TORNOS

Interim Consolidated Financial Statements 2016

Tornos Holding Ltd.

Financial Review and Management Report

General

By the end of 2015 it was already becoming apparent that the negative effects of removing the minimum exchange rate for the Swiss franc against the euro would continue to have an impact on order intake this year, all the more in a difficult global market environment. These unfavourable framework conditions present a real challenge for manufacturing companies in Switzerland.

Since worldwide demand for machine tools reached its peak in 2011, the three global regions Europe, Asia and the USA have trended downwards, apart from a short period of stability in 2014. This is also true of China, the world's largest machine tool market. Tornos has also been affected by this trend in the global regions, with order intake in some cases significantly below expectations and the figures for the previous year. The effects of customers' reluctance to invest in major, project-related new machinery were particularly noticeable.

Order intake and backlog

In the first six months of the current year, order intake came to CHF 62.6 million, which represents a substantial decrease of 32.2%, or CHF 29.7 million, compared with the same period of last year (CHF 92.3 million).

The market—particularly the automotive supply industry—showed a definite reluctance to invest, especially in major, project-related development schemes of the kind that use our multi-spindle machines.

By contrast, order intake for single-spindle machines was on a par with the previous year. The SwissNano —developed and manufactured in Switzerland—performed very gratifyingly: the number of machines sold in the first six months of the year equalled the number sold in twelve months during each of the preceding two years. Demand for our Asian machines in the Swiss DT and Swiss GT ranges is also satisfactory. Around half of the Tornos machines ordered are made in Xi'an (China) or Taichung (Taiwan).

The business of service and spare parts is stable at Tornos and indicates that the order situation on the customer side is intact. In the first half of 2016, order intake here was CHF 19.9 million, up CHF 0.7 million on the prior-year period.

The order backlog as at June 30, 2016 stood at CHF 24.2 million (December 31, 2015: CHF 29.7 million).

Net sales

At CHF 69.8 million, net sales in the first semester 2016 were 15.4% or CHF 12.8 million lower than in the year-back period (CHF 82.6 million). The first quarter of 2016 was particularly disappointing: sales came to CHF 29.5 million compared to CHF 41.3 million a year previously. By contrast, in the second quarter of 2016 sales amounted to CHF 40.3 million, i.e. approximately the same as in the prior-year quarter (CHF 41.3 million).

In the Swiss domestic market, net sales were CHF 12.9 million, down CHF 3.6 million or 22.1% on the same period of the previous year (CHF 16.5 million). However, an increase in order intake year-on-year gives us cause for optimism regarding the second half. In the rest of Europe, net sales were CHF 40.6 million, also down CHF 3.5 million (-8.0%) on the prior-year period (CHF 44.1 million). Sales in the Americas came in well below expectations at CHF 6.6 million, down CHF 2.2 million or 25.0% on the same period of last year (CHF 8.8 million). In the faltering Asian market (including the rest of the world), Tornos generated net sales of CHF 9.8 million, which was a year-on-year decrease of CHF 3.4 million or 25.6% (CHF 13.2 million).

Switzerland contributed 18% to net sales (previous year: 20%), while the rest of Europe accounted for 58% (previous year: 53%). The Americas contributed 10% (previous year: 11%), and Asia (including the rest of the world) 14% (previous year: 16%).

Gross profit

At 27.8%, the gross profit margin was on a par with the previous year (27.7%) in percentage terms. In absolute terms, gross profit was CHF 19.5 million, down CHF 3.4 million or 15.1% on the previous year (CHF 22.9 million).

This result was boosted by changes in the product mix, lower material prices following intensive negotiations with suppliers, and lower personnel costs thanks to selectively introduced short-time working and reduced overtime payments.

The accompanying notes form an integral part of these interim consolidated financial statements

Operating expenses / Operating result

As in previous years, Tornos constantly strives to reduce its operating expenses. Although cost-cutting potential is decreasing all the time, expenses were reduced once again in the first half of 2016 compared with the year-back period, falling by CHF 0.8 million to CHF 23.0 million (previous year: CHF 23.8 million). Most of the savings were made in the area of general and administrative expenses and in marketing and sales. The cost of research and development remained at the same level as in the previous year. It is important for Tornos that cost minimization does not jeopardize the planned launch of new products.

Certain cost-cutting measures introduced in the first half will not start to have an impact on costs until the second half.

In the first half of 2016, the operating result stood at CHF -3.5 million, CHF -2.6 million lower than in the previous year (CHF -0.9 million). The operating margin was -5.1% (previous year: -1.1%).

Ordinary result

Financial income and expenses were at much the same level as in the previous year. Net currency losses came to CHF 0.6 million. The United Kingdom's decision on Brexit had a significant negative impact on this figure right at the end of the reporting period. In the previous year, currency losses were CHF 1.2 million. In that period, the Swiss National Bank's removal of the EUR/CHF exchange rate floor had the biggest negative impact.

Non-operating result

As part of its strategy implementation, Tornos took a further step to rationalize the real estate at its Moutier site by selling the "Foyer" building (Rue Industrielle 95) to a local company in a related sector, resulting in an accounting profit of CHF 1.1 million.

Net result

The net result for the first half of 2016 thus came to CHF -3.5 million (previous year: CHF -2.5 million). The profit margin was -5.1% (previous year: -3.0%).

Balance sheet

Compared with December 31, 2015, the total balance sheet fell by CHF 9.5 million to CHF 131.3 million as at June 30, 2016.

On the asset side, cash and cash equivalents (CHF -9.4 million) and sales-related trade receivables (CHF -1.8 million) made a notable contribution to the decrease. By contrast, the inventory rose by CHF 2.4 million.

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On the liabilities side, there was a drop in trade payables (CHF -5.9 million). This, too, was related to the fall in sales. Furthermore, other liabilities declined by CHF 1.9 million because of the decrease in customer advances. On the other hand, accrued liabilities and deferred income rose by CHF 2.5 million to CHF 8.4 million.

As at June 30, 2016, net cash stood at CHF 1.8 million (December 31, 2015: CHF 11.3 million).

Shareholders' equity decreased by CHF 3.6 million in the first half of the year, falling to CHF 80.5 million as at June 30, 2016 (December 31, 2015: CHF 84.1 million), including minority interests of CHF 0.6 million (December 31, 2015: CHF 0.7 million). The equity ratio increased by 1.6 percentage points compared with December 31, 2015 because of the decline in the total balance sheet; it stood at 61.3% on the reporting date (December 31, 2015: 59.7%).

Cash flow

Cash flow from operating activities came to CHF -9.1 million in the first half (previous year: CHF -6.7 million). This figure includes a negative change in net working capital amounting to CHF 8.0 million (previous year: negative change of CHF 5.9 million) due in particular to higher inventories and a decrease in trade payables. Cash flow from investment activities is balanced (previous year: CHF -0.9 million). Income from the disposal of the property at Rue Industrielle 95 and of a small plot of land equalled the investment expenses. The latter were primarily spent on renovating the Tour Bechler, a property not required for operating purposes (CHF 1.1 million), and on software and hardware (CHF 0.5 million). Free cash flow in the reporting period thus came to CHF -9.1 million (previous year: CHF -7.5 million).

Employees

As at June 30, 2016, headcount (FTE) was 628 (December 31, 2015: 657) and 39 apprentices (December 31, 2015: 38). Around 30 full-time jobs were cut at the Moutier site, affecting 20 permanent and 10 temporary employees. On the other hand, jobs were created at the production facilities in Xi'ian (China) and Taichung (Taiwan) in order to cope with rising production volumes.

Foreign currency translation

The most significant exchange rates against the Swiss franc for the Tornos Group in the period under review are shown in the table below.

Currency	Average rate		Closing rate	
	1.1.–30.6.2016	1.1.–30.6.2015	30.6.2016	31.12.2015
1 EUR	1.0957	1.0578	1.0863	1.0825
1 USD	0.9819	0.9470	0.9783	0.9925
1 GBP	1.4075	1.4423	1.3099	1.4691
1 RMB	0.1502	0.1543	0.1472	0.1529

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Interim Consolidated Income Statement *(unaudited)*

In CHF 1'000	Notes	1st HY 2016 1.1.–30.6.2016	1st HY 2015 1.1.–30.6.2015
Net sales	10	**69'848**	**82'586**
Cost of sales		–50'396	–59'681
Gross profit		**19'452**	**22'905**
in % net sales		*27.8%*	*27.7%*
Marketing and sales		–11'355	–11'663
General and administrative expenses		–8'277	–8'732
Research and development		–3'483	–3'463
Other income – net		129	43
Operating expenses		**–22'986**	**–23'815**
Operating result		**–3'534**	**–910**
in % net sales		*–5.1%*	*–1.1%*
Financial income		7	8
Financial expenses		–272	–153
Exchange result, net		–640	–1'179
Ordinary result		**–4'439**	**–2'234**
Non-operating result	11	1'107	–
Earnings before income taxes		**–3'332**	**–2'234**
Income tax		–209	–257
Net result		**–3'541**	**–2'491**
in % net sales		*–5.1%*	*–3.0%*
Thereof attributable to shareholders of Tornos Holding Ltd.		–3'457	–2'353
Thereof attributable to minority interests		–84	–138
Result per share	9		
– basic (CHF per share)		–0.18	–0.12
– diluted (CHF per share)		–0.18	–0.12
Additional information (in CHF 1'000)			
EBITDA		**–1'134**	**408**
in % net sales		*–1.6%*	*0.5%*
Depreciation and amortisation		–1'293	–1'318
EBIT		**–2'427**	**–910**
in % net sales		*–3.5%*	*–1.1%*

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Interim Consolidated Balance Sheet *(unaudited)*

In CHF 1'000	Notes	30.6.2016	in %	31.12.2015	in %
ASSETS					
Cash and cash equivalents		11'160		20'608	
Trade receivables		21'456		23'219	
Inventories, net		66'525		64'123	
Other short-term receivables		5'262		6'637	
Prepayment and accrued income		3'214		2'020	
Total current assets		**107'617**	**82.0%**	**116'607**	**82.8%**
Property, plant and equipment		22'334		22'853	
Intangible assets		915		797	
Deferred tax assets		437		541	
Total non-current assets		**23'686**	**18.0%**	**24'191**	**17.2%**
Total assets		**131'303**	**100.0%**	**140'798**	**100.0%**
LIABILITIES AND EQUITY					
Interest bearing borrowings	7	9'086		9'060	
Trade payables		19'258		25'112	
Current tax liabilities		111		99	
Other liabilities		4'275		6'205	
Accrued liabilities and deferred income		8'409		5'876	
Provisions		2'926		3'552	
Total current liabilities		**44'065**	**33.5%**	**49'904**	**35.5%**
Interest bearing borrowings		274		245	
Retirement benefit obligations		5'730		5'779	
Provisions		655		654	
Deferred tax liabilities		104		105	
Total non-current liabilities		**6'763**	**5.2%**	**6'783**	**4.8%**
Total liabilities		**50'828**	**38.7%**	**56'687**	**40.3%**
Share Capital		89'450		89'450	
Capital reserve		28'814		28'814	
Treasury shares		-6'734		-6'734	
Retained earnings		-27'366		-28'661	
Currency translation adjustments		-857		-666	
Net result		-3'457		1'176	
Equity attributable to shareholders of Tornos Holding Ltd.		**79'850**		**83'379**	
Minorities interests		625		732	
Total equity		**80'475**	**61.3%**	**84'111**	**59.7%**
Total liabilities and equity		**131'303**	**100.0%**	**140'798**	**100.0%**

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Interim Consolidated Statement of Changes in Equity *(unaudited)*

In CHF 1'000	Share capital	Capital reserve	Treasury shares	Retained earnings	Currency translation adjustments	Total attributable to shareholders of Tornos Holding Ltd.	Minority interests	Equity
December 31, 2014	**89'450**	**28'814**	**–5'242**	**–28'843**	**278**	**84'457**	**746**	**85'203**
Capital increase of the joint venture in Xi'àn							310	310
Net result				–2'353		**–2'353**	–138	–2'491
Currency translation adjustments					–518	**–518**	–47	**–565**
Share-based compensation				149		**149**		**149**
June 30, 2015	**89'450**	**28'814**	**–5'242**	**–31'047**	**–240**	**81'735**	**871**	**82'606**
December 31, 2015	**89'450**	**28'814**	**–6'734**	**–27'485**	**–666**	**83'379**	**732**	**84'111**
Net result				–3'457		**–3'457**	–84	**–3'541**
Currency translation Adjustments					–191	**–191**	–23	**–214**
Share-based Compensation				119		**119**		**119**
June 30, 2016	**89'450**	**28'814**	**–6'734**	**–30'823**	**–857**	**79'850**	**625**	**80'475**

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Interim Consolidated Statement of Cash Flows *(unaudited)*

In CHF 1'000	Notes	1st HY 2016 1.1.–30.6.2016	1st HY 2015 1.1.–30.6.2015
Net result for the period		**–3'541**	**–2'491**
Adjustments for expenses and income not affecting cash:			
Income taxes		209	257
Depreciation of property, plant and equipment		1'081	1'123
Amortization of intangible assets		212	195
Result on disposal of property, plant and equipment		–1'107	–
Share-based compensation		119	149
Allowance and write-offs on inventories		1'900	289
Other non cash items		–5	–7
Change in Net Working Capital		–8'032	–5'906
Thereof trade receivables		*1'728*	*–4'828*
Thereof other assets and prepayments		*398*	*1'735*
Thereof inventories		*–4'575*	*–2'905*
Thereof trade payables		*–5'776*	*–1'798*
Thereof other current liabilities and provisions		*193*	*1'890*
Interest expense		185	60
Income tax paid		–155	–323
Cash flow from operating activities		**–9'134**	**–6'654**
Investment in property, plant and equipment		–1'330	–879
Disposal of property, plant and equipment	11	1'677	7
Investment in intangible assets		–343	–
Cash flow from investing activities		**4**	**–872**
Free Cash Flow		**–9'130**	**–7'526**
Repayments of borrowings, including finance lease liabilities		–34	–33
Proceeds from borrowings		–	5'000
Cash received from minority interests for Xi'an		–	310
Interest paid		–185	–60
Cash flow from financing activities		**–219**	**5'217**
Net cash flow		**–9'349**	**–2'309**
Cash and cash equivalents and bank overdrafts at January 1		20'608	15'434
Effects of exchange rate changes		–99	–226
Cash and cash equivalents and bank overdrafts at June 30		**11'160**	**12'899**

The accompanying notes form an integral part of these interim consolidated financial statements

Selected notes to the Interim Consolidated Financial Statements

All figures are presented in CHF 1'000 unless otherwise stated.

1 General information

Tornos Holding Ltd. is a company domiciled in Moutier, Switzerland and is listed on the Swiss Reporting Standard of SIX Swiss Exchange in Zürich. The Tornos Group, which consists of Tornos Holding Ltd. and all its subsidiaries, is active in the development, manufacture, marketing, sale and servicing of machines and related spare parts. Tornos manufactures in Moutier and La Chaux-de-Fonds (CH), in Taichung (TW) and in Xi'an (CN) and markets the product lines on a worldwide basis. The Group's sales operations outside of Switzerland principally include European countries, Americas and Asia.

These interim consolidated financial statements have been approved for issue by the Board of Directors on July 22, 2016.

2 Basis of preparation

The unaudited interim consolidated financial statements of the Tornos Group for the six months ended June 30, 2016 have been prepared in accordance with the Accounting Standard 31 "complementary recommendation for listed companies" of Swiss GAAP FER as well as the requirements of SIX Swiss Exchange. These interim financial statements do not contain all the information and disclosures required in the annual consolidated financial statements. This interim financial information should be read in conjunction with the annual financial statements for the year ended December 31, 2015 which have been prepared in accordance with Swiss GAAP FER.

3 Accounting policies

The accounting policies applied by the Tornos Group in this interim financial report are consistent with those applied in the consolidated financial statements as at December 31, 2015.

The new specifications adopted as of January 1, 2016 regarding revenue recognition from transactions with multiple-elements arrangements with changes in the Swiss GAAP FER Framework, the Swiss GAAP FER 3 and the Swiss GAAP FER 6 have been adopted accordingly. These changes in accounting rules have no impacts on the accounting policies adopted by the Group since Tornos does not have further separate identifiable performance obligations within its sales arrangement (which include either the sale of a machine, of spare parts or the provision of services which can be directly charged to customers) which would have to be valued on a standalone basis. As described in the consolidated financial statements as at December 31, 2015, revenues, sales are recognised on the full completion of the delivery or the service (upon delivery of products or customer acceptance in the case of "bill and hold" sales, or performance of services), net of sales tax and discounts. Sales are only recognized if it is probable that the economic benefit will flow to the Group and the amount can be reliably estimated.

4 Estimates

The preparation of interim financial statements requires Management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expense. Actual results may differ from these estimates. On an ongoing basis, Management evaluates the estimates, including those related to provisions for warranty, provisions resulting from pending litigations as well as other present obligations of uncertain timing, inventory obsolescence, bad debts, valuation of intangible assets, assessment of income taxes including deferred tax assets and retirement benefit obligations. In preparing these interim financial statements, the significant judgements made by Management in applying the Group's accounting policies and the key sources of estimation uncertainty were the same as those applied to the consolidated financial statements for the year ended December 31, 2015.

Management and Board of Directors believe the basis of planning and the assumptions to be realistic.

5 Seasonality and cyclicality of interim operations

Tornos business areas are not subject to any significant seasonal influences. The Group's operations are sensitive to economic cycles which can quickly impact its clients' investment decisions.

6 Scope of consolidation

On January 29, 2016, the sales and service company “Tornos Technologies (HK) Limited” domiciled in Hong Kong has been liquidated with no material impact on the financial statements of the Group. Other than this, there are no changes in the scope of consolidation in the period under review. To further simplify the structure of the Group, the dormant companies “Almatronic Ltd.” in La Chaux-de-Fonds as well as “Cyklos Ltd.” in Yverdon-les-Bains have been put in liquidation. It is expected that these two companies will be liquidated at the year-end.

7 Loan from shareholders

Tornos has a credit agreement for a total of CHF 20 millions granted from two shareholders to finance its net working capital. The loan agreements mature on March 31, 2017, but are renewed automatically, if they are not terminated by a written notice 6 months prior to the maturity date. These loan agreements have not been terminated. As of June 30, 2016 the credit line has been used with an amount of CHF 9 million (December 31, 2015: CHF 9 million).

The aforementioned shareholder loans bear fixed interest rates of 4%.

At the end of June 30, 2016, CHF 3.5 million (December 31, 2015: CHF 3.1 million) were used under the ancillary facilities for guarantees purposes.

8 Stock compensation plan

Tornos has since 2011 one stock participation plan, namely the Management and Board Participation Plan 2007 (MBP07). Compensation expense is recognised for options over the vesting period and for shares purchased immediately in the accounts as the shares do not need to be returned in case the employment contract is terminated. The expense recorded in the income statement spreads the cost of each option equally over the vesting period. Assumptions are made concerning the forfeiture rate which is adjusted during the vesting period so that at the end of the vesting period there is only a charge for vested amounts. Compensation expense of KCHF 119 was recorded for the six months period ended June 30, 2016 (June 30, 2015: KCHF 149).

The fair value of the grants under the MBP07 stock option plan is estimated using the Black-Scholes valuation model.

9 Result per share, basic and fully diluted

9.1 Basic

Basic earnings per share is calculated by dividing the net income attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the year, excluding ordinary shares purchased by the Company and held as treasury shares.

	1st HY 2016 1.1.–30.6.2016	1st HY 2015 1.1.–30.6.2015
Net result attributable to equity holders of the Company (in CHF 1'000)	–3'457	–2'353
Weighted average number of ordinary shares in issue (in 1'000)	18'935	19'490
Basic result per share (CHF per share)	**–0.18**	**–0.12**

9.2 Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. The Company has one category of dilutive potential ordinary shares: share options. For the share options, a calculation is done to determine the number of shares that could have been acquired at fair value (determined as the average annual market share price of the Company's shares) based on the monetary value of the subscription rights attached to outstanding share options. The number of shares calculated as above is compared with the number of shares that would have been issued assuming the exercise of the share options.

	1st HY 2016 1.1.–30.6.2016	1st HY 2015 1.1.–30.6.2015
Net result attributable to equity holders of the Company (in CHF 1'000)	–3'457	–2'353
Weighted average number for diluted earnings per share (in 1'000)	18'935	19'490
Diluted result per share (CHF per share)	**–0.18**	**–0.12**

10 Segment information

The Group's core activity is the development, manufacture, marketing, sale and servicing of machines. The top management is responsible to steer the business and regularly review the Group's internal reporting for its only operating segment, "machines", in order to assess performance and assess resource needs. The primary internal reporting to the top management is presented on the same basis as the Group's consolidated income statement and consolidated balance sheet and is reported on a consistent basis over the periods presented.

The top management assesses the performance of the business based on operating result. Additional reporting such as geographical area are also provided to the top management but they are not considered as substantial information to strategic decisions, allocate or plan resources or monitor the Group's operational performance. These operational decisions are all executed by the top management based on internal reporting of the core activity.

Revenues generated are derived from sales of machines, spare parts and service.

The operating result for the period under review amounts to a loss of KCHF -3'534 and for 2015 to a loss of KCHF -910.

10.1 Net sales by category

In CHF 1'000	1st HY 2016 1.1.–30.6.2016	1st HY 2015 1.1.–30.6.2015
Machines and spare parts	65'166	78'951
Service	4'682	3'635
Net sales	**69'848**	**82'586**

Switzerland is the domicile of the parent company and of the main operating and distribution companies. The Swiss operating companies conduct all main development and manufacture activities. The subsidiaries located in the other European countries (France, Germany, Italy, Poland, Spain and the United Kingdom), the Americas and Asia, except the Branch in Taiwan and the production company in Xi'an, only have support or sales and distribution activities. The entities in Taiwan and Xi'an are companies which on behalf of the parent company conduct some developments on new products, which are then marketed through the Group's distribution network. The transactions between Group companies are conducted based on internationally acceptable transfer pricing policies, thereby leaving reasonable margins at local subsidiary level. The top management reviews sales for the four material geographical areas, namely, Switzerland, Other European countries, the Americas and Asia. For the purpose of presenting net sales by location of customers, one other geographical region, namely Rest of world, is identified.

10.2 Net sales by region

In CHF 1'000	1st HY 2016 1.1.–30.6.2016	1st HY 2015 1.1.–30.6.2015
Switzerland	12'855	16'498
Other European countries	40'562	44'070
Americas	6'584	8'774
Asia	9'567	12'347
Rest of world	280	897
Total net sales	**69'848**	**82'586**

10.3 Non-current assets

The total of non-current assets other than financial instruments and deferred tax assets is as follows:

In CHF 1'000	30.06.2016	31.12.2015
Switzerland	21'811	22'008
Other European countries	665	775
Americas	15	21
Asia	758	846
Total non-current assets for geographical area disclosure	23'249	23'650
Reconciling unallocated assets:		
– Deferred tax assets	437	541
Total non-current assets per balance sheet	**23'686**	**24'191**

11 Non-operating result

The gain of KCHF 1'107 relates to the sale of non-operating buildings and lands which have been sold for KCHF 1'877 as part of the rationalization of its real property inventory.

12 Subsequent events

There are no subsequent events to be mentioned.

We keep you turning

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