

Alternative performance measures 2019

- 18 Definitions of alternative performance measures
- 19 Organic sales growth
- 20 Adjusted consolidated statement of income
- 22 Free cash flow
- 23 Capital management

Definitions of alternative performance measures

The annual report, the half year report and other communication to investors contain certain financial performance measures, which are not defined by IFRS. In addition to information based on IFRS, management uses these alternative performance measures to assess the financial and operational performance of the Group. Management believes that these non-IFRS financial performance measures provide useful information regarding Galenica's financial and operational performance. Alternative performance measures are used in Galenica's value-based management as the basis for management's incentive and remuneration schemes. Such measures may not be comparable to similar measures presented by other companies. The main alternative performance measures used by Galenica are explained and/or reconciled with the IFRS measures in this section. The alternative performance measures are unaudited.

IAS 19 – Employee benefits

The pension plans of Galenica are organised in legally independent pension funds and are based purely on the defined contribution principle as stated in the Swiss "BVG" law. Nevertheless, Galenica's pension plans are classified as defined benefit pension plans under IAS 19.

Galenica's management is of the opinion that this accounting treatment can lead to discussions of the financial statements and performance indicators of the Galenica Group. For this reason, Galenica also evaluates its performance by adjusting personnel costs as if those plans were defined contribution plans (adjustments for the effects of IAS 19). For these adjustments, the costs of defined benefit plans and long-service awards determined in accordance with IAS 19 are replaced by an expense based on the employer's contribution and long-service awards for the period of service.

IFRS 16 – Leasing

Since 1 January 2019 lessees have to account for most leases on balance sheet by recognising lease liabilities and corresponding right-of-use assets. The right-of-use assets are depreciated over the lease term and the lease liabilities generate interest expense in the statement of income. Variable lease payments, not dependent on an index or rate, such as sales-based rental expenses are accounted for as operating expenses when they are incurred. With its large network of retail pharmacies, the introduction of IFRS 16 has a significant impact on Galenica's balance sheet and the presentation of lease related expenses in the consolidated statement of income.

Galenica has lease agreements with fixed and variable lease payments and these payments affect various line items in the statement of income making comparisons across individual pharmacies and points-of-sale difficult. For this reason management also monitors results by adjusting the statement of income and balance sheet as if lease agreements were still accounted for as operating leases, e.g. all lease expense is presented in other operating costs on a straight-line basis and the depreciation of the right-of-use assets and the interest expense on the lease liabilities are removed. Income taxes are also adjusted accordingly.

These adjustments allow management to evaluate results with periods prior to the introduction of IFRS 16. In addition, IFRS 16 adjusted measures are important for Galenica's value-based management and therefore for management's incentive and remuneration schemes. As the type and duration of rental agreements under IFRS 16 have a significant influence on the invested capital and accordingly on the return on invested capital (ROIC) and on the Galenica economic profit (GEP), the invested capital is stated after removing lease liabilities. This minimises the risk that management makes decisions that are not in the interest of Galenica due to false incentives when concluding leases.

Organic sales growth

Organic sales growth shows the development of net sales of the business sectors Retail and Services excluding the effects of acquisitions and disposals (effect of expansion). It provides a “like-for-like” comparison with previous periods. In the Retail business sector, organic sales growth is calculated only including points of sale with a full year period comparison. In order to show the impact of mandatory price reductions of reimbursed medications on net sales transparently, organic sales growth is also disclosed without the effect of price reductions. This price reductions effect is calculated for mandatory price reductions of reimbursed medications of the specialities list based on volumes of previous period.

Organic sales growth first half of 2019

in thousand CHF	Retail	Services
Net sales	726,105	1,192,369
Change to previous period	4.3%	1.3%
Effect of expansion ¹⁾	35,323	–
In % of net sales of previous period	5.1%	–
Net sales excluding effect of expansion	690,782	1,192,369
Organic sales growth	(0.7%)	1.3%
Mandatory price reductions of reimbursed medications of the specialities list ²⁾	13,356	30,067
In % of net sales of previous period	1.9%	2.6%
Net sales excluding effect of expansion and mandatory price reductions	704,138	1,222,436
Organic sales growth excluding price reductions	1.2%	3.9%

¹⁾ Difference of net sales to previous period of points of sale without a full year period comparison

²⁾ Mandatory price reductions of reimbursed medications of the specialities list, calculated based on volumes of previous period

Organic sales growth first half of 2018

in thousand CHF	Retail	Services
Net sales	695,849	1,177,118
Change to previous period	2.6%	0.9%
Effect of expansion ¹⁾	9,088	–
In % of net sales of previous period	1.3%	–
Net sales excluding effect of expansion	686,761	1,177,118
Organic sales growth	1.3%	0.9%
Mandatory price reductions of reimbursed medications of the specialities list ²⁾	7,693	22,064
In % of net sales of previous period	1.2%	1.9%
Net sales excluding effect of expansion and mandatory price reductions	694,454	1,199,182
Organic sales growth excluding price reductions	2.5%	2.8%

¹⁾ Difference of net sales to previous period of points of sale without a full year period comparison

²⁾ Mandatory price reductions of reimbursed medications of the specialities list, calculated based on volumes of previous period

Adjusted consolidated statement of income

Galenica's consolidated statement of income adjusted by IAS 19 effects related to employee benefits (defined benefit plans and long-service awards) and IFRS 16 lease effects allowing financial results to be assessed on a comparable basis.

Adjusted consolidated statement of income first half of 2019

in thousand CHF	As reported	Adjustments		Adjusted
		IAS 19	IFRS 16	
Net sales	1,600,422	-	-	1,600,422
Health & Beauty ¹⁾	781,393	-	-	781,393
Services ¹⁾	1,192,369	-	-	1,192,369
Other income	8,125	-	-	8,125
Operating income	1,608,547	-	-	1,608,547
Cost of goods	(1,189,316)	-	-	(1,189,316)
Personnel costs	(227,183)	(286)	-	(227,469)
Other operating costs	(69,433)	-	(24,637)	(94,070)
Share of profit from associates and joint ventures	4,073	(12)	19	4,080
Earnings before interest, taxes, depreciation and amortisation (EBITDA)	126,688	(298)	(24,618)	101,772
Health & Beauty ¹⁾	94,211	-	(23,516)	70,695
Services ¹⁾	34,082	-	(1,102)	32,980
Depreciation and amortisation	(43,889)	-	23,229	(20,660)
Earnings before interest and taxes (EBIT)	82,799	(298)	(1,389)	81,112
Return on sales (ROS) ²⁾	5.2%	-	(0.1%)	5.1%
Health & Beauty ¹⁾	61,575	-	(1,313)	60,262
Return on sales (ROS) ²⁾	7.9%	-	(0.2%)	7.7%
Services ¹⁾	22,698	-	(75)	22,623
Return on sales (ROS) ²⁾	1.9%	-	-	1.9%
Net financial expenses	(2,736)	224	1,248	(1,264)
Earnings before taxes (EBT)	80,063	(74)	(141)	79,848
Income taxes	(15,136)	158	110	(14,868)
Net profit	64,927	84	(31)	64,980

¹⁾ Reported for each Segment not taking into account Corporate and Eliminations

²⁾ Return on sales (ROS) is calculated as EBIT divided by net sales

in CHF	As reported	Adjustments		Adjusted
		IAS 19	IFRS 16	
Earnings per share	1.32	-	-	1.32
Diluted earnings per share	1.32	-	-	1.32

Alternative performance measures of the Galenica Group

Adjusted consolidated statement of income first half of 2018

in thousand CHF	As reported	Adjustments IAS 19	Adjusted
Net sales	1,566,133	-	1,566,133
Health & Beauty ¹⁾	745,665	-	745,665
Services ¹⁾	1,177,118	-	1,177,118
Other income	7,404	-	7,404
Operating income	1,573,537	-	1,573,537
Cost of goods	(1,178,227)	-	(1,178,227)
Personnel costs	(217,117)	4,667	(212,450)
Other operating costs	(91,198)	-	(91,198)
Share of profit from associates and joint ventures	2,411	112	2,523
Earnings before interest, taxes, depreciation and amortisation (EBITDA)	89,406	4,779	94,185
Health & Beauty ¹⁾	63,362	-	63,362
Services ¹⁾	32,758	-	32,758
Depreciation and amortisation	(19,303)	-	(19,303)
Earnings before interest and taxes (EBIT)	70,103	4,779	74,882
Return on sales (ROS) ²⁾	4.5%	(0.3%)	4.8%
Health & Beauty ¹⁾	54,270	-	54,270
Return on sales (ROS) ²⁾	7.3%	-	7.3%
Services ¹⁾	22,345	-	22,345
Return on sales (ROS) ²⁾	1.9%	-	1.9%
Net financial expenses	(1,259)	124	(1,135)
Earnings before taxes (EBT)	68,844	4,903	73,747
Income taxes	(12,366)	(1,006)	(13,372)
Net profit	56,478	3,897	60,375

¹⁾ Reported for each Segment not taking into account Corporate and Eliminations

²⁾ Return on sales (ROS) is calculated as EBIT divided by net sales

in CHF	As reported	Adjustments IAS 19	Adjusted
Earnings per share	1.15	0.08	1.23
Diluted earnings per share	1.15	0.08	1.23

Alternative performance measures of the Galenica Group

Free cash flow

The free cash flow shows Galenica's capacity to pay dividends and repay debt and equity. It provides information on the remaining cash and cash equivalents from the operating cash flow, reduced by all lease payments and after consideration of investment activities.

Free cash flow

in thousand CHF	1.1.-30.6.2019	1.1.-30.6.2018
Cash flow from operating activities before working capital changes	116,016	87,004
Payment of lease liabilities	(23,404)	-
Cash flow from operating activities before working capital changes adjusted	92,612	87,004
Working capital changes	(41,151)	(5,425)
Cash flow from operating activities adjusted	51,461	81,579
Cash flow from investing activities without M&A ¹⁾	(24,640)	(21,389)
Free cash flow before M&A	26,821	60,190
Cash flow from M&A ²⁾	(54,616)	(21,025)
Free cash flow	(27,795)	39,165

¹⁾ Cash flow from investing activities without purchase and sale of subsidiaries (net cash flow)

²⁾ Cash flow from purchase and sale of subsidiaries (net cash flow)

Cash conversion

	1.1.-30.6.2019	1.1.-30.6.2018
Cash conversion ¹⁾	75.7%	77.3%

¹⁾ Calculated as EBITDA adjusted less CAPEX (investments in property, plant and equipment and intangible assets) divided by EBITDA adjusted

Capital management

The capital of Galenica is managed and monitored at Group level. The objective of capital management at Galenica is to ensure the continuity of operations, increase enterprise value on a sustainable basis, provide an adequate return to investors, provide the financial resources to enable investments in areas that deliver future benefits for patients and customers and further returns to investors.

Galenica defines the capital that it manages as invested interest-bearing liabilities and equity. Galenica uses a system of financial control based on various key performance indicators. Capital is monitored based on the gearing, for example, which expresses net debt as a percentage of shareholders' equity including non-controlling interests and is communicated regularly to management as part of internal reporting. The debt coverage expresses net debt as a multiple of earnings before interest, taxes, depreciation and amortisation (EBITDA). Debt coverage ratio provide information about the creditworthiness of the Group. Galenica has no covenants requiring a minimum level of debt coverage.

Total assets and shareholders' equity are adjusted for the cumulative effects of the IAS 19 and IFRS 16 adjustments and net debt is adjusted for lease liabilities.

Total assets

in thousand CHF	30.6.2019	30.6.2018
Total assets	2,221,350	1,826,096
Cumulative effects of IAS 19 adjustments	(9,959)	(6,316)
Cumulative effects of IFRS 16 adjustments	(239,078)	-
Total assets adjusted	1,972,313	1,819,780

Net debt

in thousand CHF	30.6.2019	30.6.2018
Current financial liabilities ¹⁾	92,965	39,733
Current lease liabilities	42,867	-
Non-current financial liabilities ¹⁾	380,855	381,164
Non-current lease liabilities	202,547	-
Cash and cash equivalents	(55,175)	(67,802)
Interest-bearing receivables	(2,132)	(2,379)
Net debt	661,927	350,716
Lease liabilities (current and non-current)	(245,414)	-
Net debt adjusted	416,513	350,716

¹⁾ Excluding non-interest-bearing financial liabilities

Shareholders' equity

in thousand CHF	30.6.2019	30.6.2018
Shareholders' equity	917,803	836,929
Cumulative effects of IAS 19 adjustments	58,964	30,553
Cumulative effects of IFRS 16 adjustments	4,832	-
Shareholders' equity adjusted	981,599	867,482

Alternative performance measures of the Galenica Group

Equity ratio

	30.6.2019	30.6.2018
Equity ratio ¹⁾	41.3%	45.8%
Equity ratio adjusted ²⁾	49.8%	47.7%

¹⁾ Calculated as shareholders' equity divided by total assets

²⁾ Calculated as shareholders' equity adjusted divided by total assets adjusted

Gearing

	30.6.2019	30.6.2018
Gearing ¹⁾	72.1%	41.9%
Gearing adjusted ²⁾	42.4%	40.4%

¹⁾ Calculated as net debt divided by shareholders' equity

²⁾ Calculated as net debt adjusted divided by shareholders' equity adjusted

Debt coverage

	30.6.2019	30.6.2018
Debt coverage ¹⁾	2.6x	2.0x
Debt coverage adjusted ²⁾	2.0x	1.9x

¹⁾ Calculated as net debt divided by two times EBITDA of the first half year

²⁾ Calculated as net debt adjusted divided by two times EBITDA adjusted of the first half year