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## Documentation

### ***Address by Armin Meyer, Chairman and CEO Ciba Specialty Chemicals Annual General Meeting 2004***

Dear Shareholders,

The Ciba ship weathered the storm in 2003 and is still on course. We are even moving ahead faster and have become more agile. Our efforts to reduce current assets and to generate cash flow have been very successful. What's more, we've made significant progress with our "Managing for Growth" program. Ciba Specialty Chemicals is well positioned for the anticipated upturn. Once a sustainable economic recovery sets in, we expect to see this translate into a substantial improvement in net income and margins.

You too, our shareholders, can participate in our solid position. For the third year in a row, the Board of Directors is proposing a high payout of 3 Swiss francs a share, plus the cancellation this year of 1.3 million shares in order to enhance the share value.

Those are the key points.

I'd like to take this occasion to thank our employees the world over for their great dedication in difficult times and to thank you, our shareholders, for the trust you show in our company.

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2003 was another challenging year. Ciba Specialty Chemicals was, once again, confronted by the rise of the Swiss franc against the US dollar. At the same time, business conditions remained extremely volatile against a background of geopolitical uncertainties. Competition from rival producers in Asia became ever tougher.

Amid these genuinely difficult conditions, we kept Ciba Specialty Chemicals on course.

In 2003 Ciba generated an exceptionally high free cash flow of 728 million Swiss francs thanks to a series of targeted measures. This result, which was 7% higher than

in the already good level of the previous year, was well above expectations. A major factor was our concerted effort in the fourth quarter to reduce net current operating assets. This involved a drive to reduce accounts receivable and inventories of raw materials and products. In order to reduce our inventories, we instigated the temporary shutdown of a number of production plants in the final weeks of the year, taking into account the one-off costs this incurred.

The success is obvious. We reduced our inventories by more than 200 million Swiss francs, from 20.4% to 18.5% of sales. On the whole, net current operating assets declined from 27.0% to 24.7% of sales. We have thus completed one of the last of our major tasks. We compare well with our competitors in the industry and, as regards accounts receivable, we are even one of the best in the specialty chemicals sector.

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With our strong cash flow in 2003, we have further reinforced our rock solid balance sheet. We are thus building on the success of past years. Despite the difficult economic situation, we have reduced our net debt by almost two thirds in the past three years. At the same time, we have more than doubled our cash holdings. This enables us to maximize our financial flexibility (in other words our liquidity), which is something that sets us apart from most of our competitors. Financial strength in difficult economic times is an incalculable advantage.

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We have taken full advantage of the growth opportunities. In what were at times extremely difficult conditions, we have managed to maintain our sales in local currencies at the level of the previous year. However, the stronger Swiss franc has meant that our Group-wide sales in Swiss franc terms have contracted by 6%. Despite a strong headwind, three segments – Plastic Additives, Water & Paper Treatment and Home & Personal Care – expanded their positions. Business in the Asia-Pacific region, where sales increased 5% in local currencies, was very successful. In China alone, sales soared 15% in local currency terms. And we added innovative products and technologies to our strong portfolio.

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We have ensured our profitability for the future.

Various trends and one-off costs reduced profits in 2003. But we have created the necessary conditions to increase our margins again with a company that is operationally and financially leaner. In 2003, various factors caused a decline in both operating profit and earnings before interest, taxes, depreciation and amortization or EBITDA.

Firstly, profitability was impacted by extremely unfavorable exchange rate fluctuations. In particular, the Swiss franc rose by 13% against the US dollar. More than half of the decrease in the EBITDA margin was caused by this currency effect.

Secondly, the temporary plant closures at the end of the year impacted on our profitability. Normally, the products manufactured cover fixed operating costs. Since we produced fewer products, though, not all our fixed costs were covered. This has

resulted in a non-recurring charge of 60 million Swiss francs in the fourth quarter. However, this one-off price is worth it to us in order to gain the notable improvements in current assets.

Thirdly, we were confronted, as expected, by higher costs for pensions and insurance and with a decrease in margins because volume growth could not quite keep pace with falling prices.

On the plus side, though, further cost savings and efficiency increases had a positive impact. We made further significant progress in our integrated purchasing system, and administrative costs in local currencies were kept at the previous year's level. At several plants, we took measures to reduce capacity and boost productivity. One such measure was the announcement last November that production of Textile Effects in Basel would be modernized and streamlined. In a bid to cut costs and boost efficiency, we merged the support structures for Germany and Switzerland into the Central Europe Region. We shed jobs in regions with lower growth while increasing headcount in countries displaying higher growth.

The above-mentioned charges also impacted on net income, which declined by 15% compared with the previous year. This despite lower financial expenses owing to the reduction in net debt and lower interest rates, a significantly improved result due to currency hedging and non-recurring effects.

On the whole, therefore, we posted very acceptable financial results despite the difficult environment. With our current balance sheet structure, the company is healthier than ever.

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That means that Ciba is a solid and reliable partner for you, our shareholders, in the current difficult environment.

The price of the Ciba share has clearly outperformed Swiss Market Index SMI® in the past three years. Even if other companies closed the gap somewhat in 2003, we have still outperformed the broad market by about 25 per cent since January 2001.

And the yield we offer is also impressive. Last year, we again distributed three francs a share. Moreover, most shareholders do not have to pay any income tax on the par-value reduction, so that the yield comes to over 4 per cent if you factor in tax effects.

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We have done well in a difficult environment and we have a solid and reliable foundation.

We are drawing on a long-term package of measures whose continuity is essential for substantial and sustainable improvements.

- With our "Fit for Growth" program, launched in 2001, we created a company with a lean structure and a narrower cost base.
- By focusing on cash flow, we durably strengthened our balance sheet.
- And in 2003, with "Managing for Growth", we geared the company to long-term, profitable growth.

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The "Managing for Growth" program is crucial for the future of Ciba Specialty Chemicals. In the second half of my talk, therefore, I will deal with this program and the related strategic considerations in greater detail.

Last year all 18,700 employees world-wide, participated in special "Managing for Growth" workshops. They helped us achieve two goals: Firstly, we have developed a corporate culture that is geared to profitable growth. Secondly, Ciba employees have developed concrete ideas and already implemented them to a large extent in their particular area of work. A large number of ideas were produced, ranging from reduction in waste and energy consumption in production to a market forum for the exchange of industry and product knowledge between the segments.

In addition, 29 projects got off the ground in the areas of cross-segment sales, geographic growth markets, integrated service solutions, innovation, training and acquisitions. In relation to our ambitious, medium-term goal of averaging 6% sales growth annually in the local markets, the "Managing for Growth" drive will have to contribute at least 2%, with market growth and acquisitions each contributing a further 2%. We expect these projects to start delivering results already this year and to make a real impact as of 2005.

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The first major pillar of "Managing for Growth" is the geographic growth markets. As I have already mentioned, the China region increased its sales in local currencies by 15% in 2003. Growth in Eastern Europe and Latin America was 5%. These growth markets have a double strategic significance for us. They show strong growth in a global comparison and they are an opportunity to gain further market share.

Within the framework of "Managing for Growth", we have created new business support centers. In Eastern Europe, we cover the new EU member states such as Hungary, Poland, the Czech Republic, Slovakia and Slovenia from Budapest. From Bahrain we cover the Gulf States, where the plastic industry is showing the world's highest growth rates and water supply is a particular challenge (to mention two of many market opportunities).

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We see even greater growth potential in Asia, especially in the two giants, India and most of all China. There is no doubt that Asia — one-third of the world, 30 countries, three billion people — will shape the world economy of the 21<sup>st</sup> century. This is especially true of our industry as, on the one hand, Asia presents competitive advantages as a production location, and on the other, Asia will continue to grow in importance as a market for our output. In a moment you'll learn more about this key market of the future and our activities there in a short video and a first-hand presentation by one of Ciba's leading managers in Asia. So I'll restrict myself here to the significance of Asia for Ciba from a global strategic point of view.

Allow me one preliminary remark: if we are giving particular attention to Asia at today's general meeting, it is because Asia is an important market where we plan to make further investments. Nevertheless, the other major markets such as Europe and the United States remain equally important, even if demand there is relatively sluggish at the moment. The fairly even geographic distribution of our markets, with 28% in

Asia, 31% in the Americas, and 41% in Europe, shows that we are well-balanced but still have significant opportunities for growth. Ciba's market is the whole world!

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The importance of Asia for the future of Ciba Specialty Chemicals however, can scarcely be over-estimated. We hold a strong position in Asia-Pacific and were historically one of the first chemical companies to make substantial investments there. With the region accounting for 28% of our sales, Ciba Specialty Chemicals holds a leading position in our branch of industry. We have become insiders with over 3100 local employees and a network of research, production, marketing, customer service, and sales facilities. Nevertheless we hold fast to our Ciba identity, which represents quality, innovation, safety, and reliability.

All this is good, but not good enough. In order to remain competitive against increasing competition from Asia, especially China, and to take full advantage of the growth opportunities in these markets, we will further expand our position in Asia. For our customers' industries as well as for us, Asia is gaining in importance. Our vision is that we achieve a notable, profitable growth over the next few years and that the share of sales is evenly spread over the three areas of the world.

This makes Asia an engine of growth for the entire company. Consequently, it also means that we will have to deploy additional resources to these Asian markets. Specifically, most of the expansion in Ciba's production capacity to meet market needs for the next few years will take place in Asia. With a regular, yearly investment of approximately CHF 250 million, we can build significant additional production capacity in Asia, in that we already have a well-developed network of production sites there.

By expanding our capacity in Asia we are facing our Asian competitors on their own ground. At the same time, we are bringing costs and sales in the various regions into better balance, thus reducing our exposure to exchange rate fluctuations. In parallel, we are increasingly bundling purchasing for the entire company and switching to more cost-effective suppliers in Asia, Eastern Europe, and throughout the dollar zone.

Again: investing in Asia does not mean that we are neglecting our traditional regions such as the United States and Europe. Instead, our focus in these areas is to continue to ensure the highest standards of quality and competitiveness. These production sites continue to play an important role in the global group and will also benefit from our strength in Asia. Moreover, our production facility in Switzerland remains a key center of excellence for the introduction of new products thanks to its proximity to our research and development operations.

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A second pillar of "Managing for Growth" is innovation. Continually bringing innovative products to market ever faster is crucial for profitable growth, higher margins, and global competitiveness. Despite the weak economy, we invest a good 4% of sales into research and development, as continuity is crucial. Last summer we expanded our special research fund for new breakthrough technologies from CHF 10 to 15 million.

As part of our Asian development program, we will enlarge our research center in Mumbai, India and open a new research center in Shanghai. Superior innovation is part of our response to the ever more aggressive competition we face from Asia.

In the medium term, we want about a third of our sales to consist of products less than five years old — a 25 per cent increase. In this way we hope to fulfill our customers' needs even better and help them realize their visions. Whenever I visit customers, I find that they very highly value Ciba Specialty Chemicals' ability to innovate.

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Ciba Specialty Chemicals files some 200 patents and launches some 300 new products each year. Out of these numerous examples of innovation, I'd like to focus here on just one.

Our new Ciba® Tinocat® oxidation catalysts make laundry detergents that work effectively on every stain even at low wash temperatures, a real possibility. Achieving this effect requires a mere half-gram of Tinocat per kilogram of detergent. The secret is in our product's catalyst effect, which makes bleaching agents effective even at temperatures as low as 20 degrees Celsius. This not only saves energy and cost, but also opens entirely new markets, particularly in Asia, where washing is still frequently done by hand and at low temperatures.

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The theme of our 2003 Annual Report is "know-how". We intend not only to use this "know-how" in our products, but also to sell it in the form of integrated services as part of our "Managing for Growth" projects.

A key step in this direction is the new Expert Services business unit, which markets the broad expertise that exists across the corporation to both new and existing customers. With some 180 employees in a worldwide network, the unit provides a wide range of services in the fields of product registration, environment and safety, testing, and training and education. We use not only our specialized knowledge of chemistry, but also our application experience and network of relationships with government and manufacturing partners to generate competitive advantages for our customers.

Additionally we offer Color Services and Textile Services where we have a core competency in applying color to various materials, ranging from plastics, paints and printing inks to textiles.

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In the educational area of "Managing for Growth", our priority is to further reinforce the company's marketing and sales skills and make optimal use of the various business opportunities we have with major customers. We have also set up a Sales and Marketing Board to increase bundling of opportunities across our various customer industries and segments.

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We are frequently asked why we have not yet undertaken any major acquisitions. Ciba Specialty Chemicals is in an enviable position — we have the wherewithal for external

growth, but thanks to our focused portfolio we are under no pressure in this respect. And we are not interested in assuming excessive risks. We adhere strictly to our criteria for acquisitions:

- An acquisition must fit in with our existing business
- and contribute to profits in the second year.

We will not pass up good takeover opportunities, but we will not make a move before all conditions have been met.

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Besides economic performance, Ciba Specialty Chemicals also places great emphasis on social responsibility and environmental protection. Profitability and sustainability are not mutually exclusive. Ciba Specialty Chemicals began comparing its key environmental parameters with gross earnings in 2001. Since then, the UN has promoted a program for uniform environmental reporting across industries and regions. This year, therefore, we became the first company in the world to base our environmental reporting on the UNCTAD Eco-efficiency Indicator Guidelines.

In 2001, we set three ambitious goals for ourselves in the domains of environment, health, and safety: no lost-time accidents, a 10% reduction in energy consumption, and a 10% reduction in material consumption. We have achieved substantial progress:

- The number of lost-time accidents per thousand employees declined by more than half. Just in the last three years they went from 9.6 to 4.6.
- We are using energy more efficiently: absolute energy consumption declined by 6.4% over the past three years while consumption per metric ton of output fell by 16%.
- And our material consumption efficiency improved by 3.4%.

After achieving this very satisfactory performance in environment and safety, we have now set new goals for the 2004 to 2006 time frame.

- The first goal remains our initiative for zero lost-time accidents. Even with the progress made to date, we must do everything in our power to avoid accidents.
- Second, we hope to reduce water consumption by 10% per metric ton of output. Water is becoming an ever more precious resource.
- Our third goal is to reduce CO<sub>2</sub> emissions by 10% per metric ton of output in accordance with the international Kyoto Agreement.

By pursuing these goals we seek to fully embrace our responsibility for the environment while simultaneously managing our operations more cost-effectively and sustainably.

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Ciba Specialty Chemicals is a socially responsible company and a good corporate citizen. We continued our commitment to good-neighborly relations and youth programs in the natural sciences in 2003. As a global organization, Ciba also supports diversity within its workforce, from equal-opportunity hiring to standardized

management development programs. The Company is aware that career opportunities for women in technology, science, and management must be further improved. And when senior managers work overseas, their duties normally include training a local successor. With 48 nationalities, Ciba's management team represents a breadth of cultural diversity. 17% of senior management is from the Asia-Pacific region.

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Let's conclude with the outlook for the current year. Is the upturn coming or not? Every day brings new reports in the media which are often contradictory and sometimes generate more confusion than clarity. Naturally we all hope that the economic engine in Europe and America will begin to run smoothly again, and naturally we are keeping watch for signs of recovery. But we are guided by a highly developed sense of realism and only make forecasts that can be supported by facts.

So what is our outlook for 2004? Ciba Specialty Chemicals sees only the first signs of an upturn in its customers' industries. Near the end of the fourth quarter 2003, there was a certain improvement in sales to early-cycle sectors such as the paper, printing ink, and packaging industries.

However, the Company sees no signs of a sustainable improvement in global business conditions. Therefore, we will continue with firm measures to control costs globally as well as restrict hiring in lower-growth markets specifically.

For 2004, assuming that business conditions are at least comparable to last year and that currency levels do not worsen, we expect sales in local currencies, the EBITDA margin and net income in Swiss francs to exceed last year's levels. Considering the Company's now lowered net current operating assets level, the free cash flow target is between CHF 400 million and CHF 500 million.

Should a sustainable economic recovery begin to take shape, we would expect a rapid and substantial improvement in net income and margins.

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With its substantially improved cost and capital base, Ciba is well-positioned for a recovery.