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AHL1V.HE - Q1 2013 Ahlstrom Oyj Earnings Conference Call

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## CORPORATE PARTICIPANTS

**Juho Erkheikki** *Ahlstrom Oyj - Financial Corporation Officer*

**Jan Lang** *Ahlstrom Oyj - President, CEO*

**Seppo Parvi** *Ahlstrom Oyj - CFO*

## PRESENTATION

### Operator

Good day, ladies and gentlemen, and welcome to the Q1 2013 Ahlstrom Earnings Conference Call. At this time, I would like to turn the conference over to Mr. Juho Erkheikki. Please go ahead.

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**Juho Erkheikki** - *Ahlstrom Oyj - Financial Corporation Officer*

Thank you and good afternoon from Helsinki. And welcome to Ahlstrom's First Quarter Interim Report Conference Call and Audio Webcast.

My name is Juho Erkheikki, and today's conference call will be hosted by our president and CEO, Jan Lang, and our CFO, Seppo Parvi. Following the presentation, you will have the chance to ask questions. Please note that the links to the webcast and the slides are available on our website at Ahlstrom.com.

So, Jan, please go ahead with the presentation.

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**Jan Lang** - *Ahlstrom Oyj - President, CEO*

Thank you and welcome from my side. We have had a quarter that sequentially was better than quarter four of 2012. And you could say also that the market environment was better than in the end of last year. However, we were seeing quite a lot of volatility in demand, various parts of the economies of the world.

But if we go to the presentation, the January-March in brief, first, highlights, as I said, sequential improvement, positive developments in our advanced filtration business which we now have as of January of 2013 separated in a separate business area at the same -- from the filtration business and also transportation segment.

And the reason why we did that was that we believed that the advanced filtration deserves its own focus, if you will, because of the fact that it is a growing business for us and we see good opportunities in this business going forward.

Transportation filtration made also progress, but particularly positive is that we now are starting some good growth numbers in Asia. We were also able to make certain adjustments in selling prices in the quarter.

The lowlights was a somewhat sluggish demand in North America, volatile, one could say, which certainly to me is somewhat surprising given the, in general, step-by-step positive elements of the economy, but we certainly have had some effects in (inaudible) demand in North America. Volumes were somewhat short of last year's quarter and, at the same time, we had higher input costs. Basically, the main challenge we have, in performance terms, the biggest one is our food and medical business. And I'll come back to that issue.

If you look at our Q1 numbers, in comparable terms to quarter 1 '12, we did have an earnings that was lower than quarter 1 '12. There is also a restated number that Seppo is going to refer to later, so EUR6.5 million against EUR10.6 million and percentage of net sales at 2.5%. Growth was 1.9% negative in the quarter. And, on the next slide, we can see the development by quarter in this slide.



I'll go to the following one to explain the quarterly operating profit development where we see that we had, during '12 the highest quarter actually in quarter 1 where we then saw a step-by-step weakening of the environment and our performance during last year. So, therefore, we are comparing to the best quarter now with the EUR6.5 million.

And the basic impact on this result was, on the positive side, price movement was somewhat up with, but at the same time, lower volumes and input costs higher, which we can see on the following slide where we have a waterfall charge from '12 quarter 1, where selling prices had an impact of EUR3.2 million whereas volumes were negative, about the same amounts, and raw material energy costs, the impact is negative, about EUR3.8 million. So, more or less, we've been able to mitigate the raw material input costs that we had, which are energy and certain specialized selling raw materials that had been increasing for us.

So, okay, price management, I would say the volume shortfall particularly in North America, a bit surprising for us when, other the hand, Europe where the economies are in worse shape, have been rather decent given the very difficult business environments. The volumes declined by 3% however, excluding capacity closures which show they were 1.3% negative.

And then a few comments of which business area, first, advanced filtration, which we have a 30 percent plus growth in the business helped by the Munktell acquisition obviously, with an underlying growth of 9.6%, which is a nice performance. And, here, as I said, we do have the growth opportunities and, therefore, it's been important that we put this in a separate business area to get full focus and our resource application to the business.

The generational growth came from the sale of filter media to gas turbine business and the life science applications, which, at the same time, was the main business of Munktell that we acquired.

Lowlights, we have increasing raw material costs, mercerized pulp, specifically, so, operating profits, EUR3.2 million of EUR24.3 million sales, which gives you about a 13% EBIT to the net sales. So this is our most profitable business in our portfolio.

Moving on, building and energy had a negative growth of 8.5% volumes, minus 6.5%. However, the majority or almost all of this was already due asset closures that happened during last year.

Some positive development on the flooring material demand in Europe, also, we have a strong position there, and then we've been able to recover the shortfalls we have in the wallcover business in China last year and I'm seeing again some good growth numbers there.

On the negative side, adverse product mix driven by sales of construction and consumer-related application in Europe which are -- meaning, that they have better margins in those than other production portfolio for building and energy. Business has been slow really given the economic environment in Europe.

But underlying I would say we've had lot of changes and actions in building and energy to get it in better shape. The underlying performance is continuing to strengthen overall even if we have a lower earnings than the previous quarter in this business.

The particular challenge in this business that we have reported and talked about earlier in the meetings (inaudible) business meetings that we have in this business era.

If we go to food and medical. Here the performance is poor. We have had some time challenges in the business and haven't yet been able to sort it out, working very hard to do that but there's some underlying challenges and problems that we still have in this business area.

Volumes were down quite dramatically very much dependent on demand for our tape business and also medical products and particularly in Europe, we have also some products and -- in various parts of the business to clean up the, if you will, the product range here in business with the medical.



Our key challenge in earnings terms is driven by commercialization of the Mundra plant which is in the medical business slowly but surely making progress there but it has been extremely slow to mitigate that, same concerns with Chirnside (inaudible) products that we are making slowly, but surely progress. But, again, we still haven't seen this again a challenge for us.

The Longkou plant is a tape manufacturing plant for Asia particularly China that started up around year end. So they're right now in a qualification process which at the same time has a negative impact on our earnings as we start up the plant (inaudible) this is a joint venture with a Chinese partner. So here we continue to take firm and solid actions to address the challenges.

Transportation filtration, the last one to comment here had a rather okay quarter. Volumes were up by 2.3% net sales, 4.2% earnings were also up slightly from previous quarter in this business. Higher sales volumes and the positive here is Asia where we have and acquired two and a half years ago a business plant in China which we have been rebuilding in terms of asset base and strengthening the platform their own capabilities. And now we start to see some positive growth out of this business.

Positive was certainly was our European development here in a rather difficult market environment. But, nevertheless, we've been able to have a slight growth in this business. We have to remember that the biggest part of the transportation filtration is driven by replacement rather than OEM, OEM as we all know as being rather challenging car sales in recent months in Europe but this doesn't short-term I think that's not significant. And then the regional performance has been positive.

And then (inaudible) we are -- this relates to the North America situation. Our heavy duty filtration, it represents a bigger part of the business in transportation filtration and it is predominantly a replacement business. We had a poor demand and consequently a poor sales in heavy duty filtration media in North America, despite as I said the economy is kicking along into a positive direction however (inaudible).

And here we have increased raw material specialized (inaudible) materials that -- and energy cost and input costs that were higher, but overall as I said okay performance. Seppo cash flow and (inaudible).

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**Seppo Parvi - Ahlstrom Oyj - CFO**

Okay, thank you, Jan.

First of all [on page 14] we have some information and some news (inaudible). We have (inaudible) became effective as of January 1st this year; that is why (inaudible) statement that is reflective of this page and outline what (inaudible) 2012 because for the profit and loss and balance sheet.

First of all, very positive EBITDA EUR3.1 million operating profit which is coming from the fact that part of the (inaudible) relating to (inaudible) that (inaudible) that part of the personnel costs that is now moved (inaudible). It's a net effect of EUR0.7 million positive that is coming from the fact that discount rate is not the same for (inaudible) related to investments in potential (inaudible), so that's why there's small net positive gain on the bottom line.

Then comes the total equity and benefit obligation differences and there we have some bigger figures. Now the background to the change in the rules and accounting principles is that we have earlier applied so-called corridor method, that means that the full liability (inaudible) has been recognized in profit and loss and that has been now taken fully into account and previous figures have been restated (inaudible) EUR 58.8 million negative and (inaudible) short of 7% that is 6.7 percentage points .

So that means that reported here at the end of the year which was 55.8% (inaudible) 62.5% (inaudible). Then moving to quarterly net cash flow from operating activities, and this is including discontinued operations, and the net cash from operating activities was negative by EUR21.4 million for the quarter. This was mainly negatively impacted by increased operating in capital.

And as you might remember we have had very good positive cash flow for all the quarters for the last couple of years and this wasn't changed now and, of course, something (inaudible) now very carefully and focusing on ensuring that there's no negative threat.



On the next page, you'll see the (inaudible) operating working capital (inaudible) some explanations on why there was such an increase. (inaudible) promote their acquisition that was done in the advanced filtration business. But the main part is coming from increased (inaudible) coming from the fact that (inaudible) some of the businesses especially related on processing we have been taking volumes or collecting volumes from the markets where we have not been so active in the past (inaudible) along the payment that have been difficult in traditional markets.

So we have opportunity for (inaudible) the payment in terms of the (inaudible) customers as such and also some (inaudible) in the factory volumes. Like I said, we are putting a lot the focus now to (inaudible) to reverse the negative (inaudible) the first quarter of this year. Turnover rate was 45 days at the end of the quarter, which is reasonable, but four days up from the end of the year.

Then we'll get to gearing -- gearing ratio was 73.9% reflecting the higher net debt used to make (inaudible) cash flow (inaudible) cash flow (inaudible). Also something to remember about the gearing that dividends in the EGM -- EGM at the end of March was booked and in the previous year those were booked in mid-Q2 in April but this year it took place in in March.

Also we have as you all know option to repay our EUR80 million (inaudible) loan in November this year. It's not a must but it's an option. And we are exploring refinancing options at the moment on packaging the potential repayment. But no decision has been made yet relating to repayment as such.

On page18 we have maturity profile of our medium and long term credit facilities and as Jan told you earlier we do not have any serious maturities in front of us this year or the following year in 2014. So the first peak in maturity in 2015 when we have our EUR100 million domestic bond mature. And those are the (inaudible) at our main facilities. We were in great (inaudible) of EUR200 million expires.

It is by the way unutilized at the moment. Liquidity remains good, total liquidity including cash and unused credit facilities was almost EUR300 million at the end of the quarter and on top of that we have undrawn (inaudible) facilities and cash flow overdrafts of EUR 555 million available for the cost.

Then moving to a couple of comments on income statement and balance sheet, first of all on income statement net sales down about EUR5 million. They're looking as Jan already commented, operating profit for the quarter EUR8.3 million compared to EUR10.7 million a year ago. This is including nonrecurring items of 1.9 million in third quarter this year and EUR0.5 million a year ago. Something maybe to note this is a small profit from equity accounting investments, that is from Suominen Oyj Thermal EUR0.4 million.

I think Suominen have (inaudible) performance, which is also reflected (inaudible) but this of course, we are the major shareholder Suominen. Op profit before tax is EUR4 million this quarter, compared to EUR6 million a year ago. And profit for the period including discontinued operations EUR7.9 million compared to EUR8.1million a year ago.

And just to remind that profit for the period from discontinued operations which was EUR5.4 million includes no depreciation as it is reported as discontinued operations, so no depreciation is taken that's why the result is a bit higher than expected.

Then moving to next page -- Balance sheet. I think the major change is the working capital we have already comment this, so I don't comment those. It is just to remind that on both sides of the balance sheet, we have first the full assets classified as (inaudible) sale and distribution to owners.

About EUR500 million end of quarter and on the liability side, liability is classified as (inaudible) for sale and distribution to owners about EUR210 million. And the (inaudible) was EUR171.9 million that includes EUR80 million (inaudible) and dividends EUR29 million were booked in March -- end of March after the annual shareholders meeting.

Then cash flow. And this is including discontinued operations. Net cash from operating activities was negative EUR21.4 million compared to EUR14.6 million positive a year ago and (inaudible) negative in this year by changing in net working capital EUR40.6 million and that is including not only effect from trade receivables (inaudible) or inventories but also from changes in some accruals and prepayments end of Q1.



Investments EUR24.2 million compared to EUR21.4 the year earlier. This year, we had some major payments including for the wallcovering materials (inaudible) in Binzhou, China, as well as filtration materials investment going on in Turin, Italy.

Then I have nothing else to add on the cash flow. And I move it back to Jan to comment on future prospects.

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**Jan Lang** - *Ahlstrom Oyj - President, CEO*

All right. Thank you, Seppo. Then on future prospects, first a couple words on high priority programs and focus for 2013. We have internally talked earlier about this also -- five high priority programs that are listed here on this slide. I will not walk through them -- each of them, but they direct our activities to execute on our continuing agenda.

This year, as far as focus topics and a high priority for us is to generate a platform for growth. And there are two elements in here that we have high attention. And one is bringing your products successfully to the markets, meaning go to market, launch product.

We have during the past two, three years to be able (inaudible) a process to be strong in generating new ideas -- ideas for product development and that starts to be in rather good shape from development process per se is -- and has already been rather good now (inaudible) trying to do and gearing up for is to be able to create higher level of differentiation and unique products.

The third is, which is right now is focusing very hard on this to be able to more successfully go to market, meaning launch product, and therefore bringing the products to the market here is a key element. And last week -- only this week, we launched a product in filtration with this increased capability called (inaudible) the Idea exhibition in Miami.

The other high priority initiative is sales growth in general and that is to be stronger in creating new business opportunities with existing and new customers. And a number of steps have been taken to improve that capability including (inaudible) organization that we did before year end amongst other -- ourselves, organization which is regional, meaning Europe, North America, South America, Asia.

We have organized ourselves in application-based structure per region, meaning segment driven rather than country-driven. So we now have application teams across Europe, across North America, et cetera. And that will give us, again, better focus on driving business opportunities. But there are a number of other things also that we've been working on to strengthen.

And finally, outlook is unchanged, meaning that we expect our sales to be between EUR980 million and EUR1.140 billion in revenue and our operating profit to be between 2% and 5% of net sales from continuing operations.

Thank you. That's my and Seppo's introduction. Thanks to you all.

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## QUESTIONS AND ANSWERS

**Juho Erkheikki** - *Ahlstrom Oyj - Financial Corporation Officer*

Thank you very much, Jan and Seppo. We have now concluded the first part of this conference call and are ready for your potential questions. Please note that you can also ask questions by writing them online.

Operator, if you would please go ahead with the questions from the telephone lines and we'll pause here for a couple of minutes.

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**Operator**

Thank you. (Operator Instructions). We have no questions over the telephone line at this time.



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**Juho Erkheikki** - *Ahlstrom Oyj - Financial Corporation Officer*

Okay. Well, if there are no further questions, I think we are ready to conclude this conference call. So thank you, ladies and gentlemen. And we hope to hear from you again in August when we are scheduled to report our Q3 -- sorry, Q2 2013 financial results. Thank you.

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**Jan Lang** - *Ahlstrom Oyj - President, CEO*

Thank you.

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**Seppo Parvi** - *Ahlstrom Oyj - CFO*

Thank you.

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**Operator**

That will conclude today's conference call. Thank you for your participation, ladies and gentlemen. You may now disconnect.

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