

Schlatter Group posts lower net revenue and profit

The Schlatter Group suffered a decline in both net sales and profit in the 2019 financial year. Economic sentiment in the Schlatter markets was marked by uncertainties, making our customers extremely reluctant to place orders. The Welding segment benefited from a good order backlog in the first half of the year, but the decline in orders made it impossible to maintain its good capacity utilisation in the second half. Even so, the Welding segment posted a substantial operating profit. In contrast, the Weaving segment suffered a significant loss due to low capacity utilisation. At the end of the year, the outlook in both segments' individual markets brightened somewhat. Given the order backlog as of 31.12.2019 and uncertainty about order intake, the Board of Directors and management expect lower revenues for the current financial year. However, they are striving to achieve at least a break-even result, excluding the corona effect. Should the measures taken worldwide to combat the corona virus last longer, this could have a negative impact on the 2020 financial statements.

Dear shareholder

In the 2019 financial year, the Schlatter Group generated net sales of CHF 93.6 million (2018: CHF 111.5 million) and an order intake to the value of CHF 74.8 million (2018: CHF 114.2 million). The order backlog on 31.12.2019 stood at CHF 26.4 million (31.12.2018: CHF 45.2 million). The operating result (EBIT) for the period under review was positive at CHF 1.0 million (2018: CHF 3.8 million). With a consolidated net result of CHF 0.5 million (2018: CHF 3.7 million), the Group ended the 2019 financial year with a profit that was substantially below the prior year's result.

Markets

Systems for the manufacture of reinforcing mesh

2019 was marked by a worldwide reluctance to place orders for reinforcing mesh systems. Schlatter's largest product area was faced with the biggest drop in orders in our entire product

range. Our customers' production performance remained at a high level, however, which had a positive impact on our after-sales activities.

The predicted decline in orders in Europe, our most important market, was much sharper than expected. Mesh producers had significantly expanded their capacities in prior years, and most of the large industrial groups that dominate the European market have completed the modernisation of their production facilities. Economic uncertainty, furthermore, led to a substantial decline in capital investment in the markets relevant to Schlatter. Reinforcing mesh production is under pressure from single-rod reinforcement and precast concrete elements.

Demand picked up at the end of the year in several eastern European countries where there had been little investment in past years.

Mesh producers throughout Asia are reluctant to invest. In China reinforcing mesh systems from Schlatter are more or less ruled out on grounds of price. In addition, the market is strongly influenced by single-rod reinforcements – and increasingly by precast concrete elements.

In numerous emerging markets, a growing requirement for high-performance machines for standardised reinforcing mesh is stimulating demand.

Systems for the manufacture of industrial mesh

The continuing development of the MG950 industrial mesh product family and the range of products for the manufacture of reinforcing mesh, which has expanded in past years, constitute a stable foundation for Schlatter's business. There was also a significant decline in orders in the industrial mesh field in the year under review. Europe and the USA are among the most important markets for industrial mesh.

There is growth potential in the area of systems for the production of mesh fences, and also in automated solutions for customers' entire production processes.

Despite the decline in orders in 2019, we believe the industrial mesh area has growth prospects.

Rail welding

Sales of stationary rail welding systems in the year under review were unsatisfactory. One reason for the decline is that the expansion of capacities for welding high-speed track in China has led to saturation. But new opportunities are presenting themselves in other regions, where governments have already given the go-ahead for numerous major new railway line construction projects.

The market for mobile rail welding systems remains sluggish. Schlatter systems are mainly designed for the western European market, where there are currently no new construction projects in the pipeline.

Systems for the manufacture of paper machine clothing and wire netting

Paper production was stable at a good level in 2019. It is posting worldwide growth of around 1-2 percent. The market for printing paper and newsprint is declining, whereas the brown paper and tissue area is growing. Moreover, paper production is benefiting from critical attitudes to plastic packaging.

Our customers' capacities for the production of paper machine clothing are well utilised. There has been a significant improvement in the quality of weaves, which can thus be used for longer – more or less eliminating any volume increase. With competition becoming stiffer, prices per square metre of weave are falling continuously, forcing our customers to reduce their production costs and replace their machinery. Weave quality is also a critical success factor for efficient, low-cost paper production.

Trade conflicts and the ensuing uncertainties have resulted in significant delays to investment decisions, making 2019 a difficult year for the Weaving segment. However, we are currently noting an improvement in our customers' propensity to invest and see good prospects of securing major projects in the first quarter of 2020.

The Wire Weaving systems area has potential, especially in fields of application such as security grilles, sieving and mosquito grilles. Determined to improve its marketing in this product area, Schlatter has reorganised its sales organisation effective 1 January 2020.

Spare parts and service

Our customers' good capacity utilisation and the introduction of new Schlatter services have helped to ensure that – despite a sharp decline in orders in plant business in all product areas – net sales from spare parts and services could be kept stable.

Product development

The Schlatter Group invested a total of CHF 5.6 million in product development in the 2019 financial year (2018: CHF 4.9 million). Sums of a similar magnitude will be invested in the further development of our products in the 2020 financial year.

In the Welding segment, the innovation focus is on the product area of systems for the production of reinforcing and industrial mesh. The development of the machine platform has made good progress. Initial platform modules are currently being installed for customers to field-test certain applications. This project's objective is to cut product costs significantly, and to achieve a substantial reduction in the complexity due to the breadth of the product portfolio. With its medium- to long-term targets, this project is designed to achieve lasting competitive advantages for the wire product area.

We continue to focus on the refinement of the MG950 industrial mesh generation and the expansion of the MG800 systems family in the reinforcing mesh area. The MG800 systems family, known for its high production output, flexibility and short retooling times, will be supplemented with a lower-cost variant in the lower output range.

The "Industry 4.0" project involving the digitalisation of our systems was continued. The first projects, focusing on greater customer benefits, have been implemented. These include data backup solutions for customers, digitalised machine set-up aids for industrial mesh systems, and a dashboard that is in the course of implementation. One important point will be the renewal of our machine control and operating software: the existing machine control software has reached its limits in terms of performance and complexity, and the replacement of the existing operating software will make our systems easier to operate and boost their availability.

Our Münster site is developing a weaving machine for technical weaves with other applications for growing markets. This is designed to reduce dependence on the volatile paper machine clothing market and take us into growth markets.

New site in Münster completed on schedule

The new site in Münster is due for completion on schedule in the first quarter of 2020 so that it is ready for occupation in the second quarter. The new-build plant enables us to formulate optimum corporate processes, ultimately leading to an increase in productivity.

Welding segment

Net sales in the Welding segment in the 2019 financial year totalled CHF 77.3 million (2018: CHF 91.8 million). At CHF 61.3 million, order intake was significantly down on the previous year's figure of CHF 94.8 million. The order backlog at the year-end stood at CHF 21.5 million (31.12.2018: CHF 37.5 million).

In the light of the decline in new orders in the period under review and the resulting poorer net revenue prospects for the 2020 financial year, Schlatter initiated a comprehensive cost-cutting programme in the Welding segment to avoid impending losses. Implemented in the last quarter of 2019, the measures will bear fruit in the 2020 financial year.

In spite of the current market weakness, the action taken in past years to increase productivity, along with heavy investment in new product development and measures to strengthen our presence in the market, make us confident about the future. With the development of a new machine platform for reinforcing and industrial mesh production systems, Schlatter will reduce the complexity of its systems and deliver lasting reductions in product costs.

Systems for the manufacture of reinforcing mesh

The wire product area, Schlatter's most lucrative, was hit hardest by the decline in orders as economic uncertainties persuaded numerous customers to postpone investment decisions. We expect a moderate recovery, but revenues are still likely to be lower in the current financial year than they were in the past.

The MG800 machine, a flexible, high-performance concept for the manufacture of reinforcing mesh in small batch sizes, generated project cost overruns in the previous year that had a negative impact on earnings. These were eliminated in the period under review.

The machine platform's initial configuration, relating to an application in the field of reinforcing mesh, was field-tested on a customer's premises early in 2020. Product development focuses on flexible systems in the mid-range price segment, where Schlatter has expansion potential.

Systems for the manufacture of industrial mesh

The flexible, productive MG950 industrial mesh product family was extended by applications taking it in the direction of a sector solution. Development work is focused on integrated system solutions for the manufacture of end products. These manufacturing concepts integrate machines and systems whose functions extend beyond pure mesh production.

One application within industrial mesh production is systems for the manufacture of mesh fences. In tandem with the development of the machine platform, a new product generation of mesh fences will be created in the next few years that will meet customer requirements even better.

During the last two years Schlatter has developed wider machines that weld larger-diameter wires. This enables our systems to manufacture other products that will give our customers new market opportunities.

Rail welding product area

Thanks to our strong position in the global market for stationary rail welding systems, Schlatter handled an unusually large number of projects in 2019 – especially in the first half. Orders declined sharply in the second half, but new market potential will open up in India from 2020.

Competition in the mobile rail welding field has intensified, as major groups active in all areas of track superstructure have expanded their product portfolios into this market. Our mobile rail welding systems focus strongly on markets in Western Europe – but as these are building hardly any new tracks, sales have been declining. Schlatter's mobile welding systems are less competitive in emerging markets because of cost pressure from the competition.

Welding segment outlook

With the current order backlog, existing capacities in the Welding segment are under-utilised. Schlatter has therefore selectively reduced capacities in the context of cost-cutting measures. As well as action to increase productivity and reduce production costs, other measures that will produce effects in the medium term have priority. Schlatter continues to invest selectively in product development and in opening up new markets. Despite the current market weakness, this investment programme is not being curtailed. We also continue to work on the expansion of our after-sales services.

The Welding segment has got off to a good start in the new year, but the challenge of achieving a satisfactory operating result in the 2020 financial year remains daunting.

Weaving segment

At CHF 13.5 million, order intake in the Weaving segment was down on the previous year (2018: CHF 19.4 million). Net sales in the year under review stood at CHF 16.4 million (2018: CHF 19.6 million). The order backlog as at 31.12.2019 stood at CHF 4.9 million (31.12.2018: CHF 7.7 million).

The Münster site suffered a substantial loss in the Weaving segment, due partly to lower net revenues and partly to cost and productivity problems, which must be addressed as a top priority. Comprehensive measures have been initiated to increase productivity. One prominent example of increased productivity is shop floor management in manufacturing and assembly, which has already increased efficiency substantially.

The Münster site has also reduced its capacities and initiated cost-cutting measures in the Weaving segment. The objective is to reduce the site's profit threshold by 20 percent. In

addition, a service initiative has been launched to increase both customer satisfaction and net revenues.

Development of new business fields in the technical textiles area

The volatile market for weaving machines for the production of paper machine clothing is leading to sharp fluctuations in capacity utilisation at the Münster site. A product development project launched in 2019 will enable us to enter growth markets for the production of other technical weaves, reducing Schlatter's dependence on the volatile market for weaving machines for the production of paper machine clothing and generating growth. Important milestones were reached in the year under review, giving us confidence that a prototype will be in operation at a customer's facility by the end of the 2020 financial year. The focus is currently on developing a machine platform and achieving target product costs.

Paper machine clothing area

In the paper machine clothing area we shall concentrate on reducing the production costs of our machines in the 2020 financial year.

Weaving segment outlook

The Schlatter Group believes the market will be in a rather improved overall state in the new financial year. Capacities at the Münster site are still under-utilised. The overriding objective is to eliminate losses and significantly improve Operational Excellence in various corporate areas. Our aim for the Weaving segment in the 2020 financial year is a break-even result.

Thanks

The Schlatter Group has posted continual growth in revenue in recent years, achieving major increases in EBIT and consolidated earnings. The decline in orders in the year under review and the loss at the Münster site are disappointing, however. Short-term measures made necessary by the decline in sales have been implemented, and long-term measures are being consistently pursued. On behalf of the Board of Directors and management, we express our gratitude to you, our shareholders, for the confidence you place in Schlatter and in our work.

We look forward to welcoming you to the General Meeting here in Schlieren on 4 May 2020 and answering any questions you may have. You can download the full 2019 Annual Report from our website at www.schlattergroup.com, or order it using the attached form.

Outlook

The Schlatter Group benefited from the positive sentiment in the markets in the three years before 2019. We successfully launched product innovations, intensified our marketing activities in regions where we had previously been under-represented, and significantly expanded our service business.

The decline in our net sales and overall result in the 2019 financial year presents us with challenges that we are actively addressing – with comprehensive cost-cutting measures affecting both segments, for example, by reducing capacities at our largest sites, and with measures to increase productivity that are already in the course of implementation.

The medium-term measures are being consistently pursued – among them higher-than-average investment in product development and intensive marketing, both of which will help to strengthen our market position.

Despite the currently unsatisfactory state of the market, the Schlatter Group has numerous competitive advantages. Given the order backlog as of 31.12.2019 and uncertainty about order intake, the Board of Directors and management expect lower revenues for the current financial year. However, they are striving to achieve at least a break-even result, excluding the corona effect. Should the measures taken worldwide to combat the corona virus last longer, this could have a negative impact on the 2020 financial statements.

At the General Meeting on 4 May 2020 the Board of Directors will propose that no dividend be paid for the 2019 financial year.

Schlieren, March 17, 2020



Paul Zumbühl
Chairman of the Board of Directors



Werner Schmidli
Chief Executive Officer

Key figures of the Schlatter Group

		2019	2018
Net sales	CHF million	93.6	111.5
Change compared to previous year	%	-16.0	10.2
Operating result (EBIT)	CHF million	1.0	3.8
in % of net sales	%	1.0	3.4
Net result	CHF million	0.5	3.7
in % of net sales	%	0.5	3.3
Order intake	CHF million	74.8	114.2
Order backlog	CHF million	26.4	45.2
Headcount at period end	FTEs	344	373
Average headcount	FTEs	362	357
Interest-bearing liabilities	CHF million	9.0	1.1
Net financial position (debt)¹	CHF million	-5.5	12.4
Gearing²	%	18.8	0.0
Free cash flow³	CHF million	-17.9	2.2
Current assets	CHF million	39.7	51.4
Non-current assets	CHF million	18.6	7.3
Liabilities	CHF million	29.0	29.8
Equity	CHF million	29.3	28.9
Equity ratio	%	50.2	49.2
Return on equity (ROE)⁴	%	1.8	13.7
Key share figures			
Share capital as of December 31	CHF 1,000	17,675	17,675
Total registered shares	No.	1,104,704	1,104,704
Registered shares entitled to dividend payments	No.	1,104,704	1,104,704
Net result per registered share ⁵	CHF	0.46	3.37
Equity per registered share ⁵	CHF	26.49	26.16
Dividend per registered share	CHF	0 ⁶	0
Payout ratio	%	0 ⁶	0
Share price development			
High	CHF	46.80	50.50
Low	CHF	31.20	32.40
Year-end	CHF	35.80	32.40
Market capitalization			
High	CHF million	51.7	55.8
Low	CHF million	34.5	35.8
Year-end	CHF million	39.5	35.8

¹ Net financial position (debt): cash and cash equivalents less interest-bearing liabilities

² Gearing: net financial position divided by equity

³ Cash flow from operating activities less purchase of tangible fixed assets and intangible assets, plus sale of tangible fixed assets and intangible assets

⁴ Net result divided by average equity

⁵ Determined on the basis of dividend-entitled shares

⁶ In accordance to the proposal to the Annual General Meeting of May 4, 2020

2019 Annual Report of Schlatter Industries AG

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