Interim Group Management Report

as of September 30, 2012

- Challenging macroeconomic environment
- Sales down by 7.6% against the very strong prior-year quarter
- Declining raw material costs lead to price adjustments
- Scheduled maintenance shutdowns and weaker demand impact earnings
- EBITDA pre exceptionals decreases from €311 million to €255 million
- EBITDA margin 11.8% compared to 13.3% in the prior-year quarter
- Net income and earnings per share recede to €94 million and €1.13, respectively
- Net financial liabilities show a business-related increase since year end 2011 to €1,606 million, but shrink compared to the preceding quarter
- Guidance for 2012: growth in EBITDA pre exceptionals compared to 2011 at the lower end of the 5%–10% range
- New medium-term target: €1.8 billion EBITDA pre exceptionals in 2018

Group structure

Legal structure

LANXESS AG is the parent company of the LANXESS Group and functions largely as a management holding company. LANXESS Deutschland GmbH and LANXESS International Holding GmbH are wholly owned subsidiaries of LANXESS AG and control the other subsidiaries and affiliates both in Germany and elsewhere.

A list of the principal direct and indirect subsidiaries of LANXESS AG and a description of the Group's management and control organization are provided on page 71 of the Annual Report 2011.

Key additions to the Group portfolio

During the first nine months of 2012, we made one acquisition in the United States and one acquisition in Germany to strengthen the Group portfolio. Details are provided in the Notes to the Condensed Consolidated Interim Financial Statements as of September 30, 2012.

Business and strategy

As predicted, there have been no changes to the Group's organizational structure or strategy so far this year. The LANXESS Group continues to be structured in three segments with 13 business units, each of which conducts its own operations and has global profit responsibility. These are supported by centralized services and by local organizations in the countries. Further details are given on pages 72–74 of the Annual Report 2011.

There were no material changes to the production basis, product portfolio or key customer industries in the reporting period.

Business trends and economic environment

Business conditions

General economic situation The risks in the international financial sector discussed in the previous quarter's report continue to apply, despite the announcements by the European Central Bank and the expanded multilateral protection mechanisms in the eurozone. The resulting uncertainty and the austerity measures introduced in the affected economies continued to slow the pace of global growth in the third quarter of 2012. The economy in Western Europe, particularly, was weak and shrank by 0.5%. Growth in the United States was on the level of the previous quarter at 1.5%. The 7.4% growth rate in China also matched the second quarter.

Chemical industry The global chemical industry continued to grow in the third quarter of 2012, albeit somewhat more slowly than in the preceding quarter. Production in Germany was at the previous quarter's level. Against the same period a year ago, however, output was down by 2.5%. The picture for the European Union as a whole was similar, with production in the chemical industry down by 2% from the prior-year level. By contrast, the North American chemical industry raised production by 2%.

Evolution of major user industries Growth in global automobile production weakened considerably in the reporting period, with regional variations persisting. North America and China remained the main drivers of growth, with gains of 10% and 9%, respectively, from the prior-year period. Production in Europe fell by 11% because of the economic situation in some countries. Third-quarter production in Latin America decreased by 4%. The tire industry was also affected by the negative market development. Global production of OEM truck tires declined in line with the reduced demand for new vehicles. The replacement tire business was also sluggish, with only Latin America showing signs of a positive trend. Europe's car tire market experienced softer demand in both the OEM and replacement tire segments compared to the same period a year ago. By contrast to the preceding quarter, demand for replacement tires in North America dropped by 4%, while it grew by a similar percentage in Latin America.

Construction demand in Europe varied, remaining low especially in the crisis countries of Western Europe but growing in certain parts of Eastern Europe, for example. Demand in the U.S. construction market also continued to develop positively.

The demand for agrochemicals remained at a gratifying level.

Comparison of forecast and actual business

Comparison of Forecast and Actual Business in 2012

	Forecast for 2012 in Annual Report 2011 & Q1 Interim Report	Forecast for 2012 in H1 Interim Report	Actual Q3 Interim Report 9M 2012
Raw material prices	volatile, long-term trend upward	volatile, long-term trend upward	returned to level of early 2012
Research and development			
Research and development expenses	+40%	+40%	9M: +40%
Business development: segments			
Performance Polymers	solid business performance	solid business performance	9M: Sales +6%
Advanced Intermediates	solid business performance	solid business performance	9M: Sales +4%
Performance Chemicals	solid business performance	solid business performance	9M: Sales +4%
Business development: Group			
EBITDA pre exceptionals	5% to 10% increase	5% to 10% increase	9M: €986 million
Financial condition: Group			
Cash outflows for capital expenditures	€600 million	€650 – 700 million	9M: €381 million

Based on the assumption that the general trend toward higher procurement costs, especially for petrochemical raw materials, could continue even beyond 2012, we had forecast volatile raw material prices. While raw material prices rose in the first months of the year, the trend reversed toward the end of the second quarter and led to declining raw material prices in the third quarter as well. Butadiene accounted for a large part of this volatility. Developments thus far are therefore consistent with our initial assumptions. We still expect raw material prices to continue increasing over the long term.

In light of our targeted research and development activities, designed to enable us to generate our own customer- and market-oriented innovations and process improvements, expenditures in this area increased by 40% so far this year. This is the same percentage increase as we expect for the full year. The emphasis was on the Performance Polymers segment, which accounted for around 58% of R&D spending.

The year-to-date performance of our segments shows a positive sales trend that has been fueled by positive price and currency effects and negative volume effects. Based on our assessment and with our price-before-volume strategy intact, the performance of our business remains solid.

In the half-year financial report, we confirmed the forecast we had issued after the first quarter for an increase in EBITDA pre exceptionals in 2012 compared with 2011. We also estimated that we would achieve EBITDA pre exceptionals in the second half of 2012 on the level of the second half of 2011. Earnings of €986 million were recorded in the first nine months, slightly above the level of the prior-year period. As usual, our current guidance for the year can be found in the Outlook section of this interim management report.

Sales

Group sales in the third quarter came to €2,159 million, down €177 million or 7.6% from the same period a year ago. Sales were supported by a slight portfolio effect of 0.5% and by positive currency effects of 5.4% that were largely attributable to the U.S. dollar. An overall 7.1% adjustment in selling prices driven by the drop in raw material costs – especially in the Performance Polymers segment – hampered sales development, as did a 6.4% decline in volumes. After adjusting for portfolio and currency effects, operational sales were thus 13.5% lower than in the prior-year quarter.

Effects on Sales

%	Q3 2012	9M 2012
Price	(7.1)	1.6
Volume	(6.4)	(4.8)
Currency	5.4	4.7
Portfolio	0.5	3.3
	(7.6)	**4.8**

Compared to the third quarter of 2011, the performance of our Performance Polymers segment was affected by the adjustment in selling prices caused by the lower raw material costs, particularly for the key raw material butadiene, and by declining volumes. Positive shifts in exchange rates had the opposite effect. The segment's sales receded by 16.8% overall.

By contrast, sales of the Advanced Intermediates segment rose by 8.6% against the prior-year quarter. In light of continuing heavy demand for agrochemicals, we were able to raise volumes and selling prices, with price increases for raw materials, particularly toluene and benzene, being passed along to the market. Sales growth was supported by positive currency effects.

The Performance Chemicals segment grew sales by 6.1% compared to the prior-year quarter. With volumes stable, modest declines in prices were amply offset by favorable changes in currency parities and the contributions from the acquisitions made in our Rhein Chemie, Functional Chemicals and Material Protection Products business units in the previous quarters.

LANXESS experienced lower demand in all regional markets. Latin America was the most-affected region, while Germany proved to be the company's most resilient region with only a 5% decrease in sales. The decline in sales in all markets reflected the negative price and volume trends in major customer industries. Business development in the Performance Polymers segment was largely responsible for the overall drop in sales.

Order book status

Most of our business is not subject to long-term agreements on fixed volumes or prices. Instead, our business is characterized by long-standing relationships with customers and revolving master agreements. Our activities are focused on demand-driven orders with relatively short lead times which do not provide a basis for forward-looking statements about our capacity utilization or volumes. Our business is managed primarily on the basis of regular Group-wide forecasts with respect to Group operating targets.

Any disclosure of the Group's order book status at a given reporting date therefore would not be indicative of the Group's short- or medium-term earning power. For this reason, no such disclosure is made in this report.

Gross profit

The cost of sales declined in the third quarter by 5.9% to €1,698 million, mainly because of the substantially lower raw material costs and also due to lower volumes than in the prior-year quarter. In particular, prices for the key raw material butadiene moved downward. By contrast, the cost of sales was increased by currency effects.

Sales by Segment

€ million	Q3 2011	Q3 2012	Change %	Proportion of Group sales %	9M 2011	9M 2012	Change %	Proportion of Group sales %
Performance Polymers	1,433	1,192	(16.8)	55.2	3,798	4,010	5.6	57.5
Advanced Intermediates	371	403	8.6	18.7	1,182	1,231	4.1	17.7
Performance Chemicals	523	555	6.1	25.7	1,640	1,698	3.5	24.3
Reconciliation	9	9	0.0	0.4	32	32	0.0	0.5
	2,336	**2,159**	**(7.6)**	**100.0**	**6,652**	**6,971**	**4.8**	**100.0**

Gross profit came in at €461 million, down by 13.2% against the same quarter a year ago. The gross profit margin receded from 22.7% to 21.4%. The softer demand led to a corresponding drop in volumes and thus to lower gross profit. The significantly lower capacity utilization compared to the prior-year quarter led to increased idle capacity costs that impacted the gross profit. Expenses were also incurred in connection with scheduled maintenance shutdowns, particularly in the Performance Polymers segment. Exchange rates, however, had a positive net effect.

EBITDA and EBIT

In the third quarter of 2012 the operating result before depreciation and amortization (EBITDA) pre exceptionals declined by €56 million, or 18.0%, year on year to €255 million. The decrease was mainly due to negative volume effects resulting from lower demand. Sharply lower raw material costs were offset by corresponding adjustments to selling prices. Selling expenses were at the prior-period level of €183 million. Research expenditures came to €49 million, versus €40 million in the prior-year period, due to the expansion of our research activities as part of the LANXESS Technology Initiative. Earnings were supported by the favorable movements in exchange rates. The Group EBITDA margin pre exceptionals declined from 13.3% to 11.8%.

Third-quarter EBITDA pre exceptionals in our Performance Polymers segment came to €152 million, down €61 million from the prior-year period. Lower raw material costs were offset by selling price adjustments. Lower volumes and scheduled maintenance shutdowns led to lower capacity utilization, with a corresponding negative impact on earnings. Positive exchange rate developments had the opposite effect.

EBITDA pre exceptionals in the Advanced Intermediates segment, at €75 million, surpassed the prior-year quarter's €68 million by €7 million, or 10.3%. Positive price effects compensated for the higher raw material costs. The earnings improvement was attributable to volume gains and exchange rate developments.

EBITDA pre exceptionals in our Performance Chemicals segment was unchanged from the prior-year level of €75 million. The relief resulting from lower raw material costs led to selling price adjustments in the segment as a whole. Volumes remained at the previous year's level in light of comparable demand. The positive effect from shifts in exchange rates was accretive to earnings, which were also supported by a minor portfolio effect from the acquisitions made in the previous quarters.

The Group operating result (EBIT) came to €156 million in the third quarter of 2012, compared to €223 million in the year-earlier period. The exceptional charges included in other operating expenses totaled €4 million, the full amount of which impacted EBITDA. They related to expenses for the design and implementation of IT projects and for corporate transactions. Exceptional charges in the prior-year quarter came to €5 million.

Financial result

The financial result in the third quarter of 2012 came to minus €34 million, against minus €23 million in the same period last year. Interest expense, at €25 million, was nearly level with the previous year's €27 million. Construction-period borrowing costs relating to the major capital expenditure project to build a new butyl rubber plant in Singapore were capitalized in both periods. The investment of liquid assets generated interest income of €1 million, against €5 million in the prior-year period. The pro-rated earnings of companies accounted for in the consolidated financial statements using the equity method, mainly Currenta GmbH & Co. OHG, decreased from €7 million in the prior-year quarter to minus €3 million in the reporting period.

Income before income taxes

Income before income taxes decreased in line with the lower third-quarter operating result from €200 million to €122 million. The effective tax rate was 23.0%, the same as in the prior-year period.

EBITDA Pre Exceptionals by Segment

€ million	Q3 2011	Q3 2012	Change %	9M 2011	9M 2012	Change %
Performance Polymers	213	152	(28.6)	641	664	3.6
Advanced Intermediates	68	75	10.3	208	224	7.7
Performance Chemicals	75	75	0.0	260	236	(9.2)
Reconciliation	(45)	(47)	(4.4)	(137)	(138)	(0.7)
	311	**255**	**(18.0)**	**972**	**986**	**1.4**

Net income and earnings per share

As in the prior year, non-controlling interests accounted for less than €1 million of third-quarter income. Net income for the third quarter of 2012 amounted to €94 million, compared with €154 million in the prior-year period. With the number of LANXESS shares in circulation unchanged, earnings per share, at €1.13, were below the €1.85 achieved in the same quarter of last year.

Business trends by region

Sales in the EMEA region (excluding Germany) receded by 9.1% to €596 million in the third quarter of 2012. Adjusted for currency and portfolio effects, sales were down by 10.2%. The decrease was mainly the result of business development in the Performance Polymers segment, where the drop in sales was well into double digits. By contrast, sales of the Advanced Intermediates segment rose by a high-single-digit percentage. The Performance Chemicals segment sustained the previous year's sales level. Sales in this region saw the largest declines in Italy, Spain, the United Kingdom and Turkey. However, BRICS countries Russia and South Africa recorded higher sales compared to the prior-year quarter.

With a 27.6% share of total sales against 28.1% in the same quarter a year ago, EMEA (excluding Germany) remains the largest of the LANXESS Group's regions in terms of sales.

In Germany, our sales in the third quarter of 2012 were down by 3.7% to €392 million. Adjusted for portfolio effects, the decrease came to 4.7%. The overall drop in business was attributable to the Performance Polymers and Performance Chemicals segments. By contrast, the Advanced Intermediates segment lifted sales by a low-double-digit percentage compared to the prior-year period.

Germany's share of Group sales came to 18.2% for the quarter, against 17.4% for the same period a year ago.

Sales in North America in the third quarter of 2012 moved back by 2.5% to €391 million. Adjusted for currency and portfolio effects, the decrease came to 16.8%. This development was again mainly attributable to the Performance Polymers segment, where sales receded by a double-digit percentage. Sales in the Advanced Intermediates and Performance Chemicals segments were also lower than in the year-earlier period, with declines in the low single digits.

North America's share of Group sales amounted to 18.1% for the quarter, against 17.2% in the prior-year period.

Sales in Latin America receded by a substantial 18.7% to €287 million in the third quarter of 2012. The decrease – amounting to 25.6% after adjusting for currency and portfolio effects – was due to the development of the Performance Polymers segment. Lower raw material costs led to selling price adjustments, which in turn resulted in a tangible decrease in sales. By contrast, the Advanced Intermediates segment grew sales by a mid-single-digit percentage. The Performance Chemicals segment also performed well, with sales growth in the low double digits. The modest business development in Brazil was the dominant factor in this region's performance.

The region's share of Group sales came to 13.3% for the quarter, against 15.1% for the same period a year ago.

Third-quarter sales in the Asia-Pacific region shrank by 5.0% to €493 million. Adjusted for currency and portfolio effects, the decrease came to 13.9%. All segments were affected, especially Performance Polymers with a decline in the double digits. Sales in the Advanced Intermediates and Performance Chemicals segments receded by single-digit percentages. China, Hong Kong and Taiwan accounted for a large proportion of the drop in business in this region, while some other countries, such as Malaysia, posted small gains in absolute terms.

LANXESS generated 22.8% of the Group's quarterly sales in this region, compared with 22.2% in the prior-year period.

Sales by Market

	Q3 2011		Q3 2012		Change	9M 2011		9M 2012		Change
	€ million	%	€ million	%	%	€ million	%	€ million	%	%
EMEA (excluding Germany)	656	28.1	596	27.6	(9.1)	1,963	29.5	1,945	27.9	(0.9)
Germany	407	17.4	392	18.2	(3.7)	1,216	18.3	1,204	17.3	(1.0)
North America	401	17.2	391	18.1	(2.5)	1,097	16.5	1,253	18.0	14.2
Latin America	353	15.1	287	13.3	(18.7)	904	13.6	919	13.2	1.7
Asia-Pacific	519	22.2	493	22.8	(5.0)	1,472	22.1	1,650	23.6	12.1
	2,336	**100.0**	**2,159**	**100.0**	**(7.6)**	**6,652**	**100.0**	**6,971**	**100.0**	**4.8**

Segment information

Performance Polymers

	Q3 2011		Q3 2012		Change	9M 2011		9M 2012		Change
	€ million	Margin %	€ million	Margin %	%	€ million	Margin %	€ million	Margin %	%
Sales	1,433		1,192		(16.8)	3,798		4,010		5.6
EBITDA pre exceptionals	213	14.9	152	12.8	(28.6)	641	16.9	664	16.6	3.6
EBITDA	211	14.7	151	12.7	(28.4)	639	16.8	661	16.5	3.4
Operating result (EBIT) pre exceptionals	168	11.7	99	8.3	(41.1)	524	13.8	513	12.8	(2.1)
Operating result (EBIT)	166	11.6	98	8.2	(41.0)	522	13.7	510	12.7	(2.3)
Cash outflows for capital expenditures[1]	88		93		5.7	200		241		20.5
Depreciation and amortization	45		53		17.8	117		151		29.1
Employees as of September 30 (previous year: as of Dec. 31)	4,977		5,317		6.8	4,977		5,317		6.8

1) Intangible assets and property, plant and equipment

The positive business development seen in the Performance Polymers segment in the first half of 2012 did not continue in the third quarter. Sales decreased by 16.8% to €1,192 million against the strong prior-year quarter. Selling prices were reduced by 12.0% due to the drop in raw material procurement prices, especially for butadiene. Volumes receded by 10.8% due to the lower demand, while currency factors had a 6.0% positive effect.

The lower prices and the drop in volumes affected all of the segment's business units. In the Performance Butadiene Rubbers business unit, there was less demand for standard-quality rubber grades, especially in Latin America. Demand for high-performance rubber grades, however, remained robust. The Butyl Rubber business unit, which like Performance Butadiene Rubbers has close ties to the tire industry and therefore to the replacement tire and OEM tire markets, experienced a drop in prices and volumes, particularly in Asia. The Technical Rubber Products business unit registered lower demand from the automotive industry. The High Performance Materials (formerly Semi-Crystalline Products) business unit, which generates a substantial portion of its sales with customers in the automotive and electrical/electronics industries, posted a slight decrease in volumes, especially in Europe. However, the demand in Asia and the United States had a mitigating effect. Segment sales receded in all regions.

EBITDA pre exceptionals in the Performance Polymers segment fell by a substantial €61 million to €152 million, mainly because of the idle capacity costs related to the lower demand and the expenses for scheduled maintenance shutdowns. All business units were affected. Capacity utilization was below the level of the prior-year quarter due to the factors mentioned. Lower raw material costs led to an adjustment in selling prices at the segment level. Exchange rate developments had a positive effect on earnings. The segment's third-quarter EBITDA margin was down from 14.9% to 12.8%.

The exceptional charges of €1 million in EBITDA – like the €2 million figure for the third quarter of 2011 – related to corporate transactions.

Advanced Intermediates

	Q3 2011		Q3 2012		Change	9M 2011		9M 2012		Change
	€ million	Margin %	€ million	Margin %	%	€ million	Margin %	€ million	Margin %	%
Sales	371		403		8.6	1,182		1,231		4.1
EBITDA pre exceptionals	68	18.3	75	18.6	10.3	208	17.6	224	18.2	7.7
EBITDA	68	18.3	75	18.6	10.3	208	17.6	224	18.2	7.7
Operating result (EBIT) pre exceptionals	52	14.0	58	14.4	11.5	158	13.4	174	14.1	10.1
Operating result (EBIT)	52	14.0	58	14.4	11.5	158	13.4	174	14.1	10.1
Cash outflows for capital expenditures [1]	26		22		(15.4)	59		54		(8.5)
Depreciation and amortization	16		17		6.3	50		50		0.0
Employees as of September 30 (previous year: as of Dec. 31)	2,883		2,855		(1.0)	2,883		2,855		(1.0)

1) Intangible assets and property, plant and equipment

Sales in the Advanced Intermediates segment rose by 8.6% to €403 million in the third quarter of 2012. Selling prices were raised by 3.5% due to higher procurement prices for raw materials. Volumes increased by 1.6% in light of the steady demand. In addition, shifts in exchange rates gave a positive effect of 3.5%.

The positive demand situation for agrochemicals persisted in the third quarter of 2012, supporting both of the segment's business units. The Saltigo business unit benefited from this through higher volumes, while the Advanced Industrial Intermediates business unit achieved year-on-year volume growth in its sale of products from the integrated aromatics production network to the agrochemical industry. Higher demand from customers in the flavors and fragrances industry helped to compensate for lower volumes of products for the construction industry. Higher prices for raw materials, including toluene and benzene, were passed along to the market in the form of selling price adjustments. In regional terms, Germany was the growth engine in this segment, posting the largest increase in business in absolute and relative terms.

EBITDA pre exceptionals in the Advanced Intermediates segment increased by €7 million to €75 million against the prior-year quarter, partly due to the higher volumes and to favorable shifts in exchange rates. The inflation in raw material costs was offset by price adjustments at the segment level. The EBITDA margin rose against the already strong prior-year level from 18.3% to 18.6%.

Performance Chemicals

	Q3 2011		Q3 2012		Change	9M 2011		9M 2012		Change
	€ million	Margin %	€ million	Margin %	%	€ million	Margin %	€ million	Margin %	%
Sales	523		555		6.1	1,640		1,698		3.5
EBITDA pre exceptionals	75	14.3	75	13.5	0.0	260	15.9	236	13.9	(9.2)
EBITDA	75	14.3	75	13.5	0.0	260	15.9	221	13.0	(15.0)
Operating result (EBIT) pre exceptionals	55	10.5	54	9.7	(1.8)	203	12.4	173	10.2	(14.8)
Operating result (EBIT)	55	10.5	54	9.7	(1.8)	203	12.4	156	9.2	(23.2)
Cash outflows for capital expenditures [1]	31		29		(6.5)	59		61		3.4
Depreciation and amortization	20		21		5.0	57		65		14.0
Employees as of September 30 (previous year: as of Dec. 31)	5,819		6,030		3.6	5,819		6,030		3.6

1) Intangible assets and property, plant and equipment

Sales in the Performance Chemicals segment advanced by 6.1% to €555 million in the quarter under review. Selling prices were adjusted by 1.5% in view of lower procurement prices. Volumes held steady at just 0.2% below the previous year's level. A portfolio effect of 2.5% from the recent acquisitions in North America and favorable exchange rate effects of 5.3% factored heavily into the sales growth.

Volumes remained stable compared to the prior-year quarter, but development varied from one business unit to another. Lower demand and inventory reductions by customers in the tire and automotive industries led to lower volumes in the Rhein Chemie and Rubber Chemicals business units. The Inorganic Pigments business unit registered a small increase in demand from the Asian construction industry and raised volumes slightly, with selling prices at the previous year's level. The Leather business unit suffered from lower chrome ore prices and instability of the CO_2 supply at the site in Newcastle, South Africa. In the Material Protection Products business unit, lower volumes were more than offset by higher selling prices and a positive portfolio effect.

EBITDA pre exceptionals in the Performance Chemicals segment equaled the prior-year period at €75 million. Lower raw material costs led to an adjustment in selling prices at the segment level. Volumes were at the level of the prior-year period due to the stable demand. Capacity utilization decreased on account of maintenance shutdowns, and this adversely affected earnings. By contrast, earnings were improved by exchange rate developments and the portfolio effect from the acquired businesses. The segment's EBITDA margin came in at 13.5%, against 14.3% in the same quarter a year ago.

Reconciliation

	Q3 2011	Q3 2012	Change	9M 2011	9M 2012	Change
	€ million	€ million	%	€ million	€ million	%
Sales	9	9	0.0	32	32	0.0
EBITDA pre exceptionals	(45)	(47)	(4.4)	(137)	(138)	(0.7)
EBITDA	(48)	(50)	(4.2)	(150)	(146)	2.7
Operating result (EBIT) pre exceptionals	(47)	(51)	(8.5)	(146)	(148)	(1.4)
Operating result (EBIT)	(50)	(54)	(8.0)	(159)	(156)	1.9
Cash outflows for capital expenditures [1]	3	8	> 100	7	25	> 100
Depreciation and amortization	2	4	100.0	9	10	11.1
Employees as of September 30 (previous year: as of Dec. 31)	2,711	2,876	6.1	2,711	2,876	6.1

1) Intangible assets and property, plant and equipment

EBITDA pre exceptionals for the reconciliation came to minus €47 million, compared with minus €45 million in the prior-year quarter. Among the main factors here was the planned expansion of the central research activities. The €3 million in exceptional charges reported in the reconciliation for the third quarter related mainly to expenses for the design and implementation of IT projects.

Statement of financial position and financial condition

Structure of the statement of financial position

As of September 30, 2012, the LANXESS Group had total assets of €6,965 million, up €87 million, or 1.3%, from €6,878 million on December 31, 2011. The main reasons for the increase were the higher net working capital and purchases of property, plant and equipment. The decrease in liquid assets had the opposite effect.

Non-current assets rose by €110 million to €3,599 million. The intangible assets and property, plant and equipment included in this figure increased by €149 million to €3,201 million. Cash outflows for purchases of property, plant, equipment and intangible assets, at €381 million, were well above the figure of €325 million as of September 30, 2011 on account of our targeted growth strategy. Depreciation and amortization in the first nine months totaled €276 million, compared with €233 million in the prior-year period. The first-time consolidation of Tire Curing Bladders, LLC, Little Rock, United States, which was acquired in the first quarter of 2012, and Bond-Laminates GmbH, Brilon, Germany, which was acquired in the quarter under review, also had an impact on non-current assets, leading to additions in the double-digit million range. The increase in the carrying amount of investments accounted for using the equity method was chiefly attributable to the positive earnings of Currenta GmbH & Co. OHG and LANXESS-TSRC (Nantong) Chemical Industrial Co., Ltd., China, in the reporting period. The change in investments in other affiliated companies was partly due to the purchase of a strategic minority interest in BioAmber, Inc., Minneapolis, United States, in the first quarter of 2012 and the mark-to-market valuation of the interest in Gevo Inc., Englewood, United States, in light of the recent development of its share price. The ratio of non-current assets to total assets was 51.7%, up slightly from 50.7% on December 31, 2011.

Current assets amounted to €3,366 million, down €23 million, or 0.7%, from December 31, 2011. Inventories rose by €215 million to €1,601 million compared to year end 2011. This was slightly above their level at the reporting date for the first half of the year and is attributable to the fact that the declining demand outweighed an expected decrease in inventories for scheduled maintenance shutdowns. The balance of cash and cash equivalents and near-cash assets decreased by a substantial €226 million to €302 million, largely as a result of the scheduled redemption of the Euro Benchmark Bond issued in 2005. The ratio of current assets to total assets was 48.3% against 49.3% as of December 31, 2011.

The LANXESS Group has significant internally generated intangible assets that are not reflected in the statement of financial position due to accounting rules. These include the brand equity of LANXESS and the value of the Group's other brands. A variety of measures were deployed in the reporting period to continually enhance these assets. These measures contributed to the continued success in positioning the business units in the market.

Our established relationships with customers and suppliers also constitute a significant intangible asset, which cannot, however, be reflected in the statement of financial position. These long-standing partnerships with customers and suppliers, built on trust and consistently high product quality, enable us to firmly adhere to our price-before-volume strategy. Our specific competence in technology and innovation, also a valuable asset, is rooted in our specific knowledge in the areas of research and development and custom manufacturing. In this way we generate significant added value for our customers.

Our commercial success is also founded on the knowledge and experience of our employees. In addition, we have sophisticated production and business processes that create competitive advantages for us in the relevant markets.

Equity grew by €239 million, or 11.5%, compared with December 31, 2011, to €2,313 million, predominantly due to the net income of €463 million for the first nine months of the year. The principal offsetting items were negative effects in other equity components from the development of pension obligations. The ratio of equity to the Group's total assets reached 33.2% as of September 30, 2012, against 30.2% as of December 31, 2011.

Non-current liabilities grew by €392 million to €3,107 million as of September 30, 2012. In addition to the three-year CNH 500 million (roughly €60 million) Chinese off-shore renminbi bond that we placed in the first quarter of 2012, we issued two further bonds with a volume of €100 million each and maturities of 10 and 15 years, respectively. The main reason for the €200 million increase in pension provisions to €879 million was the change in the discount rates used for measurement due to the fall in market rates of interest in Germany. The ratio of non-current liabilities to total assets amounted to 44.6%, against 39.5% as of December 31, 2011.

Current liabilities came to €1,545 million, down by €544 million, or 26.0%, from December 31, 2011. The decrease resulted mainly from the scheduled redemption of the Euro Benchmark Bond issued in 2005. In addition, trade payables declined by €112 million to €654 million due to the slight decrease in manufacturing activity. The ratio of current liabilities to total assets amounted to 22.2% as of September 30, 2012, against 30.3% as of year end 2011.

Financial condition and capital expenditures

Changes in the statement of cash flows Net operating cash flow in the first nine months of 2012 amounted to €424 million, compared with €411 million in the prior-year period. With income before income taxes amounting to €599 million, the increase in net working capital compared to December 31, 2011 resulted in a cash outflow of €339 million. The corresponding cash outflow in the prior-year period was €518 million. The development in both periods was mainly attributable to the business-driven increase in inventories and receivables and preparations for maintenance shutdowns, along with higher raw material prices. The changes in other assets and liabilities relate in part to payments that had to be made to counterparties under roll-over hedges for intra-Group foreign currency loans due to the marked decrease in the value of the euro. These payments did not affect earnings.

There was a €17 million net cash inflow from investing activities in the first nine months of 2012, compared with a €540 million net cash outflow in the same period a year ago. Cash inflows in the reporting period mainly comprised receipts of €432 million from financial assets. These were mainly attributable to the sale of near-cash assets and were partially offset by the disbursements for the 3.4% stake in BioAmber, Inc., United States. Cash outflows for purchases of intangible assets, property, plant and equipment totaled €381 million, following €325 million in the prior-year period. Depreciation and amortization came to €276 million. Cash outflows for the acquisition of subsidiaries, less acquired cash and adjusted for subsequent purchase price adjustments, amounted to €44 million. The companies acquired were Tire Curing Bladders, LLC, Little Rock, United States, and Bond-Laminates GmbH, Brilon, Germany.

Financing activities resulted in a net cash outflow of €316 million, compared with a €210 million net cash inflow from financing activities in the first nine months of 2011. Cash outflows in the reporting period related mainly to the scheduled redemption of the Euro Benchmark Bond issued in 2005, interest payments, and the dividend payment to LANXESS AG stockholders for fiscal 2011. These were partially offset by the issuance of two long-term bonds with a volume of €100 million each and a Chinese off-shore renminbi bond with a volume of CNH 500 million, equivalent to €60 million.

Financing and liquidity The principles and objectives of our financial management discussed on page 92 of the Annual Report 2011 have remained valid during the current fiscal year. They are centered on a conservative financial policy built on long-term, secured financing.

Cash and cash equivalents increased by €124 million compared with the end of 2011, to €302 million. The €350 million of instant-access investments in money market funds reported under near-cash assets at year end 2011 was liquidated in connection with the redemption in the reporting period of the remaining €402 million of the Euro Benchmark Bond issued in 2005.

At the beginning of April 2012 we made two private placements under our debt issuance program: a €100 million bond with a 10-year term and a 3.5% coupon, and a second €100 million bond with a 15-year term and a 3.95% coupon. The proceeds have contributed to safeguarding long-term liquidity and further improving the maturity profile of the company's financial debt.

Net financial liabilities totaled €1,606 million as of September 30, 2012, compared with €1,515 million as of December 31, 2011. The near-cash assets of €350 million recognized in the statement of financial position as of December 31, 2011, were sold. Cash and cash equivalents, however, rose by €124 million.

Net Financial Liabilities

€ million	Dec. 31, 2011	Sep. 30, 2012
Non-current financial liabilities	1,465	1,704
Current financial liabilities	633	236
less		
Liabilities for accrued interest	(55)	(32)
Cash and cash equivalents	(178)	(302)
Near-cash assets	(350)	0
	1,515	**1,606**

Financing instruments off the statement of financial position As of September 30, 2012, LANXESS had no material financing items not reported in the statement of financial position, such as factoring, asset-backed structures or sale-and-lease-back transactions.

Significant capital expenditure projects Significant capital expenditures in the Performance Polymers segment were related to the construction of the new butyl rubber facility in Singapore for the Butyl Rubber business unit. The facility is scheduled to go on stream in the first quarter of 2013. Also in Singapore, the Performance Butadiene Rubbers business unit broke ground for the world's largest production facility for neodymium-catalyzed performance butadiene rubber (Nd-PBR), which will have an annual capacity of 140,000 tons. This facility is due on stream in the first half of 2015. In Changzhou, China, our Technical Rubber Products business unit is currently building the world's largest manufacturing plant for ethylene-propylene-diene (EPDM) rubber. This plant, which will utilize the innovative Keltan ACE technology, is also scheduled to start up in 2015. At the site in Geleen, Netherlands, 50% of production will be converted to the Keltan ACE technology. This work is due for completion in 2013. Our High Performance Materials (formerly Semi-Crystalline Products) business unit opened a new compounding plant in Gastonia, United States, in the third quarter. In addition, the business unit and U.S. chemical company DuPont doubled the capacity of their joint compounding facility for polybutylene terephthalate (PBT) in Hamm-Uentrop, Germany. We are also investing in a new world-scale facility for polyamide plastics with an annual capacity of around 90,000 tons at the site in Antwerp, Belgium. Completion of that facility is expected in the first quarter of 2014.

The Advanced Intermediates segment's Advanced Industrial Intermediates business unit is expanding cresol production at the site in Leverkusen, Germany. Completion is expected by mid-2013. This follows the expansion of menthol production in the first half of 2012 and the start-up of the new formalin plant at the site in Krefeld-Uerdingen, Germany.

The Rhein Chemie business unit in the Performance Chemicals segment is building a facility for manufacturing rubber additives and release agents in Lipetsk, Russia, with production scheduled to start in the first half of 2013. Another plant for release agents and additives was commissioned at the site in Jhagadia, India, at the beginning of 2012.

Also in Jhagadia, the Material Protection Products business unit completed the construction of a production plant for biocides. The Leather business unit is building a facility for leather chemicals with an annual capacity of up to 50,000 tons at the site in Changzhou, China. This plant, which is due on stream in the first half of 2013, will feature the latest technology. We are also investing in the construction of a CO_2 concentration unit at the site in Newcastle, South Africa, which is scheduled to start up in the second half of 2013.

Research and development

We are continuing to systematically expand our research and development activities in 2012. Existing products and processes are being refined and optimized with a short- to medium-term time horizon. The Innovation & Technology Group Function, in particular, initiates medium- to long-term research projects to ensure the company's success in future growth areas and thus safeguard its viability going forward. With energy prices climbing, we created a central energy task force within this group function. Comprising experts from various disciplines, the task force implements energy efficiency projects and acts as a Group center of energy technology competence.

Third-quarter research and development expenses were €49 million, or 2.3% of sales. These functional costs rose by 22.5% compared to the prior-year period. In the nine months from January to September 2012, the increase was 40.0%. We are resolutely pursuing the goal we defined in our Annual Report 2011 (page 105) of aligning our research programs in the future more directly and more systematically with the major global megatrends that are significant to our activities: mobility, urbanization, agriculture and water.

Important research projects were advanced in the Performance Polymers segment, which focuses on the mobility trend. Investments in this segment have included the optimization of high-performance rubbers that help improve the braking performance, abrasion resistance and wet grip of tires. As part of this effort, we developed a concept tire that has already received a AA rating in accordance with the new E.U. tire labeling regulations for fuel efficiency and wet grip. Our high-performance rubber Nd-PBR also contributes to improved tire life. In this way, we are cementing our position as the leading company in the field of specialty chemicals for "Green Mobility." Sustainability in raw material sourcing is also particularly important. In this area, LANXESS is focusing on bio-based rubber. Since the end of 2011, the company has been marketing various grades of EPDM rubber made of ethylene derived from sugarcane rather than from oil. The Performance Chemicals segment is also setting trends in the area of research and development. Following the successful start-up of the membrane production plant in Bitterfeld, Germany, we added new membrane separation elements with high rejection and high flow rates to our product portfolio. We also developed a highly effective synthetic iron oxide for removing hydrogen sulfide from biogas. This can be easily metered into the fermentation reactor.

At the end of the third quarter of 2012, LANXESS employed 828 people in research and development, compared to 731 as of December 31, 2011. The increase is mainly attributable to the expansion of our technology centers.

For more information, readers are referred to the section on Research and Development (page 104 ff.) and to the Opportunity Report in the Annual Report 2011, including, in particular, the statements about global megatrends starting on page 115.

Research and Development Expenses

€ million	Q3 2011	Q3 2012	Change %	9M 2011	9M 2012	Change %
Research and development expenses	40	49	22.5	105	147	40.0
in % of sales	1.7%	2.3%		1.6%	2.1%	

Significant opportunities and risks

There have been no significant changes in the opportunities or risks of the LANXESS Group compared with December 31, 2011. For more information, readers are therefore referred to the information on pages 109 to 119 of the Group management report for the 2011 fiscal year. Based on an overall evaluation of risk management information, the Board of Management at the present time cannot identify any sufficiently likely risks or risk combinations that would jeopardize the continued existence of LANXESS.

Outlook

The third quarter of 2012 was already marked by lower demand in some of the customer markets relevant to LANXESS. In addition, the general macroeconomic situation clouded as the third quarter progressed. With customer order patterns hard to predict and raw material prices expected to stay volatile for the medium term, a forecast of the business development for the remainder of the year is therefore difficult.

In addition to the risks related to the euro debt crisis, weaker growth in many parts of Asia and only limited economic momentum in the United States can be expected to impact economic development in Europe, in particular. Therefore, we predict a weak environment in Europe, with the pace of growth continuing to vary from one country to another. We anticipate moderate growth in the Asia and Latin America regions in the months ahead. However, they are also unlikely to experience any significant upturn for the time being. We expect growth to remain weak in the United States. In light of macroeconomic developments, we do not anticipate any additional growth momentum in the remaining months of 2012.

For this reason, LANXESS already introduced measures in the third quarter aimed at countering the effects of declining demand over the rest of the year. These include flexible asset management and our rigorous cost discipline.

We anticipate mixed trends in our customer industries over the coming months. For example, we expect Europe's automotive sector to remain weak, while growth will be sustained in North America and China, although the high growth rates are slowing.

Demand from the tire industry for our synthetic rubbers is expected to stay weaker, albeit with regional variations. We predict that demand for agrochemicals will remain stable. We see no improvement in Europe's construction industry through year end. By contrast, we think that the prospects in the North American construction industry will improve slightly. We believe that developments in the chemical industry as a whole in the fourth quarter will be characterized by slight growth.

We expect the prices for raw materials – especially petrochemical raw materials – and energy in the fourth quarter to be comparable to the quarter under review. Our goal remains to adhere to our price-before-volume strategy.

We continue to anticipate total cash outflows of €650 to €700 million for capital expenditures in 2012 as part of our targeted investment strategy to strengthen our position in the key markets.

The measures already introduced in the area of flexible asset management will help us address the growing economic challenges. Against this backdrop and assuming the economic climate does not worsen further in the fourth quarter, we expect growth in EBITDA pre exceptionals for 2012 at the lower end of the 5 to 10% range from the prior-year level of €1,146 million.

Forecasts Unchanged in the Reporting Period

Information in the Annual Report 2011	Page
Future organization and corporate structure	115 ff.
Future corporate objectives and strategy	115 ff.
Future production and products	116 ff.
Future sales markets and competitive position	115 ff.
Future research and development activities	104 ff., 116
Future dividend policy	119
Future financing	119

Events after the end of the reporting period

No events of special significance occurred after September 30, 2012 that are expected to materially affect the financial position or results of operations of the LANXESS Group.