Alfa Laval

Moderator: Tom Erixon
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OPERATOR: This is Conference # 3360788.

Operator: Ladies and gentlemen, good morning. Thank you for standing by, and our apologies for the technical issues. Welcome to the acquisition of StormGeo Conference Call.

At this time all the participants are in a listen-only mode and after the speakers' presentation, there will be a question-and-answer session. To ask your question during the session, you will need to press star one on your telephone.

I would now like to hand the conference over to your speaker today, Mr. Tom Erixon, CEO; and Jan Allde, CFO. Please go ahead.

Tom Erixon: Thank you, and good morning, everybody. We decided it was a good idea to give you some background and rationale for the announcement today on the acquisition of StormGeo. So this will be an update on the background and strategic intent with this acquisition. We will provide some transactional details as well. And then maybe most of it will a shorter Q&A session.

Rather than me and Jan giving you a lot of color as to StormGeo. And by the way, you will find a lot of publicly information on them, so I'm sure you're doing your own research. But we thought we'll just share with you a brief video. I hope it's going to work. We take technical risks here. If it breaks down, we will cover up for it. But it's a 90-second intro on StormGeo. And

after that, I will get to the Alfa Laval story on this one. So I hope it works. Let's go.

(Presentation)

Tom Erixon: OK. So with that as a background, let me just give you some words on why we find this to be an excellent fit and an attractive and important step for us. And let me start with the Marine Division and what we are trying to do there.

Since you well know that since many years, a lot of our development work has been focused on environmental application in the marine industry. The change is relatively dramatic in the marine sector when it comes not only to general environmental issues, but certainly as well on the question on decarbonization. And there are targets to reduce the CO2 emissions in the marine industry, with 50 percent in the years to come.

Our view on this has been for a long time that there is no single recipe for addressing this. There will be – has to be a toolbox available for shipowners to draw from. And our intent, since years back, has been to be an important supplier of solutions going in that direction.

As you well know, on the environmental side, we've launched a number of important products over the last five years, including the PureSOx and the PureBallast solution. You recently saw the launch of PureCool, a way to reduce methane slip problems on LNG-fueled vessels and a host of other environmental applications. We work with multi-fuel solutions. And as you know, we are pioneering and participating in the possibility of using fuel cells and hydrogen as fuel, at least for the auxiliary engines and systems.

So the question on fuel efficiency on board is in no way new to us. And StormGeo fits in this context very well with our ambitions in the marine industry by being active in routing services, (inaudible) as there are – this is an important tool to help shipowners reduce fuel consumption on board on any given route.

The second aspect, which is maybe almost equally important is that we've talked about digitalization for many years. You are constantly looking at this

question. We are slowly and surely progressing when it comes to digital capabilities in a mechanical engineering company. But the step towards full-blown digital services and our ability to build competencies, skills, capabilities on an adequate level and in the platform that is strong enough, we found that to be a challenge within our organization and our culture and our background. Consequently, this is a way for us to create the capabilities that we need to roll out digital services on a broader scale within Alfa Laval.

We've talked with you many years about the increase of service agreements. We talked to you recently about how we manage the corona crisis with the moving to remote guidance and remote digital services. We've talked to you about the amount of machine hours that we are now recording with sensor technology and our existing equipment within Alfa Laval. But our ability to productify this fully and take full advantage of it and have all the skills in that area are, we judge, not fast enough. And so from that point of view, we expect that the capabilities and human resources we bring into the company through the platform of StormGeo will help us to accelerate the digital transformation of the rest of Alfa Laval.

Finally, point three is, well, what are the options here in order to do this. One option is obviously has been to recruit organically and grow. We think it's difficult. Most companies find that a lot of those people come join, leave and we're back to square zero. The other option is to buy a smaller start-up company. And you may know and remember that we announced a small minority investment of a few million dollars in Internet of Things companies in the flow sector called AMI. You can find the press release if you go back some six months.

That team of people, we felt very concerned to integrate fully a small platform company that needs to build its capabilities, revenues and profitability over time. And we find a risk in putting a lot of money into the start-up sector in these type of companies as relatively high.

So that turns sort of the table towards the StormGeo type of platform, which is a company that's been around for many years with an established customer base, established revenue and a stable recurring revenue and with a clear

profitable growth history and trajectory going forward, that gives us the stability that we feel is the adequate way and adequate base for us to build on. So those three reasons were the main driver behind this transaction.

Let's move to the next. Now from the video and from what you might have read, you have some idea in terms of what is the value proposition of StormGeo, why do we find that the company as such has a relevance in our portfolio. And I think there are three very important value propositions of the company that fits well with what we are trying to do versus our end user. One is the performance and efficiency of the assets, mainly today, of course, in fleet optimization, but in the future possibly expanding into other areas where we operate as Alfa Laval.

There's clear safety implications on their product offering that they have in terms of how you safeguard assets onshore and offshore in terms of assets, (operators), transports and other things. And finally, there is also, when it comes to the navigational side, compliance issues that are getting more and more complex. As you know, we've talked about this to you many times when it came to high sulfur, low sulfur regulations or PureBallast regulation in terms of the risks of not having appropriate records and operating the equipment in the right way, risking penalization from harbor authorities and others around the world.

So this is an increasingly complex area to navigate in a ship owner and operator, and we think the compliance side will be strengthened also based on the value proposition of StormGeo. So those three fit well with what we try to do with our customers as well as they try to do with theirs. Next slide.

Not repeating too much of the video and not extending too far into StormGeo's operations at this time, but as you can see from the core data, they are way ahead over we are when it comes to connected assets. We are in the 1,000 maybe at best, and they are (75), a fair reasonable share on the fleet has software installed globally. We talk normally about 60,000 vessels around the world and you find 6,000 here. So it is a reasonable penetration. The number of voyages is relatively high at 65,000 voyages per year.

Three thousand subscription, meaning 3,000 customers. A fairly broad customer base onshore, of course, but to a degree also land-based assets that are connected. So it gives us, I think, a lot of comfort (inaudible) an established business viable for the long term, proven in the short term. And we look very much forward to the closing on this deal in a couple of weeks' time and then to develop jointly together with the StormGeo team as part of Alfa Laval.

And with that, we'll go into some transactional details with Jan, please?

Jan Allde: Thank you, Tom. So as you've seen from the announcement, the purchase price here is NOK 3.6 billion on a cash and debt-free basis. It is financed through – fully through our own funds. And closing expected here during. And there is really no antitrust clearance deemed required for the close.

Then if you look at the financials, as you've seen, the sales of StormGeo in 2020 was NOK 714 million, and they have an EBITDA margin of 22.5 percent. The deal itself will be neutral Alfa Laval's EBITDA margin and also EPS. And if we look at kind of pro forma, one, we say that net debt-to-EBITDA ratio will stay below 1, to be precise at 0.93; and a debt ratio of 0.22.

So if you go to the next slide then. So why do we think this acquisition is attractive, and particularly the StormGeo, because it has an attractive financial profile as we see it. It's, as Tom was saying, an established and profitable software company. And it really will accelerate the digitalization journey that Marine and also Alfa Laval as a group is on. It has a large addressable market with a higher growth rate expected for a number of years to come.

And thirdly, it's a scalable software technology platform that we have to continue to build on. And it also has a large number O-F blue-chip companies and a fairly large share of subscription-type revenues. So pretty sticky business model, hence, predictable recurring revenue stream. And finally, it will increase Alfa Laval and the Marine Division service scope. So it probably adds about 3 percent service on the Marine and about 1 percent for Alfa Laval Asset Company.

So by that, I think we hand over to a Q&A session.

Operator: Thank you. We will now start the Q&A session. And to ask your question, you will need to press star one on your telephone. And to withdraw your question, please press the hash key.

We will now take our first question from the line of Robert Davies from Morgan Stanley. Please go ahead. Your line is open.

Robert John Davies: Thank you for taking my question. My question was just really around sort of, I guess, the outlook for the broader M&A for the – across the overall group. We've obviously had the discussion with Neles going on to quite some time. Now this is obviously something quite different. Just trying to sort of tie into the broader sort of acquisition strategy.

What exactly are you looking to sort of plug into the portfolio? Is there – should we expect more on the Marine side? Could we expect a sort of broader rate and sort of smaller bolt-ons from here? I would just be curious going forward after this – and I know today is sort of focusing on this, but just be kind of keen to hear what you're thinking about the broader acquisition strategy.

Tom Erixon: Yes. We often have these type of questions. I always say that you cannot drive an M&A agenda without an element of opportunism and catch the right deal when it's around and there. Obviously, it needs to play a role in the strategic development of our business and our business portfolio. I think this one does. I don't think anybody is surprised nor concerned that we are trying to accelerate the digital development of the group. That's a pretty obvious one.

And the fact that I think what's been important for us in this case is that there is a business that there is a customer base that creates a firm and stable foundation for the company. It wasn't so important to us whether that stability was to be found in the marine, with marine applications, or in any other area. The issue for us is that all divisions and the group needs to go in the same direction with a full portfolio. And here was the right opportunity and the right time to get it done.

I think we are looking not only on adding short-term value here, we're also looking at gaining time and accelerate the process that we already are in. And that's the importance of this deal. It's not necessarily a capital allocation to the Marine Division as such.

With that said, if you look at the implications for the Marine Division, of course, we are taking – we've guided you for many years that new contracting and volatility at the shipyards is about 1/3 of our business in the Marine Division and 10 percent of our business in the group. So sometimes we get a little bit of overreaction, I think, when it comes to how we are viewed in terms of underlying cyclicality.

And I think this does, I think, guide you also in the direction that the underlying volatility and cyclicality of our Marine Division is getting smaller, and the revenue stream coming from operating the global fleet becoming, as a share, somewhat bigger. It's a step. It's not a giant leap, but it's a step, and there's been many of those over the last 5, 10 years. So I think from a profile point of view, it takes us in the right direction in the Marine Division also.

Robert John Davies: And then maybe just one follow-up. Just in terms of sort of barrier to entry with other competitors, how big is the sort of moat around this technology? What would stop somebody else coming into this segment and trying to compete with you? I would just be kind of curious on some of the details around the actual technology itself.

Tom Erixon: It's a very good question, and I'd be a little bit perhaps superficial in answering it. I think we may have the opportunity at the Capital Markets Day to dive a little bit deeper into the competitive dynamics. It's clear that this is an area where you see certain system builders and engine builders and suppliers who are coming at it from a performance management point of view. You have a couple of companies, not so many like StormGeo, that came from weather analysis originally. And you have some actors that are coming from navigation, positioning systems and others.

So there are various actors involved. It's not – in that sense, you can say it's somewhat of a fragmented competitive landscape. And I would say, at least

from my point of view, it creates perhaps – it's not crystal clear exactly how all these market spaces will develop in the future, but they create some confidence for me that the market leader where StormGeo is backed up by a sizable player of Alfa Laval is a pretty good bet in this space compared to the other options that we see.

So I really thought that our ability to see specifically in this space, leaving any development in the rest of Alfa Laval side, but succeeding with StormGeo in the current domain was partly a scale-driven success game, where we are really well positioned together to achieve that. So – but it is a good question, and there's a lot of color to this. And I think we will have reason to share that with you going forward as well.

Robert John Davies: That's great. Thank you very much.

Operator: And your next question comes from the line of Johan Eliason from Kepler Cheuvreux. Please go ahead. Your line is open.

Johan Eliason: Yes. Hi. It's Johan. Thank you for taking my question. I was just curious you mentioned here other providers. But how would StormGeo sort of stack up versus the navigation software from the Kongsberg Group of (inaudible)? Would it be an input to their navigation solutions? Or would it be a competitor? Or how do you see it? And secondly, why is Alfa Laval (inaudible) StormGeo then, for example, these two names.

Tom Erixon: Yes. I don't see – I see StormGeo as the clear ambition to grow into a full-blown supply in this area. So you can name any company in this space, generally, I would say the starting point is that it is competing interest. Then you know and we know that this is a very dynamic area. Partnerships are not unheard of. So I don't think there's a reason to start by closing a lot of doors per se.

We are still not owning the company. I would not say that the definition of a long-term strategic plan is finished at this point in time. I think that journey is starting. But you should definitely see StormGeo in principle as a major player in the area of navigation as well. And certainly, the product portfolio is in place for getting there.

Johan Eliason: This must be …

Tom Erixon: Was another spin to your question as well, did I lose that?

Johan Eliason: Well, I just wondered if these other names would have been the more natural buyers. I mean do you have any other offering really that goes to the bridge of the ship rather than …

Tom Erixon: We don't. Absolutely not. No. And that's why we are making a bigger step and not a smaller step. I think – you see a lot of companies trying various ideas in this area and we are of the firm opinion that it's much better to get a solid business in, a solid team with experience and customers and profitability than to venture into a small start-up environment with 50 ambitious engineers that never made money.

So this was not a way to say that we're going to help some StormGeo with all of our existing resources. To a degree, StormGeo is going to help us. That's my expectation. My expectation is that the capabilities of this team will be instrumental in driving the digital service growth in the rest of Alfa Laval. That's why we're doing it and that's why we pay a premium to perhaps the trading level that you otherwise would have seen.

Johan Eliason: OK. Excellent. Thank you very much.

Operator: Your next question comes from the line of Sven Weier from UBS. Please go ahead. Your line is open.

Sven Weier: Yes. Good morning. Thanks for taking my question. It's regarding the point you mentioned earlier, Tom, regarding decarbonization of Marine. And you mentioned it yourself, I mean, the penetration of weather routing systems in the marine sector is already relatively high. And so the incremental CO2 savings from that end might be a bit more limited. So I was wondering what has this company already to offer in terms of port connectivity because I think the reduction of waiting times in the harbors is another major lever to reduce CO2. So can you tell us a little bit about the product portfolio beyond just weather routing?

Tom Erixon: Yes. You are spot on in your question, of course. And I think I would sort of disagree with you that – well, it depends what you mean with route advisory and routing per se. But we think we are still in the beginning our basing, routing and the whole process around it. We're still in the beginning of using data as a decision-making tool.

And as you well know and as you indicate, there is a lot of ships that today across the oceans – fuel consumption is intimately related with speed. And if you have a better understanding for what speed you should apply at any given point in time, you will have your fuel consumption drastically reduced. So arriving two days early to port, it's not a very fuel-efficient way to travel. And I would still argue that there are relatively few routing services that largely controls the harbor congestion factor with the traveling speed of the vessels.

So the digitization is still the beginning. I think the value add of actually having a functioning – fully functioning network and infrastructure around this can bring tremendous value still. So we are – my view is that we are still in the beginning of this, not in the end.

Sven Weier: And Tom, you mentioned, obviously, the price of the deal. The multiple is relatively high. So I was just curious, was it a competitive bidding, were you up against other companies in the process, and also if we would be willing to share with us kind of a revenue level for the company that you see in the next three to five years?

Tom Erixon: It's difficult for me to comment on the competitiveness on the bidding. We obviously been aimed to overpay to where the rest of the market was. But I think in any transaction, there is a seller and a buyer and both need to find an agreement on some sort of level. This is where we came in. It makes economic sense for us and our shareholders in our analysis and in our planning. So in that sense, we think it works for us.

The – in terms – we will eventually – we will integrate this. And as you know, we're super, super transparent on, let's say, business unit level in terms of where things are going. But let me say that at least from history and from planning going forward, that this is a company that should have the ambition

to grow faster than the corporate average target of 5 percent that we use for Alfa Laval.

So in that sense, in terms of guidance, we should assume to be somewhat higher than the Alfa Laval in terms of the growth ambition. We should be pretty much on par as we look at it on the EBITDA level in terms of our performance level and in terms of bottom line due to step-up values and some depreciation over a period of time, just as we did with Framo, we will have a somewhat marginal negative impact on the sort of the EPS level. So that's a bit how the financial mix look like from our point of view.

Sven Weier: OK. Thank you, Tom.

Operator: And your next question comes from the line of Madhvendra Singh from BofA. Please go ahead. Your line is open.

Madhvendra Singh: Yes, hi. Thanks for taking my questions. I just wanted to understand the revenue model a bit. If I look at your reported numbers from StormGeo sales of around SEK 700 million. And the number of subscriptions is around 3,000. So is it correct for me to understand that the whole SEK 700 million basically is coming from these 3,000 subscriptions. And whether the revenue – the service lines, which are used to generate these revenues are only weather routing right now? Or there are other major product service lines, which are contributing to this? And if you could give the split between these major service lines.

Tom Erixon: I understand your genuine interest in skinning the cat and slicing the onions. As you know, we are not super fans of guiding the spreadsheets too much in detail. But in general, let's just say that, yes, there are revenue streams that comes from outside of routing (inaudible). There are revenues that comes from outside of subscriptions as well. But I think it's not appropriate for us at this point in time to get into the financial details of StormGeo.

Madhvendra Singh: OK, sure. And then another question is basically on the competitive landscape for you. How does it change your competitiveness compared to your peers? Are there – your major peers or competitors, do they already have such capabilities with them? And in that sense, are you doing it more as

a catch-up? Or this actually gets you a genuine competitive advantage against your competitors?

Tom Erixon: I think we are becoming the coolest kid on the block, if you ask me. I think this is a fair – I mean it's – let's not overstate the size of the deal or all of that. But it is a fairly substantial expansion of digital capabilities that is happening. And of course, our priority is going to be to safeguard StormGeo's business and business model and core.

That is a no-brainer. Obviously, that's what's been building that company should continue. But the potential of leveraging experience, resources, knowledge and accelerate what we have already started in Alfa, I think it's a great opportunity.

Let's put it like this. It's something that is difficult to put a number on. But in a world where we all are convinced that as traditional industry need to digitalize the way of operating and the way of selling and the way of service is something that needs to be taken for real. And we prefer not to make fancy statements to the capital markets about all the good things we are doing and instead of getting some real things done.

And this is a sizable step for us in addressing the challenge and the opportunities that we see in digital. I don't think we were behind our competitors in any shape or form before this With this, I think we have a real muscle. And we look forward to see, together with the team at StormGeo, how we best can utilize it.

Madhvendra Singh: Great. Thank you very much and all the best.

Operator: And your next question comes from the line of Anders Roslund from Pareto Securities. Please go ahead. Your line is open.

Anders Roslund: Yes. Hello. I was a little bit curious on the synergies here. It looks like they are forward-looking and sales in directed, but are there any sort of direct cost synergies in this deal?

Tom Erixon: No cost synergies.

Anders Roslund: OK. And then the future synergies you already mentioned here. But what sort of projects are you talking about when you discuss to combine the efforts here? What sort of projects should we look out for?

Tom Erixon: I think you're going to have to hold it a little bit on that. Obviously, when there is a bidding situation with the company, you are not really in the (inaudible) to discuss joint strategic plans. So understandably, this journey is starting now, given what we know about the digital process within our existing core businesses and our existing service business are about SEK 12 billion, SEK 13 billion, we see opportunities to accelerate that with digital capabilities.

We have been in those internally for years. We are in that process. But gone faster, yes. Will it go faster? I hope so. And from there on, there is obviously a revenue model and the potential profit pool that is very, very relevant for us to accelerate.

Anders Roslund: OK. And the final question regarding the margins. Also, those margins here, EBITDA at 22.5 percent, is that your target margin? Or is it internal things that support a more positive view in the coming five years? Or is it sort of the best guess of a long-term EBITDA margin, the 22.5 percent?

Tom Erixon: Well, we figure the 22.5 percent was pretty much you could find if you did your own research, so we think we might as well put it for your convenience in the press release. So there is no secret about that. I think we will see two aspects of that going forward. One is as a software company, as you well know, the marginal effect of additional sales and volume is positive. So of course, it's a scalable platform. There is no God-given a limit on 22.5 percent.

At the same time, we see this also as a long-term investment and growth opportunities for the rest of the business. And obviously, that may also consume some resources. So there are variables that may play in both directions. I refrain from giving you a forecast for this company as well as we don't do for Alfa Laval, but you should be aware, of course, about the mechanics of this.

Anders Roslund: OK. Thank you.

Operator: As a reminder, if you'd like to ask a question please press star one on your telephone and wait for your name to be announced. And if you wish to cancel your request just press the hash key.

Your next question comes from the line of Karl Bokvist from ABG Sandal Collier. Please go ahead. Your line is open.

Karl Bokvist: Thank you and hello. So my first question is just if it's possible for you to provide some historical numbers just to understand. Has, for example, growth for past three years been in the double digits on sales? And also, you mentioned a margin level for 2020 and just to understand where these margins are coming from? Or have the margins been expanding for some time? Or have they been at a steady level?

Tom Erixon: Yes. I'd sort of defer the question – takes us into a historic analysis and review of the drivers and you – I think that is driving this discussion too far at this point in time. Let me just say that we think that 2020 was a fair representation of the company in terms of where it is. And given that we assume that this company has the growth potential somewhat higher than the 5 percent that we have as a target for the group, it should give you some indication from where they were coming from. I think that frames it may be on a reasonable level for you.

Karl Bokvist: All right. Understandable. And then two follow-ups is just any – do you see any kind of obstacles to why this shouldn't close in the second quarter as you guide for? And the follow-up is also perhaps mainly towards you, Jan, if it's possible to give any kind of insight into what kind of step-up values you estimate for this acquisition.

Jan Allde: Yes. I mean, of course, in an acquisition like this, it's not surprising that you creating or we are creating sizable intangibles. I wouldn't like to go into the exact split of how we see that PPA being done at this point. But I would say you are creating intangibles on par with the acquisition price.

Tom Erixon: And closing?

Jan Allde: And closing, yes, we don't see really any significant reason. We don't see an antitrust clearance required. So at this point, we don't see any significant reason why we wouldn't be able to close here during Q2.

Karl Bokvist: Understandable. Thank you.

Tom Erixon: Take the last question at this time.

Operator: There are no further questions at this time. So I will hand back over to you for your final remarks.

Tom Erixon: I think that was the final remark. Thank you very much, and I hope you share some of the excitement among you that we feel here at Alfa Laval. And we'll keep you updated in capital markets to come. Thank you.

Operator: This concludes today's conference. Thank you all for participating, and you may now all disconnect.

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