Financial review

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Group financial review

- Full year revenue of €3.13 billion with an acceleration in fourth quarter revenue growth
- Platforms & Services revenue exceeded €1 billion, a year ahead of the current multi-year development plan
- Company gross margin increased by +185 basis points, to 40.5%
- Profit from operations grew to €453 million with strong free cash flow of €318 million, leading to net debt of €67 million

Basis of preparation of financial information

Segment information
The Mobile segment reports on businesses associated with mobile cellular technologies including Machine-to-Machine, mobile secure elements (SIM, embedded secure element) and mobile Platforms & Services. The Payment & Identity segment reports on businesses associated with secure personal interactions including Payment, Government Programs and Enterprise. The SafeNet acquisition in 2015 is part of the Enterprise business. In addition to this segment information the Company also reports revenues of Mobile and Payment, & Identity by type of activity: Embedded software & Products (EAP) and Platforms & Services (P&S).

Historical exchange rates and constant currency figures
The Company sells its products and services in a very large number of countries and is commonly remunerated in other currencies than the Euro. Fluctuations in these other currencies exchange rates against the Euro have in particular a translation impact on the reported Euro value of the Company revenues. Comparisons at constant exchange rates aim at eliminating the effect of currencies translation movements on the analysis of the Group revenue by translating prior-year revenues at the same average exchange rate as applied in the current year. Revenue variations are at constant exchange rates and include the impact of currencies variation hedging program, except where otherwise noted. All other figures in this press release are at historical exchange rates, except where otherwise noted.

Adjusted income statement and profit from operations (PFO) non-GAAP measure
The consolidated financial statements are prepared in accordance with the International Financial Reporting Standards (IFRS) and with section 2:362(9) of the Netherlands Civil Code. To better assess its past and future performance, the Company also prepares an adjusted income statement where the key metric used to evaluate the business and make operating decisions over the period 2010 to 2017 is the profit from operations (PFO).

PFO is a non-GAAP measure defined as IFRS operating profit adjusted for: (i) the amortization and depreciation of intangibles resulting from acquisitions, (ii) restructuring and acquisition-related expenses, (iii) all equity-based compensation charges and associated costs; and (iv) fair value adjustments on business acquisitions. These items are further explained as follows:

- Amortization and depreciation of intangibles resulting from acquisitions are defined as the amortization and depreciation expenses related to the intangibles recognized as part of the allocation of the excess purchase consideration over the share of net assets acquired.
- Restructuring and acquisitions-related expenses are defined as: (i) restructuring expenses which are the costs incurred in connection with a restructuring as defined in accordance with the provisions of IAS 37; (ii) reorganization expenses defined as the costs incurred in connection with headcount reduction, consolidation of manufacturing and offices sites; (iii) the rationalization and harmonization of the product and service portfolio; and the integration of IT systems, consequent to a business combination; and (iv) transaction costs (such as fees paid as part of the acquisition process).

- Equity-based compensation charges are defined as (i) the discount granted to employees acquiring Gemalto shares under Gemalto Employee Share Purchase plans; (ii) the amortization of the fair value of share options and restricted share units granted by the Board of Directors to employees, and the related costs.
- Fair value adjustments over net assets acquired are defined as the reversal, in the income statement, of the fair value adjustments recognized as a result of a business combination, as prescribed by IFRS3. Those adjustments are mainly associated with (i) the amortization expense related to the step-up of the acquired work-in-progress and finished goods assumed at their realizable value and (ii) the amortization of the cancelled commercial margin related to deferred revenue balance acquired.

These non-GAAP financial measures are not meant to be considered in isolation or as a substitute for comparable IFRS measures and should be read only in conjunction with our consolidated financial statements prepared in accordance with IFRS.

In the adjusted income statement, Operating Expenses are defined as the sum of Research and Engineering expenses, Sales and Marketing expenses, General and Administrative expenses, defined as the sum of Research and Engineering expenses, Sales and Marketing expenses, General and Administrative expenses, and Other Income (expense) net. EBITDA is defined as PFO plus depreciation and amortization expenses, excluding the above amortization and depreciation of intangibles resulting from acquisitions.

Net debt and net cash
Net debt is a non IFRS measure defined as total borrowings net of cash and cash equivalents. Net cash is a non-IFRS measure defined as cash and cash equivalents net of total borrowings.
## Adjusted financial information

### Extract of the adjusted income statement

<table>
<thead>
<tr>
<th></th>
<th>Full year 2016</th>
<th>Full year 2015</th>
<th>Year-on-year variations at historical exchange rates</th>
<th>Year-on-year variations at constant exchange rates</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>€ in millions</td>
<td>As a % of revenue</td>
<td>€ in millions</td>
<td>As a % of revenue</td>
</tr>
<tr>
<td>Revenue</td>
<td>3,126.5</td>
<td></td>
<td>3,121.6</td>
<td></td>
</tr>
<tr>
<td>Gross profit</td>
<td>1,266.2</td>
<td>40.5%</td>
<td>1,215.9</td>
<td>39.0%</td>
</tr>
<tr>
<td>Operating expenses</td>
<td>(813.5)</td>
<td>(26.0%)</td>
<td>(792.3)</td>
<td>(25.4%)</td>
</tr>
<tr>
<td>EBITDA</td>
<td>593.5</td>
<td>19.0%</td>
<td>566.9</td>
<td>17.5%</td>
</tr>
<tr>
<td>Profit from operations</td>
<td>452.7</td>
<td>14.5%</td>
<td>422.6</td>
<td>13.5%</td>
</tr>
<tr>
<td>Net profit</td>
<td>266.9</td>
<td>8.5%</td>
<td>303.5</td>
<td>9.7%</td>
</tr>
<tr>
<td>Basic earnings per share (€)</td>
<td>3.00</td>
<td>3.45</td>
<td>(13%)</td>
<td></td>
</tr>
<tr>
<td>Diluted earnings per share (€)</td>
<td>2.97</td>
<td>3.41</td>
<td>(13%)</td>
<td></td>
</tr>
</tbody>
</table>

### Adjusted financial information

The consolidated financial statements are prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union. To better assess its past and future performance, the Company also prepares an adjusted income statement.

Total revenue for 2016 came in at €3,127 million, up +1.2% at constant exchange rates and stable at historical exchange rates.

In 2016, currency translation effects generated a (1) percentage point effect on revenue generation. The hedging program which aims at partially neutralizing the impact of currency variations on the Company’s profit from operations, produced a 0.3 percentage point difference in revenue in comparison to last year.

Gross profit was up by €50 million, to €1,266 million, representing a gross margin of 40.5%, up +155 basis points year-on-year. The two main segments recorded gross margin improvement that more than offset the decrease in the Patents & Others segment.

Operating expenses were up by 61 basis points to 26% of revenue, at (€814) million. This increase came mainly from the investments made in the Enterprise business as mentioned in the first semester.

As a result, profit from operations was €453 million, up €30 million year-on-year. Profit margin from operations increased +94 basis points to 14.5% compared to 13.5% in 2015.

Gemalto’s financial income was (€34) million compared to (€38) million for 2015. Interest expense and amortized costs on the public bond, private placements and credit lines facilities were (€0.2) million lower, at (€12) million in 2016 while foreign exchange transactions and other financial items amounted to (€20) million versus (€24) million a year ago, mainly due to currency variation impacts.

Share of profit in associates was €2 million for the full year 2016, stable compared to 2015. Net impairment of associates recorded (€21) million in 2016, versus nil in 2015, mainly due to the change in market capitalization of an associate.

As a result, adjusted profit before income tax and net impairment of associates came in at €420 million compared to €387 million the previous year, an increase of +9%.

Adjusted income tax expense increased to (€133) million, compared to (€83) million the previous year. This (€49) million expense increase mainly reflects the estimated non-cash deferred tax asset reduction following Gemalto’s 2017 profit from operations outlook.

Excluding this non-recurring impact, the effective tax rate for the Company would have been 20% this year. This 2016 exceptional charge has no impact on the expected normative effective tax rate going forward.

As a result, the 2016 adjusted net profit for the Company was €267 million, leading to adjusted basic earnings per share of €3.00, and adjusted diluted earnings per share of €2.97 compared to adjusted basic earnings per share of €3.45, and adjusted diluted earnings per share of €3.41 in 2015.
As a result, Gemalto recorded an increase of €144 million in its IFRS operating profit (EBIT), at €347 million in 2016 compared to €203 million a year ago. This performance mainly reflects the increase in operating profitability, the marginal effect of the non-cash IFRS fair-value adjustments related to SafeNet’s pre-acquisition deferred revenue in 2016 and the decrease in restructuring & acquisition-related expenses.

The income tax charge increased to (€107) million compared to (€31) million the previous year. This increase in expense mainly reflects the estimated non-cash deferred tax asset reduction following Gemalto’s 2017 profit from operations outlook.

Consequently, IFRS net profit increased by +36% at €186 million for 2016 versus €137 million in 2015.

Overall, IFRS basic earnings per share and diluted earnings per share came in at €2.09, up +34% and €2.07, up +34% in 2016, compared to €1.56 and €1.54 respectively in 2015.
As a result, in 2016 Gemalto generated strong free cash flow of €318 million increasing by +87% compared to €170 million in 2015. Acquisitions used (€3) million in 2016 versus (€897) million in 2015 which had seen the closing of both the SafeNet and Trüb acquisitions.

Gemalto’s share buy-back and liquidity programs generated a €1 million net cash inflow in 2016. As at December 31, 2016, the Company held 717,835 shares i.e. 0.8% of its own shares in treasury. The total number of shares issued increased by +920,930 in 2016 to 89,928,639 and, net of the 717,835 shares held in treasury, 89,210,804 shares were outstanding as at December 31, 2016. The average acquisition price of the shares repurchased on the market by the Company and held in treasury as at December 31, 2016 was €40.46.

On May 26, 2016, Gemalto paid a cash dividend of €0.47 per share in respect of the fiscal year 2015, up +12% on the dividend paid in 2015. This distribution used €42 million in cash.

Net proceeds from financing activities generated a (€14) million cash outflow, mainly coming from commercial paper repayment. Cash in hand, net of bank overdrafts amounted to €663 million versus €405 million at the end of 2015.

Considering the €730 million total amount of borrowings as at December 31, 2016, Gemalto’s net debt position was reduced to €67 million compared to a net debt position of €335 million at the end of 2015. This significant (€268) million variation is due to the strong free cash flow generated by the Company over the last twelve months. The Company net debt currently represents 0.1 times its EBITDA.

Outlook
For 2017, Gemalto expects its profit from operations to be between €500 million and €520 million supported by positive trends in Government Programs, Machine-to-Machine, Enterprise and taking into account the adverse mobile environment and slower migration of payment cards in the United States.

The Company expects to finalize the acquisition of 3M Identity Management business in the first semester of 2017 and will update its 2017 outlook after the closing.

<table>
<thead>
<tr>
<th>Statement of financial position and cash position variation schedule</th>
</tr>
</thead>
<tbody>
<tr>
<td>For the full year 2016, operating activities generated a cash flow of €468 million before changes in working capital, up +6%, compared to the €443 million generated in 2015. Change in working capital reduced the cash flow generation by €(23) million in 2016 compared to a positive €65 million impact in 2015. Net trade and other payables reduced due to advance payments received from customers in 2015. Net trade receivables increased towards the end of the year with the growth in Government Programs, Machine-to-Machine and Enterprise. Capital expenditure and acquisition of intangibles amounted to (€140) million, i.e. 4.5% of revenue compared to 5.9% in 2015. Property, Plant, and Equipment accounted for (€63) million in 2016, lower by (€35) million compared to the high level of 2015 that was related to initial investments made to support the strong start in payment business in the United States. Acquisition and capitalization of development expenses represented (€77) million, with capitalization of development expenses representing 2.0% of revenue in 2016.</td>
</tr>
</tbody>
</table>

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Segment financial review

**Revenue by segment**

1. Payment & Identity 62%
2. Mobile 38%
3. Patents & Others 0%

**Full year 2016**

<table>
<thead>
<tr>
<th>(€ in millions)</th>
<th>Payment &amp; Identity</th>
<th>Mobile</th>
<th>Total including Patents &amp; Others</th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenue</td>
<td>1,948</td>
<td>1,174</td>
<td>3,127</td>
</tr>
<tr>
<td>As a percentage of total revenue</td>
<td>62%</td>
<td>38%</td>
<td>100%</td>
</tr>
<tr>
<td>Gross profit</td>
<td>793</td>
<td>471</td>
<td>1,266</td>
</tr>
<tr>
<td>Profit from operations</td>
<td>290</td>
<td>171</td>
<td>453</td>
</tr>
</tbody>
</table>

**Segment information**

Revenue variations are expressed at constant currency exchange rates unless otherwise noted.

During the fourth quarter, revenue expanded by +3% at constant exchange rates and historical exchange rates. The Payment & Identity segment grew by +8% in the fourth quarter. The strong performance of Enterprise and Government Programs during the fourth quarter more than offset lower sales in Payment. Mobile segment revenue was lower by (2%) in the fourth quarter compared to 2015. In that segment, the sales trend improved compared to the first nine months of 2016, with a slower decrease in SIM sales and +13% expansion in the Machine-to-Machine business as well as in the Mobile Platforms & Services activity.

Overall, the diversification of the Company has again been reinforced in 2016 with Payment & Identity now accounting for 62% of the Company revenue, compared to 58% last year.

In 2016, Embedded software & Products revenue decreased by (3%) mainly due to lower SIM sales to mobile network operators and payment cards revenue in China. Platforms & Services exceeded the €1 billion mark one year ahead of the current multi-year development plan, to represent 33% of total Gemalto revenue in 2016. The expansion in the Platforms & Services activity has been supported by a double-digit growth in each of the Payment & Identity segment’s businesses while the Mobile Platforms & Services activity grew by +3% over the year.

Full year profit from operations increased by +7% year-on-year. In 2016, the Payment & Identity segment recorded a +22% increase in profit from operations and the Mobile segment profit from operations was lower by €1 million compared to 2015. This performance was driven by the gross margin improvement in the two main segments which largely offset the operating loss from the Patents & Others segment.
The digital age is creating seemingly limitless opportunities to deliver services more conveniently and efficiently. At the same time it also creates ever greater demand for the protection of data and identities, to provide trust, authenticate people and combat fraud.

Payment & Identity

Payment & Identity’s full year revenue came in at €1,948 million, increasing by +9% at constant exchange rates compared to 2015. The segment’s Embedded software & Products sales were up by +3% at €1,180 million and its Platforms & Services sales were up by +19% to €768 million.

The Payment business came in at €998 million, up by +2% in 2016 versus 2015 with moderate revenue growth in both the Americas and the Europe, Middle East & Africa regions. The lower sales in China were fully offset by an increase in revenue from the rest of Asia. In 2016, performance was contrasted between the semesters with second semester revenue lower year-on-year due to the high comparison basis in the United States related to the 2015 EMV liability shift deadline. Payment Embedded software & Products sales were lower by (4%) and Payment Platforms & Services revenue expanded by +24% compared to 2015.

Revenue from the Enterprise business came in at €462 million in 2016, up +10% when compared to 2015. The trend in revenue mix within the authentication business line continues to move towards a higher proportion of software and services. The Enterprise business increased its sales coverage expanding Gemalto’s network of technology partners. It also accelerated investment in its R&D in order to strengthen the Company’s offering to meet increasing market demand for cybersecurity solutions.

Revenue from the Government Programs business came in at €488 million, up +26% at constant exchange rates compared to 2015. Government Programs posted an outstanding fourth quarter revenue performance with the completion of a large scale project and increased deliveries from the finalized transformation of a production site. Government Programs Embedded software & Products revenue was up +21% and Government Programs Platforms & Services sales were up +39% in 2016 compared to 2015.

The Payment & Identity segment’s gross margin improved to 40.7%, up +2.3 percentage points compared to 2015, with the optimization of the Payment business and the expansion of the Enterprise business.

Operating expenses grew to (€503) million in 2016, in large part due to investments made in the Enterprise business as well as the shift of internal resources to this segment in order to capture the market growth of Government Programs.

As a result, profit from operations in Payment & Identity came in at €290 million, up +22% from the €239 million recorded in 2015, leading to a 14.9% profit margin from operations, up +1.8 percentage points.
Piloting digital drivers’ licenses in the US

Through a grant awarded by the U.S. National Institute of Standards and Technology (NIST), Gemalto is partnering with Colorado, Idaho, Maryland and Washington D.C. to pilot digital drivers’ licenses (DDL) in these jurisdictions. Building on a common need for trusted infrastructure, the pilot responds to the growing trend towards consumer mobility and digital dependence, especially among those aged 18–29. Serving as a companion to the physical ID card, this interoperable, smartphone-based solution will address enrollment, document updates, attribute sharing and law enforcement.

How Norway’s post office is getting instant ID verification all wrapped up

How do you counter identity fraud? Norway’s national post and logistics service will soon be able to, using our ID verification technology. Specialized scanners will enable branch staff to detect if an ID document is genuine by instantly checking it against our global database. Using our secure solution Norway’s national post will become a trusted third party, verifying customer identities for banks and other service providers in the country.

Cloud-based mobile payment supporting Apple Pay in Japan

Gemalto and Dai Nippon Printing (DNP) are providing a cloud-based payment service supporting Apple Pay. This service provides credit, debit and prepaid card companies with a cloud-based payment solution to deploy highly secure payment with smartphones thanks to a tokenization technology which replaces a credit card number with a surrogate number. Major credit card issuers have announced their participation in Apple Pay, so they can offer their customers this convenient and private way to pay.
**Segmental review**

**Mobile**

Mobile connectivity is bringing consumers a convenient digital life, wherever they go. Services are proliferating on the devices they carry every day. Machines too, are increasingly connected in the rapidly expanding Internet of Things (IoT).

<table>
<thead>
<tr>
<th>Revenue</th>
<th>Gross margin</th>
<th>Profit from operations</th>
<th>Profit margin operations</th>
</tr>
</thead>
<tbody>
<tr>
<td>€1,174m</td>
<td>40.1%</td>
<td>€171m</td>
<td>14.6%</td>
</tr>
<tr>
<td>2015: €1,279m</td>
<td>up +1.4 percentage points</td>
<td>2015: €172m</td>
<td>up +1.1 percentage points</td>
</tr>
</tbody>
</table>

The Mobile segment recorded annual revenue of €1,174 million, (8%) lower year-on-year at constant exchange rates and historical exchange rates.

Embedded software & Products revenue for the segment came in at €924 million, (11%) lower compared to 2015 at constant exchange rates. SIM sales decreased by (19%) at €605 million for 2016. This was mainly due to the tail-end effect of the closure of a mobile payment venture in the United States, coupled with lower demand in Latin America and Africa. Conversely, the Machine-to-Machine business continued to grow, by +11% year-on-year, at €319 million on the back of expanding global demand of connected devices and embedded secure elements for the Internet of Things (IoT).

Platforms & Services revenue for the segment came in at €251 million, up by +3%. In 2016, Gemalto’s Mobile Subscriber Services business reached important milestones with more than 20 references on embedded SIMs remote activation and management. Gemalto is deeply involved in setting up the ecosystem, as device manufacturers and mobile network operators adopt the GSMA specifications for the consumer device market published in the fourth quarter of 2016.

Gross margin for the Mobile segment was 40.1% in 2016, up by +1.4 percentage points compared to 2015. Operating expenses decreased to €300 million from €322 million in line with the trend observed in the first semester of 2016 due to the shift of part of the segment’s resources to the growing Payment & Identity segment.

As a result, profit from operations came in at €171 million, i.e. a 14.6% profit margin from operations, up +1.1 percentage points on 2015.
Orange teams up with Gemalto and Samsung to launch the first smartwatch that’s also a phone

Now you can leave your smartphone at home. This Samsung smartwatch has a built-in eSIM that allows you to receive calls, messages and app notifications synchronized with your phone – wherever your phone may be. To launch the watch in France, Orange chose Gemalto to provide the secure solution that makes all this possible.

Connecting cars throughout their life-cycle

Gemalto is fitting PSA Group’s next generation of connected cars with its On-Demand Connectivity solution, giving the group, which includes Peugeot, Citroën and DS, complete flexibility over subscription management throughout the automotive life-cycle. The solution, which can be deployed across all models and regions, allows the automobile manufacturer to customize connectivity packages to different customer and market needs around the world, as well as manage their fleet and software updates remotely.

Securing China’s IoT market

Gemalto has teamed up with Alibaba to provide connectivity and security for YunOS, Alibaba’s cloud-based data and services-oriented IoT operating system which connects cars, smart homes and mobile devices all across China and other regions. Our trusted solution allows easy provisioning of security sensitive applications throughout the identity life-cycle management, creating a uniform identity framework for disparate IoT applications.