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Q3 2019 NKT A/S Earnings Call

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## PRESENTATION

### Operator

Ladies and gentlemen, thank you for standing by, and welcome to the Q3 report 2019 conference call. (Operator Instructions) I must advise you that this conference is being recorded today, this 21st of November 2019. And I would now like to turn the conference over to your speaker today, Alexander Kara, President and CEO of NKT. Please go ahead.

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### Alexander Kara *NKT A/S - CEO*

Good morning, everybody, and welcome to the presentation of NKT's Q3 2019 results. My name is Alexander Kara, CEO of NKT. After you have noticed our forward-looking disclaimer on Slide 2, I will continue with today's presentation.

Today, with me, I have my colleague, Roland Andersen, CFO of NKT; and Basil Garabet, CEO of NKT Photonics; Mads Bodenhoff, CFO of Photonics; Michael Nass Nielsen, Head of Investor Relations, here in the room.

Let us move now to the next slide. And to give you an update here on Photonics. The NKT A/S Board of Directors have decided to review strategic alternatives for NKT Photonics, with the objective of maximized value creation, positioning NKT Photonics for long-term growth and to support the deleverage of NKT A/S balance sheet. NKT A/S have not set a definitive schedule to complete this review and no decision on any particular transaction or alternative has been reached at this time. NKT does not intend to make further announcements regarding the review unless it concludes they are warranted by the circumstances or are expressly required by law.

Let us go now to NKT's Cables business and the highlights of Q3. As you have seen, our announcement of financial performance in Q3 2019 is as expected, impacted by reduced activities in Solutions. It outweighed improvements in Applications, Service & Accessories.

On high-voltage order backlog driven by a number of orders of boards, small order boards, but also a big order, Viking, the Viking Link cable. After the quarter end, we announced NKT's largest order ever, the Dogger Bank, Creyke Beck A/B wind farm, which is -- each one is 1,200 megawatts out of the total 5,500 megawatts with roughly 40% of the total CfD.

NKT's financial outlook updated is applications will not deliver sufficient profitability improvement and sub-order type of job orders will not have a material impact in 2019.

Let us now move to the next slides, to the business specifics and then go to Solutions. As expected, the reduced activity levels is reflected in the financial performance. On average, exclusion on the current project, we're in line with expectation. Karlskrona is better and Cologne had some production delays, which would also impact on the revenue. We completed the large Caithness-Moray project in Scotland where we also used the first time our Victoria vessel, which was a very big success.

Our leadership team Solutions strengthened its presence in a co-leadership forum. So we have a dedicated manager, general manager for Karlskrona and Cologne and Chief Commercial Officer function in Solutions. This strengthens the P&L ownership, and is also a support of harder decision-making on both sides.



Moving to the market update. The project in high-voltage were around EUR 2 billion, which have been awarded in the first 9 months 2019. We have been awarded a number of these projects. The biggest one is Viking and then several small orders. The CfD offshore in U.K. took the strong momentum in offshore wind, and we are happy to work with Equinor and SSE on the Dogger Bank wind farm, which is, as I mentioned, 2.4 gigawatts out of 5.5 gigawatts. We still see an attractive market outlook in the medium and to long-term, with continued progress on several standards.

Going to the next -- to the order backlog. Our order backlog has increased in Q3 when Viking was added. Not included in the backlog, what you see on the graph is the Dogger Bank, which we have just booked and announced 1 day back. So this will come in -- will be added to the backlog, means we are reaching practically 2x revenues with adding these yearly revenues -- having these the backlog called Creyke Beck A/B. We are also the best dealer for Attica-Crete onshore (inaudible) cable. And with this backlog, which we are building up, we're building up the future for 2020 and onwards. As you know, it's important to have a strong backlog for Solutions.

Coming to Applications. We delivered a slight improvement in our Applications business, but the profitability is still not satisfactory. So strong growth was driven by Germany and Eastern European countries. We have delivered satisfactory production in Eastern Europe, but the performance in Scandinavia was not satisfactory. We are fully focused on proving efficiency, and thereby, the profitability on all sites.

Coming to Service & Accessories. Service & Accessories (inaudible) delivered satisfactory performance in Service & Accessories and had a double-digit growth in both area. This also led to an increased profitability where operational EBITDA almost doubled.

In Service, we were successful in completing a large offshore assignment. It started in Q2 and finished in Q3. And success of this was mainly driven by increased output of the production and solutions for offshore as well. We deeply have completed the NKT Cables portion, and I would now hand over to Basil for NKT Photonics part.

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**Basil Garabet NKT A/S - CEO & President of NKT Photonics**

Thank you, Alexander. Good morning. The key highlights for NKT Photonics in Q3. Our revenue came in at EUR 16.7 million. This is up from EUR 15.2 million in the same quarter of 2018.

Imaging & Metrology and Material Processing were the main drivers for that growth, corresponds to a organic growth level of 8%, and it's expected to improve a little bit further in Q4.

Our EBITDA came in at EUR 3.9 million and adds up significantly from a EUR 1.5 million in the same quarter of 2018 driven mainly by higher revenue and effective cost containment and some positive nonrecurring items.

The order intake for the quarter came in at 12% growth over the same quarter in 2018, again, a healthy growth. And the value of the orders exceeded the revenues for the quarter and will continue to contribute to further growth.

In October of 2018, we opened our facility in Boston, Massachusetts in the U.S. The site will be a manufacturing site, and we'll supply advanced lasers to the U.S. market, which is one of the fastest-growing markets in our sector. And we'll improve our ability to service and access different customers in the U.S. and the Americas.

In Q3, we delivered lasers for a directed energy program at 20 kilowatts. The 20-kilowatt laser was a defense project in cooperation with our partner, the German company, Rheinmetall Waffe Munition.

Also in the quarter, we went live with our new global ERP system. We have some expected delays in the system, which postponed some of our revenue to Q4. The new ERP systems integrate all our primary sites under 1 IT platform. We have a number of smaller sites, and this is the first time that the company has been integrated over 1 platform. We hope to see vast improvements on that, especially going into 2020.

The financial outlook for 2019 has been adjusted. The organic revenue growth has been adjusted to around 10%. Previously, it was 15% to 20%. However, our EBITDA margin is unchanged at 15% to 20%, and it's actually coming in at the higher end of that range.

We move on to the business development in Q3. If you looked at 3 sectors that we are in, Imaging & Metrology, they're roughly about 1/3 each, but the largest is Imaging & Metrology at 38% of our revenue. That still continue to be the primary growth driver in 2019 and for the quarter. We have new potential OEM customers taking possession of some of our supercontinuum lasers in the quarter. Those are new projects that will have much larger deliveries in, again, in 2020 and onwards. These are OEMs that are introducing us to new markets in the industrial side.

In Sensing & Energy, which is 29% of our revenue, we disposed of a small entity, FIOPs, which was mainly focusing on monitoring of pipelines. We closed a small facility down in September 2019. We've also been selected in the products that we manufacture for a very important project in India to supply our single-frequency Koheras lasers in large quantities, and deliveries had already started in a small way in Q3, but mainly in Q4, and we see that increasing in 2020.

In Material Processing, which is 33% of our revenue, the growth was mainly driven by our aerospace and defense market segment, specifically with our large projects with Rheinmetall. We also have several new opportunities in industrial micro machining with a number of different customers worldwide. And that's also driving a lot of our future growth as we move forward.

Moving from that, it ends my sector, and I pass it on to Roland.

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**Roland M. Andersen NKT A/S - CFO**

Thanks, Basil. And let's shift to Slide 16. Just briefly on the group's revenue development. We're moving from market prices to standard prices. And in standard prices terms, for the quarter, we have had about EUR 3.9 million in currency impact, which is primarily the Swedish kroner, but also a little bit in Poland and on the divestment side, it's the disposal of the railway cable activities back in February 2019. And the rest is the organic growth, of which the negative part of EUR 44 million is in NKT Solutions business, and the organic growth in Photonics of 8% equals EUR 1.2 million.

And if we then just walk through the next slide, Slide 17. Operational EBITDA in Q3 year is impacted by lower revenue price, primarily in the Solutions business of NKT. And it is still the overhang of the lower load in our factory in Karlskrona while earnings increased slightly in both the Applications business and also our Service & Accessories business.

The implementation of IFRS 16 has impacted positively our operational EBITDA by EUR 1.4 million, of which EUR 1.1 million is in NKT and EUR 0.3 million in Photonics. And then there has been one-off items of EUR 4.9 million in Q3 related to NKT, our cost program and also a few production efficiency improving initiatives.

We're going to the next slide, our group's operational EBITDA. So I expect that the EBITDA margin as we have looked down in '19 and primarily driven, of course, by the possibility in NKT. And just a reflection on historical numbers, the improvement of 15% to 17% was primarily driven by the acquisition of ABB HV Cables and also by the divestment of NKT's Chinese operations.

So we'll move to the next slide, 19. We continue to work with our working capital, and it has improved since last quarter, primarily in NKT, driven by development in Applications. And for Photonics, at the end of Q3, working capital was up by EUR 0.9 million compared to the end of the previous quarter. And this increase reflect mostly buildup of inventory ahead of the expected revenue increase in Q4. Separately here on the net interest-bearing debt, we can see the impact of balance sheet of the lease liabilities coming from IFRS 16 is around EUR 32.9 million.

So moving to the next slide, 20. Working capital development, so working capital is continuously work with in NKT, especially and also improving over the quarters for '19.

We move to next slide, 21. Group cash flow, cash flow from operating activities have been positive, so positive EBITDA contribution and building NKT and NKT Photonics. And our working capital development was positive in NKT. In Q3, our investment activities were higher, and that's mainly driven by the NKT investment in upgrade of equipment in -- qualifying our Cologne plant for DC high-loss production.

Cash flow from financing activities were impacted by coupon payment of EUR 8.1 million made on the hybrid security in September 2019.

So if we then move to Slide 22, which is the group's financial leverage ratios. And our net debt is flattish over 2019 and slightly up in Q3 from EUR 302 million to EUR 317 million primarily driven by the coupon payment. But the drop in EBITDA, LTM, leads to a higher leverage ratios in 2019 ForEx, so a relatively low EBITDA gives a high leverage ratio.

If we then move to Slide 23. As mentioned, we are making a position to our guidance for NKT, and we previously guided EUR 0.9 billion to EUR 1 billion in revenue, and we will now be more precise and say, we'd end up in the lower half of that range. And for operational EBITDA, we previously guided EUR 30 million in earnings, and we will now make that more precise and say that we will end in the lower half of that range.

And for NKT Photonics, we are changing the guidance from an organic growth from 15% to 20% to around 10%. And then we will be more precise on the EBITDA margin and say that the margin will now end up in the high end of the 15% to 20% range.

And with that, I will give it over to the audience for Q&A.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions) Your first question comes from the line of Benjamin Szekeres from Goldman Sachs.

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### **Benjamin Szekeres Goldman Sachs Group Inc., Research Division - Analyst**

I have 3 actually, 2 of them are -- which are related. And the first one would be to Alexander. Now that you have been in the business for a bit longer than during the conference call at 2Q, what would you say are some of the key improvements or key strategic kind of initiatives that you expect in the business or that you see as important? And that's related to my second question is -- which is about the photonics disposal. And the question there would be, why now? Why not a quarter ago? Why not in 1 or 2 quarters? Why do you see that as, right now, as being the right time to make that move?

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### **Alexander Kara NKT A/S - CEO**

Okay, maybe I'll say something to the first one. What I have seen obvious is what we need to look into Solutions to build up the backlog and build in the future what I meant also during the presentation. So if we have started, we were successful with the Dogger Bank, and so we are working on that. So this is absolutely important in backlog in order that you can fill the factories in Cologne and Karlskrona.

If it comes to Service & Accessories, here we are on a good track, on a growth momentum. And this means so that we continue on both areas. If it comes to Application, we need to work on the productivity, on output, get more out of the factory. So that the operational performance of the factories will be key, whereas, we have a different view. As also indicated, we compete in the factories in Central Europe and Northern Europe. So this is operational, excellent output factory in Applications and Others, as I mentioned.

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### **Basil Garabet NKT A/S - CEO & President of NKT Photonics**

Okay. Thank you, Alexander. And then to Photonics, why now? I think that Photonics is the only subsidiary in the NKT Group left on the conglomerate base, and that company has been developed over the past years. And over the past 2 years, I think they have, since their last acquisition, performed quite well in terms of commercial improvements and also organic growth. And in Q3, they proved that also earnings is following. So we actually think that Photonics is in a good shape and form, and that's why we're starting the process. We've not disposed anything yet. We're starting the process to explore, the options, and then we'll be more precise once we have more clarity on that, both with regards to the options structure and also a potential time line. So that's the first reason. And the second reason is that this will obviously help us getting closer to an optimal capital structure and reduce the group's net debt level.

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**Benjamin Szekeres Goldman Sachs Group Inc., Research Division - Analyst**

And then my third question is about the guidance for NKT, for the Cables business, which you have lowered to be in the lower half of the previous range. And I'm just interested in what are some of the moving parts that could result in you being towards the lower end of that lower half or perhaps the higher end.

**Roland M. Andersen NKT A/S - CFO**

Yes. So from the outset, in Q4 last year, we said that in order for us to get into the higher end of that range, we would need some order wins and bigger order wins that would impact 2019 production, and thereby, revenue and earnings. And also we would need a certain traction on Applications. And I think sitting where we are today, we're quite happy with that Applications are starting to grow. But the earnings are not following sufficiently fast compared to what we had expected. And secondly, we have taken a big chunk on high-voltage orders this year, if you count in the top bank. So we are quite happy with that, actually. But -- and none of those will have production impact in '19. That will only be from 2020 and onwards. So that's where we are narrowing the interval for launching to the low end. At the same token, we reiterate that 2020 will be better than 2019. And we have the highest backlog as we speak for a long time, and I think that will underpin that statement.

**Operator**

Your next question comes from the line of Kristian Johansen from Danske Bank.

**Kristian Tornøe Johansen Danske Bank Markets Equity Research - Senior Analyst**

A few questions from me. The first one, in regards to the strategic view in NKT Photonics, does that then mean you have decided on keeping NKT Victoria? Or is that still a possibility you have in front of you to potentially divest it?

**Roland M. Andersen NKT A/S - CFO**

Kristian, thanks for that question. There has been no plans to sell NKT Victoria. First, that is a strategic asset, so that's not related to Photonics.

**Kristian Tornøe Johansen Danske Bank Markets Equity Research - Senior Analyst**

Okay. Then looking at the Q3 numbers, in my view, there are sort of 2 disappointments, right, lower-than-expected revenue in Solutions and lower-than-expected margins there in Applications. If we look at these 2 factored into 2020, is there any means of read-over from these? I mean, should we be more concerned in our estimates on these 2 parameters for 2020?

**Roland M. Andersen NKT A/S - CFO**

Yes. For me, I think, I'm quite happy about the fact that we are building the backlog. We're building the backlog, so it's the highest level today as it has been for a while. And not only are we building it, we're also building it with the right (inaudible). As we have discussed, we need more MI and we need more DC. And Dogger Bank is actually DC, high-voltage interconnects; and Viking is MI; and potentially, Attica-Crete is also MI. So this is adding to our ability to fill all 3 lines in Karlskrona more efficiently. So that's clearly a positive. Now on the Applications side, it's positive that we can start growing that business organically in a European market that may be converting towards O. But we are clearly delayed in terms of earnings pickup. And as Alexander also says, that will be a key focus for the next year or two to make sure that we execute properly on making that happen. So potentially, a little bit of carryover negatively in Applications, but de-risking 2020 in terms of looking at the backlog.

**Kristian Tornøe Johansen Danske Bank Markets Equity Research - Senior Analyst**

Okay. And on Applications, I mean, because you have been speaking about improving productivity for some time, and it hasn't really happened, I mean, do you need to take more drastic steps here? I mean, looking at your Scandinavian factories, which seems to be the problem, is that the right setup? Or do you need to close some down and move production elsewhere? Or I mean, what are your thoughts around this?

**Roland M. Andersen NKT A/S - CFO**

We have some thoughts around that, but we are not ready with that yet. I think Alexander is also reviewing our wholesale up and so on. So there's no decisions on that. I think the existing setup needs to perform a lot better than we see currently. That's the starting point.

**Kristian Tornøe Johansen Danske Bank Markets Equity Research - Senior Analyst**

Okay. But would it be fair to expect that you sort of addressed the strategy for this business a bit more in detail in connection with the annual report?

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**Roland M. Andersen NKT A/S - CFO**

I think with the annual report, we will give a bit of a strategic update.

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**Operator**

Your next question comes from the line of Claus Almer from Nordea.

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**Claus Almer Nielsen Nordea Markets, Research Division - Senior Analyst of Capital Goods and IT**

I also have few questions from my side. The first is to the strategic review. Maybe you could share a bit more details on this process. So what are you doing at the moment? Are you hiring in consultants? Whatever you do, can you give an update on that one? That will be my first question.

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**Roland M. Andersen NKT A/S - CFO**

Thanks for the right question. I think, currently, we don't have so much more color than we just have had done. We have started the process. We'll be structured around this in terms of the team in Photonics, in terms of the Board of Directors and we'll start working with all options. And as soon as we have a more crystallized picture of that, we will also start to work a little bit with a potential time line and what that entails for both the company and also for the group. And I think I'll leave it at that for now.

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**Alexander Kara NKT A/S - CEO**

Maybe I can add. We've been lucky with consultants. That's our plan.

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**Claus Almer Nielsen Nordea Markets, Research Division - Senior Analyst of Capital Goods and IT**

Okay. Let me just -- one question to this. Do you think keeping Photonics is a possible scenario?

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**Roland M. Andersen NKT A/S - CFO**

Currently, we are not disposing, so it's clearly a scenario.

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**Claus Almer Nielsen Nordea Markets, Research Division - Senior Analyst of Capital Goods and IT**

Okay. Then the second question goes to the backlog. At the annual report for 2018, the value of, let's say, 2019 backlog, so the revenue to recognize this year was close to EUR 450 million. And based on the information in the Q3 report, that has grown to EUR 466 million roughly. So not much increase. I would have thought in and out orders would have increased the value of the '19 backlog by more. You say, anything we should be aware of that, be aware of?

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**Roland M. Andersen NKT A/S - CFO**

No. I think some of the -- this is a pretty narrow interval you're asking about, I think, (inaudible) some of the in and out orders that we have received in '19 will probably have production in '20 instead of '19, if that is what's disturbing you a little bit.

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**Claus Almer Nielsen Nordea Markets, Research Division - Senior Analyst of Capital Goods and IT**

Yes. Yes, you can say that. So why is that? Is that due to these issues you had in Cologne you mentioned during the presentation? Or is it just coincidence?

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**Roland M. Andersen NKT A/S - CFO**

Well, it's not just a coincidence. We have been full in Cologne. And then some of the orders we have taken in, we can only produce in 2020. So there's an element of that.



**Claus Almer Nielsen *Nordea Markets, Research Division - Senior Analyst of Capital Goods and IT***

Okay. And can you also just, that will be my final question, an update on the one-off costs this year and the cost savings program. So is this the effect on 2020?

**Roland M. Andersen *NKT A/S - CFO***

Yes. So I think the cost-saving program, we are currently at about 70 FTE where the target was 130. As one element, and the other element was, say, a reduction in general spend. But I think with regards to the FTEs, we are not exactly where we want to be by end of the year, but we will be there coming out of -- coming into first half of 2020. But on general spend, we are ahead. So we will meet our savings targets for 2019. And the reason why it's not moving as fast as we would have wanted is because some of the projects that we have taken in, in the small end needs some of this main power. So it's a little bit of planning around it, and then we will complete it in the first half.

**Claus Almer Nielsen *Nordea Markets, Research Division - Senior Analyst of Capital Goods and IT***

Okay. But I think you initially said the one-off cost will be between EUR 8 million to EUR 10 million, but then you also had the gain from the divestment. So I don't think it fully adds up. So, yes, where are we in that respect? (inaudible) more money?

**Basil Garabet *NKT A/S - CEO & President of NKT Photonics***

Well, I think we have a few one-off costs as well on some of the production and efficiency initiatives and so on. So probably, we're spending a bit more on that and a little less on this program actually.

**Operator**

Your next question comes from the line of the Akash Gupta from JPMorgan.

**Akash Gupta *JP Morgan Chase & Co, Research Division - Research Analyst***

I have a few questions, please. My first one and first couple of questions on Solutions business. So first of all, if you can talk about backlog margins in a bit more detail. We know that some of the orders that you have taken have come at a time when everybody was struggling with the backlog, and therefore, if you can say how much of backlog is healthy backlog or similar to 2016, '17 margins that you have delivered in the past? And how much of a backlog is under pricing? And what should we expect for 2020 and 2021 in that respect? So that's question #1.

**Basil Garabet *NKT A/S - CEO & President of NKT Photonics***

I think that -- thanks for that question. I think it's a little bit delicate one. I think we've been clear that our Hornsea 2 project was below what we found really, really, really attractive, right? And that the market has been competitive. But for the remainder of the projects we have taken in, I think we will keep that between us and then the customers.

**Akash Gupta *JP Morgan Chase & Co, Research Division - Research Analyst***

So basically, you are saying it's not really a major issue and is margin mix in the backlog when we look at margin for -- I mean, it is an issue, but not a major one for next year and after.

**Basil Garabet *NKT A/S - CEO & President of NKT Photonics***

I don't think that's an issue. But what I'm saying is that, that precise information I would like to keep between us and the customers.

**Akash Gupta *JP Morgan Chase & Co, Research Division - Research Analyst***

Okay. And my second question on Solutions is about the pipeline. I mean, I think we have -- all of us then have seen activities picking up. I think your competitors have also announced some orders, and we see more and more activity in offshore wind space. There is also some talks that as SuedLink might come for award next year and some of the customers in SuedLink have already dedicated some budget in their planning for that. So is it fair to say that, at this point, if everything goes according to plan, then 2020 can turn out to be a record year for industry in terms of orders, both submarine and land interconnections?



**Alexander Kara NKT A/S - CEO**

Yes. I mean, our indication is that these corridor projects go ahead. And so that means Q1, Q2 there should be some of both if there is no delay. But the customer is always at risk here. And there are several other projects, which will be next year order, so on the offshore side and so on.

**Akash Gupta JP Morgan Chase & Co, Research Division - Research Analyst**

And do you have any internal expectation in terms of when do you expect SuedLink to come forward. One of your competitors said it might come for second half next year. But do you have any update on your side?

**Alexander Kara NKT A/S - CEO**

Yes. It could be second half or in Q2. Our indication is Q2.

**Akash Gupta JP Morgan Chase & Co, Research Division - Research Analyst**

And moving on to Applications business, I wanted to understand what exactly the core of the issue there is? Like is it the demand? Or is it the competitive behavior? Or is it something internally with you because you are also in the middle of this IT systems rollout? So maybe if you can talk about what exactly is the core of the issue because we are seeing for last many quarters that profitability in that business has been, I would say, maybe low expectations? And maybe if you can also talk about how long do you think it will going to take because I think previously, you have said that you may not reach normalized margins there in 2020. But is it -- like, maybe if you can update us with your road map and plan for this business to turn the margins around.

**Roland M. Andersen NKT A/S - CFO**

Yes. So I think that the issue here is that we have been doing too much, too fast for that business for handle. And that's everything from organizing a global supply chain on top of the entire business. So adding an ERP upgrade, at least in the Nordics, and further introducing lean programs and different -- also introducing an outsourcing of core processes. And doing that, I think it's going quite okay for us, but it's not efficient. We're putting too many resources into that where we should be moving the other way. And that we rectified a little bit in April, where we reversed the structure a little bit. And so far, the positive sign of that is organic positive organic growth, so it works in terms of hitting the markets. But we still need to fix the machine. As Alexander said, we need the throughput in the factories to come up at a lower unit cost. So it's a mixed bag of having, I think, a too ambitious road map in terms of what that business could deliver in 2 years. That will take a little time Q-by-Q from here on to improve, but we will get there.

**Akash Gupta JP Morgan Chase & Co, Research Division - Research Analyst**

So basically, you -- just to summarize, you are saying that it's all internal issues, there are no external issues in terms of demand or competitive behavior is just -- you are just doing too many things, too fast.

**Roland M. Andersen NKT A/S - CFO**

That is primarily an internal issue. The markets are relatively strong. We have grown organically, probably also faster than the market in Q3. So it's primarily an internal thing.

**Akash Gupta JP Morgan Chase & Co, Research Division - Research Analyst**

And my final one is on cash flow. I mean, year-to-date, in the first 3 quarters, you have built up some working capital. I think you may get some down payments for this U.K. offshore project in Q4. So if you can talk about what should we expect for Q4 as well as full year cash flow, and where do you expect to end your net financial debt by end of the year?

**Roland M. Andersen NKT A/S - CFO**

Yes. So also, I'll answer some of that. So I think we have guided on the EBITDA, right? And that gives you a number. And on our investment level, I think we probably said it will be slightly below last year. And I also think we said in Q1 that our working capital shouldn't, by the end of the year, be higher than it was in Q1. So if you add those numbers up, then you will get there approximately.

**Operator**

Your next question comes from the line of Artem Tokarenko from Crédit Suisse.

**Artem Tokarenko *Crédit Suisse AG, Research Division - Research Analyst***

My first one is around the Applications business. Could you maybe help us understand a bit better in terms of year-over-year bridge for next year, how much of a headwind those incremental costs which you have because of IT rollouts and internal issues in that business have been a headwind this year? And how much of those you would expect to reverse next year?

**Roland M. Andersen *NKT A/S - CFO***

That is also -- it's not necessarily IT cost or IT issue that is giving us headwinds. I think we are getting that under control. It's a matter of getting the organization back to a structure where they can work efficiently, where they can make their lean processes work, where they can get throughput up on a day-to-day basis. And also where the supply chain functions are sufficiently coordinating with funding sales so that we're more efficient you produce exactly what we need to use and sell month by month. A little bit of planning. Very, very operational measures, and the good news is we know what has to be done, and now we need to execute it.

**Artem Tokarenko *Crédit Suisse AG, Research Division - Research Analyst***

Okay. So I guess, I guess the question is, the cost base for that business, do you expect it to be flat for next year? And is there any way you can quantify those potential efficiency improvements which you see?

**Roland M. Andersen *NKT A/S - CFO***

And I think the way we think about it here is that we need to do more of the same. We simply need the assets to deliver more throughput. At the (inaudible), we can sell it to customers there. So that's how we think about it. So less under absorption in the factories.

**Artem Tokarenko *Crédit Suisse AG, Research Division - Research Analyst***

Right. Because it sounds like the market is doing maybe a bit better than you've expected. And then from outside, it's very hard to get any visibility on margin recovery in that business if cost base remains flat. And that is just a question of high efficiency.

**Roland M. Andersen *NKT A/S - CFO***

Yes. Yes, exactly.

**Artem Tokarenko *Crédit Suisse AG, Research Division - Research Analyst***

Okay. My next question is on Solutions business. Could you maybe help us understand a bit better what will be -- how do you see the shape of recovery and revenue delivers in that business throughout next year with your current order book? And also, I guess, you disclosed that from current order book, you have around EUR 450 million of revenue for next year in Solution already. Could you help us to also understand how the Dogger Bank and Creyke Beck, which are not part of the order book will be -- how much of those will be delivered next year? And what should we expect for in-for-out for next year?

**Roland M. Andersen *NKT A/S - CFO***

Yes. So I think what we said is that Dogger Bank expectedly will be initiated in -- for production also in 2020. So part of that needs to be included in 2020 as well. We haven't completely updated our production plans yet, but that will be a meaningful amount of that. That will be started in 2020. Now as to Creyke, it's not in the order book yet, just to be clear on this. But that will be started in 2020 as well expectedly.

**Artem Tokarenko *Crédit Suisse AG, Research Division - Research Analyst***

Okay. And maybe in terms of the shape of recovery because, I guess, consensus is consensus looking for EUR 40 million of EBITDA in that business. And so far, if you look at the current revenue and profitability run rate, it's kind of behind that. So throughout 2020, would you expect it to be H2-weighted?

**Roland M. Andersen *NKT A/S - CFO***

Yes, I would expect it to be H2-weighted? Absolutely.

**Artem Tokarenko *Crédit Suisse AG, Research Division - Research Analyst***

Okay. And then in terms of the utilization of NKT Victoria, how does this look for next year compared to this one?

**Roland M. Andersen NKT A/S - CFO**

Yes. But currently, that was the same last year. The bookings of that ship is not necessarily fully booked by the end of the year. That's something we do as we move along. And that's also the case now, but we're not so worried about that. We will get deployment for that still, the world's best cabling vessel, and that will be both service jobs and installation jobs for that.

**Artem Tokarenko Crédit Suisse AG, Research Division - Research Analyst**

Right. And looking at the awards of interconnector this year, I think you've been primarily securing the land sections. So 2 questions. Firstly, why you think you're not more successful on subsea sections? And secondly, given that NKT Victoria, my understanding is primarily made to do complex interconnect installations, do you see that lower market share in subsea interconnections but as potentially a threat to NKT Victoria's utilization coming back to previous healthy levels in the future.

**Roland M. Andersen NKT A/S - CFO**

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No, no. Not really. I think you're mentioning 1 or 2 specific instances where the customers have been quite close to the customers of these projects and where they have done something similar before, and in addition, probably have been really, really sharp in terms of their offers. So it's a combination of that. I think we would be able to do also these projects. But by the end of the day, the customer needs to make their choices.

**Artem Tokarenko Crédit Suisse AG, Research Division - Research Analyst**

Right. And also on Solutions. With the Dogger Bank, and assuming, Creyke Beck is finalized, for next year, is it fair to assume that now all lines will be utilized in H2 next year?

**Roland M. Andersen NKT A/S - CFO**

It's not that simple. All lines will be utilized, but it's not the lines, it's also the different production steps in the factory. I don't know if you've ever seen our process there, but we need to have projects in this full flow and the facts that we need to have projects on its way in. We need to have projects in the middle, and we have [assist projects] on its way out. So yes, we will now start to fill both lines. While we don't have yet, most likely in '20, all production phases full in 2020, that will only come from 2021 onwards. So it takes a little while to build up again, if that is a meaningful answer.

**Alexander Kara NKT A/S - CEO**

And may be I can add. Dogger Bank and Attica-Crete (inaudible) can not be completely manufactured next year. So it will be also in 2021, which is the part there will be mainly in the second half, I could say. Another will be in 2021.

**Artem Tokarenko Crédit Suisse AG, Research Division - Research Analyst**

Right. And my last question is on cash flow and net debt for next year. And in particular, Photonics business, obviously, comes as a remedy on your revolver. So firstly, why you've accelerated? Why have you accelerated the strategic process now? Does this mean that there are some concerns that the cash flow generation has maybe been weaker than you have expected in H2 and will be weaker in the next year? Because as it sounds to me, recovery next year will also be more skewed towards the year-end.

**Basil Garabet NKT A/S - CEO & President of NKT Photonics**

No. No, I think the in the beginning of this call, we talked about why we're doing Photonics now, right? And it has to do with Photonics' performance. It has to do a little bit with how we view the options. Potentially the options for that business, both structurally and also ownership-wise, and then secondly, it's obviously also a deleveraging of the group's balance sheet. So that's why we decided to start the process now. I mean, there's no disposal yet, there's no nothing yet. It can take some time until we've become clear on that.

**Artem Tokarenko Crédit Suisse AG, Research Division - Research Analyst**

I guess, let me ask differently, if free cash flow generation continues at the current level for the next 2, 3 or maybe 4 quarters, is your agreement on your revolver is still sufficient to withstand that?

**Basil Garabet NKT A/S - CEO & President of NKT Photonics**

So I think that's why we are disposing Photonics, right? And we expect to have sufficient financial headroom next year.

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**Operator**

Your last question comes from the line of Casper Blom from ABG.

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**Casper Blom ABG Sundal Collier Holding ASA, Research Division - Lead Analyst**

There's been a lot of questions already, so just 1 from my side. A bit hypothetical maybe, but let's assume that you (inaudible) Photonics and you get in some proceeds. How would you sort of rank your ways to pay back debt? You have the mortgage, you have the credit revolver and then you have also a hybrid capital. As I recall, there's first call on the hybrid in 2022, and you're paying a debt of -- an interest of a little more than 5%. Is it possible to pay back hybrid to start with? Or sort of how would you sort of start deleveraging? If you could rank that, Roland?

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**Roland M. Andersen NKT A/S - CFO**

I think, as you correctly say, Casper, that's a little hypothetical. So I'll refrain from speculating that for now.

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**Operator**

Thank you. There are no further questions at this time. Please continue.

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**Alexander Kara NKT A/S - CEO**

Okay. Thank you, everyone, for participating, then. Thanks for that. Cheers.

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**Operator**

That does conclude our conference for today. Thank you for participating. You may all now disconnect.

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