

## 2015 RESULTS

### Management Discussion & Analysis

In 2015, the Kudelski Group achieved double digit growth of consolidated revenues and operating income in spite of major exchange rate volatility. Foreign exchange movements had an overall negative effect of CHF 28.5 million on revenues, while the overall impact on operating income was slightly positive, as the average EUR/CHF rate declined from 1.2145 to 1.0684 and the USD/CHF rate went from 0.9155 to 0.9627.

Operationally, the Group expanded its distribution capabilities in the Public Access segment and continued to optimize its Integrated Digital TV (iDTV) activities.

In Public Access, the Group acquired 60% of Sentry Control Systems, SKIDATA's largest distributor in the United States, for CHF 14.0 million with an option to acquire the remaining 40% share for an additional CHF 9.9 million of deferred and contingent consideration. SKIDATA also acquired Don Harstad, a smaller distributor in the Midwestern region of the United States, for CHF 0.5 million. In addition, SKIDATA purchased for a nominal amount the intellectual property portfolio of 3M's parking business, gaining privileged access to an installed base of close to 10'000 former 3M parking customers. Finally, following the acquisition of a 50% stake in October 2014, SKIDATA assumed operational control of its Australian distributor, now renamed SKIDATA Australasia Pty Ltd, at the beginning of the year and maintains an option to acquire the remaining shares in this entity. With these acquisitions, SKIDATA significantly expanded its presence outside its traditional European markets, increasing its non-European revenue base by CHF 47.1 million to CHF 115.7 million to become a worldwide leader in the off-street parking business.

In iDTV, the Group's SmarDTV subsidiary merged with EchoStar's European set-top box operations. SmarDTV completed the acquisition of such entities for CHF 0.5 million, thereby extending the Group's set-top box portfolio with a feature-rich set of gateways and set-top boxes and gaining access to a next-generation chipset platform. As the identifiable net assets acquired exceed the consideration paid to EchoStar, this transaction qualifies as a bargain purchase for accounting purposes. Hence, a CHF 4.1 million gain was booked as other operating income. Concurrently with this acquisition, the Group sold 22.5% of SmarDTV's equity and debt to EchoStar for a total cash consideration of CHF 12.7 million.

Finally, the Group continued its positive momentum in the field of intellectual property licensing, signing patent license agreements with Netflix, Google, Disney, Bloomberg and a European broadcaster, resulting in a positive contribution to 2015 revenues and operating income.

Overall, 2015 Group revenues in constant currency increased by 11.1% over the previous year, primarily driven by the 31.2% constant currency growth of the Public Access segment. iDTV constant currency revenues were 3.9% higher compared to the previous year. Reported revenues increased by 7.8% to CHF 939.6 million.

The Group reported operating income of CHF 81.2 million in 2015, representing growth of 32.7%. Net income improved by 47.6% to CHF 49.3 million in 2015, as compared to CHF 33.4 million in the prior year.

### CHANGE IN ACCOUNTING POLICIES

In 2015, the Group retrospectively adopted an amendment to IAS 19R – 'Defined Benefit Plans: Employee Contributions.' The amendment allows contributions that are linked to service and do not vary with length of employee service to be deducted from the cost of benefits earned in the period

in which the service is provided (e.g. contributions dependent on the employee's age or contributions representing a fixed percentage of the employee's salary). The Group elected to apply this amendment as it improves the accuracy of estimated pension commitments. As a result, 2015 employee benefits liabilities decreased by CHF 17.6 million, while deferred tax assets decreased by CHF 3.9 million. The impact on the consolidated income statement is minor.

The accounting treatment of foreign exchange differences was revised to consider all exchange differences in connection with subsequent measurements and settlements of debtors and suppliers as part of finance income/expense. In the past, the Group recognized exchange differences related to debtors and suppliers as part of revenue and cost of material, licenses and services. As a result of this change, revenues increased by CHF 1.9 million in 2015, while cost of material decreased by CHF 1.4 million. Reported operating income is therefore CHF 3.3 million higher, while other finance income decreased by the same amount.

Note 37 of the financial report provides further details on the impact of these changes in accounting policies.

## **GROUP REVENUES AND PROFITABILITY**

Total revenues and other operating income in 2015 increased by CHF 64.1 million to CHF 950.8 million. Revenues grew by CHF 68.2 million, while other operating income declined by CHF 4.1 million, due on the one hand to the CHF 4.1 million gain from the acquisition of EchoStar's European set-top box operations and on the other hand to a decrease of CHF 5.0 million in government grants (mainly French "Crédit d'Impôt Recherche").

"Margin after cost of material" (a pro-forma, non-IFRS item) increased by CHF 15.4 million to CHF 664.1 million. Relative to total revenues, margin after cost of material decreased from 73.2% to 69.8%, reverting close to the level seen in 2013. The main driver of this margin reduction relates to a shift of the revenue mix from relatively higher margin iDTV revenues to Public Access revenues. Public Access accounted for 29.3% of total revenues and other operating income in 2015 compared to 26.1% in 2014.

Personnel expenses increased by CHF 12.4 million to CHF 393.0 million, as the Group consolidated the additional operating expenses of its newly acquired subsidiaries. Total Group headcount at year end was 3'459 full time equivalents compared to 3'034 at the end of 2014. SKIDATA was the primary driver of this headcount increase, accounting for most of the additional 155 employees in the United States (mainly from the Sentry acquisition) and the additional 61 employees from SKIDATA Australasia. The integration into SmarDTV of the newly acquired operations from EchoStar was the main driver of the Group's headcount expansion in the United Kingdom by 108. In Switzerland, the Group marginally decreased overall headcount by 8 employees. Finally, the Group continued to expand its Indian operations, adding another 82 employees in 2015.

Compared to 2014, the Group reduced other external operating expenses in 2015 by CHF 15.2 million to CHF 148.6 million. Development and engineering expenses were CHF 4.3 million lower, with currency effects as the key driver of this cost reduction. In 2015, the Group released net provisions of CHF 4.0 million compared to the additional net provisions of CHF 9.3 million in 2014, as collection of outstanding receivables in the iDTV segment exceeded expectations.

The Group's operating income before depreciation and amortization was CHF 122.6 million in 2015, a CHF 18.2 million increase from the previous year. At CHF 41.3 million, depreciation, amortization and impairment were CHF 1.9 million lower than in 2014, reflecting the reduced levels of capital expenditures over the last four years and in spite of the additional amortization costs related to the acquisitions made by the Group in 2015 as well as the 2014 acquisition of Conax.

Overall, the Group generated operating income of CHF 81.2 million in 2015, representing a 32.7% improvement compared to 2014.

At CHF 14.5 million, interest expense increased by CHF 3.1 million over the previous year, as the Group fully amortized transaction costs related to the syndicated credit facility entered in connection with the Conax acquisition, which was fully repaid in the first half. The Group posted CHF 9.3 million of net finance expenses, primarily due to the negative foreign exchange effects from the declining EUR/CHF rates. Income tax expense decreased by CHF 3.3 million to CHF 9.8 million. Overall, the Group improved net income by CHF 15.9 million to CHF 49.3 million.

## **INTEGRATED DIGITAL TV**

Reported iDTV revenues increased by 3.2% to CHF 661.1 million, representing constant currency growth of 3.9%.

The Group's European iDTV business posted constant currency growth of 13.1%. In Italy, strong adoption of SmarDTV's new WiFi CAM resulted in solid year-on-year growth. In Spain, the Group benefitted from Telefonica's migration of its multiscreen users onto the MediaLive-powered "Yomvi by Movistar+" platform. Through the addition of Conax, the Group also gained an important presence in the Scandinavian region and further expanded its Eastern European footprint.

Constant currency revenues in the Americas region declined by 6.8% compared to the previous year. Resilient business from North American digital TV customers as well as the revenue contributions from the patent license agreements with Netflix, Google, Disney and Bloomberg supported the region's results. Brazil slowed down in the second half, while other South American markets, including in particular Peru, experienced positive momentum.

The Asia/Pacific and Africa region posted constant currency growth of 9.2%. Digitization of the Indian cable market renewed its momentum in the second half of 2015. In addition to the three major national MSOs (multiple-system operators) already deploying Nagra technology, five new regional Indian MSOs have selected the Group's solutions. In China and Taiwan, Beijing Cable, Shandong Cable, Guangdong Cable, TBC and KBRO are the primary drivers of the Group's growth in these markets, due to the digitization of their networks and the deployment of OpenTV5 and MediaLive.

Overall, operating income from the iDTV segment improved by 28.9%, reaching CHF 83.3 million in 2015. Resilient revenues and a double digit million reduction of operating expenses resulted in solid performance of the Group's core digital TV business. Five new patent license agreements also contributed to segment profitability and reflect the continued momentum of the Group's intellectual property licensing activities with key industry players. The iDTV segment also benefitted from the consolidation of Conax for the full year, compared to consolidation of only three quarters of results in the previous year. Conax's business was highly resilient in 2015 with new contract wins in Asia and Africa. While on the right track to expand for the future, the cybersecurity business is still in an early stage of development, generating low revenues and an operating loss in 2015.

## **PUBLIC ACCESS**

Following a strong first half of 2015, SKIDATA's growth further accelerated in the second half, resulting in year-on-year constant currency revenue growth of 31.2%. Reported revenues increased by 20.6% to CHF 278.5 million. The full consolidation of newly acquired Sentry and SKIDATA Australasia, together with the entry into new markets such as Latvia, Botswana, Guatemala, Panama and Paraguay, set the foundation for the continued growth of the SKIDATA's business.

SKIDATA's European business developed favorably in the second half of 2015. Year-on-year constant currency growth in revenues for the European region was at 12.1%. Among the positive highlights, the Austrian, German and UK markets posted solid revenue growth.

In the Americas, constant currency revenues increased by 99.1% in 2015. Reported revenues for the region were at CHF 66.1 million compared to CHF 32.3 million in 2014. The first time consolidation of the newly acquired Sentry business was the main factor underlying the high growth rate of this region. With the integration of Sentry, SKIDATA has considerably strengthened its service organization in the parking segment for the US market, establishing a solid foundation to further grow top line results from this region.

Constant currency revenues for Asia/Pacific and Africa grew by 55.9%. Reported revenues for the region were at CHF 49.6 million compared to CHF 36.3 million in 2014. This growth reflects the consolidation of SKIDATA Australasia, the newly acquired parking subsidiary. As a result of this acquisition, Australia is now the second largest market for SKIDATA after the United States.

Following a weak first half, Public Access operating income recovered in the second half of 2015, reaching CHF 15.7 million for the full year, an increase of 4.4% from the previous year.

## **BALANCE SHEET AND CASH FLOW**

Total non-current assets decreased by CHF 18.5 million to CHF 599.3 million at the end of 2015, with tangible fixed assets increasing by CHF 6.0 million and intangible fixed assets decreasing by CHF 19.4 million. The first time consolidation of the Group's newly acquired entities added CHF 30.5 million to tangible and intangible assets, including CHF 18.4 million of goodwill, while foreign exchange effects resulted in a CHF 35.2 million decrease. The CHF 8.1 million reduction of financial assets and other non-current assets was primarily driven by a reduction of long-term deferred contract costs. The Group's continuing tight control over capital expenditures was a further driver of the reduction of non-current assets.

Total current assets increased by CHF 60.1 million to CHF 490.2 million in 2015. The CHF 1.0 million increase of inventory reflects a CHF 6.7 million increase at SKIDATA and lower inventory levels at Nagravision and SmarDTV. Trade accounts receivable increased by CHF 37.0 million to CHF 257.0 million, as the Group generated significant revenues during the last quarter of 2015. SKIDATA, in particular, ended the year with total net receivables that was CHF 31.9 million higher than at the end of 2014, as seasonality effects were even more pronounced in 2015 than in previous years. Other current assets decreased by CHF 22.7 million, mainly reflecting a CHF 15.1 million reduction in amounts due from government grant programs. The Group managed to reduce this item, as it collected outstanding government grants and only recognized net new grants of CHF 3.4 million, compared to CHF 8.7 million in the previous year. At the end of 2015, cash and cash equivalents amounted to CHF 136.8 million, a CHF 44.5 million increase from the end of 2014.

Total equity declined by CHF 6.4 million, as the Group generated CHF 49.3 million of net income, distributed a dividend of CHF 16.2 million and booked a negative CHF 34.0 million currency translation adjustment and a positive CHF 9.2 million effect from the SmarDTV and the SKIDATA Australasia transactions.

Total non-current liabilities decreased by CHF 21.0 million, while total current liabilities increased by CHF 69.1 million. These changes mainly reflect the CHF 55.6 million decrease of long-term financial debt and CHF 47.7 million increase of short-term financial debt. On May 12, 2015, the Group issued a new CHF 200 million bond with a 1.875% interest rate and maturity of 7 years and 3 months. With the proceeds of this bond, the Group fully repaid the remaining CHF 165 million credit facility obtained in 2014 to finance the acquisition of Conax. Following the repurchasing of CHF 7.0 million in 2015, the outstanding CHF 102.8 million of the CHF 110 million bond due in December 2016 was reclassified from long-term to short-term financial debt.

Employee benefits liabilities increased by CHF 18.9 million to CHF 77.8 million, of which CHF 10.1 million were due to changes in financial assumptions (discount rate). Other long-term liabilities and derivative financial instruments increased by CHF 17.7 million to CHF 21.0 million. With its acquisition of 22.5% of SmarDTV's equity, EchoStar also acquired the same percentage of the

company's CHF 30 million debt, resulting in a CHF 6.75 million liability. A CHF 7.3 million increase of deferred/contingent consideration relates to the estimated future payments for the acquisition of the minority interest in Sentry. A CHF 10.8 million higher deferred income linked to a large iDTV project to be delivered in the first half of 2016 is the main driver for the CHF 14.9 million increase of other current liabilities.

In 2015, the Group generated CHF 106.4 million of cash from operating activities, representing a decrease of CHF 2.9 million as compared to cash flows generated in 2014. Change in working capital is the primary driver of this decrease, with a drop from CHF 7.1 million in 2014 to CHF –6.1 million in 2015, which corresponds to a year-on-year reduction of CHF 13.2 million. SKIDATA materially expanded its working capital, with a CHF 38.7 million increase in 2015, in line with the accelerated growth momentum of the last 12 months.

The Group used CHF 45.5 million of cash for investing activities. Cash used for purchasing tangible and intangible assets represented CHF 32.6 million, while cash used for the acquisition of subsidiaries was CHF 12.1 million.

Cash out for financing activities amounted to CHF 12.3 million. This includes CHF 199.1 million net proceeds from the new bond and the CHF 165.0 million repayment of the credit facility established in 2014 for the acquisition of Conax. In 2015, Kudelski SA paid a dividend of CHF 16.2 million. Cash from financing activities includes CHF 12.7 million proceeds received for the sale of 22.5% of SmarDTV. Overall, changes in foreign exchange rates had a CHF –4.2 million effect on cash and cash equivalents during 2015.

## **OUTLOOK**

In 2016, the Group expects to maintain the positive momentum from the previous year.

In the core digital TV business, the Group expects to benefit from the solid momentum of key Asian markets, where the Group has established a strong competitive position. In Europe and the Americas, particularly in South America, market conditions are expected to be less favorable this year. As IP licensing activities have established a robust track record in the past two years, the Group expects to benefit from further agreements in 2016. Overall, iDTV business resilience is expected to be sustained in 2016, resulting in a growing revenue base.

In the Public Access segment, the Group will complete the integration of its newly acquired entities, with the aim to maintain the growth trajectory of the last few years and materially improve cash generation. Following a year with a particularly strong seasonality, the Group is implementing measures to mitigate the impact of year-end seasonality effects on revenue and profit generation by the Public Access segment.