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Transcript :: NKT Interim Report Q3 20.11.2013 ::

Welcome to NKT's webcast for the third quarter 2013. My name is Michael Lyng, Group Executive Director and CFO of NKT Holding. Today we introduce a new structure for our webcast by including CEOs from the business units. In the future, the CEO Marc van't Noordende from NKT Cables and Jonas Persson who will be joining Nilfisk-Advance in January 14 will assist me in these presentations. The reason for the change is identical to the main reasoning behind the new NKT governance structure that was announced back in August this year. But as Jonas has not yet joined the group only Marc is with me during today's call so welcome Marc. Let us start off turning to page 3. The agenda for today follows our usual formats. First I will cover some general highlights followed by a walk-through of the financial results for the third quarter 2013. Then Marc will bring an update on NKT Cables covering some numbers as well as key operational highlights from the third quarter. After that I will cover the two other business units, Nilfisk-Advance and Photonics Group. And finally an update on expectations for the full year 2013 followed by a Q&A session. But let us go directly into the highlights on page 4. Overall, the third quarter developed on a par with our internal expectations both on revenue and earnings. In NKT Cables we completed the acquisition of Ericsson's energy cable business adding roughly DKK 300 million to the nominal revenue in the quarter. Organically, we still see a diverse picture in the European cable market with high voltage onshore and offshore acting as the solid base while construction and medium voltage segments are still under severe pressure. Growth in China continued with the anticipated back to normal situation in the railway business. We have started up a programme focusing on improving earnings by reducing costs and improving efficiency. Marc will come back on this later on. Nilfisk-Advance continues to gain market share with 7% organic growth. Especially EMEA and Americas are pooling the growth, much in line with the picture we saw in the second quarter. In Asia-Pacific the negative trend has reversed and now also contributes positively to organic growth. Profitability remains relatively flat despite pressure on gross margins but that has been compensated by lower overhead costs. I will come back to this later in the presentation. Photonics Group continued to grow now realising 25% organic growth. Both the Imaging and Sensing segments are showing the potential that we strongly believe in. The overall development across the Photonics Group is okay in light of lack of performance within fibre processing which we now have initiated to turn around but I will also come back to this later on.

Let us go into the financial results on page 6. Total revenue at market prices came in at DKK 4.1 billion corresponding to organic growth of 3% in quarter-on-quarter and 4% year-to-date. We realised 7% nominal growth due to the Ericsson acquisition. Year-to-date revenue totals DKK 11.6 billion versus DKK 11.3 billion in the same period last year. NKT Cables realised -2% organic growth, Nilfisk-Advance 7% and Photonics Group 25% in the third quarter. Year-to date positive growth across all business units, 4% in Cables, 4% in Nilfisk-Advance and 11% in Photonics Group. More details later on.

Q3 Operational EBITDA reached DKK 257 million versus DKK 251 million in the third quarter 2012. This corresponds to a slight decline in margins from 8.3% in the third quarter 2012 to now 7.8%. As mentioned very much in line with expectations. Year-to-

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date EBITDA reached DKK 753 million compared to DKK 719 million in the prior year. Margins year-to-date are 8% which is also in line with last year.

Working capital is unchanged in absolute numbers from the second quarter at DKK 3.3 billion but should be seen in relation to the addition of around DKK 150 million related to the Ericsson acquisition. All in all a slight decline from 19.9 % in the second quarter to 19.8% in the third quarter. Net interest-bearing debt ended at DKK 2.7 billion, similar to 2.6 x operational EBITDA for the last 12 months. Down a notch from the second quarter but also here it should be seen vis-à-vis the Ericsson acquisition that was paid during the third quarter. As a consequence, cash conversion went up to 77% in the third quarter compared to 47% at the end of the second quarter. Consistent with previous forecasts for the year, operational EBITDA is expected to be on par with 2012 if we look at the full year 2013. Based on revenue for the year's first nine months, organic growth for 2013 is now specified and expected to be around 2-4%.

Turning to the next slide, we see the trend in operational EBITDA on page 7. With Q3 Operational EBITDA of DKK 273 million [NKT correction: DKK 257 million in accordance with slides] the last 12 months' EBITDA amounted DKK 1,073 million thereby continuing the positive momentum that we have seen so far in 2013. Looking at EBITDA margins, these are more or less flat from 8.6% in the second quarter to 8.5 % in the third quarter.

As will be seen on the next slide the slight decline in margins can be ascribed to slightly lower margins in both Nilfisk-Advance and in NKT Cables. Turning to page 8. Comparing the third quarter 2013 to last year there are four things that are key to note. First, revenue has increased both in market and standard metal prices. DKK 305 million naturally relates to acquisitions but DKK 90 million is added from organic growth and then we are also negatively impacted by metal prices, with DKK 53 million, and FX changes, with DKK 81 million. Secondly, operational EBITDA is flat in absolute terms and hence a slight decline on the marginal level. This can be ascribed to NKT Cables which is down from 7% to 6.3% [NKT correction: 6.2% in accordance with slides] but still adding DKK 1 million. As we have more and more project business, it becomes more difficult to look at earnings in a single quarter. And on top we have the impact from adding revenue related to Ericsson.

Looking at Nilfisk, we are down from 10.4% to 10.0% losing DKK 2 million. A small note to add here is that DKK 15 million in cost are considered somewhat extraordinary and will not recur and on top we are also negatively impacted from FX, for example from a lower US dollar this year compared with last year. This has a translation impact of around DKK -5 million. Photonics Group and Holding showed an improvement of DKK 7 million, mainly because of savings in Holding.

Thirdly, we have significantly lower financial items, mainly as a result of reduced interest-bearing debt which can be seen if you compare the DKK -44 million last year to DKK -36 million realised in the third quarter this year.

Finally, worth noting as mentioned in the earlier presentation, Capex is a key focus area after years of significant investments and now returning to a more normal level.

On the next slide you can see the same picture, but on a year-to-date basis, on page 9. Seen on an aggregated level, year-to-date looks quite the same as in the third quarter alone. Yet some key differences stand out. NKT Cables realised 4% organic growth and expanded the EBITDA margin with 0.3 % to 5.1 % which combined added DKK 29 million to the EBITDA. Nilfisk-Advance also adding 4 % organic growth but experienced a slight decline in Margin leaving the EBITDA more or less on par, up by DKK 6 million.

Also on year-to-date Capex is significantly lower than in the same period in 2012 going down 21% to DKK 319 million in 2013 compared to DKK 407 million in 2012.

If we add that up we have improved cash conversion in the third quarter significantly as can be seen from the following slide, page 10. The cash conversion rate developed positively from 47% in the second quarter 2013 to now 77% realised in the third quarter measured on the basis of the last 12 months.

Outside the key drivers, EBITDA and Capex, that we covered on the past two slides, working capital levels are important so let us look closely at the working capital on page 11. Working capital remained at approximately DKK 3.3 billion in the third quarter. Yet comprised of declining working capital levels of DKK 172 million on existing activities but an increase of DKK 153 million in working capital related to the Ericsson acquisition. This results in a decline of 0.1% from 19.9% in the second quarter to 19.8% in the third quarter.

NKT Cables succeeded in lowering levels from 20.3% to 20.0% since the second quarter, mainly caused by improvement in payables and some reduction in inventory.

Nilfisk-Advance kept it unchanged at around 19.0%.

Turning to the next page, we can see the absolute change in working capital tie-up year-to-date on page 12. Working capital tie up has increased from the beginning of the year but with understandable reasons. Nilfisk-Advance started at a low level at the end of 2012 and in addition the growing business naturally requires additional working capital funding. Not shown here, but all key parameters in inventories, receivables and payables have moved in the right direction when, for example, you look into number of days of tie-up in the single areas. NKT Cables has increased the working capital level by DKK 636 million, mainly related to two elements. Firstly, the project division had large payments on projects just before year-end 2012. Up-front payments are normal in the beginning of the project life cycle and we are now normally also able to keep negative working capital during the project execution. We are now in the situation that several projects are getting close to full completion. And the final payments are pending, which in turn requires working capital funding in the final stage. Secondly, the Ericsson acquisition added net working capital of DKK 153 million, which was of course expected.

The next page shows the full picture on the free cash flow for the third quarter and year-to-date, turning to page 13. Free cash flow from operating and investing activities of DKK 30 million in the third quarter, so all in all a relatively strong cash flow in the third quarter. We consider that as being satisfactory considering the acquisition of businesses with DKK 230 million. Working capital impacted cash flow positively with DKK 193 million making cash flows from operations total DKK 356 million which is much better than last year. Also notable, the low working capital level in December 2012 is visible in year-to-date changes where additional funds of DKK 619 million were tied up during the first nine months. All in all we cannot be fully satisfied with a negative free cash flow of DKK 726 million during the first nine months. However, a big part of it follows the nature and seasonality of our businesses and we expect further decreases in working capital during the fourth quarter thereby improving the free cash flow for the full year.

Let us move into the position for net interest-bearing debt on page 14. Net interest-bearing debt amounted to DKK 2.7 billion by the end of the third quarter reducing the financial leverage from 2.7x Operational EBITDA at the end of the second quarter to now 2.6x Operational EBITDA by the end of the third quarter. As can be seen, the gap towards reaching the internal target of max. 2.5x Operational EBITDA is closing and we are well within the range of our other internal targets for an optimal capital structure.

We are constantly monitoring our financial leverage as the previous example of the project business in Cables clearly showed it is very important that we maintain our financial flexibility with a yearly swing factor in working capital of up to a range of around DKK 1 billion.

Let us look into our cash resources available on the next slide, page 15. Taking a brief look at credit facilities we have sufficient funds to support our strategic objectives but it also allows us to maintain a longer-term focus and perspective on value creation. Last comment, we are currently in the process of refinancing approximately DKK 1 billion committed debt portion below 1 year that you can also see in the blue column on the slide. That will bring our committed cash resources to approximately DKK 5.7 billion expected at year-end. We still expect to be able to be in a position with a committed debt structure without any financial covenants after the refinancing round.

That completes the first part of the presentation and by that I would like to hand it over to you Marc.

16.10

Marc van't Noordende

Thank you, Michael, I would then move on to page 18 where you see our sales mix by field of application, by geography and by customer segment. Mind you that these data are the 2012 data so they should not show any change for you. Obviously, we will update these data by year-end or for full year 2013 and that will then also reflect, of course, the addition of the power cable business of Ericsson in the middle of the graph. If I move to page 19 and the financial highlights as already mentioned by Michael we have seen negative organic growth of 2% in the third quarter but year-to-date organic growth of 4%. Nominally, our growth was 13% realised thanks to the acquisition of the Ericsson power cable activities. The electricity infrastructure declined 11% compared to the third quarter of last year. The positive trend within high voltage particularly offshore, which also by the way yielded a very high utilisation rate in the Cologne factory and we also did a lot of offshore installation work, this positive trend was not enough to offset the challenging European markets within the medium voltage segment. It varies a little bit by European country but by and large in Europe the utility companies have over the last two years pulled the brakes on their investment programmes and this trend has accelerated this year and particularly the medium-voltage segment has seen the consequences of that. Our railway business continued the positive trend for the first half of the year but you have to indeed realise that we compare against last year, which was a very low year due to the fact that there was a moratorium in new construction in the Chinese railway segment. Construction in Europe remains also a very tough market. Q3 showed some signs of some stabilisation with only -2% growth but we are still 12% down on a year-to-date basis compared to 2012. The automotive market showed positive growth in the segment with 12% and that brings our volumes this year very close to last year's performance but here I can make the same comment. Also last year we were not satisfied with our performance in this segment. All in all our third quarter EBITDA yielded DKK 103 million versus DKK 102 million in prior year so pretty much flat. Our margin at standard prices was down from 7 to 6.2%, which really reflects the significant price pressure that we see both in European and in the Chinese markets. Looking therefore at the big picture we can only say that we are not satisfied with the earnings of our company. And based on the diverse performance picture within different segments but also based on an outlook that for certain segments does not bring any signs of immediate recovery we have decided to start a substantial cost reduction programme to secure earnings improvement and to secure our long-term competitiveness. We will give you a more detailed update on this programme further down in the future.

If I move to page 20, as stated we have a slight organic decline in the third quarter compared to the third quarter 2012. In absolute numbers though, the Ericsson activities add substantial revenue to our business generating nominal growth of 13% for the quarter. Talking about that acquisition the post-merger integration process is fully up and running and is on schedule. We have reconfirmed the strong fit between the original NKT Cables business in the Nordic market and the acquired assets in Sweden. We have made a post-acquisition validation of our business case and this has affirmed our belief in the synergy potential between the two companies. We will follow up on this subject and give you more details at a later point in time. As mentioned we have intensified our cost saving initiatives. To give you some initial insight into this programme, this is not about some smaller twigs, this is not about some smaller modifications to our cost structure. We intend to have a very fundamental look at our cost structure and to fundamentally drive our cost structure down to secure our long-term competitiveness. In a final initiative that I want to mention – and I have mentioned it before – is safety. In 2012 we had an accident frequency rate of 22 that is 22 accidents per 1 million hours worked. Over the 12-month period of the last six months of 2012 and the first six months of 2013 this frequency rate was reduced to 8 thanks to many initiatives taken throughout our organisation in all of the countries and sites that we operate. Of course, we are not satisfied with that performance. Our medium-term target is smaller than 5, a frequency rate smaller than 5, but our long-term target remains a zero accident target. Not only do we feel that we have a clear moral obligation to ensure a safe working environment for employees and our guests at our sites but we also believe that it provides common sense and it will provide clear financial results and we believe that a structurally profitable business can only come with a structurally safe company. Finally, before I turn the microphone back to Michael again, a brief note on the statement of objections. We have updated our expectations on the timing of a decision by the European Commission and we now believe that the decision will be pending over the coming six months. We have not at this moment in time changed any other views that we have on this matter. With that said I will hand it back over to you again, Michael.

22.46.5

Michael Lyng

Thank you, Marc, for the presentation. I will now take you through Nilfisk-Advance starting on page 22 where we have more or less the same overview as Marc just described on the Cables side. First a quick note here. I guess that you are all familiar with the structure. One red dot has been added and that is our newly established sales company in Romania so that we now have sales companies in 45 countries worldwide. Turning to page 23 as mentioned before Nilfisk-Advance achieved organic growth of 7% in the quarter and especially gained market shares in the EMEA region with 8% organic growth. Americas have also shown 7% growth in the quarter which was also to a large extent driven by the industrial customer segments. APAC is back with 4% organic growth after a slow start of the year. This growth was mainly driven by Japan and Korea but signs of improvements also emerged in the important Chinese and Australian markets. Looking at peer we are satisfied with our performance and we are particularly happy with the fact that we continue to take market share in Europe with 8% organic growth in the third quarter and 5% year-to-date compared with -6% and -9%, respectively, for peer. EBITDA was DKK 156 million in the quarter compared to DKK 158 million for the same period last year. Included in this is DKK 15 million in cost that we consider extraordinary and we are also negatively impacted by approximately DKK 5 million from FX but overall we are satisfied that we have been able to maintain earnings as gross margins are negatively impacted primarily from a different product mix. However, constant focus on optimisation and lower overhead costs has mitigated the gross profit pressure and I will talk more about this later on. Operational EBITDA margin at the end of the third quarter only declined a little bit but is still in the range of what has been achieved in the past years.

If we turn to page 24, some more highlights – as pointed out we are satisfied with the organic growth in the third quarter and the fact that we have gained market share, which was most clear in Europe. The strong growth we see is linked to the strong distribution and service organisation that we have set up over the last years in addition to the benefit from strong customer relations where we have seen increased customer satisfaction recently. I have already commented on Americas, however, I would like to emphasise that Latin America is showing a positive sales trend, in particular in Mexico where we also have established a production facility some years back. There was growth of 4% in the APAC region in the third quarter where things seem to be moving in the right direction in the Chinese markets. Gross margin and fixed costs I will come back to shortly. On the product side I want to mention our newly introduced stand-on wet and dry rack, the VL500. It has already received two awards for innovative design and functionality. We see this as a result of our effort invested each year in R&D. We continue to spend a little more than 3% of turnover developing new products and expect to introduce more than 30 new products in 2013. Finally, just to mention that Jonas Persson will join as CEO for Nilfisk-Advance as of mid-January 2014. We are looking very much forward to starting working with Jonas and at the same time I would like to thank Jørgen Jensen for years of outstanding contribution to where Nilfisk-Advance is today and also for being available to Jonas in a transition period to ensure seamless handover.

Turning to page 25 looking at our gross profit. Coming back to this Nilfisk is seeing a negative trend in our reported gross margins coming mainly from a natural consequence of changes in sales mix but we also see some price pressure here and there in the markets. This is not unique to Nilfisk-Advance and we believe that customer focus on price is increasing due to the economic climate. We are constantly focusing on margins and have several initiatives ongoing to mitigate the development going forward.

Turn to page 26, while losing a bit on the gross margin Nilfisk-Advance has succeeded in reducing fixed costs. As you can see the overhead cost percentage has gone from 33.3% to 31.9% of revenue in one year, quite impressive. Here there is of course a link to the change in product mix that is impacting the gross margin negatively. It is important that we make sure that we also have lower cost servicing the lower margin segments as for example for the do-it-yourself segment where less sales efforts and lower distribution costs are a fact, but it is also a result of our focused efforts the last years where we have worked on several initiatives with the aim of reducing fixed cost ratio to sales. That concluded the part for Nilfisk-Advance and I will now turn to Photonics Group.

If we turn to page 28, again a short overview and there are no changes since last reporting. Turning to page 29, Photonics Group continued the strong growth path by realising 25% organic growth and together with the strong second quarter year-to-date organic growth has reached 11% following a slow start of 2013. Both the Imaging and Sensing segments enjoy years of hard work on bringing frontier technologies outside the R&D environment into new application fields. For example supercontinuum laser to leading high-end microscopes together with blue chip manufacturers. Within Sensing the hard work has been focused on bringing distributed temperature sensing into broader industrial use with prime focus currently being on power cable monitoring and fire protection but a wide range of opportunities exist in other industries like the oil and gas industry. The Fibre Processing segment continued at a low activity level and although the recent downward trend has been stabilised it is still not performing okay. We have therefore decided to make a change in management by appointing Ed Connor, our former VP of Sales, now as being the CEO effective from 1 November 2013.

Turning to page 30, order intake in both Imaging and Sensing was very high and we believe this to be the outcome of the year-long focused sales efforts within both segments. Imaging has recently entered into a new development agreement with a leading player in the medtech industry. Furthermore, a large 12-month frame agreement was signed with a leading blue chip manufacturer within another field in the medtech industry. This all supports our firm belief that we are on the right track within the use of SuperK as light source in several high-end applications. In the Sensing segment we also continued the strong order intake and among other projects was the order for a fire detection system in a metro project in Asia. The oil and gas segment has yet to show the full potential which is a key strategic focus area.

By that we have covered now our three business units and I will now return to our expectations for the full year turning to page 32. In terms of revenue we now expect organic growth around 2-4% based on the first nine months' revenue. This does not include the effect from the Ericsson acquisition and adding that revenue at standard price is expected to be around DKK 13 billion and DKK 16 billion at market prices.

On an operational EBITDA level we maintain our view that this will be on par with last year's performance.

32.06

That is it for our presentation, and I will now turn to the Q&A. So operator, is there anybody online with a question?

32.17

Operator

Yes there is. Ladies and gentlemen, if you have a question for the speakers, please press 01 on your telephone keypad. Please hold until we have the first question. We have a question from Claus Almer from Carnegie. Please go ahead sir.

32.43

Claus Almer, Carnegie

Yeah, hi Michael. I have three questions. The first goes to Nilfisk. Should we going forward be more focusing on the EBITDA margin rather than the gross margin? That would be my first question.

32.59

Michael Lyng

You want an answer now or should we take all three?

33.02

Claus Almer

Yeah. One at a time.

33.04

Michael Lyng

Okay. Well, we should always be focusing on EBITDA because that is where we generate the cash flow to pay the bills, so EBITDA is key for us, but of course it is also important to look at the gross margin. But the development we are seeing now is not scary and we feel that we are still in full control and a large part of the gross margin decline is related to mixed changes.

33.31

Claus Almer

Okay, and then a second question to Nilfisk. You showed a chart with the fixed cost percentages and revenue that is declining. Should we expect that to continue or have you now found a new plateau?

33.47

Michael Lyng

We will continue to work on our fixed cost base and I think that there is still more to come, but of course it will be harder and harder to achieve further improvements but we expect that we will be able to reduce it further going into the future.

34.07

Claus Almer

Okay and then my third and final question. It is about your 2013 guidance. You are still guiding a flat EBITDA year-over-year despite that after nine months it is up 5% compared to the same period last year. Can you give some more flavour why it should be declining that much in Q4?

34.30

Michael Lyng

Well, Claus, you know that we are guiding EBITDA in the range of last year and that could be that we will be above last year. We are looking at plus/minus 10% variations here. The fourth quarter is looking okayish, we still have some risk factors in the fourth quarter, mainly related to our offshore business in the cable business where we are currently installing projects and thereby we are also exposed to weather conditions and that is why we do not want to change our guidance on EBITDA yet.

35.06

Claus Almer

Okay, Michael, thank you so much.

35.11

Michael Lyng

You are welcome.

35.20

Operator

We have a question from Patrik Setterberg from Nordea, please go ahead sir.

35.25

Patrik Setterberg, Nordea

Yes, hello, a couple of questions from my side. The first one is related to your current order book within submarine, cables and onshore high voltage cables. You are saying that you are going to have a high capacity utilisation at the Cologne factory for the remainder of this year. Could you please give an indication of how the situation is looking for 2014? That is my first question.

35.54

Michael

Well, maybe I should also answer that. Currently, we are only focusing on 2013 when we announce expectations so it is too early for us to be more firm on 2014 but I guess it is not a big surprise that we are depending on getting more visibility into 2014, in particular in the offshore segment where if we look at traditional high voltage business, now we are doing fine, we have more or less the same picture today compared to the same period last year.

36.30

Patrik Setterberg

Just because I saw an interview with you, Michael, on Ritzau, which I will quote you that you are seeing a satisfactory order backlog situation for a part of 2014 within high voltage and submarine cables.

36.48

Michael

Yes, but that is linked to the order that we also announced early on this year that resulted in more visibility, both for 2013, but also going into 2014.

37.03

Patrik Setterberg

Okay, thank you. My second question is regarding this cost programme you are going to carry out in the NKT Cables division. Could you come closer about the timing of when we will see the details? Is it going to be in connection with the Q4 result or are we going to see it earlier or later than this?

37.21

Michael

Currently we are working hard to get our arms around it and I do not want to be firm about when you should expect to receive communication on this, but latest in connection with the annual report for 2013.

37.39

Patrik Zetterberg

It seems like quite a big programme you are going to launch here, is it going to involve plant closure for instance?

37.48

Michael

I don't know, Marc, will you give a little bit more flavour on our thinking behind this?

37.51

Marc van't Noordende

We are certainly looking at all aspects of our cost structure and plant utilisation rates in the current economic environment, is of course a key concern. At this moment in time it is too early to make any further comment on whether this will lead to plant closures but there are no sacred cows and we are looking at everything that is possible, so I would like to leave it at that for this moment, but as Michael said latest at the occasion of the annual results we will come back with a full update on this.

38.23

Patrik Setterberg

Okay, thank you. And my last question, housekeeping question. Are you planning for structural costs in the fourth quarter as well?

38.33

Michael

Currently we are not planning with any structural costs, of course the work that is ongoing in Cables, it is a question mark how that will impact that line but most likely it will be more a 2014 issue.

38.47

Patrik Setterberg

Okay, thank you.

38.55

Operator

We have a question from Daniel Patterson from SEB. Please go ahead sir.

39.00

Daniel Patterson, SEB

Yes, good morning gentlemen. I have a couple of questions, first of all for Cables; I guess it is a question for Marc. When we look at the Q3 margin in Cables, it is obviously down quite a lot but a big part of that is the Ericsson power cable acquisition, I can see in note 3 how much it added both on earnings and top line, so if we exclude this part and then look at the underlying margin in Cables, excluding the effect of power cables, the margin in Cables is still down from 7% to 6.4% year-on-year, so my question is which segment is really hitting you here? Is it that pricing is worse in a specific segment or is it more the negative organic growth that is hitting you sort of on an operating leverage? Any flavour here would be helpful, Marc.

39.52

Marc van't Noordende

Yeah, if we exclude our project business for which it is always difficult to talk about gross margin percentages, but if we look down into all of our other product segments it is basically across the board that we see very much price pressure, both in our European markets as well as in China. So it is an effect of market demand being reduced and competition increased and intensified.

40.17

Daniel Patterson

Okay. And maybe I could add onto that, I noticed that you stated in the report that you have lower low voltage and medium voltage sales in the third quarter, and that had a negative effect on earnings. I just want to clarify here, normally I would think that low voltage and medium voltage sales have low margin and a part of the lower margin segments in your business and hence that should be a positive mixed effect. Am I wrong in thinking about this?

40.48

Marc van't Noordende

I think it is a good question but I think my answer is that we are normally not a price fighter, so we try to maintain our margins as much as we can even in the traditional commodity segments of our business of [...] and we try to protect our margin as much as possible, so as I said earlier, it is more an effect across the board, across all product ranges that we see that margin decrease.

41.19

Daniel Patterson

Okay. And then a final question on Cables, it is on the railway segment, obviously you are growing massively on a low base here. The question is just on profitability in railway in China. Is that coming back to let's say 'the good old days' or how are you seeing the profitability in the railway segment in China?

41.38

Marc van't Noordende

What is true for a lot of segments in China also is true for the railway segment, that we see the number of competitors increasing and some of them have been held by the moratorium which allowed them to make their investments and to be ready for when the market picks up again, so what we are currently executing are contracts closed in the years 2011 and 2012 so therefore they have a certain margin that we know, but I do expect for the future some margin pressure coming from those new entries in the Chinese market.

42.13

Daniel Patterson

Okay, thanks, that is very clear. I just have one question for Michael on Nilfisk. On your presentation you mentioned there were sort of 15 million in cost that could be sort of classified as non-recurring. Maybe I missed that, but could you explain what that was in Nilfisk?

42.31

Michael
Well, I don't want to go into a discussion about what it is, I just want to mention that if you compare the third quarter this year with the third quarter last year we have this number that you somehow should understand and you know, we are looking at margins last year of 10.4 and now 10, if you look at that in real numbers, you are looking for a variation of DKK 5 million and thereby it is important to understand that number.

43.03

Daniel Patterson

But it is not the reason for the gross margin pressure?

43.07

Michael

No, it is not the reason for the gross margin pressure.

43.10

Daniel Patterson

Okay, thank you, very clear.

43.17

Operator

We have a question from Jakob Pedersen from Sydbank. Please go ahead sir.

43.20

Jakob Pedersen

I have a couple of questions, first of all concerning your guidance for the full year. Now I would have expected that operational leverage would have meant that increasing organic growth would also increase your earnings. It is the reverse that we are seeing. You stick to your earnings expectations on a high organic growth platform. What has gone wrong this year? What has surprised you in that you are not able to increase your expectations for the full year's EBITDA?

43.59

Michael Lyng

Well, I think you should understand the logic behind our guidance. We are guiding a range similar to last year so that could also be that we are on the positive side or on the negative side and an EBITDA margin improvement from 2% organic growth could easily be absorbed by that guidance. That is one thing. Another thing is that we are still in a business with a lot of projects that we need to close in the fourth quarter in the Cables and there is a risk for part of that shifting from this year into next year due to customer delays and I want to make sure that I can absorb that in my guidance.

44.49

Jakob Pedersen

Okay that is very helpful. Now for the past years we have been very focused on the potential within high voltage, on the Cologne factory, the submarine. It seems as if you have had a very, very high utilisation on this factory for 2013 and now we are not going to know what is going to happen in 2014 but even if all contract negotiations pan out as you expect, will you be able to lift your activities and your volume in 2014 in Cologne compared to 2013?

45.33

Michael Lyng

Well, Jakob, it is a little bit too early to comment firmly on 2014 but...

45.40

Jakob Pedersen

Okay then let me rephrase, if you had such a good – can you do it better in 2014 volume-wise in Cologne than you have done?

45.51

Michael Lyng

Yes we can definitely have a more optimal product mix in the Cologne factory.

45.57

Jakob Pedersen

Okay, then to my third question, pricing power in Nilfisk-Advance it is not something that you have talked a lot about in the past but it seems as if it is becoming more part of every day. Is this what we should expect going forward that you might have a more difficult time getting your price hikes through? And also concerning the mix changes, what are you doing to revert these or can you do something to improve gross margins on the products that you currently sell more of?

46.39

Michael Lyng

First on the pricing. As you know we are normally increasing prices at the beginning of the year and we also did that at the beginning of this year and we also succeeded in increasing prices but you are also right saying that it has probably been a little bit more tough this year than it normally has been but that does not change the fact that we will continue to increase prices and I think that is well known to the industry that we will do it again at the beginning of next year. But I think it is also a natural logic if you link it to the overall economic climate that our customers are of course focusing more and more on prices. And then coming to your question about the mix, well, we do not see any reason to reverse the mix impact. What is key and what is extremely important here is to make sure that our costs to serve the lower margin segment are also reduced and that you can see by looking at our overhead costs slide and in the end on our more or less flattish EBITDA margin

47.52

Jakob Pedersen

Okay, thank you. You have been very helpful.

47.57

Operator

We have a question from Fasial Ahmed from Handelsbanken, please go ahead sir.

48.00

Fasial Ahmed

Yes, Fasial Ahmed. I have got both a question for you Michael. Firstly on Nilfisk-Advance. Can you comment on if prices actually [...] quarter on quarter and how much of gross margin decline which we saw will actually be related to pricing if you could try to quantify that. That is the first question, Michael.

48.27

Michael Lyng

Yes of course, it is extremely complicated to analyse these effects because you are looking at an extremely broad customer range and also product range but if we compare the prices year-over-year we don't see a significant decline. We have actually been able to increase our prices as I mentioned on previous questions so it is mainly related to our product mix change.

48.59

Fasial Ahmed

Okay, that is very clear. And the second question relates to Cables, I mean a few weeks ago you commented on these rumours regarding Gemini I mean that seems to be quite a big project and if you are able to succeed in that I mean it seems like your capacity will be fully booked next year. How will you try to manoeuvre around that? Should we expect some incremental investments from your side or will you just be satisfied with having full utilisation of your submarine capacity in Cologne?

49.38

Michael Lyng

Marc, do you want to take that question?

49.41

Marc van't Noordende

Yes, I think I like to answer to the question without going into the details of project Gemini and other projects but I think it is true that we have the possibility to expand our capacity substantially with a marginal investment in the Cologne facility and that is on our medium-term horizon. It would make of course the old role of investment much more attractive since the incremental operating cost for any additional ton that we can produce there would be rather limited so yes there is a possibility to expand that capacity – yes we are looking at that and that is on our medium-term horizon.

50.23

Fasial Ahmed

Okay, perfect, thank you

50.31

Operator

I remind you if you have a question, please press 01 on you telephone keypad. We have a question from Jesper Christensen from Almindelig Brand Markets, please go ahead sir.

50.44

Jesper Christensen

Thank you, hello. Four questions from me, three on Cables and one on the Group. The first one on Cables – that is you, Marc – looking at your history in the Group, I remember the first you were presented to the financial community at the Capital Markets Day in Cologne you presented a slide with I think it was 15 or more initiatives, restructuring initiatives that were going on in Cables at the time and now you are going to go into a new initiative soon could you perhaps tell us about the journey that you have been through from then to now and the second question is about China and your new cable, 220 voltage cable that you are now selling. Should we expect a margin increase that you now have that approved and in the market and the third question is in this year you have been negotiating the frame agreements you have with certain large German power companies. Could you perhaps elaborate a bit on how those negotiations have evolved and I would expect they were all negative given what you mentioned in your report on that market and then the fourth question on the Group. You are now at 2.7 net debt to EBITDA. How do you view that level and should we look for a lower dividend because you want to get that level down or how do you feel about a gearing of that size? Thank you.

52.24

Michael Lyng

Maybe I will just take the last question first because then I could hand over to Marc afterwards. First of all it is not 2.7 times – I think it is 2.6 times but the debt is 2.7 billion that is correct. But as I also mentioned in my presentation we expect to see a further working capital reduction during the fourth quarter and thereby stronger cash flow in the fourth quarter. So let us see where we will end the year. Our dividend policy is firm and is not changed so we continue to have a dividend policy where we want to pay out one third of the net result as dividend. And then you, Marc.

53.09

Marc van't Noordende

Yes, so coming then to your first question which referred back to the Capital Market Day of I think it was August or September 2011 where I presented 15 or more initiatives in a restructuring programme you have to think about the time that this was done. It was in a time that in 2010 and 2011 we built the new factory in Cologne and we went into a, for us, totally new business, the large project turnkey project business. That is one thing and the other thing that happened is that in the same period 2010 and 2011 we moved away from a country-based organisation to an integrated one group functionally oriented organisation so the 15 or more projects that you refer to had all to do with preparing the company for the future given the changes that I just mentioned. I will give you one example – of course the subject of risk management should be on our agendas always but if you move from a sort of commodity type business into a large project turnkey business then the subject of risk management becomes part of your success and therefore we spent a lot of time in one of those initiatives in setting up an internal risk management system so again it was all about preparing the company for the future which is different than the initiatives that we are now developing and that is indeed working specifically on our cost structure so in 2011 it was not a cost restructuring it was not a cost reduction programme, it was a programme of a different nature. Now coming to your second question around 220 kW cable order that I think we refer to in one of our quarterly updates you mentioned that can we or you ask can we now start to see additional margin coming from this business now you have your approval. I have to explain a little bit that in China the high voltage business is predominantly the state grid and therefore if we talk about are we approved or not then we talk about are we approved for sales to state grid and the approval process is not only for that company, not only the traditional prequalification test that takes anywhere between 12 and 18 months but it also in this case has that you need to develop a number of references, a number of kilometres of cables in operation and therefore you sell projects into the market that can serve as a reference that in turn is part of the approval procedure. So we are still in the middle of our approval procedure and therefore it is too early now to say that we can expect a lot of additional margins since for us it is more important to get those reference projects than to get any large margins out of that at this moment in time. And then your final question was around framework agreements with German companies, utility companies I assume but we are not at this moment in time negotiating any such agreement with German utility companies that was done I think at the end of last and the beginning of this year but of course negotiating multi-year framework agreements with utility companies is part of our sort of almost a daily part of our business given our European spread and it is at this moment in time and I think that is probably the background for your question with the market volumes and the market demand being substantially down – yes the market for large framework agreement with utility companies is a tough market at this moment in time. They understand the market very well; they know that their own consumption is really down. They can understand that that is the same for their colleagues in the field in other countries and they know therefore that there is substantial volume that needs to be sold by the cable suppliers and they try to make the best out of it for themselves so they try to impose not only prices that are not very attractive to us but they also try to impose liabilities on the supplying companies that are totally unattractive for us so it is a tough market at this moment in time where I will be very frank, the question is often on our table, should we really want still to have this business with the price levels that the customers are asking and with the liability profile that he is also asking so it is a very difficult market at this moment in time.

57.43

Jesper Christensen

Okay thank you

57.49

Operator

Once again, if you have a question press 01 on your telephone keypad. We have a question from Patrik Setterberg from Nordea please go ahead sir.

58.00

Patrik Setterberg

Hi gentlemen, I had a follow-up question before but it has been answered so thank you.

58.15

Operator

There are no further questions at this time. Go ahead speakers.

Michael Lyng

Thank you operator so that concludes our webcast for the third quarter and here on page 34 you can see our financial calendar for 2014 and also going into 2015 so thank you very much for attending our presentation and as you can see on the calendar we will be back on 28 February with our annual report for 2013 including our expectations for 2014. Goodbye.