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**Nolato**

Q4 2019



## Prepared Remarks

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Hello, and welcome to the Nolato AB Q4 Report for 2019. Throughout the call, all participants will be in listen only mode. And afterwards, there will be a question and answer session. Today, I'm pleased to present Christa Walqvist, the CEO and Per Ola Holmstrom, the CFO. Please go ahead with your meeting.



Thank you, and welcome to Novartis presentation of the Q4 2019. This is Christo Walker speaking. I will start on Page 2 in the presentation deck. Also to summarize the Q4 on the group level, we had a good increase of sales and amounted up to close to SEK 2,300,000,000 that is adjusted for currency, an increase of sales of 22%. We saw during the quarter good performance by all our business areas and a very strong growth for Integrated Solutions.



The operating profit during the quarter rose to SEK 271,000,000 compared with SEK 214,000,000 if we exclude the non recurring items of SEK 22,000,000. We saw positive earnings performance by all business areas. We had a strong margin of 11.8 percent excluding the non recurring items. We had a very, very strong cash flow during the quarter of EUR 601,000,000 excluding acquisition of JBAR. Of course, this is a strong effect during the Q4 and should be looked as on the total year.



But Per Ola will come back to that. We have a continued solid financial performance. Then I'm turning to page 3 and focusing on the full year of 2019. We had a strong finishing up of the year following a tentative start And the earnings per share rose to SEK 27.2 which is the highest in our history so far, if we exclude the non recurring items. The financial position is strong.



We have net financial assets of 1,000,000 enabling us to be ready for M and A activities, of course. And we have, during the last month, sensed an increased sell side activity. And as you know, we have a long term focus in the M and A field and are mainly focused on U. S. The Board of Directors is has proposed a dividend for the year, a raise by 4% to and amounting to SEK 14.5 per share and that is a payout ratio of 55% of profit.



Turning to Page 4, summarizing up the group with our 3 business areas that in common, even though they are different markets, we have corporate responsibility. We use the same material across and we are working as solution oriented development partner across all business areas. And of course, we have the same production technology across. Jumping into Medical on Page 5. We concluded the last 2019, another record year.



I think it's number 20, 20 years of records. So we're pleased with that. On Page 6, we show the 2 parts of the Medical Solutions business area. So the medical device is the larger portion of the medical business. And that's mainly devices and active things that are supporting your well-being and getting drugs into your body and so on.



Then we have the smaller part called pharma packaging, which is packaging for drugs. It could be solid drugs, it could be liquid drugs, but it's more containers for that. Turning to Page 7, jumping into Medical Solutions 4th quarter. We saw an 8% increase in sales, but if we adjust for the currency effect, it amounted to 4%. We saw volume increase on both on the medical device and the pharma packaging side.



Previous year contained high sales of development work and production equipment as we previously explained. So the comparison is a little bit off on that. The margin, a sustained healthy margin of 12.8% within our long term targets. On Page 8, we see the presentation of the Integrated Solutions. This quarter, we amounted to close to €1,100,000,000 in sales.



And on Page 9, you will see the split of the business area in between different segments. The first and the largest portion is the consumer electronics, consisting of different type of devices containing mostly containing electronics and high glass and high finished products. And the smaller portion of the business area is the EMC and Thermal. In this area, we use working with shielding solutions and heat distribution products for electronic devices. And in this part, we have made the latest acquisition to JVAR going into that part of the business area.



On Page 10, we dive into the Q4 of Integrated Solutions. We had a very strong increase of sales amounting to 56%. But if we adjust that for currency effects, it amounts to 45%. During the quarter, the heating devices delivered new product variances due to a buildup of inventory by the customer. We saw we had low volumes in the VHP segment the previous year due to the inventory adjustment.

- During the quarter, we also saw some weak growth for the EMC, but positive mobile phone performance. The margin amounted to 13.4%. It's based on high production efficiency and a very good utilization capacity. And the strong combination of those 2 gave the strong margin. We have consolidated the U.S.-based JBAR from 18th December. Currently in the Integrated Solution, we have had a situation where a lot of our Chinese facilities has been production stopped due to the coronavirus. We had a production start today, not on full capacity yet, but it's been closed for approximately 10 days more than planned. And this will, of course, affect the Q1 numbers. But our we really believe that these volumes will be sort of evened out during the year.
- So it will not have a yearly effect, only a quarterly effect. If we then turn to Page 11, you see the development of our Industrial Solutions business. And we amounted to EUR 573,000,000 in this quarter. It was a strong growth. I will come back to the details about that.
- But if we look on Page 12, we see the split of the Industrial Solutions business area consisting of general industry and automotive in which the general industry is the largest portion of this business area. On Page 13, we will go into details about the Q4 of Industrial. We had a 13% increase in sales, but if we adjust that for currency, it amounted to 10%. So it was strong. However, part of that growth, approximately half of it, was due to nonrecurring billings of due to a ramp of a new product.
- Over across the business, we have stable volumes during the quarter. Our margin ended up at 8.2% compared to 7.7% in the comparison quarter 2018. We had during the quarter impact of start up costs for the new customer projects, and we estimate that to be approximately 0.8% effect on the margin.
- Hello. This is Pero Larsson commenting group financial highlights on Page 14. You can see a lot of detailed numbers for certain financial headlines. The Q4 numbers on the left side and the full year numbers on the right side. The net sales increased with 22% if we take away the currency effects, meaning SEK 2,300,000,000 almost in sales compared to almost SEK 1,800,000,000 last year.
- The EBITDA number this year is €249,000,000 compared to 214,000,000. However, all numbers on this page include the one time non recurring item of €22,000,000 2,000,000. If we do exclude that, the EBITDA number is SEK 271,000,000. The €22,000,000 in non recurring cost is connected to cost for one site closing down one site in U. K.
- As we announced in January. There will be additional cost in Q1 of about EUR 13,000,000 from this expected closing down cost of that site. So EUR 22,000,000 this quarter and EUR 13,000,000 in Q1 2020. The tax rate is 18%. This quarter, We had some positive effects, some smaller ones on non recurring items.
- We did see a lower tax rate in Switzerland compared to last year. And the best expectation for next year or this year 2020 is between 19% 20% The cash flow was very strong in this quarter. I would say the quarter is maybe not so good to compare with. I would prefer the full year number €800,000,000 The increase compared to last year, the €593,000,000 is having decreased CapEx from €452,000,000 to €360,000,000 2019. We also did see less need of working capital compared to 2018.
- The quarter was affected by high sales numbers in the beginning of the quarter and with the mix with a lot of sales having very short credit days. That meant that we could cash out most of the sales, the high volume sales in the beginning of the quarter, during this quarter in our cash. And at the same time, we had higher credit days in our accounts payables, giving us a good cash flow of course from the sales in this quarter. That will of course not happen every quarter, but that was the fact during this quarter. The CapEx EUR 360,000,000 we expect a similar CapEx during 2020, maybe some 1,000,000 more, but in that level.
- Earnings per share, DKK 26.60. Excluding non recurring items that is SEK 27 and SEK 20.20. We had a strong financial position at the end of the year. The equity assets rates yield ended up 48% and we had a net financial asset, if we exclude pension liabilities and if we exclude lease liabilities of €666,000,000 compared to €341,000,000 last year. On page 15, we have a 5 year summary of our financial targets.
- Starting with EBITA margin, we ended with 11.3 percentages. All of those financial targets should be seen during the business cycle in that time. The EBITDA margin has been above our target of 10% during this time period, the 5 years. And it has, of course, been a good business cycle during most of these periods. The cash conversion is the target having 75% of our EBIT result in cash flow after investments and after working capital need.



We ended up with 88% this year and that was the end of the year during this time period we did reach our target. We have instead been creating possibilities for our good growth during this time period. And with the working capital need and high CapEx numbers to cope with that, we haven't been able to reach the target except for this last year. The strong balance sheet giving us 48% in equity asset ratio, well above the target of 35%.



Turning to page 16 and focusing on the current situation by business area. If we start with the Medical Solutions, we have a maintained growth strategy, a lot of focus on innovation and very strong customer relationships. Within the integrated solutions, we have established a position in the new product areas. We see continued strong position within the EMC. We have a flexible production structure, but we also see disruptions as a result of the coronavirus.



In the Industrial Solutions, we have advanced our market positions. We see that the efficiency measures taken and gradually having an effect. And we see indications of slowdown in the economy, but stable volumes. Now we're open for questions.

## Q&A

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Thank you very much. If you do wish to ask a question, please press 1 on your telephone keypad. If you wish to withdraw your question, you may do so Our first question comes from the line of Karl Ragnostan of Nordea. Please go ahead. Your line is open.



Hi. It's Karl here from Nordea. First of all, can you give an indication of how much of Integrated Solutions volumes that sort of relates to inventory buildups? And how should we look at that going into Q1? Should we expect still continued high levels?



We don't have the full picture of what is sell through for our customer and what is not. We, however, base our statement that we believe the sales is higher than what the end consumer is buying from these products. And of course, going into Q1, there are a couple of things to consider. We have concluded that there is a certain inventory buildup this quarter with the new products. Then of course in the Q1 2020 that quarter is containing the Chinese New Year and then of course the situation with the coronavirus, which has to be considered looking at Q1.



Okay. Perfect. And I mean in terms of the coronavirus, can you I mean, I guess it will impact both integrated and the Medical Solutions because you have production in Medical in China as well, right?



The impact that we see will be on the integrated solutions. Medical production in China is a very small portion of the total and will not be seen in the total numbers. But on the integrated side, we will see an impact definitely.



Okay. Perfect. And also in terms of Medical Solutions, I mean, your previous guidance going into the quarter was or implied more or less negative organic growth for the segment in the quarter. I mean, can you explain what happened during the quarter that maybe surprised you? I mean, it's quite the difference between negative organic growth and mid single digits?



I think we explained it previously that we would see the second half of twenty nineteen in comparison to second half of twenty eighteen as flat or something like that. So that's sort of the communication we had previously. But we had strong performance in the medical field, but it's not that big of a deal. It's yes, more how many production days and if the delivery goes on this side or the other side of the quarter end.



Okay. And final one for me. You also talk about new contract burdening Industrial Solutions margins by 100 basis points. Can you give us any idea what type of project it is as well as the size of it?



During this quarter, we saw an increased size due to the non time onetime sales. And the product is within existing customer, but it's a new product and it's in the general industry area.



Okay. Thank you.



Our next question comes from the line of Oskar Vikstrom of ABG Sundal Collier. Please go ahead. Your line is open.



Hi, thank you. Just I have some follow-up questions on the heating products and I was thinking a bit about the old generation products. Obviously, you saw volumes here as well that drove the margin and so forth. What is the outlook for these type of products? I think previously you mentioned that progressively the new products will switch with the old ones and you wouldn't have this sort of inventory buildup situation.



But could we could you just get an update on how you view the future of the old generation products?



The old generation products, they will continue to decrease going forward. And there won't be very much left of those in the coming quarters. Still there was a part of those during the last quarter 2019 And that is sort of the effect in some of the markets where the new ones wasn't released or launched and mainly, of course, in the beginning of Q4.



Yes. Okay. Thank you. And so going forward, the margin here, so you said the margin benefited from this because you have high efficiency on them. What's the situation with the new generation products?



Do you think you will get these to the same sort of profitability? Or will that take longer? Or how should we view the margin in the for the heating products going forward?



I think you should view the margin within Integrated Solutions that we had a margin situation this Q4 of 13 0.4%. And we comment that that is a high number. It is high compared to most of the quarters we have seen with the heating products in the quarters during quite some time. And that is what we are explaining with the comments we had in the report. And of course, as the part of those older products will go down to almost 0 quite quickly.



We won't see them effecting upwards as we did in those two last quarters this year



or in 2019. Understood. Thank you. And just one quick question on Medical. So obviously, you guided for the flat growth in H2 2019.



Could you say anything of just about 2020? Is this will this be like a normal situation from a historical perspective? Or do you have any comps or anything that we should consider into 2020 that are difficult?



Medical, we have been guiding the medical that we should have any growth above market. And that's our long term target and that should be viewed over a business cycle or something. And I think our ambition is the same. And when things are ramping and not ramping will affect quarterly, but that the long term target stays.



All right. Thank you. That's all from me. Thanks.



Thank you.



Our next question comes from the line of Mikael Lasseyan of Carnegie. Please go ahead. Your line is now open.



Okay. Hi. A couple of questions. First of all, regarding the Industrial segment's margin and the negative impact from this ramp up, will this be sort of a Q4 phenomenon? Can we expect an impact also going forward gradually decreasing of course?



Can you please explain that?



We think that, that is a Q4 situation.



Okay. Got it. And what about the general efficiency for that segment? Do you believe that you can come back to 10%? Or has something happened more of a structural nature?



Our ambition is to come back to the 10%. That's what we are working for. And we've seen gradual improvements even though we had this one time thing. But that's definitely step by step our ambition to come back to the 10%.



Okay. And can you also talk about the general demand for the industrial segment and the main customer groups that you have and the situation that you see right now?



Yes. I think we explained that during our current situation, and we see across customers a stable demand. We have also then, of course, taken some market share with this new project and so on. But we see stable volumes going forward.



So any weakness, weak areas or particularly strong areas that you can highlight?



Not particular. No.



Okay. And then so going back to this Integrated Solutions situation with the corona effect, Can you be a bit more specific maybe what you have experienced so far in Q1? And I mean the New Year effect and things like that help out a bit? Because I mean the swing factor is quite large potentially.



Yes. We have seen, 1st, the New Year's closed down, the Chinese New Year's, but that was planned. And after that, we had additional 10 production days where we intended to produce, but we had to close down due to the coronavirus situation. Today, we started our production. We got approval.



You had to ask for approvals from authorities. And our estimation is that approximately half of the factories in China got that approval. We did get it and we started. Of course, there's still a situation where you lack operators because a lot of people have not been able to move after the Chinese New Year and then the corona situation. So we are not running our facility at full speed yet.



Okay. So what will happen with the market demand and your orders? That will just take longer to deliver? Or will it be a catch up effect in Q2 maybe? What do you think would happen here?



I think, 1st, we had to secure long term components. It could be lack of some components if this affects some of our parts where we need components or parts into our production. We have secured that for a period of time. But of course, after that, we need the supply chain to go on. But looking at the end market demand, I think it will not be affected from this situation.



So the end market demand is the same. So it will only be a movement of volumes from quarter to quarter. And depending on how fast we can get the supply chain going and the operators going, it depends on where we can catch up. But we believe on the year 2020, we will not see an effect of this.



Okay. Can you explain that the last part you mentioned about any effect of



What I mean the sales the anticipated sales volumes for Integrated Solutions, if we look on 2020 from our perspective, it will be as we expected before this situation. So it will not affect the end market need of our products.



Okay. Yes. Okay. Of course. And in total, this change from the older version of THP products or heating devices to the new one, Can you explain the difference for you when you do this transition?



It's I would say from our perspective, the production is very similar. It's, of course, different solutions and new products. But it's I would say, it's just changing a model or something for us.



Yes. And you have more models right now, I guess, than you had before?



Yes. We have been adding models.



Okay. Do you have all the new products that this customer has launched or only a couple of them? Or how does that work?



Yes. We have a position where all products in this area that our customer is selling is produced by us.



Okay. Do you have any vaping products in your product portfolio right now? Or is it only heating?



It's heating devices.



Okay. Got it. Thanks.



And there are no further questions. Please go ahead speakers.



Thank you for participating in the presentation of the Lattice Q4. And I wish you all a good day. Thank you.

