Group business review

Oerlikon delivered a good performance for the full year of 2016 in the challenging market environment and in line with the guidance it provided. The Group's results were boosted by a strong closing in the fourth quarter, during which a noticeable increase in sales and orders were recorded. The Group also succeeded in protecting its operating profitability and market leadership position despite weak end markets caused by geopolitical and macroeconomic developments.

In 2016, Oerlikon executed the first steps in its transformation to become a global powerhouse in surface solutions and advanced materials and to position the company in markets characterized by attractive structural growth. Organizationally, the Group headquarters and the Surface Solutions Segment were merged, making the company leaner, more market-oriented and more focused on its surface solutions business. Strategically, Oerlikon successfully closed the sale of the vacuum business to Atlas Copco for an enterprise value of CHF 525 million, increasing funds and resources to invest in core businesses.

Reflecting the developments in the end markets, the full-year Oerlikon Group order intake in 2016 was CHF 2 413 million (including a positive currency impact of 1.2 %) versus CHF 2 537 million in 2015, a decrease of 4.9 %, although order backlog increased by 3.7 % to CHF 447 million at year-end 2016, compared with CHF 431 million at year-end 2015. Group sales were CHF 2 331 million in 2016 (including a positive currency impact of 1.2 %), or 12.7 % lower than the 2015 figure of CHF 2 671 million. As the Group increased its customer focus, the Group improved the ratio of Group service sales to 36.6 % of total Group sales (2015: 33.6 %).

Oerlikon Group progressively improved its operating profitability each quarter in 2016, as measured both by EBITDA and EBIT. Despite demanding market conditions, Oerlikon achieved for the full year a resilient EBITDA margin of 14.3 %, corresponding to an EBITDA of CHF 334 million (including restructuring and pension adjustments totaling CHF 19 million). That compares with reported EBITDA of CHF 338 million (including restructuring adjustments of CHF -112 million), or an EBITDA margin of 12.7 % in 2015. Full-year 2016 Group EBIT was CHF 158 million (including restructuring, pension and impairment adjustments totaling CHF 18 million), yielding a margin of 6.8 %. EBIT for 2015 was CHF -306 million in 2015 (including restructuring and impairment adjustments of CHF -588 million), or minus 11.4 % of sales.

Oerlikon Group returned to net profitability in 2016, with a net result of CHF 388 million. This translates to underlying earnings per share of CHF 1.14. In 2015, the Group reported a loss of CHF 418 million (including impairments, restructuring costs, amortization of acquired intangibles from Metco, net of tax and results from discontinued operations totaling CHF -625 million) or a loss of CHF 1.24 per share. The tax expense for 2016 was CHF 53 million, while in 2015, it was CHF 63 million.

Cash flow from operating activities before changes in net current assets remained strong at CHF 269 million in 2016 compared with CHF 393 million in 2015. The Group's return on capital employed (ROCE) was 5.7 % in 2016. In 2015, the Group's ROCE was -19.8 %.

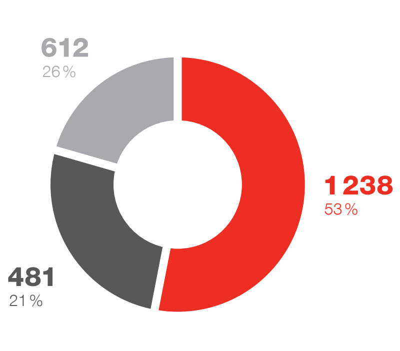
Performance in the Segments

The Surface Solutions Segment, Oerlikon's largest segment as measured by sales and profit contribution, continued to perform well in 2016 in the difficult market environment. Its performance underscores its pivotal role in the Group and offers further validation of the strategy. The Segment's order intake remained strong in 2016 at CHF 1 236 million (including a positive currency impact of 1.3 %) compared to CHF 1 233 million in 2015, as did the order backlog of CHF 80 million, which was around the same level as the CHF 81 million in the previous year. The Segment's sales increased slightly by 0.7 % in 2016 to CHF 1 238 million (including a positive currency impact of 1.4 %), and contributed 53 % to total Oerlikon sales. In 2015, sales stood at CHF 1 229 million, or 46 % of total Oerlikon sales.

Continuing its profitable growth trend, the Surface Solutions Segment achieved an EBITDA margin of 21.6 % in the fourth quarter of 2016, making a total of nine consecutive quarters where the Segment had an EBITDA margin of over 20 %. For the full year 2016, EBITDA for the Segment increased 4.9 % to CHF 277 million (including restructuring and pension adjustments totaling CHF 9 million), and yield an EBITDA margin of 22.2 %. In 2015, the Segment's EBITDA was CHF 264 million (including restructuring adjustment of CHF -2 million) and the EBITDA margin was 21.4 %. In 2016 and 2015 respectively, the Surface Solutions Segment represented 83 % and 78 % of total Oerlikon EBITDA. The Segment's EBIT in 2016 increased 2.5 % to CHF 161 million (including restructuring, pension and impairment adjustments totaling CHF 8), or 13.0 % of Segment sales, compared with CHF 157 million (including restructuring adjustments of CHF -2 million), or 12.7 % of Segment sales, in 2015.

In 2016, the Segment continued to invest in technologies and customer services, while building up new business such as additive manufacturing (AM). It opened new sites in South Korea and expanded an automotive competence center in India. It acquired DMX SAS in France, a specialist in Physical Vapor Deposition (PVD) coatings for forming tools and precision medical implants and components, to strengthen its technology and market position in the French coating market. Additionally, the Segment took important strides in 2016 in the emerging additive manufacturing market, with the intent to play a leading role in the industrialization of that market. It acquired citim GmbH, a leader in additive manufacturing design and production of metal components, to add additive production expertise and capabilities to its portfolio. The Segment is also building a new state-of-the-art manufacturing facility in the USA to produce advanced materials for additive manufacturing and high-end surface coatings.

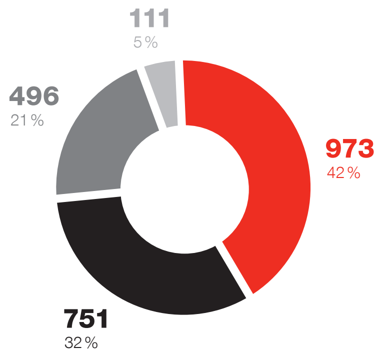
In 2016, the Manmade Fibers Segment continued to be impacted by the prevailing overcapacity in the filaments equipment market. China's 13th 5-year plan (2016–2020) depicted a 2-year consolidation period, and the Segment is currently in the midst of this period. The oversupply and resulting negative investment trend strongly affected the Segment's performance in 2016.



Sales 2016 by Segment[1]
in CHF million

- Surface Solutions Segment
- Manmade Fibers Segment
- Drive Systems Segment

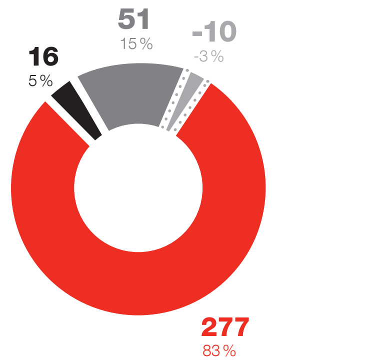
[1] Continuing operations.



Sales 2016 by region[1]
in CHF million

- Europe
- Asia Pacific
- North America
- Other regions

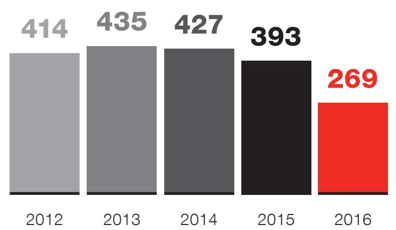
[1] Continuing operations.



EBITDA 2016 by Segment[1]
in CHF million

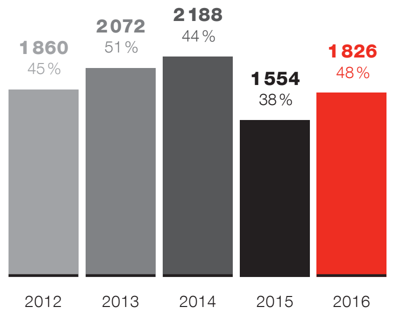
- Surface Solutions Segment
- Manmade Fibers Segment
- Drive Systems Segment
- Others

[1] Continuing operations.



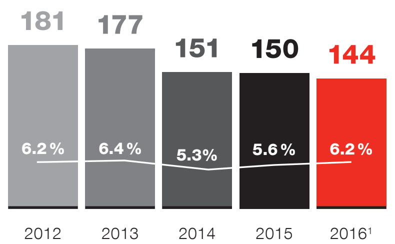
Operating cash flow[1]
in CHF million

[1] Before changes in net current assets.



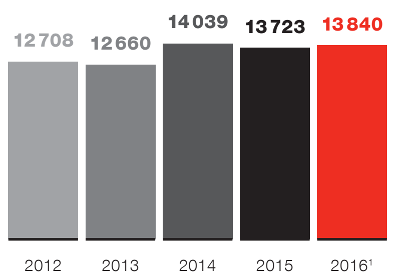
Equity[1]
in CHF million (as % of assets)

[1] Attributable to shareholders of the parent.



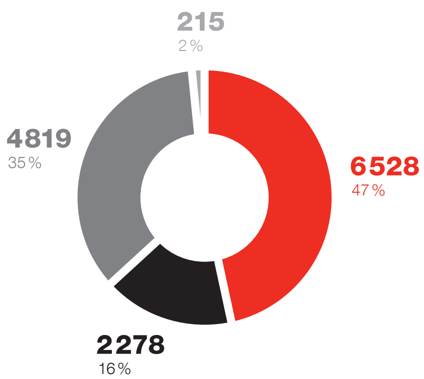
Capital expenditure
in CHF million

— In % of sales.
[1] Continuing operations.



Employees

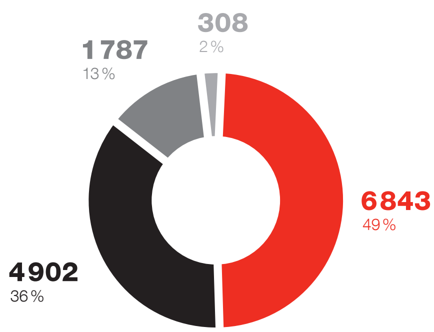
[1] Continuing operations.



Employees 2016 by Segment[1]

- Surface Solutions Segment
- Manmade Fibers Segment
- Drive Systems Segment
- Other

[1] Continuing operations.



Employees 2016 by region[1]

- Europe (EMEA)
- Asia Pacific
- North America
- Other regions

[1] Continuing operations.

However, toward the end of 2016, the Segment saw positive development in order intake and order backlogs, confirming that the bottom of its trough was reached in 2016.

Segment order intake for full year 2016 was CHF 577 million (including a positive currency impact of 0.9 %), a decrease of 21.3 % from CHF 733 million in 2015. In contrast, Segment order backlog increased 13.9 % to CHF 270 million at year-end 2016 versus CHF 237 million at year-end 2015. Sales declined 39.4 % in 2016 to CHF 481 million (including a positive currency impact of 0.7 %) versus CHF 794 million in 2015.

Considering the significantly lower top lines, the Segment managed to deliver positive operating profitability as it reduced its cost base through restructuring. Segment EBITDA amounted to CHF 16 million in 2016 (including restructuring adjustments of CHF 3 million), or 3.3 % of sales, versus CHF 85 million in 2015 (including restructuring adjustments of CHF -43 million), or 10.6 % of sales. EBIT in 2016 was CHF -3 million (including restructuring adjustments of CHF 3 million), or -0.6 % of sales. In 2015, EBIT was CHF 67 million (including restructuring adjustments of CHF -43 million) and the margin: 8.4 %.

To mitigate the impacts from the down cycle, the Segment further diversified its focus by developing its business in texturing, bulked continuous filaments (BCF), polymer processing and staple fibers, and in regional markets outside of China such as India, Turkey and USA. The Segment acquired the staple fibers technology portfolio from Trützschler, making it a leader in the synthetic staple fibers market. In 2016, the Segment's joint venture, Oerlikon Barmag Huitong Engineering, recorded its first sale of a polycondensation system.

In 2016, all of the Drive Systems Segment's end markets continued to be under pressure. Continued volatility in commodity prices and sluggish economic development resulted in equipment investments being kept on hold. The agriculture, construction, energy and mining sectors remained weak, although there are first indications that the trough in the oil & gas sector has been reached and the start of a slow recovery could be expected. Due to market developments, Segment recorded lower sales in 2016. However, the Segment's strategic reshaping of its product portfolio has led to initial positive results. The Segment managed to increase its order intake year-on-year by winning customers and projects, such as in the US and European construction and transportation sectors, in the public transportation sector in China and in the agriculture market in India.

Segment order intake increased 5.1 % in 2016 to CHF 600 million (including a positive currency impact of 1.4 %) compared to CHF 571 million in 2015, while order backlog declined 14.2 % to CHF 97 million from CHF 113 million in 2015. Segment sales totaled CHF 612 million in 2016 (including a positive currency impact of 1.4 %), a 5.6 % decrease from CHF 648 million in 2015.

Thanks to the consistent execution of restructuring and process optimization measures, the Segment succeeded in delivering a significantly improved EBITDA, amounting to CHF 51 million (including restructuring adjustments of CHF 5 million), or 8.4 % of sales. In 2015, the EBITDA was CHF -19 million (including restructuring adjustments of CHF -68 million), and the margin was -3.0 %. 2016 EBIT stood at CHF 12 million (including restructuring adjustments of CHF 5 million), or 2.0 % of sales. In 2015, EBIT was CHF -534 million (including restructuring and impairment adjustments of CHF -544 million) and the margin was -82.3 %.

To support customers in agriculture and construction, the Segment appointed new distributor partners in France, Brazil and the Gulf Region. To strengthen its position as a provider of solution/engineered products, it acquired the remaining shares of its UK-based Vocis subsidiary, an engineering firm providing transmission controls technology and developing new driveline controls. To extend the reach of key products to adjacent industries, the Segment introduced its fuel-consumption saving hybrid electric technologies for off-highway vehicles. It also made some targeted strategic partnerships and joint ventures, including for the Chinese mass transportation market and with customers in the areas of e-axles, e-drives and electronically controlled differentials.

A globally balanced business

Maintaining a portfolio of market and technology leading technologies, a global presence and comprehensive services is an important aspect of the Oerlikon strategy. By Segment – the Surface Solutions Segment contributed 53 % to total Group sales in 2016, the Manmade Fibers Segment accounted for 21 % of Group sales, and the Drive Systems Segment represented 26 % of Group sales. As an international company with a strong global footprint, Oerlikon operates over 180 sites in 37 countries. In 2016, Europe accounted for the largest proportion of Group sales, with CHF 973 million or 42 % of Group sales, versus CHF 1 023 million, or 38 % of Group sales, in 2015. Asia Pacific remained the second largest regional contributor to Group sales, despite the substantial decline in sales in China by the Manmade Fibers Segment. In total, the Group's sales in Asia Pacific totaled CHF 751 million in 2016, or 32 % of sales, compared with CHF 1 007 million or 38 % of Group sales in 2015. Group sales in North America totaled CHF 496 million in 2016, which is 21 % of Group sales, in 2016 – a decline of 5 % versus CHF 520 million, which represented 19 % of Group sales in 2015. Sales in other regions in 2016 accounted for 5 % of Group sales at CHF 111 million.

Increased balance sheet strength with equity ratio of 48 %

As of December 31, 2016, Oerlikon's balance sheet totaled CHF 3 825 million, compared to CHF 4 097 million at year-end 2015. The Oerlikon Group had equity (attributable to shareholders of the parent) of CHF 1 826 million, representing an equity ratio of 48 %, compared to CHF 1 554 million and an equity ratio of 38 % at December 31, 2015. The year-on-year decrease in the total balance sheet and the strong equity ratio primarily reflected the impacts from the closed strategic divestment of the Vacuum Segment in 2016, while the equity ratio was also attributable to the reduced current liabilities. Net cash amounted to CHF 401 million at year-end 2016, compared with CHF 79 million at December 31, 2015.

In December 2016, Oerlikon obtained a new, unsecured syndicated revolving credit facility amounting to CHF 600 million, consisting of a revolving credit facility and an ancillary credit facility with a five-year term and two optional one-year extensions. The new facility improves Oerlikon's financial flexibility and will reduce the company's annual financing costs by approximately CHF 0.5 million. Underscoring the continued financial strength of Oerlikon, both the pricing and the terms and conditions are in line with syndicated loan market standards for investment-grade companies. The new credit facility replaced the existing credit facility that was due to expire in July 2017.

Continued strong operating cash flow

Cash flow from operating activities before changes in net current assets remained strong at CHF 269 million compared with CHF 393 million in 2015. Net working capital, defined as trade and trade notes receivables plus inventories minus trade payables and current customer advances, amounted to CHF 316 million, corresponding to 14 % of Group sales in 2016, versus CHF 391 million, or 15 % of Group sales, in 2015.

Disciplined investment and use of cash continued to be Oerlikon's top priorities. Capital expenditure (CAPEX) amounted to CHF 144 million, compared to CHF 150 million in 2015. Excluding amortization of acquired intangible assets, the CAPEX-to-depreciation ratio was 1.01 times, with the Group's target continuing to be between 1.0 to 1.2 times. Among the significant capital expenditures in 2016 were: the new sales and production sites in South Korea and the expanded automotive center for the Surface Solutions Segment, and extending production facilities for the Drive Systems Segment.

Cash flow from investing activities amounted to CHF 57 million, mainly attributable to procceds from sale of vacuum business less capital expenditure and short-term deposits investments, compared with minus CHF 107 million in 2015. Cash flow from financing activities amounted to minus CHF 448 million, primarily reflecting the dividend payments of CHF 104 million, repayment of financial debt of CHF 301 million and interest paid of CHF 38 million. This compares with minus CHF 142 million in 2015, primarily reflecting the dividend payments of CHF 105 million and interest paid of CHF 41 million. Primarily reflecting the Group's operating cash flow, Oerlikon reported a cash and cash-equivalent position at the end of 2016 of CHF 751 million compared to CHF 851 million for 2015.

Oerlikon continued to invest around 4 % of its revenues in research and development (R&D). In 2016, R&D expenditures were CHF 94 million, or 4.0 % of Group sales, compared to CHF 103 million, or 3.9 % of Group sales, in 2015.

Oerlikon believes that dividend payout is an important mean of returning value to shareholders. Accordingly, at the Annual General Meeting (AGM) of Shareholders, taking place on April 11, 2017, the Board of Directors will propose a dividend payout of CHF 0.30 per share, maintaining the same level of payout as in the prior year.

2016 key Group figures at a glance

- Order intake totaled CHF 2 413 million versus CHF 2 537 million in 2015, a decline of 4.9 %.
- Order backlog increased 3.7 % in 2016 to CHF 447 million versus CHF 431 million in 2015.
- Sales decreased 12.7 % to CHF 2 331 million from CHF 2 671 million in 2015.
- EBITDA was CHF 334 million, or 14.3 % of sales, versus CHF 338 million in 2015, or 12.7 % of sales.
- EBIT was CHF 158 million, or 6.8 % of sales. EBIT for 2015 was CHF -306 million.
- The result from continuing operations was CHF 82 million. In 2015, it was CHF -402 million.
- Oerlikon returned to net profitability with net result of CHF 388 million, representing earnings per share of CHF 1.14.
- Headcount totaled 13 840 compared with 13 723 employees worldwide in 2015.
- ROCE stood at 5.7 %, compared with -19.8 % in 2015.
- The Board of Directors will propose at the 2017 AGM a dividend payout of CHF 0.30 per share, maintaining the same level of payout as in 2015.