Management report

In dynamic market environment

In a dynamic market environment characterized by high demand, supply chain bottlenecks and the ongoing COVID-19 pandemic, SFS seized opportunities that arose in each of its segments to boost its sales by 11.0% to CHF 1,893.1 million, an outcome based on its ability to fill customer orders. All end markets and regions contributed to this good growth. The result was a high level of production capacity utilization that strengthened profitability and generated a strong EBIT margin of 15.9%.

Heinrich Spoerry

Jens Breu

Dear shareholders,

2021 was a highly eventful year for the SFS Group and the COVID-19 pandemic continued to be the defining theme. The market environment had already begun showing signs of recovery in the third quarter of 2020 and this recovery persisted throughout the first half of 2021 for year-over-year growth of 23.8%. While the summer brought some relaxation and an easing of the strict pandemic measures, the next wave of the virus hit hard in the fall and case numbers shot up. Production slowdowns, another consequence of the COVID-19 pandemic, triggered global supply chain disruptions as well as shortages of semiconductors and other raw materials, some of which also had an impact on call-offs at SFS. Despite sales declining slightly by 2.3% in the second half of 2021 compared to the first half of 2021, total sales compared to the previous year increased substantially by 11.0% to CHF 1,893.1 million. Consolidation effects contributed 0.8% to full-year sales, while foreign currencies only had a slightly negative effect of –0.1%. As a result, sales in the year under review clearly exceeded the 2019 figures (CHF 1,781.4 million) and confirmed SFS's good positioning throughout the cycle.

Shaping the future through high flexibility and solidarity
Unlike in 2020, when the development of the automotive industry, in particular, was heavily impacted by the pandemic, our markets were subject to fewer COVID-19 restrictions in 2021. This was quite beneficial in terms of general demand. Protecting employees' health while simultaneously ensuring our ability to fill customer orders at high capacity utilization called for a great degree of flexibility and solidarity from all employees. In this challenging situation, SFS even succeeded in making some important headway with respect to its future positioning:

- The divisions' strong competitive edge enabled them to acquire important new projects, gain market share and win over new customers, which in turn lay the foundation for future growth. One lighthouse project is a major order acquired at the Heerbrugg (Switzerland) location that relates to precision components for a new generation of electric brake systems; this order will generate total sales in excess of CHF 100 million from 2024–2033.
- The Riveting division's relocation of its Chinese production facility from Nansha to Nantong, the production platform also used by other divisions, was concluded with flying colors.
- Our efforts to develop and adopt our Enviromental Roadmap take us one important step closer to reaching our goal of being able to continuously reduce emissions on the basis of measurable targets. In specific terms, this means that SFS is aiming to reduce its internal CO_2 emissions by ≥90% by 2030, compared to 2020, measured in terms of tons of CO_2 per CHF of added value.
- Together with Hoffmann, the SFS Group gains an internationally strong position in the attractive area of quality tools. The two companies have been collaborating successfully for many years and have a great deal of common ground with respect to their value proposition and values. Both companies are positioned as leading providers in their industries. The joining of forces marks a milestone and opens up attractive development opportunities for both companies.

Profitability increased through high capacity utilization
Strong yet occasionally volatile market demand led to good overall utilization of production capacities. Phases of high utilization as well as targeted, forward-looking cost management resulted in a record-high operating profit (EBIT) of CHF 301.7 million and an EBIT margin of 15.9% of net sales (PY 13.3%). At CHF 248.0 million (PY CHF 184.8 million), net income corresponds to 13.1% of net sales.

The positive development of the operating profitability resulted in a Return on Capital Employed (ROCE) of 26.1%. The equity ratio was further improved to 78.9%.

Expertise and skills preserved
The SFS Group had 10,509 employees (full-time equivalents) at the end of 2021 (PY 10,692). This largely stable development is an expression of the long-term "local for local" strategy with robust, efficient supply chains as well as the decision to nearly exclusively make temporary adjustments to production capacities during the now two-year pandemic. Doing so enabled SFS to largely maintain its ability to fill customer orders despite challenges presented by material availability and occasionally long delivery times and benefit from the dynamic market conditions that prevailed during the period under review.

Engineered Components (EC)

Characterized by pent-up demand in automotive-related areas and industrial sectors

The EC segment, which is geared toward industrial applications, benefited substantially from the recovery that began in the wake of the COVID-related slump of the 2020 financial year. This recovery followed different patterns depending on the end market. In the Automotive industry, the good development of the first half of 2021 was slowed down with beginning of the summer months by bottlenecks in the semiconductor supply chain. While the development in the various industrial niche markets served by the Industrial division exhibited a similar pattern, it was delayed and withouth a material impact from supply chain bottlenecks. The Aircraft business lingered at a low level but started showing initial signs of a recovery toward the end of the year. The Electronics division profited from a persistently positive market environment that was, however, also hit by semiconductor scarcity in the second half. Demand in the Medical division followed an upward trend.

Overall, the segment generated sales of CHF 975.2 million, representing growth of 8.6% compared to the same period of the previous year. In addition to our customers' supply chain bottlenecks mentioned above, the strong baseline effect is another factor that contributed to the declining growth rate during the second half of the year. Sales growth was almost exclusively organic in nature; foreign currency and consolidation effects only had minor impacts of –0.5% and +1.2%, respectively.

The good demand situation resulted in a high overall level of capacity utilization that was beneficial for the EC segment's profitability. The EBIT margin rose by 160 basis points and amounts to 17.1% for the 2021 financial year, which is on a par with the pre-COVID level. Supply chain bottlenecks resulted in a lower utilization of capacities during the second half of 2021, which then caused the EBIT margin to contract slightly.

Fastening Systems (FS)

Dynamic market situation throughout the entire year

The exceptional demand situation that the Fastening Systems segment had already successfully leveraged in the first half of the reporting period to generate record results continued in the second half of the year. The strong demand resulted in widespread supply shortages on the market, however. Both divisions successfully managed to largely uphold their ability to fill customer orders in this challenging environment.

Robust value chains enabled the Construction division to both serve its existing customers and gain new customers. Through its acquisitions of Jevith A/S (Denmark, as of July 1, 2021) and GLR Fasteners (USA, as of August 1, 2021), the division succeeded in expanding its market access in Europe and the US.

Whereas the Riveting division made use of the good demand situation among industrial customers, the business with customers from the automotive industry cooled down substantially over the course of the second half of the year. This was triggered by bottlenecks in the semiconductor supply chain, which impacted OEMs' production figures and had a delayed impact on call-offs in the division.

In this exceptional environment, the segment generated CHF 574.9 million in sales, which corresponds to a remarkable 17.4% increase over the same period of the previous year. Consolidation effects contributed +0.5% to the reported sales figure and there were minimal currency effects of +0.3%.

Both divisions benefited from a high level of capacity utilization throughout the entire year. Prudent cost and price management enabled the segment to overcome both turbulences attributable to the ongoing pandemic as well as the supply chain disruptions to achieve a record-breaking EBIT margin of 17.4%. This is an extraordinary result that is 5.5 percentage points higher than the EBIT margin for the same period of the previous year.

Distribution & Logistics (D&L)

Good initial situation from first half of year exploited

The Distribution & Logistics segment, which primarily serves customers from the industrial manufacturing and construction industries in Switzerland, grew substantially and achived strong results in the financial year just ended. Thanks to stable demand in all areas of application and good overall availability of materials, the segment's sales rose by 8.2% year on year to CHF 343.0 million in the period under review. Currency effects added +0.2% to the result. Existing business relationships with prominent customers were expanded and new business with new customers resulted in growth on an even broader basis.

The strong sales growth and prudent management enabled the segment to generate an operating profit (EBIT) of CHF 32.6 million, which corresponds to an EBIT margin of 9.4%.

Internationalization of the D&L segment through inclusion of Hoffmann

The planned inclusion of Hoffmann lends the D&L segment an internationally strong position in the attractive area of quality tools. Hoffmann is a leading international systems partner for quality tools that is well-known on European markets and serves more than 100,000 customers with a product range comprising around 500,000 items. Customers appreciate not only the company's comprehensive range of products but also its high level of product and logistics expertise, which will be strengthened even further through the commissioning of the new LogisticCity in Nuremberg (Germany), Europe's most high-performance logistics center for quality tools.

The transaction is subject to the usual closing conditions. It is expected to be concluded in the first half of 2022.

Strong competitive position lays foundation for future growth

SFS focuses on innovation trends that once again proved robust in the 2021 financial year. The segments' strong competitive edge enabled important new project acquisitions and market share gains, which in turn lay the foundation for future growth. With respect to the manufacturing of assemblies for electric brake systems for the automotive industry, for example, cooperation was intensified with the major Tier-1 suppliers in the US and Europe.

Growth-related expenditure on property, plant, equipment, hardware and software amounted to CHF 121.4 million (PY CHF 104.1 million) in the period under review. This was driven by the construction of the new production hall in Heerbrugg (Switzerland) for the Automotive division, ongoing efforts to switch to S/4HANA (the new generation ERP system), the strong commitment to cybersecurity and other project-specific investments. The additional production hall will offer the capacity required for manufacturing assemblies for electric brake systems. Construction work is proceeding on schedule and commissioning will take place in the third quarter of 2022. Current projects, including those acquired in 2021, will already lead to the utilization of some two-thirds of the building capacities under construction.

Preparations for the announced expansion of the location in Nantong (China) are proceeding according to schedule and construction will begin in 2022. The expansion will increase the location's production area by around 70% and be available for use by the Electronics, Automotive, Industrial, Riveting, Medical and Distribution & Logistics divisions in late 2023 to implement their growth projects. The expansion of the location in Hallau (Switzerland) for the Industrial and Medical divisions was completed on schedule and successfully put into operation. An existing production hall in the immediate vicinity of the Unisteel Malaysia site in Johor Bahru (Malaysia) was purchased to facilitate the new projects expected in the areas of Hard Disk Drives and Medical.

Expenditure on research and development amounted to CHF 45.6 million (PY CHF 44.5 million) and was charged in full to the income statement for the period.

Sustainability is a strategic priority

Sustainability is important to us! Embracing a sustainable mindset and practices gives us a chance to re-examine our products and processes on a daily basis and improve them continuously for the good of all stakeholders. As a value engineering specialist, working with our customers to develop sustainable products and solutions gives us a multitude of opportunities to utilize our expertise and offer our customers lasting added value – in keeping with our corporate principle of "Inventing success together".

Important steps were taken and progress made again in the 2021 financial year.

Key elements to improve sustainable development

Detailed information to sustainability at SFS can be found at sustainability.sfs.com →

Focus
- Regular reporting on progress
- Management remuneration tied to ESG KPIs

KPIs
- Economic performance
- Occupational health and safety
- Training and education
- Emission reductions
- Socioeconomic compliance

Reporting
- UN Global Compact (SDGs)
- GRI ("Core" option), Sustainability report 2021 released end of May

CO_2 Roadmap
- CO_2 emission reduction:
  - Scope 1 and 2 by ≥90% by 2030
  - Scope 3 by ≥90% by 2040

Outlook 2022
- Continued focus on set goals
- Update materiality assessment

Potential risks evaluated
The Group Executive Board and the Board of Directors regularly assess the main business risks to which SFS Group is exposed. A comprehensive risk assessment is conducted at least once a year. In this assessment, the relevant risks are systematically classified according to the likelihood of occurrence and the severity of the potential consequences. Potential risks and actions to contain these risks were examined once again during the year under review. The focus was on data breaches and business interruptions due to cyberattacks, investment-related risks associated with major projects, delayed order fulfillment due to the pandemic, risks associated with acquired companies, warranty risks arising from product recalls, geopolitical instabilities, company exposure to the global economic environment, compliance and currency-related risks.

Change in the Group Executive Board
At the Annual General Meeting on April 22, 2021, Volker Dostmann took over as CFO of SFS from Rolf Frei, who will continue to serve the company in selected strategic projects until his retirement in 2023.

With closing of the transaction, Hoffman will be embedded into the SFS organization as the second division within the Distribution & Logistics segment. Hoffmann's current CEO, Martin Reichenecker, will then join the Group Executive Board of SFS.

Change in the Board of Directors
At the Annual General Meeting 2021, the Board of Directors of the SFS Group appointed Manuela Suter, currently CFO of Bucher Industries and a member of its Executive Board, to the Board of Directors. With her many years of experience in multi-divisional, international and listed industrial companies, she is a valuable addition to the Board of Directors.

Extraordinary General Meeting on January 31, 2022
The current owners of Hoffmann will contribute 100% of the shares of Hoffmann SE to the SFS Group. A portion of the purchase price will be paid in the form of SFS shares. For that, a proposal was made at the extraordinary General Meeting to create authorized capital amounting to a maximum of CHF 160,000 (corresponds to no more than 1,600,000 shares). The shareholders of SFS Group AG approved this request with 99.3% in favor, thereby expressing their support for the transaction. The capital increase will be performed under the exclusion of subscription rights for existing shareholders.

29th Annual General Meeting on April 27, 2022
The Board of Directors of SFS Group AG proposes to the Annual General Meeting on April 27, 2022, that Thomas Oetterli, born 1969, be appointed to succeed Heinrich Spoerry as Chairman of the Board of Directors. Heinrich Spoerry will retire from the Board of Directors after reaching the age limit as defined in the Articles of Association. Thomas Oetterli has served as an independent member of the SFS Group's Board of Directors since 2011 and has chaired the Audit Committee since 2014. Through his many years of service on the SFS Group's Board of Directors, Thomas Oetterli has gained indepth knowledge of the Group.

The Board of Directors also proposes that shareholders elect Dr. Peter Bauschatz, currently the Chairman of the Supervisory Board of Hoffmann SE, to SFS's Board of Directors. The election of Dr. Peter Bauschatz is subject to the condition precedent of the closing of the acquisition of Hofmann SE. Hoffmann's inclusion at various levels of the SFS organization establishes continuity and lays a basis for successful future development.

In view of the good earnings and balance sheet, the outlook for the future business activity and the upcoming financing of the Hoffmann transaction, the Board of Directors will propose a dividend of CHF 2.20 per share.

In accordance with the Swiss Federal Council's ordinance on measures to combat the COVID-19 pandemic, SFS Group's Annual General Meeting will be held without the physical presence of shareholders, as was the case in the previous year. This desicion was taken already prior to the cancellation of pandemic-related restrictions, in agreement with the partner company with whom we usually split the organizational efforts that arise in connection with the operation of the infrastructure required for the annual general meeting. Shareholders may exercise their voting rights by issuing a power of attorney to the independent proxy in writing or electronically. The Annual General Meeting will be held at the headquarters of SFS Group AG in Heerbrugg (Switzerland) in the presence of the independent proxy and the Company's external auditor. Further information will follow with the invitation.

Outlook for the financial year 2022
Performance in the 2022 financial year will remain characterized by major uncertainties as a result of smoldering geopolitical developments like the current war in Ukraine, trade conflicts and sustained disruptions in supply chains. Uncertainties in international supply chains, which should gradually subside as the COVID-19 pandemic abates, are expected to persist until early 2023. In this environment, ensuring the highest possible focus on customers takes top priority. Investments in the selective expansion of our production capacity and thus the implementation of ambitious growth projects will continue. Major projects during the current financial year include the start work to expand the production platform in Nantong (China), moving into the new production hall at the Heerbrugg (Switzerland) site and the first go-lives of S/4HANA, the new generation ERP system.

The expansion of our global production platform for medical device applications remains a strategic priority. We expect the successful transaction with Hoffmann to take place in the first half of 2022, once the usual closing conditions have been met.

SFS expects product call-offs to be partly subdued in the first half of the year but for these pick up over the course of the year. Given the solid project pipeline, we are confident that the development will be positive in all end markets. Based on that, SFS expects standalone sales growth of 3–6% for the 2022 financial year at an EBIT margin of 13–16%. The outlook will be updated once the transaction with Hoffmann has been closed.

Thank you
We would like to take this opportunity to offer our most sincere thanks to each and every one of our employees for their outstanding efforts under the exceptional conditions during the COVID-19 pandemic. Despite the challenging times we live in, we still experience outstanding commitment, team spirit and perseverance from our employees.

Our thanks also go out to our customers and other business partners. Our collaborative partnership with them and the trust they place in us lay the foundation for our work together to develop solutions that generate lasting added value.

We would also like to thank our shareholders for their trust in SFS and their loyal support, which lend our company stability.

Heinrich Spoerry
Chairman of the
Board of Directors

Jens Breu
CEO