Half-year report

Higher sales – Group loss resulting from special charges – New company strategy – Focus on two businesses with a global potential

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Dear shareholders

In terms of sales, the business showed a positive development in the first half-year 2004 compared with the first six months of the previous year. The adhesives and belting businesses recorded clear increases, whereas sales of the flooring business remained on the previous year's level. The operating profit before special charges of CHF 4.6 million is 34.2 million (previous year: CHF 34.8 million), and after special charges of CHF 29.6 million. Including special charges of CHF 20.0 million in total, the Group loss in the first half of 2004 is CHF 16.2 million (previous year: Group profit of CHF 14.2 million).

Sales and profit development

In the first half-year 2004 Forbo reached net sales of CHF 827.0 million, 4.4 % up on the previous year. As a result of currency translations, the flooring business recorded a sales plus of 2.4 % to CHF 377.0 million, but in local currencies sales declined slightly by 0.4 %. As opposed, the adhesives business had 6.7 % higher sales of CHF 296.5 million, and belting sales rose by 5.1 % to CHF 153.5 million. The total effect of currency translations is insignificant for these two businesses. With about 31 %, the gross profit margin is somewhat below the previous year resulting from continued competitive pressure on sales prices as well as the unfavourable development of the US Dollar against the Euro and the Swiss Franc.

The operating profit before depreciation and amortization (EBITDA) is CHF 79.2 million (previous year: CHF 81.4 million). Reasons for this decrease are the slightly lower gross profit margin and higher operating expenses.

The operating profit (EBIT) amounts to CHF 29.6 million (previous year: CHF 34.8 million). Before a special depreciation charge of CHF 4.6 million, the operating profit is CHF 34.2 million. Contributing to this, is a clearly better result of CHF 17.9 million (+ 31.6 %) from adhesives and a slightly improved EBIT of CHF 1.0 million in the belting business. In contrast, the operating profit of the flooring business declined to CHF 19.5 million (–17.0 %). After special charges the operating profit is CHF 17.7 million.

Net financial expenses rose by CHF 19.2 million to CHF 32.1 million due to higher interest costs and lower interest income as well as a recognized valuation adjustment on marketable securities of CHF 12.0 million. The resulting half-year loss before taxes is CHF 2.5 million (previous year: Group profit before taxes of CHF 21.9 million).

After clearly higher tax charges of a total of CHF 13.7 million (previous year: CHF 7.7 million), including valuation adjustments on deferred taxes of CHF 3.4 million, the Group loss in the first half-year 2004 amounts to CHF 16.2 million (previous year: Group profit of CHF 14.2 million). This includes special charges of CHF 20.0 million in total.

Financial situation

The balance sheet total as per June 30, 2004 decreased by CHF 28.1 million (–1.8 %) compared with previous year-end. This is essentially due to the decrease of marketable securities and cash (CHF –40.6 million) as well as long-term assets (CHF –38.5 million). As opposed, operating current assets (inventories and trade receivables) clearly increased for seasonal reasons compared to year-end 2003, however, they are still below the level at the end of June 2003. Investments in fixed assets amount to CHF 25.3 million, CHF 8.7 million higher than in the corresponding period of the previous year, but lower than current periods' depreciation of CHF 42,5 million. Net debt increased, mainly for seasonal reasons, by CHF 15,3 million compared with previous year-end, but is CHF 93.5 million lower than at the end of June 2003. The reduction of securities and cash in the period under review by CHF 40.6 million was predominantly used for repayment of long-term debt (CHF –28.9 million). The credit conditions agreed with the lenders were adhered to.

The gearing (net debt/equity) at the end of June 2004 is 70.3 %, 4 percentage points higher than at the end of 2003.

Employees

As per June 30, 2004 Forbo employed 5,597 people. Compared to year-end 2003, this is an increase by 12 employees. Whereas there was an increase in North America and Asia, the number of employees decreased in Western Europe.

Outlook

Provided that today's positive economic development continues, Forbo is expecting slightly higher sales for the year 2004 to previous year. Operating profit before special charges is likely to be somewhat lower to previous year.

Strategy review

The review of the corporate strategy and operative processes carried out by Forbo over the past five months has shown that the successful development of the Group's three businesses is beyond the company's financial means and management capacities. There is a clear earnings improvement potential in all the three businesses. Consequently, Forbo will focus on the two businesses of adhesives and belting with global development potential. For the successful further development of the capital-intensive flooring business (linoleum and cushion vinyls), Forbo is looking for a partnership offering the segment optimum future chances. With this focusing strategy, the Board of Directors wants to strengthen the Group's profitability in the medium term and create new growth perspectives.

Focus on adhesives and belting

Following a review of Forbo's corporate strategy, the Board of Directors decided that the company will in the future focus on two businesses, i.e. adhesives and belting. The two businesses are well positioned in global growth markets, and they already have several production sites in key regions worldwide.

In the adhesives business, Forbo has a leading market position in selected core segments. The adhesives market promises attractive growth and profitability. It allows the company organic growth in a less capital-intensive business. Besides, the market which is still heavily fragmented will consolidate in the coming years, with Forbo playing an active part in this process.

In the belting business, Forbo with its world market share of 20 % is among the world's three leading suppliers with production sites in Asia, Europe and America. With its good strategic position, this business has a considerable earnings improvement potential. The Board of Directors is convinced that the downswing in this industry is over and that the Group's goals can be reached with the steps that have been initiated.

Securing the flooring business' future

The review of strategies, structures and operative processes has shown that the flooring business, too, has a market position with further development potential. However, in addition to the successful development of the adhesives and belting businesses, Forbo on its own is not able to advance the flooring business fast enough and successfully participate in the market consolidation.

With linoleum and cushion vinyl, Forbo is mainly active in the resilient flooring market. Other flooring materials such as laminates, stone or ceramics recorded stronger growth in the past years. Forbo and its products are represented mainly in Western Europe and in the contract market which is heavily dependent on the public spending policy. Expanding the product range or entering growth markets requires the massive use of financial means and management resources which are beyond Forbo's possibilities.

The Board of Directors has therefore concluded that this business should be strengthened by means of a partnership and that the employees should be given a credible perspective for the future. The complete divestment of the business is not being excluded, either. The proceeds from such a divestment would be used for the further development of the core businesses – adhesives and belting – and for debt repayment.

Measures for improving profitability

Despite the Group's promising starting position, Forbo is not satisfied with the current earnings situation of the businesses. There is a great earnings improvement potential in all the three businesses. Forbo has planned and partly already initiated appropriate measures for improving the profitability.

In the flooring business, the production capacities have to be adjusted to the sales volume, and production costs have to be lowered. In the adhesives business, focusing on attractive core segments and the consistent continuation of globalization are in the foreground. In the belting business, the expansion in Asia and Eastern Europe must be used in order to obtain higher margins with premium products.

Strategy holding

In line with the focusing efforts, Forbo will adapt the corporate structure to the new situation, clearly assign responsibilities and reduce overhead costs. The legal and financial structure of the individual businesses will we simplified and integrated and directly linked to the strategy holding. This move shall enhance the compeny's flexibility and focusing potential.

New head of adhesives business

At the same time, Forbo appointed Michel Riva as new head of the adhesives business. Formerly, he had various international management roles with chemical group DuPont. His task is to focus the existing activities on strategic market segments and to continue the globalization of the adhesives business.

Yours sincerely,

Willy Kissling
Chairman of the Board of Directors

This E. Schneider
Delegate of the Board of Directors and CEO

Forbo Holding AG
Eglisau/Zurich, August 20, 2004

Consolidated half-year financial statements

Summary of consolidated income statement

	First six months 2004 m CHF	First six months 2003 m CHF
Net sales	**827.0**	**791.8**
Cost of goods sold	–567.5	– 535.3
Gross profit	**259.5**	**256.5**
Operating expenses	–229.9	– 221.7
Operating profit (EBIT)	**29.6**	**34.8**
Financial expenses, net	–32.1	– 12.9
Loss/profit before taxes	**–2.5**	**21.9**
Taxes	–13.7	– 7.7
Group loss/profit	**–16.2**	**14.2**
Operating profit before depreciation and amortization (EBITDA)	**79.2**	**81.4**
	CHF	CHF
Loss/profit per share (basic)	–12.34	10.91
Loss/profit per share (diluted)	–12.18	10.79

Summary of consolidated balance sheet

	30.6.2004 m CHF	31.12.2003 m CHF	30.6.2003 m CHF
Long-term assets	**774.4**	**812.9**	**859.7**
Tangible assets	536.0	558.8	574.9
Intangible assets	156.1	163.9	175.1
Investments in associates, deferred taxes and other long-term assets	82.3	90.2	109.7
Current assets	**761.3**	**750.9**	**788.7**
Inventories	265.8	247.9	278.1
Accounts receivable, prepaid expenses and deferred charges	347.4	314.3	363.8
Marketable securities, cash and cash equivalents	148.1	188.7	146.8
Total assets	**1 535.7**	**1 563.8**	**1 648.4**
Shareholders' equity	**561.1**	**572.5**	**621.5**
Long-term liabilities	**626.7**	**670.7**	**718.8**
Long-term financial debt	525.3	554.2	618.5
Employee benefit obligations, provisions and deferred taxes	101.4	116.5	100.3
Current liabilities	**347.9**	**320.6**	**308.1**
Trade payables	128.5	114.9	117.9
Short-term financial debt	17.4	13.8	16.4
Other current liabilities and accrued expenses	202.0	191.9	173.8
Total shareholders' equity and liabilities	**1 535.7**	**1 563.8**	**1 648.4**

Summary of consolidated cash flow statement

	First six months 2004 m CHF	First six months 2003 m CHF
Cash flow from operating activities	**10.6**	**19.3**
Cash flow from investing activities	**–22.0**	**–16.6**
Cash flow from financing activities	**–29.4**	**–10.9**
Decrease in cash and cash equivalents	–40.8	–8.2
Translation differences	–0.4	1.9
Cash and cash equivalents at January 1	169.8	128.5
Cash and cash equivalents at June 30	**128.6**	**122.2**

Summary of consolidated statement of changes in shareholders' equity

	First six months 2004 m CHF	First six months 2003 m CHF
Shareholders' equity at January 1	**572.5**	**590.6**
Group loss/profit	–16.2	14.2
Changes in treasury shares	1.0	0.9
Fair value adjustments financial instruments	10.5	0.1
Translation differences	–6.7	15.7
Shareholders' equity at June 30	**561.1**	**621.5**

Additional notes to the consolidated half-year financial statements

The unaudited half-year report as per June 30, 2004 has been prepared in accordance with the accounting policies set out in the 2003 Annual Report and International Accounting Standard 34 on Interim Financial Reporting.

The scope of consolidation has not changed in the period under review.

The Annual General Meeting of Shareholders approved of a nominal value reduction of CHF 8.00 per share. The payment was made on July 23, 2004.

Comments on the businesses

Sales and results first half year

	Flooring business m CHF	Adhesives business m CHF	Belting business m CHF	Corporate and consol. m CHF	Total m CHF
Net sales 2004	377.0	296.5	153.5		**827.0**
Net sales 2003*	368.0	277.8	146.0		**791.8**
Change in % actual	2.4	6.7	5.1		**4.4**
Change in % currency adjusted	–0.4	6.6	4.7		**3.0**
Operating profit (EBIT) 2004	17.7	15.1	1.0	–4.2	**29.6**
Operating profit (EBIT) 2004 before special charges	19.5	17.9	1.0	–4.2	**34.2**
Operating profit (EBIT) 2003*/**	23.5	13.6	0.2	–2.5	**34.8**

* Restated due to new classification in 2004 of sales of adhesives products realized by the flooring business
** Restated due to changed distribution keys in 2004 for corporate and consolidation

Flooring business

The **flooring business** reached 2.4 % higher sales of CHF 377.0 million in the first half of 2004 resulting from currency translation. In terms of local currencies, sales decreased slightly by 0.4 %. While North America recorded double-digit sales growth, sales declined in some key markets of Western Europe, for instance in Germany and in Scandinavia. Especially in the retail business, trading conditions for cushion vinyl remained difficult due to overcapacities in production. In spite of restricted public spending and consequently difficult market conditions in the contract business, linoleum sales could be maintained on the previous year's level thanks to strong sales growth in the USA. As a result of the still difficult market environment in Western Europe and the unfavourable development of the US Dollar against the Euro and the Swiss Franc, the operating profit (before special charges) declined by 17.0 % to CHF 19.5 million compared to previous year.

Adhesives business

The **adhesives business** showed a positive development in the period under review, with sales rising 6.7 % to CHF 296.5 million. This is essentially due to the successful conclusion of the integration of the American adhesives producer SWIFT, and accelerated growth in the USA and parts of Europe. Besides, Forbo Adhesives recorded slightly better gross margins with new, higher value adding products. Raw material prices are still on a high level and could only be partly passed on to the customers in some segments. The fact that during the past half-year some customers shifted their activities to lower-cost countries where Forbo Adhesives is not yet active, had a negative impact on profits. Before special charges, the operating profit increased by 31.6 % to CHF 17.9 million based on the all in all positive development.

Belting business

The **belting business** recorded sales of CHF 153.5 million against CHF 146.0 million in the previous year. Thus, the sales decline could be stopped. The belting business is heavily dependent on general plant construction and investments in traffic and transport systems. Continued market weakness and reluctant investment activities led to strong price pressure in the logistics market. A positive market mood is prevailing in China, however, there are already some signs of a slow-down of the growth trend. The still weak US Dollar made exports from Europe to the USA essentially more expensive, the currency-related extra cost of European products led to lower profits. To a lesser extent this also holds true for China. The initiatives in the drive belt segment (Extremultus product line) show first signs of success but a sustainable increase in market shares will materialize only later. The operating profit of CHF 1.0 million (previous year: CHF 0.2 million) is still unsatisfactory.

Stock exchange information

Issued and outstanding shares	30.6.2004	1 316 188
Market prices	Half-year high	CHF 404.00
	Half-year low	CHF 324.00
	30.6.2004	CHF 324.00
Stock market capitalization	30.6.2004	m CHF 426

Calendar

Media release on the first three quarters 2004: October 29, 2004
Annual results media conference: March 22, 2005
Presentation to financial analysts: March 22, 2005
Annual General Meeting of Shareholders: April 29, 2005