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PRESENTATION

Operator

Good day and welcome to the NKT Annual Report 2017 Conference Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Mr. Michael Hedegaard Lyng. Please go ahead, sir.

Michael Hedegaard Lyng *- NKT A/S - President, CEO & Member of Executive Management Board*

Thank you, operator, and good morning and welcome to the NKT webcast covering the annual report 2017 that we released this morning. My name is Michael Lyng, President and CEO in NKT and together with me here today I have CFO, Roland Andersen; and Basil Garabet, CEO of NKT Photonics. Let's look at the agenda on Page 4. First, I will start with a short presentation on highlights '17 including our perspective on NKT. Then Roland will follow me presenting the financial highlights for '17 and after this, we'll move to NKT Photonics where Basil will do the presentation before we then join the ends with the Q&A session.

Slide 5, just to -- for the last time show that the Nilfisk demerger has been executed with success back in October '17. In connection with that, we also changed the name from NKT Holding A/S to NKT. So I guess you are all very familiar with this, so I suggest we just move on. Here, slide -- on some group highlights for '17, for the NKT part, we increased revenue and operational EBITDA also supported by the ABB acquisition that we closed back in March '17. We increased revenue by EUR 307.6 million up to EUR 1.058 billion and with that we more or less met our guidance top line of around EUR 1.1 billion. On the operational EBITDA side, we almost doubled that to EUR 138.3 million and we increased the margin from 9.7% to 13.1% and embedded in these numbers are a good fourth quarter where we realized an EBITDA margin of 12% compared to 9.6% last year. Later on we will probably talk a lot about the visibility for '18 and also the projects awarded in '17 and it should not come as a surprise that we have not succeeded in filling up backlog for '18. However, that being said, we are pretty satisfied with the order intake we saw in the offshore wind segments with the Borssele Beta order award that we announced earlier the year, but also the preferred supplier awards on the Moray East and Triton Knoll that will give good visibility in [end] '18 going into '19.

In the Products business, we saw a negative 3% organic growth. This is primarily due to the fact that we had very high comparison numbers in Germany because of the [photo year] and we talked about that earlier in this -- in '17 also and then we saw some challenging markets in particular in Poland that were tough in particular in the first half of '17. However, that market improved slightly in the second half of '17. Just touching briefly on NKT Photonics before Basil will go into the depth here. We actually crossed a milestone of reaching EUR 50 million in top line yielding an organic growth of 7% and operational EBITDA of EUR 3.5 million and here it should be noted that as also announced back in third quarter, we were negatively impacted by EUR 2.5 million related to some long-term incentive programs. We also in this business concluded the acquisition of Onefive and Basil will explain more about that later on in presentation and we continue to strengthen the organization from being development-oriented to a real industrial company. So we continue the journey of investing into the future in this business.

If we move on to Slide 7, just looking at the guidance that we have had throughout '17. For the NKT part, we can conclude that we are in line with the targets for '17. We realized operational EBITDA of EUR 138 million over EUR 140 million that we guided throughout the entire '17 after announcing the conclusion of the ABB transaction. NKT Photonics had slightly lower numbers compared to what we communicated back in third quarter, announcement in November. However, you should also remember that we are talking pretty small numbers, so EUR 0.5 million actually improved the margins -- have a negative impact on margins quite dramatically. So we are also here satisfied with the developments.

If we move into the hot topic for today's call, the outlook for '18, we are guiding a top line for the NKT part of revenue of between EUR 1 billion, EUR 1.1 billion standard metal prices and that should yield operational EBITDA in the level of EUR 90 million to EUR 110 million and this is of course reflecting the fact that we do not have sufficient visibility into the factories in the second half of '18 predominantly in the Karlskrona site that are being half empty in the second half of '18. For the NKT Photonics part, we are guiding a revenue of EUR 65 million to EUR 70 million and with that we should be able to do a EBITDA of around EUR 10 million. So with that, we actually start to demonstrate strong potential for this business and also strong operational gearing when we manage to increase the top line.

If we move on to Slide 9, for the NKT part, we see 2018 as a transition year. We are fully aware of the fact that the guidance, operational EBITDA level is not what was expected and it's also a number that we cannot be satisfied with. I think, however, it's also important to mention that we cannot change it a lot. We are in a business with a lot of fixed cost and a lot of capital employed and there is a limit to what we can do to reduce costs. In particular, because we do look into '19 and '20 where we expect and continue to expect a significant pick up in activity levels and this is what we currently are seeing in the pretty intense tendering activity that we see. So it is a tough situation to be in where a big part of the organization are extremely busy servicing the customers with what they expect from us, doing a lot of detailed tendering work on a lot of numbers of projects, and also very complicated projects. And in the other area of the business, we have that half empty factory, but that is just a reality and we cannot change that. Now we start with this guided [interval earlier], we will of course do whatever is possible to be in the upper end of that range and if we manage to get in business that can have a meaningful impact in '18, and also later on in the year look into opportunities, so maybe moving production from '19 into '18, we will of course try to do that in order to maintain the number or also have it slightly better. but that's too early to be more precise and that's why we have started with this range.

I think also -- before we move on, I think also it should be noted that we still do not yet have full flexibility between the site in Cologne and the site in Karlskrona, so the Cologne site is actually fully utilized and expects to be fully utilized in '18 and also with the visibility that we have on new orders that we have received in the offshore wind segment, we will continue to see a very high capacity utilization, but unfortunately we cannot yet move that order backlog to be produced in Karlskrona.

If we move into Slide 11, looking at the different segments, we can conclude that we realized 7% organic growth for '17. If we look at the projects area and if I should try to put a little bit more flavor on that, we are satisfied with the execution of the offshore projects and segment that we saw in fourth quarter and throughout '17 actually, and in the legacy ABB business, we also had seen a very high activity level on the NKT Victoria vessel and also a high utilization of the factory in Karlskrona. So taking into account that we only have 10 months of ABB into the numbers, we are actually pretty satisfied with the EUR 138 million that we achieved in '17. There is a small element of postponement of revenue in the end of '17 into '18, but that's how it is in project business, we from time to time see delays either caused by us or caused by our customers. In the Products business, we actually had an okay-ish year in some markets, but that being offset by markets or the markets being more challenging. In particular, Sweden, U.K., Scandinavia, we saw good traction in the market, and as we also have explained a little bit throughout '17, we actually have been in situations where we could not supply sufficient volume to the market, which is something we try to compensate for by optimizing our manufacturing footprint, but that's -- good traction was then offset by the Polish market being very difficult in particular in the first half of '17, and then also from the fact that the German medium-voltage market were very strong in '16 and we saw a decline of up to 10% to 15% into '17 and that of course impacted the numbers.

If we look into what is it that we try to work on and also try to tie it in a little bit to the EXCELLENCE 2020 journey that we launched a couple of years back, then we continue the work to drive excellence in whatever function we have in the organization. We did a lot of organizational changes in '17, and since October '17 we have been operating in a completely new structure. The aim of that is of course to imbibe excellence into what we do. One example on that is that we now have all our factories reporting to COO. The COO's responsibility is really to get more capacity out of our factories and also to optimize capacity planning across the sites. That should yield more capacity and looking into '18 in particular in the product area, it is also a capacity that we expect we're able sell to the market.

So we continue that journey. We of course also looking into how to accelerate growth and here the ABB acquisition that we finalized in March last year is of course key. We have a completely unchanged view on the attractiveness of that business and we are very confident that we will see a significant pick-up in the markets in the years to come. Early on, we have -- and also on the Capital Market Day, we communicated on expected orders awarded to the industry in '18 and '19, the [2x 5] that you clearly remember and difficult to be precise on the numbers, but we actually have an unchanged view on the potential -- and the potential awards to the industry in the years to come. There can probably be elements of slight disappointments or areas where we see small delays in project awards. There have also been awards in the U.S. market that did not really develop the way we expected 6 months back, but it doesn't change our view that we are looking into '19 and '20 with a significant higher utilization.

That's also tying into the next slide here, on Slide 13 that you have seen before, we still have a lot of the business in the segment develop and grow, that goes for the DC high-voltage onshore, but also the AC and DC offshore segments that we are -- that we just talked about. We also continue to see a pretty good traction in the accessory business and as well as in the service and installation business. The building wire segment medium-voltage, we don't do anything in order to improve it, we will see declining margins over time and that's why we -- it is very important and it's a [must-win battle] for us to continue to improve the business in order to offset the price pressure that are very typical for commoditized segments.

In the last column here, the turnaround, the (inaudible) we have not talked a lot about that in the last year, but we have now reached a conclusion that we will look into a potential divestment of that business and bear in mind that it's not really a significant volume for us, but we somehow have concluded that there are better owners for that business that can do the necessary investments in order to improve the business and also we have concluded that it's not really core business for NKT.

It's probably the last area that we will divest following the automotive divestment and the China divestment that we did in '17 and '16 and if we manage to do this, we will be a pure play business focusing on energy cables and service and accessories.

The high voltage onshore business continues continues to be tough. This is the segment below 220 kilovolt onshore segment that are also being more and more commoditized and also a segment that are impacted by the relatively low order intake in the [other] end of the segment that we saw in '17, not only for NKT, but also for the industry in general.

The next Slide 14 is probably not new for you, this is just touching on the ABB acquisition we finalized back in '17, the integration of that business is progressing according to plan. We will do some initiatives in '18 in order to speed it up because we have time to speed it up and become even stronger when we then move into '19. The synergy potential of around EUR 30 million that we communicated back in March, our view on that is unchanged, but as you also know, the majority of that or 2/3 of that somehow relates to having more volume to execute and produce in our factories. So it will be impossible to realize that synergy potential if we do not see a significant pick up in the markets and that is also what we expect to see.

Then on the Slide 15, we have a fewer more words on the market development in the high-voltage power cable segment. I think we can conclude that for '17, we saw very few DC projects award and unfortunately the [2] result did not go our way, but it's not only NKT that somehow are in the situation where we could do more, that also goes for some of our key competitors. Having said that, we do see a lot of positive traction in markets. We early on talked about the offshore wind market where we also have been awarded significant orders and we are still working on more orders to be hopefully realized in the coming quarters. We can also look at the European Commission that also have looked into this and have declared more than 100 projects as being projects of common interest where some of these projects were provided funding in the beginning of this year. So we continue to see a very intense tendering activity, but having said that, I share your view that we also very soon would like to see that being crystallized in actual order intake, but as said before, we expect to see that during '18. So with that I have finalized my part of the presentation and I would like to hand it over to Roland to take us through the financial parts.

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

Thank you, Michael. My name is Roland Andersen and I'm CFO in NKT. On Slide 17, we have an overview of our backlog and the projects included in that by end of the year. Our high voltage order backlog at the end of '17 was EUR 760 million in market prices and EUR 690 million in standard prices and compared to the end of Q3, this was slightly lower and that reflects obviously the part that we have produced during that quarter and then the addition of the offshore wind order of Borssele Beta in The Netherlands.

The 2 preferred supplier agreements in the U.K. are not part of the backlog as the customers have not reached final investment decisions yet. We, however, expect that to happen. The options for booking more tenders or more projects with an impact to our P&L in '18 is still present. The available projects are relatively limited. We're working on a few tenders, but obviously also tenders that can start filling our backlog for 2019 and onwards.

If we flick to Slide 18, this picture many of you know that shows our improving EBITDA level and also EBITDA margin over the past 3 to 4 years. During the course of '17, our operational EBITDA development is obviously driven by the acquired activities from ABB. Q4 this year also was characterized by seasonality in products as well as phasing and a little bit of delays in projects in the high voltage business.

If you look at Slide 19, the development in working capital is also continuing the positive trends. The development in '17 has been strong and it has been a continuation of the focus we have seen the previous 3 years. The driver, especially in '17 is driven by the acquired business, also the working capital initiatives that we continue to work on and of course, the composition of our project portfolio as it looks today. I think that there is a point in by the end of the year is probably not a sustainable level, but an extraordinary good level for us.

If we move to Slide 20, this summarize the numbers and the highlights for '17. Revenue increased in Q4 driven by the acquired business. Also operational EBITDA and correspondingly a significant good performance in the acquired business is driving the EBITDA up. With the acquisition of ABB, we also added around EUR 390 million in goodwill, that means that even though we have also picked up our earnings, our RoCE is lower by the end of '17 compared to previous year.

Our investment level for '17 has gone to EUR 62.9 million, it reflects -- supports the added business, but it also indicates that we are still investing in IT infrastructure platform upgrade for our applications business and investment into DC capabilities in Cologne.

If you move to Slide 21, this is not so different from the other slide, but this is NKT A/S and basically have now included the Photonics numbers in the P&L. For the full year, Nilfisk is considered discontinued operations and that means not included in the P&L number. Revenue was up by EUR 96 million in standard metal prices. This was mainly due to the acquisitions, but also the divestment of our automotive is reflected as we can see in the table on the right hand side as divestments. So revenue increased by EUR 111 million from acquisitions, divestments of EUR 11 m and then there is metal prices and few other things basically leaving a flat organic growth on [group level].

Our one-off cost in Q4 totaled EUR 17.7 million. We account EUR 6.1 million as ABB integration costs. We also had costs related to the demerger of Nilfisk of EUR 4.4 million and then we had EXCELLENCE 2020 costs and other strategic initiatives of EUR 7.2 million including [here under] broken deal costs associated with our engagement in the general cable process.

If we move to Slide 22, this shows the development of NKT A/S and the leverage ratio moving down by the end of 2017, (inaudible) pro forma calculate the leverage point by end of Q3, excluding Nilfisk leverage ratio was 2.2. By the end of this year NIBD was EUR 293 million and the leverage ratio was 1.9. This leverage ratio was obviously positively impacted by the extraordinary good level of working capital. And with that, that was the financial highlights you can see in the group and I'll give it over to you Basil.

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

Thank you, Roland. So if we move on to Page 24. We've as per usual divided our business into the 3 segments, the 3 market segments and the first one, which is Imaging and Metrology, which this year actually went up to 56% of our revenue. That's because we saw significant organic growth in that particular segment. We've also released new products into the segment primarily the SuperK EVO, which is a supercontinuum white laser product platform and we're seeing first OEM projects already running in that segment.

In the Sensing and Energy segment of the market that we are in, that accounts it to 30% -- just over 30%, 31% of our revenue. We had solid demand for our Koheras fiber lasers in the year, up significantly on the year before. However, we did see a couple of steps backwards due to delays in a lot of the infrastructure projects that we had in the LIOS segment. That has started to reverse into the Q4 and we're seeing a lot of the contracts that got pushed out are now in primarily in 2018.

And finally, in the Material Processing segment, which is one of our new growth areas where we're concentrating on, we acquired Onefive in Switzerland. Onefive is a leading ultrafast laser manufacture. The acquisition was completed on the 1st of September '17 and that has given us a significant strength and foothold in the industrial market and the medical market. In that segment, our fiber and gain modules actually went up on the year before. That segment is only 13% of our revenue, but going into 2018, we expect that percentage to be much higher.

We move to Page 25 and we go through the financial summary for '17. Q4 came in at EUR 21 million compared to EUR 16.2 million in the fourth quarter of '16. As mentioned, we saw an organic growth of 13% in the quarter and EBITDA numbers of EUR 5.7 million. For the year, as mentioned earlier, we broke through the EUR 50 million mark and came in EUR 51 million. Our organic growth came in at 7% and our operational EBITDA is as also as mentioned before, lower than the year before. That really is impacted by a provision of EUR 2.5 million for LTI (Long-Term Incentive) program for senior management. Excluding these, the EBITDA numbers would have been slightly down compared to '16.

The year came in at [18%] over the year before and obviously a portion of that as we mentioned was the organic growth, the other portion was the acquisition of Onefive in which we had 4 months of revenue. We are preparing for future growth. We've implemented a new ERP system and we've added a number of new employees in engineering and manufacturing. The capital employed for the year including goodwill was up by EUR 19.7 million, that's mainly due to the acquisition of Onefive.

And finally, if we move to Page 26, these are the strategic priorities for us in 2018. First one is to move up the food chain, expand from being primarily supplier of components to complete optical systems. We've undertaken that in all 3 market segments that we are in and that's moving satisfactorily. We're also focusing on organic growth in '18. We're looking at the consolidation of the companies we've acquired and increasing our revenue with our OEMs. We also are implementing throughout our operations, LEAN manufacturing and scalable manufacturing and we are putting through a program of commercial excellence that we will see the benefits for in this quarter, actually in Q1 going forward. And finally, as all high-tech companies that are successful, fast introduction of new products is a key action item for us and we'll continue doing that into the year. And with that, I hand over to Michael.

Michael Hedegaard Lyng - *NKT A/S - President, CEO & Member of Executive Management Board*

Good. Thank you, Basil, and thank you, Roland. So, with that, we have concluded the presentation and we are ready to move into the Q&A session. So, operator, anybody with a question?

QUESTIONS AND ANSWERS

Operator

Yes. certainly, Sir. (Operator Instructions) We will now take our first question from David Vos from Barclays.

David Anton Vos - *Barclays Bank PLC, Research Division - Analyst*

I have 3 if I may. First of all, could you shed some light on understanding the earnings bridge into 2018. It occurs to me that on revenue that is virtually flat year-on-year, this is quite a big drop, which is coming, of course from the project business as you've indicated, but could you just say how much each of volume pricing and if you will sort of synergies perhaps negative as the vessel utilization for example is a lot lower impact on that earnings bridge, rough back of envelope calculation suggests that you may see as much as 50% of the earnings disappear. So it would be very helpful if you could shed some light on that, that will be the first question. I'll take the other 2 afterwards, please.

Michael Hedegaard Lyng - *NKT A/S - President, CEO & Member of Executive Management Board*

Yes. Roland, do you want to answer that?

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

Yes, thank you. Thank you, David. First of all, if look at our order backlog, it is clear that we're missing orders for production next year of EUR 150 million or more, so that is one thing. The second thing is, of course, when you do that, we also have 12 months of the factory in Karlskrona, so that's another one, you need to consider. And then as we have discussed before, 2017 were actually quite a strong year. If you look at our production portfolio for '17, we have had MI, mass impregnated cable production in Karlskrona. We have had basically full load on our extrusion lines. The ship hit the water in beginning of May and was deployed less than 10 days after and has been so for most of the time since then. And in Cologne, apart for our challenges in the onshore market, also the offshore line there has been been fully utilized. So we're coming out of a relatively good '17 into an '18 with less utilization on the different lines both in the factory, but also installation wise, so that's what's causing that decline in EBITDA.

David Anton Vos - *Barclays Bank PLC, Research Division - Analyst*

Okay, that's clear and are -- if each of that effect sort of 1/3 of that overall decline, then is that fair to assume?

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

No, that's too -- [let's not generalize] -- so it has to do with the composition of the MI line and the time it took to produce that in Karlskrona and so on. So it's a mix of these elements.

David Anton Vos - *Barclays Bank PLC, Research Division - Analyst*

Okay, you did not mention pricing. Is it fair to assume that pricing will turn a little bit worse versus what you've seen in the past as presumably you will now need to take some actions to get the factory back and fully loaded or more fully loaded perhaps?

Michael Hedegaard Lyng - *NKT A/S - President, CEO & Member of Executive Management Board*

I guess you refer only here to the project business and we do not see a significant lower price level in the orders that we are tendering, all the orders that we were awarded in -- throughout '17 compared to prior years. Having said that, we of course have a strong aim of filling up our capacity, but we always want to balance that with what is expected from market development. So for '18, we don't see a significant pricing impact in the numbers.

David Anton Vos - *Barclays Bank PLC, Research Division - Analyst*

Okay, my second question would then be on the cash flow in 2018. There is no guidance on that in your presentation. Could you perhaps shed a bit of light on what you're expecting there, and also in relation to maybe your ending net debt position by fiscal 2018?

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

Yes, we're not guiding specifically on this, David, but if you assume EBITDA is cash equivalent, that would be a fair assumption. Then I think the investment level you have seen in '17 is probably at par in '18 because we'll continue to finalize what we are doing on the platform side and especially on the DC capability side in Cologne. So that's also a data point for you. And then, on the working capital side, I think we ended the year quite extraordinary good actually, right? So, most likely that will have a negative impact to the cash flow during next year. So if you add that up, I think it may end up breakeven-ish or slightly negative.

David Anton Vos - *Barclays Bank PLC, Research Division - Analyst*

Yes, that's my sense as well. I mean, by my calculation, which differs perhaps slightly from yours, 2017 was already a modestly negative outflow in free cash flow. It would be fair to assume, I presume that, if we only look at the drop in EBITDA year-on-year that, that will be the sort of magnitude of deterioration in cash flow, is that fair?

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

That is a fair assumption, but you need to bear in mind that the number of projects is also impacting working capital, right, the way you construct the projects, so actually a inflow of projects would most likely benefit your working capital whereas if projects are running off, it will be negative for your working capital.

Michael Hedegaard Lyng - *NKT A/S - President, CEO & Member of Executive Management Board*

If I can just add on the CapEx side, we, as you all know, we are constantly looking into when and how to potentially add more capacity in either Karlskrona or Cologne in order to be able to supply more DC capacity to the market if that is required. And that is, of course, a little bit difficult to put in into a bucket because we don't want to see it, we don't want it to hit that bottom or [start] push before we actually also see the requirement for more capacity in the market. So we expect that, that will happen in '18, but it's difficult to say and we of course, also have some opportunities for timing that into '18 or potentially into '19, so that's also affects us.

David Anton Vos - *Barclays Bank PLC, Research Division - Analyst*

Understood, understood and then my final question, Michael, would be in relation to your sale of equity shares at the end of 2017. Could you just help us understand a little bit why you sold such a substantial amount of shares and also perhaps contextualize that in relation to your holdings in Nilfisk as a result of the split that was effectuated in October last year? Thank you.

Michael Hedegaard Lyng - *NKT A/S - President, CEO & Member of Executive Management Board*

No, I actually don't think I want to entertain you more on this topic. I know you have been discussing this with Michael heavily and I also know that you even have tried to get out information that are not particularly available, which is not really the way we want to do business here. What you can see is that I still have a lot of holding in NKT and you can also see from the notes that I'm about to execute new options that I can do now, which means that I still have [around 1% invested business]. So I'm pretty exposed to NKT and also committed to the long-term development and more than that, I don't want to comment.

Operator

We will now take our next question from Claus Almer from Nordea.

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

I have a few questions also. The first question goes to this probability weighted order intake potential. Michael, you touched upon this during your presentation, but maybe you could give a little bit more flavor into the more let's say absolute numbers. I guess it's fair to assume the EUR 5 billion order intake in '18 is probably downgraded, should we expect it's kind of EUR 4 billion, and then should we add this less EUR 1 billion to the '19 number, that will be the first question.

Michael Hedegaard Lyng - *NKT A/S - President, CEO & Member of Executive Management Board*

I think Claus, when we gave you these numbers, it was an order to somehow demonstrate the potential of the market development in the years to come and we gave you the numbers back in September last year and what is very important for us to stress is that, that view is actually unchanged, but of course, it can be very difficult to then be precise on whether the [5 is 4 or 3] or whatever and whether that missing 1 or 2 is then moved into '19 or some of it moved into '20. You know exactly how we have calculated the potential by looking into concrete tenders and expected tenders in the market. We have added a probability factor to that, in order somehow to demonstrate what do we foresee being orders being awarded to the industry as such. Then I would also like to say that we probably had or we had hoped for a better result of the [RFP] in the U.S. because there were some significant orders there, that does not mean that we do not continue to work on them. It just means that, that given [that's] part of what was being awarded recently, but the potential have been -- are unchanged. We are also working together with our competitors on significant order awards hopefully to be visible here in '18 on a number of interconnect projects, for example the [Whitinger] projects, the Sudlink projects are moving forward as expected. We have significant offshore wind projects also being awarded to the industry as such in the coming quarters. So for us, the overall picture is unchanged, but I probably also agree with you that the 5 is maybe lower than 5 for '18, but it's not canceled, it's postponed into '19 and potentially into '20.

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

Okay, thanks and then the second question goes to the Q4, it seems like Q4 has been -- more on the low side, I know you explained part of these trends, but maybe you could add more into the exact numbers on an underlying lower level or it's more a timing Q4 2018 that cause this lower profitability? Thanks.

Michael Hedegaard Lyng - *NKT A/S - President, CEO & Member of Executive Management Board*

I think we have stressed a number of times that you should not expect much more than [114]. And you also know that when you have these pretty complicated and large projects, there is always management assumptions on how much risk provisions do you want to release et cetera, et cetera and we have not released a lot of risk provisions in '17 in order to reach the EUR 138 million target. So for us, fourth quarter is not any weaker than expected, you should also remember that there is a negative seasonality impact from the product business in fourth quarter and of course the NKT Victoria is not as busy as it is in second and third quarter in the fourth quarter. So we also want to make sure that we -- for the guidance in '18, we have as good a starting point as possible to deliver hopefully the upper end of that range as indicated. So much more than that is difficult to add, Claus.

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

Okay, so then just a follow-up on that one. In the new guidance or the guidance for cables in 2018, do you include some risk release provisions or how should we think about that?

Michael Hedegaard Lyng - *NKT A/S - President, CEO & Member of Executive Management Board*

No, there won't be any big chunks laying for release as you've seen in the past because we have in all modesty our risk management and our project management has been a bit more sophisticated in the sense that we will release risk more often related to different gates or milestones reached in the project, so it will come more as a successive release as and when we complete stages in the projects, so more than that, no.

Operator

(Operator Instructions) We will now take our next question from Kristian Johansen from Danske Bank.

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

Thank you. So first question is on the guidance. So obviously you are guiding for a spread of EUR 100 million on revenue in ['17, you had a gross margin of 48%], so theoretically that should sort of imply an almost EUR 50 million earnings spread, but you are obviously only guiding EUR 20 million, can you just sort of help me understand the dynamics going from the spread in revenue to earnings?

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

I think you cannot do it that way because the way we calculate gross margin is basically top line minus material costs, right? So you don't have the variable production cost in that number, that is somehow below and then -- and of course, the incremental margin on [missing] or more top line are significant in a project business like ours with a lot of high fixed costs. So we are talking about an operational EBITDA margin of 25% to 30% or even higher in some situations.

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

But your guidance only imply 20% then?

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

No, it doesn't Kristian. Well, maybe I misunderstood your question a little bit, can you explain a little bit what you're looking at?

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

I mean, I assume your revenue in the higher end indicates that more orders and more business, which will increase your top line by EUR 100 million. Given the high levels you just explained, I would have assumed your earnings to increase by more than EUR 20 million from the lower-end to the higher-end?

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

That depends, but that depends on the composition of the product portfolio. So you can't reason like that, that's actually the question from David, I think, your [not know] exactly what is the composition and how much revenues are derived from outside the factories, installation, civil works and so on, and how much is inside the factories.

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

Okay, fair enough, then just on the topic, can you just on the applications business and on the high voltage onshore, what are you assuming sort of '18 versus '17 on earnings?

Michael Hedegaard Lyng - *NKT A/S - President, CEO & Member of Executive Management Board*

No, we are not guiding that, but in the applications business we are expecting some nice organic growth rates from pick-up in markets, from the fact that we have realized a nice [payment agreement with EDS] in France and on medium-voltage that partly actually will be produced in Cologne. So we do see a nice organic growth journey for the applications business.

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

But is it fair to assume you are expecting higher earnings then for the applications in '18 and '17?

Michael Hedegaard Lyng - *NKT A/S - President, CEO & Member of Executive Management Board*

Yes, it would be fair to assume, we expect improvements in that part of the business.

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

And then high-voltage onshore, you've previously been fairly specific in stating that the [law], should we expect a similar level for '18?

Michael Hedegaard Lyng - *NKT A/S - President, CEO & Member of Executive Management Board*

I think we -- the cost of the new organization that we implemented, we will somehow take a different view on the high-voltage onshore, historically that were only being produced in Cologne and we did not produce anything else in Cologne. Now as we are having a more realistic view on our operating sites, we will try to optimize across and move away from the somehow [siloed] thinking that we have had for a number of years, one example of that is that we are, that we are moving medium-voltage to the Cologne facility that will improve the factory Cologne results. And it is not necessarily fantastic business, but it will somehow dilute a lot of fixed costs. So we take a holistic view on how can we maximize our top line looking at the installed capacity. It doesn't change the fact that the high-voltage onshore, which is when we talked about that this way is below 220 kilovolt. So the more commoditized part of that is under significant pressure, but you should see the way that we somehow also are trying to offset part of that pressure by allocating the machines to producing for example in this case medium-voltage and that should somehow improve the results. The market for high-voltage onshore, we don't expect any significant improvements there, before we start to see improvements in the upper end of the segment, because that will automatically have a positive spillover impact on the capacity that are used for the lower-end of high-voltage.

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

Okay, that's quite clear, thank you. Then my last question here is on the merger synergies. First of all, can you just specify how big a proportion of the EUR 30 million will be realized by '18?

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

Yes. It's clear, Kristian, that by far most of the synergies are related to our ability to run relatively high capacity, our large utilization and be flexible across the 2 factories and as long as we are not there and not filling the factories, it won't be a very large amount in '18. We still believe in the EUR 30 million, but it will be delayed.

Michael Hedegaard Lyng - *NKT A/S - President, CEO & Member of Executive Management Board*

And then to -- if I can just add the approximately 1/3 that do not relate to capacity, more capacity, more volume, the part that are more fixed cost related, [white color], we have a cost already since closing of the acquisition back last year, started to realize that, but we will also use '18 somehow to accelerate that further in order to become even stronger and we then move into '19.

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

If I can just follow-up on Roland's comment on the delay. I mean, if I guess you're working with one scenario where you can get close to full capacity utilization in 2019 if sufficient orders come in. In that scenario, would you then realize the full merger synergies?

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

Yes, absolutely.

Michael Hedegaard Lyng - *NKT A/S - President, CEO & Member of Executive Management Board*

Yes, I agree.

Operator

We will now take our next question from Akash Gupta from JPMorgan.

Akash Gupta

I have 3 questions, please and I'll take one by one. My first one is on guidance and there is no surprise that the operating EBITDA guidance is materially below consensus and given the lead times that you have in your business, you should have some idea in second half of last year about the shortfall versus market expectations. My first question is that, is there any order that got delayed or maybe lost it to competitors that have resulted in this lower EBITDA, which could be something that you have not expected at the time of your Capital Markets Day or perhaps Q3 results?

Michael Hedegaard Lyng - *NKT A/S - President, CEO & Member of Executive Management Board*

No, I think you are touching on something that have impacted the '18 negatively and we had hoped to be able to get orders in and there were also a number of few orders in the market in the second half of last year that potentially could have solved '18 completely for us. It's not that we did not win any of the orders mentioned, but for a number of reasons, the orders were somehow being either canceled or postponed.

Akash Gupta

My second question is, we have talked a lot about the cable or basically high-voltage part of the business, if I look at the operating EBITDA guidance, what is embedded for the business outside of high-voltage, I'm talking about this medium-voltage and low-voltage part of the business?

Michael Hedegaard Lyng - *NKT A/S - President, CEO & Member of Executive Management Board*

Yes. So back to what Kristian talked about, the applications business, we expect to improve in 2018 whereas the onshore part is still a more subtle outlook on the market, but where we will by ways of more action production planning between medium-voltage factories and then our Cologne factories try to mitigate and allocate part of the fixed costs to part of that business. So the answer is, improvement in that part of the business and on the onshore, not market-wise, but structurally we will, we have a few handles we can pull.

Akash Gupta

And my third and final question is that, you mentioned in the slide that performance of new vessel NKT Victoria was satisfactory, which does not sound for some reason that positive, so maybe if you can elaborate what has been, which is not working, and why the performance is just only satisfactory?

Michael Hedegaard Lyng - *NKT A/S - President, CEO & Member of Executive Management Board*

Well, I think that maybe our humbleness, I don't know. I think the performance of NKT Victoria has been absolutely satisfactory. There has been no fall-outs, the customers have been very, very content with the work we've done for them with that vessel, both installation wise and also in the service jobs that we have done. So if you have read that differently, that's a misunderstanding. There is no doubt that, that vessel is absolutely performing.

Operator

We will now take our next question from Casper Blom from ABG.

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

A lot already said, just 2 things for me. First of all, if you can just give an update on your expected non-recurring cost or integration cost for '18, maybe also '19. And then secondly, Roland, you mentioned a little bit of cost related to broken deal from General Cable. The first time I sort of really heard you confirm that you were looking into that. Could you elaborate a little bit on the strategic rationale for you guys looking at General Cable or were you just how can I say, having a look? Thanks.

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

So for integration costs, we have guided that the integration costs of integrating the acquiree [the detail] is EUR 35 million to EUR 40 million, that still stands and we are guiding [about EUR 15 million] in one-offs for '18. And most of that will be integration costs. So that was first part of the question.

Michael Hedegaard Lyng - *NKT A/S - President, CEO & Member of Executive Management Board*

And the second part, yes, we can clearly confirm that we were a part of that auction process and also pretty advanced and spent a lot of resources on it as well with a strong strategic rationale around being a global cable provider with a full fledged offering to the market, that was a very interesting opportunity. Unfortunately, it did not really move our away because we were not able to and we would also not pay the price that in the end were offered by our Italian competitor because we did not look into the same synergy [percentage], but yes, we could confirm that we were actively looking at it.

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

If I may just follow-up, it seems as a slightly different approach than the ABB acquisition, where it seems that the focus is really to focus on complicated high-voltage solutions, General Cable to my knowledge is somewhat more a widespread, wouldn't it be sort of, it seems as if you were sort of leaving behind the rationale behind ABB or am I getting that wrong?

Michael Hedegaard Lyng - *NKT A/S - President, CEO & Member of Executive Management Board*

I think you are getting that wrong, but I suggest that since we did not end up doing it right, because we were not the winner of this, I suggest that we take it offline that discussion.

Operator

There are no further question at this time. (Operator Instructions) We will now take our next question from David Vos from Barclays.

David Anton Vos - *Barclays Bank PLC, Research Division - Analyst*

Just with respect to your financial debt and the covenants you might have on that, would you be able to help us understand sort of the main covenants on the debt -- so on the debt to EBITDA -- EBIT coverage that kind of stuff? Thank you.

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

Yes, there are covenants on that debt that we also speak a little bit about in general report, but it's up for refinancing, so we are currently refinancing but then part of that debt within the next 2 months or 3 months I think the [net will be more relevant to look at the source after that].

David Anton Vos - *Barclays Bank PLC, Research Division - Analyst*

Okay, but are they public, the covenants there or will they be both financing?

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

No, they are not public, not currently. We have an acquisition that [laying] that we will roll over and then do a new startup and that will be in place within a few months, then it will be clear.

Operator

(Operator Instructions) There are no further questions in the queue, sir.

Michael Hedegaard Lyng - *NKT A/S - President, CEO & Member of Executive Management Board*

Good. Thanks, everybody for listening in and asking good questions. And on the last slide here you can see that we will have our AGM meeting on 22nd of March and then we will be back with the first quarter result '18 on the 15th of May. So thank you and goodbye.

Operator

Ladies and gentlemen, this concludes the NKT Annual Report 2017 Conference Call. Thank you for your participation. You may now disconnect.

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