

REPORT ON ECONOMIC POSITION

Economic Environment

Global economy

The coronavirus pandemic had a substantial negative impact on the economy worldwide in the year 2020. The global economy weakened significantly, contracting by 4.1% year over year, and posted negative growth rates in all regions. Whereas the gross domestic product in the Asia-Pacific region was down only slightly thanks to still-positive growth in China, the other regions took a much harder hit.

Economic environment

	Growth ¹ 2019	Growth ¹ 2020
	%	%
World	+2.5	-4.1
Europe	+1.6	-6.7
of which Western Europe	+1.3	-7.2
of which Germany	+0.6	-5.3
of which Eastern Europe	+2.7	-4.8
Middle East	+1.1	-5.3
Latin America	-0.4	-7.5
Africa	+2.6	-3.6
North America²	+2.0	-4.0
of which United States	+2.2	-3.6
Asia-Pacific	+4.1	-1.6
of which China	+6.1	+2.1

¹ Real growth of gross domestic product; source: IHS (Global Insight), as of January 2021.

² North America (not including Central America): Canada, Mexico, United States.

Main customer industries*

In fiscal 2020, automotive production worldwide was down 16%. All regions experienced significant declines. Still the largest sales market for the automotive industry, China generated a less negative growth rate of around 4%.

At approximately 2%, negative growth in the global construction industry in fiscal 2020 was somewhat less severe than in the prior year. The construction industry in North America was stable, but Eastern Europe and the Asia-Pacific region exhibited mildly negative trends, and growth in Western Europe and Latin America was sharply negative.

The approximately 1% growth rate in the global electrical, electronics, and household appliances industry in fiscal year 2020 was well below the previous year's level. A key driver of the upturn was the Asia-Pacific region. In contrast, Europe and Latin America saw a substantial decline in growth rates. The North America region reported a slight drop compared with the prior year.

The global furniture industry experienced a 10% downturn with strongly negative growth rates in all regions in fiscal 2020. The impact in the Asia-Pacific region was milder, with a decline of around 6% resulting from a comparatively small downturn in China (roughly 4%).

* Covestro's estimate, based on the following sources: LMC Automotive Limited, B+L, CSIL (Centre for Industrial Studies), Oxford Economics.

Business Performance at a Glance

Significant Events

Coronavirus pandemic

Business performance in the year 2020 as a whole was heavily influenced by the coronavirus pandemic. Demand in our main customer industries reached its low in the second quarter of fiscal 2020, followed by a strong recovery in demand in the second half of the year. Covestro took a wide range of steps early on to protect the health of all its employees, secure its delivery capabilities, and safeguard its strong liquidity position. For instance, we implemented far-reaching health, safety, and hygiene measures at our sites. Depending on the local situation in each case, some of our staff, particularly employees in administrative departments, are working from home. Production has continued at our sites, for the most part unimpeded by the pandemic.

In anticipation of economic challenges, the Board of Management initiated measures for cost control in the course of the planning for fiscal 2020. In response to the coronavirus pandemic, the Board of Management once again raised the target for these cost savings. In total, we achieved short-term cost savings of €360 million during the reporting year compared with the original planning before resolving the additional measures. This step was taken in addition to the Perspective efficiency improvement program, which was launched in the year 2018 and successfully completed in fiscal 2020, cutting costs by €130 million in total. In addition, the figure for capital expenditure was lowered from the original projection. Investments totaled €704 million in fiscal year 2020 (projected: €900 million).

The Board of Management, the Supervisory Board, and Covestro employees are working together in solidarity to reach these goals and put the company in an even more robust position in the current environment. At all our German companies, the Board of Management and employee representatives agreed to implement a model to reduce working hours for six months while adjusting pay for all employees. The percentage reduction in compensation increased up the pay scale. Covestro's Board of Management and Supervisory Board are participating by accepting a 15% pay cut. All Covestro Group companies outside Germany implemented comparable country-specific measures to reduce costs. However, because the economic situation during the second half of fiscal 2020 proved to be more positive than expected, participants in the solidarity initiative worldwide received a one-time gross compensation payment at year-end.

Covestro is continually monitoring the development of the coronavirus pandemic worldwide to ensure that the company can react quickly when necessary. Existing measures are modified or expanded as required in line with recommendations and instructions issued by the relevant governments and committees of experts.

Other events

On January 2, 2020, Covestro successfully concluded the sale of its European polycarbonate sheets business to the Serafin Group. This included central management and distribution functions in Europe and production sites in Belgium and Italy. Serafin has pledged to continue operations at all sites. Covestro will continue to act as a key supplier of raw materials for the foreseeable future.

Covestro has taken various steps to safeguard its liquidity. Effective March 17, 2020, Covestro obtained a syndicated revolving credit facility totaling €2.5 billion with a term of five years. On June 5, 2020, Covestro also successfully placed €1.0 billion in euro bonds on foreign debt markets.

 See "Financial position" for additional details and other key funding measures.

Moreover, a dividend for fiscal 2019 of €1.20 per share carrying dividend rights was resolved at Covestro's first virtual Annual General Meeting (AGM) on July 30, 2020. The Board of Management had previously proposed a dividend of €2.40 per share carrying dividend rights to the AGM originally scheduled for April 17, 2020, in Bonn (Germany).

In July 2020, Covestro AG's Supervisory Board voted in favor of an early extension of the contract with Board of Management member Dr. Thomas Toepfer. The contract now runs for five years from April 1, 2021, to March 31, 2026. Dr. Toepfer has held the position of Chief Financial Officer (CFO) and Labor Director since April 1, 2018.

On September 30, 2020, Covestro signed an agreement to acquire the Resins & Functional Materials (RFM) business from Koninklijke DSM N.V., Heerlen (Netherlands), for a preliminary purchase price of €1.6 billion. The goal is to build up Covestro's sustainable and innovative business activities to support the long-term corporate strategy. RFM's integration into the Coatings, Adhesives, Specialties segment significantly expands the portfolio of high-growth sustainable coating resins. As part of the announced acquisition, Covestro successfully carried out a capital increase of 10,200,000 no-par value bearer shares on October 13, 2020, using a portion of the Authorized Capital 2020 for this purpose. The gross issuing proceeds (before commission and costs) amounted to €447 million and will be used to finance the purchase price.

 See "Financial position" and note 7.2 "Acquisitions and divestitures" in the Notes to the Consolidated Financial Statements.

Overall Assessment of Business Performance and Target Attainment

Business performance

Fiscal year 2020 was a challenging one for the Covestro Group, in part owing to the coronavirus pandemic. Compared with the prior year, core volume growth trailed well behind the results of fiscal 2019. This development is primarily due to a pandemic-related drop in demand in the first half of fiscal 2020, whereas in the second half, core volumes sold again exceeded the prior-year figure. At €1,472 million, EBITDA was down (previous year: €1,604 million), although cost-cutting measures played a major role in countering an even greater decrease. As a result of the pandemic, cash outflows for additions to property, plant, equipment, and intangible assets declined to €704 million (previous year: €910 million). Despite the lower EBITDA, free operating cash flow rose to €530 million (previous year: €473 million).

Target attainment

In the 2019 Annual Report, the Covestro Group published a forecast for key performance indicators in fiscal 2020. The Board of Management lowered the forecasts for all key management indicators for fiscal 2020 as a whole on April 15, 2020, as a result of business performance in the first quarter of fiscal 2020, which was heavily influenced by the coronavirus pandemic. After the business situation showed signs of a robust recovery in the second half of the year 2020, the Board of Management again adjusted the fiscal 2020 forecast on October 9, 2020. The recovery continued apace, and the forecast for the year as a whole was again modified on December 8, 2020. The Covestro Group most recently anticipated a decline in volumes between –5% and –6% after originally projecting volume growth in the low-single-digit percentage range. Also adjusted was the expected FOCF and ROCE performance. After initially projecting FOCF of between €0 million and €400 million, the Covestro Group changed this range in December 2020 to between €400 million and €550 million for the full year. The original ROCE forecast of 2% to 7% was lifted to the mid-single-digit percentage range in October 2020.

Despite the massive downturn in business in the first half of 2020, we were able to meet or exceed the profitability and liquidity forecasts from fiscal 2019. At –5.6%, our core volume growth fell below our original forecast target. Free operating cash flow for fiscal 2020 amounted to €530 million, exceeding the originally announced range, while ROCE at 7.0% came in at the upper end of the bandwidth originally communicated. In view of the most recently adjusted forecast from December 2020, the performance of all key performance indicators was as anticipated.

Target attainment for fiscal year 2020

	2019	Forecast 2020 ¹	Adjusted forecast 2020 ²	Target attainment 2020
Core volume growth	+2.0%	Low single-digit-percentage range increase	Decrease of between –5% and –6%	–5.6%
Free operating cash flow	€473 million	Between €0 million and €400 million	Between €400 million and €550 million	€530 million
ROCE	+8.4%	Between 2% and 7%	Mid-single-digit-percentage range increase	+7.0%

¹ Published on February 19, 2020 (Annual Report 2019).

² Published on December 8, 2020 (ad hoc notification).

Results of Operations, Financial Position, and Net Assets of the Covestro Group

Key data Covestro Group

	4th quarter 2019	4th quarter 2020	Change	2019	2020	Change
	€ million	€ million	%	€ million	€ million	%
Core volume growth¹	+3.8%	+1.7%		+2.0%	-5.6%	
Sales	2,864	3,007	+5.0	12,412	10,706	-13.7
Change in sales						
Volume	-0.7%	+4.7%		+0.8%	-5.1%	
Price	-13.3%	+5.4%		-17.3%	-5.7%	
Currency	+1.5%	-4.0%		+1.9%	-1.6%	
Portfolio	0.0%	-1.1%		-0.5%	-1.3%	
Sales by region						
EMLA	1,179	1,288	+9.2	5,289	4,600	-13.0
NAFTA	719	654	-9.0	3,141	2,554	-18.7
APAC	966	1,065	+10.2	3,982	3,552	-10.8
EBITDA	278	637	>100	1,604	1,472	-8.2
Depreciation and amortization	185	205	+10.8	752	776	+3.2
EBIT	93	432	>300	852	696	-18.3
Financial result	(26)	(13)	-50.0	(91)	(91)	0.0
Net income	37	312	>700	552	459	-16.8
Operating cash flows	637	635	-0.3	1,383	1,234	-10.8
Cash outflows for additions to property, plant, equipment and intangible assets	307	241	-21.5	910	704	-22.6
Free operating cash flow	330	394	+19.4	473	530	+12.1
Net financial debt ²				989	356	-64.0
ROCE				+8.4%	+7.0%	

¹ Reference values calculated on the basis of the definition of the core business effective March 31, 2020.

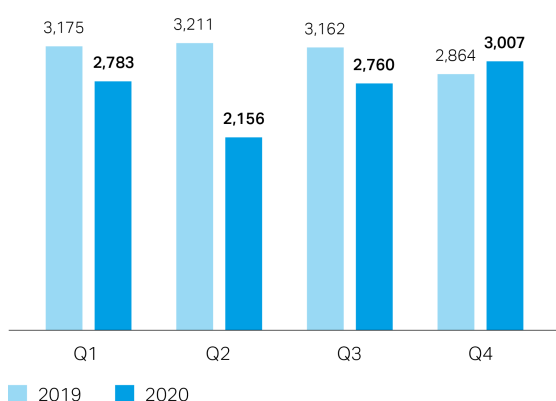
² As of December 31, 2020, compared with December 31, 2019.

Results of Operations

The coronavirus pandemic had a significant impact on Covestro's results of operations in fiscal year 2020. In the second half of fiscal year 2020, we charted a recovery in demand for our products that differed in degree depending on the region and industry.

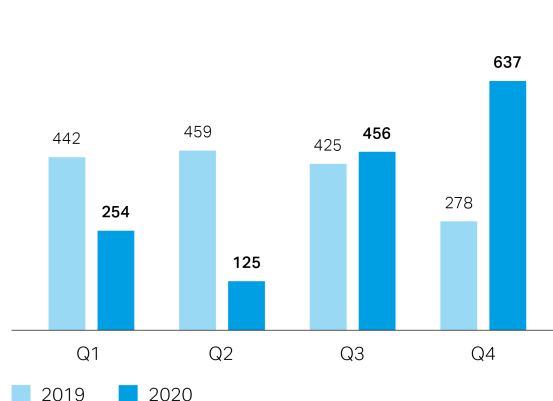
Covestro Group Quarterly sales

€ million



Covestro Group Quarterly EBITDA

€ million



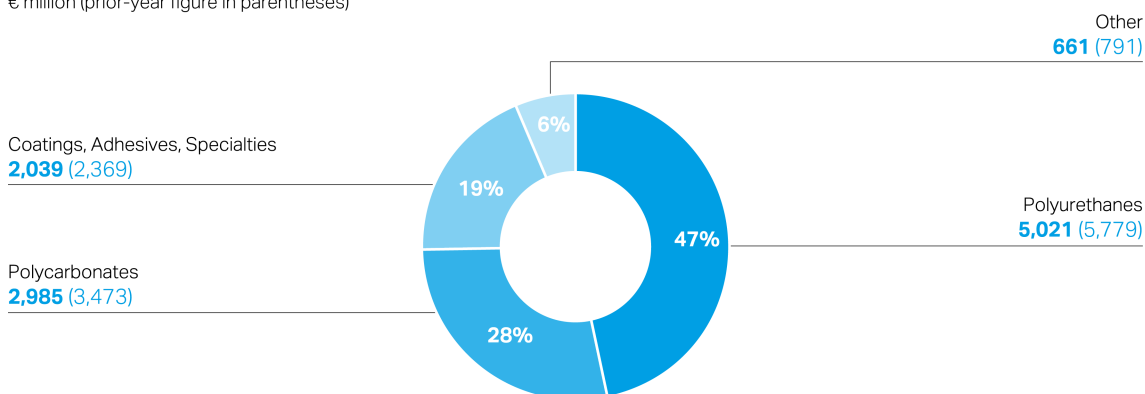
Sales

In the year 2020 as a whole, the Group's core volumes sold decreased by 5.6% from the prior year, primarily on account of weaker demand in the first half of 2020 driven by the coronavirus pandemic. The Polyurethanes and Polycarbonates segments reported declines of 6.1% and 3.0%, respectively. Core volumes sold fell by 8.9% in the Coatings, Adhesives, Specialties segment.

In fiscal 2020, Group sales were down by 13.7% year over year to €10,706 million (previous year: €12,412 million). This is largely due to lower selling prices, which reduced sales by 5.7%. This development was mainly driven by the increased competitive pressure in the Polyurethanes and Polycarbonates segments. In addition, the drop in total volumes sold had a negative effect on sales of 5.1%. Exchange rate movements also had a negative impact of 1.6%. Changes in the portfolio had an overall negative effect on sales of 1.3%. The sale of the European polyurethane systems house business in the fourth quarter of the year 2019 adversely affected sales in fiscal 2020, as did the sale of the European polycarbonate sheets business in the first quarter of fiscal year 2020. In contrast, the step acquisition of shares and subsequent full consolidation of DIC Covestro Polymer Ltd., Tokyo (Japan), in the second quarter of fiscal 2019 had no notable effect on sales in the year 2020 as a whole.

Sales by segment

€ million (prior-year figure in parentheses)



Sales in all reportable segments were down in fiscal 2020. In the Polyurethanes segment, sales fell by 13.1% to €5,021 million (previous year: €5,779 million), and the Polycarbonates segment's sales slid 14.1% to €2,985 million (previous year: €3,473 million). The Coatings, Adhesives, Specialties segment's sales declined by 13.9% to €2,039 million (previous year: €2,369 million).

EBIT

Covestro Group summary income statement

	2019	2020	Change
	€ million	€ million	%
Sales	12,412	10,706	-13.7
Cost of goods sold	(9,658)	(8,207)	-15.0
Gross profit	2,754	2,499	-9.3
Selling expenses	(1,380)	(1,195)	-13.4
Research and development expenses	(266)	(262)	-1.5
General administration expenses	(372)	(310)	-16.7
Other operating expenses (-) and income (+)	116	(36)	.
EBIT	852	696	-18.3
Financial result	(91)	(91)	-
Income before income taxes	761	605	-20.5
Income taxes	(204)	(151)	-26.0
Income after income taxes	557	454	-18.5
of which attributable to noncontrolling interest	5	(5)	.
of which attributable to Covestro AG shareholders (net income)	552	459	-16.8

The cost of goods sold was down by 15.0%, amounting to €8,207 million (previous year: €9,658 million), on account of lower raw material prices. The ratio of the cost of goods sold to sales therefore decreased to 76.7% (previous year: 77.8%).

Gross profit sank by 9.3% to €2,499 million (previous year: €2,754 million), primarily due to a decline in total volumes sold. In contrast, lower raw material costs more than compensated for the low level of selling prices, which boosted earnings.

Selling expenses were 13.4% lower, coming in at €1,195 million (previous year: €1,380 million) and yielding an almost unchanged ratio of selling expenses to sales of 11.2% (previous year: 11.1%). Research and development expenses (R&D) fell by 1.5% to €262 million (previous year: €266 million). As a share of sales, this produced an R&D ratio of 2.4% (previous year: 2.1%). General administration expenses were down by 16.7% to €310 million (previous year: €372 million), for an almost unchanged ratio of administration expenses to sales of 2.9% (previous year: 3.0%). Cost-cutting measures in the sales, R&D, and general administration functions led to a significantly lower cost level than in the previous year.

Net other operating expenses totaled €36 million (previous year: net other operating income of €116 million). In the reporting period, positive one-time effects from the previous year, including insurance reimbursements of €63 million and proceeds from divestitures amounting to €53 million, stood in contrast to expenses relating to the planned acquisition of the Resins & Functional Materials (RFM) business from Koninklijke DSM N.V., Heerlen (Netherlands) totaling €32 million and lower insurance reimbursements of €21 million.

EBIT amounted to €696 million, down 18.3% in the reporting period (previous year: €852 million). The EBIT margin fell to 6.5% (previous year: 6.9%).

EBITDA

Calculation of EBITDA

	2019	2020
	€ million	€ million
EBIT	852	696
Depreciation, amortization, impairment losses and impairment loss reversals	752	776
EBITDA	1,604	1,472

In the year 2020 as a whole, depreciation, amortization and impairment losses rose by 3.2% to €776 million (previous year: €752 million). This item comprised €754 million (previous year: €732 million) in depreciation and impairment losses on property, plant and equipment and €22 million (previous year: €20 million) in amortization and impairment losses on intangible assets. This included €20 million (previous year: €28 million) in impairment losses and €0 million (previous year: €1 million) in reversals of impairment losses.

The Group's EBITDA in the year as a whole decreased by 8.2% from the prior-year period to €1,472 million (previous year: €1,604 million). EBITDA in the Polyurethanes segment slid by 3.5% to €625 million (previous year: €648 million). In contrast, the Polycarbonates segment's EBITDA rose by 3.2% to €553 million (previous year: €536 million). At €341 million, EBITDA in the Coatings, Adhesives, Specialties segment dropped by 27.3% from the prior-year figure (previous year: €469 million).

Net income

In the fiscal year, the financial result was unchanged at €–91 million (previous year: €–91 million) and largely consisted of net interest expense of €–47 million (previous year: €–45 million). In view of the financial result, income before income taxes was down by 20.5% to €605 million (previous year: €761 million). The change in income resulted in the income tax expense declining by 26.0% to €151 million (previous year: €204 million). After taxes and noncontrolling interests, net income shrank by 16.8% and amounted to €459 million (previous year: €552 million).

Return on capital employed (ROCE) and Value Contribution

Calculation of the Value Contribution

	2019	2020
	€ million	€ million
EBIT	852	696
Effective tax rate ¹	+26.8%	+25.0%
Taxes ²	(228)	(174)
Net operating profit after taxes (NOPAT)	624	522
Weighted average cost of capital (WACC)	+6.8%	+7.3%
Average capital employed	7,406	7,475
Cost of capital	(504)	546
Value contribution	120	(24)
ROCE	+8.4%	+7.0%

¹ The calculation of the effective tax rate is presented in note 13 "Taxes" in the Notes to the Consolidated Financial Statements.

² The imputed income taxes used in the calculation of NOPAT are determined by multiplying EBIT by the effective tax rate.

The Covestro Group's NOPAT totaled €522 million (previous year: €624 million), and average capital employed amounted to €7,475 million (previous year: €7,406 million). This resulted in a decline in ROCE to 7.0% (previous year: 8.4%), which fell below the WACC of 7.3% (previous year: 6.8%). The company therefore did not generate a premium on the cost of capital. The above figures resulted in a Value Contribution of €–24 million (previous year: €120 million).

 Additional information on the calculation of indicators is available in "Management."

Calculation of average capital employed

	Dec. 31, 2018 ¹	Effects of IFRS 16	Jan. 1, 2019	Dec. 31, 2019	Dec. 31, 2020
	€ million	€ million	€ million	€ million	€ million
Goodwill	256	–	256	264	255
Other intangible assets	77	–	77	114	109
Property, plant and equipment ²	4,409	660	5,069	5,286	5,175
Investments accounted for using the equity method	214	–	214	192	173
Other noncurrent financial assets ³	8	–	8	7	5
Other receivables ⁴	361	–	361	376	309
Deferred taxes ⁵	256	–	256	221	253
Inventories	2,213	–	2,213	1,916	1,663
Trade accounts receivable	1,786	–	1,786	1,561	1,593
Claims for income tax refunds	55	–	55	104	55
Assets held for sale ^{6,7}	–	–	1	12	36
Gross capital employed	9,635	660	10,296	10,053	9,626
Other provisions ⁸	(721)	–	(721)	(422)	(360)
Other liabilities ^{9,10}	(335)	–	(335)	(284)	(269)
Deferred tax liabilities ¹¹	(153)	–	(153)	(204)	(177)
Trade accounts payable ¹⁰	(1,536)	–	(1,536)	(1,431)	(1,241)
Income tax liabilities	(279)	–	(279)	(164)	(162)
Liabilities directly related to assets held for sale ^{12,13}	–	–	–	(8)	(7)
Capital employed	6,611	660	7,272	7,540	7,410
Average capital employed				7,406	7,475

¹ Reference information was not restated for financial reporting standard IFRS 16.

² As of January 1, 2019, this also contains the right-of-use assets from initial application of IFRS 16.

³ Other noncurrent financial assets were adjusted for nonoperating assets.

⁴ Other receivables were adjusted for nonoperating and financial receivables.

⁵ Deferred taxes were adjusted for deferred taxes from defined benefit plans and similar obligations.

⁶ Assets held for sale have been included in the calculation of capital employed since January 1, 2019. The prior-year figures were not restated.

⁷ Assets held for sale were adjusted for nonoperating and financial assets.

⁸ Other provisions were adjusted for provisions for interest payments.

⁹ Other liabilities were adjusted for nonoperating and financial liabilities.

¹⁰ Reference information was restated accordingly. See note 4.1 "Change in presentation of rebates granted to customers" in the Notes to the Consolidated Financial Statements.

¹¹ Deferred tax liabilities were adjusted for deferred tax liabilities from defined benefit plans and similar obligations.

¹² Liabilities directly related to assets held for sale have been included in the calculation of capital employed since January 1, 2019. The prior-year figures were not restated.

¹³ Liabilities directly related to assets held for sale were adjusted for nonoperating and financial liabilities.

Financial Position

Statement of cash flows

Covestro Group summary statement of cash flows

	4th quarter 2019	4th quarter 2020	2019	2020
	€ million	€ million	€ million	€ million
EBITDA	278	637	1,604	1,472
Income taxes paid	(31)	(40)	(296)	(155)
Change in pension provisions	26	(1)	49	25
(Gains)/losses on retirements of noncurrent assets	(35)	6	(51)	8
Change in working capital/other noncash items	399	33	77	(116)
Cash flows from operating activities	637	635	1,383	1,234
Cash outflows for additions to property, plant, equipment and intangible assets	(307)	(241)	(910)	(704)
Free operating cash flow	330	394	473	530
Cash flows from investing activities	(252)	(764)	(838)	(1,769)
Cash flows from financing activities	(57)	377	(668)	1,204
Change in cash and cash equivalents due to business activities	328	248	(123)	669
Cash and cash equivalents at beginning of period	422	1,157	865	748
Change in cash and cash equivalents due to changes in scope of consolidation	–	–	(1)	1
Change in cash and cash equivalents due to exchange rate movements	(2)	(1)	7	(14)
Cash and cash equivalents at end of period	748	1,404	748	1,404

Cash flows from operating activities/free operating cash flow

Cash flows from operating activities dropped to €1,234 million (previous year: €1,383 million). A reduction in EBITDA and increase in funds tied up in working capital stood in contrast to lower income tax payments. Thanks to the reduction in cash outflows for additions to property, plant, equipment, and intangible assets from the original forecast (projected: €900 million), free operating cash flow increased to €530 million (previous year: €473 million) despite the decrease in cash flows from operating activities.

 Additional information on the calculation of indicators is available in "Management."

Cash flows from investing activities

In fiscal 2020, net cash used in investing activities totaled €1,769 million (previous year: €838 million). This item comprised investments in money market funds of €771 million, short-term bank deposits of €355 million, as well as cash outflows for additions to property, plant, equipment, and intangible assets of €704 million (previous year: €910 million).

Capital expenditures in fiscal 2020 were targeted at maintenance and improvement of existing plants as well as new capacity in all three reportable segments. In the Polyurethanes segment, an investment was made in the construction of a chlorine production facility at the Tarragona (Spain) site, which promotes the use of energy-saving technologies, following commissioning of the MDI pilot plant at the Brunsbüttel (Germany) site. What is more, an investment at the Rotterdam (Netherlands) site improved water treatment, while capital expenditure in Shanghai (China) secured and optimized the supply of chlorine. Strategically relevant investments comprised the expansion of capacity at the Shanghai and Krefeld-Uerdingen (Germany) sites in the Polycarbonates segment and of global production capacity for specialty films at the Map Ta Phut (Thailand) and Dormagen (Germany) sites in the Coatings, Adhesives, Specialties segment. In addition, the new Group headquarters building in Leverkusen (Germany) was completed.

Cash outflows for additions to property, plant, equipment, and intangible assets

	2019	2020
	€ million	€ million
Polyurethanes	543	409
Polycarbonates	209	157
Coatings, Adhesives, Specialties	158	138
Others/Consolidation	–	–
Covestro Group	910	704

Cash flows from financing activities

Net cash inflow from the Covestro Group's financing activities amounted to €1,204 million in fiscal 2020 (previous year: net cash outflow of €668 million). For the most part, this relates to the issue of euro bonds totaling €1.0 billion and the net proceeds of the capital increase in October 2020 amounting to €444 million. The dividend payout for Covestro AG was €219 million (previous year: €438 million).

Net financial debt

	Dec. 31, 2019	Dec. 31, 2020
	€ million	€ million
Bonds	997	1,990
Liabilities to banks	10	227
Lease liabilities	735	672
Liabilities from derivatives	10	9
Other financial liabilities	–	1
Receivables from derivatives	(15)	(13)
Financial debt	1,737	2,886
Cash and cash equivalents	(748)	(1,404)
Current financial assets	–	(1,126)
Net financial debt	989	356

In comparison with December 31, 2019, the Covestro Group's financial debt increased by €1,149 million to €2,886 million as of December 31, 2020. The increase was due to the assumption of a loan from the European Investment Bank totaling €225 million in the first quarter of 2020. The loan is for research and development with a focus on sustainability and the circular economy in the European Union. On June 5, 2020, Covestro also successfully placed a total of €1.0 billion in euro bonds on the capital market.

Current financial assets increased to €1,126 million and comprised money market funds in the amount of €771 million and short-term bank deposits totaling €355 million. At the same time, cash and cash equivalents rose to €1,404 million (previous year: €748 million).

On the one hand, the higher level of cash and cash equivalents and current financial assets at year-end reflected Covestro's aim to secure liquidity in view of the economic impact of the coronavirus pandemic. On the other hand, these are earmarked for financing of the purchase price of the announced acquisition of the RFM business from Koninklijke DSM N.V., Heerlen (Netherlands).

In fiscal 2020, net financial debt decreased by €633 million to €356 million (previous year: €989 million).

Financial management

The main purpose of financial management is to ensure solvency at all times, continuously optimize capital costs and reduce the risks of financing measures. Financial management for the Covestro Group is performed centrally by Covestro AG.

Effective March 17, 2020, Covestro AG obtained a new syndicated revolving credit facility totaling €2.5 billion with a term of five years. It includes two options to extend the term by one year in each case. An important new feature of the credit line is its link to an ESG (environment, social, and governance) rating: The better (worse) the externally calculated ESG score is, the lower (higher) the interest component of the credit facility. The new facility replaces the existing revolving credit line of €1.5 billion and, like it, functions as a backup liquidity reserve. No loans had been drawn against this syndicated credit facility as of December 31, 2020. On September 30, 2020, Covestro arranged another syndicated credit facility in the original amount of €1.7 billion. This second credit facility was reduced on October 26, 2020, and stood at €1.2 billion as of December 31, 2020. This serves as bridge financing for the purchase price of the announced acquisition of the RFM business from Koninklijke DSM N.V. No loans had been drawn against the second syndicated credit facility as of December 31, 2020, either. This credit facility used for bridge financing was terminated as of January 29, 2021, thanks to Covestro's strong liquidity position.

Covestro AG operates a Debt Issuance Program with a total volume of €5.0 billion to facilitate obtaining flexible financing from the capital market. The company is thus in the position to issue fixed- and variable-rate bonds as well as to undertake private placements. Covestro AG successfully placed several bonds from its Debt Issuance Program in March 2016. The outstanding bonds with a total volume of €1.0 billion are fixed-rate bonds maturing in October 2021 (1.00% coupon, €500 million) and September 2024 (1.75% coupon, €500 million), and carry a Baa2 rating with negative outlook from Moody's Investors Service, London (United Kingdom). On June 5, 2020, Covestro successfully placed a total of €1.0 billion in euro bonds on the capital market. The proceeds of the new bonds placed will be used to further reinforce Covestro's liquidity in view of the economic effects of the coronavirus pandemic and, among other things, to repay the existing bond maturing in fiscal 2021. The bonds mature in February 2026 and June 2030 and carry coupon rates of 0.875% and 1.375%, respectively.

As a company, Covestro AG currently holds a Baa2 investment-grade rating with negative outlook from the rating agency Moody's Investors Service. Covestro intends to continue to maintain financing structures and financial ratios that support a solid investment-grade rating.

The Covestro Group pursues a prudent debt management strategy to ensure flexibility, drawing on a balanced financing portfolio. This is based for the most part on bonds, syndicated credit facilities, and bilateral loan agreements.

As a company with international operations, Covestro is exposed to financial opportunities and risks. These are continuously monitored within the context of Covestro's financial management activities. Instruments including derivatives are used to minimize risks.

For a detailed presentation of financial opportunities and risks as well as further explanations, please see Covestro's opportunities and risks report.

 See "Opportunities and risks report."

Net Assets

Covestro Group summary statement of financial position

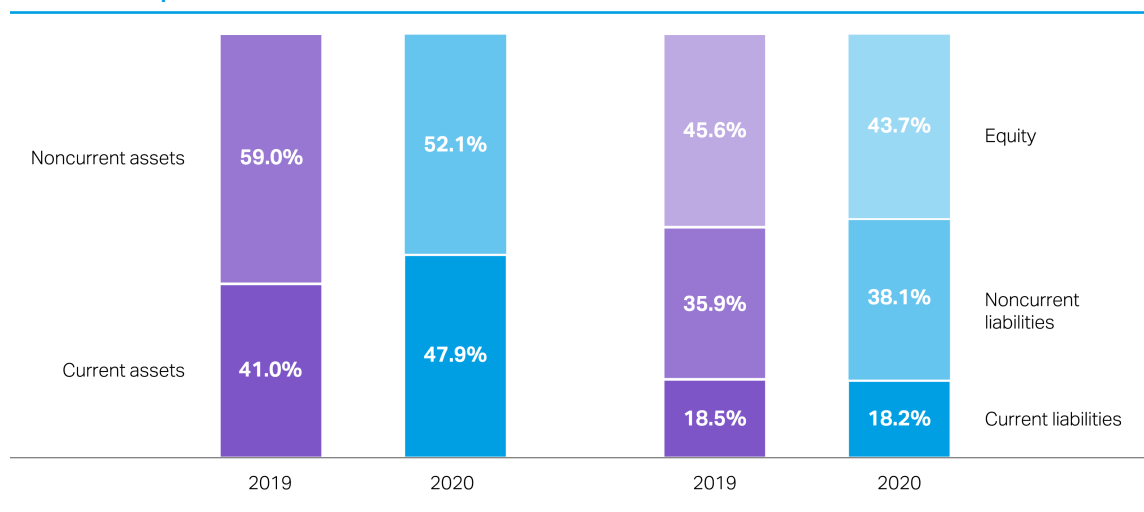
	Dec. 31, 2019	Dec. 30, 2020
	€ million	€ million
Noncurrent assets	6,791	6,734
Current assets	4,727	6,190
Total assets	11,518	12,924
Equity	5,254	5,644
Noncurrent liabilities	4,129	4,916
Current liabilities	2,135	2,364
Liabilities	6,264	7,280
Total equity and liabilities	11,518	12,924

Total assets increased by €1,406 million to €12,924 million as of December 31, 2020 (December 31, 2019: €11,518 million).

Noncurrent assets were down by €57 million to €6,734 million (previous year: €6,791 million) and accounted for 52.1% (previous year: 59.0%) of total assets. This was mainly due to the decline in property, plant, and equipment, as depreciation and impairment losses exceeded cash outflows for this item in the reporting year.

Current assets were up by €1,463 million to €6,190 million (previous year: €4,727 million) and therefore accounted for 47.9% (previous year: 41.0%) of total assets. This increase was chiefly attributable to investments in money market funds and short-term bank deposits and the higher level of cash and cash equivalents.

Covestro Group's balance sheet structure



Equity increased by €390 million to €5,644 million as of December 31, 2020 (previous year: €5,254 million). The equity ratio was 43.7% as of the reporting date (previous year: 45.6%). Equity grew primarily on account of the capital increase and the income after income taxes. This more than offset the degree to which the dividend distribution and remeasurement of pension obligations as well as negative exchange rate changes reduced equity.

Noncurrent liabilities increased by €787 million to €4,916 million as of the reporting date (previous year: €4,129 million) and accounted for 67.5% (previous year: 65.9%) of liabilities. This was mainly due to an increase in noncurrent financial liabilities as well as in provisions for pensions and other post-employment benefits. Noncurrent financial liabilities were higher principally as a result of the issue of euro bonds totaling €1.0 billion and the assumption of a loan for research and development from the European Investment Bank amounting to €225 million.

Net defined benefit liability for post-employment benefits

	Dec. 31, 2019	Dec. 31, 2020
	€ million	€ million
Net defined benefit liability for post-employment benefits	1,963	2,121

The net defined benefit liability for post-employment benefits (pension obligations less plan assets) rose by €158 million in the reporting year to €2,121 million (previous year: €1,963 million). An increase in the value of the plan assets was unable to offset actuarial losses primarily resulting from the lowering of the discount rate in Germany and the United States.

Current liabilities were up by €229 million to €2,364 million (previous year: €2,135 million) and accounted for 32.5% (previous year: 34.1%) of liabilities. This increase is mostly attributable to the reclassification of the bond maturing in October 2021 to current liabilities at the end of the fiscal year and a decrease in trade accounts payable.

Performance of the Reportable Segments

Polyurethanes

Polyurethanes key data

	4th quarter 2019	4th quarter 2020	Change	2019	2020	Change
	€ million	€ million	%	€ million	€ million	%
Core volume growth¹	+3.6%	+0.8%		+2.3%	-6.1%	
Sales	1,336	1,519	+13.7	5,779	5,021	-13.1
Change in sales						
Volume	-0.2%	+2.9%		+1.5%	-5.0%	
Price	-16.9%	+16.2%		-24.7%	-5.1%	
Currency	+1.5%	-4.8%		+1.8%	-2.0%	
Portfolio	-0.7%	-0.6%		-0.1%	-1.0%	
Sales by region						
EMLA	546	683	+25.1	2,487	2,189	-12.0
NAFTA	394	365	-7.4	1,680	1,389	-17.3
APAC	396	471	+18.9	1,612	1,443	-10.5
EBITDA	123	379	>200	648	625	-3.5
EBIT	24	264	>900	250	197	-21.2
Operating cash flows	282	285	+1.1	575	423	-26.4
Cash outflows for additions to property, plant, equipment and intangible assets	168	138	-17.9	543	409	-24.7
Free operating cash flow	114	147	+28.9	32	14	-56.3

¹ Reference values calculated on the basis of the definition of the core business effective March 31, 2020.

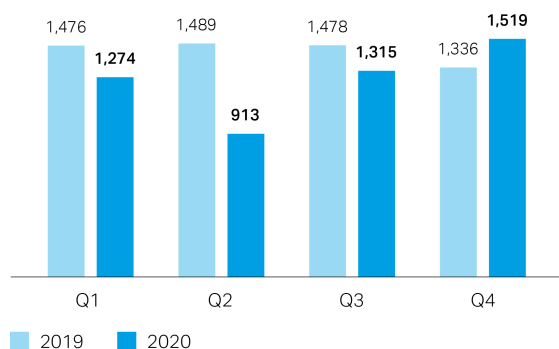
In fiscal 2020, core volumes sold in Polyurethanes dropped by 6.1% from the prior-year period. This is mainly due to lower core volumes sold in the furniture and wood processing industry, the automotive and transportation industry, and the construction industry, particularly in the EMLA region. Core volumes sold were down in the first six months of the year 2020 as a result of a steep pandemic-related downturn in demand. In the second half of fiscal 2020, demand improved considerably and the competitive situation was favorable, which resulted in core volumes sold increasing over the prior-year figures.

The Polyurethanes segment's sales were down by 13.1% to €5,021 million (previous year: €5,779 million). The lower average selling price level for the year reduced sales by 5.1%. Both prior-year effects and price volatility in the 2020 reporting year influenced the individual quarters to various degrees. In addition, the decline in total volumes sold and exchange rate movements reduced sales by 5.0% and 2.0%, respectively. The portfolio effect from the sale of the European systems house business in the fourth quarter of 2019 had a negative effect of 1.0% on sales in fiscal year 2020.

Sales in the EMLA region fell by 12.0% to €2,189 million (previous year: €2,487 million) on account of significantly lower average selling prices. Moreover, total volumes sold and exchange rate changes along with the aforementioned portfolio effect reduced sales somewhat. In the NAFTA region, sales decreased by 17.3% to €1,389 million (previous year: €1,680 million). Total volumes sold and average selling prices had a significantly adverse effect on sales. Exchange rate developments pushed sales down slightly. Sales in the APAC region dropped by 10.5% to €1,443 million (previous year: €1,612 million), with total volumes sold exerting a considerable negative effect on sales. At the same time, changes in exchange rates and a decline in the selling price level each caused sales to decline slightly.

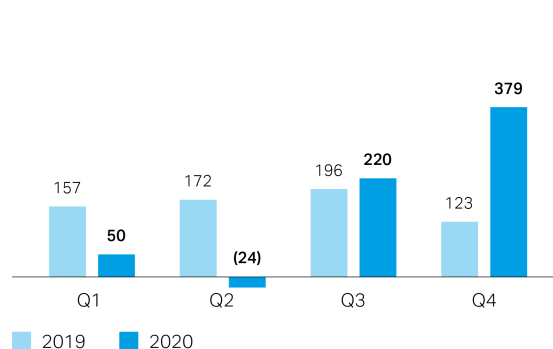
Polyurethanes Quarterly sales

€ million



Polyurethanes Quarterly EBITDA

€ million



EBITDA fell by 3.5% from the prior-year period to €625 million (previous year: €648 million). The decline in total volumes sold and positive one-time effects from the previous year, including insurance reimbursements of €63 million and proceeds from divestitures amounting to €34 million, reduced earnings. In contrast, lower raw material prices more than compensated for reduced selling prices, which led to higher margins. These, along with costs lowered by cost-cutting measures, had a positive effect on EBITDA.

EBIT was down by 21.2% to €197 million (previous year: €250 million).

Free operating cash flow declined to €14 million from the previous year, a reduction of 56.3% (previous year: €32 million). Funds were freed up from working capital in the previous year but tied up in working capital in the reporting year, which had a negative effect on free operating cash flow. This was mostly balanced out by reduced cash outflows for additions to property, plant, and equipment.

Polycarbonates

Polycarbonates key data

	4th quarter 2019	4th quarter 2020	Change	2019	2020	Change
	€ million	€ million	%	€ million	€ million	%
Core volume growth¹	+3.5%	+3.2%		+2.7%	-3.0%	
Sales	814	803	-1.4	3,473	2,985	-14.1
Change in sales						
Volume	0.0%	+7.4%		+2.4%	-2.3%	
Price	-13.5%	-2.1%		-16.5%	-7.0%	
Currency	+1.6%	-3.7%		+2.0%	-1.5%	
Portfolio	0.0%	-3.0%		-2.2%	-3.3%	
Sales by region						
EMLA	270	244	-9.6	1,146	942	-17.8
NAFTA	160	154	-3.8	734	610	-16.9
APAC	384	405	+5.5	1,593	1,433	-10.0
EBITDA	95	200	>100	536	553	+3.2
EBIT	39	143	>200	300	332	+10.7
Operating cash flows	204	178	-12.7	613	484	-21.0
Cash outflows for additions to property, plant, equipment and intangible assets	84	61	-27.4	209	157	-24.9
Free operating cash flow	120	117	-2.5	404	327	-19.1

¹ Reference values calculated on the basis of the definition of the core business effective March 31, 2020.

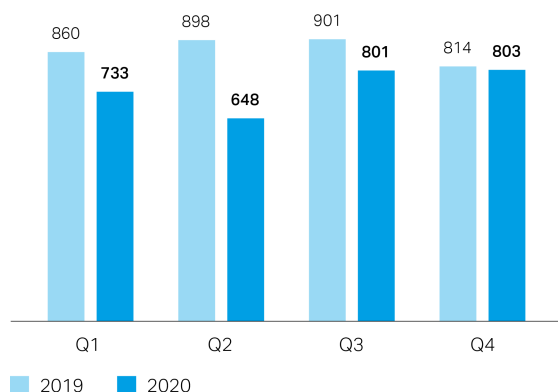
In fiscal year 2020, core volumes sold in Polycarbonates were down by 3.0% from the prior-year period. Key drivers were lower volumes sold in the automotive and transportation industry, mainly in the EMLA and NAFTA regions, and in the electrical, electronics and household appliances industry, especially in the APAC region. In contrast, demand from the construction industry increased. The coronavirus pandemic led to a sharp slide in demand, particularly in the first six months of fiscal 2020, which in turn resulted in a drop in core volumes sold. In the second half of the year, a robust recovery in demand pushed core volumes sold over the prior-year level.

Sales in the Polycarbonates segment fell by 14.1% in the year 2020 to €2,985 million (previous year: €3,473 million), mostly due to lower selling prices, which reduced sales by 7.0%. A decrease in total volumes sold and exchange rate movements had negative effects on sales of 2.3% and 1.5%, respectively. The portfolio effect from the sale of the European polycarbonate sheets business in the first quarter of fiscal 2020 adversely affected sales, which declined by 3.3%.

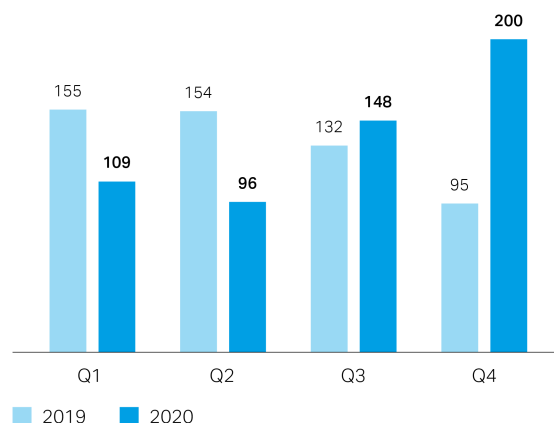
In the EMLA region, sales tumbled 17.8% to €942 million (previous year: €1,146 million). The aforementioned portfolio effect and a reduction in average selling prices each significantly lowered sales. Exchange rate developments also pushed sales down somewhat. Total volumes sold remained at the prior-year level, however. Sales in the NAFTA region declined by 16.9% to €610 million (previous year: €734 million). Lower total volumes sold and a lower selling price level both had a strong adverse effect on sales. Moreover, exchange rate changes reduced sales somewhat. The APAC region saw sales slide by 10.0% to €1,433 million (previous year: €1,593 million), largely driven by a sharp drop in average selling prices. At the same time, exchange rate movements had a mildly negative effect on sales. However, total volumes sold remained stable year over year.

**Polycarbonates
Quarterly sales**

€ million

**Polycarbonates
Quarterly EBITDA**

€ million



In fiscal 2020, EBITDA in the Polycarbonates segment grew by 3.2% over the prior-year period, rising to €553 million (previous year: €536 million). Lower raw material prices along with an improved cost level thanks to cost-cutting measures had a positive effect on earnings. However, reduced selling prices and a decline in total volumes sold adversely affected EBITDA. Moreover, the portfolio effect from the sale of the European polycarbonate sheets business in the first quarter of 2020 reduced sales.

EBIT increased by 10.7% to €332 million (previous year: €300 million).

Free operating cash flow was down by 19.1% to €327 million (previous year: €404 million). A decrease in funds released from working capital had a negative effect, whereas reduced cash outflows for additions to property, plant, and equipment had a positive effect.

Coatings, Adhesives, Specialties

Coatings, Adhesives, Specialties key data

	4th quarter 2019	4th quarter 2020	Change	2019	2020	Change
	€ million	€ million	%	€ million	€ million	%
Core volume growth¹	+6.2%	+2.8%		-1.0%	-8.9%	
Sales	533	529	-0.8	2,369	2,039	-13.9
Change in sales						
Volume	+0.1%	+7.5%		-2.1%	-9.0%	
Price	-4.2%	-4.9%		-1.1%	-4.2%	
Currency	+1.9%	-3.4%		+2.3%	-1.0%	
Portfolio	+2.0%	0.0%		+1.2%	+0.3%	
Sales by region						
EMLA	224	227	+1.3	1,052	908	-13.7
NAFTA	129	116	-10.1	562	469	-16.5
APAC	180	186	+3.3	755	662	-12.3
EBITDA	62	52	-16.1	469	341	-27.3
EBIT	32	19	-40.6	352	215	-38.9
Operating cash flows	170	113	-33.5	349	327	-6.3
Cash outflows for additions to property, plant, equipment and intangible assets	55	43	-21.8	158	138	-12.7
Free operating cash flow	115	70	-39.1	191	189	-1.0

¹ Reference values calculated on the basis of the definition of the core business effective March 31, 2020.

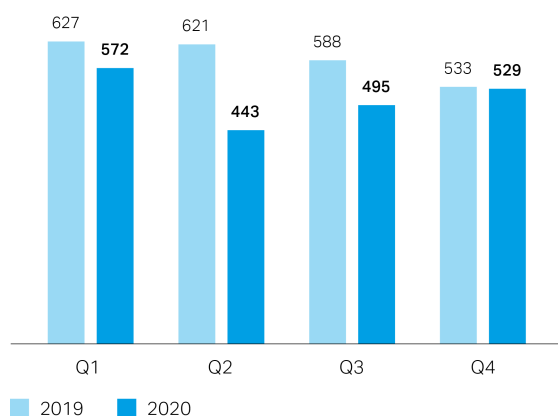
In the 2020 fiscal year, core volumes sold in Coatings, Adhesives, Specialties were down by 8.9% from the prior year. The main factors behind this trend were pandemic-related developments in core volumes sold, especially in the automotive and transportation industry, and in the construction industry, particularly in the EMLA and NAFTA regions. Core volumes sold were down in the first six months of fiscal 2020, chiefly because demand crashed as a result of the coronavirus pandemic. By the end of the year, demand had recovered and, as a result, core volumes sold in the fourth quarter of the 2020 fiscal year exceeded the prior-year figures.

Sales in the Coatings, Adhesives, Specialties segment slid by 13.9% to €2,039 million (previous year: €2,369 million). This was largely due to a downturn in total volumes sold, which in turn reduced sales by 9.0%. Lower average selling prices and exchange rate developments had negative effects on sales of 4.2% and 1.0%, respectively. The change in the portfolio increased sales by 0.3%.

In the EMLA region, sales fell by 13.7% to €908 million (previous year: €1,052 million). This was chiefly due to a decrease in total volumes sold, which had a significant negative effect on sales, and to a lower selling price level, which pushed sales down somewhat. Sales were not noticeably affected by exchange rate movements. In the NAFTA region, sales were down by 16.5% to €469 million (previous year: €562 million), primarily due to a substantial decline in total volumes sold. Lower average selling prices and exchange rate developments both exerted a mildly negative effect on sales. Sales in the APAC region declined by 12.3% to €662 million (previous year: €755 million). Lower selling prices had a strong negative effect on sales. The decline in total volumes sold and exchange rate changes in turn reduced sales slightly. The portfolio effect had no notable impact with regard to sales.

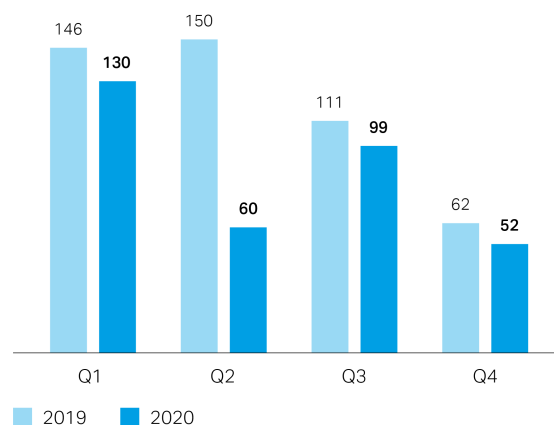
Coatings, Adhesives, Specialties Quarterly sales

€ million



Coatings, Adhesives, Specialties Quarterly EBITDA

€ million



EBITDA fell by 27.3% compared with the prior-year period, coming in at €341 million (previous year: €469 million). Lower total volumes sold and margins reduced earnings. Moreover, expenses for the announced acquisition of the Resins & Functional Materials (RFM) business from Koninklijke DSM N.V., Heerlen (Netherlands), resulted in a €33 million decrease in earnings, of which €1 million were general administration expenses. This contrasts with a low cost level thanks to cost-cutting measures, which had a positive effect on EBITDA. EBITDA in the prior-year period was affected by a one-time gain of €19 million from the remeasurement of the shares of DIC Covestro Polymer Ltd., Tokyo (Japan), previously reported according to the equity method.

EBIT was down by 38.9% to €215 million (previous year: €352 million).

Free operating cash flow decreased by 1.0% to €189 million (previous year: €191 million). The low EBITDA had a negative effect. Funds were tied up in working capital in the previous year, but freed up in the reporting year, which had a positive effect, as did lower outflows for additions to property, plant, equipment, and intangible assets.

Results of Operations, Financial Position, and Net Assets of Covestro AG

Covestro AG is the parent company and strategic management holding company of the Covestro Group. The principal management functions for the entire Group are performed by the Board of Management. These include strategic planning for the Group, resource allocation and executive and financial management. Covestro AG's net assets, financial position and results of operations are largely determined by the business performance of its subsidiaries.

The financial statements of Covestro AG are prepared in accordance with the German Commercial Code (HGB) and the German Stock Corporation Act (AktG). The company, headquartered in Leverkusen (Germany), is registered in the commercial register of the Local Court of Cologne under No. HRB 85281.

Covestro AG performs energy-specific services for Covestro Brunsbüttel Energie GmbH, Brunsbüttel, (affiliated power and gas grid operator) and therefore prepares activity reports in the areas of electricity supply and gas supply pursuant to Section 6b (3) Sentence 1 Nos. 2 and 4 of the German Energy Industry Act (EnWG).

There is a control and profit and loss transfer agreement between Covestro AG and Covestro Deutschland AG, Leverkusen (Germany). All profit not subject to a prohibition on transfer is transferred in full to Covestro AG at the end of the year. Losses are absorbed in full. Other retained earnings recognized during the term of the agreement must be released upon request by Covestro AG and used to compensate a net loss for the year or transferred as profit.

Results of Operations

Covestro AG income statements according to the German Commercial Code

	2019	2020
	€ million	€ million
Income from investments in affiliated companies – net	695	77
Interest expense – net	(14)	(23)
Other financial income – net	(3)	(16)
Net sales	21	22
Cost of services provided	(19)	(18)
General administration expenses	(48)	(46)
Other operating income	–	19
Other operating expenses	(3)	(31)
Income before income taxes	629	(16)
Income taxes	(6)	(29)
Net income/net loss	623	(45)
Retained earnings brought forward from prior year	1	220
Allocation to/withdrawal from other retained earnings	(185)	76
Distributable profit	439	251

In fiscal 2020, Covestro AG generated a net loss for the period of €45 million (previous year: net income of €623 million). This is due to factors including the reduced income from investments in affiliated companies of €77 million (previous year: €695 million). Income from investments in affiliated companies was solely attributable to income from the control and profit and loss transfer agreement with Covestro Deutschland AG.

General administration expenses totaling €46 million (previous year: €48 million) mainly consisted of personnel expenses for the employees of the Group holding company and members of the Board of Management. The interest result included interest expense of €20 million for the euro bonds issued. Other financial income and expenses mainly comprised bank fees totaling €15 million. These included fees for the provision of credit lines, one-time fees associated with the issue of the new euro bonds, the pro rata reversal of the discount on the euro bonds issued, and ancillary costs for the capital increase performed in fiscal 2020. Other operating income of €19 million related almost solely to the reversal of provisions for settling possible tax claims by Bayer AG in

connection with the contribution, indemnification, and post-formation agreement. Other operating expenses mainly resulted from expenses associated with the announced acquisition of the Resins & Functional Materials (RFM) business from Koninklijke DSM N.V., Heerlen (Netherlands), in the amount of €30 million. Other income and expense items had no notable effect on earnings.

The result of operations was €-16 million (previous year: €629 million) and led to income taxes of €29 million (previous year: €6 million). After adding retained earnings brought forward from prior year of €220 million (previous year: €1 million) and withdrawing an amount of €76 million from other retained earnings (previous year: allocation of €185 million to other retained earnings), distributable profit amounted to €251 million (previous year: €439 million).

For fiscal 2020, net income was expected to be well below the level in fiscal 2019 in line with our forecast from the Annual Report 2019. With a net loss of €45 million this forecast was met. The Board of Management and the Supervisory Board are proposing a dividend of €1.30 per share carrying dividend rights for the 2020 fiscal year to the Annual General Meeting.

Net Assets and Financial Position

Covestro AG statements of financial position according to the German Commercial Code

	Dec. 31, 2019	Dec. 31, 2020
	€ million	€ million
ASSETS		
Noncurrent assets	1,767	1,767
Intangible assets, property, plant and equipment	1	1
Financial assets	1,766	1,766
Current assets	3,999	5,401
Trade accounts receivables	7	30
Receivables from affiliated companies	3,902	5,337
Other assets	90	34
Deferred charges	5	12
Excess of plan assets over pension liability	8	9
Total assets	5,779	7,189
EQUITY AND LIABILITIES		
Equity	4,636	4,823
Capital stock	183	193
Own shares	-	-
Issued capital	183	193
Capital reserves	3,500	3,942
Other retained earnings	514	437
Distributable profit	439	251
Provisions	125	90
Provisions for pensions	3	4
Provisions for taxes	81	77
Other provisions	41	9
Liabilities	1,018	2,276
Bonds	1,000	2,000
Liabilities to banks	-	225
Trade accounts payables	11	17
Payables to affiliated companies	3	1
Other liabilities	4	33
Total equity and liabilities	5,779	7,189

Covestro AG had total assets of €7,189 million as of December 31, 2020 (previous year: €5,779 million). The net assets and financial position of Covestro AG are dominated by its role as a holding company in managing subsidiaries and financing corporate activities. This is primarily reflected in the levels of financial assets (24.6% of total assets), of receivables from affiliated companies (74.2% of total assets) and of the liabilities.

Receivables from affiliated companies increased by €1,435 million to €5,337 million (previous year: €3,902 million). This was primarily due to a higher intercompany loan to Covestro Deutschland AG.

All receivables and other assets have maturities of less than one year.

Property, plant, equipment, and intangible assets were of secondary importance. Current other receivables of €30 million (previous year: €7 million) and deferred income of €12 million (previous year: €5 million) were also immaterial in relation to total assets. Other assets of €34 million (previous year: €90 million) mainly included income tax and VAT receivables.

Covestro AG's equity amounted to €4,823 million (previous year: €4,636 million). This corresponds to an equity ratio of 67.1% (previous year: 80.2%). The October 2020 capital increase lifted capital stock by €10 million and capital reserves by €437 million. In addition, capital reserves increased by €4 million due to the issue of treasury shares to employees as part of the Covestment stock participation program. In contrast, the payment of the dividend for the 2019 fiscal year in the amount of €219 million and the net loss for the period of €45 million reduced equity.

In contrast to equity, provisions amounted to €90 million (previous year: €125 million) and other liabilities totaled €2,276 million (previous year: €1,018 million).

Provisions comprised provisions for pensions and other post-employment benefits of €4 million (previous year: €3 million), tax provisions of €77 million (previous year: €81 million), and other provisions of €9 million (previous year: €41 million).

The increase in liabilities was mainly due to the issue of euro bonds in June 2020 with a total volume of €1.0 billion. The bonds amounting to €2.0 billion have the following maturities: €500 million mature in 2021, another €500 million mature in one to five years, and €1.0 billion mature in 2026 or later. Moreover, liabilities to banks totaling €225 million are due in one to five years. All other liabilities are due within one year.