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Compay **Outotec Oyj**

Conference **Q1 2019 Interim Report**

Speakers **CEO Markku Teräsvasara**
CFO Jari Ålgars
Vice President – Investor Relations Rita Uotila

Operator Hello, and welcome to the Outotec Q1 Interim Report 2019. Throughout the call, all participants will be in a listen-only mode, and afterwards, there will be a question and answer session. Today, I am pleased to present CEO, Markku Teräsvasara, and CFO, Jari Ålgars. Speakers, please begin.

Markku Teräsvasara Thank you. Good afternoon, and welcome to Outotec's Quarter One Results release. It has been a promising quarter with improving market sentiment and strong service growth. Now, let's look at the quarter more in details.

While customers continue to focus on improving existing operations, we also see some large greenfield projects moving ahead. Markets continue strong for mineral processing equipment and hydrometallurgical plants, but now also some greenfield projects are moving ahead, and we are improving workload in Metals, Energy and Water engineering from a number of basic engineering projects.

So, where is the demand coming from? Battery metals continue to be active and we are involved in most of the lithium projects, globally. We also are well-positioned in the fertilising industry with our sulphuric acid plant technology. As you know, most of the sulphuric acid plants we sell go to metallurgical applications, but we also have a good position in the fertiliser industry.

Looking at the segments, Mineral Processing again experienced some solid demand. So, Mineral Processing continues to develop in all areas. In Metals, Energy and Water, as I said, we have improving workload, as we have several projects in basic engineering phase, and they are ongoing. This is not yet visible in sales, but we believe that at least some of these large projects will proceed to construction phase this year. And service order intake also performed well. What has developed particularly well in service-side, was long-term service agreements and modifications and upgrade projects. And these are the areas that we have been focusing on lately, and maybe for the ones that don't remember, we, actually, in the beginning of 2017, we changed the way report order intake in service. So, today, service agreements are reported on a monthly basis, not on a quarterly or yearly or longer basis. So, comparing this column for Quarter 1 this year to the previous ones from 2016 and beyond, you will need to add for Quarter 1 about 10 million more to this.

When it comes to ilmenite smelter project in Metals, Energy and Water, we have the negotiations ongoing in cooperation with the customer. We remain confident that we are provided adequately for the project, and, of course, we'll update that

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the market announces any following, substantial news. Our work with the five strategic focus areas continues, and we have had good progress in all of them. Maybe two examples to mention is that from Product Competitiveness and Project Excellence point of view, we have actually already visible in our Quarter one results. Good impact when it comes to improving project margins, and Jari will tell a bit more about that in his session, but clearly that is the result of this focused activities. Again, mentioning also service side, particularly good progress in long-term service agreements, and modification and upgrade projects are resulting from this Must Win battle programme. But, now, let's look at more in details the main finances, Jari.

Jari Älgars

Thank you, Markku, and good afternoon also on my part. If you look at the numbers, the order intake was good – to be a first quarter of the year. It was on the same good level as last year. It was particularly important to have a good order intake now as second half last year was slow in getting big orders. If you look backwards, we might have to look over five years to find numbers which are on the same level, so it is a very good start, a promising start.

If we go into the sales: yes, it was slower than last year, but as we guided earlier in our sales, we built tilted more towards the end of the year. Despite the low sales, our result clearly improved, supported by solid project execution. If you look first at MP, more in detail, order intake was good – increasing with 19%; 194 million compared to 163 million last year. And, obviously, as we want to continue to grow our MP, have our successful story continue, it is important, as we can see from the sales, due to the second half last year getting our bigger orders have led to that the sales have been flattening out, year-on-year comparison. Now, with this clearly improved order intake we can continue on that growth path. But it is also very positive, is that service sales grew with 11%, which is according our overall target level. With the flat sales, the result was on the same level as last year.

If we, then, go into Metal, Energy and Water, our order intake was 143 million, which is not a bad number, as such, but a clear decline compared to last year's, when we had a very strong order intake in Q1. But if you look at it as an absolute figure, it is clearly above the sales currently, and clearly above the sales we had last year, so it's having also room for growth going forward. What else to say about MEW, is that despite the sales declined considerably, the profitability still improved somewhat, and this was due to that the bigger projects developed solidly, going forward.

If you look at this in graphical form, we can see that margins clearly improved year-on-year and helped a little bit also by fixed cost savings, while again the lower volume decreased the profitability. And this solid project execution helped us improve our result despite the sales was lower. If you look at the cash flow, there were timing issues in payment, and also our work in progress increased. This led to that the free cash flow was negative for the quarter. This was impacted by the net working capital increase of 39 million. Other things to mention in that quarter was that we paid hybrid interest of 11 million during this quarter, and if we look at the financial position, the net working capital, as I said, decreased compared to end of last year, and this is explained by lower milestone payment as well as increased work in progress. And, if you look at the numbers, also, you see they have changed. This is due to implementing IFRS 16. It has impacted the

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key ratios and the leasing liabilities which has now been booked into both sides of the balance sheet as a right on the asset and as a liability; on the liability side, was 67 million. And if you look at the footnotes, you see what the numbers are without this implementation of IFRS 16.

And, then, if you go to market outlook and guidance, Markku, please.

Markku Teräsvasara Thank you, Jari. Before we look at the outlook, let me just summarise Quarter One, one more time. It has been a promising quarter with improving market sentiment for our products and services. We see some greenfield projects moving ahead. Service continues to grow and our Must Win Battles are bringing results as we see our profitability is improving.

So, what are the drivers behind the early signs of market recovery? Main drivers are coming from activities in copper, gold and battery metals. And, as I mentioned, we have a number of basic engineering projects ongoing with the customers in MEW, also MP, but even more so MEW space. Many of them are related to copper, so there is signs that in the copper space investments are being prepared and, of course, we are hopeful that they will turn into construction projects, then, later on during this year.

As one sign of that, we have this 140 million greenfield order from Saudi Arabian mining company. It is a typical, good order for Outotec where our competencies and experience comes well in use because our technologies and equipment cover the whole process from mineral processing to metal refining. We have the process expertise and we can also in this case, we did it, and we can also do it in other case. We actually can test and pilot the whole process in our R&D centre. We have a proven track record in application and, of course Ma'aden, as a customer, is a long-term customer where we have done a number of projects together with them successfully, ranging from mineral processing to alumina calcination technology and three sulphuric acid plants for fertiliser application; actually being the largest in the world. And, what is, of course, good for the workload point of view, is that this order is more or less 50/50 split between Minerals Processing and Metals, Energy and Water.

So, as we see, the market is active and some of the larger projects are moving ahead. So, we are reiterating our guidance for 2019. We believe that we have better and more stable markets. Service continues to increase. MP is improving and smaller order intake is turning faster around. And, of course, last but not least, we have these bigger projects which are – two have actually already been received and there is an opportunity for more.

So, now, let's open the line for questions.

Operator Thank you. Ladies and gentlemen, if you do have a question for the speakers, please press zero followed by the one on your telephone keypad. Once again, to register for a question, it's zero followed by the one on your telephone keypad. One moment for the first question.

Thank you, the first question comes from Omid Vaziri from Jefferies. Please, go ahead. Your line is now open.

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- Omid Vaziri** Yes, good afternoon, gentlemen. Thanks for taking my questions. I have three questions. First one, with the more positive outlook that you are giving here today, how should we interpret that? --Do you expect a sequential improving of orders in the subsequent quarters from the visibility that you have looking ahead at what you're engaged with, the bidding activity and engagement with the customers, and so on? Second question relates to the timing and the schedule of when you might next have an update, or yourself have an update, from the ilmenite smelter project in Saudi Arabia. Just to help us understand timeline and when we might be getting an update from there. And, lastly, how much of the current backlog should we be expecting you to deliver this year, within the current year? Thanks very much.
- Markku Teräsvasara** Yes. If I start from the bidding activity, what was said during the presentation, I think we see a difference compared to the second half of last year. There was more uncertainty, these big projects were not moving ahead. Maybe you remember us in the last results release of the Quarter Four saying that now there is more optimism and we expected to see some of the projects moving ahead. And that is exactly what we see happening at the moment. Ma'aden order was, of course the first one, but there is a number of sizeable large basic engineering projects that we are doing. So far not so much visible in order intake and the sales. However, if they then into construction projects, and of course, that requires customer decision, then they will all be sizeable projects. So, in that sense, there is a fair bit of optimism in the area. When it comes to ilmenite, we continue our dialogue with the customer in cooperation. We have, basically, nothing new to tell at this stage, other than, of course, we are confident that our provision we made 2018 is sufficient. And we continue working closely with the customer. And, of course, whenever we have some new things to report, then, we will come back. And, maybe the backlog question, maybe Jari you can report on that?
- Jari Älgars** Yes. We are expecting that 760 million out of the backlog will turn into sales this year.
- Omid Vaziri** OK. Thanks very much.
- Operator** Thank you. The next question comes from Magnus Kruber from UBS. Please, go ahead. Your line is open.
- Magnus Kruber** Hi, Magnus here from UBS. I think, first, you guided up the nominal value expect to invoice from your backlog sequentially this year from Q4 into Q1. And I think this has only happened once before in the past ten years. Could you give us a little bit more colour on what that is? I think, obviously, you saw some positive build on the service backlog, but I don't think that's enough to explain it. Any colour there will be very helpful.
- Markku Teräsvasara** Yes, out of the backlog, obviously, also some of the orders are-- the order intake we've had is smaller orders, maybe what you also see in the margin during this quarter. So, it's just from smaller orders, shorter orders, orders that are faster to turn around currently.

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- Magnus Kruber** OK, so no difference than what you just told us in Q4, I think, you said the same thing then, more or less. I think, secondly, in regards to the lower invoicing in minerals, energy and water: was that an underlying issue, essentially lower backlog or was there any slippage of project delivery from Q1 into Q2?
- Markku Teräsvasara** Sorry, could you repeat the questions?
- Magnus Kruber** Yes. So, was there any slippage in project deliveries in metals, energy and water in Q1? Something that you expected in Q1 that now falls into Q2?
- Markku Teräsvasara** There were some. Yes.
- Magnus Kruber** OK. Perfect. And, finally, could you give us an update on the remaining high-impact projects? Have you seen any progress in any of them, and do you still expect them to close in 2019?
- Markku Teräsvasara** This is our target. However, we are also dependent on the customer and customer actions. So, this is the target. And, obviously, we are doing our best to do it in this way. Except for ilmenite which we have earlier said that will go into next year.
- Magnus Kruber** For sure. But nothing closed yet, right?
- Markku Teräsvasara** No, nothing closed.
- Magnus Kruber** Brilliant. Got it. Thank you so much.
- Operator** Thank you. The next question comes from Manu Rimpelä from Nordea. Please go ahead your line is now open.
- Manu Rimpelä** Good afternoon. My first question would be on the EBIT bridge that you showed. So, could you help us a bit better understand this project execution which was a big possibility in the quarter that– is this the kind of reversal of no longer having the negative extra cost from those high-impact projects? Or, is it actually the new projects that you're taking on, which are generating higher margins than the old projects?
- Markku Teräsvasara** I would say its roughly half and half if you look at it from that standpoint.
- Manu Rimpelä** And, then, are you able to say that this is mainly in MEW? Or, is it also in minerals processing?
- Markku Teräsvasara** It's mainly in MEW, but also in minerals processing we have improvement.
- Manu Rimpelä** OK. And, then, I was just wondering if you could also help me to understand the logic in MEW where you had significantly lower sales compared to year-over-year, but then the earnings were still only– or earnings improved. Even if you adjust for these loss-making projects, I would just like to understand how does the cost flow through? Is there rationale that you've been taking on these new large projects? Are you able to allocate the cost to them and that's why you are able to with lower sales show good profitability?

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- Markku Teräsvasara** To a smaller extent the latter, but yes, there is that too, that we have a good workload at the moment and that has improved the profitability somewhat. But the main part is coming from no impact from legacy projects, and, secondly, then, also, the projects that led to revenue had good margin on average. Planned margins.
- Jari Älgars** Maybe, add that, also, that I think we have several times earlier discussed about that this resource utilisation impacts our result. And, of course, in MEW, I think we are fortunate to have a higher workload in average than we have seen for quite some time. And, of course, there is less annual option if any, and that improves the result. There also, obviously, has impacted that we did some trimming in last year. So, it's helped both ways. We have more work and we have also less under obstruction in the area where we have had. It is positive both ways.
- Manu Rimpelä** OK. And, I assume, as we go forward and get higher revenues in the coming quarters from the backlog and from projects that were pushed forward, so shall we then see a multiplier on this effect, or the other way to ask this is do you think we're going to be in black figures in Q2? Are you willing to comment that in MEW?
- Jari Älgars** We are not giving guidance on the different segments, but I think it is, obviously, when you look from the numbers, we need more volume. So, more order intake is needed. This Q1 was a good start. I said, yes, it was lower than last year, but still it was a good absolute number going forward that these big projects will move ahead; we'll further build on that. So, it's really continuing on the good volume now and, then, having good workload and good project execution. We are definitely going in the right direction.
- Manu Rimpelä** OK. And, final question: Can you give us a sense about the number of basic engineering projects that you have been working on?
- Markku Teräsvasara** Of course, they are many, but what I meant in that case, I meant projects, sizeable projects that if they go into construction, they would all be bigger than 100 million. I don't give any more guidance, but I say that they are all 100+ size of projects. And we have a number of those that we are doing basic engineering for the moment. But, of course, as I said, we finalise the basic engineering, then the customer decides whether it goes for bidding or not. And, then, of course, at some point, there will be a construction project. We believe that at least some of them will turn into real construction projects later on and, then, of course, having been done the basic engineering, we are quite well positioned.
- Manu Rimpelä** Thank you. No further questions.
- Operator** Thank you. As another reminder, to register for a question, please press zero followed by the one on your telephone keypad. The next question comes from Antti Suttelin from Danske Bank. Please, go ahead. Your line is now open.
- Antti Suttelin** Thanks. You have partly already answered, but just to be crystal clear: when you say that you have big projects in basic engineering, does this mean that they are

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not reflecting orders already received? They are, rather, indicative of future orders, if that is correctly understood.

Markku Teräsvasara That is correctly understood. But, of course, I think what we have done is that if it's a basic engineering project, you'll see that – maybe you know this – we have this Indonesian smelter projects where we announced actually a front-end engineering and design contract. That is only engineering, but it is fairly sizeable, because we announced that as a 10 million project. So, all that 10 million is basic engineering. Maybe to clarify a little bit on this. Obviously, there are projects out there where the customer is using an engineering company to do the free engineering and, then, ask for bids, for instance, from us, on the process or equipment. And, then, there are customers who come to us and ask that we should do this work. And, obviously, this gives us an advantage going forward. First of all, obviously, we get our quotation costs paid for. And, then, secondly, when we will do the process engineering as part of the pre-engineering, we do it in such a way that this is positive for us when it, then, finally moves into the bidding phase. So, then it's more a question of does the project move ahead than are we going to get the order? That's a bigger question.

Antti Suttelin OK. Then on the ilmenite project, can you give any update now that you have been looking into the plant? How does it look like? How confident are you that you can get it operational?

Markku Teräsvasara I think what I said initially, basically, we don't have so much news to tell. Answering your question, yes, we are confident that the provision that we have made is sufficient. And, also, we believe that that plant is going to be commissioned again early next year.

Antti Suttelin That is all. Thank you.

Markku Teräsvasara Thank you.

Operator Thank you. There appear to be no further questions. I'll return the call back to the speakers.

Rita Uotila OK. Thank you, operator. And, thank you for everyone for participating in this Q1 briefing and Q&A. And, just as a reminder, the second quarter results are coming out July 26th. Have a nice day. Thank you.

Operator Thank you. This now concludes today's conference call. Thank you all for attending. You may now disconnect your lines.