Solid Financial Performance Despite Continuing Market Headwinds

Order intake decreased by 2.0%. A further significant decline in the oil and gas market was partially compensated by growth in the other market segments and by acquisitions. Sales decreased by 2.0% as a result of lower orders and the lower order backlog at the beginning of the year. Sulzer Full Potential (SFP) program savings of CHF 88 million helped to partially offset the impact of the severe headwinds on profitability. Free cash flow improved markedly to CHF 201 million.

Growth in the power and water markets and the effect of acquisitions largely offset lower order volumes in the oil and gas market

Overall order intake decreased by 2.0% from 2015 (nominal: –3.4%). The effect of acquisitions amounted to CHF 110.7 million. Order intake gross margin slightly increased nominally by 0.2% to 34.0%, because the share of higher-margin aftermarket business increased and more than offset the margin erosion in the oil and gas market.

Order intake of the Pumps Equipment division decreased by 5.4%. Strong growth in the power market and slight growth in the water market were offset by the continuing decline of orders in the oil and gas market. In the Rotating Equipment Services division, order intake decreased by 3.1%. This was mainly due to the lower sales volume in the electromechanical business in Europe and the oil-and-gas-related downturn in the North Sea. Order intake in the Chemtech division grew by 6.1%. Order intake of Sulzer Mixpac Systems increased significantly as a result of healthy organic growth and additional volume from the Geka and PC Cox acquisitions. This more than compensated a sharp decline in order intake in the Tower Field Services business unit due to fewer large projects.

Order intake in the oil and gas market decreased significantly. The industry continued to cut cost and capital investments as expected, while oil prices began to recover during the year. Order intake grew strongly in the power market, driven by the Pumps Equipment division, and in the general industry market, mainly because of the Geka and PC Cox acquisitions.

Order levels decreased in the Americas and in Europe, the Middle East, and Africa (EMEA) due to the oil and gas market downturn and — in Europe — due to the weaker performance of the electromechanical business. Order intake significantly increased in Asia-Pacific, mainly supported by China, which recovered from the very low order levels last year.

Currency translation effects amounted to a negative CHF 40.9 million affected by a weaker British pound, South African rand, Chinese yuan, Mexican peso, US dollar, and euro.

"We delivered substantial cost savings and significantly improved free cash flow in a difficult market environment."

Thomas Dittrich, Chief Financial Officer

Orders

millions of CHF	2016	2015
Order intake	2797.5	2895.8
Order intake gross margin	34.0%	33.8%
Order backlog as of December 31	1439.1	1510.7

Free cash flow

CHF 200.5m

(2015: CHF 155.8m)

Abbreviations

EBIT: Operating income
ROS: Return on sales (EBIT/sales)
opEBITA: Operating income before restructuring, amortization, impairments, and non-operational items
opROSA: Return on sales before restructuring, amortization, impairments, and non-operational items (opEBITA/sales)
opROCEA: Return on capital employed (opEBITA/average capital employed)
EBITDA: Operating income before depreciation and amortization

If not otherwise indicated, changes compared with the previous year are based on currency-adjusted figures.

As of December 31, 2016, the order backlog amounted to CHF 1 439.1 million (December 31, 2015: CHF 1 510.7 million).

Sales slightly lower

Sales amounted to CHF 2 876.7 million — a decline of 2.0% (nominal: –3.2%). Negative currency translation effects totaled CHF 34.5 million and the effect of acquisitions amounted to CHF 90.6 million.

In 2016, strong growth in the power market and the effect from acquisitions were offset primarily by the significant sales decline in the oil and gas market. Sales in the water market were also below the prior-year level, mainly due to a low starting backlog and timing of projects.

Sales increased in EMEA, while the Americas and Asia-Pacific regions were down from the previous year. Consequently, the share of sales in emerging markets slid from 40% in 2015 down to 38% in 2016.

Gross margin positively affected by cost savings

Gross margin remained stable at 30.6%. The positive effect of the factory footprint optimization and a larger share of higher-margin aftermarket business offset the price erosion effect in the oil and gas market. Total gross profit decreased to CHF 879.4 million (2015: CHF 910.1 million) as a result of lower sales volumes.

Operational EBITA impacted by lower sales volumes

Operational EBITA (opEBITA) amounted to CHF 238.9 million compared with CHF 254.1 million in 2015, a decrease of 4.4% (nominal: –6.0%). Savings from the Sulzer Full Potential (SFP) program helped partially offset the lower sales volume and acquisition-related cost increases.

Operating expenses excluding amortization, impairment on property, plant, and equipment, restructuring expenses, and other non-operational items were down by 5.7%, ahead of the 2.0% sales decline. Savings measures in selling as well as administrative expenses were partly offset by acquisition-related cost increases. Research and development expenses slightly decreased.

Operational ROSA (opROSA) decreased to 8.3% compared with 8.6% in 2015.

Operational key performance ratios

	2016	2015
opROSA	8.3%	8.6%
opROCEA	15.7%	17.0%

opROSA

8.3%

(2015: 8.6%)

The divisions achieved the following profitability figures (opROSA):
— Pumps Equipment: 5.7% (2015: 7.3%). The lower profitability was due to headwinds in the oil and gas market that resulted in lower sales volumes and pricing pressure.
— Rotating Equipment Services: 9.9% (2015: 10.2%). This drop was mainly due to a lower sales volume that could only be partially offset by lower operating expenses.
— Chemtech: 11.4% (2015: 10.1%). This increase resulted mainly from a larger share of the high-margin Sulzer Mixpac Systems business.

See abbreviations on page 33.

Bridge from EBIT to operational EBITA

millions of CHF	2016	2015
EBIT	**115.3**	**120.9**
Amortization	47.3	42.3
Impairment on tangible and intangible assets	18.4	13.0
Restructuring expenses	57.0	41.2
Adjustments for other non-operational items[1]	0.9	36.7
opEBITA	**238.9**	**254.1**
opROSA	**8.3%**	**8.6%**

[1] Other non-operational items include significant acquisition-related expenses, gains, and losses from sale of businesses or real estate (including release of provisions), and certain non-operational items that are non-recurring or do not regularly occur in similar magnitude.

Restructuring expenses and SFP program costs impacted operating income

As part of the SFP program, Sulzer has continued to implement planned actions to adapt its global manufacturing capacities and streamline its organizational setup. The measures resulted in higher restructuring expenses than in 2015. The costs were mainly associated with measures taken in Germany, Switzerland, Brazil, USA, Singapore, the United Kingdom, Sweden, and China. Overall, the number of full-time equivalents (FTE) came down from 14 253 at the end of 2015 to 14 005 at the end of 2016. This is mainly due to a reduction of roughly 1 350 FTE from SFP measures, partly offset by approximately 1 100 FTE from acquisitions.

Other non-operational items amounted to CHF –0.9 million in 2016. SFP-related expenses (CHF –26.9 million), acquisition-related expenses, and other items were offset by the favorable effect resulting from a lower conversion rate of the Swiss pension plans (CHF 35.4 million).

Consequently, EBIT amounted to CHF 115.3 million compared with CHF 120.9 million in 2015. Return on sales (ROS) was 4.0% compared with 4.1% in 2015.

Financial income: lower interest expenses

Total financial expenses amounted to CHF 19.3 million compared with CHF 24.7 million in 2015. Interest expenses were reduced by CHF 10.5 million, partly offset by lower interest income and higher other financial expenses. Lower interest expenses in 2016 resulted from the bond refinancing at favorable conditions at around mid-year (coupon expenses of CHF 7.4 million compared with CHF 12.0 million in 2015).

Furthermore, there were no significant extraordinary expenses in 2016; this stands in contrast to the CHF 5.2 million in 2015 that were related to the settlement of a dispute with the purchaser of the group's locomotive business.

See abbreviations on page 33.

Oil and gas market downturn impacted results from joint ventures

In 2016, Sulzer incurred a loss of CHF 0.8 million from joint ventures compared with a profit of CHF 3.7 million in the prior year. This relates to a joint venture in China for the service of gas turbines and a joint venture in the Middle East for the service of rotating equipment for its oil and gas and power customers.

Slightly lower adjusted effective tax rate

Income tax expenses increased to CHF 35.1 million (2015: CHF 24.9 million) on a broadly stable pre-tax income. This increase was due to restructuring expenses in 2016 without corresponding tax effect. The effective tax rate for 2016 amounted to 36.9% compared with 24.9% in 2015. Adjusted for the restructuring expense tax effect, the effective income tax rate for 2016 would have amounted to 24.3%.

Core net income

In 2016, net income amounted to CHF 60.1 million compared with CHF 75.0 million in the previous year. Core net income excluding the tax-adjusted effects of non-operational items totaled CHF 153.8 million compared with CHF 175.0 million in 2015. Basic earnings per share decreased from CHF 2.17 in 2015 to CHF 1.73 in 2016.

Improved balance sheet efficiency

Total assets as of December 31, 2016, amounted to CHF 3 735.9 million, which is a decrease of CHF 518.9 million from 2015.

Non-current assets increased nominally by CHF 235.9 million due to higher goodwill (CHF 100.3 million), other intangibles (CHF 88.9 million), and higher property, plant, and equipment (CHF 19.6 million). Goodwill, other intangible assets, and property, plant, and equipment increased by CHF 233.7 million on a currency-adjusted basis, mainly due to acquisitions.

Current assets decreased nominally by CHF 754.8 million, mainly due to the dividend payments to Sulzer shareholders of CHF 617.5 million in April 2016 as well as lower marketable securities and working capital.

Total liabilities nominally increased by CHF 124.3 million to CHF 2 144.9 million as of December 31, 2016. An increase of trade accounts payable (CHF 55.5 million), defined benefit obligations (CHF 44.8 million), provisions (CHF 39.1 million), and tax liabilities (CHF 30.2 million) was partly offset by lower borrowings (CHF 56.2 million).

Equity nominally decreased by CHF 643.2 million to CHF 1 591.0 million, mainly due to the above-mentioned dividend payments to Sulzer shareholders.

Net debt to EBITDA increased from –2.78 in 2015 to 0.14, mainly due to the special dividend payment and acquisitions.

See abbreviations on page 33.

Strong free cash flow

Free cash flow amounted to CHF 200.5 million compared with CHF 155.8 million reported in the prior year. This was driven by dynamic net working capital management, lower tax payments, and the fact that a substantial portion of restructuring expenses recorded in 2016 will only be paid in 2017.

Cash flow from investing activities totaled CHF –168.8 million compared with CHF –242.0 million in the prior year. Cash-out for acquisitions amounted to CHF –313.4 million compared with CHF –70.1 million in 2015. In 2016, marketable securities of CHF 208.4 million were sold to fund the dividends paid in April 2016, while in 2015 marketable securities were purchased (CHF –104.6 million). Capital expenditures amounted to CHF 74.9 million, broadly unchanged compared with CHF 73.7 million in 2015.

Cash flow from financing activities totaled CHF –680.6 million. It included the dividend payments of CHF 617.5 million (including the special dividend of CHF 498.1 million) compared with dividend payments of CHF 119.2 million in 2015. Repayments of borrowings reduced cash by CHF 59.4 million (2015: CHF 9.9 million). Exchange gains on cash amounted to CHF 6.7 million compared with a loss of CHF 34.0 million in 2015.

Outlook 2017

Sulzer expects that the oil and gas market, which accounted for approximately half of its revenue before recent acquisitions, will remain challenging in 2017 and that pricing pressure will persist throughout the year. Early signs of an impending recovery of oil CAPEX should only translate into a commercial rebound for Sulzer in 2018. Sulzer's other businesses are expected to grow slightly in 2017, leading to an organic order level for the company broadly stable versus 2016, supplemented by additional volume from newly acquired businesses.

Sulzer expects its SFP program to deliver incremental cost savings in 2017 in the range of CHF 40 to 60 million. The company confirms its overall target of CHF 200 million from 2018 onwards.

For the full year 2017, including acquisitions signed in 2016 and adjusted for currency effects, order intake is expected to grow by 5 to 8% and sales to grow by 3 to 5%. Sulzer expects opEBITA margin at around 8.5% (opEBITA in percent of sales).

See abbreviations on page 33.