SCRIPT—THE SPOKEN WORD PREVAILS

April 6, 2017

Sulzer Ltd—Annual General Meeting 2017
Speech Greg Poux-Guillaume, Chief Executive Officer

Dear Shareholders,

For those who are not fluent in Swiss German, I just said that last year I stated that my ambition was to make this presentation in German. I believe this is the only 2016 target Sulzer did not meet! I'm sure that the company benefited more from my concentration on the business rather than my language skills. I hope that you will forgive me.

***

In 2016, we had a solid year despite challenging markets. We beat our guidance on all three performance indicators: order intake, sales, and operational profit. We worked hard to be predictable in a market that did not lend itself to that.

There is still a lot to do, but we are heading in the right direction. For 2017, we expect growing order intake and sales, based on the acquisitions we announced. Our operational profitability should also start to pick up, if only slightly at this point.

***

Our Chairman Peter Löscher has already given you an excellent overview, so please let me give you some more details.

Our order intake was down a reported 3.4% and adjusted for foreign exchange rates and acquisitions by 5.8%. The main reasons for this development were again the challenging market conditions in the oil and gas Industry. I will comment more on that in a minute.

Sales were down 3.2% as reported and 5.1% organically, meaning adjusted for exchange rates and acquisitions. Here again, the adverse market conditions in oil and gas were the main drivers.

We are continuing to rebalance our portfolio, in part through acquisitions, in part because of the oil and gas slowdown and growth in the other markets. The share of oil and gas in our order intake is now 45%. If we were to deduct the CPI or chemical processing industry, the number would be 39%. So, the markets outside oil and gas, which are power, water, and general industry, contributed 55% — or even 61% if you add CPI — to our order intake.

We are regionally well balanced. You will notice that the Asia-Pacific region has gone from 18% of total order intake in 2015 to 21% in 2016, driven by a rebound in China, which continued to recover. With that, also the portion of our order intake in emerging markets has gone up again from 42% to 44%.

Finally, our aftermarket business is 53%, when we exclude our new Applicator System division, which has a completely different business model. The aftermarket business is much more resilient than the new equipment business.

***

Let’s start with the 55% of Sulzer that is not oil-and-gas related.

Orders in power, water, and general industry were all up in 2016.

In power, we have seen good activity levels driven by China and India. Europe, Middle East, and Africa are still slow, but we have seen investments in the gas industry in the US. The challenge we are facing in the power market is depressing pricing. The engineered pumps sold in oil and gas and power are similar and come from the same factories, so the low volumes in oil and gas are making power more competitive, leading to low prices.

In the water market, we have seen solid municipal wastewater investments in the US and China and a continuously active desalination segment in the Middle East and South East Asia.

Finally, a comment on the ever-larger general industry part of Sulzer. Still reported within Chemtech in 2016, Sulzer Mixpac Systems performed strongly. Additionally, we had the positive impact from the acquisition of Geka, which is consolidated since end of August. In general industry pumps, orders were up despite a drop in the pulp and paper business.

In Rotating Equipment Services, our electromechanical shops in the UK suffered the continuous change in the UK industrial landscape.

***

Let’s now turn to our oil and gas business, which represents 45% of our order intake. Overall, our oil and gas order intake decreased by 11%.

It shouldn’t surprise you that the activity in the upstream segment was impacted the most. Upstream means mainly the production of crude oil. Our customers have again invested less in that area. As you can imagine with fewer projects, price competition has intensified. This is also something that you need to consider when looking at our guidance because the order intake in 2016 will be our sales in 2017.

We not only experienced a weak new equipment market but in 2016, again, our customers postponed non-essential maintenance, impacting our aftermarket business.

In midstream, which is mainly the pipeline business, we saw some projects, but overall they have slowed considerably.

Downstream, comprising all refining activities, was the relative bright spot. We saw activity pick up in the last quarter of 2016. As we have explained in the past, lower oil prices meant robust refining spreads, which led to very high refinery utilization as our customers ran their plants to failure and postponed anything that could be postponed, mainly maintenance and upgrades. Here we seem to have passed an inflection point: as the price of feedstock has crept up again, refining margins have come down and our customers are arbitrating again in favor of much needed maintenance and turnarounds.

So, overall, 2016 was a tough year in oil and gas. And 2017 is not going to be much better. Downstream will continue to pick up somewhat, but upstream will further make its way down to what we think will be the trough. You will have to wait for 2018 to hear us give a rosier outlook for oil and gas.

***

Last year, I gave you detailed information about the Sulzer Full Potential program or “SFP,” as we call it internally.

Now let me give you an update on the program.

In 2016, we achieved additional savings of CHF 88 million, to be compared with the CHF 60–80 million we had guided on. So, two years into SFP, we have cumulated savings amounting to CHF 124 million, ahead of our plan in quantum and in timing. For 2017, we expect another CHF 40–60 million, and the rest in 2018 to take us to the CHF 200m target.

We are confident we will reach that CHF 200 million target because more than 90% of the savings are based on actions that are already launched, but not all finalized yet. These actions are in various stages implementation, sometimes in consultation with our social partners. The risk is mostly timing. We are also on track with the implementation costs, which amounted to CHF 96 million in 2016. We expect around CHF 55 million in 2017 and a CHF 10 million tail in 2018. But, all-in-all, we will remain within our guidance of costs of 1.2x savings (CHF 240 million implementation costs).

Most of the cost savings are structural changes and they are here to stay. We, therefore, expect high savings stickiness once the market rebounds.

Given the initial confusion about SFP targets, I always feel the need to add that the cost savings are *PRE* market impact. The unknown remains how fast and how far the market will rebound and where prices will settle.

In 2016, we were able to absorb most of the market impact through SFP cost savings. And therefore, our operational EBITA margin was only down 30 basis points from 8.6% to 8.3%.

***

So our margin declined slightly but if we compare our performance to the one of our closest competitors, we still made progress in closing the profitability gap.

We started around the time we launched SFP with a gap of approximately 730 basis points (bps) vs. our best performing competitors. Now, we don't all have the same portfolio, are not always in all the same segments, there is clearly a mix effect. But still, it is an interesting benchmark.

Last year, we told you that we had narrowed the gap by some 200 bps to 530 bps. In 2016, we narrowed the gap once again by some 180 bps to 350 bps.

It would be great if that had come with margin expansion. Still, our cost cutting is allowing us to protect our margins, overall better than our competitors.

So we are heading in the right direction, but there is still work to do.

***

Our Chairman has given you a good overview of the acquisitions we announced in 2016. These businesses will enable us to grow again in 2017.

With that let me come to our financial guidance for the year 2017.

We expect a rebalancing of supply and demand in the oil and gas market later in 2017. But because Sulzer is late cyclical, this will not lead to a noticeable commercial rebound before 2018. We expect price pressure to persist as long as load in the factories remains an issue for most manufacturers, so probably into late 2018 or early 2019. New equipment as well as services will be impacted.

In Power, we believe that gas should develop positively, but that there is increasing competition in services, driven by a very aggressive push by the big manufacturers. Coal is still substantial but decreasing with the exception of Asia. We expect the price pressure that carries over from oil and gas to persist.

In water, we see active municipal markets and desalination projects.

Now, general industry is the sum of many different things:

The markets of our Applicator Systems division — meaning dental, beauty and industrial adhesives — are expected to grow.

Pulp and paper should be healthy, whereas metals and mining remains challenging although we see the commodity cycle turning slowly.

With these assumptions, we have set our financial guidance as follows:

We expect our order intake to be up 5–8% including acquisitions announced in 2016 and adjusted for currency effects. Organically order intake is expected to be flattish to slightly down.

We expect a rather soft Q1— on or slightly above Q1 2016 levels. So the 2017 order intake profile is more back-end loaded than in 2016.

Sales — again including acquisitions announced in 2016 and adjusted for currency effects — we expect to grow by 3–5%. Organically, sales are expected to decrease around 4%.

Our operational EBITA margin or operational return on sales should start to rebound to around 8.5%.

This guidance — ladies and gentlemen — is more ambitious, even organically, than that of most of our competitors. We are raising the bar, up to us to deliver.

***

Dear Shareholders, in 2017, we will again face a challenging oil and gas market. However, the other markets we are in, are set to increase slightly. And, with the acquisitions announced in 2016, we will be able to grow again.

We have accelerated SFP, which should allow us to improve our operational profitability slightly in 2017. Nevertheless, you will only see the full effect of the program once the market rebounds.

Thank you for your support and loyalty, which we highly appreciate. And thank you for your attention.

****