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Q3 2018 Valmet Oyj Earnings Call

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PRESENTATION

Calle Loikkanen Valmet Oyj - Director of IR

Ladies and gentlemen, good afternoon, and welcome to Valmet's Q3 2018 results presentation. My name is Calle Loikkanen, and I'm Head of Valmet's Investor Relations. Valmet's President and CEO, Pasi Laine, and Valmet's CFO, Kari Saarinen, will today walk us through the highlights and results of the quarter, and also say a few words about Industrial Internet. And after the presentation, as always, we will end with a Q&A session. But without any further introductions, let's begin. So Pasi, please, the floor is yours.

Pasi Kalevi Laine Valmet Oyj - President & CEO

Thank you, Calle. Welcome to this quarterly conference call, and if I have counted correctly, this is the 20th for Valmet. So nice that you are here today. So our message is that orders received increased in all business lines and our comparable EBITA increased. So positive news.

First, I will go through the quarter in brief, then couple of words about the business line developments, then a couple words, like Calle promised about Industrial Internet, Kari will go through the financial development and I will come back with the guidance and short-term market outlook.

So in Q3, in 2018, our orders received in stable business grew to EUR 381 million. And our orders received in capital business were EUR 570 million, which was good level. Net sales increased to EUR 765 million, and due to the difference in orders received and net sales, our backlog grew to record level and it was about EUR 2.8 billion.

Our comparable EBITA increased to EUR 61 million and margin was 8.0%. And gearing was minus 11%. So reasonably good numbers in many respect.

More in details the numbers. So orders received were EUR 940 million, and it's good quarterly order intake for us. Net sales, like I said, EUR 765 million and comparable EBITA EUR 61 million, and now we were in the targeted EBITA margin level, so EBITA margin was 8.0%.

And we employed about 12,500 people. Then if you look at the orders received by business lines, now there was, of course, a lot of more capital than in previous quarter. So Services and Automation were together a little bit under 40% and the rest about 61% coming from capital businesses.

Pulp and Paper -- Pulp and Energy was strong, but Paper continued still to be strong as well. So we are happy with orders received in all the business lines.

Area wise; Europe was strong, 43%; North America was strong as well, 22%; China continued to be strong; Asia-Pacific had good volumes; and South America, not very much capital businesses yet. So it's more from Services and 6% of our order intake.

So orders received trend is now, for 12 last months, about EUR 3.4 billion, and we are, of course, happy that now last 3 quarters, the



trend has going upwards, again. And like you see from here, this EUR 940 million was the second best after the exceptional quarters in beginning of 2014. So it was good order intake for us.

Area wise, 44% were from in -- then these numbers are for the whole year -- for 3 quarters. So Europe has been 44% and North America 22%. So strong markets, both. China has been 17%, which is again, at the good level. Last year was good and this year will be good as well. And Asia-Pacific has started to grow. So -- and Services in South America is good. So we are actually happy with the performance in all the geographical areas as well.

Stable business has been our focus the whole time we have been in the -- operating as an independent company, called Valmet. And we have good track record here, how we have been able to grow organically and also with 1 acquisition in the stable business. And now our cumulative 12 months orders received are about EUR 1,650,000,000.

So it's good -- good development has continued also in quarter 3.

Then backlog almost EUR 2.8 billion. So EUR 2,791,000,000, and it's the record for Valmet. And I have been earlier saying that this EUR 2.4 billion is good level and even EUR 2.3 billion is good level. And with this EUR 2.8 billion, I am not concerned that we would have too strong backlog or too strong -- long delivery times. So I think this EUR 2.8 billion is still such a level that we can continue to take orders in almost all the business lines. And of course, this gives good visibility, also, for 2019 when we start our planning process. So good development in backlog.

And now because it's the third quarter, we are not telling how big percentage is expected to be recognized as revenue in this year. But we are telling still, of course, that the stable business contributes about 30% and the rest is coming from capital businesses, of our backlog.

Then a couple words about the business line development. Services, orders received increased and net sales remained at the previous year's level. So one positive thing and one negative thing, I would even call it negative. So we have been growing EUR 30 million, so about 3% in the first 3 quarters. Our target is to grow faster than twice the size of the growth of the market. And we are roughly there currently, according to our estimates. So 3% growth, and we are of course, happy with that.

And then net sales was EUR 282 million, and comparing to the last year, we have EUR 16 million more in net sales. And that's maybe a little bit disappointment for us, and you can be sure that we work very hard in getting net sales to increase in coming quarters. So that's, of course, very much the focus in Services business line and areas.

Then Automation has been growing about EUR 9 million and about 4% in percentages in order intake. And that's also a little bit lower than it traditionally has been, but we are still happy with the growth rate in any case.

Net sales has been growing EUR 13 million, so in Automation, the growth has taken place in both orders received and net sales.

Then Pulp and Energy. Orders received and net sales increased. So orders received was EUR 272 million and now cumulatively, EUR 520 million. So now, we are, of course, very happy that we have got a strong order intake in Pulp and Energy.

And like we said in Capital Markets Day, we then said that there is a possibility that we will get about EUR 100 million orders in marine scrubber business. And those orders have materialized, so that in Q3, we booked about EUR 100 million marine scrubber orders in Pulp and Energy. And that's, of course, impacting the number, but EUR 272 million is good order intake for Pulp and Energy.

Net sales has been growing, so EUR 631 million against last year's EUR 581 million.

Then Paper has continued to perform strong. Cumulative orders are EUR 921 million, so about EUR 90 million more -- almost EUR 90 million more than a year ago. Quarterly order intake was EUR 299 million, and it's a strong quarter for our Paper business. So we are very happy with the -- with the development. Net sales was cumulatively EUR 657 million and in the quarter EUR 196 million. So, of course, it will still take some time before the net sales starts to recognize at the same level as order intake. So good development in Paper

business line.

Then, like, also in Capital Markets Day, we were talking about industry -- Industrial Internet, and that has been a focused area for us since we acquired Automation. And it's now clearly benefit -- giving us benefit and also benefits to our customers. So how we've been building it up is that we have Industrial Internet applications. So different kind of applications, how we help customers in visualization, reporting or guidance to their personnel.

And then Services, like we have been building 5 global and 2 local Valmet performance centers, wherefrom we can remotely help our customers wherever they are in the world. And that concept has been now built and basis has been built. On top of that, we now launched Customer Portal, so we want to develop different kind of digital communication tools between ourselves and our key customers. And we have now first installations ongoing and first pilots in use already. And with that tool, we want to emphasize different kind of tools and ways how to communicate effectively between Valmet and Valmet's customers.

And then we have been building this ecosystem, try to work with companies who are strong also in pulp and -- pulp and paper and energy. And up to now, we have made contracts or agreements with Tieto, Kemira and Energy Opticon. And with those companies, we continue to develop common offering towards our customers. So a lot of work has been ongoing on this arena.

And then, what is the status today. We have 5 industry-specific Valmet Performance Centers in operation, 1 for Paper and Board, 1 for Energy, 1 for Pulp, 1 for Tissue and 1 for Automation. Then we have 2 regional centers, we started up China and North America. So we want to have industry-specific and then we want to have centers, which are close by the customers so that they can talk the local language and be in local time zone.

We have about 540 connections -- online connections with customers. So we can connect to their system, and see how the system is working or how the process is working. We have about 90 agreements with remote connections. So we are using those as agreement business and then helping customers in different kind of situations, like just an example from Paper and Board Performance Center, we have been solving 170 tickets this year, where remotely we have been able to help customers all around the world. So this concept starts to work and it's proving every day that there is future potential to improve -- to develop it even further. But it will take long time, and we have patience to develop it long term.

Good. That's the short summary of businesses, and now it's Kari's turn to talk about financial numbers.

Kari Juhani Saarinen Valmet Oyj - CFO

Okay, thank you, Pasi. And good afternoon from my behalf as well. So some words on Valmet's financial development on quarter 3.

So orders received were EUR 940 million, so a 27% increase compared the year ago. So this is -- as Pasi was saying, this is good and all business lines increased. Pulp and Energy, over double than a year ago. So we booked around EUR 100 million worth of orders from marine scrubbers this quarter. Geographically, our biggest increase from Asia-Pacific and North America, which actually both doubled their orders this quarter. Order backlog record high, EUR 2.8 billion. Also, the quality of the order backlog is quite good. So the increase in the order backlog pretty much all coming from our stable business.

Quarter's net sales, EUR 765 million, that's 7% increase. Services was flat. All other business lines increased there. Biggest increase in Asia-Pacific, over 40% increase.

Important to notice here -- is that share of stable business was low 45% in quarter 3 of net sales, last year that -- or a year ago that figure was 48%.

Quarter's comparable EBITA, EUR 61 million, which equals to 8.0%. So this is the second time now, during Valmet, that we have been able to reach our target range between 8% and 10%.

Cash flow for the quarter, EUR 119 million, around EUR 40 million higher than a year ago, and then cumulatively. Cumulatively orders

EUR 2.7 billion, 6% higher than a year ago. Paper business line strongest, 11% increase. Automation and Pulp and Energy, 4% increase, and Services 3%.

Cumulative net sales, EUR 2.3 billion, there we have 12% increase. This increase pretty much all coming out of capital business, where Paper business line increased close to 40% and Pulp and Energy, 9% increase. Stable business increase was 2% there.

Cumulative comparable EBITA EUR 144 million, which equals to 6.2%. A year ago we did EUR 138 million, which turns to 6.6%, and here we need to remember that quarter 1 this year, we booked EUR 15 million worth of losses of 1 project.

Cumulative cash flow, EUR 141 million, that's below last year's, and gearing was minus 11%.

Our gross profit. So the gross profit percentage was the same as a year ago. Absolute gross profit increased from last year. The share of stable business of net sales was 45%, last year -- for the quarter, last year, 48%. So that means that quarter's sales mix was not the most favorable for the profitability point of view.

Also, cumulatively, stable business was also 45%. Last year it was 49%.

SG&As, they remained flattish compared to a year ago. The share of SG&As came down from 16% of last year to 15% this quarter.

Business volumes are quite high and actually, we have a lot of improvement projects now ongoing that increase now Valmet's SG&As momentarily, and -- but then on the other hand, they improve Valmet's profitability in the longer run and -- such as ERP, new HR systems, Industrial Internet, Field Services, we are ramping that up, also other IT platforms, to name a few.

And then looking at our EBITA. So our EBITA target as said between 8% to 10%. Quarter's EBITA 8%. And this is now the second time that we have reached this target range. And then also looking at the seasonality within one year, so quarter 4 with us has traditionally been the highest quarter except year 2016.

Cash flow. So after 2 low quarters, our cash flow was now EUR 119 million, this is the highest in 2 years and also second highest ever. Full year, is below last year's though. Our net working capital reduction, EUR 65 million, that was the biggest contributor for the good cash flow and that driven by the higher customer advances.

Capexes for the quarter were a bit higher than unusually, EUR 21 million.

Net working capital, minus 12% of the rolling 12 months orders, so quite good level. So that turns to minus EUR 427 million. So this is actually the lowest if we look at the timeline here. So we have worked quite a lot to keep the inventories and accounts receivables low even though the volumes are high, and also, we have received quite good amount of customer advances and those are higher than previous quarters as well.

Net debt and gearing. Net debt, minus EUR 98 million. Last year, this was minus EUR 30 million. Gearing was minus 11%. Last year, or year ago, we were minus 3%. So this is good development from -- also from previous quarter's 0 levels. Equity-to-asset ratio, 43%, so slight increase from before year as well.

And then looking at capital employed and also then return on capital employed. So the comparable ROC, that was 18%, so this is the highest here. And here we are also within our target range, between 15% and 20%. So profit has increased and also capital employed now remains at the lower level because of repayment of some loans. So, thank you, and back to you, Pasi.

Pasi Kalevi Laine *Valmet Oyj - President & CEO*

Thank you, Kari. Then guidance and short-term market outlook. So we keep our guidance like earlier, Valmet estimates that net sales in 2018 will increase in comparison with 2017, and comparable EBITA in 2018 will increase in comparison with 2017. So that's the same as earlier.

Then short-term market outlook. So in Services, we keep good outlook. In Automation, we keep good outlook. In Pulp, we increase that to satisfactory. And the reason is that, like you know, we have announced MAPA project and then -- that will bring some workload to our organization, and that will help with the workload and that has been the reason why we are now increasing the Pulp outlook to satisfactory.

Then, it will be -- maybe discussed many time in the question-and-answer session, so I will answer once again now. So we see that there are plenty of other or not -- there are some other big projects as well in development, but we see that it will take some time before they will be maturing enough, so that the customers are making the final decision and final selection of the technology suppliers.

In Energy, we keep the level -- market outlook level at satisfactory. Like you have seen, our marine scrubber business has picked up, but at the same time, boiler business is not going as strong as it could be. And that's the reason why we still say satisfactory for the Energy.

Board and Paper. You saw the market has been good. So all the organizations are very well loaded, and we still see that there is market activity as well. So we keep good for Board and Paper.

And Tissue, we keep good and all the time, we remind that 2017 was extremely high and 2016 was high, and for us also, current level where we are operating is a good level. So that's why we keep the market outlook as a good. So those were the market outlooks and guidance.

And then summary. Orders received increased in stable business, orders received increased in capital business. Net sales increased. Backlog is at high, EUR 2.8 billion level. Comparable EBITA increased to EUR 61 million, and margin was 8.0%, and gearing was 11 (sic) [minus 11]. So it was reasonably good quarter for Valmet.

Calle Loikkanen Valmet Oyj - Director of IR

All right, thank you very much, Pasi, and thank you, Kari, for the presentation. Now let's continue with questions. So if you gentlemen please, move behind the Q&A table. And as always, let's first start with any questions here in Keilasatama and then continue with questions over the phone lines.

So do we have any questions here in Keilasatama at this time? It seems that we don't have any questions here right now. So let's continue with questions on the phone lines. So operator, please do we have any questions?

Operator

(Operator Instructions) Your first question comes from the line of Johan Eliason.

Johan Eliason Kepler Cheuvreux, Research Division - Analyst

This is Johan Eliason at Kepler Cheuvreux. Starting maybe on this marine scrubber theme. It seems like you're stealing the orders away from Wärtsilä today. Now, you talked about EUR 100 million order opportunity at the Capital Markets Day, and I sort of understood that to be the opportunity over the coming year or so, not this quarter. How big could this opportunity be for you, let's say, over the coming 2 to 3 years? Are you sold out now? Have you taken what you can? Or how does it look like?

Pasi Kalevi Laine Valmet Oyj - President & CEO

I think, we still have some possibilities to take orders in. And then, of course, we can't now estimate how much it will be, but there's still -- I would guess that there are orders coming in. And then, of course, at the same time, we have to very carefully evaluate what is our delivery capability. Not to oversold and have later on problems with the deliveries if we don't have enough capacity in engineering to deliver the start-up. So we are currently analyzing very carefully that what's our capability on yearly basis. And -- but we might still take some more orders.

Johan Eliason Kepler Cheuvreux, Research Division - Analyst

And is this business helping towards -- the set margin target? Or is it sort of diluting it? Or how do you see it?



Pasi Kalevi Laine Valmet Oyj - President & CEO

No, we are not, of course, giving the profitability of different businesses, but all the businesses have to be businesses and our Environmental system fulfills that criteria.

Johan Eliason Kepler Cheuvreux, Research Division - Analyst

And talking about the margin on another view. You obviously have very strong order intake on the equipment side. Now we saw this on scrubbers and then Paper and Board has continued to be good, then you seem to be expecting this to be good going forward as well. And then we have this MAPA order, as well, coming. It seems like you're moving rather further away from your 8% margin target than getting closer to it? Admittedly this quarter you still managed to improve the margin despite the fact that the share of -- the high-margin business was lower in the quarter than a year ago. But can you sort of shed some light on how do you see this playing out, because it looks pretty strong on the equipment side and the Services is not moving, in my view, the same pace, it looks like?

Kari Juhani Saarinen Valmet Oyj - CFO

Well, there was a -- lot of like dimensions here. But of course, we are very happy with this 8% margin. So as I said, this was the second time that we made this our target range, 8% to 10%. And yes, the capital business, we have a good market there also, then Pulp is picking up, we increased that to satisfactory. And then, I -- we were also saying that the quality of the order backlog is now in a kind of quite good level now. And meaning that the backlog has increased in stable business, and we have been saying that 8% to 10% is our target range. And this is what we have been working quite hard now for a long time already to make this.

Pasi Kalevi Laine Valmet Oyj - President & CEO

And we have been also ...

Johan Eliason Kepler Cheuvreux, Research Division - Analyst

Do you think, you can achieve this in this order development currently?

Pasi Kalevi Laine Valmet Oyj - President & CEO

We have been saying earlier on already that it can't be so that we have -- we reach that 8% to 10% only in cases where capital business is low compared to the stable business. So of course, our target is to reach 8% even if the capital business volume is high.

Operator

So your next question comes from the line of Manu Rimpelä.

Manu M. Rimpelä Nordea Markets, Research Division - Head of Equity Research of Finland & Senior Analyst

My first question would be on the margins, and how should we think about going into the fourth quarter. I think you will have probably quite similar mix between the Service and Automation -- Services and Automation and then the equipment business in the second half of the year as you had in second half of the year last year. And you were able to improve your margins in this third quarter, even though the kind of share of equipment is quite high. So do you think that there is the normal seasonality between the margins in the fourth quarter compared to the third quarter? And I mean, I remember that in 2016, there was a very big jump between the Q3 and Q4 margins. So just kind of help us understand what is the normal seasonality in the normal mix scenario in Q4?

Kari Juhani Saarinen Valmet Oyj - CFO

Well, normal seasonality goes so that if we look at capital business, so there's no clear seasonality. Projects are percentage of completion and there is no clear seasonality at capital business. And then if we look at the stable business, so there we typically have high orders in the first half of the year and a bit lower then in the second half, and then the net sales goes vice versa. So that net sales for stable business typically is a bit higher in the second half of the year. And partially, this is now also visible in our order backlog.

Manu M. Rimpelä Nordea Markets, Research Division - Head of Equity Research of Finland & Senior Analyst

And if you think about between the quarters, so is 2017 a good base to compare the Q3 and Q4 margin evolution due to this seasonality? Or should we more look at 2016?

Kari Juhani Saarinen Valmet Oyj - CFO

Well, Manu, that's quite difficult to say. It's so long time ago that nobody remembers that anymore.

Pasi Kalevi Laine Valmet Oyj - President & CEO

It's -- I don't remember 2016 numbers by heart, and I think, Kari has the same. So sorry, Manu, but it's...

Kari Juhani Saarinen Valmet Oyj - CFO

It was so that 2016 was actually, we had -- quarter 3 was a bit higher than '16 and -- or quarter 4, and '17 was the normal. The normal seasonality is so that quarter 4 is the highest EBITA. So that's how it usually goes.

Manu M. Rimpelä Nordea Markets, Research Division - Head of Equity Research of Finland & Senior Analyst

Okay, and then in terms of the Paper business, you have had very strong order intake there, and you talked about improving backlog and improving pricing. And -- are we starting to see that the improving pricing coming through already in the sales in the third quarter? And will that kind of start to filter through even more in the fourth quarter and in early '19?

Pasi Kalevi Laine Valmet Oyj - President & CEO

So we've been earlier saying that it's -- we have been recognizing low level -- low profitability level projects, which we took in 2016, beginning of '17. And that was still the case in Q3. So there was quite a lot of recognition from those older projects, then you can interpret yourself what comes in the future.

Manu M. Rimpelä Nordea Markets, Research Division - Head of Equity Research of Finland & Senior Analyst

Okay. Is there a lot of these old projects left in the backlog?

Pasi Kalevi Laine Valmet Oyj - President & CEO

Not very much.

Manu M. Rimpelä Nordea Markets, Research Division - Head of Equity Research of Finland & Senior Analyst

Okay, and then final question on the Services growth. So it seems to be fluctuating between the quarters quite a lot, at least this year. So should we kind of think about the organic growth rate more on a year-to-date basis running at around 6% and that's kind of how we think that is the target rate, but then it just fluctuates between the quarters?

Pasi Kalevi Laine Valmet Oyj - President & CEO

I am following the 12 months and 6 months trend. So quarters have variations. So I myself am following more the trends.

Operator

(Operator Instructions) And the third question comes from the line of Mikko Ervasti.

Mikko Ervasti SEB

Thank you. So going back to this profitability question, I think it was already asked earlier as well, but a bit more detailed. Given the quite high share of the capital business, I still consider the margin, especially gross margin, is quite high in the historical context. So would you say that the pricing environment has now improved, and there are not that many of these weaker margin projects there involved anymore? And how does it look going forward? Is there a better pricing environment for you?

Pasi Kalevi Laine Valmet Oyj - President & CEO

Pricing environment is, of course, like I have been saying earlier that the higher backlog we have in a specific business, the better pricing discipline we and our friends from Austria and Germany have. So -- and then for those deals to be recognized in revenue, it can take some years. So what kind of pricing environment we have now, we will see it maybe in a year in our revenue recognition with current system. So of course, the things what we saw in quarter 3, they were results of decisions made in '17 -- beginning of '17, middle of '17. Currently, our backlog is -- in Paper is side good. So then, of course, we could think that we have good pricing discipline. We had quite empty hands in Pulp, so then, of course, we can assume that one has to get orders, and we hopefully, now can continue with MAPA and it

creates work. So it varies business to business all the time. And difficult to say exactly that what kind of impact this quarter's -- or of course, we can say, what kind of impact this quarter will have in the future. But -- pricing situation currently is better than it was a year ago.

Mikko Ervasti *SEB*

Okay. Would you like to guide that the MAPA order was perhaps still quite a low margin?

Pasi Kalevi Laine *Valmet Oyj - President & CEO*

No, but we were going to the negotiations with empty backlog. So then, I don't know -- or I know, what was the result, but I'm not telling to you.

Kari Juhani Saarinen *Valmet Oyj - CFO*

And also, MAPA order was not booked in quarter 3. So that's the other point to remember, yes.

Operator

We got another question from the line of Antti Kansanen.

Antti Kansanen *DNB Markets, Research Division - Analyst*

Yes, it's Antti from DNB. The first question would be on scrubbers. Now that you got this EUR 100 million orders already in Q3, was that-- that a surprise for you compared to the potential that you said on the CMD, so did it materialize just faster? Or do you see a higher opportunity for you guys? And then on the deliveries, are you now sold out for '19 when you think about your internal delivery capabilities? Or how should we expect your appetite for the scrubber orders for the coming quarters as well?

Pasi Kalevi Laine *Valmet Oyj - President & CEO*

Well, we were quite confident with this order during the Capital Markets Day. So that's why we were able to tell that there might come that size of orders. So we were quite confident. And it came like we expected. So it was not a surprise. Our scrubber business is now growing fast, and it's doing the same for the other vendors as well. And now the critical thing is to have good team to start up the scrubbers on ships where they will be installed. So now we have to analyze very carefully, how much more orders we can take and with what kind of delivery time. So can't tell you exactly, what will the volume be in coming years, but it will be good size of the business, but we have to be careful.

Antti Kansanen *DNB Markets, Research Division - Analyst*

So is it reasonable to assume that you will deliver this EUR 100 million, almost all of it, on '19? And now if we see some additional orders on, for example, Q4, that would go more into '20 deliveries? Or how should we look at this?

Pasi Kalevi Laine *Valmet Oyj - President & CEO*

No, of course, business-by-business, we are not telling that, but in next quarterly result, we will, of course, tell, how much is the backlog for 2019 we expect to be recognized as revenue. And -- but then, from the other point of view, one can say that of course the delivery time for scrubber is a lot of shorter than for pulp mill.

Antti Kansanen *DNB Markets, Research Division - Analyst*

And the second question would be on the SG&A costs. What kind of annual normal inflation would we assume for those? And what kind of additional SG&A cost ramp-up should we expect going into next 12 months or 2019?

Kari Juhani Saarinen *Valmet Oyj - CFO*

Well, if we look at like historically, so SG&As have been quite flat and not increased. And now there is some inflation but quite difficult to make any -- We are just in the middle of the planning process now and quite difficult to throw any numbers now in the future on this. But historically, we've been quite prudent with SG&As. But at the moment, as I was saying earlier, we have now activity also that we are building a future now on some activities that take some time.

Antti Kansanen DNB Markets, Research Division - Analyst

But you are not willing to give any numbers on what kind of impact would these activities have? I assume that they are not visible as of now on your cost line?

Kari Juhani Saarinen Valmet Oyj - CFO

Well, as said that we are just in the middle of planning process now. And also difficult to say anything on the future.

Pasi Kalevi Laine Valmet Oyj - President & CEO

No, but ERP is and Industrial Internet is, so...

Kari Juhani Saarinen Valmet Oyj - CFO

They are there.

Pasi Kalevi Laine Valmet Oyj - President & CEO

Yes. So, of course, there will be some more cost coming from some new development of things but...

Operator

(Operator Instructions) Another question comes from the line of Tom Skogman.

Tom Skogman Carnegie Investment Bank AB, Research Division - Head of Research of Finland

Yes, this is Tom from Carnegie. I am a bit curious about how the situation will change in South America with this order. You have had very weak orders for quite some time in South America. And if you exclude the Service business, I do not -- believe you have had a lot of project sales there and now you will start to have some, but -- and basically, how many people do you have in your project organization that have had nothing to do almost the last year? And will they have something to do already next year, or will that move into 2020?

Pasi Kalevi Laine Valmet Oyj - President & CEO

Our capacity utilization in South America has been quite good. So we have been delivering a couple bigger projects, which are not of that size that they are of interest to investors, but -- so that there have been tens of millions of projects and we have been using engineers for those ones. And then we have had quite good order intake for mill type of improvement projects in 2017. So that has given utilization. Now, of course, we can use part of the engineers for this new project. So we haven't had utilization problem in South America.

Kari Juhani Saarinen Valmet Oyj - CFO

And also we have had 7% growth now -- year-to-date, 7% growth in the orders and also, South America. So the currencies have devaluated quite big time against euro.

Operator

A follow-up question comes from the line of Manu Rimpelä.

Manu M. Rimpelä Nordea Markets, Research Division - Head of Equity Research of Finland & Senior Analyst

I would have a follow-up question on the 8% to 10% margin target. So you mentioned in your comments that it's -- there is still a lot of work to do in order to kind of reach the 8% to 10% range on a more sustainable basis. So can you just give us the kind of the biggest moving parts when you kind of think for the next 12 months? What is going to be driving you towards that range?

Pasi Kalevi Laine Valmet Oyj - President & CEO

It will be the same list than earlier. So try to sell with as high price as possible, and that's what we have been doing now in the units, where we have a good workload. Then develop the cost competitiveness so -- of the product offering. So we are following our design-to-cost actions all the time, meaning that what -- how much with R&D we can reduce the cost of our offering. Then improving project management. Of course, if you have hits like we had beginning of this year, then of course, it will impact your profitability. And then improving the quality further. So same topics, and we believe that with those same topics, we can continue to improve our profitability even from today's level.

Operator

Sir, we got another follow-up question comes from the line of Johan Eliason.

Johan Eliason *Kepler Cheuvreux, Research Division - Analyst*

Yes, I just have a short one. On the scrubber order, the EUR 100 million. Was that a single order, or were there a couple of them that you got in the third quarter?

Pasi Kalevi Laine *Valmet Oyj - President & CEO*

It was orders.

Operator

Another question comes from the line of Antti Suttelin.

Antti Suttelin *Danske Bank Markets Equity Research - Head of Research of Finland*

Still on the margin. I understand that you have headwinds and then you have tailwinds potentially. And as far as I understand, one of the potential tailwind is that if you got your project to run smoothly, you could still quite notably improve the margin. Could you just update where you are there? You didn't touch this topic much in the CMD, but just as I look you with ANDRITZ, I can see that there was more than 2 percentage points difference in favor of ANDRITZ, Pulp and Paper last year. So why is this, and is there still things you can do?

Pasi Kalevi Laine *Valmet Oyj - President & CEO*

I don't know about ANDRITZ results and how they calculate it. Corporate numbers are roughly as ours. So, I think, in Capital Markets Day, we were opening this project execution a little bit, and we were saying that in Paper business line, margin deviation is positive. And then, we were saying that in Pulp and Energy, we have, I don't remember exactly the word, but some challenging projects where we have negative variation. But generally, the project execution, actually in Pulp and Energy is good. And then, we have had these issues in couple of the projects. So of course, our profitability will improve if we are getting project execution to the level that not that kind of negative -- big negative surprises will happen. And all in all, I think the best measurement what we have is the variation over the whole product -- project portfolio. And in Paper, it's positive, and in Energy, we still have work to be done.

Antti Suttelin *Danske Bank Markets Equity Research - Head of Research of Finland*

Yes. If I remember right, last year, you have said that you incurred 2.7% of sales as quality costs. I know that you had this unsuccessful project in Q1 this year, but if you -- exclude that, where is the level now? Have you been able to bring the level down?

Pasi Kalevi Laine *Valmet Oyj - President & CEO*

Quality costs have been reduced. So I don't remember by heart now the number. But maybe, in -- after quarter 4, we will tell it. And of course, when analyzing it, we have to take or we are taking internally away big hits like we had beginning of this year and then analyze also the quality cost without it. And we have had progress in quality costs. So it's getting down all the time.

Antti Suttelin *Danske Bank Markets Equity Research - Head of Research of Finland*

Yes. Please report that number, it would be...

Pasi Kalevi Laine *Valmet Oyj - President & CEO*

Let's see. Let's see. Let's see.

Operator

Sir, we got another follow-up question comes from Tom Skogman.

Tom Skogman *Carnegie Investment Bank AB, Research Division - Head of Research of Finland*

Yes, this is Tom on -- from Carnegie. On the scrubbers. I was just wondering a bit that what are your target markets here? Is it Nordic shipping companies or certain ship segment? Then I also want a verification in a way that you are not operating as a subsupplier to Wärtsilä or Alfa Laval or someone else, that you are actually dealing with the end customers yourself here?

Pasi Kalevi Laine Valmet Oyj - President & CEO

We are dealing with end customers ourselves. And we are selling globally.

Tom Skogman Carnegie Investment Bank AB, Research Division - Head of Research of Finland

And what are your preferred ship end-markets?

Pasi Kalevi Laine Valmet Oyj - President & CEO

No, we -- our customers haven't yet given permission to make announcements that who has been buying from us. So, sorry, Tom.

Tom Skogman Carnegie Investment Bank AB, Research Division - Head of Research of Finland

(inaudible)

Pasi Kalevi Laine Valmet Oyj - President & CEO

No, people can guess, if I tell. So sorry, but I can't make the announcement yet.

Tom Skogman Carnegie Investment Bank AB, Research Division - Head of Research of Finland

And then about this market, it's red hot at the moment. And a lot of companies in the industry are now kind of looking for more capacity, and you have a very good global supply chain. Could you even change your model here if there is a really overheated situation next year and operate as a subsupplier to someone as well?

Pasi Kalevi Laine Valmet Oyj - President & CEO

We are not planning to be a subsupplier, but we are building the business with our own resources that -- and we have been building the supply chain. And like I said couple of times already, the critical issue is to have the start-up crews who are going with the scrubber onboard when the ship is leaving.

Tom Skogman Carnegie Investment Bank AB, Research Division - Head of Research of Finland

Do you see any service opportunity?

Pasi Kalevi Laine Valmet Oyj - President & CEO

We see some service opportunities in coming years, but it's not maybe changing the Services number.

Operator

Sir, there are no more questions at this time. You may continue.

Calle Loikkanen Valmet Oyj - Director of IR

All right. Thank you very much then for the questions. Thank you for the answers. And that then concludes the event for today. Thank you for participating, and I hope to see you all at the Q4 results presentation in early February. Thank you, and goodbye.

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