

CIBA SPECIALTY CHEMICALS: LETTER TO SHAREHOLDERS

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Ciba



HALF YEAR 2005

VALUE BEYOND CHEMISTRY

LETTER TO SHAREHOLDERS

DEAR SHAREHOLDERS,

Today we are announcing our financial results for the first half of 2005, and I would like to give you an overview of our performance and an update on some important strategic steps.

We made progress in the second quarter of 2005, with several areas of the business developing well and further sales price increases being pushed through. Project Shape is on track, with the integration of Raisio Chemicals moving ahead rapidly and measures in Textile Effects being accelerated.

We are taking further measures in the second half to enhance margins, with a continued drive to increase sales prices and realize cost savings. Cash flow will be improved with a strong focus on profitability and the reduction of current assets. In addition, we are well advanced with the evaluation of strategic options to reposition the Textile Effects business. These range from internal solutions to a divestment.

I would also like to update you on a decision made by the Board of Directors of Ciba Specialty Chemicals, to adapt the structure of the Executive Committee to reflect the changing needs of the Company and its markets and thereby, strengthen its strategic and operational leadership.

We will introduce a new position of Chief Operating Officer, responsible for the operational management of the businesses. Brendan Cummins,

over the first half of 2004. This figure includes an estimated acquisition effect of 10 percent, relating to Raisio Chemicals.

Our margins remain under pressure due to higher raw material costs. Adjusted EBITDA margin before restructuring of 13.2 percent of sales, showed an improvement from the first to the second quarter, although it is lower than the 15.1 percent of the previous year.

The Coating Effects and Plastic Additives segments remain strong, high margin businesses which continue to deliver good results. We will further improve the margins in the Water & Paper Treatment segment, with the integration of Raisio Chemicals. Decisive action is also being taken to bring Textile Effects to higher, sustainable levels of profitability.

Net income for the first half was CHF 146 million, compared with CHF 201 million for the first half of 2004. Included in this figure is CHF 36 million of restructuring, as well as CHF 30 million of income from the release of a provision related to the divestment of the Performance Polymers business in 2000. Comparable net income for the first half of 2005 was 18 percent lower, at CHF 152 million (CHF 186 million in the first half of 2004).

The balance sheet remains strong, with a debt to equity ratio of approximately 1:2.



ARMIN MEYER, Chairman of the Board and Chief Executive Officer

currently Head of the Plastic Additives segment, has been appointed to this position. He has been with Ciba for more than 30 years in a number of leading international positions. In the future, the Company will be led by the Executive Committee with two dedicated teams – the Chairman's Committee, focusing on strategic development, and the Operating Executive Committee, focusing on the operational management of the business. These changes take effect on October 1st, 2005.

RESULTS OVERVIEW

In general, we found business conditions for the first half of the year to be fairly mixed, with continued strong growth in Asia, especially China and India, as well as in South America, while Europe and NAFTA were flat. There was strong demand in some of our customer industries, notably in personal care and packaging; however, in others, like the automotive industry, demand was lower than in the first half of 2004. We were also impacted by the lockout of the paper industry in Finland, which resulted in a loss of sales of CHF 30-40 million and reduced sales growth in the second quarter by around 2 percent.

Sales in the first half year were up 9 percent in local currencies and 7 percent in Swiss francs. We were able to further increase sales prices by 2 percent, compared with the first half of 2004. Volumes were up 7 percent

Free cash flow, excluding dividends, was a negative CHF 200 million, compared with CHF 10 million during the first half of 2004. Free cash flow is typically weaker in the first half than in the second half of the year, as we have to pay our interest payments and tax during the first six months and traditionally have a current asset build-up before the summer. This year it also reflected the increased inventory value relating to higher raw material costs, as well as a lower operating income.

Overall, we are not yet satisfied with the results, but we have taken decisive measures to improve our performance.

PROJECT SHAPE ACCELERATED

The integration of Raisio Chemicals into the Water & Paper Treatment segment is moving ahead rapidly. Measures have been implemented to fully leverage synergies and our target for the Water & Paper Treatment segment to reach 14-15 percent adjusted EBITDA margin next year, is on track.

In Textile Effects, the action taken to realign the business in response to the shift of the textiles market to Asia has made progress, and we have expanded and speeded up this process in order to achieve higher savings earlier.

Savings from Project Shape of approximately CHF 20 million were made, with a reduction of approximately 200 positions globally. The

acceleration and expansion will increase the expected savings for 2005 to CHF 60 million, with 600 positions in total reduced during the year. As a result, restructuring charges for Project Shape in 2005 are expected to be CHF 130 million.

STRATEGIC REPOSITIONING OF TEXTILE EFFECTS BUSINESS

The shift of the textile market to Asia is being greatly accelerated by the ending of the WTO quotas and is expected to continue over the coming years. We have conducted a comprehensive strategic review of our Textile Effects business and its environment, and concluded that the global textile market continues to offer attractive opportunities. Our underlying business has a strong market position and is a leader in innovation and quality. We need, however, to take additional action in order to put Textile Effects on a lower cost base, with higher, sustainable levels of profitability. The evaluation of a number of strategic options is now well advanced. These options range from internal solutions to a divestment of the business.

Ciba Specialty Chemicals is committed to finding a solution that secures a sustainable future for Textile Effects, strengthens the Company's overall position and takes into account the interests of our employees.

production facility for Plastic Additives in Asia Pacific in the next few months, to further serve the anticipated growth in plastics manufacturing in Asia and the Middle East.

OUTLOOK

Business conditions for the first half of the year were influenced by varying demand across different customer industries. The Company anticipates a similar pattern for the remainder of the year. Growth in Asia is expected to continue, with little change in demand in Europe and the Americas. Raw material costs are expected to stabilize in the second half, however, it is difficult to make an accurate forecast with volatile oil prices. Further steps will be taken during the second half to assure improved results, and particularly, a significantly higher level of cash flow.

Assuming this continuation of current business conditions, for the full year 2005, the Company expects higher sales in local currencies and a slightly higher adjusted EBITDA in Swiss francs, compared with 2004. Net income on a comparable basis, excluding aperiodic benefits and restructuring charges, is expected to be around the same level as 2004. It will, however, be challenging to achieve a free cash flow within the range previously indicated, CHF 380-480 million, excluding dividend.



Our strategy remains focused on further strengthening our businesses with sustainable profitable growth from a strong, customer focused, geographically balanced portfolio."

STRENGTHENING INNOVATION – FURTHER EXPANSION IN ASIA

Innovation remains a priority for Ciba Specialty Chemicals, and we continue to invest more than 4 percent of sales in research and development. During the first half of the year, we acquired Metasheen, a high reflectance aluminum technology, to strengthen our high value, high technology pigments business. Together with the joint venture for pearlescent effect pigments in China and other technological cooperation in this field, we have now built up a comprehensive product offering in this attractive market. We have also successfully launched a new photoinitiator for the lucrative LCD market.

We are seeing continued strong growth potential in Asia, with a quarter of our sales already coming from the region and further expansion planned. The acquisition of Daihan Swiss, our joint venture in Korea, has provided us with a stronger, integrated pigments platform. Similarly, the acquisition of the Raisio Chemicals businesses in China and Korea has further built up market presence for Paper Chemicals. Our new research center in Shanghai was opened in April and is expected to have around 100 scientists working on innovation projects for the region.

Substantial investment is being made into new production facilities for Coating Effects in India. In addition, there will be investment into a new

Project Shape will result in savings for 2005 of approximately CHF 60 million, with 600 positions in total reduced during the year. Restructuring charges for Project Shape in 2005 will increase by CHF 80 million to CHF 130 million.

Overall, the acceleration and expansion of Project Shape will increase annualized savings by 2007, from the CHF 130 million (CHF 90 million after tax) previously announced, to CHF 180 million. The financial impact of the repositioning of Textile Effects is not yet quantifiable.

Our strategy remains focused on further strengthening our businesses with sustainable, profitable growth from a strong, customer focused, geographically balanced portfolio.

I thank you, on behalf of the Board of Directors, for your trust and continued loyalty.

Armin Meyer
Chairman of the Board and Chief Executive Officer
Ciba Specialty Chemicals

FINANCIAL SUMMARY HALF YEAR 2005

(in millions of Swiss francs, except per share data)

Six months ended June 30, (unaudited)

STATEMENTS OF INCOME	2005	2004
Net sales	3 649	3 405
Gross profit	1 062	1 114
Operating income before restructuring charges	272	330
Restructuring charges ^(a)	(50)	0
Operating income	222	330
Financial income and expense, net	(57)	(71)
Income from continuing operations before income taxes and minority interest	165	259
Provision for income taxes	(46)	(55)
Minority interest	(3)	(3)
Income from continuing operations	116	201
Income from discontinued operations, net of tax	30	0
Net income	146	201
Net income before restructuring charges	182	201
Earnings per share, basic and diluted	2.22	3.03
Earnings per share before restructuring charges, basic and diluted	2.77	3.03
Adjusted EBITDA^(b) before restructuring charges	480	513

^(a) Restructuring charges, net of taxes of CHF 14 million would be CHF 36 million.

^(b) Adjusted EBITDA is calculated as operating income plus depreciation and amortization. In financial statements published prior to June 30, 2005, the Company referred to adjusted EBITDA as EBITDA.

VALUE BEYOND CHEMISTRY

BALANCE SHEETS	JUNE 30, 2005 (unaudited)	DEC. 31, 2004
Current assets	4 001	4 382
Property, plant and equipment, net	3 113	3 015
Other long-term assets	3 747	3 609
Total assets	10 861	11 006
Current liabilities	1 879	2 140
Long-term liabilities	4 691	4 647
Minority interest	78	68
Shareholders' equity	4 213	4 151
Total liabilities and shareholders' equity	10 861	11 006
Net debt	2 418	1 840

Six months ended June 30, (unaudited)

STATEMENTS OF CASH FLOWS	2005	2004
Net cash (used in) provided by operating activities	(104)	122
Net cash used in investing activities	(128)	(796)
Net cash used in financing activities	(641)	(382)
Effect of exchange rate changes on cash and cash equivalents	38	(20)
Net decrease in cash and cash equivalents	(835)	(1 076)
Free cash flow^(c)	(200)	10

^(c) Free cash flow is calculated as cash flows from operating activities from continuing operations less net cash from investing activities before sale (acquisition) of businesses, net of cash. In financial statements published prior to June 30, 2005, the Company also deducted a pro-forma CHF 2 per share dividend from the calculation of free cash flow. The 2004 free cash flow figures presented here have been adjusted accordingly.

EXCHANGE RATES OF PRINCIPAL CURRENCIES TO CHF (UNAUDITED)

		STATEMENT OF INCOME		BALANCE SHEET	
		AVERAGE RATES		PERIOD-END RATES	
		SIX MONTHS ENDED JUNE 30,		JUNE 30,	DEC. 31,
		2005	2004	2005	2004
1	U.S. dollar (USD)	1.20	1.27	1.27	1.15
1	British pound (GBP)	2.25	2.30	2.32	2.21
1	Euro (EUR)	1.55	1.55	1.54	1.54
100	Japanese yen (JPY)	1.13	1.17	1.16	1.11

FREE CASH FLOW (UNAUDITED)

(in millions of Swiss francs)

Six months ended June 30,	2005	2004
Free cash flow before restructuring payments	(178)	10
Less: restructuring payments	(22)	0
Free cash flow	(200)	10
Add: net cash used in investing activities	128	796
Less: sales (acquisition) of business, net of cash	(32)	(684)
Net cash (used in) provided by continuing operations	(104)	122

NET INCOME BEFORE RESTRUCTURING CHARGES (UNAUDITED)

(in millions of Swiss francs)

Six months ended June 30,	2005	2004
Net income before restructuring charges	182	201
Restructuring charges, net of tax	(36)	0
Net income	146	201

EARNINGS PER SHARE BEFORE RESTRUCTURING CHARGES (UNAUDITED)

Six months ended June 30,	2005	2004
Net income per share before restructuring charges	2.77	3.03
Restructuring charges, net of tax	(0.55)	0.00
Net income per share	2.22	3.03

VALUE BEYOND CHEMISTRY

COMPONENTS OF NET DEBT (UNAUDITED)

(in millions of Swiss francs)

	JUNE 30, 2005	DEC. 31, 2004
Short-term debt	261	559
Long-term debt	2 943	2 917
Total debt	3 204	3 476
Cash and cash equivalents	(779)	(1 614)
Short-term investments	(7)	(22)
Net debt	2 418	1 840

FORWARD-LOOKING STATEMENTS

Forward-looking statements and information contained in this Shareholder Mailing are qualified in their entirety as there are certain important factors that could cause results to differ materially from those anticipated. Certain such forward-looking statements can be identified by the use of forward-looking terminology such as "believe," "expect," "may," "are expected to," "will," "will continue," "should," "would be," "seek" or "anticipate" or similar expressions or the negative thereof or other variations thereof or comparable terminology, or by discussions of strategy, plans or intentions. Such statements reflect the current views and estimates of the Company with respect to market conditions and future events and are subject to certain risks, uncertainties and assumptions. Investors are cautioned that all forward-looking statements involve risks and uncertainty. In addition to the factors discussed above, among the factors that could cause actual results to differ materially are the following: the timing and strength of new product offerings, pricing strategies of competitors, introduction of competing products by other companies, lack of acceptance of new products and services by the Company's targeted customers, changes in the Company's business strategy, the Company's ability to continue to receive adequate raw materials from its suppliers on acceptable terms, or at all, and to continue to obtain sufficient financing to meet its liquidity needs, and changes in the political, social and regulatory framework in which the Company operates or in economic or technological trends or conditions, including currency fluctuations, inflation and consumer confidence, on a global, regional or national basis and various other factors. Furthermore, the Company does not assume any obligation to update these forward-looking statements.

ADJUSTED EBITDA BEFORE RESTRUCTURING CHARGES (UNAUDITED)

(in millions of Swiss francs)

Six months ended June 30,	2005	2004
Adjusted EBITDA before restructuring charges	480	513
Restructuring charges	(50)	0
Depreciation and amortization	(208)	(183)
Operating income	222	330
Financial income and expense, net	(57)	(71)
Provision for income taxes	(46)	(55)
Minority interest	(3)	(3)
Income from discontinued operations, net of tax	30	0
Net income	146	201

OPERATING INCOME BEFORE RESTRUCTURING CHARGES (UNAUDITED)

(in millions of Swiss francs)

Six months ended June 30,	2005	2004
Operating income before restructuring charges	272	330
Restructuring charges	(50)	0
Operating income	222	330

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in both English and German.
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Ciba Specialty Chemicals Inc.

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Value beyond chemistry