



We stand for sustainable success

Dear Stockholders:

We look back on an eventful year. The fourth quarter, particularly, was marked by the unexpectedly severe financial and economic crisis. While the economy remains surrounded by considerable uncertainty, we are looking to the future with relative confidence. Our Group strategy is tried and tested, and our commitment to research and development stands undiminished even in difficult times. A further budget increase, to €2.9 billion, will make this year's R&D spending the highest in our history and lay the foundations for future growth.

We believe Bayer is well equipped, we trust in its strengths, and we stand for sustainable success. Our performance last year bolsters that confidence. Operationally, 2008 was Bayer's most successful year ever. We again improved our key data compared to the prior year and achieved our published earnings targets:

- Sales rose to €32.9 billion, up by a currency- and portfolio-adjusted 4.4 percent. EBITDA before special items increased by 2.3 percent to €6.9 billion, with the margin edging up to 21.1 percent from 20.9 percent in 2007.
- At Bayer HealthCare, the EBITDA margin before special items moved ahead to 27 percent.
- Bayer CropScience achieved an underlying EBITDA margin of 25 percent, reaching its 2009 target a year earlier than originally planned.
- Bayer MaterialScience – despite a substantial drop in business toward the end of the year – posted a cash flow return on investment (CFROI) of 10.1 percent, clearly exceeding the internal hurdle.
- With a CFROI of 13 percent for the Bayer Group, the highest in our history, we created appreciable value for you, our stockholders.

These achievements were made possible by an outstanding level of commitment on the part of our employees, whom I would like to thank on behalf of the entire Board of Management. And I can assure you that we are taking the overall economic situation and the related concerns of our workforce very seriously. Of course, Bayer too must take appropriate steps in response to the crisis. Yet now more than ever, positive signals are needed to encourage and motivate our people.

It goes without saying that you, our stockholders, should also benefit from the solid performance of our business. The Board of Management and the Supervisory Board are therefore proposing to raise the dividend by 3.7 percent from the previous year, to €1.40.

Bayer stock was unable to escape the general market trend, which was determined by the changing economic situation. Yet its 32 percent decline on the year was significantly smaller than that of the DAX (minus 40 percent) or the EURO STOXX 50 (minus 42 percent).

We achieved a great deal in 2008. It was a strong year for Bayer HealthCare, with all divisions performing very well and posting above-market rates of growth. The integration of Schering, Berlin, Germany, was successfully completed. And we strengthened key areas of the business with further acquisitions and inlicensed products.

A highlight of 2008 is featured on the cover of this Annual Report: the first marketing approvals for our new anticoagulant Xarelto. We believe this innovative drug could achieve peak annual sales of more than €2 billion.

Bayer CropScience turned in the best performance in the history of our crop protection business, benefiting from the positive conditions on agricultural markets around the world. Given the favorable market environment and the high demand for innovative solutions, we now expect that our €2 billion sales target for new active ingredients from the launch program initiated in 2000 will be reached by the end of this year. That would be two years earlier than originally planned.

As a result we have already set ourselves a new goal. Between 2008 and 2012 we plan to launch new active substances with peak sales potential totaling over €1 billion. This underscores the success of our alignment toward the research and development of new crop protection solutions and emphasizes our innovation leadership in this area.

Bayer MaterialScience experienced a much weaker year, with declines in sales and earnings. Business in the fourth quarter, particularly, was tangibly harmed by the effects of the global financial and economic crisis. But we responded prudently to the difficult market conditions at an early stage, reinforcing the foundations for our long-term success. We significantly strengthened our presence in the expanding Chinese market with the inauguration of the world's largest MDI production facility in Shanghai. At the same time this entire production complex sets standards for energy-efficient and environmentally compatible production. Bayer MaterialScience will have invested a total of €2.1 billion in Shanghai by the end of 2012.

The strategic alignment of the Bayer Group allows us to look forward to 2009 with relative confidence despite the current financial and economic crisis. The fact that the less cyclical life-science businesses – HealthCare and CropScience – account for more than 70 percent of our sales is paying off. For these two subgroups we expect a gratifying trend in 2009, and aim to improve the EBITDA margin before special items toward 28 percent at HealthCare and maintain the margin for CropScience at the high level of about 25 percent. The business situation at MaterialScience runs counter to this. We anticipate an extremely difficult year for this subgroup, with a severe drop in sales and earnings. In this negative scenario for MaterialScience, we are nevertheless confident of limiting the decline in Group EBITDA before special items to about 5 percent. Should there be a tangible recovery in our MaterialScience business in the short term, Group EBITDA before special items could match the very high level of 2008 or even post a slight increase.

We are convinced that Bayer can emerge from the financial and economic crisis even stronger than before. Sustainable success requires responsible interaction with all stakeholders, sound business models and investment in the future. And sustainable success is Bayer's utmost priority. We are aiming for sustainability in everything we do.

In these turbulent times we could, of course, help to improve earnings in the short term by cutting back on research, for example. But that would not be a sustainable strategy. It would simply be short-sighted. Our investment in research and development is intended to drive our growth and produce groundbreaking innovations. That is how we safeguard growth – and with it jobs and prosperity. Success tomorrow demands investment today. The time to compete for tomorrow's best products and technologies is now.

But we must not lose sight of the long-term challenges either. By these I mean the major issues such as demographic change, global food supplies, energy conservation and

climate protection. Bayer's climate program is already making very encouraging headway. We have good answers that address long-term challenges and at the same time take advantage of related business opportunities for our enterprise.

There are also other fields in which politicians, industry leaders and society as a whole need to think – and act – in terms of sustainability. Safeguarding the future also involves investing more heavily in education, for example. That is a crucial task to which we should all pay special attention. And for that reason Bayer has for many years trained more young people than it will need to employ at its own facilities. We also support numerous school projects aimed at improving science teaching through the Bayer Science & Education Foundation.

We have seen success in recent years. I and my colleagues on the Board of Management would like to thank you, our stockholders, for your renewed trust in 2008. We will do all we can to ensure that we continue along our successful path.

Sincerely,



WERNER WENNING
Chairman of the Board of Management of Bayer AG