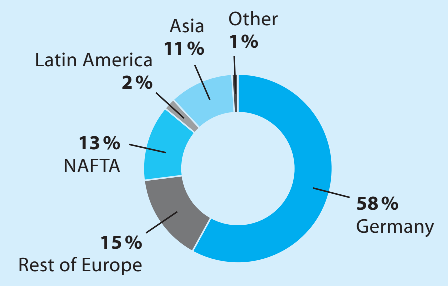
[a)] Further information in the Corporate Citizenship Report and Statistics.

A global presence The Degussa Group had 45,553 employees worldwide on December 31, 2005. 1,992 of them were employed in discontinued operations, which includes staff working for Food Ingredients.

The number of staff working for the continuing operations increased by 1,291 to 43,561. The headcount was increased by operations consolidated for the first time in 2005 (including around 700 employees at CYRO, USA, and about 660 at Degussa Sanzengh, China) and by internal growth. At the same time, a number of employees left the group as a result of restructuring and divestments. Personnel expenses increased to €2,837 million (2004: €2,771 million). Performance-oriented pay is central to human resources management at Degussa. Managers receive a variable bonus of between 15 and 50 percent of their base salary. The performance-related bonus is based on corporate earnings, the performance of the organizational unit where the manager works and personal performance.

42 percent of staff are employed outside Germany, reflecting Degussa's international focus. In view of the planned growth, especially in Asia and Eastern Europe, both the absolute number of jobs outside Germany and their percentage of the total are set to rise further in the future.

Employees by region



Effective employee development Skilled and committed staff are the key to Degussa's success. To ensure it remains competitive, it is continuing to invest in initial and ongoing training of its staff. The in-house skills enhancement programs offered in Germany, China and a number of European countries are very popular and there are plans to roll them out to other countries. Degussa's success in human resources management has been corroborated by the HR consultancy Hewitt which ranked Degussa eighth in a survey of the most attractive European employers for leaders. The key assessment criteria were the efficiency of management development, integrated succession planning, the strategic alignment of the processes and whether top management leads by example.

Employees[1)]

as of December 31		2001	2002	2003	2004	**2005**
Employees		53,378	47,623	45,348	45,139[2)]	45,553[2)]
Personnel expenses	in € million	3,441	3,115	2,871	2,771	2,837

[1)] Data for 2001–2003 include operations subsequently divested.
[2)] Including Food Ingredients employees.

our values

Training for the future Degussa is also extremely committed to initial training of young people. Nearly 600 young people started training courses at Degussa in September 2005. The company is also training nearly 60 young people on behalf of third parties. In total, there are nearly 2,100 young people on 40 different vocational training courses at 29 sites in Germany. These figures demonstrate Degussa's commitment to the "Training for the Future" industry agreement: The number of trainees is nearly 60 percent above the sector average. Degussa's strong commitment to training is also reflected in the fact that trainees account for 7.7 percent of the workforce, compared with an average of 5.0 percent in the German chemical industry. It spends about €50 million on vocational training every year.

Employee suggestions generate savings In 2005 Degussa introduced a new initiative to encourage employees to suggest improvements and utilize ideas that have already been put into practice at other sites. In Germany alone, around 7,600 ideas were submitted to the idea management program, generating benefits totaling nearly €10 million (2004: €7 million).

Events after the end of the reporting period

Material event after the end of the fiscal year Following due consideration of all relevant circumstances, on February 6, 2006 the Board of Management decided to enter into negotiations on divesting the construction chemicals activities. Having evaluated all offers received, it decided on February 14, 2006 that it would initially only pursue negotiations with BASF. The aim of both companies is to conclude an agreement on this deal in the short term.

The sale of these activities would have a major impact on our earnings, financial position and assets in fiscal 2006. It would reduce sales, EBIT and income before income taxes from continuing operations by eliminating the positive contribution made by Construction Chemicals. The assets and liabilities and earnings of the divisions are outlined in the segment report in the notes to the consolidated financial statements.

This segment's assets totaled €1,472 million at end-December 2005 and its liabilities were €419 million. Construction Chemicals reported sales of €1,968 million and EBIT of €223 million in 2005. Pension provisions, financing and tax effects relating to the division are not included in the segment report.

The proceeds from this transaction would improve the net interest position. We would expect the divestment to generate a profit, which would be shown as income from discontinued operations, together with the operating income of the Construction Chemicals segment as of the date of divestment. That would increase Group net income.

The cash inflow from the sale would also bring an appreciable reduction in our net financial debt.

Risk report

Risk policy As the global leader in specialty chemicals, Degussa is exposed to a number of risks and opportunities in the course of its business. Managing these risks and opportunities is an integral part of corporate management and of all business decisions. The central element of our risk policy is that we only enter into business risks if we are confident that they will enable us to achieve a sustained rise in the value of the company and believe that the possible negative effects can be controlled.

Risk management system The aim of our risk management system is to identify and evaluate risks as soon as possible and to introduce measures to limit and prevent such risks so the company is not placed in a situation that jeopardizes its future. It also creates risk awareness within the company. This is characterized by careful and responsible behavior on the part of all employees.

Degussa's decentralized organizational structure focused on business requirements is reflected in the decentralized structure and operation of its risk management system. As reporting units, the business units, corporate center and service units are responsible for identifying and evaluating risks and developing and implementing suitable risk prevention and risk management strategies. Within the organizational units, risk coordinators are responsible for coordinating and enforcing all risk management activities. As a monitoring and control function, Risk Management supports the workflows and systems used by the organizational units.

The reporting units conduct an annual risk inventory with the aid of standard software tools. These include a full checklist of potential risk factors. For example, the checklist used by the business units includes individual risk factors arising from business conditions and situation, and all relevant processes in the value-added chain (research, product development, procurement, production, marketing, delivery, etc.). Using these software tools, all business risks are systematically identified and documented and their probability of occurrence and the potential consequences are assessed. To ensure uniform and comparable assessments, Group-wide assessment intervals are specified. Moreover, the applicable risk limitation measures have to be specified in the risk inventory, together with an assessment of their effectiveness and level of implementation. To evaluate risks and include all risk limitation measures in the reporting units, the risk coordinator consults both the management and knowledge owners in individual functions, who are able to obtain assessment from representatives of sub-units. This decentralized structure is reflected in a very broadly based risk captivation structure, which runs right up to the management. Quarterly risk reports are submitted on the basis of the annual inventory. These outline any change in the risks identified and any new risk factors. This also provides an opportunity to review and update preventive measures.

Monthly earnings reports filed by the business units and immediate notification of the Board of Management of major risks ensure timely identification of risks and allow counteraction to be taken. Analysis and structured presentation of the findings in the quarterly risk reports are the task of the Group Risk Manager, who prepares a detailed report on the Group's risk situation for the Board of Management. Degussa's Risk

Manager is the central contact for documentation, coordination and information for the entire Group and is responsible for ongoing development of the risk management system. The system is analyzed every two years to identify how well it is implemented and which elements could be optimized. The Group Risk Manager modifies and updates the risk checklists in consultation with the risk coordinators in the reporting units.

The principles of risk management at Degussa are set out in a Group guideline. This is available to all employees in the intranet, together with other basic information on risk management. An annual meeting of risk coordinators is held to discuss Degussa's risk situation in detail and examine ways of improving the risk management system.

The functioning and efficiency of the risk management system are reviewed at regular intervals by the internal audit department. Once a year the independent auditors also evaluate the suitability of the system for identifying developments that could jeopardize the company's existence and report on their findings to the Board of Management and Supervisory Board. Risk management is regularly discussed by the Supervisory Board's Audit Committee.

Overall risk position Taking into account measures taken or planned, no risks have been identified that could jeopardize the continued existence of Degussa as a whole, either on their own or in conjunction with other risks.

Competition risks The intensive competition in various market segments is a major risk factor. In particular, competitors in low-wage countries increase competitive pressure through aggressive pricing policies. In 2005 this had a particularly negative impact on several business units in the Fine & Industrial Chemicals Division. Moreover, the continued strength of the euro means that competitors from Asia and North America are entering the European market. The units affected use various methods of increasing customer loyalty to reduce these risks. Alongside customer relationship management these include establishing strategic research alliances with customers. Similarly, the business units enhance their competitive position through technical expertise and by improving their cost position and the services they offer. Regional diversification, especially establishing a production base and gaining a foothold in markets in high-growth regions (e.g. China, Eastern Europe), is another way of countering risk.

Production and environmental risks As a manufacturing company, Degussa is exposed to a risk of production stoppages and quality problems. It is also exposed to risks relating to product safety, occupational safety and environmental protection. Group-wide guidelines on project and quality management, product safety, occupational safety and environmental protection are an effective way of reducing these risks. Production stoppages due to plant failures are insured. Further, production processes and workflows, which are certified as conforming to international standards, are constantly being upgraded and improved, careful maintenance is carried out on all plants and employees receive appropriate initial and further training. Adequate provisions have been set up for the need to deal with environmental contamination from the past. As a responsible member of the chemical industry, Degussa's processes are based on the principles of the chemical industry's global Responsible Care initiative.

The impact of hurricanes Katrina and Rita was a major risk factor in the third quarter of 2005. Degussa has several sites in the Gulf of Mexico in the United States, which were affected by these storms. However, these facilities sustained comparatively little damage. The main damage was caused by temporary production stoppages as the supply of energy and raw materials collapsed. and the loss of products that were en route to customers. This was effectively limited by insurance cover, early action to find alternative sources of supply for the products to be manufactured and timely reactivation of the production facilities affected.

Procurement risks Other factors of importance for Degussa’s risk position are the availability and price of raw materials, starting products and intermediates. In particular, raw material prices of significance to Degussa are dependent on exchange rates and the price of crude oil. To raise the reliability of supply, long-term agreements are concluded with existing suppliers where possible or alternative suppliers are found. Pricing and procurement risks are reduced through worldwide procurement and optimized processes to ensure immediate sourcing of additional raw material requirements. Similarly, use of alternative raw materials is examined for various production processes and Degussa is working on the development of alternative production technologies.

As well as the higher cost of raw materials, production costs at Degussa have been significantly affected by the sharp rise in energy prices. In recent months, heating oil, natural gas and electricity have become far more expensive and further cost increases are foreseeable in the first few months of 2006. Efficient Group-wide energy management and optimized global procurement activities are used to increase the reliability of supply.

Sales and marketing risks These include the dependence of individual business units on major customers. Risks affecting sales in the sectors Degussa supplies and a deterioration in the competitive position of its customers evidently impact Degussa’s operating business. Permanent monitoring of the market, acquiring new customers, developing customer strategies and efforts to establish new applications and gain access to new markets as early as possible are used to counter these risks. Expanding business with low exposure to cyclical fluctuations is another way of minimizing risk. In 2005, sales and marketing also faced the problem of how to pass on the significant rise in the price of some raw materials to customers with long-term agreements. In some cases, it was possible to raise prices to reflect higher raw material prices by integrating price formulas into supply agreements.

Interest and exchange rate risks In the course of its business, Degussa is exposed to the risk of changes in exchange rates and interest rates. Financial derivatives are used to reduce these risks. The objective of risk management is to reduce fluctuations in earnings and cash flow. The purpose is to protect Group earnings from the risks arising from changes in interest and exchange rates.

Financial derivatives are used for hedging purposes only, in other words, they are only used in connection with transactions originated by business operations whose risk profile is exactly opposite to that of the financial derivatives. A financial guideline issued by the Board of Management contains binding rules on the type and extent of transactions that are hedged. A detailed overview of interest rate and currency management and the use of derivative financial derivatives is given in Note 28 to the consolidated financial statements.

Liquidity risks Degussa AG has committed credit lines totaling €2.4 billion to secure its liquidity. At the end of December 2005 €1.7 billion of these credit facilities had not been drawn. The availability of significant unused credit lines excludes liquidity risks at any time.

Risks relating to acquisition and investment decisions In view of their long-term nature and the large amount of capital involved, acquisitions and investments involve a wide range of complex risks. Degussa has defined structured responsibilities and approval procedures for the preparation, implementation and monitoring of such decisions.

Information technology risks Degussa-wide guidelines provide details of how to handle information and the secure use of information systems. Internal communication is used to raise employees' awareness of IT security. State-of-the-art back-up systems, database mirroring, virus scanners, firewalls, access control and user authorization systems are used to protect user interfaces and operating systems and maximize data security.

Risks arising from litigation In the normal course of business, Degussa is exposed to risks of possible litigation, especially in the areas of product liability, patent law, tax law, antitrust and cartel law and environmental law. Moreover, acquisitions and divestments may lead to guarantee claims against the company. Where necessary, provisions are set up for such risks. Further details can be found on Note x to the consolidated financial statements.

Other risks Degussa also has contingency plans to deal with the outbreak of a pandemic, for example, as a result of the spread of bird flu. A Group-wide guideline and a phased action plan are in place to deal with such eventualities. Implementation of the contingency plan has started in all organizational units.

Global Code of Conduct Since it operates worldwide, Degussa is exposed to risks of infringing local and international law. To avoid such problems, a Group-wide Code of Conduct on compliance with statutory requirements forms a central element in Degussa's corporate philosophy. In order to prevent possible violations of the law, all employees are required to align their professional activities to the rules set out in the Group-wide compliance program and, above all, the company's Global Code of Conduct. This sets demanding minimum standards that are applicable throughout the Group, even if they go beyond local custom and legislation. Compliance is monitored by the Group Compliance Officer in collaboration with the operating units and regional managers.

The Code of Conduct brings together all Group guidelines. Where infringement could lead to substantial risks, the staff who are required to ensure compliance with the relevant laws and regulations are given special training. Training on the compliance program, including the Global Code of Conduct, antitrust and cartel law, environmental law, export control regulations, anti-terrorism controls and other topics was stepped up in 2005. Interactive training modules are available via the intranet to provide more detailed information on certain compliance issues.

Degussa is convinced that ensuring compliance with all rules, regulations and laws is the necessary basis for business success.

Corporate Governance

A wide range of rules, recommendations and suggestions have been added to the German Corporate Governance Code since its introduction. The latest amendment was in June 2005. Degussa has implemented most of these for many years. Corporate governance has a firm place in the company's management philosophy. On December 13, 2005, the management issued its fourth declaration of conformity pursuant to § 161 of the German Stock Corporation Act. The declaration and explanations of deviations from the code can be found on page 154 and on our website at:

www.degussa.com/en/investors/corporate_governance.html

Note 32 to the consolidated financial statements outlines the compensation system for the members of the Board of Management and provides a breakdown of the remuneration of the members of the Board of Management and Supervisory Board showing fixed and variable components.

Outlook

Good global economic trends The global upswing is expected to continue undiminished in 2006 and 2007. The USA will remain one of the driving forces, with growth expected to remain around last year's high level. The emerging Chinese, Indian and Russian markets are expected to post similar growth rates to 2005 and thus contribute to the global upswing. The upward trend in Europe should continue and growth rates are expected to rise. The chemical industry is expected to remain on its present dynamic growth track.

Degussa is on track for growth Degussa should benefit from the global economic uptrend. Thanks to planned and completed capacity expansions, we will be able to meet higher demand and thus secure and strengthen our market position. We are therefore continuing our strategy of profitable growth and focusing consistently on our goal of positioning all our business activities among the market leaders. Research and innovation will remain central elements of our strategy, so we intend to raise our R&D spending from €350 million to €450 million in the mid-term.

The main risk factors are a slowdown in the global economy and further increases in raw material and energy prices. Opportunities include higher-than-anticipated economic growth and reductions in production costs.

The main business opportunities are expected to come from our planned expansion into the high-growth Eastern European and Chinese markets. Separate projects dedicated to these regions have therefore been defined as part of the "Degussa 2008" strategy program.

Successful business performance expected We expect to raise sales slightly year-on-year in 2006 to €12.0 billion. EBIT should also increase slightly to €1.0 billion as a result of continued high demand and moderate price trends.

A slight improvement in the net interest position is expected. Total expenses for the "Degussa 2008" program will be around €150 million in fiscal 2006 and 2007 and the "Strategy & Organization" project is likely to involve additional expense of around €50 million in 2006. These costs will be recognized as non-operating expense. We expect the divestment of the Food Ingredients activities to generate a book gain, which will be shown as income from discontinued operations. We anticipate that Group net income after minority interests will be around €0.4 billion in 2006.

ROCE should improve again and should be above the cost of capital, which is currently 9 percent.

Capital spending on intangible assets, property, plant and equipment will be around €800 million. Capital expenditures should be financed in full out of cash flow.

For fiscal 2007 we are forecasting a further rise in sales and EBIT. The net interest position should improve further but the non-operating result will probably be around the same level as in 2006. In view of the improvement in operating earnings, Group net income after minority interests should increase.

Düsseldorf, February 14, 2006

This report contains forward-looking statements based on the present expectations, assumptions and forecasts made by the Board of Management and the information available to it. These forward-looking statements do not constitute a guarantee of the future developments and earnings expectations. Future performance and developments depend on a wide variety of factors which contain a number of risks and unforeseeable factors and are based on assumptions that may prove incorrect.

Consolidated Income Statement
Degussa Group

in € million	Note	Jan. 1 – Dec. 31, 2005	Jan. 1 – Dec. 31, 2004
Sales	(8)	**11,752**	**10,740**
Cost of sales		– 8,365	– 7,449
Gross profit on sales		**3,387**	**3,291**
Selling expenses		– 1,605	– 1,500
Research and development expenses		– 350	– 319
General administrative expenses		– 553	– 565
Other operating income	(9)	533	394
Other operating expenses	(10)	– 631	– 405
Impairment write-downs on long-term assets	(11)	– 867	– 75
Income from operations		**– 86**	**821**
Net income expense	(12)	– 257	– 257
(thereof financing expense)		(– 310)	(– 319)
Income from investments recognized at equity	(13)	39	24
Other financial income	(12)	5	3
Income before income taxes from continuing operations		**– 299**	**591**
Income taxes	(14)	– 159	– 213
Income from continuing operations		**– 458**	**378**
Income from discontinued operations	(7)	– 13	– 18
Income from the divestment of discontinued operations	(7)	– 8	– 51
Group net income/loss		**– 479**	**309**
thereof share attributable to minority interests in net income/loss	(15)	12	11
thereof share attributable to shareholders of Degussa AG		– 491	298
Earnings per share (€) diluted and undiluted			
Share of net income/loss attributable to shareholders of Degussa AG		– 2,39	1,45

The notes form an integral part of the financial statements.

Consolidated Balance Sheet
Degussa Group

Assets

in € million	Note	**Dec. 31, 2005**	Dec. 31, 2004
Long-term assets			
Intangible assets	(17)	2,494	3,394
Property, plant and equipment	(17)	4,869	4,718
Investment property	(18)	13	16
Investments recognized at equity	(19)	221	255
Long-term securities and other financial assets	(19)	134	273
Deferred taxes	(14)	643	595
Other assets	(21)	118	133
		8,492	**9,384**
Short-term assets			
Inventories	(20)	1,574	1,493
Trade accounts receivable	(21)	1,986	1,847
Receivables from tax assets	(21)	62	127
Financial receivables	(21)	103	82
Other assets	(21)	362	353
Liquid assets	(22)	211	203
		4,298	4,105
Discontinued operations/assets held for sale	(7)	708	144
		5,006	**4,249**
Total assets		**13,498**	**13,633**

The notes form an integral part of the financial statements.

Liabilities and Shareholders' Equity

in € million	Note	Dec. 31, 2005	Dec. 31, 2004
Shareholders' equity			
Issued capital	(23)	206	206
Capital reserve	(23)	4,104	5,124
Revenue reserve		– 239	– 766
Accumulated other comprehensive income	(23)	37	– 154
Group net income	(23)	0	226
Shareholders' equity of Degussa AG		4,108	4,636
Minority interests	(23)	78	45
		4,186	**4,681**
Long-term liabilities			
Pension provisions	(24)	2,890	2,839
Provisions for taxes	(14)	621	606
Other provisions	(25)	807	867
Financial liabilities	(26)	1,481	1,585
Tax liabilities	(26)	90	53
Other liabilities	(26)	44	32
		5,933	**5,982**
Short-term liabilities			
Other provisions	(25)	769	743
Financial liabilities	(26)	892	774
Trade accounts payable	(26)	1,020	918
Income tax liabilities	(26)	198	184
Other liabilities	(26)	329	333
		3,208	2,952
Discontinued operations/liabilities held for sale	(7)	171	18
		3,379	**2,970**
Total shareholders' equity and liabilities		**13,498**	**13,633**

The notes form an integral part of the financial statements.

Statement of Shareholders' Equity
Degussa Group

in € million	Issued capital	Capital reserve	Revenue reserves	Group profit
As of December 31, 2003	**206**	**5,124**	**– 829**	**226**
Dividend payment				– 226
Comprehensive income after taxes				
Group net income			72	226
Change in companies consolidated			– 9	
Other comprehensive income				
Total comprehensive income			72	226
As of December 31, 2004	**206**	**5,124**	**– 766**	**226**
Dividend payment				– 226
Total comprehensive income				
Group net income			– 491	0
Change in companies consolidated			– 2	
Set-off of net loss of Degussa AG		– 1,020	1,020	
Other comprehensive income				
Total comprehensive income			– 491	0
As of December 31, 2005	**206**	**4,104**	**– 239**	**0**

The notes form an integral part of the financial statements.

	Accumulated other comprehensive income				Shareholders' equity of Degussa AG	Minority interests in shareholders' equity	Total shareholders' equity Degussa
	Translation differences	Fair value valuation of securities	Revaluation reserve for acquisitions made in stages	Unrealized gains/losses on cash flow hedges			
	– 162	**26**	**0**	**20**	**4,611**	**42**	**4,653**
					– 226	– 10	– 236
					0		**0**
					298	11	309
					– 9	2	– 7
	– 26	– 20	0	8	– 38		– 38
	– 26	– 20	0	8	260	11	271
	– 188	**6**	**0**	**28**	**4,636**	**45**	**4,681**
					– 226	– 4	– 230
					0		**0**
					– 491	12	– 479
					– 2	23	21
					0		0
	192	– 5	11	– 7	191	2	193
	192	– 5	11	– 7	– 300	14	– 286
	4	**1**	**11**	**21**	**4,108**	**78**	**4,186**

Consolidated Cash Flow Statement
Degussa Group

in € million	**Jan. 1 – Dec. 31, 2005**	Jan. 1 – Dec. 31, 2004
Group net income	**– 491**	**298**
Minority interests	12	11
Reconciliation to the cash flow provided by operating activities		
Depreciation, write-downs/reversals of write-downs on long-term assets	1,501	733
Change in provisions (excluding deferred taxes)	33	– 124
Change in deferred taxes	– 38	18
Change in non-cash income and expense	– 39	– 7
Profit/loss on the disposal of long-term assets	– 53	– 33
Change in net working capital[1]	– 123	9
Change in other assets and liabilities	12	127
Change in the impact of discontinued operations	21	69
Cash flow provided by operating activities	**835**	**1,101**
Proceeds from the disposal of investments	62	76
Proceeds from the disposal of other financial assets	144	32
Proceeds from the disposal of long-term assets and assets held for sale	186	35
Expenditures for the acquisition of investments	– 128	– 11
Expenditures for investment in other financial assets	– 22	– 3
Expenditures for investment in other long-term assets	– 761	– 715
Inflows/outflows relating to marketable securities	– 6	– 9
Net cash used in investing activities	**– 525**	**– 595**
Inflows in connection with financial liabilities	170	2,887
Outflows for the repayment of financial liabilities	– 252	– 3,168
Dividends paid		
to shareholders of Degussa AG	– 226	– 226
to minority interests	– 4	– 10
Net cash used in financing activities	**– 312**	**– 517**
Change in cash and cash equivalents	**– 2**	**– 11**
Change in cash and cash equivalents due to exchange rate movements	19	– 1
Cash and cash equivalents at start of fiscal year (continuing operations)	172	184
Cash and cash equivalents at year end (continuing operations)	**189**	**172**
Other short-term investments and securities at year end	22	19
Liquid funds as of December 31 (continuing operations)	**211**	**191**

[1] Net working capital comprises inventories, trade accounts receivable and trade accounts payable.

The notes form an integral part of the financial statements.

Notes to the Consolidated Financial Statements for the Degussa Group – Fiscal 2005

(1) Basis of reporting

The consolidated financial statements for Degussa AG, Bennigsenplatz 1, Düsseldorf, Germany, and its subsidiaries (Degussa) for fiscal 2005 have been prepared in accordance with the International Financial Reporting Standards (IFRS or IAS) issued by the International Accounting Standards Board (IASB) and their interpretations (SICs or IFRICs) in compliance with EU regulations and the supplementary regulations applicable under § 315 a paragraph 1 of the German Commercial Code (HGB). Degussa changed its accounting from US GAAP (US Generally Accepted Accounting Principles) to the International Financial Reporting Standards in fiscal 2004.

The consolidated financial statements as of December 31, 2005 are presented in euros throughout.

Until May 31, 2004 RAG Aktiengesellschaft (RAG), Essen, Germany, and E.ON AG (E.ON), Düsseldorf, Germany, each held a direct stake of 46.48 percent of the issued capital of Degussa AG. Since June 1, 2004, RAG has held a stake of 50.1 percent, while E.ON has held a stake of 42.86 percent in the issued capital of Degussa AG. Since June 1, 2004 Degussa has been included in the consolidated financial statements for the RAG Group. E.ON recognizes its stake in Degussa at equity. In December 2005 RAG announced that it would be making a voluntary public offer to acquire Degussa's free float. At the same time, RAG and E.ON signed a basic agreement under which E.ON will divest its 42.86 percent stake in Degussa to RAG effective July 1, 2006.

The consolidated financial statements for the Degussa Group are published in the Commercial Register in Düsseldorf, Germany, and the Federal Gazette. RAG publishes its consolidated financial statements in the Commercial Register in Essen, Germany.

(2) Accounting, valuation and consolidation principles

The accounting, valuation and consolidation principles outlined here have been applied consistently in all reporting periods presented here. They have also been applied consistently by all companies consolidated in the financial statements for the Degussa Group.

Estimates The preparation of the consolidated financial statements requires the use of estimates and assumptions that affect the reported value of assets and liabilities, the disclosure of contingent liabilities on the balance sheet date and the reported amounts of income and expenses during the reporting period, see Note (3). The actual values may differ from these estimates. The estimates and the underlying assumptions are reviewed regularly. Corrections are recognized in the period in which the estimates were reviewed and in subsequent periods where the review also refers to current and subsequent periods.

Principles of Consolidation For business combinations, Degussa has elected to use the option in IFRS 1 "First-time Adoption of International Financial Reporting Standards". For the IFRS opening balance sheet as of January 1, 2003 it took over the consolidated financial statements for the Degussa Group as of December 31, 2002. These form the basis for subsequent reporting in accordance with IFRS rules.

All major subsidiaries in which Degussa directly or indirectly holds over 50 percent of the voting rights are included in the financial statements for the Degussa Group. Major shareholdings are valued at equity as associated companies if Degussa is able to exert a significant influence. Essentially, this applies where its share of the voting rights is between 20 percent and 50 percent. Joint ventures are also valued using the equity method. Further details of the group of consolidated companies are given on page 88.

In accordance with IFRS 3 “Business Combinations”, capital is consolidated using the purchase accounting method. The cost of acquisition is offset against the pro rata share of shareholders’ equity held by the parent company, which is revalued at the time of acquisition. The assets, liabilities and contingent liabilities of the subsidiary are included at their fair values. Any remaining goodwill (difference between the purchase price and the pro rata share of equity attributed to the parent company) is capitalized. Negative goodwill from capital consolidation is expensed immediately.

All material receivables, liabilities, sales, expenses, income and profits relating to transactions between consolidated companies have been eliminated. Unrealized gains from transactions with associated companies have been eliminated proportionately to the Group’s stake in such companies. Unrealized losses are eliminated in the same way as unrealized gains, but only insofar as they do not represent an impairment.

Currency translation Foreign currency receivables and liabilities stated in the annual financial statements of Group companies are translated at closing rates on the balance-sheet date. Any translation differences are stated under other operating income or other operating expenses and therefore have an impact on earnings.

Any goodwill and adjustments to fair value relating to acquisitions made by E.ON (former Degussa AG and SKW AG) and other acquisitions made prior to January 1, 2003 are shown—in compliance with the relevant option permitted by IFRS 1—at their original value in euros. Goodwill and adjustments to fair value relating to acquisitions made after this point in time are carried in the functional currency of the acquired foreign subsidiary and translated at the closing rate.

Degussa also made use of the option permitted by IFRS 1 and set the differences arising from currency translation at foreign subsidiaries outside the euro zone that was included in other comprehensive income at zero on the date of transition from US GAAP to IFRS. Revenue reserves were reduced accordingly.

The financial statements of foreign subsidiaries included in the consolidated financial statements for the Degussa Group are translated using the concept of functional currencies. Since all subsidiaries are economically independent, their balance sheets are translated at the exchange rates on the reporting date. Items on the income statement are translated at average rates for the year. Differences arising from the translation of assets and liabilities compared to the previous year and translation differences between the balance sheet and income statement are included in accumulated other comprehensive income and thus have no impact on earnings.

Average annual exchange rates are calculated using the method commonly used by RAG. They are determined from the average exchange rate at month-end in the preceding thirteen months.

The following exchange rates were used to translate the major currencies into euros.

Currency

		Closing rate		Average rate at year-end	
		Dec. 31, 2005	Dec. 31, 2004	**2005**	2004
US dollar	USD	1.1797	1.3621	1.2475	1.2475
Pound sterling	GBP	0.6853	0.7051	0.6847	0.6813
Japanese yen	JPY	138.9000	139.6500	137.1010	133.9960
Swiss franc	CHF	1.5551	1.5429	1.5475	1.5447
Brazilian real	BRL	2.7661	3.5996	3.0374	3.6368
Chinese renminbi yuan	CNY	9.5204	11.2221	10.2155	10.3449

Revenue recognition Sales comprise the fair value from the sale of goods and services (excluding value-added tax) after deduction of discounts and rebates. Sales and other revenues are generated as follows:

(a) Revenues from the sale of goods
Revenues from the sale of goods are recognized when a company in the Degussa Group has delivered products to a customer, the customer has accepted the goods and it is sufficiently probable that this will lead to an economic benefit. Provisions are established to account for the risks inherent in such transactions.

(b) Revenues from the rendering of services and production orders
Revenues for services are recognized in the fiscal year in which the service is rendered. Where the provision of services extends over more than one fiscal year, sales are recognized proportionately to the total service to be provided. In the case of customer-specific manufacturing orders extending beyond the reporting date, income and expenses are recognized by the percentage of completion method. The percentage of completion is derived from the costs incurred by the reporting data as a percentage of the anticipated overall cost.

(c) Interest income, usage fees, dividend income
Interest income is recognized on a pro rata temporis basis using the effective interest method. Income from usage fees is accrued on the basis of the commercial terms of the relevant agreement and recognized on a pro rata basis. Dividend income is recognized as of the date of the right to receipt of payment.

Research and development expenses Research costs are expensed. Development costs have to be capitalized if they meet a number of specific conditions. For example, it must be possible to utilize or commercialize the intangible assets created by the company and economic benefits must accrue to the company from them. Since these conditions were not met in most cases on December 31, 2005, the development costs capitalized for fiscal 2005 were immaterial.

Other product-related expenses Advertising and sales promotion expenses and other sales-related costs are expensed when they are incurred. Provisions for guarantees are set up if utilization is sufficiently probable.

Intangible assets Purchased intangible assets with a definite useful life, including licenses, patents, franchises, trademarks and customer portfolios, are capitalized at the cost of acquisition and amortized over their useful life, which is normally 3–20 years, using the straight-line method. Scheduled amortization is not recognized for purchased intangible assets with an indefinite useful life. Instead they are subject to an annual impairment test, which may give rise to a write-down (impairment charge).

Under IFRS 3 "Business Combinations", scheduled amortization of goodwill is not permitted. Instead, goodwill is subject to an annual impairment test, which may give rise to a write-down (impairment charge). An impairment test also had to be carried out under US GAAP, which Degussa applied until fiscal 2003. Using the option permitted by IFRS 1, goodwill resulting from acquisitions made after July 1, 2001 is not amortized. Instead it is tested annually for impairment. Until December 31, 2001, goodwill relating to acquisitions made before July 1, 2001 was amortized over a period of 8–20 years. Goodwill resulting from acquisitions made after this date was valued analogously to goodwill from acquisitions made after July 1, 2001.

A token amount has been recognized for emissions trading rights allocated free of charge.

Property, plant and equipment Property, plant and equipment are valued at the cost of acquisition or cost of production less accumulated depreciation charges. The straight-line depreciation method is used. Additions made to property, plant and equipment during the year are depreciated on a pro rata basis. Low-value assets are depreciated in full in the year of acquisition.

If material components of a long-term asset have different useful lives, they are recognized as separate long-term assets in property, plant and equipment and depreciated accordingly (component accounting). Costs relating to obligations to dismantle or remove long-term assets at the end of their useful life are capitalized as acquisition costs at the time of acquisition or production.

The useful life is 5–60 years for buildings, 4–25 years for machinery and equipment, and 3–20 years for other facilities, and factory and office equipment.

The cost of acquisition includes direct acquisition expenses.

The cost of production of assets manufactured within the Group comprises the direct cost of materials and labor, plus the applicable proportion of material and manufacturing overheads, including depreciation.

Costs incurred for pre-engineering work for capital expenditure projects are expensed and depreciated over the useful life of the project.

Where production covers an extended period, interest on loan capital incurred in the construction period is also included in the cost of production. Maintenance and repair expenses are stated immediately as expense items. Under the component accounting approach, regular major repairs are recognized in the carrying amount of the relevant long-term asset and depreciated over the period until the next major repair. Expenses designed to prolong the useful life or enhance the future use of assets are capitalized.

Investment property Investment property is principally property held to earn rentals or for capital appreciation. It does not include owner-occupied premises where portions are let to third parties as well as Group companies, if used by third parties is not significant. This is ascertained by examining how the property is used.

Investment property is valued at cost of acquisition or production less depreciation.

Leasing In leasing transactions Degussa is almost exclusively a lessee. Insofar as Degussa bears the substantive risks and benefits of using the leased asset and is thus regarded as the economic owner (finance leases), the leased asset is capitalized under long-term assets at the lower of fair value or the net present value of the non-cancelable minimum leasing payments. Leasing liabilities are stated in the same way. All other leasing agreements where Degussa is the lessee are treated as operating leases and the leasing payments are expensed in equal installments.

Financial assets and marketable securities Material investments in which the company can exert a significant influence are recognized using the equity method. The accounting principles used by Degussa are generally also applied to associated companies.

All other investments and securities are classified as available-for-sale financial assets and recognized at fair value. The resultant unrealized gains and losses (insofar as such losses are not permanent) are recognized in other comprehensive income, after taking account of deferred taxes. Loans are carried at cost of acquisition less amortization; interest-free or low-interest loans are recognized at net present value on the date on which they are first included. Write-downs are made for all investments and securities where a loss of value is expected to be permanent. They are written back if there is evidence that the reasons for this no longer apply.

Impairment charges on long-term assets Long-term assets are tested for impairment as soon as events or altered circumstances indicate that the recoverable value of an asset or group of assets could fall below the carrying amount. In such cases, the net proceeds from the sale of the asset and the net present value of estimated future cash flows from use of the asset are set against the carrying amount. Impairment charges are reversed if the reason for the write-down no longer applies.

Goodwill and intangible assets with an indefinite useful life are not amortized. Instead they have to be tested annually for impairment in accordance with IAS 36 “Impairment of Assets”.

Discontinued operations/assets held for sale Assets held for sale are not depreciated. If the carrying amount of these assets is above the fair value after probable divestment expenses (fair value less cost to sell), they are written down. The fair value is based on the estimated proceeds of the divestment. The operating result and valuation adjustments relating to assets held for sale are included in the consolidated operating result. Discontinued operations are shown separately as soon as a component of an entity comprising a major separate area of business or geographical area or a subsidiary held exclusively for sale is placed on the market and the management has initiated an official selling process. The discontinued operations are recognized at their carrying amount or fair value less cost to sell, whichever is lower. Income from discontinued operations, comprising current income and the proceeds of the divestment, is stated separately in the income statement.

Intangible assets and property, plant and equipment are reclassified when they are recognized as discontinued operations/assets held for sale. As prescribed by the applicable accounting standards, the values recognized in the balance sheets for discontinued operations have not been restated. However, the key figures discussed in this report are based on restated prior-year figures.

Inventories Inventories are carried at the lower of cost (acquisition or production cost) and net selling price, in other words the expected price that can be realized in a normal business transaction less the estimated production and selling expenses. The acquisition cost of inventories is generally derived using average values or the fifo method (first-in, first out).

Acquisition costs include the purchase price and all direct acquisition expenses.

Production costs include the cost of materials and labor, plus the applicable proportion of material and manufacturing overheads, including production-related depreciation and production-related administrative expenses.

Write-downs are reversed if the reason for them is no longer applicable; they may be written back at most to the historical cost of acquisition or production.

Receivables and other assets Receivables and other assets are carried at amortized cost less bonuses, discounts and valuation adjustments. In addition to individual write-downs to take account of specific risks, the overall credit risk is reflected by recognizing receivables at the net present value of anticipated future payments.

Deferred taxes In accordance with IAS 12 “Income Taxes”, deferred tax assets and liabilities are recognized for temporary differences between valuation for the tax accounts and the consolidated financial statements for the Degussa Group. In addition, tax assets are recorded for tax-deductible loss carryforwards. The impact of changes in tax rates on tax assets and liabilities is reflected in the income tax expense for the period in which the change in the tax legislation occurs. Where the realization of deferred tax assets is unlikely, they are written down. Where the specifications of IAS 12 are met, deferred taxes are recognized for temporary differences between the taxable valuations of the companies included in the consolidated financial statements for the Degussa Group and the balance of the assets and liabilities of these companies.

Performance-related remuneration The Degussa Long-Term Incentive Plan is a performance-related compensation plan for senior executives and members of the Board of Management. The related liabilities are determined in accordance with IAS 19 “Employee Benefits” and recognized in the income statement. For further details see Note (29).

Accumulated other comprehensive income This item comprises the following changes in shareholders’ equity that are not recognized in the income statement: foreign currency translation adjustments since January 1, 2003, unrealized gains and losses from the mark-to-market valuation of available-for-sale securities, the effect of successive acquisitions of shares in companies (component accounting) and the changes in the market value of derivative financial instruments held as cash-flow hedges and net investment hedges and the related deferred taxes.

Provisions for pensions Degussa utilized the option permitted by IFRS 1 and recognized all actuarial gains and losses on defined-benefit obligations at the time of transition from GAAP to IFRS in the IFRS opening balance sheet as of January 1, 2003 (fresh start).

Commitments under defined benefit pension and healthcare plans are recognized in accordance with IAS 19 “Employee Benefits” using the projected unit credit method. In future, anticipated adjustments in salary and pension payments will be included when calculating the defined benefit obligation. The future service cost is calculated from the expected change in the net present value of pension obligations. Differences between the forecast and actual pension obligations at year end and discrepancies between the forecast and actual present value of plan assets (actuarial gains and losses) at year end are spread over the expected remaining service lives of future pensioners, providing this does not exceed 10 percent of the present value of benefit obligations or assets, whichever is higher (corridor method). The pension obligations in Germany are calculated using the new Heubeck generation tables RT 2005 G. The pension obligations outside Germany are determined using country-specific parameters. The pension obligations at year end are compared with the fair value of the plan assets (funded status). Unrecognized actuarial gains and losses and past service cost are deducted from this to arrive at pension provisions, taking into account the asset ceiling specified in IAS 19.

Defined contribution plans give rise to expense in the period in which payments are made.

Other provisions Other provisions are recognized in accordance with IAS 37 “Provisions, Contingent Liabilities and Contingent Assets” and IAS 19 “Employee Benefits”, as appropriate. Provisions are set up where the Group has a legal or constructive obligation as a result of a past event and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation. If the effect of the time value of money is material, long-term provisions are discounted. The discount factors used in Europe are between 3.75 percent and 4.50 percent.

Provisions are based on payment obligations and take account of future cost increases.

Provisions are set up for the cost of dealing with environmental damage where utilization is sufficiently probable and a realistic estimate of the costs is possible. These are adjusted in line with new findings as the investigations and remediation work proceed. The level of individual provisions is affected by factors such as the extent of the contamination, required remediation work and other claims made by authorities or private individuals.

Provisions are set up for restructuring expenses when a detailed restructuring plan has been approved and the restructuring has either been publicly announced or initiated.

Liabilities Long-term liabilities and financial debt are carried at cost of acquisition less depreciation unless they represent the underlying in a fair value hedge. Short-term liabilities are recognized at payment or redemption cost. Liabilities arising from finance leases are valued at the net present value of the leasing installments when they are first recognized and subsequently carried at amortized cost.

Financial instruments Financial instruments comprise both primary financial instruments such as trade accounts receivable and payable and financial receivables and liabilities, and financial derivatives. Financial derivatives are used exclusively to hedge the risk of changes in exchange rates, the price of goods and interest rates. The principal financial derivatives used for this purpose are swaps, forward rate agreements and, to a lesser extent, options.

Derivative financial instruments are carried at fair value and recognized in other assets or other liabilities. Changes in fair value are recognized to income, except whether the derivative financial instruments form the effective portion of a cash flow or net investment hedge.

Hedge accounting of derivative financial instruments is permitted if they qualify for this under IAS 39. In cash flow hedge accounting the effective portion of any change in the fair value of derivative financial instruments used to hedge the risk of fluctuations in future cash flows is recognized directly in "accumulated other comprehensive income". This also includes the effective portion of changes in the fair value of financial instruments recognized as net investment hedges and that are used to hedge the currency risks of net investments in foreign subsidiaries.

Derivative financial instruments that are used to hedge the risk of changes in the fair value of assets or liabilities carried on the balance sheet may be recognized as fair value hedges. The impact of changes in the fair value of the derivative financial instrument on income are offset by the mark-to-market recognition of the underlying in the same income statement item.

Consolidated companies As of December 31, 2005 the fully consolidated companies in the Degussa Group comprised 82 (2004: 99) German companies and 298 (2004: 316) foreign subsidiaries. 20 companies were consolidated for the first time in 2005. The impact of the first-time consolidation of companies on the shareholders' equity of the Degussa Group is shown separately in the consolidated statement of shareholders' equity. 55 companies were no longer consolidated, mainly because of the divestment of the Proligo Group and the ESM Group and the merger of Group companies. 17 companies were included at equity (2004: 18), including 7 in Germany (2004: 6).

Recently adopted/newly applied accounting standards
As part of the Improvement Project, members of the International Accounting Standards Board (IASB) have revised IAS 8 "Accounting Policies, Changes in Accounting Estimates and Errors", IAS 16 "Property, Plant and Equipment" and IAS 24 "Related Party Disclosures". Degussa has applied these standards since January 1, 2005. They did not have any material impact on the consolidated financial statements as of December 31, 2005.

The revised version of IAS 8 stipulates retrospective application of voluntary changes in valuation and accounting policies and retrospective restatement to correct prior period errors. It thus removes the previous option of recognizing prior period adjustments in the profit or loss for the current period.

The revised version of IAS 16 details directly allocable costs and costs that cannot be capitalized when recognizing property, plant and equipment for the first time. This standard also clarifies the component accounting approach which stipulates that depreciation expense for each material component of an asset has to be calculated separately. Further, it redefines the recognition of subsequent costs.

The revised version of IAS 24 expands the definition of related parties to include parties with joint control over an entity, joint ventures in which the entity is one of the partners and post-employment benefit plans for the benefit of employees of an entity or of any entity that is a related party to that entity. It also defines the details of the compensation of key management personnel to be disclosed in the notes to the financial statements.

In November 2004 the International Financial Reporting Interpretation Committee (IFRIC) published Interpretation IFRIC 2 "Members' Shares in Co-operative Entities and Similar Instruments", which is applicable for fiscal years beginning on or after January 1, 2005. This interpretation examines the classification of shares in co-operative entities and similar interests accounted for in accordance with IAS 32 "Financial Instruments: Disclosure and Presentation". The application of this interpretation had no material impact on Degussa.

Also in November 2004, an amendment was adopted to SIC 12 "Consolidation – Special Purpose Entities". This is mandatory for business years beginning on or after January 1, 2005. Application of this amendment had no impact on Degussa.

The amendments published by the IASB to IAS 39 "Financial Instruments: Recognition and Measurement": "Fair Value Hedge Accounting for a Portfolio Hedge of Interest Rate Risk" and "Transition and Initial Recognition of Financial Assets and Financial Liabilities", which had to be applied from January 1, 2005, had no impact on Degussa.

In December 2004, IFRIC 4, Interpretation "Determining whether an Arrangement contains a Lease" ("IFRIC 4") was issued. This is mandatory for business years beginning on or after January 1, 2006. Degussa decided to apply this interpretation in its annual financial statements as of December 31, 2005. IFRIC 4 stipulates when contracts should be accounted for as leases in accordance with IAS 17 and when they do not qualify for treatment as leases. It clarifies that arrangements should be treated as leases if fulfillment of the arrangement is dependent on the use of a specific asset and the arrangement conveys a right to the use of the asset. An arrangement convey the right to use the asset if it conveys to the purchaser the right to control the use of the underlying asset. The right to control the use of the underlying asset is conveyed if the purchaser has the ability to operate the asset in his interest, the ability to control physical access to the asset or there is no other purchaser for more than an insignificant amount of the output or other utility of the asset and the price the purchaser pays for the output is not contractually fixed. First-time application of this interpretation had no material impact on Degussa.

The following new standards and amendments have to be applied by Degussa for business years starting on or after January 1, 2006 or 2007.

In December 2004 the IASB issued IFRS 6 "Exploration for and Evaluation of Mineral Resources" outlining the valuation of mineral resources and the associated assets. This standard will have no impact on Degussa.

In December 2004, the IFRIC issued IFRIC Interpretation 5 "Rights to Interests Arising From Decommissioning, Restoration and Environmental Rehabilitation Funds", which outlines the accounting treatment of fund units used to finance shutdown and recultivation expenses. This interpretation will have no major impact on the consolidated financial statements of the Degussa Group.

In September 2005, the IFRIC issued IFRIC Interpretation 6, "Liabilities Arising from Participating in a Specific Market – Waste Electrical and Electronic Equipment". This governs the extent to which provisions set up in accordance with IAS 37 "Provisions, Contingent Liabilities and Contingent Assets" apply for expenses relating to disposal obligations for privately used electrical and electronic equipment. This interpretation will have no impact on Degussa.

The IASB has also adopted amendments to IAS 19 "Employee Benefits – Actuarial Gains and Losses, Group Plans and Disclosures", IAS 39 "Financial Instruments: Recognition and Measurement": "Cash Flow Hedge Accounting of Forecast Intragroup Transactions" and "The Fair Value Option", and to IAS 39 Financial Instruments: Recognition and Measurement" and IFRS 4 "Insurance Contracts": "Financial Guarantee Contracts". Further, it has adopted amendments to IFRS 1 "First-time Adoption of IFRS" and IFRS 6 "Exploration for and Evaluation of Mineral Resources". The amendments to these standards will have no impact on Degussa.

In November 2005 the IFRIC issued Interpretation IFRIC 7 "Applying the Restatement Approach under IAS 29". This is mandatory for business years beginning on or after March 1, 2006. It outlines the restatement of comparative figures in financial statements prepared in accordance with IFRS when the country's functional currency is subject to hyperinflation which did not exist in the prior period and deferred taxes stated in the opening balance sheet have to be adjusted. According to this interpretation, IAS 29 "Financial Reporting in Hyperinflationary Economies" should be applied as if the functional currency had always been hyperinflationary. This interpretation will have no material impact on Degussa.

In August 2005 the IASB issued IFRS 7 "Financial Instruments: Disclosures". This standard is to be applied for annual periods beginning on or after January 1, 2007. It replaces IAS 30 "Disclosure in the Financial Statements of Banks and Similar Financial Institutions". At the same time, parts of

IAS 32 relating to disclosure obligations have been revised and transferred to IAS 7. It also requires the disclosure of information on the significance of financial instruments for the company's financial position and performance and contains new requirements on reporting risks associated with financial instruments. Adoption of IFRS 7 is linked to the extension of IAS 1 "Presentation of Financial Statements". Degussa will determine the impact of this standard on its reporting during 2006.

The IASB has also issued an amendment to IAS 1 "Presentation of Financial Statements – Capital Disclosures". This amendment is mandatory for business years beginning on or after January 1, 2007 but will have no impact on Degussa.

(3) Material assumptions entailing a considerable risk of a change in value

The consolidated financial statements for the Degussa Group also contain the following items whose valuation is essentially dependent upon the underlying assumptions and estimates:

Provisions for pensions The actuarial valuation of pensions is based on assumptions regarding discount rates, the expected long-term return on plan assets, future salary and pension rises and mortality rates. The expected development of healthcare costs is also taken into account. These assumptions may differ from the actual data as a result of changes in economic and market conditions and changes in the assumptions on the development of healthcare costs (e.g. as a result of healthcare reforms).

Reducing the discount rate by one percentage point increases the net present value of pension obligations (defined benefit obligation) by €1,136 million. Conversely, increasing the discount rate by one percentage point decreases the defined benefit obligation by about €927 million.

This could have a major impact on future pension expenses. For further details see Note (24).

Impairment of long-term assets Goodwill and other intangible assets are tested annually for impairment.

For this purpose, assets are valued on the basis of the company's plans using market or company-specific discount rates, taking into account expected growth rates and exchange rates. The relevant assumptions may change, leading to impairment charges in future periods. A relative increase of 10 percent in the interest rate and a relative reduction of 10 percent in the growth rate used in the perpetual annuity calculation would increase write-downs for the fiscal year by €147 million. For further details see Note (11).

Environmental provisions Provisions are set up for the cost of eliminating environmental damage where utilization is sufficiently probable and the costs can be estimated realistically. The level of individual provisions is affected by factors such as the extent of the contamination, required remediation work and other claims made by authorities or private individuals. Provisions may have to be modified as a result of changes in these factors. Degussa could be exposed to additional remediation requirements as a result of changes in the law. For further details see Note (31).

Provisions for legal risks It is not possible to predict accurately the likely outcome of legal disputes on product liability, patent rights, antitrust law and other statutory and contractual provisions. Adequate provisions for possible fines and claims for compensation are included in the financial statements of the Degussa Group where they can be estimated. The actual outcome of legal disputes may differ greatly from such estimates. For further details see Note (30).

Restructuring provisions Provisions are set up for restructuring expenses when a detailed restructuring plan has been approved and the restructuring has either been publicly announced or initiated. For this purpose, assumptions are made with regard to demolition costs, the termination of contracts, headcount reductions or pension payments. The actual values may differ from these estimates. For further details see Note (25).

Realization of deferred taxes Deferred taxes are based on the tax rates applicable on the date when temporary differences will be offset and estimates as to the probability of future tax refunds. Changes in tax rates and differences between future income and assumptions may reduce the probability of realizing tax assets resulting in a valuation adjustment. For further details see Note (14).

Useful life of long-term assets Property, plant and equipment and purchased intangible assets with a limited useful life are valued at production or acquisition cost and depreciated over their useful life using the straight-line method. Their useful life is determined on the basis of factors such as depletion, ageing, technical standards, the term of agreements, changes in demand and the availability of raw materials. Changes in these factors may reduce the useful life of an asset. In such cases, the residual carrying amount is written down over the new useful life, resulting in higher annual depreciation charges. For further details see Note (17).

(4) Segment reporting

In accordance with IAS 14 "Segment Reporting", segment reporting is based on the company's internal organization and reporting structures. On December 13, 2005 the Supervisory Board approved the organizational changes proposed by the Board of Management. Further details are given in the management report (see page 38). Since these changes only became effective on January 1, 2006, the segment data in this report are based on the old structure. Details of the segments, which are identical to the divisions at Degussa, are given below.

The Construction Chemicals Division is the world's biggest supplier of construction chemicals, systems and services for new buildings, repairs and renovation. Its product range comprises concrete admixtures, construction and oilfield polymers, flooring for sports facilities and industrial premises, paints and coatings, exterior insulation and finish systems, building systems and expansion joints. It has five business units grouped in two product-oriented business areas—Admixture Systems and Construction Systems—which are organized on a regional basis.

The Fine & Industrial Chemicals Division comprises most of Degussa's organic chemical operations. Its chief focus is on markets with above-average growth rates and it ranks among the world's leading suppliers to the agrochemicals, pharmaceuticals, specialty polymer additives, catalysis and feed additives sectors. This division is composed of five business units: Building Blocks, Exclusive Synthesis & Catalysts, Peroxygen Chemicals, C_4-Chemistry and Feed Additives.

The Performance Materials Division supplies high-quality specialties and advanced systems for industrial applications and consumer goods. Its position is based on its extensive knowledge of interfacial and polymer chemistry. Its operations are divided into three market-oriented business units: Superabsorber, Care Specialties and Oligomers & Silicones. The Water Chemicals activities also form part of this division.

The Coatings & Advanced Fillers Division specializes in products for coating and reinforcement, a field that requires competence in both chemistry and physics. It makes sure everyday products such as tires, paints and colorants are durable, easier to work and more environment-friendly. A number of products and applications are based on the knowledge of nanotechnology, where the Coatings & Advanced Fillers Division has a global edge. This division is composed of three business units: Coatings & Colorants, Aerosil & Silanes and Advanced Fillers & Pigments.

The Specialty Polymers Division develops solutions for global customers based on custom-tailored polymers and monomers. Its innovative products are used in high-growth areas such as the automotive, construction, coatings and colorants, plastics, electrical and electronics, pharmaceuticals, aviation, aerospace and lifestyle sectors. This division has four business units: High Performance Polymers, Specialty Acrylics, Methacrylates and Advanced Polymer Shapes.

Ten site service units and six multisite service units support the business units in all tasks not directly related to their operating business. They are run on commercial lines and compete with external suppliers.

Corporate comprises costs for the Corporate Center in Düsseldorf, Germany, and strategic research.

The return on capital employed (ROCE) and EBITDA margin are used as internal management parameters. ROCE is calculated from the ratio of EBIT (earnings before interest and taxes) to capital employed. The EBITDA margin comprises EIBTDA as a proportion of external sales.

The Board of Management regards EBIT as a particularly suitable yardstick for measuring the operational performance of individual segments as it contains the main variables that can be influenced by the management of the segment.

EBIT is defined as earnings before interest and taxes, after adjustment for non-operating items. The non-operating items reflect business transactions that Degussa defines for purposes of internal management as events that occur rarely and that have a material impact on the company's earnings position. As a result of adjustments the income items stated in the segment accounting may deviate from the key ratios calculated in accordance with IFRS. In fiscal 2005, the company's non-operating result was minus €982 million (2004: minus €83 million), comprising non-operating income of €95 million (2004: €108 million) and non-operating expenses of €1,077 million (2004: €191 million). The non-operating expenses mainly relate to the €836 million impairment write-down on the fine chemicals activities. They also contain restructuring expenses for these activities, expenses for antitrust proceedings, expenses relating to the optimization of the Frankfurt site, write-downs on property, plant and equipment, the shut-down of a site in the UK, expenses relating to the use of different mortality tables (Heubeck RT 2005 G), expenses for divested businesses and expenses for the “Degussa 2008” strategy program, see discussion in the management report on page 37. The income comes from the sale of the Frankfurt site, financial assets held for capital appreciation and the valuation and reversal of a write-down on an option in the joint venture European Oxo GmbH (see Notes 11 and 28). The non-operating loss of €83 million reported for 2004 contains, among other things, one-off restructuring costs, write-downs on property, plant and equipment, expenses for antitrust proceedings and income from the reversal of provisions.

Reconciliation from EBITDA to income before income taxes from continuing operations

in € million	2005	2004
EBITDA	**1,585**	**1,583**
– Depreciation	– 645	– 652
= **EBIT**	**940**	**931**
– Income from investments recognized at equity	– 39	– 24
– Non-operating result	– 982	– 83
= **Segment result**	**– 81**	**824**
+ Income from investments recognized at equity	39	24
– Net interest expense	– 104	– 102
– Interest on pension provisions	– 153	– 155
= **Income before income taxes from continuing operations**	**– 299**	**591**

Capital employed is calculated initially from the total of intangible assets, property, plant and equipment, investments, investment property, inventories, trade accounts receivable and other non-interest-bearing assets. Provisions (excluding pension provisions), trade accounts payable, other non-interest-bearing liabilities and deferred tax liabilities are deducted from this. In fiscal 2005 other long-term interest-bearing provisions were no longer deducted from capital employed. The prior-year figures have been restated accordingly. This change of definition increased capital employed by €897 million in 2005 (2004: 922 million).

The capital employed recognized under Corporate also contains purchase price adjustments in connection with the purchase method used to account for the Degussa/Hüls and VEBA/VIAG mergers. This item also includes purchase price adjustments relating to the revaluation of minority shareholdings in SKW. At year end these valuation differences included €505 million (2004: €607 million) which increases the capital employed assigned to this item. In addition, goodwill from the acquisition of Laporte is assigned to Corporate as a result of synergies.

Reconciliation from segment assets to total assets

in € million	**2005**	2004
Segment assets	11,587	11,510
+ Carrying amounts of associated companies	221	255
+ Deferred taxes	643	574
+ Financial receivables	190	301
+ Income tax receivables	65	125
+ Liquid assets	211	191
+ Receivables on pension provisions	0	6
+ Discontinued operations	581	671
= **Total assets**	**13,498**	**13,633**

Reconciliation from segment liabilities to total shareholders' equity and liabilities

in € million	**2005**	2004
Segment liabilities	3,012	2,823
+ Shareholders' equity	4,186	4,681
+ Pension provisions	2,890	2,832
+ Deferred taxes	621	596
+ Financial liabilities	2,373	2,337
+ Income tax liabilities	288	229
+ Discontinued operations	128	135
= **Total shareholders' equity and liabilities**	**13,498**	**13,633**

Segment reporting by divisions

in € million[1]	Construction Chemicals 2005	Construction Chemicals 2004	Fine & Industrial Chemicals 2005	Fine & Industrial Chemicals 2004	Performance Materials 2005	Performance Materials 2004
External sales	1,968	1,788	3,282	3,038	1,761	1,598
Intersegment sales	0	0	182	196	25	14
Total sales	1,968	1,788	3,464	3,234	1,786	1,612
Income from investments recognized at equity			8	– 2	17	15
Carrying amounts of investments recognized at equity			27	17	63	64
EBITDA	269	251	380	439	233	244
EBIT	223	201	212	263	156	166
Capital employed (Dec. 31)	1,475	1,327	2,083	2,322	1,042	972
Capital employed (annual average)	1,401	1,332	2,203	2,307	1,007	964
ROCE in %[2]	15.9	15.1	9.6	11.4	15.5	17.2
EBITDA margin in %[2]	13.7	14.0	11.6	14.4	13.2	15.3
Capital expenditures						
Intangible assets, property, plant and equipment	51	52	245	263	87	93
Depreciation[3]						
Intangible assets, property, plant and equipment	47	49	170	188	80	79
Segment result as defined by IFRS	204	192	– 681	186	137	167
Segment assets as defined by IFRS	1,472	1,373	3,200	3,804	1,364	1,233
Segment liabilities as defined by IFRS	419	359	645	573	272	202
Employees (Dec. 31)	7,685	7,388	8,761	8,181	3,838	3,743

[1] Discontinued operations have been stripped out of the prior-year figures.
[2] Percentages calculated from original values.
[3] Excluding impairment write-downs, c.f. (11), (17).

Segment reporting by region

in € million	Germany 2005	Germany 2004
External sales	**3,269**	**3,046**
Capital expenditures		
Intangible assets, property, plant and equipment	429	379
Segment assets as defined by IFRS	**6,172**	**6,206**
Employees (Dec. 31)	25,415	25,909

	Coatings & Advanced Fillers		Specialty Polymers		Total segments		Services		Corporate		Continuing operations	
	2005	2004	**2005**	2004	**2005**	2004	**2005**	2004	**2005**	2004	**2005**	2004
	2,279	2,190	1,688	1,420	10,978	10,034	740	667	34	39	11,752	10,740
	24	34	11	13	242	257	1,167	1,111	45	91	1,454	1,459
	2,303	2,224	1,699	1,433	11,220	10,291	1,907	1,778	79	130	13,206	12,199
	4	3	10	8	39	24					39	24
	91	75	43	103	224	259			– 3	– 4	221	255
	419	458	277	250	1,578	1,642	138	122	– 131	– 181	1,585	1,583
	289	330	194	178	1,074	1,138	60	46	– 194	– 253	940	931
	1,749	1,584	1,090	929	7,439	7,134	494	452	1,575	2,153	9,508	9,739
	1,666	1,595	1,009	975	7,286	7,173	474	484	1,864	2,235	9,624	9,892
	17.3	20.7	19.2	18.3	14.7	15.9					9.8	9.4
	18.4	20.9	16.4	17.6	14.4	16.4					13.5	14.7
	169	138	88	68	640	614	138	95	36	13	814	722
	130	127	82	72	509	515	72	76	62	70	643	661
	257	325	175	171	92	1,041	86	3	– 259	– 220	– 81	824
	2,738	2,534	1,439	1,170	10,213	10,114	1,117	1,110	257	286	11,587	11,510
	453	420	349	311	2,138	1,865	596	557	278	401	3,012	2,823
	6,219	6,373	4,284	3,632	30,787	29,317	12,090	12,387	684	566	43,561	42,270

	Other European countries		NAFTA		Asia		Latin America		Africa, Australia		Continuing operations	
	2005	2004	**2005**	2004	**2005**	2004	**2005**	2004	**2005**	2004	**2005**	2004
	3,793	**3,499**	**2,370**	**2,082**	**1,626**	**1,494**	**413**	**345**	**281**	**274**	**11,752**	**10,740**
	200	191	78	90	93	54	9	5	5	3	814	722
	1,994	**2,629**	**2,012**	**1,560**	**1,102**	**868**	**186**	**144**	**121**	**103**	**11,587**	**11,510**
	6,578	6,734	5,421	4,851	4,975	3,599	664	679	508	498	43,561	42,270

The regional breakdown of sales is based on point of sale.

(5) Major acquisitions

In June 2005 the Specialty Polymers Division acquired the other half of the US company CYRO Industries, Rockaway, NJ, USA, from its previous joint venture partner for a purchase price of US$ 95 million (€74 million). The company, which was previously recognized at equity, has been consolidated since then. The acquisition strengthens the division's activities in methylacrylate chemicals.

This was also the largest acquisition made in 2005. A number of smaller acquisitions were made to round out Degussa's business portfolio.

The Construction Chemicals Division expanded its market position by acquiring the Acrocrete business in the USA in August, which includes façade coating and stucco systems. In December, Beijing Xinzhuang Huiquiang Admixture Company Ltd., China, a major local producer of concrete admixtures, was acquired in the key Beijing market.

The Fine & Industrial Chemicals Division acquired majority stakes in a number of joint ventures in China that manufacture and market products for animal feeds, agrochemicals and preproducts for UV stabilizers.

In May the Performance Materials Division acquired all shares in Ratec International GmbH, Germany, a producer of release agents for demolding polyurethane, with retroactive effect.

In June, the Specialty Polymers Division took an 80 percent interest in the newly formed joint venture JIDA Degussa High Performance Polymers Changchun Co. Ltd., China, to expand its range of high-performance polymers.

In June 2004 the Fine & Industrial Chemicals Division acquired all shares in Agroferm Hungarian-Japanese Fermentation Industry Ltd. (Agroferm), from Kyowa Hakko Kogyo Co., Ltd., Tokyo, Japan. This Hungarian company, which has 160 employees, generated sales of €25 million.

The following transactions were undertaken between January and July 2004:

The Fine & Industrial Chemicals Division acquired the hydrogen peroxide operations of PT Risjad Brasali Industries, Indonesia. In Eastern Europe the Construction Chemicals Division acquired Woermann Slovakia s.r.o., Slovak Republic and Woermann BH d.o.o., Bosnia Herzegovina. It also raised its interest in Iranian Degussa Construction Chemicals Co Ltd., which is now included in the group of consolidated companies. The Coatings & Advanced Fillers Division raised its stake in the Turkish company Egesil Kimya Sanayi ve Ticaret A. S. to over 50 percent, so this company is now consolidated. The Specialty Polymers Division acquired all shares in Mönch GmbH, Germany.

The overall impact of the acquisitions made in 2005 and 2004 on the consolidated financial statements of the Degussa Group was not material.

(6) Major divestments

The following major operations were divested:

In February 2005 Degussa divested its Fruit Systems Product Line to the US financial investor Speyside Equity LLC, Delaware, USA. This business, which was recognized in assets/liabilities held for sale in 2004, was part of Food Ingredients, which has been classified in discontinued operations since mid-2005.

At the end of March 2005 the Fine & Industrial Chemicals Division divested the BDF business and the Rotherham site to the British company Victrex plc.

With effect from the start of April 2005 Degussa sold the Proligo Group, Boulder, Colorado, USA, to the life-science company Sigma-Aldrich, St. Louis, Missouri, USA. The Proligo Group operates in the field of nucleic acids and the synthesis of oligonucleotides.

In September 2005 Degussa sold the Food Ingredients Business Unit to Cargill, Minneapolis, USA, for a gross price of €540 million. This transaction has not yet been closed because the European antitrust authorities have not yet given their approval.

In October 2005 Degussa divested the ESM Group Inc., Amherst, New York, USA, the final part of the former metallurgical operations, to the US financial investor Platinum Equity, Los Angeles, USA. The purchase price was US$ 55 million (€44 million) and the transaction was closed in December.

The following activities were divested in 2004:

The metallurgical operations were almost completely divested for €72 million. This stepwise divestment took place in three parts with economic effect from January 1, 2004.

The divestment of the global foundry products business to Süd-Chemie AG, Munich, Germany, took place in April 2004 and included the deconsolidation of three companies.

The sale of Stollberg Group to the Greek company S&B Industrial Minerals S.A. was closed in June 2004. This transaction comprised the divestment of five companies and stakes in two further companies.

The transfer of the steel technology business to the German private equity investor ARQUES Industries AG, Starnberg, took place in August 2004. This comprised the divestment of a further nine companies and additional shares in one company.

The sale of the vitamin B_3 business to Reilly Antwerp N.V., a wholly owned subsidiary of Reilly Industries, Indianapolis, USA, was completed in April 2004.

Effective July 1, 2004 Degussa's site in Radebeul near Dresden, Germany, (chemical synthesis/active ingredients) was sold to the German pharmaceuticals producer HEXAL AG, Holzkirchen. This transaction was part of the restructuring of the Fine Chemicals operations.

For further details see Note (7).

Notes to the Income Statement for the Degussa Group

(7) Discontinued operations/assets held for sale

The earnings stated for discontinued operations contain income and expense items until closing of the transaction and the proceeds of the divestment. The impact on the income statement was almost entirely due to divestments in fiscal 2005. Only a small proportion related to transactions in previous years. In fiscal 2005 the Proligo Group, the ESM Group and the Food Ingredients activities were classified as discontinued operations. Assets held for sale mainly comprised the Water Chemicals activities (disposal group), which are assigned to the Performance Materials Division.

The expected adverse earnings impact of the disposal of the Proligo Group, which was divested in 2005, was recognized almost entirely as an impairment write-down in fiscal 2004.

Since the European antitrust authorities have not yet given their approval for the divestment of the Food Ingredients activities, the relevant companies could not be deconsolidated in 2005, nor was it possible to recognize a gain on the divestment of these activities. Current income and expenses also contain the divestment of the Fruit Systems Product Line which was recognized as a disposal group as in the previous year.

In connection with the planned divestment of the Water Chemicals activities, assets of €121 million and liabilities of €41 million were classified as assets and liabilities held for sale. €5 million of this amount comprises intangible assets, €37 million comprises property, plant and equipment, €30 million comprises inventories and €49 million comprises receivables and other assets. The liabilities are subdivided into €15 million in liabilities and €26 million in provisions.

Further assets totaling €6 million and liabilities of €2 million were reclassified to assets and liabilities held for sale. Almost all of the assets related to the interest in a non-consolidated associated company.

The earnings impact of businesses divested in previous years was minus €1 million (2004: minus €25 million). These are one-off expenses.

The following activities were classified as discontinued operations in 2004:

The foundry operations, Stollberg and most of the steel technology operations grouped in the non-core metallurgical business were sold separately; see Note (6). This divestment comprised 17 companies and stakes in three further companies. The business of the ESM Group was also included in discontinued operations.

As a result of the decision to examine the options available and divest the Proligo Group, these activities were also classified as discontinued operations in 2004.

The Fruit Systems Product Line (disposal group) was reclassified from the Performance Materials Division to assets held for sale in fiscal 2004. Assets of €35 million and liabilities of €6 million were therefore transferred to this item. €18 million of this amount comprised property, plant and equipment, €12 million comprised inventories and €5 million comprised receivables and other assets. The liabilities were subdivided into €4 million liabilities and €2 million provisions.

In addition, this item contained €2 million relating to a range of other Group companies.

The table shows the main impact of discontinued operations on the income statement.

Main impact on the income statement

in € million	2005 Income	2005 Expenses	2005 Divestment proceeds	2005 Earnings	2004 Income	2004 Expenses	2004 Divestment proceeds	2004 Earnings
Metallurgical operations	113	103	– 12	– 2	217	210	– 47	– 40
Proligo	7	8	– 2	– 3	33	81	0	– 48
Food Ingredients	473	457		16	513	488	0	25
VIATRIS	0	0	– 1	– 1	0	0	– 19	– 19
Gelatines	0	0	0	0	0	0	– 5	– 5
Other	0	0	0	0	0	0	– 1	– 1
Total	**593**	**568**	**– 15**	**10**	**763**	**779**	**– 72**	**– 88**
Tax income/expense		38	– 7	31		2	– 21	– 19
Net		**606**	**– 8**	**– 21**		**781**	**– 51**	**– 69**

Sales from discontinued operations are not included in the income statements for 2004 and 2005. The income after taxes from discontinued operations or the after-tax proceeds of their divestment is stated separately in the consolidated income statement for the Degussa Group before net income.

The table below shows the main impact of discontinued operations on the balance sheet.

Main impact on the balance sheet

in € million	2005 Metallurgical operations	2005 Proligo	2005 Food Ingredients	2005 Total	2004 Metallurgical operations	2004 Proligo	2004 Total
Property, plant and equipment	0	0	143	143	12	18	30
Other long-term assets	0	0	143	143	0	21	21
Inventories	0	0	149	149	27	7	34
Trade accounts receivable	0	0	76	76	8	6	14
Other receivables	1	0	0	1	2	2	4
Other short-term assets	0	0	69	69	1	3	4
Total assets	**1**	**0**	**580**	**581**	**50**	**57**	**107**
Pension provisions	0	0	7	7	0	1	1
Trade accounts payable	0	0	36	36	5	1	6
Other short and long-term liabilities	2	0	83	85	0	5	5
Total liabilities	**2**	**0**	**126**	**128**	**5**	**7**	**12**

The relevant asset and liability items have been reclassified in the consolidated balance sheet and are stated under “discontinued operations/assets held for sale” or “discontinued operations/liabilities held for sale”.

(8) Sales

The continuing operations generated sales of €11,752 million (2004: €10,740 million). A breakdown of sales by segment and region is given in Note (4).

(9) Other operating income

in € million	2005	2004
Income from exchange-rate differences	191	76
Income from the disposal of long-term assets	92	49
Income from the release of provisions	67	94
Other trade income	21	17
Income from the reversal of write-downs of assets	11	5
Other reimbursements, grants and subsidies	9	11
Other	142	142
Other operating income	**533**	**394**

Income resulting from differences in exchange rates is stated gross because the extensive hedge accounting prescribed by IAS would be extremely time-consuming. The actual hedging of exchange rate risks for the Group takes the form of macro hedges on a net basis. The income relating to differences in exchange rates has to be set against expenses relating to differences in exchange rates, which should be viewed together from an economic viewpoint.

Income recognized in 2005 from the disposal of long-term assets mainly relates to the sale of property, plant and equipment. A large proportion comprises the sale of Degussa’s premises in Frankfurt and the divestment of the BDF business. €58 million of this is included in non-operating income. In 2004 income from the disposal of long-term assets mainly comprised the sale of financial assets held for capital appreciation. €30 million relating to this was recognized as non-operating income.

Income resulting from the release of provisions in fiscal 2005 chiefly related to other provisions, which contained a number of separate items, and to a lesser extent to provisions for restructuring. €12 million (2004: €70 million) of this was released to non-operating income. In 2004 reversals of provisions mainly related to restructuring provisions. Provisions are released when use is no longer probable.

Income from write-backs of noncurrent assets totaling €6 million (2004: €4 million) are reflected in the non-operating result.

The other income refers to a number individual items such as income from previous years, income from the reversal of write-downs on current assets, income from embedded derivatives and subsidies for research projects. In fiscal 2005 €19 million of this was booked to non-operating income (2004: €4 million).

(10) Other operating expenses

in € million	2005	2004
Exchange-rate differences	179	83
Restucturing expenses	61	75
Losses on the disposal of long-term assets	52	20
Project expenses	31	17
Write-downs on receivables	24	21
Cartel proceedings and expenses relating to price-fixing	19	19
Other trade accounts passed on	15	12
Other	250	158
Other operating expenses	**631**	**405**

The majority of restructuring expenses, €57 million (2004: €61 million), are recognized as non-operating expenses. A large proportion of the restructuring costs relate to the refocusing of the Fine & Industrial Chemicals Division. In 2004, restructuring expenses also related principally to the Fine & Industrial Chemicals Division.

€31 million of the losses on the disposal of long-term assets impacted the non-operating result, compared with €5 million in 2004. Significant sums relate to businesses divested in previous years, the sale of Degussa's premises in Frankfurt and the streamlining of the product portfolio in connection with the restructuring of Fine & Industrial Chemicals.

As in the previous year, expenses for cartel proceedings in connection with price-fixing are included in the non-operating result.

The remaining operating expenses relate to expenses for additions to environmental provisions and miscellaneous provisions, write-downs on software and licenses, expenses for embedded derivatives, expenses relating to previous years, fees, contributions, outsourcing costs, donations, fees for advisory and assessment services, the cost of the "Degussa 2008" strategy program, expenses for training more young people than the company requires, litigation expenses, other taxes, modernization costs, one-off charges relating to actuarial adjustments as a result of the use of new mortality tables, and removal and idling costs.

€111 million of other operating expenses were stated under non-operating income. The €38 million recognized in 2004 included €4 million for environmental protection.

(11) Impairment charges on long-term assets

Goodwill and other intangible assets with an indefinite useful life: The annual impairment test on goodwill and other intangible assets with an indefinite useful life in the cash generating units was carried out as of September 30, 2005. IAS 36 "Impairment of Assets" states that an impairment charge must be taken if the recoverable amount of a cash generating unit is below its carrying amount. The recoverable amount is defined as the higher of its fair value or value in use. Degussa has identified the business units—a reporting level below its divisions—as cash generating units.

Degussa determined the fair value of all cash generating units as the recoverable amount. The starting point for this comprised expected future cash flows based on the mid-term budget drawn up by the Board of Management. This includes all major parameters affecting the cash flow of each cash generating unit and is based on uniform assumptions on key exchange rates, raw material prices, growth rates in major regional markets and personnel expenses. In the five-year detailed planning period, it is assumed that cash flows will grow by 1.5 percent.

The expected future cash flows were discounted using the weighted average cost of capital (WACC). These were derived from the level of debt and the cost of equity and debt at peer group companies with the aid of capital market models. The specific business risks of each business unit were reflected by a discount or premium. The discount rates derived in this way were between 5.6 percent and 6.2 percent after taxes. After deducting interest-bearing net liabilities, the net present value of cash flows obtained in this way was compared with the carrying amount of the cash generating units. In this way, the difference between the allocated assets (including goodwill) and debt was calculated.

The fair value of two cash generating units classified as discontinued operations or assets held for sale was not derived from planned cash flows. In these two cases, the offers obtained as part of the divestment process were used to derive their fair value.

In fiscal 2005 the impairment test specified by IAS 36 resulted in a total impairment charge of €836 million on the Fine & Industrial Chemicals Division as its carrying amount was above its recoverable value. This was attributable to unsatisfactory business trends and a sharp reduction in earnings prospects for three business units: Building Blocks, Exclusive Synthesis & Catalysts and Peroxygen Chemicals. €712 million of the €836 million write-down related to goodwill and €124 million to long-term assets (see next section). The carrying amounts were written down via the non-operating result. A large proportion of the impairment charge relates to the former British fine chemicals group Laporte, which was acquired in 2001. No impairment was established for the other cash generating units.

Since 2004, when no impairment was ascertained, the business situation and market prospects of the fine chemicals activities have been well below expectations due to substantial overcapacity and rising competitive pressure, especially from Asian suppliers. Degussa therefore stepped up the restructuring of its fine chemicals activities significantly. This resulted in additional non-operating expenses of €18 million; see Note (10).

Other long-term assets For the reasons outlined above, impairment write-downs totaling €124 million were also taken on long-term assets with a definite useful life at various sites used by the Fine & Industrial Chemicals Division. The recoverable amount of these assets corresponded to their value in use. €2 million of these write-downs related to intangible assets. €27 million of the write-down on property, plant and equipment related to land and buildings, €93 million related to technical equipment and machinery and €2 million to other property, plant and equipment. In the previous year, the Fine & Industrial Chemicals Division made a €27 million write-down on property, plant and equipment.

An impairment test was also carried out on other business units in the light of present market trends and planning data. Expected future cash flows were discounted using the weighted average cost of capital and the results were compared with carrying amounts of the assets. The discount rates were between 5.6 percent and 6.2 percent after taxes. This revealed impairment of €34 million (2004: €15 million). €2 million of this related to intangible assets (2004: €6 million), €17 million was for land and buildings (2004: €7 million), €13 million for technical equipment and machinery (2004: €29 million) and €2 million for other property, plant and equipment.

The Coatings & Advanced Fillers Division reported impairment of €5 million at the site in Mobile, USA (2004: €5 million). €1 million of this related to land and buildings and €4 million related to technical equipment and machinery.

Services took an impairment write-down of €5 million on property, plant and equipment at the Marl site in Germany.

The Performance Materials Division reversed the write-down of a plant at its site in Greensboro, USA, which had been mothballed in 2001. This resulted in other operating income of €3 million. In 2004 this division recorded write-downs of €3 million on production facilities and €1 million on buildings.

Land and buildings relating to acquisitions and mergers were recognized at fair value on the date of acquisition. A write-down of €15 million (2004: €33 million) was taken to reflect reductions in fair value.

In 2005 €148 million of the impairment charges on other property, plant and equipment were recognized in the non-operating result (2004: €65 million). Further, the non-operating result contained a €6 million reversal of a write-down on the joint venture European Oxo GmbH in the Fine & Industrial Chemicals Division. This was reported in other operating income in the income statement (2004: write-down of €6 million); see Note (19).

(12) Net interest expense and other financial income

in € million	2005	2004
Income from securities and loans held as financial assets	11	17
Other interest and similar income	42	45
Interest and similar expense	– 310	– 319
Net interest expense	**– 257**	**– 257**

The net interest expense of €79 million (2004: €78 million) for financial liabilities includes expenses of €2 million for the ineffective portion of fair value hedges. Changes in the fair value of interest/currency swaps have no impact on the net interest position because they are recognized as cash flow hedges. Interest expense comprises interest on long-term provisions of €35 million (2004: €35 million), interest expense for pension provisions of €153 million (2004: €155 million) and capitalized interest of €10 million (2004: €11 million). All three items were basically unchanged year-on-year.

in € million	2005	2004
Income from investments	6	6
Write-downs on long-term financial assets and marketable securities	– 1	– 3
Other financial income	**5**	**3**

(13) Income from investments recognized at equity

in € million	2005	2004
Income from investments recognized at equity	42	30
Expenses for investments recognized at equity	– 3	– 6
Income from investments recognized at equity (net)	**39**	**24**

Income from investments recognized at equity in 2005 includes the proportionate income from Syncserv Ltd. up to March 31, see Note (6) and from CYRO Industries up to May 31, see Note (5).

In fiscal 2004 this item mainly related to a restructuring provision at the joint venture European Oxo GmbH.

(14) Income taxes on continuing operations

As of December 31, 2005 short and long-term deferred tax assets relating to German companies were calculated on the basis of the tax rates applicable since January 1, 2004: a corporation tax rate of 25 percent, a solidarity surcharge of 5.5 percent and an average trade profit tax (after corporation tax) of 13 percent. The total tax rate derived from this was 39 percent. Deferred taxes for foreign companies are calculated on the basis of country-specific tax rates.

Total tax expense was €159 million in 2005 (2004: €213 million). It was broken down as follows:

in € million	2005	2004
Current income taxes	209	180
thereof German corporation tax	60	16
thereof German trade profit tax	21	44
thereof foreign income tax	128	120
Deferred taxes	– 50	33
thereof German	25	11
thereof foreign	– 75	22
Income tax expense for continuing operations	**159**	**213**

Tax benefits totaling €10 million relating to purchase accounting were offset against goodwill without any impact on income in 2005 and previous years. The effective tax rate in fiscal 2005 was minus 53.4 percent (2004: 36 percent). The difference between the actual tax rate and the Group tax rate of 39 percent, which contains German corporation tax, the solidarity surcharge and taxes on trade profit, is calculated as follows:

in € million	**2005**	2004
Calculated corporation tax based on a tax rate of 39%	– 117	230
Change in the basis for calculating German trade profit tax	3	– 2
Difference from foreign tax rates	– 19	– 22
Changes in tax rate	0	4
Tax effect of:		
Tax-free income	15	– 18
Other permanent differences/non-deductible expenses	– 4	4
Change in the utilization of loss carryforwards	8	– 37
Income from investments recognized at equity	– 8	0
Non-tax-deductible write-downs on goodwill	278	0
Tax expense relating to prior periods	88	48
Other	– 85	6
Income tax expense for continuing operations	**159**	**213**

The change in loss carryforwards and non-periodic tax expense relates principally to a completed tax audit at Degussa AG for the period 1994 to 1998 and the adjustment of tax accounts in the following years. The biggest single item is €278 million relating to the write-down of goodwill which is not tax-deductible, see Note (11).

Earnings before income taxes were split between Germany and other countries as follows:

in € million	**2005**	2004
Germany	76	199
Foreign countries	– 375	392
Total	**– 299**	**591**

The table below provides a detailed overview of the deferred tax assets relating to individual items calculated in accordance with IFRS:

Deferred tax assets

in € million	2005	2004
Intangible assets	26	20
Property, plant and equipment	75	67
Other investments and other financial assets	15	13
Inventories	96	93
Receivables and other short-term assets	13	14
Loss carryforwards and tax credits	223	233
Provisions and liabilities	445	446
Other	142	52
Subtotal	**1,035**	**938**
Write-downs	– 19	– 26
Netting at individual legal entities	– 373	– 317
Deferred tax assets	**643**	**595**
thereof long-term	437	441

In view of the earnings reported by subsidiaries in the past and the results they are expected to report in the future, the future taxable income of these subsidiaries will probably be sufficient to realize the related deferred tax assets. A valuation adjustment has been recorded for deferred assets to which these assumptions do not apply. Degussa has recognized deferred tax assets of €182 million which it considers reasonable in the light of its tax planning.

Deferred tax liabilities are materially affected by purchase price accounting:

Deferred tax liabilities

in € million	2005	2004
Intangible assets	245	243
Property, plant and equipment	475	460
Other investments and other financial assets	2	1
Inventories	77	60
Receivables and other short-term assets	64	49
Provisions and liabilities	95	49
Other	36	61
Subtotal	**994**	**923**
Netting at individual legal entities	– 373	– 317
Deferred tax liabilities	**621**	**606**
thereof long-term	460	450

At year-end, the loss carryforwards were as follows:

in € million	2005	2004
Loss carryforwards in Germany		
Corporation tax	511	272
Trade profit tax	1,229	734
Loss carryforwards in other countries	455	530

In Germany losses can be carried forward indefinitely. In view of the time lag on the utilization of loss carryforwards in Germany, no deferred taxes were recognized for loss carryforwards of €270 million relating to corporation tax and €494 relating to trade profit tax. Foreign loss carryforwards can either be carried forward indefinitely or expire on the dates shown in the following table:

Foreign loss carryforwards

Year of expiration	in € million
2006	8
2007	5
2008	2
2009	3
2010	1
After 2010	340
Unlimited	96
Total	**455**

The sum of positive temporary differences between the taxable valuations of the companies included in the consolidated financial statements for the Degussa Group and the balance of assets and liabilities of these companies valued in accordance with IFRS was €504 million (2004: €589 million). Neither future payouts nor the divestment of investments is likely to result in a material tax burden in the future. Therefore, no deferred tax liabilities have been set up for this. Deferred tax assets of €87 million were recognized for the disposal of foreign investments. In the tax reconciliation this amount is stated under “Other”.

The following table shows the overall tax impact on shareholders’ equity.

in € million	2005	2004
Income taxes impacting earnings		
Continuing operations	159	213
Discontinued operations	31	– 19
Tax income/expense included in accumulated other comprehensive income	– 3	8
Total	**187**	**202**

Tax income/expense for discontinued operations mainly relates to the Food Ingredients activities, the Proligo Group and parts of the metallurgical operations. The tax income on the components of accumulated other comprehensive income was almost entirely due to the impact of the valuation of financial instruments.

(15) Minority interests

Minority shareholders' interests in income comprise an interest of €13 million (2004: €11 million) in the net income and an interest of €1 million in the net loss of fully consolidated subsidiaries.

(16) Additional information in accordance with § 315 a HBG

Personnel expenses

in € million	2005	2004
Wages and salaries	2,306	2,236
thereof discontinued operations	95	122
Social security contributions	378	392
thereof discontinued operations	24	29
Expenses for pensions and similar obligations	153	143
thereof discontinued operations	3	5
thereof for pensions €130 million (2004: €138 million)		
Total	**2,837**	**2,771**

Expenses for pensions contain employers' contributions to defined-contribution pension plans in excess of the expenses for defined-benefit pension plans outlined in Note (24).

Average number of employees during the year
Degussa had an average of 44,874 employees in 2005 (2004: 45,661). 2,397 of them (2004: 3,255) were employed in discontinued operations.

Auditors' fees From fiscal 2005 Degussa is required to disclose the auditing fees incurred in Germany for the services of the Group auditors, PricewaterhouseCoopers AG. The auditors' fees must be broken down into fees for auditing the financial statements, other auditing and valuation services, tax consulting services and other services and stated separately for these categories.

The fees for auditing the financial statements contain all fees for auditing the financial statements of individual companies and the consolidated financial statements. This item also includes the cost of auditing corporate forms and other auditing services that the auditors are required by law to perform. In fiscal 2005 the fees amounted to €4 million.

The fees for other auditing and valuation services were €3 million and €0.8 million was charged for other services.

Tax consulting fees were immaterial in 2005.

Notes to the Balance Sheet for the Degussa Group

(17) Intangible assets, property, plant and equipment

Intangible assets

in € million	Franchises, industrial property rights and similar rights and assets and licenses on such rights and assets	Goodwill	Advance payments	Total
Cost of acquisition or production				
As of December 31, 2003	**1,168**	**2,933**	**9**	**4,110**
Additions	28	2	0	30
Acquisitions	3	8	0	11
Disposals	– 41	– 38	0	– 79
Reclassifications	13	0	– 9	4
Exchange differences	– 9	1	0	– 8
Changes in companies consolidated	3	– 7	0	– 4
As of December 31, 2004	**1,165**	**2,899**	**0**	**4,064**
Additions	19	1	0	20
Acquisitions	5	32	0	37
Disposals	– 59	– 126	0	– 185
Reclassifications	18	0	0	18
Exchange differences	16	10	0	26
Changes in companies consolidated	– 1	– 6	0	– 7
As of December 31, 2005	**1,163**	**2,810**	**0**	**3,973**
Accumulated amortization				
As of December 31, 2003	**426**	**156**	**4**	**586**
Additions in fiscal year	109	0	0	109
Impairment	6	0	0	6
Acquisitions	3	0	0	3
Disposals	– 33	0	0	– 33
Reclassifications	4	0	– 4	0
Exchange differences	– 5	0	0	– 5
Changes in companies consolidated	4	0	0	4
As of December 31, 2004	**514**	**156**	**0**	**670**
Additions in fiscal year	109	0	0	109
Impairment	4	712	0	716
Acquisitions	1	0	0	1
Disposals	– 33	0	0	– 33
Reclassifications	8	0	0	8
Exchange differences	9	0	0	9
Changes in companies consolidated	– 1	0	0	– 1
As of December 31, 2005	**611**	**868**	**0**	**1,479**
Carrying amount				
As of December 31, 2004	651	2,743	0	3,394
As of December 31, 2005	**552**	**1,942**	**0**	**2,494**

Intangible assets contain €15 million for trademarks that are not amortized because they have an indefinite useful life. Instead they are tested annually for impairment.

The residual carrying amount of goodwill is allocated among the divisions as follows:

Carrying amounts for goodwill

in € million	**Dec. 31, 2005**	Dec. 31, 2004
Divisions		
Construction Chemicals	632	627
Fine & Industrial Chemicals	162	470
Performance Materials	69	190
Coatings & Advanced Fillers	109	100
Specialty Polymers	88	69
Services	1	1
Corporate	881	1,286
Total	**1,942**	**2,743**

For impairment testing purposes and the presentation of segment assets, the goodwill recognized under Corporate is allocated among the cash generating units; see Notes (4) and (11).

Property, plant and equipment

in € million	Land, land rights and buildings, including buildings on leased land	Technical equipment and machinery	Other plant, factory and office equipment	Advance payments and construction work in progress	Total
Cost of acquisition or production					
As of December 31, 2003	**3,235**	**9,324**	**1,268**	**530**	**14,357**
Additions	39	159	65	463	726
Acquisitions	10	16	2	0	28
Disposals	– 134	– 428	– 123	– 8	– 693
Reclassifications	70	400	10	– 460	20
Exchange differences	– 28	– 121	– 8	– 4	– 161
Changes in companies consolidated	7	1	2	3	13
As of December 31, 2004	**3,199**	**9,351**	**1,216**	**524**	**14,290**
Additions	88	244	61	412	805
Acquisitions	37	106	3	1	147
Disposals	– 255	– 450	– 120	– 24	– 849
Reclassifications	53	366	12	– 450	– 19
Exchange differences	86	301	23	16	426
Changes in companies consolidated	9	– 6	– 4	0	– 1
As of December 31, 2005	**3,217**	**9,912**	**1,191**	**479**	**14,799**
Accumulated depreciation					
As of December 31, 2003	**1,523**	**7,033**	**997**	**2**	**9,555**
Additions in fiscal year	79	410	94	0	583
Impairment	40	29	0	0	69
Acquisitions	5	13	1	0	19
Reversals of write-downs	– 3	0	– 1	0	– 4
Disposals	– 88	– 376	– 113	– 1	– 578
Reclassifications	16	9	0	0	25
Exchange differences	– 14	– 87	– 6	0	– 107
Changes in companies consolidated	4	4	2	0	10
As of December 31, 2004	**1,562**	**7,035**	**974**	**1**	**9,572**
Additions in fiscal year	72	390	83	0	545
Impairment	44	106	3	1	154
Acquisitions	0	3	0	0	3
Reversals of write-downs	– 1	– 4	0	0	– 5
Disposals	– 114	– 338	– 108	– 1	– 561
Reclassifications	0	0	– 8	0	– 8
Exchange differences	29	194	17	1	241
Changes in companies consolidated	2	– 8	– 5	0	– 11
As of December 31, 2005	**1,594**	**7,378**	**956**	**2**	**9,930**
Carrying amount					
As of December 31, 2004	1,637	2,316	242	523	4,718
As of December 31, 2005	**1,623**	**2,534**	**235**	**477**	**4,869**

Reversals of write-downs in 2005 relate to plants at Greensboro in the USA and at Durban and Port Elizabeth in South Africa. In 2004 they related to a plant at the Trostberg site in Germany.

For further details of impairment, see Note (11).

(18) Investment property

In accordance with IAS 40 Degussa recognizes investment property at cost of acquisition or production less depreciation. The fair values, which were calculated using an inflation-based estimate, were essentially in line with the cost of acquisition or production less depreciation. Investment property essentially comprises land and buildings used for commercial and residential purposes that are currently let. In fiscal 2004 €7 million was reclassified from property, plant and equipment to investment property. Investment property is depreciated over 15–50 years using the straight-line method. Rental income was €5 million in 2005 (2004: €4 million) while rental expense was €4 million (2004: €4 million).

Investment property

in € million	
Cost of acquisition or production	
As of December 31, 2003	**22**
Additions	0
Disposals	– 2
Reclassifications	12
As of December 31, 2004	**32**
Additions	0
Disposals	– 6
Reclassifications	0
As of December 31, 2005	**26**
Accumulated depreciation	
As of December 31, 2003	**11**
Additions in fiscal year	1
Disposals	– 1
Reclassifications	5
As of December 31, 2004	**16**
Additions in fiscal year	1
Disposals	– 4
Reclassifications	0
As of December 31, 2005	**13**
Carrying amount	
As of December 31, 2004	16
As of December 31, 2005	**13**

(19) Investments, long-term securities and other financial assets

in € million	Investments recognized at equity	Other investments	Long-term securities	Other financial assets	Long-term securities and other financial assets (sum of columns 2 to 4)
Gross carrying amounts					
As of December 31, 2003	**296**	**138**	**42**	**187**	**367**
Additions	30	22	1	16	39
Acquisitions	4	0	0	0	0
Changes in fair value	0	0	– 1	0	– 1
Disposals	– 40	– 10	– 22	– 12	– 44
Reclassifications	2	– 47	0	23	– 24
Exchange differences	– 15	– 1	0	– 1	– 2
Change in companies consolidated	– 12	26	0	– 9	17
As of December 31, 2004	**265**	**128**	**20**	**204**	**352**
Additions	42	3	1	36	40
Acquisitions	0	0	0	0	0
Changes in fair value	0	0	1	0	1
Disposals	– 27	– 8	– 10	– 164	– 182
Reclassifications	0	0	0	0	0
Exchange differences	17	2	0	1	3
Change in companies consolidated	– 76	– 13	– 1	0	– 14
As of December 31, 2005	**221**	**112**	**11**	**77**	**200**
Accumulated depreciation					
As of December 31, 2003	**4**	**80**	**0**	**1**	**81**
Additions in fiscal year	0	0	0	0	0
Impairment	6	0	0	0	0
Reversals of write-downs	0	0	0	0	0
Disposals	– 1	– 1	0	0	– 1
Reclassifications	1	– 1	0	0	– 1
Exchange differences	0	0	0	0	0
Change in companies consolidated	0	0	0	0	0
As of December 31, 2004	**10**	**78**	**0**	**1**	**79**
Additions in fiscal year	0	0	0	0	0
Impairment	0	1	0	0	1
Reversals of write-downs	– 6	0	0	0	0
Disposals	– 1	– 9	0	0	– 9
Reclassifications	0	0	1	– 1	0
Exchange differences	0	1	0	0	1
Change in companies consolidated	– 3	– 6	0	0	– 6
As of December 31, 2005	**0**	**65**	**1**	**0**	**66**
Net carrying amount					
As of December 31, 2004	255	50	20	203	273
As of December 31, 2005	**221**	**47**	**10**	**77**	**134**

In 2004, the non-operating result included an impairment write-down of €6 million on the joint venture European Oxo GmbH. This impairment write-down was reversed in 2005 due to an improvement in business prospects.

A list of the Degussa Group's shareholdings is contained in the Commercial Register at Düsseldorf District Court (HRB 39635).

Investments recognized at equity The following table shows the main unaudited items in the income statements of material associated companies and joint ventures included in the consolidated financial statements at equity:

in € million	**2005**	2004
Sales	1,631	1,302
Net income	75	51
Long-term assets	263	424
Short-term assets	541	486
Provisions	86	125
Liabilities and deferred income	450	391
Shareholders' equity	268	394

Dividends paid by companies included at equity comprised €25 million (2004: €29 million).

The partner in Degussa's joint venture European Oxo GmbH has a call option to acquire Degussa's stake in European Oxo GmbH. In 2004 an impairment test was carried out on a scenario including exercise of this option. It was found that this would impair the carrying amount of this joint venture. In 2005 a renewed test was performed on the basis of new planning data. The result this time was an increase compared with the original carrying amount; see Note (11). The fair value of the corresponding put option (exercise date: January 1, 2008) held by Degussa is €8 million. It is recognized as a financial derivative.

Interim results have been presented by companies whose financial year is not the calendar year.

Syncserve Ltd., an associated company previously carried at equity, was divested in fiscal 2005; see Note (6). CYRO Industries Inc. has been fully consolidated since June 2005; see Note (5). Since December 31, 2005, RAG Versicherungs-Dienst GmbH has been recognized using the equity method.

(20) Inventories

Inventories of raw materials, supplies and merchandise purchased came to €463 million in fiscal 2005 (2004: €443 million), inventories of work in progress came to €84 million (2004: €89 million), inventories of finished goods and goods purchased for resale totaled €1,025 million (2004: €961 million) and emissions rights designated for use amounted to €2 million. There were no emissions rights to include in the previous year's accounts.

€146 million of total inventories (2004: €82 million) are valued at fair value less selling expenses.

Write-downs on inventories totaled €27 million in 2005 (2004: €29 million). Write-downs of €3 million (2004: €2 million) were reversed. In fiscal 2005 inventories amounted to €5,023 million (2004: €4,097 million) were recognized as expenses.

(21) Receivables and other assets

Receivables and other assets are shown in the following table:

Other assets, long-term

in € million	**Dec. 31, 2005**	Dec. 31, 2004
Receivables from financial derivatives	82	87
Trade accounts receivable	19	21
Receivables from pension obligations	0	6
Deferred assets	5	2
Other assets	12	17
of which due from related parties	0	5
Total	**118**	**133**

The receivables from pension obligations recognized in 2004 are no longer recognized as the corresponding healthcare obligations in the USA have essentially been assumed by the state; see Note (24).

Financial receivables, short-term

in € million	**Dec. 31, 2005**	Dec. 31, 2004
Financial receivables	103	82
thereof from associated companies	4	5
thereof from other related parties	67	49

Trade accounts receivable, receivables from tax assets and other assets, short-term

in € million	Dec. 31, 2005	Dec. 31, 2004
Trade accounts receivable	**1,986**	**1,847**
Receivables from tax assets	**62**	**127**
Receivables from financial derivatives	16	36
Deferred assets	51	31
Advance payments	8	13
Miscellaneous other assets	287	273
thereof from associated companies	5	3
thereof from other related parties	56	52
Other assets	**362**	**353**
Total	**2,410**	**2,327**

Income tax receivables result from claims for tax refunds for prepaid taxes in excess of the actual tax liability for the past fiscal year and preceding years and claims to refunds for previous years as a result of tax audits and withholding taxes.

The deferred assets principally related to other periods.

Write-downs on doubtful other assets totaled €21 million in fiscal 2005 (2004: €22 million).

(22) Liquid assets

This item contains checks, cash and cash equivalents and bank accounts. It includes cash and cash equivalents amounting to €3 million (2004: €1 million) with original maturities of more than 3 months.

(23) Shareholders' equity

Capital stock The subscribed capital of the company is €205,623,590.00 and is composed of 205,623,590 non-par bearer shares. As of December 31, 2005 all shares in Degussa AG were issued and outstanding.

The Annual Shareholders' Meeting on May 15, 2001 adopted a resolution creating authorized capital of up to €20 million (Authorized Capital II) up to May 14, 2006. Pursuant to § 3 paragraph 3 of the Articles of Incorporation the Board of Management is authorized to set a date from which such shares are entitled to a share of the profit that deviates from the statutory date. Subject to the approval of the Supervisory Board, the Board of Management may also decide to exclude subscription rights and may set the conditions for the capital increase including the conditions for the subscription rights and the issue of shares. The Supervisory Board may amend § 3 of the Articles of Incorporation following partial or complete utilization of the authorized capital to raise the capital stock and, after expiry of the period of authorization on May 14, 2006, if the authorized capital is not used or not used in full.

The Annual Shareholders' Meeting on May 15, 2001 also passed a resolution raising the capital stock by the creation of conditional capital of up to €30 million (Conditional Capital II). This conditional capital shall only be utilized if holders of convertible bonds or warrants from warrant bonds issued by the company and/or a wholly owned domestic or foreign subsidiary owned directly or directly by the company up to May 14, 2006 under the resolution adopted by the Annual Shareholders' Meeting of May 15, 2001 exercise their warrants and/or conversion rights or holders or creditors with an obligation to convert their rights fulfill the conditions for conversion. The new shares shall be entitled to a share of the profit from the start of the financial year in which the warrants or conversion rights are exercised or the fulfillment of the conversion obligations is met. Subject to the approval of the Supervisory Board, the Board of Management may define the conditions of the subscription rights and further details of the procedure for the conditional capital increase.

At the Annual Shareholders' Meeting on May 4, 2005, the company was authorized to buy back its own shares in an amount of up to 10 percent of the current capital stock up to November 3, 2006. The shares may be purchased on a stock market or through a public offer to all shareholders (or, insofar as is legally permitted, a public call to surrender the shares).

This authorization may also be utilized by Group companies or third parties for the account of the company or the Group companies in full or part, on one or more occasions.

In fiscal 2004 Degussa purchased a total of 97,370 of its own shares at an average price of €34.69 per share (nominal value €0.1 million = approx. 0.05 percent of the issued capital). 48,935 of these shares were sold to employees of Degussa AG and 43,445 were sold to employees of German subsidiaries at an average price of €28.49 per share as employee shares under the Degussa Investment Plan (DIP). In addition, a total of 4,990 free shares were allocated to trainees.

Notification pursuant to the German Securities Trading Act (WpHG) Degussa received written notifications pursuant to § 21, § 22 and § 24 of the German Securities Trading Act (WpHG) from E.ON AG, Düsseldorf, Germany, in communications dated February 14 and 20, 2004 and from RAG Aktiengesellschaft, Essen, Germany, in a communication dated February 2003. A further notification was received from E.ON Finanzanlagen GmbH, Düsseldorf, on December 29, 2005. Details of the content of these notifications can be found in the notes to the annual financial statements of Degussa AG for 2005.

Capital reserve In conformity with § 272 paragraph 2 of the German Commercial Code, the capital reserve for Degussa AG contains €2,165 million (2004: €3,186 million). The reduction in the capital reserve is attributable to the set-off of the net loss reported by Degussa AG. In addition, €1,939 million relating to differences in carrying amounts resulting from the transfer of assets to E.ON are allocated to the capital reserve.

Accumulated other comprehensive income

in € million	2005 Before taxes	2005 Taxes	2005 Net	2004 Before taxes	2004 Taxes	2004 Net
Accumulated other comprehensive income at start of year	– 134	– 20	– 154	– 104	– 12	– 116
Changes in unrealized gains/losses on the mark-to-market valuation of available-for-sale securities	– 5	0	– 5	– 19	– 1	– 20
Changes in unrealized gains/losses on financial derivatives used as cash flow and net investment hedges	– 11	4	– 7	15	– 7	8
Revaluation reserve for acquisitions made in stages	12	– 1	11	0	0	0
Translation differences	192	0	192	– 26	0	– 26
Accumulated other comprehensive income at year end	**54**	**– 17**	**37**	**– 134**	**– 20**	**– 154**

Group net income Group net income is available for the payment of a dividend in line with the proposal put to the Annual Shareholders' Meeting by the Board of Management.

Minority interests Other shareholders' material interests in the shareholders' equity of consolidated subsidiaries relate to Nippon Aerosil Co., Ltd. in Japan, Algorax (Pty.) Ltd. in South Africa, Degussa Construction Chemicals UAE LLC in Dubai, Insilco Ltd. in India, Degussa Sanzheng (Yingkou) Fine Chemicals Co. Ltd. and JIDA Degussa High Performance Polymers (Changchun) Co. Ltd. in China.

(24) Provisions for pensions

Degussa grants post-retirement pension benefits to virtually all employees in Germany. Outside Germany, post-retirement benefits are mainly paid to employees in the USA, Canada, the UK and Japan. The level of post-retirement benefits essentially depends on income and years of service with the company. Pension obligations in Germany are financed out of the assets held by the pension fund (Pensionskasse Degussa VVaG) and provisions, while pension plans in the USA, Canada, the UK and some other countries are funded by assets invested in external pension funds.

in € million	**Dec. 31, 2005**	Dec. 31, 2004
Provisions for pensions and other post-retirement obligations	**7,087**	**6,166**
thereof unfunded pension commitments	3,499	3,073
thereof funded/partially funded pension commitments	3,453	3,000
thereof healthcare obligations	135	93

Healthcare obligations mainly relate to retirees from US companies and amount to €134 million (2004: €90 million). Following the healthcare reform in the USA (Improvement and Modernization Act of 2003), reimbursement rights of €6 million were recognized in 2004 in connection with healthcare obligations. Since most of these obligations are now assumed directly by the state, no reimbursement rights were recognized in 2005.

The valuation and carrying amounts of pension commitments and the expenses required to cover these commitments are based on the projected unit credit method specified by IAS 19 “Employee Benefits”. Alongside pensions and pension rights acquired as of the reporting date, the valuation includes anticipated future increases in pensions and pension rights. This generally results in a higher valuation of pension obligations and expenses than under the discounted value method specified by § 6 a of the German Income Tax Act, which stipulates minimum valuation levels for financial reporting purposes.

The assumptions made when calculating the actuarial costs and liabilities and the expected return on plan assets are shown as weighted averages in the following table:

Valuation parameters

in %	International 2005	International 2004	Germany 2005	Germany 2004
Discount rate at year end	4.41	5.06	4.25	5.00
Expected rates of salary increases	2.80	2.84	2.50	2.54
Expected pension increases	1.59	1.51	1.50	1.50
Expected return on plan assets	5.5	5.4	5.0	5.0
Medical cost trend rate	10.0	9.0		
Expected return on reimbursements recognized as assets		6.0		

The assumptions made for each country are based on uniform principles, taking into account the relevant economic circumstances.

The table below shows the net present value of the defined benefit obligation for all post-retirement benefits determined in accordance with IAS 19, taking into account future pay rises.

Changes in the defined benefit obligation

in € million	2005	2004
Defined benefit obligation at start of fiscal year	**6,166**	**5,588**
Service cost: NPV of additional pension benefits earned in fiscal year	116	115
Employees' contributions	14	15
Interest on benefits earned	301	301
Additions and retirements	– 88	18
Discontinued operations	– 17	0
Changes in companies consolidated	75	– 1
Amortization of service cost for retroactive changes in pension plans	– 10	13
Plan curtailments and settlements	– 2	– 9
Actuarial losses	765	474
Pension payments	– 321	– 312
Exchange differences	88	– 36
Defined benefit obligation at year end	**7,087**	**6,166**

Actuarial losses are mainly due to a reduction in discount rates.

The value of plan assets managed by external pension funds (which do not hold any securities issued by Group companies) changed as follows during the year:

Change in plan assets

in € million	**2005**	2004
Fair value of plan assets at start of fiscal year	2,959	2,756
Expected return on plan assets	161	149
Gain on plan assets	50	49
Employers' contributions	79	140
Employees' contributions	14	15
Additions and retirements	– 116	20
Change in companies consolidated	41	0
Pension payments	– 141	– 150
Exchange differences	55	– 20
Fair value of plan assets at year end	**3,102**	**2,959**

In 2005 the return on plan assets was €211 million (2004: €198 million).

The majority of the plan assets—€2,126 million—relate to Degussa's German pension fund. The remainder relate to foreign pension plans.

The German pension plan is a defined benefit plan within the meaning of IAS 19.7. If the plan assets should be insufficient to cover commitments, higher contributions would have to be paid by all contributors and/or the company would be responsible for paying pension commitments.

The fair value of the plan assets in the German pension fund was €2 million in 2005 (2004: €42 million).

The table presents a reconciliation of the funded status based on the difference between the defined benefit obligation and plan assets, on which the provisions recognized in the balance sheet are based:

Funded status

in € million	**2005**	2004
Funded status at year end	3,985	3,207
Unrecognized service cost relating to retroactive plan changes	– 4	1
Unrecognized actuarial losses	1,099	456
Pension provisions before asset limitation	**2,890**	**2,750**
Asset limitation	0	89
Recognized pension provisions	**2,890**	**2,839**

The table shows the change in pension provisions:

Changes in provisions for pensions and other post-retirement benefits

in € million	2005	2004
Pension provisions at start of fiscal year	**2,839**	**2,865**
Net expense recognized in income statement	271	280
Actual employers' contributions to plan assets	– 79	– 140
Actual pension payments	– 180	– 162
Change in companies consolidated	24	– 5
Discontinued operations	– 17	0
Additions, retirements and other balances carried forward	16	10
Actuarial gains/losses on reimbursement claims	– 7	1
Exchange differences	23	– 10
Pension provisions at year end	**2,890**	**2,839**

Approx. 93 percent (2004: 94 percent), in other words, the vast majority of pension provisions as of December 31, 2005 relate to Germany.

The total expense for the defined benefit obligation is shown in the table:

Net benefit expense

in € million	2005	2004
Current service cost	116	115
Interest cost	301	301
Expected return on plan assets	– 161	– 146
Recognized past service cost	– 5	12
Recognized actuarial gains/losses	110	130
Effect of curtailments and settlements	– 1	– 9
Change in asset ceiling	– 89	– 123
Net benefit expense for defined-benefit plans	**271**	**280**

€1 million (2004: €5 million) of this relates to healthcare obligations.

Apart from interest expense and the expected return on plan assets, which are included in the net interest position, pension expense is recognized in the operating result. Since pension expense for the German pension plan is exactly in line with contributions as a result of the plan surplus and the resultant asset ceiling, pension expense for this plan is reflected fully in the operating result.

A further €12 million (2004: €9 million) is for defined contribution pension commitments, where the company pays fixed contributions to external plans, and for pensions and other post-retirement pension obligations. Employers' contributions to statutory pension insurance totaled €169 million (2004: €172 million).

(25) Other provisions

in € million	Personnel	Environ-mental	Pro-curement	Sales	Restruc-turing	Other	Total
Dec. 31, 2004	**847**	**184**	**50**	**99**	**50**	**380**	**1,610**
Additions	462	8	79	95	23	218	885
Utilization	– 453	– 15	– 66	– 86	– 30	– 192	– 842
Reversals	– 28	– 6	– 6	– 13	– 13	– 48	– 114
Reclassifications	– 3	0	– 17	11	14	– 39	– 34
Interest costs	27	6	0	0	1	1	35
Exchange differences	9	1	1	4	0	12	27
Changes in companies consolidated	1	0	0	0	1	7	9
Dec. 31, 2005	**862**	**178**	**41**	**110**	**46**	**339**	**1,576**
Long-term	438	161	1	18	11	178	807
Short-term	424	17	40	92	35	161	769
Total	**862**	**178**	**41**	**110**	**46**	**339**	**1,576**

The provisions for personnel expenses primarily comprise provisions for wages and salaries, social security contributions, early retirement arrangements, long-service anniversaries, severance pay and various other cost management programs and other accrued personnel expenses.

Provisions for environmental protection relate to the remedial treatment of sites/contaminated land, protection of surface water and the recultivation of landfills. This item also includes provisions for the cost of decontamination, emissions protection and monitoring and fines imposed under applicable environmental protection law.

Procurement provisions comprise obligations relating to products or services that have already been supplied or rendered but for which invoices have not yet been received.

Provisions for sales chiefly comprise guarantee obligations, outstanding commission payments and price reductions such as discounts, rebates and bonuses.

Restructuring provisions are set up for the shut-down, closure or restructuring of operations.

Other provisions principally relate to litigation risks, legal and advisory expenses and other uncertain liabilities.

(26) Liabilities

Financial liabilities, long-term

in € million	Dec. 31, 2005	Dec. 31, 2004
Bonds	1,304	1,305
Liabilities to banks	106	203
Financial liabilities to non-banks	4	55
Leasing liabilities	63	20
Other financial liabilities	4	2
Total	**1,481**	**1,585**

Bonds mainly comprise a capital market bond issued by Degussa AG in 2003 with a nominal value of €1.25 billion, which matures in 2013. This bond has been recognized at the issue price of 98.99 percent. The discount will be written back over the maturity of the bond using the effective interest rate method. In addition, on the date of issue a portion of the bond was recognized at fair value as part of a fair value hedge.

The reduction in financial liabilities to banks and non-banks in 2005 was due to early repayment of loans.

The increase in leasing liabilities was principally attributable to the sale and lease-back of the premises in Frankfurt.

Income taxes and other financial liabilities, long-term

in € million	Dec. 31, 2005	Dec. 31, 2004
Income taxes	90	53
Deferred liabilities	29	16
Liabilities relating to financial derivatives	1	1
Trade accounts payable	0	3
Other operating liabilities	14	12
Total	**134**	**85**

Long-term income tax expense contains appropriate amounts for fiscal years for which tax assessments have not yet been finalized. The increase results from additions to provisions for income taxes as part of risk provisioning.

Financial liabilities, short-term

in € million	Dec. 31, 2005	Dec. 31, 2004
Liabilities to banks	692	626
Commercial paper	152	70
Financial liabilities to non-banks	27	57
Liabilities relating to promissory notes	1	5
Leasing liabilities	7	5
Other financial liabilities	13	11
thereof due to associated companies	1	2
thereof due to other related parties	1	2
Total	**892**	**774**

In 2004 Degussa AG launched a European Commercial Paper program with a nominal volume of €750 million. At year-end, notes totaling €152 million with maturities of one to three months had been placed under this program.

Trade accounts payable, income tax liabilities and other liabilities, short-term

in € million	Dec. 31, 2005	Dec. 31, 2004
Trade accounts payable	**1,020**	**918**
Income tax liabilities	**198**	**184**
Payroll liabilties	44	45
Liabilities relating to financial derivatives	51	25
Deferred liabilities	13	18
Advance payments received	14	12
Other operating liabilities	207	233
thereof due to associated companies	9	7
thereof due to other related parties	17	22
Other liabilities	**329**	**333**
Total	**1,547**	**1,435**

Short term income tax liabilities contain income tax provisions totaling €196 million (2004: €176 million).

Payroll liabilities include vacation allowances and flextime credits. Other short-term operating liabilities include €21 million (2004: €36 million) in tax liabilities and €40 million (2004: €31 million) relating to social security contributions.

Financial liabilities are entirely comprised of interest-bearing amounts. The average interest rate is 4.4 percent and the average interest duration is 2.4 years. Bank loans with interest rates below market rates are immaterial and are recognized at nominal value. The average maturity of financial obligations is 5.1 years.

Liabilities to banks totaling €8 million (2004: €12 million) are secured by mortgages.

As of December 31, 2005, the maturity structure of financial liabilities was as follows:

Year	Maturity in € million	Interest duration in € million
2006	892	1,650
2007	46	34
2008	40	44
2009	57	57
2010	6	6
After 2010	1,332	582
Total	**2,373**	**2,373**

As of December 31, 2005 Degussa AG had committed bilateral and syndicated credit lines with banks of €222 million (2004: €1,080 million) with maturities of less than one year. A further €1,525 million (2004: €1,000 million) comprises maturities up to 2010.

(27) Contingent liabilities and other financial commitments

Contingent liabilities

in € million	**2005**	2004
Liabilities from guarantees, promissory notes and checks	24	37
Warranty commitments	68	68
Total	**92**	**105**

The contingent liabilities listed above have not been accrued as the risk of losses is considered unlikely. Commitments relating to guarantees, promissory notes and checks include guarantees amounting to €5 million (2004: €27 million) for companies consolidated at equity. Warranty commitments contain warranties for liabilities relating to companies included in the financial statements at equity of €59 million (2004: €64 million).

Guarantees relating to the divestment of operations
In agreements on the divestment of operations, Degussa has given undertakings to release the purchaser from various liabilities that were uncertain at the time of the transaction. Alongside the standard indemnification for the outcome of tax audits, these comprise a common indemnification clause for possible costs arising from environmental obligations, indemnification from product liability risks for products manufactured or sold prior to divestment and indemnification from other legal obligations.

In virtually all agreements, there is a limit to the level or period for which liability or exemptions are set.

Other financial commitments Binding orders for capital expenditures for the Group total €146 million (2004: €172 million).

For further details of product guarantees, litigation risks and environmental protection, see Notes (30) and (31).

The Degussa Investment Plan offers employees an opportunity to invest in special investment funds and Degussa stock. Degussa encourages savings under these plans through subsidies. Since they depend on the level and duration of investment, the resultant future commitments cannot yet be determined accurately.

Miscellaneous other financial commitments come to €25 million (2004: €6 million).

Leasing The company leases a variety of warehouses and production facilities. The majority of the long-term leasing agreements contain extension options and some contain purchase options. The liabilities relating to leasing agreements during the basic rental period when they cannot be terminated are outlined in the table.

in € million	Finance leases	Operating leases
2006	10	43
2007	9	39
2008	9	34
2009	9	30
2010	8	23
After 2010	40	53
Total leasing liabilities	**85**	**222**
Less interest portion	– 15	
NPV of leasing liabilities	70	

The liabilities relating to leasing agreements during the basic rental period when they cannot be terminated are as follows:

in € million	Finance leases	Operating leases
2005	5	49
2006	4	41
2007	4	37
2008	4	33
2009	4	31
After 2009	13	74
Total leasing liabilities	**34**	**265**
Less interest portion	– 9	
NPV of leasing liabilities	25	

Property, plant and equipment includes the following amounts for finance leases:

in € million	**2005**	2004
Land and buildings	59	17
Technical facilities	2	3
Factory and office equipment	2	2
Total	**63**	**22**

The sale and subsequent lease-back of Degussa’s premises in Frankfurt led to a rise in leased buildings. The net present value of these leasing liabilities is €54 million.

Rental and leasing expenses relating to operating leases amounted to €72 million in fiscal 2005 (2004: €57 million).

(28) Primary and derivative financial instruments

The carrying amounts and fair value of Degussa's primary financial instruments are shown in the table.

in € million	Carrying amount **2005**	Carrying amount 2004	Fair value **2005**	Fair value 2004
Assets				
Securities, long-term	10	20	10	20
Other financial assets	77	203	77	203
Securities, marketable	22	18	22	18
Financial receivables	103	82	103	82
Liabilities				
Bond	1,304	1,305	1,244	1,352
Banks	798	829	803	855
Commercial paper	152	70	152	70
Other	119	155	119	157

The fair value of securities and capital market paper are derived from stock market prices. For all other financial assets and liabilities, fair value is determined by discounting anticipated future cash flows using the current market interest rates on the reporting date. Primary financial instruments are only recognized in the balance sheet on the settlement date.

The reduction in financial assets is due to the repayment of vendor notes.

In the course of its business, Degussa is exposed to the risk of changes in exchange rates and interest rates. Financial derivatives are used to reduce these risks. The aim of risk management is to reduce fluctuations in earnings and cash flow in order to protect Group earnings from the risks arising from changes in interest and exchange rates.

Financial derivatives are used solely for hedging purposes, in other words, they are only used in connection with transactions originated by business operations whose risk profile is exactly opposite to that of the financial derivatives. A financial guideline issued by the Board of Management contains binding rules on the type and extent of transactions that are hedged by the Degussa Group.

Hedges are only concluded with counterparties with first-class credit standing (a rating of at least A– from Standard & Poor's and A3 from Moody's or exceptionally BBB+ and Baa1 in well-founded circumstances) within predetermined limits. Only marketable instruments with sufficient liquidity are used. Consequently, the Group has no material credit risks. The table shows a breakdown of the fair values of financial derivatives used to hedge interest and exchange rates by rating classes as of December 31, 2005.

			Derivates with positive market values	
Rating	Moody's	Standard & Poor's	in € million	in %
Investment grade	Aaa	AAA	0	0
	Aa1 to Aa3	AA+ to AA–	29	35
	A1 to A3	A+ to A–	53	64
	Baa1 to Baa3	BBB+ to BBB–	1	1
Non investment grade	Ba1 to C	BB+ to C	0	0
Not rated			0	0
Total			**83**	**100**

All hedging transactions and underlyings are registered and regularly evaluated in a Group-wide treasury management system. The positions are therefore clear and are subject to continuous risk monitoring. Trading, settlement, posting and controlling functions are separate.

Wherever possible, recognition of changes in the fair value of derivative financial instruments has been avoided by using IAS hedge accounting.

The aim of interest-rate management is to protect Group net income from the negative effects of fluctuations in market interest rates. The risk of interest rate changes is understood to mean the risk of an increase in interest expense for existing financing concluded at variable interest rates and for the financing budgeted in the mid-term financial plan (time horizon: 3 years). Interest risk is managed by using primary and derivative financial instruments (interest swaps, cross-currency interest swaps) to achieve an appropriate ratio between fixed interest rates (fixed for > 1 year) and variable rates (< 1 year), taking into account cost and risk considerations. Hedging of net financing requirements through fixed interest rates must cover at least 20 percent and a most 30 percent of the financing requirement. At year-end 2005 it was 30 percent. A general rise in interest rates of one percentage point would increase interest expense on financial obligations by about €13 million in a year.

The aim of currency management is to protect the operating business from fluctuations in earnings and cash flow. The majority of exchange rate risks related to changes in the exchange rate between the euro and the US dollar.

About US$ 5 billion (€4 billion) of Group sales were generated in US dollars or a currency tied to the US dollar in 2005. About three-quarters of this is hedged through production in the US dollar zone (NAFTA, Latin America and Asia) where costs are incurred in US dollars (natural hedges). This also reduces the economic risk that changes in exchange rates will alter the company's market position versus competitors in the US dollar zone. Most of the remaining sales in US dollars are generated through production sites in the euro zone. After deduction of costs incurred in US dollars, these sales are exposed to transaction risks as well as competitive risks. If the euro appreciates against the US dollar, exports become more expensive for customers. That can result in a drop in volumes or prices and thus trim margins. Transaction risks of this type are hedged at the latest when a binding order or binding contract is placed. The net balance of booked foreign currency receivables and payables is thus always fully hedged through derivative financial instruments (forward rate transactions and currency options).

In addition, the company pursues a consistent long-term hedging strategy: The operating units hedge planned foreign currency sales that are considered highly probable for up to 18 months on a rolling basis within predefined corridors which are set for specific time periods.

	Hedging ratio	
Planned sales	Minimum in %	Maximum in %
= 3 months	75	90
> 3 and = 6 months	50	80
> 6 and = 12 months	25	80
> 12 and = 18 months	0	80

Decisions on the hedging ratios within these corridors are taken on a case-by-case basis depending on the risk-tolerance of the underlying transaction and an evaluation of the risks and benefits. On the reporting date, 70 percent of planned sales in US dollars in the following 12 months were hedged through forward rate currency agreements and currency options.

Transaction risks arising from financing activities are avoided by financing investments in the local currency wherever possible. Risks relating to foreign currency translation of financial and earnings parameters for foreign companies (translation risks) are not hedged because they do not represent a cash flow risk.

If the euro were to rise by US$ 0.01 against the dollar, this would reduce EBIT for the full year by about €7 million (before hedging operations). About €5 million of this relates to transaction effects and about €2 million to translation effects. The hedging transactions outlined above reduced the transaction effect to €1.5 million a year and the overall impact to €3.5 million.

Financial derivatives are recognized immediately upon conclusion of the contract (trade date accounting). The notional value of financial derivatives, defined as the sum of all sales and purchases, and their fair value on December 31 is shown in the table: The notional values and fair values of these contracts are shown at the market prices on the reporting date.

in € million	Notional amount **2005**	Notional amount 2004	Fair value **2005**	Fair valuee 2004
< 1 year	2,701	1,954	– 30	11
> 1 year	30	4	0	0
Forward exchange contracts	**2,731**	**1,958**	**– 30**	**11**
< 1 year	25	0	0	0
Currency options	**25**	**0**	**0**	**0**
< 1 year	0	13	0	0
> 1 year	772	769	59	46
Interest swaps	**772**	**782**	**59**	**46**
> 1 year	246	246	15	40
Cross-currency interest swaps	**246**	**246**	**15**	**40**
Commodities < 1 year	**2**	**5**	**0**	**0**
Embedded derivatives > 1 year	**66**	**0**	**– 6**	**0**
Put options > 1 year	**34**	**0**	**8**	**0**
Total	**3,876**	**2,991**	**46**	**97**

As of December 31, 2005, only forward rate transactions in USD, GBP, JPY and some major European and non-European currencies were used to hedge exchange rates. The notional amount was €2,731 million (2004: €1,958 million) and the net market value was minus €30 million (2004: plus €11 million). A cross-currency interest swap concluded to hedge an intragroup loan had a fair value of €15 million on December 31, 2005 (2004: €40 million). The fair value of interest rate swaps used to hedge floating rate loans and to convert a portion of the bond issued in 2004 from fixed to floating rates was €59 million at year-end 2005 (2004: €46 million). Risks relating to the procurement of goods are hedged to a limited extent through commodity derivatives. As in the previous year, commodity derivatives totaled less than €1 million.

The fair value of embedded derivatives that qualified for separate recognition as derivatives was minus €6 million.

Degussa has a put option on one joint venture. This relates to the sale of its interest in the joint venture and is recognized on the balance sheet as a positive amount.

All derivative financial instruments are valued in the financial statements at fair value. The fair value shows how the closing out of derivatives contracts on the reporting date would affect earnings without the underlying transactions. The fair value of the financial derivatives is calculated using a Group-wide financial reporting and controlling system. As a result of market volatility, the fair value of derivative financial instruments on the reporting date may vary considerably from the current market value. The fair value of forward exchange contracts is calculated on the basis of the spot price on the balance-sheet date. A premium or discount is then applied for the exchange rate agreed in the contract. Interest swaps are valued by discounting future cash flows. This calculation is based on the market rates applicable for the residual term of the contract.

In accordance with IAS 39, the fair value of derivatives is recognized under other assets or other liabilities. Changes in fair value are recognized to income, except whether the derivative financial instruments form the effective portion of a cash flow or net investment hedge.

Where the embedded derivative has to be separated from the host contract in compliance with IAS 39.11, it is accounted for separately in the same way as other derivatives, i.e. it is recognized at fair value. Changes in fair value are recognized in the income statement in miscellaneous other income or expense.

The unrealized gains and losses on derivative financial instruments used to hedge exchange risks on items recognized in the financial statements and firm orders and contracts are reported under other operating income/expenses from exchange-rate differences. The unrealized gains/losses on these transactions are offset by a contrary movement in the value of the hedged foreign currency transactions. For all balance-sheet items denominated in foreign currencies, the market values are calculated using the spot price on the balance-sheet date. Any resultant unrealized gains/losses are also reported under other operating income/expense due to exchange-rate differences. Income and expense arising from changes in the fair values of interest swaps are booked as interest income/expense and thus impact income.

Financial derivatives used to hedge the risk of changes in exchange rates on future sales and procurement transactions are recognized as cash flow hedges. The effective portion of changes in the fair value of the derivatives is recognized in accumulated other comprehensive income. The ineffective portion of cash flow hedges came to €2 million as of December 31, 2005 and was recognized as other operating expense. As of December 31, 2005 underlyings with maturities of up to two years were included in cash flow hedging.

In 2005 cross-currency interest swaps used to hedge the cash flows from an intragroup foreign currency loan (maturity > 1 year) were recognized as cash flow hedges.

Fair value hedges are used to offset the earnings impact of the mark-to-market valuation of derivative financial instruments by revaluing the underlying. The change in the fair value of the underlying and the hedge are recognized in the same income statement item. In 2005 interest swaps used to hedge the fair value of a fixed-interest loan were accounted for as fair value hedges. The ineffective portion of fair value hedges totaled €2 million and is included in the net interest position.

Net investment hedging is used to secure the value of investments in economically independent foreign subsidiaries. Net investment hedges totaling €4 million were closed out following derecognition of some of these foreign subsidiaries.

The fair value of primary and derivative financial instruments used as cash flow hedges and net investment hedges declined by €11 million in 2005 (2004: increased by €15 million). The change in fair value was allocated directly to equity and thus had no impact on earnings. Provisions for deferred taxes were reduced by €4 million (2004: increased by €7 million).

	Cash flow hedges				Net investment hedges			
in € million	Jan. 1	Additions	Release	Dec. 31	Jan. 1	Additions	Release	Dec. 31
Fair value	18	– 10	1	9	29	0	– 2	27
Deferred taxes	– 7	3	0	– 4	– 12	0	1	– 11
Recognized in equity	11	– 7	1	5	17	0	– 1	16

(29) Performance-related remuneration

Alongside a fixed base salary and short-term incentive payments, the remuneration system for senior executives in the Degussa Group includes a long-term incentive plan (LTI Plan). The Degussa LTI Plan is a long-term compensation plan and is therefore recognized in accordance with IAS 19 "Employee Benefits".

Under this plan, Degussa offers its executives performance options. Exercising these options enables them to share in the company's development and thus in its long-term performance. The value of these options is based on key financial ratios rather than the share price.

The performance indicators defined for the Degussa LTI Plan are ROCE and EBITDA (based on outperformance of EBITDA relative to a peer group comprising specialty chemicals companies).

Members of the Board of Management and some 250 executives who hold key positions in the Degussa Group and are therefore able to exercise a significant influence on the performance of the Group are eligible to participate in the Degussa LTI Plan. The extent to which they participate in the performance of the Group depends on the number of performance options they are allocated. The number of options allocated to members of the Board of Management is set by the Executive Committee of the Supervisory Board, while the number of options allocated to other executives entitled to participate in the plan is set by the Board of Management.

The table shows the performance options allocated under the Degussa LTI Plan in 2003, 2004 and 2005:

	LTI tranche 2005	LTI tranche 2004	LTI tranche 2003
Status as of January 1	0	1,048,842	1,062,170
Allocated	1,119,751	4,400	0
Exercised	0	0	392,900
Expired	26,200	32,800	25,492
Status as of December 31	**1,093,551**	**1,020,442**	**643,778**

The 2003, 2004 and 2005 tranches of the Degussa LTI Plan each run for five years. This five-year period is divided into an initial lock-up period of two years, during which the performance options may not be exercised, followed by a three-year exercise period.

Exercise of the performance options is contingent upon achievement of a specific ROCE target. If ROCE exceeds this hurdle, the number of options that can be exercised rises in line with ROCE. The formula used to calculate this is based on the weighted average cost of capital (WACC) of the Degussa Group and is set annually for each tranche.

EBITDA is used to calculate the value of the options eligible for exercise. The value of Degussa must correspond at least to the average EBITDA performance of a peer group, otherwise the options have no intrinsic value. If EBITDA exceeds this level, the value of the options rises in line with the amount by which Degussa outperforms the peer group.

Provisions for the LTI Plan totaled €5 million in 2005 (2004: €11 million). 7 percent of this relates to members of the Board of Management of Degussa AG. The first exercise date for the 2003 tranche of the LTI Plan was in 2005. This resulted in expense of €16 million, about 7 percent of which related to members of the Board of Management.

(30) Litigation risks

Companies belonging to the Degussa Group are involved in a number of court cases and official investigations. Although there is some inherent uncertainty about the outcome of individual legal disputes, as far as can be assessed at present none of these cases will have a material impact on the Group's future financial position and earnings. Nonetheless, provisions have been set up where necessary. The cash flow could be affected by payments relating to legal disputes.

The EU Commission has fined various manufacturers of the feed additive methionine for price fixing. Degussa and the Group companies affected have appealed against the level of these fines. In this connection, a number of customers and consumers in the United States and Canada have filed class actions against virtually all producers operating on the NAFTA market to claim compensation. Degussa has reached a settlement with the majority of the plaintiffs and thus concluded the cases.

Along with other companies, Degussa and some Group companies have received complaints from the EU Commission in connection with investigations into alleged violations of antitrust law. These relate to hydrogen peroxide, perborate, percarbonate and methacrylate monomers, polymethylmethacrylate sheet, polymethylmethacrylate molding compounds and polymethylmethacrylate cast sheets for sanitary applications. In line with its corporate philosophy, Degussa is cooperating with the EU Commission on these investigations.

In the USA Degussa is being sued for compensation in connection with alleged infringement of obligations in contractual negotiations on a planned business agreement.

Degussa is involved in a number of other court cases and legal disputes relating to alleged price-fixing, including class actions in the United States and Canada. The outcome of these legal disputes cannot be predicted accurately. Adequate provisions for possible claims for compensation are included in the financial statements of the Degussa Group

Degussa is of the opinion that the resultant total payment obligations—less insurance payments or compensation from third parties where appropriate—will not be materially detrimental to the company's operating result or financial position.

(31) Environmental protection

Degussa's worldwide operations are subject to the relevant local environmental protection laws and regulations. These generally set thresholds for the release of noxious substances into the air and water and standards for the handling and disposal of hazardous substances and waste. In addition, on the basis of codified law and case law, local regulatory authorities or private individuals could make substantial claims against Degussa. The company's management assumes that the Group essentially operates in accordance with all applicable environmental regulations. To ensure this, the Board of Management has introduced mandatory guidelines on environmental protection, safety, health and quality. These are binding on all operating units worldwide. Internal audits are conducted to monitor compliance with these guidelines.

A Group-wide information system ensures that the Board of Management rapidly receives all necessary information on major incidents relating to the production, transportation and utilization of Degussa's products. In addition, the majority of production sites in Germany are certified under the voluntary EU eco audit regulation (EMAS) or the international standard ISO 14001. In 2005 the Corporate Center was also certified as complying with ISO 14001. Moreover, Degussa actively participates in the global Responsible Care initiative, a public undertaking by the chemical industry to work towards a continual improvement in environmental protection, safety, health and communication.

As of December 31, 2005 Degussa was required by local authorities to eliminate environmental damage at a number of sites. The company's policy is to set up provisions for all expenses for the remediation of environmental damage as soon as a claim appears likely and the costs can be estimated realistically. These are adjusted in line with new findings as the investigations and remediation work proceed. Total provisions for environmental protection and recultivation came to €178 million in fiscal 2005 (2004: €184 million). These relate to approximately 100 separate instances at a variety of sites. The largest of these comprises €32 million. The vast majority of environmental provisions relate to obligations to eliminate environmental damage at the company's production sites, former production sites and landfills.

At present, the company cannot make any further estimates of additional losses or the extent of possible losses in excess of the amounts already allocated to provisions.

(32) Remuneration of the Board of Management and Supervisory Board

The total remuneration of the Board of Management was €5.2 million in 2005 (2004: €4.2 million). €1.7 million (2004: €1.6 million) comprised fixed base salaries, which also cover the assumption of functions on the supervisory boards of subsidiaries, non-cash benefits and other payments. Short-term variable payments for annual bonuses totaled €2.4 million (2004: €2.6 million) and relate to the fulfillment of individually agreed performance targets. €1.1 million relates to the exercise of options from the first tranche of the LTI Plan. In addition, a total of 70,500 performance options (2004: 70,500) were issued to members of the Board of Management in 2005 under the LTI Plan. Provisions for pension commitments to members of the Board of Management total €17.3 million (2004: €12.4 million). The components of the remuneration of the Board of Management are outlined in detail in the Corporate Governance Report on page 150. The table below shows the remuneration paid to individual members of the Board of Management in 2005:

Remuneration of the Board of Management

	Annual income				Total LTI options[1]			
	Fixed salary	Variable bonus	LTI options exercised	Total	No. of options held as of Dec. 31, 2004	No. of options exercised in 2005	No. of options granted in 2005	No. of options held as of Dec. 31, 2005
	in € '000	in € '000	in € '000	in € '000				
Prof. Utz-Hellmuth Felcht	618.6	770.0	337.3	1,725.9	45,000	8,370	22,500	59,130
Dr. Alfred Oberholz	360.9	583.0	239.9	1,183.8	32,000	5,952	16,000	42,048
Dr. Thomas Schoeneberg	367.8	530.0	239.9	1,137.7	32,000	5,952	16,000	42,048
Heinz-Joachim Wagner	387.2	557.0	239.9	1,184.1	32,000	5,952	16,000	42,048
	1,734.5	**2,440.0**	**1,057.0**	**5,231.5**	**141,000**	**26,226**	**70,500**	**185,274**

[1] See also Note (29).

Assuming that the Annual Shareholders' Meeting of Degussa AG in 2006 resolves not to pay a dividend for fiscal 2005, the total remuneration of the members of the Supervisory Board would be €0.2 million (2004: €1.3 million). Members of the Supervisory Board did not receive any additional personal payments, in particular, they did not provide any advisory or intermediary services for which they received separate payment.

The table below shows the remuneration paid to individual members of the Supervisory Board in 2005:

Name in €	Notes	Fixed remuneration for 2005	Variable bonus for 2005	Total 2005	Remuneration for meetings 2005
Günter Adam	Executive Committee (from July 1, 2005)	6,250	0	6,250	3,500
Dr. Birgit Bertsch-Frank		5,000	0	5,000	3,000
Werner Bischoff	Deputy Chairman	7,500	0	7,500	4,500
Ralf Blauth	Executive Committee (until June 30, 2005)	3,750	0	3,750	3,500
Dr. Hans-Michael Gaul	Executive Committee	7,500	0	7,500	5,000
Engelbert Gerstandl		5,000	0	5,000	3,000
Ralf Hermann	Audit Committee	7,500	0	7,500	5,000
Prof. Wolfgang A. Herrmann		5,000	0	5,000	2,000
Dr. Dieter Hockel	Audit Committee	7,500	0	7,500	5,500
Dr. Manfred Krüper		5,000	0	5,000	3,000
Rainer Kumlehn		5,000	0	5,000	2,500
Dr. Werner Müller	Chairman	10,000	0	10,000	5,000
Dr. Arend Oetker		5,000	0	5,000	3,000
Roland Oetker		5,000	0	5,000	2,500
Dr. Wilfried Robers		5,000	0	5,000	3,000
Dr. Erhard Schipporeit	Chairman of Audit Committee	7,500	0	7,500	5,000
Bodo Schmidt		12,500	0	12,500	3,000
Dr. Peter Schörner	Audit Committee	7,500	0	7,500	5,000
Ulrich Terbrack	(from July 1, 2005)	2,500	0	2,500	1,500
Ulrich Weber		5,000	0	5,000	3,000
Dr. Hans-Dietrich Winkhaus		5,000	0	5,000	3,000
Total		**130,000**	**0**	**130,000**	**74,500**

Total payments to former members of the Board of Management and their surviving dependents amounted to €8.4 million (2004: €8.1 million). Provisions of €109.2 million (2004: €106.6 million) have been made for pension entitlements for former members of the Board of Management and their surviving dependents and for transitional payments.

Former members of the Supervisory Board and their surviving dependents do not receive any gratuity, pension or similar payments or benefits as a result of their membership of the Supervisory Board. Consequently, no provisions have been established for payment obligations or pensions for Supervisory Board members.

The members of the Supervisory Board and the Board of Management are listed on pages 155–160.

(33) Related party transactions

On June 1, 2004 RAG raised its stake in Degussa from 46.48 percent to 50.10 percent as planned. Since then, Degussa has been included in the consolidated financial statements for the RAG Group.

In the normal course of business the individual business areas of Degussa provide a large number of services for affiliated companies. These include all affiliated companies of Degussa and RAG and all investments of Degussa and RAG and certain investments of E.ON, RWE and ThyssenKrupp. Similarly, these companies provide services for the Degussa Group. These transactions are undertaken at the same prices that would be agreed with third parties.

The volume of services provided for related companies and sourced from related companies and the related receivables and payables are shown in the following table.

	RAG Group		E.ON Group		RWE Group		ThyssenKrupp Group		Degussa Group		Total	
in € million	**2005**	2004	**2005**	2004	**2005**	2004	**2005**	2004	**2005**	2004	**2005**	2004
Total goods and services supplied	19	18	5	12	26	3	0	0	138	149	188	182
Goods and services sourced	45	62	69	63	31	31	0	0	47	0	192	156
Receivables	4	2	1	4	2	1	0	0	55	53	62	60
Financial receivables	0	0	0	0	0	0	0	0	71	54	71	54
Liabilities	9	7	1	4	1	0	0	0	16	13	27	24
Financial liabilities	0	0	0	1	0	0	0	0	1	3	1	4
Other liabilities	0	0	4	4	0	0	0	0	0	2	4	6

Goods and services mainly comprise energy, chemical products and information technology services.

Apart from remuneration (see Note 32) no payments were made to key executives as related parties of the Degussa Group.

In 2005 Degussa had a finance lease with the Degussa pension fund as lessor. This agreement was terminated at the end of 2005. Interest and repayment installments amounted to €2 million in fiscal 2005.

(34) Additional information on the cash flow statement

The cash flow from operating activities was impacted by interest payments of €90 million (2004: €89 million) and income tax payments of €81 million (2004: €58 million), after taking into account the effect of tax reimbursements.

Cash inflows from the sale of investments mainly relate to the sale of the Proligo Group and the ESM Group Inc., see Note (6). These transactions included cash and cash equivalents totaling €3 million. The cash inflows from the sale of other financial assets mainly relate to the repayment of a €79 million vendor note by INEOS Investment Holdings Limited and the repayment of a €35 million vendor note by PolymerLatex. Degussa recorded a total cash inflow of €25 million from the divestment of the Fruit Systems Product Line, whose assets and liabilities were classified as held for sale in 2004.

In 2004 cash inflows related to the divestment of the metallurgical operations and the sale of long-term securities. After adjustment for interest-bearing debt and financial balances, the sale of the three parts of the metallurgical operations generated proceeds of €63 million. The sale of the metallurgical operations included cash and cash equivalents of €3 million.

Cash outflows for the acquisition of investments principally relate to the purchase of the remaining stake in CYRO Industries, the acquisition of shares in the Chinese joint venture JIDA Degussa High Performance Polymers Changchun Co. Ltd. and the acquisition of interests in the Chinese company Degussa Sanzheng (Yingkou) Fine Chemicals Co. Ltd., see Note (5). Liquid assets of €13 million were acquired through these transactions.

Alongside the acquisition of a few smaller companies or stakes in such companies, and some asset deals, in 2004 Degussa acquired Agroferm, see Note (5). The purchase price for this company was €39 million. Part of this resulted in cash outflows in 2003 and part resulted in cash outflows in 2005. The liquid assets of €9 million acquired as part of this transaction were set off against the purchase price. Together, these effects resulted in outflows of €15 million for capital expenditures for financial assets.

The cash flow statement has been adjusted for the impact of discontinued operations. In 2005 the discontinued operations reported cash outflows from operating activities of €28 million (2004: €18 million), cash outflows from investing activities of minus €14 million (2004: minus €35 million) and cash inflows from financing activities of €2 million (2004: €11 million).

in € million	**2005**	2004
Cash and cash equivalents	185	184
Securites held as current assets	4	0
Total maturing in less than 3 months = accrued funds	**189**	**184**
Cash and cash equivalents	3	1
Marketable securities	19	18
Total maturing in more than 3 months	**22**	**19**
Liquid assets shown on balance sheet	**211**	**203**

(35) Material transactions since the end of the fiscal year

Following due consideration of all relevant circumstances, on February 6, 2006 the Board of Management decided to enter into negotiations on divesting the construction chemicals activities. Having evaluated all offers received, it decided on February 14, 2006 that it would initially only pursue negotiations with BASF. The aim of both companies is to sign an agreement on this deal as soon as possible.

Divestment of these activities would have a material impact on our financial position, assets and earnings in 2006. It would reduce sales, EBIT and income before income taxes by eliminating the positive contribution made by Construction Chemicals, see Note (4). At the same time, the net interest position would improve as a result of the proceeds from the transaction.

(36) Right to dispense with disclosure under § 264 paragraph 3 and § 264 b German Commercial Code

The following companies fulfill the conditions set out in the above provisions:

- AQura GmbH
- Colfirmit Rajasil GmbH & Co. KG
- Construction Research & Technology GmbH
- Degussa Bauchemie GmbH
- Degussa Construction Chemicals GmbH
- Degussa Construction Polymers GmbH
- Degussa Immobilien GmbH & Co. KG
- Degussa Verwaltungs-GmbH
- Goldschmidt GmbH
- Hüls Service GmbH
- Industriepark Wolfgang GmbH
- Infracor GmbH
- Infracor Lager- und Speditions-GmbH
- Oxeno Olefinchemie GmbH
- Oxxynova GmbH & Co. KG
- PCI Augsburg GmbH
- Relius Coatings GmbH & Co.
- Röhm GmbH & Co. KG
- Stockhausen GmbH
- TEGO Chemie Service GmbH

(37) Earnings per share

Basic earnings per share are calculated by dividing the earnings reported by the continuing operations/ share of income attributable to shareholders of Degussa AG by the weighted average number of shares. This comprises the total income generated by the Group during the year after deduction/ addition of minority interests, including earnings from discontinued operations. In 2005 there was no change in the number of shares outstanding. Earnings per share were thus calculated as follows:

in € million	2005	2004
Income from continuing operations	– 458	378
Income from discontinued operations	– 21	– 69
Minority interests	12	11
Share of net income/loss attributable to shareholders of Degussa AG	**– 491**	**298**

	2005	2004
Weighted average number of shares outstanding	205,623,590	205,623,590
Earnings per share for the continuing operations in €	– 2.23	1.84
Earnings per share for the discontinued operations in €	– 0.10	– 0.34
Minority interests in earnings per share in €	0.06	0.05
Share of net income/loss per share attributable to shareholders of Degussa AG in €	**– 2.39**	**1.45**

The Board of Management and Supervisory Board will be recommending to the Annual Shareholders' Meeting that there should be no dividend payment for 2005.

(38) Declaration of conformity to the German Corporate Governance Code pursuant to § 161 of the Stock Corporation Act

The Board of Management and Supervisory of Degussa AG, which is a listed company included in the consolidated financial statements for the Group, have issued a declaration of conformity to the German Corporate Governance Code in compliance with §161 of the German Stock Corporation Act. Shareholders can find this declaration at all times on the company's website: www.degussa.com/en/investors/corporate_governance.html.

Düsseldorf, February 14, 2006

The Board of Management

Felcht Hofmann Oberholz

Schoeneberg Spindler Wagner

Auditor's Report

The translation of the Auditor's Report is as follows:

We have audited the consolidated financial statements prepared by the Degussa AG, Düsseldorf, comprising the income statement, the balance sheet, statement of changes in equity, cash flow statement and the notes to the consolidated financial statements, together with the group management report for the business year from January 1 to December 31, 2005. The preparation of the consolidated financial statements and the group management report in accordance with the IFRSs, as adopted by the EU, and the additional requirements of German commercial law pursuant to § (Article) 315 a Abs. (paragraph) 1 HGB ("Handelsgesetzbuch": German Commercial Code) are the responsibility of the parent Company's Board of Managing Directors. Our responsibility is to express an opinion on the consolidated financial statements and on the group management report based on our audit.

We conducted our audit of the consolidated financial statements in accordance with §317 HGB and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (Institute of Public Auditors in Germany) (IDW) and additionally observed the International Standards on Auditing (ISA). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the consolidated financial statements in accordance with the applicable financial reporting framework and in the group management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Group and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the consolidated financial statements and the group management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the annual financial statements of those entities included in consolidation, the determination of the entities to be included in consolidation, the accounting and consolidation principles used and significant estimates made by the Company's Board of Managing Directors, as well as evaluating the overall presentation of the consolidated financial statements and the group management report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

In our opinion based on the findings of our audit the consolidated financial statements comply with the IFRSs as adopted by the EU, the additional requirements of German commercial law pursuant to § 315 a Abs. 1 HGB and give a true and fair view of the net assets, financial position and results of operations of the Group in accordance with these requirements. The group management report is consistent with the consolidated financial statements and as a whole provides a suitable view of the Group's position and suitably presents the opportunities and risks of future development.

Düsseldorf, February 14, 2006

PricewaterhouseCoopers
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

Dr. Vogelpoth	Sprinkmeier
Wirtschaftsprüfer	Wirtschaftsprüfer

Principal Consolidated Subsidiaries of Degussa AG

As of December 31, 2005 Company name and headquarters	Country	Share-holding in %	Share-holders' equity[1)] in € million	Sales[1)] in € million	Net income[1)] in € million	Employees at year end
Germany						
Degussa Construction Chemicals GmbH, Trostberg[2)]	D	100	260	0	4	0
Degussa Food Ingredients GmbH, Trostberg	D	100	280	4	4	22
Degussa Initiators GmbH & Co. KG, Pullach	D	100	– 1	105	– 9	367
Goldschmidt GmbH, Essen[2)]	D	100	127	356	16	1,378
Infracor GmbH, Marl[2)]	D	100	66	650	16	2,432
Oxeno Olefinchemie GmbH, Marl[2)]	D	100	39	899	72	441
Relius Coatings GmbH & Co. KG, Oldenburg	D	100	23	114	3	615
Röhm GmbH & Co. KG, Darmstadt	D	100	184	938	16	3,228
RohMax Additives GmbH, Darmstadt	D	100	71	178	7	159
Stockhausen GmbH, Krefeld[2)]	D	100	127	624	37	1,054
Abroad						
CYRO Industries Inc., Rockaway	USA	100	171	278	20	659
Degussa (China) Co., Ltd., Beijing	CN	100	94	21	– 8	346
Degussa Admixtures, Inc., Wilmington	USA	100	203	208	52	309
Degussa Amalgamation Ltd., Milton Keynes	GB	100	787	0	– 12	0
Degussa Antwerpen N.V., Antwerp	B	100	112	305	12	1,064
Degussa Brasil Ltda., São Paulo	BR	100	78	151	11	321
Degussa Building Systems Inc., Wilmington	USA	100	148	186	26	206
Degussa Canada Inc, Burlington	CDN	100	40	106	10	113
Degussa Corporation, Parsippany	USA	100	1,033	1,067	113	1,580
Degussa Flavors & Fruit Systems US, LLC, Cincinnati	USA	100	34	62	2	217
Degussa Japan Co., Ltd., Tokyo	J	100	76	144	1	120
Degussa Texturant Systems France SAS, Paris	F	100	134	161	4	634
Degussa UK Holdings Limited, London	GB	100	193	0	– 203	0
Goldschmidt Chemical Corporation, Hopewell	USA	100	45	235	2	486
Laporte Speciality Organics Limited, Milton Keynes	GB	100	599	0	18	0
NIPPON AEROSIL Co., Ltd., Tokyo	J	80	44	87	13	147
NMB Co Ltd., Tokyo	J	100	61	103	0	411
RohMax USA Inc., Horsham	USA	100	28	119	9	120
Stockhausen Inc., Greensboro	USA	100	57	318	– 27	345

1) The figures correspond to the financial statements prepared in accordance with local regulations and do not show the company's contribution to the consolidated financial statements. Shareholders' equity is translated at the average rate on the balance-sheet date. Sales and net income are translated using average annual rates.
2) Before transfer of profit/loss.

Report of the Supervisory Board

Dr. Werner Müller

During the past year, the Supervisory Board made a detailed examination of all matters requiring its approval and discussed them with the Board of Management. The Chairman of the Board of Management maintained close contact with the Chairman of the Supervisory Board on all issues of material relevance to the company. The Chairman of the Supervisory Board also received regular, full and timely reports on all important business transactions and all decisions and processes that were of major importance were agreed with him. Further, the Board of Management provided extensive and timely reports to the Supervisory Board, especially on the company's strategy, planning, business position and development, risk situation and risk management and consulted it on such matters. Deviations from the plans and further expansion of business operations were explained in detail by the Board of Management and examined by the Supervisory Board. Decisions were taken on all matters falling within the scope of the Supervisory Board at its meetings after careful examination and discussion. In addition to the strategic issues discussed at regular meetings, the company's strategy was agreed with the Supervisory Board at a separate strategy meeting. Regular reports on the activities of the Supervisory Board committees were presented to the full meetings of the Supervisory Board.

The Supervisory Board's examination of the company's activities—which took place principally at meetings of the various committees and the full Supervisory Board—were based on:

- regular reports submitted by the Board of Management in compliance with statutory requirements and the rules of procedure of the Supervisory Board
- special reports compiled by the Board of Management on specific issues
- supplementary explanations by the Board of Management and external auditors.

These reports were submitted either to the entire Supervisory Board or to the relevant committee. The Supervisory Board and its committees gave their approval to business issues in twenty-nine cases. Where the Board of Management requested the approval of the Supervisory Board on business matters, a summary outlining the main points to be considered in the decision was attached to the proposed resolution. In two instances, the Executive Committee of the Supervisory Board took a decision instead of the full Supervisory Board because of the urgency of the matter. In the reporting period, the Supervisory Board had no reason to ask individual members or experts to examine the company's books and papers.

Meetings of the Supervisory Board In 2005 the meetings of the Supervisory Board of Degussa AG focused on the Group's strategy, especially in view of the risks and opportunities of the growing Asian and Eastern European markets, completion of the divestment of non-core activities, the ongoing development of the Fine & Industrial Chemicals Division and its valuation and the proposed disposal of the Food Ingredients Business Unit.

At its meeting on March 7, 2005 the Supervisory Board looked in detail at the annual financial statements and management report for Degussa AG and the Degussa Group for fiscal 2004, which were explained by the auditors for 2004, KPMG Deutsche Treuhand-Gesellschaft Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, Berlin and Frankfurt am Main, and the report on the company's business condition. It also asked for a report on the economic aspects of the activities in China. Other items on the agenda included reports by the committees, the report of the Board of Management and Supervisory Board on corporate governance, the preparations for the Annual Shareholders' Meeting on May 4, 2005, the Human Resources report, the exercise of shareholders' rights at subsidiaries, the divestment of the metallurgical operations, the divestment of the Fruit Systems Product Line, the divestment of the Proligo Group, the joint venture with Changchun Jida, the acquisition of the remaining 50 percent interest in CYRO Industries, debottlenecking of capacity for superabsorbents, the syndicated credit facility and the "Degussa 2008" strategy project. With regard to the business plans for 2005–2007, a presentation of the risks relating to economic trends, raw material prices and exchange rates was requested, together with explanations of the development of the company's headcount, its financial structure, including the increase in the equity ratio, and planned capital expenditures.

At its meeting before the Annual Shareholders' Meeting on May 4, 2005 the Supervisory Board discussed the construction of the fourth isophorone line in Herne, Germany, the conclusion of a profit-and-loss transfer agreement between Degussa Immobilien GmbH & Co. KG and Westgas GmbH, the termination of the profit-and-loss transfer agreements between Degussa AG and Degussa Food Ingredients GmbH and between Degussa Food Ingredients GmbH and Maxens GmbH, the conclusion of a control and profit-and-loss transfer agreement between Degussa Food Ingredients GmbH and Degussa Food Ingredients Deutschland GmbH and the report on the current business situation.

On June 29, 2005 the Supervisory Board held an extraordinary meeting to discuss future strategic options for the business units. Special attention was paid to the growth prospects in Europe, China, and NAFTA. The Supervisory Board specifically asked for detailed information on the situation in the pharmaceuticals sector, especially the generics market, and in custom manufacturing. In addition, Mr. Günter Adam was elected to the Executive Committee of the Supervisory Board and the Mediation Committee pursuant to § 27 paragraph 3 of the German Codetermination Act. The election was made necessary by the fact that Mr. Ralf Blauth transferred to the RAG Group.

In view of the enormous significance of the Asia region and especially China for Degussa's strategy, the Supervisory Board meeting on September 27 was held in Shanghai. The Supervisory Board visited the Degussa Group companies there and talked to employees and members of the business community in order to obtain an insight into Degussa's activities and its plans to expand its operations in China. At this meeting the Supervisory Board also discussed in detail the report on the company's situation, especially in the light of rising energy and raw material prices, progress with the "Degussa 2008" project, the divestment of the Food Ingredients Business Unit, the divestment of ESM Group Inc., the construction of a monosilanes plant and a solar silicon plant in Rheinfelden, Germany, the sale of the company's premises in Frankfurt, Germany, the conclusion of a profit-and-loss transfer agreement between Goldschmidt SKW Surfactants GmbH and Goldschmidt Rewo GmbH, and the termination of the profit-and-loss transfer agreement between Degussa AG and Degussa Assekuranz-Kontor GmbH.

At its meeting on December 13 the Supervisory Board examined the company's situation, the earnings expectations for fiscal 2006, the plans for 2006–2008 and Degussa's credit lines. With the Board of Management it discussed the development of the company in the planning period, taking into account the expected financial and economic conditions and the focus of investment on businesses with sustained growth prospects. It appointed PricewaterhouseCoopers AG, Düsseldorf, Germany, to audit the annual financial statements of Degussa AG and the Degussa Group and defined the main focus of the audit. Further, the Supervisory Board approved the acquisition of the superabsorbents activities of Dow Chemicals and the debottlenecking of Degussa's own facilities and gave its approval under § 32 of the German Codetermination

Act for the conclusion of control and profit-and-loss transfer agreements between Degussa AG and Röhm GmbH and Röhm GmbH and RohMax Additives GmbH. The committees reported on meetings held since the last full meeting of the Supervisory Board. Following the discussion at the preceding meeting of the Supervisory Board's Executive Committee, the Supervisory Board agreed that the Board of Management should enter into talks with strategic investors on divesting Construction Chemicals. Similarly, the Supervisory Board discussed and approved the new organizational structure of Degussa AG as the outcome of the Strategy & Organization project, the appointment of Dr. Bernhard Hofmann and Dr. Manfred Spindler as additional members of the Board of Management and the future allocation of responsibilities between the members of the Board of Management. Moreover, the Supervisory Board approved the Joint Report of the Board of Management and Supervisory Board on Corporate Governance and the Declaration of Conformity pursuant to § 161 of the Stock Corporation Act. Finally, at this meeting it reported on the outcome of the efficiency review and discussed ways of improving its efficiency still further.

No member of the Supervisory Board was absent from more than half the meetings in his period of office.

Supervisory Board Committees At its meetings on January 17 and March 2, 2005 the Executive Committee of the Supervisory Board discussed the business plans for 2005-2007. On March 7, 2005 it discussed adjusting the long-term incentive plan (LTIP) to align it to new accounting standards and take account of the impairment charge on the fine and industrial chemicals activities in 2003. At its meeting on March 11, 2005, it discussed the exercise conditions for the 2003 LTIP tranche, which was due for payment, and the granting of a new tranche for the Board of Management in fiscal 2005. On April 22, 2005 the Executive Committee of the Supervisory Board passed a resolution in place of the full Supervisory Board on the acquisition of the remaining 50 percent stake in the joint venture CYRO Industries Inc., because of the urgency of the matter. On June 13, 2005, because of the urgency of the issue, it adopted a resolution using the written circulation procedure on the acquisition of 80 percent of the shares in Jida High Performance Materials Co. LTD, China. At its meeting on November 24, 2005 the Executive Committee of the Supervisory Board discussed the future focus of the company and the results of the Strategy & Organization project, especially the change in the organizational structure of Degussa AG and the recommendation to be submitted to the full Supervisory Board on the appointment of two additional members of the Board of Management. At this meeting, and at the meeting of the Committee of the Supervisory Board on December 13, 2005, portfolio adjustments were discussed. At its meeting on December 13, 2005 the committee discussed the possible divestment of the Construction Chemicals Division as part of the focusing of the portfolio on specialty chemicals activities.

At its meeting on March 2, 2005 the Audit Committee discussed the annual financial statements for 2004. The auditors, KPMG Deutsche Treuhand-Gesellschaft Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, Berlin and Frankfurt am Main, explained the financial statements to the committee and answered questions. At its meeting on May 2, the committee discussed the quarterly report for the first quarter of 2005 and the valuation of the divisions. On August 3 the Audit Committee discussed the financial statements and interim report for the first six months of 2005. It also examined planned and completed improvements to the risk management system and the principles, structure and risk positions used to hedge currency risks and the hedging ratios. The focus of the audit for the annual financial statements of Degussa AG and the Degussa Group as of December 31, 2005 was also discussed. At its meeting on October 5, 2005, at which the auditors were present, the Audit Committee discussed the impact of the portfolio options for fine chemicals on the financial statements of Degussa AG and the Degussa Group and the need for an impairment write-down on the fine chemicals activities. At a further meeting on November 3, 2005 the Audit

Committee discussed the interim report as of September 30, 2005 and established that, with the exception of the fine chemicals operations, the fair value of all business units was well above their carrying amounts.

The committee set up in compliance with § 27 paragraph 3 of the German Codetermination Act was not convened.

Corporate Governance During the past fiscal year, the Supervisory Board and Board of Management continued to track developments in the requirements for good corporate governance. A detailed statement on this is contained in the joint report of the Board of Management and Supervisory Board on corporate governance. In 2005 Degussa AG complied with the recommendations set out in the German Corporate Governance Code, including the changes that took effect in 2005, with three exceptions which are explained. In compliance with § 161 of the Stock Corporation Act, the exceptions are disclosed in the joint declaration with the Board of Management on the recommendations of the German Corporate Governance Code issued on December 13, 2005.[a] At its meeting on December 13, 2005, at which the Board of Management was not present, the Supervisory Board discussed how it could improve its efficiency. During 2005 the Supervisory Board implemented the improvements suggested during the review of its efficiency in 2004. For example, it arranged a separate meeting to discuss corporate strategy.

Annual financial statements and report on associated companies The annual financial statements of Degussa AG prepared by the Board of Management as of December 31, 2005 in compliance with the German Commercial Code (HGB) and the management report for fiscal 2005, including the risk management system, as stipulated in § 91 paragraph 2 of the Stock Corporation Act, have been audited by the auditors elected by the Annual Shareholders' Meeting, PwC Deutsche Revision Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, Düsseldorf, now operating as PricewaterhouseCoopers Aktiengesellschaft, Wirtschaftsprüfungsgesellschaft (PwC). The auditors have issued an unqualified opinion. The consolidated financial statements and management report for the Degussa Group have also been audited by PwC, which has given an unqualified opinion.

This year's audit of the annual financial statements for Degussa AG concentrated on the risk identification system, the start-up of major business processes, especially sales and human resources processes, financial investments and pension provisions. The audit for the Degussa Group focused on the SAP SEM-BCS consolidation system and consolidation methods, the impairment test in accordance with IAS 36, restructuring provisions in accordance with IAS 19.37 and provisions for environmental risks. The financial statements, management reports and auditors' reports for Degussa AG and the Degussa Group were submitted to the Audit Committee immediately upon completion and discussed at its meeting on February 28, 2006. The Supervisory Board also examined the annual financial statements of Degussa AG, the consolidated annual financial statements of the Degussa Group, the management report of Degussa AG and the Group and the management's proposal for the appropriation of net income, which does not provide for the payment of a dividend. We accept the proposals made by the Audit Committee and have no objections to raise. We therefore approve the outcome of the audit. The auditors were present when the Supervisory Board met on March 1, 2006 to discuss the annual financial statements of the company and the Group and reported to the Supervisory Board on the main findings of their audit. The annual financial statements and the consolidated financial statements for the Group prepared by the Board of Management were approved. The annual financial statements for Degussa AG are thus adopted. We support the Board of Management's proposal that there should be no dividend payment for 2005.

The Board of Management has prepared a report on associated companies. This was examined by the auditors, who have issued the following unqualified

[a] See page 154

opinion in accordance with § 313 paragraph 3 of the German Stock Corporation Act:

“In accordance with our professional audit and judgment, we confirm that

1. the facts contained in the report are correct
2. the company’s expenditures in connection with the legal transactions contained in the report were not unreasonably high and compensation was received for any disadvantages
3. there is no reason to reach a significantly different assessment of the measures outlined in the report than the conclusions drawn by the Board of Management.”

The Supervisory Board also examined the report on the associated companies for completeness and correctness. This examination found that the Board of Management, had, with the necessary care,

- identified the associated companies
- taken the necessary precautions to identify transactions which the company undertook in the past fiscal year with its controlling company and any company associated with it and transactions undertaken at the instigation of or in the interests of these companies and to identify other activities undertaken or not undertaken at the instigation of or in the interests of these companies in the past fiscal year
- included these actions and transactions in their entirety in the report on associated companies.

In its examination of the transactions outlined in the report, the Supervisory Board established that under the circumstances known at the time they were undertaken, the company’s expenditures in connection with these transactions were not unreasonably high. On the basis of random samples, it obtained an explanation of the basis on which the company’s activities and the remuneration therefor were determined, particularly in the case of material transactions. The Supervisory Board saw no reason to reach a significantly different assessment of the measures outlined in the report than the conclusions drawn by the Board of Management. The Audit Committee discussed the report in advance and gave the Supervisory Board a detailed report on the outcome of its meeting.

Changes to the Supervisory Board To replace Ralf Blauth, who left the Supervisory Board on June 30, 2005, Ulrich Terbrack was appointed as an employee representative on the Supervisory Board of Degussa AG effective July 1, 2005 through a judicial decision taken by Düsseldorf District Court on June 23, 2005.

At its meeting on June 29, 2005, the Supervisory Board appointed Mr. Günter Adam to replace Mr. Ralf Blauth as a member of the Executive Committee of the Supervisory Board and the Mediation Committee set up in accordance with § 27 paragraph 3 of the German Codetermination Act.

Mr. Blauth had been a member of the Supervisory Board of Degussa and of companies subsequently merged into it since May 1986. The Supervisory Board would like to thank him for his long-standing commitment to Degussa AG and the companies from which it was formed and for his constructive work on the Supervisory Board and as a member of the Executive Committee.

Changes to the Board of Management At its meeting on December 13, 2005, the Supervisory Board appointed Dr. Bernhard Hofmann and Dr. Manfred Spindler as additional members of the Board of Management for the period until December 31, 2007.

The Supervisory Board would like to thank the members of the Board of Management, the employee representatives and all employees of Degussa AG and its affiliated companies for their hard work and commitment in 2005.

Düsseldorf, March 1, 2006

The Supervisory Board

Dr. Werner Müller
Chairman

Corporate Governance

Joint Report by the Board of Management and Supervisory Board of Degussa AG on Corporate Governance (Corporate Governance Report)

Corporate governance comprises all principles underlying the correct and responsible management and oversight of a company. It is therefore a key element in Degussa's management philosophy. The principles of corporate governance relate to collaboration between the Board of Management, Supervisory Board and shareholders, especially at the Annual Shareholders' Meeting, and the relationship between our company and other persons and organizations with which we have a business relationship. The Supervisory Board and Board of Management of Degussa AG are explicitly committed to responsible corporate governance.

Since the introduction of the German Corporate Governance Code in 2002, Degussa has complied with almost all of its recommendations and suggestions. Exceptions, together with the reasons, are detailed in a declaration of conformity pursuant to § 161 of the German Stock Corporation Act issued by the Board of Management and Supervisory Board on December 13, 2005. In addition, in this Annual Report the Board of Management and Supervisory Board outline compliance with the suggestions made by the Corporate Governance Code on the following issues. The declarations for the years 2002–2005 are available on Degussa's website.

Annual Shareholders' Meeting To help shareholders utilize their rights and prepare for the Annual Shareholders' Meeting, all relevant documents and reports are posted on Degussa's website (http://www.degussa.com). On request, they will be sent to shareholders as hard copy. If shareholders cannot exercise their voting rights personally at the Annual Shareholders' Meeting, they can authorize a proxy voting representative nominated by the company to vote in line with their instructions. Degussa provides a webcast of its Annual Shareholders' Meeting up to the end of the presentation by the Chairman of the Board of Management. This enables shareholders who cannot attend the meeting and other members of the public to listen to the meeting. A financial diary is published in the Annual Report, quarterly reports and the internet to keep the public informed of all key financial dates.

Cooperation between the Supervisory Board and Board of Management In order to fulfill his advisory and supervisory functions, the Chairman of the Supervisory Board maintains close contact with the Board of Management between meetings. The Board of Management gives the Supervisory Board regular, full and timely reports on all major aspects of corporate planning, development and strategy and risk management. Where the company's business performance deviates from the budget, the reasons are presented and explained. Corporate strategy and the status of implementation are also discussed at a meeting of the Supervisory Board dedicated entirely to strategic issues. This enables the Supervisory Board to oversee the Board of Management and provide effective advice. The Supervisory Board also receives copies of the documents used at its meetings in good time. The representatives of the shareholders and the workforce meet separately to prepare for meetings of the Supervisory Board. The Board of Management obtains the approval of the Supervisory Board on all matters where approval is required under its rules of procedure.

Corporate governance can only function effectively if discussions between the Board of Management and Supervisory Board remain confidential. The Board of Management ensures that all employees assisting it in its work are required to respect the confidentiality of such information.

In fiscal 2005 the company did not grant any loans to members of the Supervisory Board or Board of Management, nor were there any receivables outstanding from earlier loans.

The company is included in the D&O (directors' and officers' liability) insurance policy of RAG Aktiengesellschaft. This includes a deductible of a standard amount for the members of the Board of Management and Supervisory Board.

Board of Management The Board of Management manages the company with a view to its best interests and to creating value. It provides open and timely information for shareholders, business associates, employees, the financial markets and the general public.

No member of the Board of Management experienced any conflict of interests with the company. In fiscal 2005, as in the past, no transactions were undertaken between the company and members of the Board of Management, persons related to them or enterprises closely connected with them.

The rules of the procedure of the Supervisory Board set an age limit or time limit for reappointment of members of the Board of Management. The new members of the Board of Management, Dr. Bernhard Hofmann and Dr. Manfred Spindler, have initially been appointed for a period of just three years.

Remuneration of the Board of Management The individual remuneration of members of the Board of Management is based on their personal performance, the performance and financial position of the company and its future outlook, taking into account compensation paid at comparable companies.

The remuneration paid to the members of the Board of Management comprises a fixed base salary, a variable annual bonus (short-term incentive plan) and a long-term incentive plan.

The fixed base salary also covers the assumption of functions on the supervisory boards of subsidiaries, non-cash benefits (e.g. a company car) and other payments (e.g. reimbursement of business expenses). Variable payments comprise payments made under the short-term incentive plan, which are based on the attainment of individually agreed objectives for the fiscal year, and payments under the long-term incentive plan. The long-term incentive plan is based on two key financial performance indicators—ROCE and EBITDA—which are also used for financial reporting. The long-term incentive plan is not linked to the price of Degussa stock. Under this plan, the members of the Board of Management are allocated performance options every year by the Executive Committee of the Supervisory Board. These run for a maximum of five years and there is a cap on their value. The performance options are subject to a two-year lock-up period, after which the number that each member can exercise is determined by the ROCE in a given year. The value of individual performance options is derived from the extent to which the EBITDA trend exceeds the average EBITDA trend for a group of European specialty chemical companies (benchmark).

In addition, the members of the Board of Management have been granted a pension entitlement. The pension paid to members of the Board of Management is a percentage of their fixed base salary. This percentage rises with their length of service on the Board of Management. (The basic pension entitlement is 50 percent of their final monthly salary. This rises by 2 percent for every full year of service on the Board of Management, up to a maximum of 70 percent.) Pension entitlements are therefore not dependent on variable compensation payments.

Details of the remuneration paid to individual members of the Board of Management, broken down into fixed salary, short-term incentive payments and long-term incentive payments, can be found in Note 32 to the annual financial statements.

The basic principles of the remuneration system can be found on Degussa's website (http./www.degussa.com/en/investors/corporate_governance/remuneration.html). The system will also be explained to the shareholders at the Annual Shareholders' Meeting.

Supervisory Board The Supervisory Board monitors and advises the Board of Management. It fulfills these duties through its meetings and by maintaining regular contact with the Board of Management. Resolutions are adopted in cases where it is required to do so by law and for business matters of fundamental importance where the Board of Management is required by its rules of procedure to obtain a decision from the Supervisory Board.

The Supervisory Board has adopted rules of procedure to structure its work and ensure it complies with legal requirements. The chairman coordinates the Supervisory Board, chairs its meetings and represents it in dealings with others.

Degussa's Supervisory Board has twenty members. Under German codetermination legislation, half are representatives of the shareholders and the others are representatives of the workforce. The shareholders' representatives are elected at the Annual Shareholders' Meeting. When nominations are put forward, care is taken to ensure that candidates are specifically qualified for office by virtue of their professional knowledge, international experience and personality. In future, the shareholders' representatives will be elected on an individual basis. Where applications are submitted for judicial appointment of shareholders' representatives to the Supervisory Board, their term will be limited until the next Shareholders' Meeting. The shareholders will be informed of the candidates nominated for seats on the Supervisory Board. To ensure a full complement of Supervisory Board members when Mr. Ralf Blauth left the Supervisory Board effective June 30, 2005, Mr. Ulrich Terbrack was appointed a member of the Supervisory Board of Degussa AG from July 1, 2005 under a judicial decision taken by Düsseldorf District Court on June 23, 2005.

The Supervisory Board normally holds at least four meetings a year. If a member cannot attend a meeting, he or she can submit a written vote in accordance with the rules of procedure. This option was utilized in 2005. The rules of procedure also state that potential personal conflicts of interest must not influence decisions taken by the Supervisory Board. This is examined as part of the Supervisory Board's annual efficiency review. The Supervisory Board considers that it has a sufficient number of independent members. Moreover, members of the Supervisory Board are not exposed to any conflicts of interest and have no consultancy, service or similar contracts with the company.
In particular, the representatives of the two major shareholders, RAG Aktiengesellschaft and E.ON AG, have no personal or business relationships with the company and its Board of Management that could prejudice their independence. Where business relationships do exist between the two major shareholders and the company, they are undertaken on normal market conditions in accordance with the "arm's length" principle.

The rules of procedure of the Supervisory Board recommend a maximum age of 70 for members. This recommendation is observed.

To assist it in its work, the Supervisory Board has an Executive Committee, an Audit Committee and a mediation committee set up in compliance with § 27 paragraph 3 of the German Codetermination Act. The Chairman of the Supervisory Board chairs the Executive Committee, which prepares decisions to be taken by the Board of Management on personnel issues. It also decides on behalf of the Supervisory Board on the conclusion, amendment, suspension and termination of employment contracts with members of the Board of Management, sets their annual bonus payments and takes decisions on other issues relating to the Board of Management. The Supervisory Board thus utilizes the option of delegating issues relating to the Board of Management to a committee. The Supervisory Board's Executive Committee therefore functions as a personnel committee in line with common practice at large corporations. Contrary to Section 4.2.2 of the German Corporate Governance Code, it thus discusses and reviews the structure of the remuneration system for the Board of Management. It also adopts resolutions on behalf of the full Supervisory Board in cases where it would be detrimental to the company to wait for the approval of the full Supervisory Board. The Audit Committee examines matters relating to accounting, risk management, the independence of the external auditors and the award of the contract to the auditors—including determining the main focus of the audit and the fee to be paid—and prepares the relevant decisions to be taken by the full Supervisory Board. The Audit Committee is chaired by the management board member at the company's major shareholder, E.ON AG, with responsibility for finance, accounting, taxes and information technology. This ensures that he has knowledge and experience of the application of accounting principles and internal control systems. The committees report regularly on their work at subsequent meetings of the full Supervisory Board.

No former member of the Board of Management of the company or its predecessors is a member of the Supervisory Board or one of its committees.

Contrary to Section 5.4.5 of the German Corporate Governance Code, members of the Supervisory Board do not receive separate remuneration for chairing a committee of the Supervisory Board. However, Degussa AG's Articles of Incorporation do provide for separate compensation for membership of a committee. This provides appropriate recompense for the additional work involved, even as chairperson of a committee.

Details of the remuneration paid to individual members of the Supervisory Board are also given in Note 32 to the financial statements, broken down by components.

To ensure that the members of the Supervisory Board have sufficient time to carry out their advisory and supervisory functions, members who are also members of the Board of Management of a listed public company may not hold seats on the supervisory boards of more than five listed companies outside their group of companies.

At its meeting on December 13, 2005, the Supervisory Board examined its efficiency and how this could be improved. This meeting was held in the absence of the Board of Management. The review took the form of a questionnaire, which members were permitted to fill out anonymously. The Chairman of the Supervisory Board reported on the outcome.

Transparency The Board of Management provides open information on the company's performance and business situation for private and institutional investors, business associates, employees, the financial markets and the general public. Alongside regular publications such as interim reports and the Annual Report, the company arranges financial press conferences and conference calls with journalists, financial analysts and investors. These are made available live via the web. The company also uses its website for up-to-date reporting.

Degussa immediately publishes insider information on the company except in instances where the Board of Management is exempt from the obligation to disclose such information. The company immediately publishes any notification it receives of the acquisition and sale of shares as a result of which the voting rights in Degussa AG held by a single shareholder would reach, exceed or fall below the 5, 10, 25, 50 or 75 percent threshold.

The Corporate Citizenship Report of Degussa AG provides information on the company's obligation to work to the good of society as a whole. All major publications are issued in English as well as German.

In fiscal 2005 no members of the Supervisory Board, Board of Management and other persons with managerial responsibilities who have regular access to insider information about the company and are empowered to take material business decisions, or persons closely related to them, undertook transactions with Degussa shares or financial instruments on Degussa shares in excess of the statutory immateriality threshold of €5,000 per calendar year.

The total shareholding of all members of the Board of Management and Supervisory Board in shares issued by the company is less than 1 percent.

Accounting Policies Since 2004, the consolidated financial statements for Degussa AG and its subsidiaries have been prepared in accordance with the International Financial Reporting Standards (IFRS). Interim reports are published within 45 days from the end of the reporting period and the consolidated financial statements for the Degussa Group are published within 90 days from the end of the fiscal year. The consolidated financial statements contain a list of the companies in which Degussa has shareholdings that are of material significance.

Degussa offers members of the Board of Management and Executives (top management level below the Board of Management) a long-term incentive plan based on the mid- to long-term development of the company's value. The modalities of this plan are outlined in the discussion of the remuneration of the Board of Management (see above).

Auditing At the Annual Shareholders' Meeting in 2005, which was held on May 4, 2005, PwC Deutsche Revision Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, Düsseldorf, was appointed as the auditor for fiscal 2005. In the contract, the Supervisory Board defined areas on which the audit should focus.

Before the resolution was put to the Annual Shareholders' Meeting, the auditors submitted a declaration detailing business, financial, personal and other relations between the auditing company, its organs and auditors and the company and its officers. This did not indicate any circumstances that could raise doubt about the independence of the audit. Degussa has obtained an undertaking that should any such relations transpire in the course of the audit, the audit company will notify it immediately.

The auditors attended the meeting at which the Supervisory Board discussed the annual financial statements and consolidated financial statements and gave the Supervisory Board the information it required.

Declaration of conformity pursuant to § 161 of the German Stock Corporation Act Deviations from the recommendations of the German Corporate Governance Code were outlined in the fourth declaration of conformity pursuant to § 161 of the German Stock Corporation Act issued on December 13, 2005. The text of the declaration and the exceptions can be found on page 154 of this Annual report and on our website at: www.degussa.com/en/investors/corporate_governance.html.

Declaration by the Supervisory Board and Board of Management of Degussa AG pursuant to § 161 of the German Stock Corporation Act on conformity to the recommendations made by the Government Commission on the German Corporate Governance Code

The Supervisory Board and Board of Management of Degussa AG hereby declare the following:

Since issuing the last declaration of conformity pursuant to § 161 of the German Stock Corporation Act on December 10, 2004, Degussa AG has complied with the recommendations of the Government Commission on the German Corporate Governance Code as published by the German Justice Ministry in the official section of the electronic Federal Gazette (Bundesanzeiger), with the following exceptions:

1. Section 3.8 of the German Governance Code states that a suitable deductible will be agreed if a company takes out a D&O (directors and officers') insurance policy for the members of the Board of Management and Supervisory Board

   The members of the Board of Management and Supervisory Board of Degussa AG are covered by the D&O insurance taken out by RAG Aktiengesellschaft. This is a Group-wide insurance policy that includes a uniform deductible for each member of the Board of Management and the Supervisory Board.

2. Section 4.2.2 of the German Corporate Governance Code states that the full Supervisory Board will discuss and regularly review the structure of the compensation system for the Board of Management.

   Under the rules of the procedure of the Supervisory Board of Degussa AG, responsibility for this is delegated to the Executive Committee of the Supervisory Board.

3. Section 5.4.5 of the German Corporate Governance Code (Sec. 5.4.7 of the German Corporate Governance Code in the version of June 2, 2005) states that members of the Supervisory Board will receive separate remuneration, among other things, for chairing an executive committee.

   The bylaws of Degussa AG provide for a separate compensation for membership in a committee, but not exceeding that for chairing a committee.

In the future, Degussa AG will comply with the recommendations of the Government Commission on the German Corporate Governance Code as they exist in the valid version of June 2, 2005, apart from the above-named exceptions.

Düsseldorf, December 13, 2005

On behalf of the Supervisory Board of Degussa AG
Dr. Werner Müller
(Chairman of the Supervisory Board)

On behalf of the Board of Management of Degussa AG
Prof. Utz-Hellmuth Felcht
(Chairman of the Board of Management)

Dr. Thomas Schoeneberg
(Member of the Board of Management)

Members of the Supervisory Board and Board of Management

Supervisory Board

Dr. Werner Müller
Chairman of the Board of Management of RAG Aktiengesellschaft
Chairman

- ▶ Deutsche Steinkohle Aktiengesellschaft[1)] (Chairman)
- ▶ RAG Coal International AG[1)] (Chairman)
- ▶ RAG Immobilien Aktiengesellschaft[1)] (Deputy Chairman)
- ▶ STEAG Aktiengesellschaft[1)] (Chairman)
- ▶ Viterra AG[1)] (until August 15, 2005)
- ▶ Deutsche Bahn AG (Chairman) (from July 5, 2005)
- ▷ RAG Beteiligungs-GmbH[1)] (Chairman of the Advisory Board)
- ▷ Stadler Rail AG, Bussnang (Member of the Board of Directors)
- ▷ g.e.b.b. (Gesellschaft für Entwicklung, Beschaffung und Betrieb mbH) (Chairman)
- ▷ NRW.Bank (Member of the Advisory Board)
- ▷ WestLB (Member of the Economic Advisory Board) (from July 4, 2005)
- ▷ Deutsche Druck- und Verlagsges. mbH (Member of the Supervisory Board)

Werner Bischoff
Member of the Executive Committee of the Mining, Chemical and Energy Trade Union, Hanover
Deputy Chairman

- ▶ Aventis Pharma Deutschland GmbH
- ▶ Hoechst GmbH
- ▶ Beteiligungsgesellschaft der Gewerkschaften AG
- ▶ Chemie Pensionsfonds AG (Chairman)

Günter Adam
Chairman of the Joint Works Council of Degussa AG, Hanau-Wolfgang

- ▶ E.ON AG[1)]

Dr. Birgit Bertsch-Frank
Team Leader Controlling/Strategy, Oxeno Olefinchemie GmbH, Marl

Ralf Blauth (until June 30, 2005)
Chairman of the Group Works Council of Degussa AG, Marl (until June 30, 2005)
Member of the Board of Management of RAG Coal International AG, Essen (from July 1, 2005)

- ▶ E.ON AG[1)] (until June 30, 2005)
- ▶ RAG Aktiengesellschaft[1)] (until June 30, 2005)

▶ Supervisory Board mandates in accordance with § 100 para. 2 German Stock Corporation Act.
▷ Member of comparable supervisory bodies for companies in Germany and abroad.
1) Group mandate in accordance with § 100 para. 2 German Stock Corporation Act.

Dr. Hans Michael Gaul

Member of the Board of Management of E.ON AG, Düsseldorf

- ▶ Allianz Versicherungs AG
- ▶ DKV Deutsche Krankenversicherungs AG
- ▶ RAG Aktiengesellschaft 1)
- ▶ Volkswagen AG
- ▶ STEAG Aktiengesellschaft 1)
- ▶ Viterra AG 1) (Chairman) (until August 5, 2005)
- ▶ E.ON Energie AG 1)
- ▶ E.ON Ruhrgas AG 1)
- ▷ E.ON Nordic AB, Malmö 1)
- ▷ E.ON Sverige AB, Malmö 1)

Engelbert Gerstandl

Chariman of the Works Council at the Trostberg/Schalchen facilities

Ralf Hermann

Chairman of the Works Council at the Marl facilities

Chairman of the Group Works Council of Degussa AG (from July 1, 2005)

- ▷ Viterra Wohnungsgesellschaft III mbH (Deputy Chairman)

Professor Wolfgang A. Herrmann

President of Munich Technical University

- ▶ Altana AG
- ▶ GenPharmTox BioTech AG

Dr. Dieter Hockel

Head of the Economic Policy Department/Industrial Groups at the Mining, Chemical and Energy Trade Union, Hanover

- ▶ Innovene Deutschland GmbH
- ▶ Innovene Manufacturing Deutschland GmbH (from July 20, 2005)

Rainer Kumlehn

Regional Chairman of the Mining, Chemical and Energy Traide Union, Hesse-Thuringia, Frankfurt

- ▶ Hoechst GmbH
- ▶ Goodyear Dunlop Tires Germany GmbH

Dr. Manfred Krüper

Member of the Board of Management of E.ON AG, Düsseldorf

- ▶ E.ON Energie AG 1)
- ▶ Viterra AG 1) (until August 5, 2005)
- ▶ equitrust Aktiengesellschaft (Chairman)
- ▶ RAG Aktiengesellschaft 1)
- ▶ RAG Immobilien Aktiengesellschaft 1)
- ▶ Victoria Versicherung AG
- ▶ Victoria Lebensversicherung AG
- ▷ E.ON North America, Inc. 1) (Chairman)

Dr. Arend Oetker
Managing Partner of Dr. Arend Oetker Holding GmbH & Co. KG, Berlin
- ▶ Schwartau GmbH & Co. KGaA (Chairman)
- ▶ KWS Saat AG (Deputy Chairman)
- ▶ Cognos AG
- ▶ Merck KGaA
- ▷ Hero AG (Chairman)
- ▷ Bâloise Holding AG
- ▷ Leipziger Messe GmbH

Roland Oetker
Lawyer
Managing Partner of ROI Verwaltungsgesellschaft mbH, Düsseldorf
President of Deutsche Schutzvereinigung für Wertpapierbesitz e.V., Düsseldorf
- ▶ Mulligan BioCapital AG (Chairman)
- ▶ IKB Deutsche Industriebank AG
- ▶ Volkswagen AG
- ▶ Deutsche Post AG
- ▷ Scottish Widows Pan European Smaller Companies OEIC (until March 31, 2005)
- ▷ Dr. August Oetker-Gruppe

Dr. Wilfried Robers
Vice President "Solutions to Customers"/Coatings & Colorants Business Unit at Degussa AG
- ▷ Pensionskasse Degussa VVaG

Dr. Erhard Schipporeit
Member of the Board of Management of E.ON AG, Düsseldorf
- ▶ Commerzbank AG
- ▶ HDI V.a.G.
- ▶ Talanx AG
- ▶ SAP AG (from May 12, 2005)
- ▶ Deutsche Börse AG (from October 7, 2005)
- ▷ E.ON Risk Consulting GmbH[1)] (Chairman)
- ▷ E.ON Audit Services GmbH[1)] (Chairman)
- ▷ E.ON Ruhrgas AG[1)]
- ▷ E.ON UK plc[1)]
- ▷ E.ON US Investments Corp.[1)]
- ▷ E.ON IS GmbH[1)] (from January 11, 2005)

Bodo Schmidt
Chairman of the Works Council at Stockhausen GmbH, Krefeld
- ▶ Stockhausen GmbH[1)] (Deputy Chairman)

Dr. Peter Schörner

Member of the Board of Management of RAG Aktiengesellschaft, Essen

- ▶ Deutsche Steinkohle Aktiengesellschaft[1)]
- ▶ RAG Coal International AG[1)] (Deputy Chairman)
- ▶ RAG Immobilien Aktiengesellschaft[1)]
- ▶ RÜTGERS GmbH[1)] (Deputy Chairman) (until June 30, 2005)
- ▶ STEAG Aktiengesellschaft[1)]
- ▷ RAG Beteiligungs-GmbH[1)] (Deputy Chairman of the Advisory Board)
- ▷ RAG BILDUNG GmbH[1)] (Member of the Advisory Board)

Ulrich Terbrack (from July 1, 2005)

Deputy Chairman of the Group Works Council of Degussa AG

Ulrich Weber

Member of the Board of Management of RAG Aktiengesellschaft, Essen

- ▶ Deutsche Montan Technologie GmbH[1)] (Chairman)
- ▶ Deutsche Steinkohle Aktiengesellschaft[1)]
- ▶ RAG Immobilien Aktiengesellschaft[1)] (Chairman)
- ▶ RÜTGERS GmbH[1)] (until June 30, 2005)
- ▶ STEAG Saar Ferngas Aktiengesellschaft[1)]
- ▶ STEAG Saar Energie AG[1)]
- ▶ HDI Privat Versicherung AG
- ▶ HDI Industrie Versicherung AG
- ▶ HDI Service AG
- ▷ RAG Beteiligungs-GmbH[1)] (Member of the Advisory Board)
- ▷ RAG BILDUNG GmbH[1)] (Chairman of the Advisory Board)

Dr. Hans-Dietrich Winkhaus

Member of the Executive Board of Henkel KGaA, Düsseldorf

- ▶ BMW AG
- ▶ Deutsche Lufthansa AG
- ▶ ERGO Versicherungsgruppe AG
- ▶ Schwarz Pharma AG (Chairman)

Board of Management of Degussa AG

Professor Utz-Hellmuth Felcht, CEO
Chairman
- ▶ Gerling-Konzern, Versicherungs-Beteiligungs-AG
- ▶ Goldschmidt GmbH[1)] (Chairman) (until January 10, 2005)
- ▶ RAG Coal International AG[1)]
- ▶ RÜTGERS GmbH[1)] (Chairman) (until June 30, 2005)
- ▶ SGL Carbon AG
- ▶ SKW Metallurgie GmbH[1)] (Chairman) (until January 14, 2005)
- ▷ Degussa (China) Co., Ltd.[1)] (Chairman of the Board)
- ▷ Degussa Japan Co., Ltd.[1)] (Chairman of the Board) (until February 9, 2006)
- ▷ RAG Beteiligungs-GmbH[1)]

Dr. Bernhard Hofmann (from January 1, 2006), COO
- ▶ Infracor GmbH[1)]
- ▶ Oxeno Olefinchemie GmbH[1)] (Chairman)
- ▷ Degussa Corp.[1)], USA
- ▷ Degussa India Pvt. Ltd.[1)] (Member of the Board)
- ▷ Degussa UK Holdings Ltd.[1)] (Chairman of the Board)
- ▷ Vinnolit GmbH & Co. KG

Dr. Alfred Oberholz, CTO
- ▶ EVOTEC AG (from June 2005)
- ▶ Infracor GmbH[1)] (Chairman)
- ▶ RÜTGERS GmbH[1)] (until June 30, 2005)
- ▷ Degussa Corp.[1)], USA
- ▷ Degussa (China) Co., Ltd.[1)] (Member of the Board)
- ▷ Degussa Japan Co., Ltd.[1)] (Member of the Board) (until February 9, 2006)
- ▷ E.ON Ruhrgas AG[1)] (Member of the Advisory Board)

Dr. Thomas Schoeneberg, CHRO
Labor Director
- ▶ Goldschmidt GmbH[1)] (until January 10, 2005)
- ▶ Infracor GmbH[1)]
- ▷ Pensionskasse Degussa VVaG[1)]
- ▷ Degussa CEE Ges. mbH[1)], Vienna (Chairman)
- ▷ Frankfurter Versicherungs-AG
- ▷ RAG BILDUNG GmbH[1)] (Member of the Advisory Board)

Dr. Manfred Spindler (from January 1, 2006), COO

- Goldschmidt GmbH[1)] (Chairman) (from January 31, 2006)
- Industriepark Wolfgang GmbH[1)] (Chairman)
- Röhm Beteiligungs-Gesellschaft mbH[1)] (Chairman)
- Stockhausen GmbH[1)] (Chairman) (from Januar 27, 2006)
- CYRO Industries Inc.[1)], Canada (Chairman)
- Degussa Corp.[1)], USA
- Degussa France Group SAS[1)] (Chairman)
- Degussa Japan Co. Ltd.[1)] (Member of the Board)
- Degussa Australia Pty. Ltd.[1)]

Heinz-Joachim Wagner, CFO

- Goldschmidt GmbH[1)] (until January 10, 2005)
- Degussa Brazil Ltda[1)] (Chairman)
- Degussa Corp.[1)], USA (Chairman of the Board)
- Pensionskasse Degussa VVaG[1)]
- Degussa Bank GmbH
- WestLB (Member of the Economic Advisory Board) (from July 4, 2005)

Directors with power of attorney

Dr. Bernhard Hofmann (until December 31, 2005)

Dr. Peter Pohlmann (until December 31, 2005)

Dr. Manfred Spindler (until December 31, 2005)

Dr. Carl Voigt (until December 31, 2005)

Dr. Heinz Rzehak (from January 1, 2005 to December 31, 2005)

All data refer to the period January 1, 2005 to December 31, 2005
unless otherwise stated.

Glossary

Financial and business terms

ASEAN	Association of South East Asian Nations. ASEAN was established in 1967. The member states are Brunei, Indonesia, Malaysia, the Philippines, Singapore, Thailand, Vietnam (since 1995), Laos (since 1997), Myanmar (since 1997), Cambodia (since 1999).
CEFIC	Conseil Européen des Fédérations de l´Industrie Chimique; English name: European Chemical Industry Council.
COMECON	Council for Mutual Economic Assistance. Economic association of Communist states (Poland, Czechoslovakia, East Germany, Hungary, Romania, Bulgaria, Albania) from 1949 to 1991. Headed by the USSR its purpose was to develop a common economic policy for the member states but it never became an effective counterpart to the EC. Later entrants were Cuba, Mongolia and Vietnam.
Corporate Governance	Corporate governance refers to all aspects of the management and oversight of a company, including its organizational structure, business principles and guidelines and internal and external control and supervisory mechanisms. It thus ensures responsible management of the Degussa Group with a view to sustained value creation.
EBIT (Earnings Before Interest and Taxes)	This profit ratio is a yardstick of the operating performance of an enterprise irrespective of the structure of its assets.
EBITDA (Earnings Before Interest, Taxes, Depreciation and Amortization)	This profit ratio is a yardstick of the operating performance of an enterprise irrespective of the structure of its assets. It is used as an internal controlling parameter in the Degussa Group.
ECP (Euro Commercial Paper)	Bearer promissory notes denominated in euros, generally with a maturity of between 30 and 270 days. Issuers are normally corporations with strong credit ratings. Issues tend to be high volume with a high nominal value. ECP is a money-market instrument. Maturities are not standard; they can be varied to suit the issuers' needs.
GDP (Gross domestic product)	Measure of the economic performance of an economy. It shows the value of all goods and services produced in the domestic economy (value added) that are not precursors for other goods and services. The change in price-adjusted GDP is an indicator of economic growth.
Hedging	A strategy used to offset the exposure of business transactions to risks such as changes in exchange rates, interest rates and raw material prices. The company enters into an additional transaction whose profile is exactly opposite to the profile of the hedged transaction (underlying). Derivative financial instruments such as forward rate agreements, swaps and options are used as hedging tools.
IFRS	International Financial Reporting Standards. Since 2005 all companies listed on stock exchanges in the European Union have been required to prepare consolidated financial statements in accordance with IFRS.

Macro hedge	Transaction to hedge aggregated risks.
Micro hedge	Transaction used to hedge individual risk positions.
NAFTA	North American Free Trade Agreement between the United States, Canada and Mexico. Came into effect on January 1, 1994.
Non-operating result	Balance of non-operating income and expenses. The non-operating result comprises items that are outside normal operations, relate to other reporting periods or are classified as exceptional. They are generally infrequent or one-off events, for example, book gains and losses resulting from major divestments and restructuring charges.
OECD	Organization for Economic Co-operation and Development.
ROCE (Return on capital employed)	Yardstick used to measure the profitability of capital employed. Degussa calculates ROCE by dividing EBIT by the average capital employed in the reporting period.
Swaps, interest swaps, currency swaps	Financial derivatives used to swap cash flows to hedge currency and interest rate risks. Currency swaps comprise swapping payments in different currencies while interest rate swaps comprise swapping fixed interest rates for variable rates.
US GAAP	US Generally Accepted Accounting Principles. Companies listed on a US stock exchange are required to prepare their annual financial statements in accordance with US GAAP.
Volatility	Volatility is a measure of the fluctuation in share prices, exchange rates and interest rates within a given period. It generally expresses the standard deviation of relative changes in prices over a year. The term is often used to denote the fluctuations in prices or interest rates on entire markets.

Chemical and other terms

Amino acids	Components found in proteins. Amino acids (e.g. methionine, lysine) are used in animal feeds and in the treatment of illnesses (e.g. for infusion solutions or as a basis for drugs).
Blu-ray® discs	Blu-ray® discs are expected to replace DVDs. A blue laser is used to access data on these discs, allowing finer data structures and higher data storage capacity. The information is stored far closer to the surface of the disc than on DVDs. Degussa produces EUROPLEX® PC, a film used for protective coatings that meet stringent optical requirements and ensure that the distance between the surface of the disc and the information layer is exactly 0.1 mm.
Catalysis, homogeneous/ heterogeneous	In homogeneous catalysis the catalyst and the substances to be reacted are in the same phase. In heterogeneous catalysis they are in different phases. The advantages of homogeneous catalysis compared with heterogeneous catalysis is that reaction conditions (pressure and temperature) tend to be less severe while selectivity is usually higher. The disadvantage is that it is difficult to separate the catalyst from the reaction mixture.
Emulsifiers	Substances that can combine two liquids that are not miscible. Emulsifiers are used to stabilize oil/water phases. They are widely used in the food and cosmetics industries. The best-known natural emulsifier is lecithin, which is obtained from soy beans and is also found in egg yolk.
Fermentation	From the Latin fermentare. Conversion of substances with the aid of microorganisms. Fermentation has traditionally been used to produce dairy products, wine, beer and bread. Fermentation processes can be used to produce vitamins, enzymes and amino acids cost-effectively.
Ligands	Ligands are small molecules that control the reactivity of catalytically active metal ions.
Monomers	Monomers are simple molecules with a low molecular weight that can react with each other to form polymers.
MTBE/ETBE	Methyl tertiary butylether (MTBE) has been used as an anti-knock agent in gasoline world-wide since 1976, replacing toxic lead additives. An alternative is ethyl tertiary butylether (ETBE), which has very similar properties. It is generated by reacting ethanol (from biomass) with isobutene, a by-product of the processing of crude oil, and contains just under 50 percent bioethanol.
Nano particles	Minute particles measuring between one millionth and 100 millionths of a millimeter. For comparison: A human hair measures 0.02–0.16 mm, making it 20,000–100,000 times thicker than a nano particle. Because nano particles are so tiny, the ratio of surface area to mass is extremely high. This produces completely new effects and can be used to regulate the properties of a range of products, especially in the cosmetics, electronics, optics, coatings and pharmaceuticals sectors.

PEEK	Polyetheretherketones (PEEK) are partially crystalline high-performance polymers with outstanding mechanical properties and very good temperature resistance. In view of their exceptional mechanical, thermal and chemical properties, they are mainly used as components and functional parts in automotive engineering, aviation, electronics and medical appliances.
Polymers/oligomers	Long-chain, short-chain or crosslinked macromolecules produced from smaller molecules (e.g. monomers).
Polymethylmethacrylate (PMMA)	Colorless plastic (acrylic glass) that can be colored. Properties: high transparency, good moldability, extremely good stability to weathering,. Applications: construction, automotive engineering, optics, optoelectornics, household and designer goods, exhibition stands, illuminated signboards, lamps. Best-known brand: PLEXIGLAS® manufactured by Degussa's subsidiary Röhm. Supply form: thermoplastic molding compounds, cast or extruded components (sheet, film, tubes, rods).
Polyurethane (PUR)	Polymers with excellent thermal and sound insulating properties and a very broad spectrum of applications. Flexible foamed PUR is used for cushions, mattresses and interior trims. Rigid PUR is used in automotive engineering, construction and furniture.
Superabsorbents	Crosslinked polymers that are insoluble in water and can absorb and store large quantities of liquid through a mechanism that causes them to swell and form hydrogen gels. The liquid is not released even under pressure.
White biotechnology	Also known as industrial biotechnology. White biotechnology refers to sustainable industrial production processes, especially the use of enzymes and microorganisms to produce intermediates and end-products for the chemicals and pharmaceuticals industry.
World-scale facility	Production plant with the capacity to manufacture products on a global scale. World-scale facilities are often more economical because fixed costs per metric ton decline as production volume rises.

Credits

Published by
Degussa AG
Bennigsenplatz 1
40474 Düsseldorf, Germany
e-mail: info@degussa.com
www.degussa.com

Contact

Corporate Communications
Phone: +49-2 11-6 50 41-2 49
Fax: +49-2 11-6 50 41-3 77
e-mail: info@degussa.com

Investor Relations
Phone: +49-2 11-6 50 41-2 94
Fax: +49-2 11-6 50 41-5 19
e-mail: investor.relations@degussa.com

Concept and Design
Kuhn, Kammann & Kuhn AG, Cologne

Photography
Bernd Vogel, Cologne
Andreas Fechner, Düsseldorf
Chen Dan, Shanghai

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Financial diary 2006

March 3, 2006:	Financial Press Conference (Düsseldorf)
May 9, 2006:	Interim Report January–March 2006
May 29, 2006:	Annual Shareholders' Meeting
August 8, 2006:	Interim Report January–June 2006
November 8, 2006:	Interim Report January–September 2006 and Fall Press Conference (Düsseldorf)

Degussa AG
Bennigsenplatz 1
40474 Düsseldorf
Germany
www.degussa.com