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AHL1V.HE - Q3 2014 Ahlstrom Oyj Earnings Call

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CORPORATE PARTICIPANTS

Juho Erkheikki *Ahlstrom Oyj - Manager - Financial Communications & IR*

Marco Levi *Ahlstrom Oyj - President, CEO*

Sakari Ahdekivi *Ahlstrom Oyj - CFO*

PRESENTATION

Juho Erkheikki - *Ahlstrom Oyj - Manager - Financial Communications & IR*

Thank you and good afternoon from Helsinki. Welcome to our Q3 2014 conference call and audio webcast. My name is Juho Erkheikki.

Today's conference call will be hosted by our president and CEO Marco Levi and our CFO Sakari Ahdekivi.

Following the presentation you will have a chance to ask questions. Please note that the links for the webcast and the slides are available on our website at ahlstrom.com.

So please, Marco, go ahead.

Marco Levi - *Ahlstrom Oyj - President, CEO*

Good morning, good afternoon, good evening. Thanks for joining.

I will focus our discussion today on the announcements. The first one related to the new executive management team, and then I will talk about Q3 results.

Today the board has approved a proposal on a new executive management team. The executive management team of Ahlstrom is going to be smaller and much more focused on the key initiatives that we have in place. In particular, Sakari Ahdekivi will get additional responsibility in the areas of IT and communications.

I reorganized the business into business areas, filtration, building and energy, food and medical, what has changed versus the recent organization that R&D, research and development, and overall operations, manufacturing, supply chain, engineering, manufacturing processes are going to be fully aligned to the three business areas.

The new VP of HR is going to be focused only on human resources where we desperately need to support to drive change in the current organization and the way we operate. Ms. Bono will continue to be the legal counsel. And then I have decided to support my direct alignment to me for the areas where we are going to -- and some new critical initiatives in the area of commercial excellence and overall sourcing later once again by a new member and the [historical].

So we're going to have three business areas that you see in the next slide in the normal and straightforward consolidation we have offset alignment to fully offset alignment to the three business units.

Moving to the quarter three results of the company, when you look at Q3 we have got another quarter where we show in profitability versus the same quarter of 2013 where [we are pleased] to see that growth businesses like advanced filtration, transportation filtration, and food has been growing, and we have increased the volumes in medical particularly out of our Indian operation.

The results are highly impacted by the overall product mix and successful pricing initiatives.

We confirm that our key project of this year, the resizing program is still on track at the end of the third quarter. And as you know, we have successfully completed and issued a new bond (inaudible) EUR100 million during the quarter.

The lowlights of the quarter I think are much related to low volumes in sales in what we call Building and Energy. In particular, the wallcovering business has been weak, so demand (inaudible) in Europe and due to (inaudible) in China where demand is lower than what we expected. At the same time, we decided to pull the plug on one of the key initiatives that Ahlstrom had called PPT, Porous Power Technologies.

Looking at the numbers, Sakari will have a much complete analysis of our performance. Looking at the key numbers, the EBITDA of the quarter shows a significant improvement versus the same quarter of last year 57.5% improvement, and year-to-date EBITDA of the company is at EUR67.1 million, 22.5% better performance versus the same period over last year.

Operating profit excluding NRI EUR9.7 million, EUR8.2 million better than the same quarter last year, and year-to-date performance is 91% better than the same period last year. Interesting to see that we've been driving the overall operating profit excluding NRI to [4%] performance versus 2.1% of the same period last year. Gearing have gone up, and Sakari will talk about the key elements of our (inaudible), which (inaudible) gearing 84.5%, and we'll describe what item in quarter three.

Moving to the next slide, we have a summary of our quarterly sales development, pretty stable but, in particular, when we compare Q3 this year versus Q3 last year, comparable sales have gone up 2.3% pretty much driven by the business areas mix and, in fact, that margins are higher in filtration-related businesses including related businesses versus building and energy. We already mentioned (inaudible) by lower volumes in wallcovering.

Looking at the quarterly operating profit performance excluding NRI, this graph in the next slide shows the gain in other quarters where we have improved our operating profit versus last year [it was fitting the bridge], but key positive elements are the ones which I already mentioned plus some easing the raw material cost of inflation.

On the lowlights, we keep capital business units there, and (inaudible) 25 in Scotland or Longkou in China. Those two business units have shown improvements, but we have not reached the given performance, yes.

In the next slide you see the page of operating profit of Q3 this year versus Q3 last year. The EUR8.2 million that I mentioned before, EUR3.7 million is coming from [price and mix], EUR2.4 million coming from raw materials and energy, EUR2.7 million coming from rightsizing, EUR0.9 million coming from positive FX. The negative net impact comes from volume with the positives and negatives that I mentioned in the previous slide of the presentation.

Like in the previous reports updates on the rightsizing, overall targets we channel cost saving of EUR39 million. We are in line (inaudible) personnel reductions of 400 people globally.

And on third quarter 2014 we have achieved EUR22 million in cost savings in continuing operation results. The highlights in the program is [receding important risks].

The next slide as you see a deeper analysis of the different business units that we always start with our last situation, which showed quite a good performance in Quarter 3, higher sales due to a combination of volume and pricing versus the same quarter of last year, in particular industrial and gas turbine applications which show significant volume increasing the softer demand in the high efficiency air application.

Overall margins are record high in this quarter amounting to EUR5 million excluding NRI. Of course, also in this business area there has been contribution of lower fixed costs.

Building and energy, these are the numbers that confirm my previous comments. Volume is significantly down [negative 9.7%] versus the same quarter last year, comparable sales minus 6.4%. Drops from some priority areas in the area of construction and automotive with unrelated materials in Europe, and the wallcovering business and flooring in Russia due to the situation in construction business in Russia have been prevailing in the overall bonds.

So overall operating profit was [3%], same quarter of last year was negative.

Lower volumes, we have a new plant in Binzhou, China, therefore ramping up, so additional costs.

The ruble has been weakening, so (inaudible) Russia have a double negative effect. And we are seeing an increased operational cost with our Osnabruck Corporation in Germany.

The food business has been doing pretty well in the third quarter. We've got volumes growing 5% and comparable sales up to 11.5% pretty much driven by our performance in tea, coffee, and some areas of packaging materials. We've been able to increase margins 6.9% of sales and also benefiting from lower fixed and raw material cost. Overall operating profit has increased by almost EUR4 million quarter to quarter.

Medical, volumes are up mainly due to sales. Part of India, SMS-based rates and (inaudible) products. We've got also higher sales of (inaudible) and dairy products in Asia (inaudible) compared to the same quarter of last year of the partial loss that is one of the big [estimates] in the United States.

Overall, the news of overall operating (inaudible) in India is close to breakeven. Now so we have made clearer improvement operating this asset in terms of operating discipline, accuracy to sales, customers and overall cost to operate the plant. In the overall balance we've got some of those impacts on product mix because we have been selling more SMS, which is a more commoditized business.

Transportation situation doing pretty well, mainly on the margin side, volumes are up 1.3% compared with (inaudible). You'll see that volumes have been growing particularly in North America and Europe. We have increased in price and we have increased the number of products and we have additional margins in our mix.

As a consequence, all the comments of our transportation business are positive, and overall situation business confirms to be a very good performing business moving now from [post volume].

After this analysis, I'm pleased to now go to Sakari Ahdekivi who is going to comment on financial.

Sakari Ahdekivi - *Ahlstrom Oyj - CFO*

Thank you, Marco.

So turning to the income statement I'll start from there. Marco already commented on the top line. I won't go back to that, but maybe to comment on the cost side. As Marco said, rightsizing is on track so we are getting savings both in our overheads and production as well as an SG&A.

The plus clearly visible in the numbers, which is reported there for a couple of reasons, we had the pension cost in the UK in Q3 which was a non-recurring item as it hits the SG&A.

Also, when ramping up the shared service center in Vilnius we've now transferred two countries, we have more in the pipeline and, of course, we need to build up the organization to receive before we can actually get the savings. So for overlap periods we do have some extra cost in the pipeline.

The further thing which distorts the comparison is that we opened a new product and technology center in Shanghai in May, and that's, of course, a cost which we did not have in 2013. But other than that the SG&A savings from rightsizing are coming through in the end of quarter for the reasons mentioned the SG&A is actually flat.

Then, of course, the quarter was characterized by a lot of non-recurring items. We publicized the withdrawal from Porous Power Technologies or the earlier also disclosed the net of tax impacts of that event. On the operating profit level the impact was EUR11.6 million and net of tax was EUR8 million.

Also as part of our global annual process of evaluating our assets, we made an additional depreciation in our Chirnside [25] production lines, which amounted to EUR5.3 million in the P&L, as well as driving up some [unneutralized] obsolete glassfiber production assets, which was EUR2.9 million. Also during the quarter we announced that we were partnering our IT operations with an excellent third party that is a non-recurring cost related to that action, which is EUR1.7 million in the quarter.

Now these do not fully adapt the EUR23.2 million. There are other rightsizing related to non-recurring items in that EUR23.2 million make the total number.

The financial expenses were up. There's a clear reason for that. We launched a new bond during Q3 successfully, and we'll also tended for the outstanding old bond which still does not mature until one year from now.

On the tax line, we see a tax credit related to the PowerPoint [for Star] technologies action. And that those are really the main items in the income statement.

But bottom line operating profit excluding NRI is EUR9.7 million compared to EUR1.5 million. That's the real positive for the quarter.

Okay. Turning to balance sheet, in the total non-current assets we, of course, have the Munksjo shareholding. Just as a reminder, the value of that at the end of the quarter was EUR42.6 million. We also have in that number a shareholding with Suominen, another company. However, after the Q3 closing we have actually divested those shares and that divestment will have positive impacts on (inaudible) in the fourth quarter.

If I would factor that into our gearing, which is currently standing at 88.4% the ratio would be roughly 13% better than the reported figures. It would actually bring us to bid on our gearing guidance range. And the equity was, of course, impacted in the quarter by the non-recurring items, among other things. And then just as a reminder that the equity does include the EUR100 hybrid bond.

And moving forward to the development of working capital, operating working capital continue to slightly increase in the quarter. This is the difference compared to the previous year when actually in Q3 operating working capital decreased. However, last year's biggest (inaudible) discontinued operation so they're not fully comparable. And we do expect the operating working capital to decrease towards the end of the year as it usually seasonally does with December being a slow production month. So that is to be expected in Q4.

However, our working capital days are up by two days year-on-year, and this will continue to be a [profit item] for us beyond Q4 next year.

Now turning to the statement of cash flows, EBITDA was higher than in the previous year's third quarter. But the big difference in the cash flow is coming from the change in working capital. There was a sizable positive number last year. This year the positive number is pretty smaller. Also the financial items are impacting the cash flow.

And these numbers, we, of course, have the cost of the bond issue as well as the (inaudible) the existing -- the old bond.

CapEx is clearly lower than Q3 last year and we are concerned in cash in the CapEx point of view.

On the next slide, we see the quarterly net cash from operating activities in our business. Q1 typically being a negative quarter and the other quarters typically being positive. But as described earlier on the low side is some cash generation in the quarter this year.

And so the gearing development on the next slide the gearing was steady at 85% for three quarters, slightly up now largely as a result of the non-recurring items that were booked in Q3. However, again factoring in the divestment of Suominen shares, the number will be around 75% as the transaction price for the Suominen shares was EUR33.3 million.

Then our maturity profile of our credit facilities hasn't much changed with the issue of the new bond, which appears there in the 2019 column. In the 2015 you have the rest remaining amount -- outstanding amount of the previous bond are roughly at EUR54 million.

Liquidity continues to be good and no further big events in terms of debt financing are expected during this year. And finally to the outlook, we have narrowed the outlook ranges both in the net sales and the operating profit margin excluding non-recurring items.

So previously we had a net sales range of between EUR930 million and EUR1.09 billion. That has now been narrowed to EUR960 million at the low end and EUR1.02 million at the top end, so narrow from both sides. Similarly, the operating profit margin excluding non-recurring items has been narrowed from the 2% to 5% to the new range of 2.5% to 4% of net sales.

Our CapEx guidance remains unchanged of EUR80 million for the year.

That concludes my part of the presentation. And I think we are ready for questions.

QUESTIONS AND ANSWERS

Juho Erkheikki - *Ahlstrom Oyj - Manager - Financial Communications & IR*

Yes. Thank you, Marco and Sakari. We have now concluded the first part of the conference call and now ready for your potential questions.

Please note that you can also ask questions by using the webcasting center and sending them online.

So, operator, please go ahead with the telephone lines if there are questions and we'll take a break here for a couple of minutes.

Operator

Thank you. (Operator Instructions) We will pause just a moment to allow everyone to signal. (Operator Instructions)

We appear to have no audio questions at this time.

Juho Erkheikki - *Ahlstrom Oyj - Manager - Financial Communications & IR*

Okay. We'll just wait for maybe a couple of minutes if somebody has any questions online, so we'll stay tuned for a little one.

Operator

(Operator Instructions) We appear to still have no questions.

Juho Erkheikki - *Ahlstrom Oyj - Manager - Financial Communications & IR*

Okay. As there seem to be no questions at this stage, I think we are about to conclude this presentation. And we'll thank you for your time and we'll hope that we'll hear again from you in January when we are scheduled to report our Q4 and full-year 2014 results. Thank you.
