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Q3 2020 NKT A/S Earnings Call

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## PRESENTATION

### Operator

Ladies and gentlemen, thank you for standing by, and welcome to the NKT Q3 report 2020. (Operator Instructions) I must advise you that this conference is being recorded today, Tuesday, the 10th of November 2020.

I would now like to hand the conference over to your first speaker today, Alexander Kara. Please go ahead.

### Alexander Kara NKT A/S - President & CEO

Good morning, everybody. Welcome to this Q3 2020 NKT report. Thank you that you take the time to listen to our Q3 results and I would like to start now here, first, whom is that will present. And we go to -- so we have here in the room with me Line Andrea Fandrup, who's my new CFO, which, she has started some months back. And we have also here Basil Garabet, President and CEO of NKT Photonics, who will talk to you after I give an introduction to the NKT numbers.

And so coming to the NKT numbers, the quarter 3 was a satisfactory result, improved revenues and earnings from all 3 business lines, which is actually quite satisfactory, considering the circumstance of COVID-19, and particularly in application and service that we could accrue also on that part and then solution from the strong backlog and execution where we could substantially increase our revenues. In Application, we have a good, strong market in Denmark, Germany and Netherlands, which compensated other markets which were weaker due to COVID-19 impact. Service & Accessories grow due to deliveries in various countries in the region, including Middle East for Accessories. And in Service, we have done repair to Skagerrak 1 and Skagerrak 2, which, Skagerrak 1, in Q3, which was quite successful. Overall, an organic growth of 28% compared to Q3 last year, which I consider as very good compared to the current market situation with the uncertainty on COVID-19.

So you see on the graph on the right side, for the first 3 months, we increased revenues by 20% and EBITDA, we also on the right track from Q3 last year to this year from 3% to 7.1%. So overall, on a good way.

If we look now on the Solution business. We have several projects in the backlog in execution, also from different segments, offshore wind, like Dogger Bank, oil and gas and so on and different technology. Overall, the execution was satisfactory, and even partly better-than-anticipated. And as in the one project, we had some delays. So improved revenues and profitability going up. We went up from EUR 110 million, EUR 165 million on revenues and organic growth, 47% and EBITDA, EUR 12.3 million, which is -- yes.

Then we go to the next. So here, you see the list of orders, what we have received in 2020. And it's not tiered by timing. It's ordered by size. SuedLink, SuedOstLink in Q2 and then in Q3, BorWin5 and Shetland. And earlier in the year, Attica-Crete with an interconnector. So all projects sum up to EUR 2.1 billion, and all our DC projects, so all of these with the exception of Attica-Crete, which is an MI technology. And with the interconnector offshore wind, so a quite nice mix and particularly also good that it's easy as we are quite strong in DC technology. So EUR 500 million orders received in Q3 is a nice number.

Going to the next slide then. We have increased the backlog through -- from end of Q2 from EUR 2.7 billion to around EUR 3.1 billion in

Q3, which is a record high for NKT, and -- which gives us a lot outlook also for going forward in terms of execution visibility for the coming year. And so the backlog has increased to around 5x the revenue of -- LTM revenues of solution by end of Q3 from EUR 241 million (sic) [EUR 641 million] to up to EUR 3.12 billion, which is very nice to have 5 points on the backlog of the revenues. You can see the different projects here. It's a mix of offshore wind, interconnectors and oil and gas. And we're working on those, obviously, then to execute them in (inaudible).

Going to Application. Application, I mentioned already in the introduction, we had some headwind in some markets due to COVID-19, but could compensate it with a market like in Germany, Denmark and the Netherlands and with also to -- with a better mix to improve the profitability in Application. And then, of course, if revenues get tougher, we have a strict cost control and work on efficiency. So overall, we were able to grow 5% compared to last year to EUR 103 million and an operational EBITDA of EUR 5.1 million. So this is a quite nice achievement, I would say.

Going to Service & Accessories. Service & Accessories was also satisfactory, a nice growth, EUR 38 million revenues and EUR 4.4 million EBITDA. I mentioned already the Skagerrak 1 and 2 repair of an MI cable, which we repaired. We have a new facility established in Troisdorf, which allows us to have more offerings to our customers. And overall, the Accessories business is growing, particularly the medium voltage side in Europe and also outside of Europe, also here satisfactory result.

Now coming to the COVID-19. COVID-19, we have seen the first wave early this year. And now we see a second wave, which is even more massive, if you read the news. And so far, we -- our highest priority is and will be that we take care of the people, our people, in the factory. So, let's say, are protected as good as we can. And also, you say, outside, where we advise them to take care. That is very important because if they are not impacted by the COVID-19, then we can run our factories, which is without any interruption or shutdown, which is a highest priority. So we have seen some cases for example, in, with COVID-19, in Czech, what we have not seen in before, but on a very low level. I mentioned already that the market, some lower medium markets that we -- that will be slowed down, but we could manage the well so far in compensating it with other markets. So you see on the graph here on the right side, the growth quarter-by-quarter, 17%, 13%, 29% from Q1 to Q3, and overall, 20%. So that's so far, so good.

So good, several high-voltage orders. We work on tenders. So far, we have not seen any impact caused by COVID-19, which is a positive. And so let's hope it will continue like this in the -- going forward.

With this, I would like to hand over to my colleague to talk about NKT Photonics.

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

Thank you, Alex. Good morning. The NKT performance in the third quarter did improve after a very challenging first half of 2020. Organic growth was positive in the third quarter. And we do see the light at the end tunnel on our growth, and we hope that, that continues in a positive mode. The positivity was mainly pushed by the Medical & Life Science segment of our business. This market has, in fact, been quite resilient to the COVID pandemic and our sales did increase and helped that positive full result.

The industrial side of our business, the Industrial segment, is still challenging. It was challenging in 2019, and that continued into 2020. It is changing a little bit, but not as fast as our other 2 segments. And we still see some weakness in the market, mainly, again, due to the COVID pandemic slowing orders and pushing out deliveries and causing other challenges that we have in manufacturing. In Aerospace & Defence, we benefited from a push in the market and fewer restrictions from the COVID pandemic on our customers. We continue delivering on our large contracts and, in fact, have some new and very beneficial contacts -- contracts in the pipeline. For the quarter, I'm pleased to say the order intake also increased by 11% in Q3 compared to Q3 of 2019, again, showing positivity. The order increase was over all 3 segments.

We move now to an update on the impact of COVID-19 on our business. As Alex said, our main priority is our employees and the well-being of our employees. That's the thing that we cherish the most because it's the thing that makes us go forward, and it's the driving force in NKT Photonics.

The pandemic, as I said, had affected us quite dramatically in the first 9 months, more so in the first 2 quarters than in the third quarter,

and again, just to reiterate, mostly on the Industrial segment, which happens to be our largest segment. Having said that, all our production sites have been in operation. We've had some delays, but most of our sites are in full operation. And looking forward, as Alex said as well, going through a second wave at the moment. So the uncertainty still looks very high.

And with that, I'm finished with my segment, and I'll move it over to Line.

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**Line Andrea Fandrup NKT A/S - Executive VP & CFO**

Thank you very much, Basil. So going into the financial update. On the first slide here, it's Slide 16, you see the income statement in the quarter. The quarter was influenced very positive by a good improved earnings coming out of a growth on our top line, both within NKT, the 28%, as Alex mentioned, coming out of all business lines. Both Solutions, Applications and Service & Accessories. On the Photonics side, also returned to growth that materialized into good growth for the whole NKT.

On the operational EBITDA, it's good also to see the performance improvement on NKT Cables from last year to this year and Photonics also in the quarter stabilizing. So the operational EBITDA margin on the full group amounts to 7.1% on the quarter compared to a 4.3% last year. If we look at the EBITDA then after one-off items, we improved threefold from EUR 6 million last year in '19 up to EUR 21 million. Depreciation and amortization staying flat and an increase in financial items due to foreign exchange rate effects. A slight change on the tax rate with the net result improved compared to last year.

So if we turn to Slide 17, some highlights from the balance sheet. The most favorable item here is the working capital. From orders won early in 2020, we had prepayments in NKT Cables that impacted the working capital very favorably. So right now, we are at a level of minus EUR 130 million and Photonics more or less flat compared to last year. If we go into the net interest-bearing debt levels, they are improving, obviously, by the improved earnings, but also on the improved working capital. So at this point, at a 3.6x compared to last year at 16.7x, but even under Q2, we had a 7.6x.

Coming further into this presentation, you will see also our update on the capital structure that we announced today.

So going to Slide 18, just a slight peek into it -- on the net working capital. As mentioned, it's primarily the projects awarded earlier this year that the returns favorable into the working capital of EUR 130 million. And if you look at the last 12-month rolling working capital, we are now at a minus 4.8% to revenue, which is a very good level. Of course, Solutions being the business asset within NKT Cables, there will be fluctuations over the years and quarters from the (inaudible).

Going to the Slide 19, the group's cash flow statement. Positive cash generation from -- over the last year of EUR 148 million, coming from the earnings and the working capital here. If you look at the CapEx levels of the quarter, they're more or less flat against the last year. What will happen also Q4, when going into the next coming years, there's a much higher level of investments due to the corridor projects coming in this year. So that remains to be reflected even more in the numbers than compared to what you see here.

And Slide 20 is just a look into the net interest-bearing debt levels and a bit about what they consist of. Out of the EUR 153 million on net interest-bearing debt, this consist of EUR 160 million (sic) [EUR 161 million] of mortgage debt and minus EUR 8 million drawn on revolving credit facility, where we have a full availability of EUR 300 million. Further to that, we had EUR 41 million of these liabilities. So overall, at the 3.6x level this quarter, we had a good improvement from last quarter.

We have liquidity reserves of EUR 188 million, also at the end of Q3 here, where cash is EUR 7 million and our credit facilities amount to EUR 181 million. It is in our intention, as also mentioned in the announcement, to do a rights issue before end of November and close it off before end of this year.

If we go to the outlook on the next slide. This quarter, we are coming out with a specification on our outlook for 2020, which is that we will end the year on revenue around EUR 1.1 billion and in the upper end of our guided operational EBITDA of EUR 40 million to EUR 60 million, obviously, reflecting the good results in Q3.

If we look ahead to 2021, we are also giving some transparency into this. We expect revenue of EUR 1.1 billion to EUR 1.2 billion, which is

a growth compared to 2020. So we are continuing the traction as seen. On the operational EBITDA level, we're also expecting to improve to a level of EUR 80 million to EUR 110 million. There, of course, are assumptions behind each numbers. And for the outlook on 2021, we do expect this if we don't see a material impact from COVID-19. Obviously, we need to have the satisfactory execution of our project in the high-voltage backlog, and we also expect and assume here to have additional awards of high-voltage orders impacting 2021 financials, continuing good improvement in the profitability levels of applications as well as satisfactory offshore (inaudible) on [power cables].

So leaving 2021 on that and looking ahead on the medium-term ambitions that we are introducing here again. The green transformation is ongoing, and by that, also some good wins into the NKT business. What we see and look ahead against is that we will grow our compounded average growth rate over the next years to medium term, on average, above 10%. And meanwhile, also increasing the operational EBITDA margin to around 10% to 15%. The assumptions behind this is a successful -- being successful in our high-voltage tender, with satisfactory terms and conditions, a strong utilization of our production and installation assets as well as a satisfactory mix, and in general, across all business line and satisfactory execution in this.

So if we flip to Slide 22 on Photonics. On Photonics we reinstated the outlook for the year in October, and we maintained this outlook of minus 2% to minus 12% organic growth on revenue and an EBITDA margin of 1% to 6%. At this point, we will not provide more outlook for 2021, and we need to have a better visibility in the markets.

On the medium terms, we are still waiting for some more certainty or more transparency into the years to come. And therefore, at this point, we are actually -- we are abandoning the medium-term targets we have. And at this, we will await the COVID pandemic before we look at what to expect for the medium-term on Photonics. But it is the expectation that the revenue development will return to healthy growth rates once the markets have normalized.

On this final slide of the financial part, a look into our capital structure target, which we're changing this quarter and ahead. The change here is that instead of a leverage ratio target of 1.5x, we are reducing to 1.0x. This is coming out of NKT becoming a larger and even more project-driven business, and with that also comes the need for a strong balance sheet. So we are targeting a more robust capital structure. To secure, we also -- when growing, when having longer and more complex projects that we also need a higher level of bank guarantees to back this. We maintained a solvency ratio target of minimum 30%. And when the target is met on our leverage ratio and the solvency ratio, we will also aim for paying out a dividend for 1/3 of profit of the year.

So with that, I will turn over to Alex, which will give an update on the capital structure review.

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

Yes. Thank you, Line. So just let me say something about the road map about NKT from where we're coming and where we are going. If you look at the year '16, '17, we had the acquisition NKT of the ABB high-voltage cable business in Karlskrona and having source to acquire the DC technology, which enabled NKT to participate also in the corridor projects, which we were quite successful, I would consider. Further, we had 2 acquisition in NKT Photonics. Then in this period, we had the demerger of Nilfisk to focus on the cable business and Photonics and some divestment of a noncore business in the cables area.

In '17/'18, we had some challenges with the postponement of orders in high-voltage area for various reasons, and this has been reflected in the very low result from last year 2019, as you know. In -- it picked up orders in the end of second half of 2018, is more than EUR 800 million, is also in Johan Sverdrup and other projects, which was quite important. And we have also, in this period, a quite good development in Photonics with a double-digit growth.

Now in '19 and first half of 2020, we have seen a huge order intake, EUR 750 million more in 2019. And then in the first half, the corridor project with SuedLink and SuedOstLink, with amount about EUR 1.5 billion in Q3, which was very important for the future. We have done the first capital increase and (inaudible) accelerated book building of EUR 93 million in May to strengthen our balance sheet. And we said also, we will have another capital increase going forward, and we will do that now in November, as Line said. And then we had the change in the management, as you know, and also in my management team.

Today, second half and onwards, we have a record high order backlog with above EUR 3.1 billion, which is very positive. And Photonics,

we -- the Board of Directors resumed a strategic review as there's too much uncertainty in the market, as you just also heard before. We have received nonbinding offers for a smaller part, noncore part of NKT Photonics, which is currently being evaluated. We will strengthen our balance sheet going forward with the rights issue over these preemptive rights of the existing shareholders. This will come, as said in November, to have a stronger balance sheet as our projects are becoming bigger and needs more guarantees. And also we need this to order, to execute the backlog, the German corridor, but also future projects, which we're expecting as a part of the transformation of the green agenda.

So this is where we stand. Going forward, we are looking for growth at above 10% and higher profitability is the next phase of NKT.

With this, I think we can go to questions. Please feel free to ask questions to us.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions) Your first question today comes from the line of Akash Gupta of JPMorgan.

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#### **Akash Gupta JPMorgan Chase & Co, Research Division - Research Analyst**

It's Akash here from JPMorgan. My first question is on 2021 guidance. So maybe if we can start with what kind of assumptions do you have for known project segments. So I think, I mean, looking at your backlog facing 20% of projects, backlog would be converted into sales in next year. So I think you have nearly half of -- or more than half of 2021 revenue visibility secured in your backlog. But if you can tell us about what sort of assumptions you have for other 2 segments and then also on margins. That's question number one. And then I ask a second one afterwards.

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

Yes, thank you for your question. So we are still early in the year as we guided EUR 80 million to EUR 110 million. So it's another right range as we are early. We have, of course, a good backlog and visibility of the DC project. And here we are fine, but we are still capacity in the AC three-core C cable, which we are looking to catch one or the other order, which will result in utilization for next year. And then, of course, also important is that we continue the good trend started in application and also have some one or other offshore repair for next year.

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#### **Akash Gupta JPMorgan Chase & Co, Research Division - Research Analyst**

And my second question on this medium-term margin target. I mean, if you look at your next year guidance, then it looks like you would be in the high single-digit and even at upper end of guidance range, you would be slightly below 10%. So is it fair to say that by 2022, it should be in your margin guidance? Or just wanted to know this, can we assume like by '22 or will it be more '23 when you will be within your margin corridor as you target in your medium-term assumptions?

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

Yes, Akash, your math is correct. So -- but I mean we said we will grow 10% in average. So meaning in the next year. And also, yes, midterm, we define as 3 to 5 years. So there can be, of course, small differences from year to year, that we had in 1 year high, another lower.

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#### **Akash Gupta JPMorgan Chase & Co, Research Division - Research Analyst**

And my final one is on working capital. So basically, I think the improvement in Q3 was ahead of expectations. Can you say anything about Q4, whether there is any other milestone or down payments that are still pending in Q4? Or whether you were going to consume some of working capital in final quarter?

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

We don't want to be too specific. But of course, there's always milestones payment and solutions. And yes, [what else shall I say?]

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**Line Andrea Fandrup NKT A/S - Executive VP & CFO**

Yes. And I think we -- the working capital will continue to fluctuate as seen and just looking at 2019 as a -- not at a normalized level, I would say, definitely a very low level. So more or less on par going into the end of this year from current level.

**Operator**

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

**Kristian Tornøe Johansen Danske Bank A/S, Research Division - Senior Analyst**

Just first of all, a clarification on the medium-term targets. So you say 3 to 5 years with the base being 2019, so we are talking 2022 to '24?

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

Yes. Well, 2022. Yes, yes, so starting '19 and then you add 5 years, '21, '22, '23, '24, '25. These are the 5 years.

**Kristian Tornøe Johansen Danske Bank A/S, Research Division - Senior Analyst**

Okay. Great. Then in terms of the equity issue you expect to carry on towards the end of this year. So if we look at the midpoint of your EBITDA guidance for next year and take your current net debt, then in order to get to this net debt of EBITDA of 1x, you would need to lower debt by exactly EUR 100 million. Would that be fair to assume that, that is what you're targeting in this upcoming equity issue?

**Line Andrea Fandrup NKT A/S - Executive VP & CFO**

So we haven't sized the rights issue yet. That is work in progress. So we will come back further on that one that is done.

**Kristian Tornøe Johansen Danske Bank A/S, Research Division - Senior Analyst**

All right. Fair enough. Slightly along the same line. Obviously, if we look at U.S. offshore wind, there's quite a substantial build-out already, and looking at the auctions coming up over the next 12 months, that will only increase. So with the equity issue, you do plan -- what room do you have for further expansion? And specifically, what option could you pursue in the U.S. sort of short term and long term?

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

I mean we communicated that we expand a factory in Cologne and Karlskrona. This has allows us to produce all kind of cables, either DC or AC, three-core AC. So we can obvious also quote three-core AC project in the U.S., offshore or also interconnectors if they should appear or get realized. So we have, in that sense, no limitation.

**Kristian Tornøe Johansen Danske Bank A/S, Research Division - Senior Analyst**

Okay. But would -- I mean are you considering to build capacity or to do acquisitions in the U.S. market? And would your capital structure, post the equity issue, enable you to do this?

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

No. No, we have now -- we set what we plan to do, and that's it. So no further capacity expansion at this point in time nor anything else.

**Kristian Tornøe Johansen Danske Bank A/S, Research Division - Senior Analyst**

Fair enough. Then my last question on applications specifically and the assumptions you have put into your 2021 guidance. If you can elaborate on that and specifically, what you expect to sort of gain earnings rise from internal measures?

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

No. I mean, we have obvious actions ongoing to improve the efficiency in the factory and the profitability and work on profit on the portfolio as well as on discipline in pricing. That's all ongoing. But then we have the uncertainty with COVID-19. And we have that before in discussions where we said there is certain uncertainty and then some slowdown in the demand in some countries. And this is difficult

to predict how that will develop. So that is really a challenge. What we cannot say so far. We were able to compensate with other markets and also to secure the bottom line with cost out and so that was so far positive. So the assumption for next year is that we continue the trends that we have.

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**Operator**

We do have a few more questions on the line. Your next question comes from the line of Casper Blom of ABG.

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

Hello?

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

Yes, now we can hear you.

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

First of all, great to see earnings trending in the right direction again. And then a couple of questions. A couple of them actually being follow-ups. I'll start with a follow-up on Kristian's question with regards to Applications. It seems to me like Applications has kind of like turned a corner this year after some years with internal challenges. Would you say that sort of the self-imposed challenges that Applications had in '18/'19 are now kind of behind you and that you can sort of start shifting focus a bit more to the external side rather than having to solve internal issues and perhaps become a bit more offensive in the Applications business? That's my first question.

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

I mean, we continue, of course, working on, if you want to say, optimization in Applications. That's a normal thing. And we also mentioned that we will move the 1 kV from Denmark (inaudible) to Czech Republic. So that is a normal topic. So we focus on internal stuff, if you want to say. Also, we roll out an ERP system and we have received them in Central Europe, where we need to make sure that this go in the right direction. So we have internal stuff and then also external in the market with the customer, with the portfolio, how to penetrate the market. So that goes hand in hand, both is required to improve the business performance of Application.

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

Yes, I appreciate that. But is it fairer somehow to say that you've kind of like put out the fires that were on in Applications and maybe there is a bit more time to focus on clients and on the commercial side than there has been the last couple of years? Or is that a completely wrong way of looking at it?

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

No, that's -- you can say so if you want. We have also a new manager leading Application business. We have a plan to go forward. That's all fine. As I said, we will roll out the ERP system. We had some hiccups in the past in the Nordics. We do expect that we do not repeat that. But there's always rolling out the ERP system -- there's also always some risk also, which we have mitigation action in place. So you can say so if you want to, call it the fire with -- yes.

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

I will not hold you accountable for the previous management team. That's absolutely not fair. But I think they, at one point, mentioned a target of an EBITDA margin of 6% to 8% in Applications. Is that something that you could sort of recognize as being possible down the road?

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

I think the margin mentioned in the past was 7% to 9%. And if you continue with our action, this is not out of reach.

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

Okay. Fair enough. Then a question regarding your medium-term EBITDA margin target of 10% to 14%. Could you comment a bit on sort of the different variables that can take you to the high end and low end of that range? I suppose some of it is depending on the magnitude of orders that you're able to get into the Solution business. But what are sort of the most important drivers? Is it pricing in the market? Is it the number of projects? Or is it other things? What takes you around that range?



**Line Andrea Fandrup NKT A/S - Executive VP & CFO**

Casper, this is Line talking. I guess you answered more -- some of that question. So obviously with a range like this, we are, of course, dependent on the tenders coming out, some of the choices being made in different plans of interconnectors and onshore/offshore cables. So that's one prerequisite, that there are tenders out there, and we win our fair share of that on satisfactory terms and conditions and pricing, of course.

Then another assumption, which is important, is also, as we talk about in 2021, the optimal utilization of our production and installation of assets and wanting the whole execution satisfactory. So I would say that is kind of the outline of what can take us from the 10% to 14%, depending on the development here.

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

Okay. And then just a clarification at last here. Did I understand correctly that you would say that a working capital to sales ratio of around minus 2 was a sustainable level going forward? Or did I not understand that correct?

**Line Andrea Fandrup NKT A/S - Executive VP & CFO**

I don't think we said a number on that. But otherwise, it's in history, I don't know, I'm looking at margin.

**Michael Nass Nielsen NKT A/S - Head of IR**

What we're saying is that we've seen a -- it's Michael speaking here, Casper. So we've seen a good improvement in Q3, obviously. You should not expect the same magnitude of improvement in Q4 but more -- a more stable level.

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

Okay. But is that -- I mean, the minus 4.8%, is that then a sustainable level going forward?

**Michael Nass Nielsen NKT A/S - Head of IR**

Well, I'll just continue your pace here, Casper. That is very hard to say because, obviously, as you've seen in the past, it depends a lot on the order intake and the prepayments associated with those orders. I think what we've said all along is that, generally, we should be in negative territory in Solutions, and we will tie up capital in Applications. I think that still holds. But whether the level then would be exactly around the 4.8% going forward, that we are not going to guide for today.

**Operator**

Your next question today comes from the line of Andrea Scatozza of Goldman Sachs.

**Andrea Scatozza Goldman Sachs Group, Inc., Research Division - Research Analyst**

The first one is on the rights issue, and in particular, on the size. Considering year-on-year target capital structure and the fact that the CapEx for expansion will be spread between 2020 and 2022, I was wondering at a high level thinking whether you are considering the strategic review of Photonics as a moving part when it comes to the target -- the rights issuance size for this year. That's my first question.

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

I'm not sure what I understood fully your question, the connection is not so super good. So the rights issue, I mean, we communicated the rights -- focus of the rights issue to finance the investment of the capacity expansion in Cologne and Karlskrona. And we gave an indication in previous what it could be, around EUR 150 million. And for Photonics, that has no impact. And we just declared that we have incoming questions, which are the Board of Directors looking into it as it is non-core business of Photonics.

**Andrea Scatozza Goldman Sachs Group, Inc., Research Division - Research Analyst**

Understood. And then the second one is on pricing as some of your competitors have mentioned lately that they've seen some pricing pressure in the tendering environment. I was wondering if you see any risk of solution margins being diluted in the incoming orders, other than that of pricing? Or what's your view on how pricing is playing out lately?

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

I mean, in general, I can say, if -- let's take, Applications, for example, we are very price disciplined. We are really look that we get the returns that we needed for our investments in what we have in the factories. So we already are disciplined on pricing Applications. In Solutions, it's the same. So the utilization, in general, with the higher demand, is going up. That should have a positive impact on the pricing. Of course, each integral project as such have their own dynamics, depends on the capacity utilization for that window when that would fit in into production slot. So that might be different on an individual tender on Solution, but overall, it should go up, and it needs to go up.

**Operator**

(Operator Instructions) Your next question comes from the line of Claus Almer of Nordea.

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

I have also some questions. The first question goes to your capital structure target. When do you expect to reach this minimum or maximum onetime level? That will be the first one.

**Line Andrea Fandrup NKT A/S - Executive VP & CFO**

I can. Claus, this is Line talking. It is also a medium-term guidance on the capital ratio target here.

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

Then a question to Photonics and Basil. The decision -- or the possible decision to partly divest some of the activities, what drives that? And is it possible to carve out other parts of Photonics?

**Basil Garabet NKT Photonics A/S - CEO and President**

We -- well, to answer the second part of the question, no. The -- what we're looking at is a smaller noncore part that we got incoming, and we're reacting to it.

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

Right. So we should not expect that Photonics will be sold if that's the decision in different pieces?

**Basil Garabet NKT Photonics A/S - CEO and President**

No, no, no, not at all. The core of what we do in the laser business is very robust, and it's a whole piece. Like you said, this particular one is a noncore business.

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

Right. Is it fair to then assume if noncore, that the valuation, if you end up selling this business, will be below what we could expect out of the remaining of Photonics?

**Basil Garabet NKT Photonics A/S - CEO and President**

No. I can't comment on that. I mean it's -- the valuations of Photonics companies are pretty obvious in the market, and we will report on that once it happens.

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

Fair enough. Then a question regarding the midterm target for the cable activities. So you have the minimum 10% revenue growth. If you looked at your pipeline, do you, beyond 2021, at least see a more steady growth? Or would it be a bumpy road? That will be also a question.

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

Yes. The question whether they're bumpy, I mean, no. I mean, we said, in average, 10%. And we have a good backlog now and with the corridor project going forward, that's it, starting 2022, like a large base business. And then we have the others which continues build up, let's say, the revenue stream. So I do hope not that bumpy.

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

Right. And then just about the structure of the guidance. So you're coming out with a guidance for 2021...

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

Michael wanted to chip.

**Michael Nass Nielsen *NKT A/S - Head of IR***

Yes. I just want to say, Claus, that we -- you know that we have investments ongoing in Solutions. These investments will gradually translate into higher revenue in '22 and then further in '23. So there will be step-wise improvements also linked to the fact that we actually have extended our capacity during that period of time. And then we will obviously need to be capable of filling that additional capacity, which we are a firm believer of being capable of the market that we're seeing.

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

Sure. So then about the whole structure of the guidance. You gave the guidance for 2021 and that's up to a 9% revenue growth, at least on the numbers. So maybe you could put some color to why you decided to come up with that guidance compared to a minimum 10% growth guidance until 2023 or '25? It's always good to have a short-term performance that is supporting the long-term guidance, at least. Or it's just no backed on a very strong pipeline of projects?

**Michael Nass Nielsen *NKT A/S - Head of IR***

It's backed on the strong pipeline of projects, Claus. So when you look at it, that's also why we are telling it that it's a compounded annual growth rate that we are looking at. So when you look at it over the medium term, well, then it should be above 10% on average per year.

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

Okay. And then as to the margin guidance. Should we think this is a range that you may be in the early phase of 3% to 5%? You are probably closer to the 10%. And then in the end of the -- after 5 years, then you are probably aiming for the upper end of the margin guidance. Is that a way to think about your margin guidance?

**Line Andrea Fandrup *NKT A/S - Executive VP & CFO***

Yes. We're not giving that specifics into it. The assumptions can vary over the years. And by that, also the margin. So it's not early-stage or late-stage indications.

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

Okay. So in theory, it could be 14% in '23 and 10% in '25. That's the way to think about it?

**Line Andrea Fandrup *NKT A/S - Executive VP & CFO***

In theory, yes.

**Operator**

We do have one more question at this time. Your next question comes from the line of Artem Tokarenko of Crédit Suisse.

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

My first one is around your 2021 outlook. Could you maybe specify what are the main moving parts or the main determinant factors for you ending up at the lower or the high end? And also how much more order wins do you require for the next year to get you to the upper end of your outlook, please?

**Line Andrea Fandrup *NKT A/S - Executive VP & CFO***

So this is Line speaking. So talking about 2021, obviously, it's a little early stage to give a guidance for 2021. So with that, we are indicating some uncertainty by guiding as we do. As Alex also alluded to, we are seeing the, let's say, the second round of COVID-19 coming, and that is an uncertainty to our business also to a certain degree. We need to win some more orders in the high-voltage, the AC three-core [heat] cable. We do have capacity to take on a bit more there. And then further, we need to, of course, execute the projects

work that we have in our backlog already, improving profitability in Applications and satisfactory level of offshore power cable services. That is the assumptions we're working with and why we also have this little bit wider range of the outlook for '21.

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

Okay. But I guess just given your revenue range in your guidance or EUR 1.1 billion to EUR 1.2 billion, is it fair to assume you require at least another EUR 100 million of orders for next year delivery to get you to the high end?

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**Line Andrea Fandrup *NKT A/S - Executive VP & CFO***

No, no, that's not the way it's kind of built at all.

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

Okay. My second question is around your midterm targets. Could you maybe talk a little bit about whether the high end 14% margin target could be achieved with your -- only with your current backlog, considering its mix, pricing and if you are able to execute properly on the backlog? And also maybe as a follow-up to this. Also looking at your current capacity, how much years of 10% growth do you think is available from your current capacity? And how would you think about your capacity longer term?

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**Line Andrea Fandrup *NKT A/S - Executive VP & CFO***

So I'll start with your first question. The 14%, it's not only our current backlog. It's obviously also winning more projects over the years, which is an assumption around the whole medium-term ambition level. We need also to see a good level of terms of conditions and pricing, obviously, in the tenders coming out over the years.

Can you repeat your second question?

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

Yes, sure. Just with your target of growing at 10% per annum, considering your capacity, how many years of that growth do you think your capacity supports? And would you be willing to add more capacity down the line?

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

I mean we have the capacity which supports the corridor project and additional orders. So -- and then, of course, we optimize further the factory output in Solution, but also in Application and seeing whether we can get more cables out of the factories. So I mean, maybe we said 10%, above 10% over the next years, and this you can assume as it is stated there. And we said medium term is 3 to 5 years.

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

Okay. And my last question is around Photonics guidance. And could you maybe elaborate on the reasons behind you withdrawing the midterm guidance? And specifically, whether that's just timing related because the guidance was for the next 3 years. Or that's more of a structural concern that, that business wouldn't be able to make the 25% margin?

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**Basil Garabet *NKT Photonics A/S - CEO and President***

No, nothing structural. It's really where we are in the pandemic at the moment to get more clearance on the landscape. Once that happens, we will give guidance. The pandemic has affected our business in a different way than it has affected cable. We are in different markets. And once we have clearance, we will give guidance.

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

Okay. And maybe just a quick follow-up on this. You mentioned in the reports that you've added -- that you've increased the cost base in Photonics this year. Could you specify how much is that on an annual basis, please?

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**Basil Garabet *NKT Photonics A/S - CEO and President***

We're not reporting on that. We obviously had planned a year without a pandemic. So we will -- we are looking at the situation as we speak at the moment.

**Operator**

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

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

Okay then. Thank you much that you took all the time to listen, and thank you for your good questions. With this, I think we can close. And we can wish you everybody a good day and a good week. Thank you very much.

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**Line Andrea Fandrup NKT A/S - Executive VP & CFO**

Thank you.

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**Operator**

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

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