2021 RESULTS

Management Discussion & Analysis

GROUP RESULTS

Cash flow generation was a key focus for 2021. The Group delivered strong profitability and continued to manage prudently working capital and capital expenditures to optimize cash flows. As a result, the Group generated USD 89.5 million of operating free cash flow for the year. In addition, the Group generated net cash of USD 104.2 million from the sale and leaseback of its facilities in the Lausanne, Switzerland area and from the sale of a building in the south of France. Strong cash generation allowed the Group to reduce net debt by USD 182.4 million to USD 152.4 million at the end of 2021.

Digital TV delivered strong results in 2021, with year-on-year revenue growth and a USD 97.3 million EBITDA, reflecting continued strong cost discipline. The Group's Cybersecurity business accelerated its growth momentum with solid growth rates of 21.4% in Europe and 27.8% in the US. IoT more than doubled its revenues and other operating income, reaching USD 8.2 million in 2021, with strong adoption of its new asset tracking product underpinning its growth. Public Access continues to be affected by COVID-19, as large customers, including in particular airports, shopping centers and stadiums, postponed new deployments and asset refreshment projects. Demand in the North American Public Access market remains subdued, as traffic and usage of parking infrastructure in major metropolitan areas continue to lag pre-COVID levels.

In 2021, total revenues and other operating income increased from USD 741.5 million to USD 778.8 million. Net revenues for the Group increased by 3.4% to USD 753.9 million, reflecting higher sales in Digital TV, Cybersecurity and IoT. Other operating income increased by USD 12.8 million to USD 24.9 million, mainly due to a USD 13.7 million net gain from the sale and leaseback transactions.

Margin after cost of material increased from USD 529.9 million to USD 554.1 million. Relative to total revenues, margin after cost of material decreased from 71.4% to 71.1%.

Compared to 2020, the Group increased personnel expenses by USD 18.1 million in 2021. While targeted streamlining measures resulted in a reduction of total Group headcount, the phasing out of partial unemployment measures drove personnel costs higher. In addition, operating expenses in 2020 included a one-off USD 10.0 million positive effect related to the accounting treatment of the Group's pension fund in Switzerland. Compared to the end of 2020, total Group Full Time Equivalents (FTEs) marginally decreased by 33 to 3'225 at the end of the year. The Group rebalanced headcount between Digital TV and both Cybersecurity and IoT, while streamlining of SKIDATA operations in the US resulted in the reduction of 29 FTEs.

Compared to 2020, the Group cut USD 1.9 million of other operating expenses in 2021, primarily by continuing to reduce travel expenses.

For the full year, the Group generated USD 72.4 million of operating income before depreciation and amortization, an USD 8.0 million improvement from the previous year. At USD 42.1 million, depreciation, amortization and impairment were USD 6.2 million lower than in 2020, as the Group consistently reduced capital expenditures over the last reporting periods. Overall, the Group generated an operating income of USD 30.2 million, an increase of USD 14.2 million compared to 2020.

At USD 9.8 million, interest expense was USD 0.6 million lower than in the prior year. The Group posted USD 2.1 million of net finance income, primarily due to net foreign exchange gains. Income tax expense was USD 3.2 million, compared to USD 10.7 million in 2020. Net income from continuing operations in 2021 was USD 21.5 million. The sale of a building in France formerly hosting SmarDTV, a subsidiary sold in 2018, generated a USD 1.1 million loss. Overall, the Group booked net income of USD 20.4 million, representing a USD 38.3 million improvement over 2020.

DIGITAL TV

Digital TV delivered a strong 2021, increasing net revenues by 2.8% to USD 355.1 million and EBITDA by 0.4% to USD 97.3 million, compared to 2020 results, which benefitted from a one-off credit of USD 10.0 million from pension fund accounting. In relative terms, Digital TV generated a 27.4% EBITDA margin.

Digital TV continues to benefit from positive momentum from its new product offerings, including Insight, NexGuard, TVKey, OpenTV Platform and system integration services. In 2021, the Group renewed and expanded its Insight contract with Canal+ International, with the introduction of features that measure the attractiveness and economic performance of live channels. The Group's NexGuard watermarking product maintained its momentum with Hollywood, securing an agreement to deploy NexGuard Pre-release cloud watermarking at a major studio. In addition, the Group continues to grow beyond its traditional media and entertainment target market, with the first deployment of watermarking by a global videogame platform and in law enforcement to protect sensitive witness audio content. In the sports domain, the Group maintains its momentum, working with the International Bowling Federation (IBF) to launch a gamified, content-rich loyalty application providing fans and players with a unified access point to experience every aspect of the sport.

The Group's European Digital TV business posted a strong 15.0% growth compared to 2020. Most large European customers were resilient in spite of COVID-19-related market turbulences, so notwithstanding the pandemic, the Group was able to continue growing its partnerships with large operators. For example, the Group supported the deployment of Vodafone TV in Vodafone's German affiliate and the integration of fixed operators in Germany, the Czech Republic, Hungary and Romania. At Altice, the Group extended its footprint to enable streaming and on-demand services across a broad range of open devices, including iOS and Android phones and tablets and a wide variety of smart TVs. Royalty revenues from cardless deployments, including at LGI and several accounts in Africa, were a strong growth driver in 2021, with revenues growing by USD 7.7 million over the previous year. In 2021, the Group also materially increased sales of conditional access modules (CAMs) at operators such as Tivu and Slovak Telekom.

At USD 104.9 million, the Americas business posted 15.8% lower revenues in 2021. South American markets remain weak, still suffering from the negative impacts of the pandemic. In spite of these weaknesses, the Group further strengthened its overall position in South America, with Claro, the largest operator in Brazil, deploying SSP, Nagra's connected security solution. In addition, the Group entered into a multi-year anti-piracy agreement with Claro, introducing watermarking and providing investigation, traffic monitoring and attack response services. In the US, Altice continues to expand its partnership with the Group, though compared to the previous year, overall revenues from this customer declined due to the base effect of a strong 2020. DISH Network generated lower year-on-year revenues due to the declining number of active devices and reflecting the expiry at the end of 2020 of the payment period for a batch of inactive devices.

The Asia/Pacific and Africa region recovered well in 2021, posting 9.3% year-on-year revenue growth. Among the positive highlights, the number of Starhub TV subscribers using OpenTV Video Platform, Nagra Security Services Platform and Connect Player continues to grow. In addition, sales of hybrid IPTV/OTT devices increased over the previous year. In India, the Group continued to extend its footprint, winning a mobile DRM contract with a large over-the-top provider. In the Philippines, the Group benefitted from the expansion of its cardless solution at the leading satellite operator in the country.

Digital TV margin after cost of material decreased from 88.7% to 86.1%, reflecting the higher share of hardware, including conditional access modules and IPTV/OTT devices, in the segment's revenue mix. Digital TV continued to streamline operations, further reducing operating expenses by USD 0.9 million compared to 2020. In 2020, operating expenses included a positive USD 10.0 million one-off credit related to pension fund accounting. Overall, Digital TV further improved operating income before depreciation and amortization by USD 0.4 million to USD 97.3 million. As depreciation and amortization was USD 3.6 million lower, the segment's operating income increased by USD 4.0 million to USD 76.0 million in 2021.

CYBERSECURITY

In 2021, the Group's Cybersecurity business posted USD 167.1 million of gross revenues, a 19.4% increase from 2020. Net revenues in 2021 were at USD 107.3 million, representing a growth of 25.8% over the prior year. The business benefitted from growth across both of its regions. In Europe, net revenues grew by 21.4% to USD 32.4 million, while the Americas grew by 27.8% to USD 74.9 million.

Margin after cost of material increased to USD 56.5 million, representing 16.7% growth from the previous year. In relative terms, margin after cost of material decreased from 56.7% to 52.7%, as the relatively lower gross margin technology reselling business in the US was materially higher compared to the prior year. The growth of Cybersecurity bookings underscores the positive momentum of this business. In 2021, the Cybersecurity segment generated USD 207.9 million of total bookings, growing by 16.8% compared to the prior year. Bookings in high value-added business lines, including managed security services, advisory and proprietary technology sales, continue to grow and have reached 42.2% of the total 2021 bookings. Managed Detection and Response (MDR) services, including the newly launched FusionDetect cloud-native analytics platform, were among the key drivers of growth. This offering reduces the complexity of security monitoring to deliver effective threat detection and response services across environments, including endpoint, on-premises, cloud, and OT/ICS (operational technology/industrial control systems).

In 2021, the Group accelerated its investment in the expansion of the cybersecurity business, increasing headcount in both Europe and the Americas to maintain its growth momentum. As a result, the segment's operating expenses increased by USD 8.0 million compared to the previous year. The Cybersecurity segment posted a USD 17.4 million operating loss before depreciation and amortization, an improvement of USD 0.1 million from the previous year. Operating loss decreased by USD 2.1 million to USD 20.4 million.

INTERNET OF THINGS (IoT)

In 2021, the Group's IoT business launched RecovR, a two-in-one lot management and theft recovery solution. RecovR enables car dealers to manage their lots efficiently, improve the sales process and create a new revenue stream, while offering consumers an advanced and reliable wireless theft recovery solution. Despite the semiconductor shortages affecting the industry, RecovR ramped-up deployments and established strong sales momentum in the later months of 2021, announcing multiple customer wins, including the Niello Group and Folsom Lake Ford, and growing monthly revenues at double-digit rates. As of December 2021, 43 rooftops generated RecovR revenues.

The Group also opened new distribution channels for keySTREAM, entering into new agreements with some of the world's most prominent contract manufacturers who will offer keySTREAM's security capabilities to their customers. The KeySTREAM security and device management system empowers IoT product developers to securely connect, manage and update their IoT devices and supports a wide variety of critical functionalities, including zero-touch provisioning, late provisioning, end-to-end data protection, remote feature enablement/monetization, and secure firmware updates over the air.

IoT Services continued to acquire new customers and to grow its service portfolio. As part of this portfolio, Kudelski IoT Labs offers certification services for Amazon Alexa Built-in devices, Zoom and AT&T/FirstNet.

Overall, the IoT segment generated USD 8.2 million of total revenues and other operating income, more than double the USD 3.8 million generated in 2020. The Group expanded IoT's operations to support the fast-paced growth of the business. In particular, operational expenses increased, as the business invested in the organizational structure required to successfully launch and scale its RecovR asset tracking deployments. As a result, operating loss before depreciation and amortization increased by USD 4.7 million to USD 21.2 million.

PUBLIC ACCESS

COVID-19 continued to affect Public Access results in 2021, as investments in parking installations are still slow to recover. At USD 284.1 million, 2021 segment revenues decreased by 3.7% year-on-year. European sales were 3.4% lower, reaching USD 169.9 million. Italy and the Nordics achieved the best performance in the region, growing at double-digit rates. France, on the other hand, continues to suffer from a low level of activity, resulting in a further decline of revenues from the previous year. Similarly, Austria posted lower 2021 revenues compared to the prior year. In both markets, the shutdown of the 2020/2021 ski season materially affected sales of consumable products.

Demand in the US market remains subdued, as work-from-home in large metropolitan areas in California and on the East Coast continues to affect the utilization of parking facilities. As a result, parking operators continue to postpone investments in access control infrastructure. Investment activities in Latin American markets such as Chile and Mexico also remained soft throughout the year. Overall, Public Access revenues in the Americas declined by 13.7% to USD 71.8 million, reflecting a weak first half and a more resilient second half. On the other hand, the Asia/Pacific and Africa markets strongly recovered, with revenues growing by 17.7% to USD 42.4 million. SKIDATA's Australian affiliate increased its revenue contribution by USD 4.4 million compared to the prior year.

Margin after cost of material relative to revenues further increased from 58.1% to 60.3%, reflecting a higher share of software and service in the SKIDATA business mix. The digitalization of parking infrastructure, with the associated gradual replacement of traditional ticket-based systems with fully automated free-flow solutions, contributes to the increasing weight of software and service revenues in the SKIDATA revenue mix. The COVID-19 pandemic led to a further acceleration of this trend, including in particular a faster migration to digital payment solutions.

In 2021, Public Access reduced operating expenses by USD 1.1 million compared to the previous year. The reduction of operating expenses reflects savings from headcount reduction measures as well as the results of COVID-related cost saving initiatives.

Overall, Public Access generated an operating income before depreciation and amortization of USD 17.3 million, representing USD 0.8 million improvement compared to 2020. For the full year, Public Access posted a marginally positive operating income.

SALE AND LEASEBACK TRANSACTIONS

On September 30, the Group announced the sale and leaseback of a satellite office building located in Lausanne, Switzerland for an amount of CHF 19 million.

On December 23, it announced a further sale and leaseback transaction for the properties hosting the Group's headquarters in Cheseaux, Switzerland for an amount of CHF 75 million. This transaction includes two Group office buildings in Cheseaux and the adjacent land. The investor group acquiring the headquarters' properties includes members of the Kudelski family, another longtime shareholder of the Group, the Group's Swiss pension fund and Nagravision, underscoring the commitment of the Group and of its main stakeholders in the Lausanne region.

Concurrently with the closing of these transactions, the Group entered into 15-year lease agreements for the office buildings, with two options for an additional ten-year extension. The total annual rent for the buildings amounts to USD 4.7 million. As a result of these transactions, the Group booked a total of USD 21.3 million of right-of-use assets and USD 59.2 million of lease obligations. The Group generated a USD 5.9 million gain on the sale of the building in Lausanne and a USD 7.8 million gain on the sale of the headquarters' properties in Cheseaux. The total gain on sale is booked as other operating income.

Total cash proceeds from the two transactions amounted to USD 92.8 million, net of the investment retained by Nagravision in the headquarters facilities. In addition, on January 22, 2022, the Group obtained a USD 4.1 million refund of taxes paid on the real estate transaction, which will be included in the 2022 cash flow.

BALANCE SHEET AND CASH FLOWS

Total non-current assets decreased by USD 77.9 million to USD 592.5 million. The main driver of this decrease is the sale of the Lausanne and Cheseaux facilities. In addition, the overall level of investments in tangible and intangible assets continues to be lower compared to previous years. Tangible fixed assets decreased by USD 53.8 million and intangible assets decreased by USD 18.8 million. Financial assets at amortized costs decreased by USD 9.0 million, reflecting a lower long-term portion of trade accounts receivables due to collections and reclassification to short-term receivables.

Compared to December 31, 2020, total current assets increased by USD 99.9 million to USD 632.9 million as of December 31, 2021. The USD 4.8 million decrease of inventory is mainly due to a reduction of stock levels at SKIDATA, resulting from the streamlining of this business' supply chain. The Group continues to improve collections, decreasing trade receivables by USD 21.0 million, as SKIDATA reduced outstanding receivables by USD 19.9 million. The Group reduced contract assets by USD 7.9 million to USD 36.7 million, driven by the ongoing improvements of SKIDATA's invoicing cycles. Other financial assets at amortized costs decreased by USD 4.8 million, as SKIDATA collected government grant receivables, resulting in a USD 7.3 million reduction of the amount due from state and government institutions.

At the end of 2021, cash and cash equivalents amounted to USD 284.5 million, representing USD 131.9 increase from December 31, 2020.

In December 2021, the Group disposed of a building in France, formerly hosting the headquarters of SmarDTV, a subsidiary divested in 2018. This asset was classified as held for sale in the 2020 balance sheet.

Total equity increased by USD 27.6 million, mainly reflecting USD 20.4 million of net income and USD 13.6 million of other comprehensive income, driven by a reduction of pension fund liabilities. Total non-current liabilities decreased by USD 220.6 million to USD 310.2 million, as USD 202.1 million of liabilities relating to the 2022 bond were reclassified as a short-term liability. Long-term financial debt declined by USD 242.3 million due to the aforementioned reclassification as well as the repayment of USD 8.9 million of long-term bank loans.

The Group reduced employee benefit liabilities by USD 24.1 million to USD 24.7 million. Lower pension liabilities are mainly driven by USD 19.5 million of plan asset gains, reflecting a favorable performance of pension fund investments and a USD 13.0 million favorable impact from a change of the discount rate for future liabilities from 0.1% to 0.35%. This reduction of liabilities is booked as other comprehensive income and had no impact on the Group's profit and loss statements.

Total current liabilities increased by USD 201.3 million to USD 518.6 million, with short-term financial debt increasing by USD 191.8 million to USD 240.0 million, mainly driven by the reclassification of the 2022 bond. In addition, a lower utilization of credit lines resulted in a net USD 10.4 million short-term debt reduction. Overall, the Group's primary interest-bearing liabilities include the CHF 200 million bond with a 1.875% interest rate maturing in August 2022 and the CHF 150 million bond with a 1.5% interest rate maturing in September 2024. In 2021, the Group repurchased USD 16.8 million nominal amount of the 2022 bond and USD 2.5 million of the 2024 bond.

Over the last two years, the Group significantly reduced its net debt and improved its leverage ratio (net financial debt / EBITDA). Group net debt declined from USD 392.1 million at the end of 2019, to USD 334.8 million in 2020 and USD 152.4 million at the end of 2021. The leverage ratio declined from 9.7x in 2019 to 5.2x in 2020 and 2.1x in 2021.

At the end of 2021, contract liabilities increased by USD 13.4 million, mainly reflecting a prepayment received from a Digital TV customer for services to be delivered and recognized as revenue in 2022.

In 2021, the Group generated USD 103.1 million of cash flow from operating activities. The aggregate operating cash flow of the last two years amounts to USD 235.7 million. Continued working capital improvements contributed to the Group's cash generation, including USD 29.2 million of cash flow from the reduction of accounts receivables and contract assets.

The Group generated USD 91.8 million from investing activities. The sale and leaseback transactions generated USD 92.8 million, net of the Nagravision minority investment in the headquarters' buildings. The sale of the former SmarDTV building generated USD 11.4 million of cash. The Group continues to limit capital expenditures, with a cash outflow of USD 6.5 million to purchase intangible fixed assets and USD 7.4 million for tangible fixed assets.

Net cash-out for financing activities amounted to USD 55.1 million, compared to USD 52.3 million in 2020. This cash outflow includes USD 14.8 million of payments for lease obligations, and the USD 6.1 million cash distribution paid to Kudelski SA shareholders in 2021. Net debt reimbursement in 2021 amounts to USD 33.1 million.

OUTLOOK

The Digital TV segment delivered strong 2021 results, materially exceeding expectations. For 2022, the Group expects the base effect of a strong 2021 to result in revenues stable or slightly declining at single-digit rates. Operating expenditures are expected to marginally grow compared to 2021, due to investments in Digital TV growth initiatives. These developments reflect the base effect of exceptional 2021 results and will translate in a year-on-year reduction of the segment's EBITDA.

In the Cybersecurity segment, the Group expects to maintain its 2021 momentum, with revenues growing at double-digit rates. As the Cybersecurity business continues to drive the development of higher margin product lines, margin after cost of material should also grow at a double-digit rate. After the material build-up of operating expenses in 2021, OPEX growth is expected to slow down in 2022, resulting in a material improvement of segment profitability.

The strong momentum of RecovR sales is expected to drive IoT's revenues in 2022, while the Group will continue to promote IoT Services and the keySTREAM platform as a driver of long-term growth. Consistent with 2021, the Group expects IoT revenues to at least double in 2022 compared to the prior year. 2022 gross margins will decline, as the revenue mix will increasingly shift to the asset tracking business line. With operating expenses only marginally increasing compared to 2021, revenue growth is expected to translate to a lower EBITDA loss in 2022.

The Public Access business will continue to face uncertainties related to the COVID-19 impact on airports, shopping centers, stadiums and ski resorts, for at least the first half of the year. Planning for 2022 takes these uncertainties into account. The Group forecasts a partial recovery with mid-single digit revenue growth for Public Access, with a limited increase of operating expenses. In 2022, the Group expects to benefit from the streamlining of SKIDATA's operations and a tighter integration with other Group businesses, targeting a material improvement of Public Access profitability.