Alfa Laval AB

Alfa Laval Q3-26 report

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Transcript

Speakers:

Tom Erixon

Fredrik Ekstrom

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Tom Erixon

Good morning, and welcome to Alfa Laval's Earnings Call for the Third Quarter 2026. Fredrik and I will take you through the quarter, and then we open for Q&A, as always. Let me then start with a few introductory comments.

Although we had strong tailwinds from both data centers and ship contracting in the quarter, the growth was broad and balanced. Global market conditions remained firm in the quarter, driven by the US and China.

While part of our portfolio is benefiting of some cyclical growth short-term, Alfa Laval continues to invest for long-term structural growth. We continue to invest in R&D, in market positions, competitive supply chains, and service.

With substantial investments for the future market leadership, the group delivers still on the expected profitability level in the quarter at 18%. All three divisions were at their respective profitability target ranges.

Finally, we continue to optimize the capex program within the current footprint. Due to the accelerated growth, our capex guidance in the short term is increased from SEK3 billion to SEK4 billion yearly.

So, with that, let's move on to the key figures. The quarter was special with regard to order intake, with SEK23.2 billion new record order level, perhaps a bit unusual in the seasonally somewhat lower third quarter.

Invoicing and profits grew on a more normalized level with an 8% and 6% growth, respectively. As a result, the order book reached a new record level of just below SEK60 billion.

On the divisional level, starting with Energy, it was a significant growth quarter, both for orders and for invoicing. The data center business amounted to approximately SEK2 billion in the quarter in terms of order intake, and the 12-month rolling or rolling pace right now is in line with the earlier guidance, now at the level well above SEK5 billion.

To ensure a healthy order book, we do not recognize orders in this area more than 12 months forward. The return to growth in the important HVAC segment, including heat pumps, started earlier this year and continued well during the third quarter.

Then, over the last 12 months, we have as a firm and in the division concluded three important acquisitions. The first one, sometime ago, was the Fives Cryo business, and our expectations on the strategic fit on the cryo business and performance have been met, and we continue to invest to build market share in this important area.

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The last two acquisitions are heat exchanger companies in China. The last one closed just a week ago. As we build our market share in China, the two acquisitions complements Alfa Laval well, both in technologies and in market positions. They add approximately or somewhat above SEK1 billion in revenue on a yearly basis, mainly in China, and it will serve as important growth platforms going forward.

Moving on to the Food & Pharma division. Again, it was a solid quarter for the division, including some important project wins in the biofuel sector. The transactional business continued strong and is on a record level. The recent capacity increases in the US specifically was arriving timely in the quarter in that respect.

All three key markets for the division; US, China, and India had a strong quarter. Invoicing was a bit below expectations, but influenced by delivery schedules rather than supply chain constraints.

And with that, on to the Ocean division. Ship contracting is on an exceptional level at the moment, driven by longer shipping routes and high freight rates. As an asset class for ships, new orders are supported both by traditional shipowners and financial investors. The final contracting number for ships for this year, 2026, will be well above 3,000 ships, substantially ahead of the forecast a year ago.

For Alfa Laval, it resulted in a new record level of orders at SEK8.3 billion in the quarter, and in all, 2026 is far beating our expectations compared to a year ago.

Cargo pumping was, as always, converting early into Alfa Laval's order book. The major capex program at Framo in Bergen is executed with priority on upgrading the production lines for cargo pumping systems specifically, while order intake was solid across all of the business units, and the current ship contracting has not still translated fully into the Alfa Laval order books.

The project pipeline in offshore continues to build stronger, and the current turmoil in the global energy markets is expected to create a new capex boom in the offshore segments going forward.

Then on to service. Service is one of several important structural growth drivers, and it grew 6% organically, however, a bit uneven across the three divisions. The Energy division had a very strong quarter, and growing well above double-digit level for the quarter.

Food & Pharma was okay with a more modest growth, while service declined in the Ocean division, due to sanctions and

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due to a degree, the high utilization of the remaining fleet. For your reference, approximately 4,000 ships are out of the global merchant fleet of 60,000 ships are out of scope for Alfa Laval's service activities.

With the rapid growth in capital sales, service as a share of total sales is now clearly below 30%. While a positive challenge, it does perhaps impact the group margin somewhat in terms of the mix change going forward.

Then on to a couple of comments on the key markets and regions. As you know, US and China are our two top markets, currently accounting for above 40% of new orders. Both markets are currently growing faster than the other regions in the world.

We have strong Alfa Laval teams in both markets, and we allocate a substantial part of our capex program to these markets as well to ensure strong local presence and reliable supply chains.

On the overall global map, as indicated earlier, growth was broad-based globally with all regions except one growing on a good level. The India, Middle East region declined somewhat. After a record quarter in Q2, Middle East specifically struggled, for obvious reason, in a complex environment. We do everything we can to keep our customers, our own staff, and their families safe.

India specifically still had a strong quarter and is expected to be an important growth engine over the next decade. For this reason, we have allocated our Indian capex plan a higher priority and increased the efforts there substantially going forward.

And with that, I hand over to Fredrik.

Fredrik Ekstrom

Thank you, Tom, and good to have you all here for the quarter three earnings call. Some additional details around the strong SEK23.2 billion order intake in quarter three. In the Energy division, beyond the strong booking in data centers, power and fuel applications booked some SEK2 billion in the quarter.

HVAC and refrigeration, in particular, heat pumps continue to grow, and better utilization of the capacity added a few years ago is a fact. Traditional Food & Pharma applications also posted strong orders in brewery, dairy, and prepared foods and beverages.

Transactional business continues to outperform comps, and pumping systems in the Ocean division continue to benefit from a high contracting level of tankers. Contracting for bulk

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carriers, container ships, and ferries, including RoRos, contributed with a good order intake for the marine product portfolio.

SEK63.1 billion in order intake year-to-date represents a 23% growth, of which 22% is organic. Good momentum heading into quarter four with an all-time two high quarters behind us.

After another record quarter with a book-to-bill of 1.25, the order book closed the quarter at just shy of SEK60 billion. The order book is deemed to be priced well in line with input costs and current cost levels.

Quarter three sales reached SEK18.6 billion, a growth of 7.8% compared to quarter three last year. The transactional part of the business outpaces the total, meaning that manufacturing capacity is well-utilized in the majority of our manufacturing units. In certain areas and applications, a higher delivery pace and capacity will require more -- further investments.

Those investment cases will be planned and executed over the coming years with investment peaks in 2027 and 2028. These investments in capacity lead us to revise our capex guidance to a range between SEK3 billion to SEK4 billion per year for the next 3 years, and up from the guidance of SEK2.5 billion to SEK3 billion that we currently have.

Year-to-date sales of SEK52.6 billion, an organic growth of 4.5%. However, to provide more context for future investments plans, the transactional business revenue, including service, has grown with over 10% in the last 9 months.

Now to some P&L highlights. Gross profit margin of 37.6% is in line with quarter three last year and well-supported by a high utilization rate of manufacturing assets and a favorable mix effect from transactional business.

Sales and administration costs increased in the quarter with 10% with three major contributors of equal weight inflation, acquired businesses with no comps, and growth-driven addition of resources. R&D also continues to grow at 7%, which is in line with innovation ambitions and product development initiatives.

Operating income increased with 5%, but does not drop through fully into EPS due to one-off bookings in the financial items related to the termination of a JV. Year-to-date gross profit margin at 38.2%, which after all costs and taxes results in an EPS of SEK14.91. Adjusted EBITA in

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quarter three in money is at all-time high of SEK3.4 billion, equaling a margin of 18.1%.

On a divisional level, the margins in the quarter are representative of a good level going forward, with the Energy division at 18.1%, Food & Pharma division at 15.5%, and the Ocean division at 21.3%. Year-to-date, the EBITA margin stands at 17.7%, which is above the external target for the group.

Our debt position remains stable compared to quarter three 2023, with all ratios improving in relation to EBITDA last 12 months. Net debt, including leases in relation to EBITDA last 12 months, at 0.94. Good cash balance generated from a good cash conversion, which takes us to the cash flow analysis.

Cash flow from operating activities in quarter three amounted to SEK3.4 billion, a marked improvement from the year before. Capex continues at a high pace in the quarter at SEK819 million. A positive final line cash flow caps off caps off a strong quarter three.

Year-to-date, the pattern is similar with a strong cash flow contribution from operating activities, capital expenditures at SEK2.4 billion, acquisitions for SEK600 million so far, and financing activities representing mainly the shareholder dividend of SEK3.7 billion.

Now to some guidance. In line with raising the guidance on capex going forward, we have also increased the capex guidance for 2026 with SEK1 billion, expected in quarter four, and 2027 on a level of SEK4 billion.

Amortization of step-up values in on the in the order of SEK100 million -- SEK180 million in quarter four and SEK730 million for 2027, based on current acquisitions. Tax rate guidance remains in the range of 24% to 26%.

And with that, I hand over back to Tom for some closing remarks.

Tom Erixon

Thank you, Fredrik. And then finally, the forward-looking comment. It is for us, and I think globally, the demand trends are strong, and we expect the overall demand trends to remain favorable and solid into Q4. With that said, after two record quarters, we are somewhat more modest when it comes to how we believe this will convert for us.

So, we believe overall on a somewhat lower demand in Q4 than in Q3. And on the divisional level, we expect the Energy division to remain at about the same level, Food & Pharma to be at a somewhat lower level, and the Marine division or

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Ocean division, sorry, specifically at lower demand level. And so with that, we are open for Q&A.

Operator

We will now begin the question-and-answer session. Anyone who wishes to ask a question may press star and one on their telephone. You will hear a tone to confirm that you have entered the queue. If you wish to remove yourself from the question queue, you may press star and two. Questioners on the phone are requested to disable the loudspeaker mode when asking a question. Anyone who has a question may press star and one at this time.

The first question comes from Yang Meihen from Goldman Sachs. Please go ahead.

Yang Meihen

Hi, good morning. Thank you for taking my question. I just have two questions. First of all, on the rationale behind your increasing capex in '27-'28. You mentioned that you expect data center demand to remain stable over the next 2 years, which is a bit surprising. But given that, why did you decide to increase your capex?

And secondly, if you can give us more color on the visibility of your cargo pumping orders now? Is it well into '27 and '28 now? Thank you.

Tom Erixon

Yeah, let me start with the second question. That's an easy one. '27 covered, we are well into '28. So, and overall, if we look at the delivery schedules for the ships now, after this year completed, the delivery schedules for the marine side will remain quite strong into 2029, as well. We already know that. So overall, we look at a favorable scenario in general for the Ocean division over the coming years.

The capex is obviously well through, and some of these investments have been planned and decided to be executed now, and it's been sort of part of a long-term growth plan. It's not only data center that is driving it. But as we are ramping to the full level that we have indicated on data centers, we will need some additional press and business capacity to get the job done.

So, that takes us up to what we at this point in time would say is probably the peak of the capex cycle for us. We have not guided yet beyond the next two years, because those are quite firm right now, but I think Fredrik's and my expectations will be that this will be the peak of the cycle.

I remind everybody that we have rebuilt the manufacturing footprint substantially over the last five, seven years, and we are coming to an end also of that. Included in the capex going forward, we still have the decisions made in Norway in Bergen for the cargo pumping and a number of areas that

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are spilling over into '27-'28 when it comes to the cash out for the company.

So, I think we are slowing in our decision-making process right now, but we have still a number of years on ongoing programs in Ocean, in energy, and to some degree also in food and pharma to cover for the expected level.

Yang Meihen — Got it. Thank you very much.

Operator — The next question comes from the line of John Kim from Deutsche Bank. Please go ahead.

John Kim — Hi, good morning. I'm wondering if we could talk a little bit about the visibility on your energy exposure. I know you don't look orders beyond 12 months, but given what we're seeing in peers and the build-out, how would you argue your energy backlog cover would work if you remove the 12-month constraint?

Tom Erixon — Well, I mean, we are -- let me start with the basic principle. We are conservative when it comes to order recognition. We require clear projects, clear project delivery schedules, and clear down payments in order to recognize orders. So, we put a lot of -- we put a lot of emphasis on having a current order book at any moment in time.

And so, in line with that, when we look at, for example, the data center business, which to a degree are frame agreements, and to a degree are anticipations, we find that the visibility beyond 12 months is somewhat unclear. And for that reason, we prefer to be a bit stringent in how we recognize it in the order book.

And for that reason, we're also given a bit of a forward-looking comment when it comes to how we look at the ramping and rolling 12-month pace in the data center business. And as indicated, we may arrive to a number around 10 billion or so going forward, but we are communicating what we're seeing right now, what the current rates are.

Everybody is aware about the upside and the potential risks in terms of how far will the capex program be able to materialize in the coming years? So, you know, we are we are just taking a moderate view. But as you can see from the capex programs, it doesn't mean that we're going to leave our customers standing in the dark on this. We are ramping fully to be able to handle what we see as the customer's business case right now.

John Kim — Okay. Helpful. Follow-on question, if I may. If we think about the Framo investments, should we think of it more as

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capacity expansion or more efficient production? And how should we think about phasing, let's say, the next three years? Thank you.

Tom Erixon

Yeah, they I would kind of split it in two. As you know, it was about a 4 billion program that we approved. It was a multiyear program, so it will run into 2030-plus before completed. The first part is really a capacity, automation, efficiency investment in the cargo pumping production lines, so that's what we are executing first. It comes in handy, to say the least. And so, that's a modernizing of 20, 25-year-old machine and equipment situation at the units, and we're taking a giant step there.

The second part of it is more structural. We have outgrown a number of our other sites around Bergen. We are spread there in a bit of a distributed footprint, if you like. And so, we are consolidating ourselves into new area, and that is -- if there is two main drivers for that is to improve the service workshop and the space that we need for that, and to allow for much better flow and space and growth for our offshore business, which has been growing significantly over the last five years.

So, it was time to redo it. We put it in in one big package, but those are the two mainly parts of that, approximately 50-50 split.

John Kim

Okay. Thank you.

Operator

The next question comes from the line of Klas Bergelind from Citi. Please go ahead.

Klas Bergelind

Thank you. Hi, Tom and Fredrik. Klas at Citi. So, my first question is looking at capacity at the yards and particularly around product tankers. There's obviously nothing wrong with demand, but we've seen this before. Strong contracting, and then lead times, they get extended, yards get full, and we see contracting fading.

I don't think it will be as dramatic this time as last time, but curious on your thoughts, Tom, into '27 if you think the new capacity in areas like China will be enough here, or if we should start to see an order normalization in Framo next year. You're guiding for lower demand in Marine into the fourth quarter, might be linked here to these extended lead times. I'll start here. Thank you.

Tom Erixon

Difficult to forecast yard contracting. Everybody were wrong coming into this year, and so we have two strong years of contracting behind us and two strong years for tankers in general and product tankers as well. And so, of course, at some point in time, it needs to narrow down somewhat, and

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I think it's not unlikely that we will see that in terms of the order intake adjustment for 2027.

With two years of orders in the books, I think it doesn't add much value to us or to anybody to sit with too long order books on this one. So, I think our best estimate would be that we will see a moderation on those orders.

With that said, if you look at the aging of the fleet and the merchant fleet in general, and for product tankers specifically, we don't have an exceptionally young fleet even after the replacements of these ships.

Scrapping has been exceptionally low for many years. So, we see what this means, but the only thing we know for sure is that the global shipyard capacity is being extended at the moment, and it's not only China.

There are some other markets where you see clearly signs of initial investment to increase ship capacity. So, I think the expectations in general is that we will continue to have a reasonably firm contracting market for the years to come.

Klas Bergelind

That's good. Then my second one is on the margin performance in Marine. You had lower invoicing, somewhat lower service, you explained the reasons, and then you had somewhat higher cost. The current level, is that the level we should assume also into the second half, or could the margin go up again?

I mean, the service business, depending on the conflict, the conflict might not recover in the short term, but I'm interested on the cost side and the load into the second half. Thank you.

Tom Erixon

The load is good. As Fredrik said, I think we are priced reasonably when it comes to input cost, so the order book is healthy from that point of view. There are mix changes quarter-by-quarter that affects this.

I don't want to be more specific than what we said about the profitability ranges before. When we increased our overall group target to 17% on EBITA margin, we indicated that we wanted to see the Food & Pharma at about 15%, at the Energy at 17%-plus, and we expected Marine to remain at 20%-plus for a period of time. And that's where we are in the guidance right now. You will see some oscillations quarter-by-quarter, but in in terms of ranges, that's what you should expect.

Klas Bergelind

Okay. Absolute final one is on the base order growth in Food & Pharma. I mean, it's still a good level, but it was a bit lower than I thought. Can we can we talk through what you saw

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there sequentially and particularly around the indirect growth that you had from data center last quarter, the valves, the fittings on the flow side? Did you move some of the some of this business into Energy to have everything sort of data center-related under the same roof? Thank you.

Fredrik Ekstrom — Yeah. Klas, you're actually quite right. We have done that going forward. We have not done it retroactively into quarter two and quarter one, but we have, from starting quarter three, moved the volume that comes in for pumps and valves related to data centers from Food & Pharma to the Energy division, simply to be clear and transparent about where the products are ending up from an industry point of view. That means that the revenue, the order intake, and the cost will also come over to the Energy division. So, it's not only the volume that's being moved over. It's the total activity.

Klas Bergelind — Okay, then it makes sense. Thank you.

Operator — The next question comes from the line of Akash Gupta from JPMorgan. Please go ahead.

Jeremy — Hi, good morning. It's actually Jeremy on Akash's line. Thanks for taking my questions. I've got two, if I may. Firstly, can you give us a bit more insights into how much of your data center business is US hyperscalers versus non-US, and especially China? Basically, I'm trying to understand how you can benefit from investments from different customers and in different regions of the world.

Tom Erixon — I'll be maybe not 100% precise, but I think right now, if we look at this year and last quarter, US accounts for approximately 80% of our data center business. The Chinese side, we start started to see the growth coming in to our books in the beginning of the year, and that's the lion's share that is outside of the US, and that's approximately how the mix looks like.

From the trends we are seeing -- we will see a clearly continued increase in China for the next couple of years, and in fact, part of the capex guidance is related to us making sure that we are capacity-balanced in the Chinese market specifically. Was there a second part to the question? No. Maybe that was it. You have to repeat it otherwise.

Jeremy — That was it. That's helpful. The second one then, maybe. Can you talk about the margin drag you are currently experiencing due to the plant capacity expansion in Energy? And I'm asking because you're guiding for an elevated level

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of capex the next couple of years, and I'm just wondering how should we think about this drag going forward?

Tom Erixon

Well, we have -- you know, for these capacity investments, we have about 24 months' lead time, so it is a leap of faith in terms of where we believe that demand trends will be over the coming years. I think, you know, I don't -- we don't have a guidance to a very big impact on margins going forward. We expect to load these pretty much with the average margin mix, so I think the key for us is to see where the, you know, demand trends will be in terms of volumes.

Right now, the only thing I can say is that it -- this is not only about future demand. If we look at our current units, there are too many places where we run 24/7. And 24/7 operations in mechanical engineering industry is not an optimal shift structure, and so we need to ease off the pressure in our existing pressing lines, and so part of what we're doing now is creating a more balanced production schedule in our units.

I don't think it will have a big impact in terms of our product cost and the margin per se, but the increased capital allocation into the supply chain is partly being balanced by a better cost structure in the manning structures and the plant structures of operating them.

So I can't give you the exact split, but I would say maybe a third of what we're doing right now is just helping us to balance the plants better, and about two-thirds will flow into direct increased capacity. And if we need to run harder even after that, so we can do it, but that's what we're aiming for.

Fredrik Ekstrom

I think it's also fair to say that it's accelerating the removal of older assets or keeping older assets as a peak capacity leveler and bringing in new capacity a little bit earlier than we would have done otherwise. But it is part of a normal replacement schedule, as well.

And then I would add that the interchangeability of these presses is pretty good. So, if we say that data centers doesn't turn out or doesn't pan out to the same volumes that we expect, there are other growth verticals that will take up those volumes.

Jeremy

That's very clear. Thanks very much.

Operator

The next question comes from the line of Andreas Koski from BNP Paribas. Please go ahead.

Andreas Koski

Thank you and good morning. So, I would like to start with a question about your backlog and deliveries in Ocean. So, with yards expanding in China, how do you think about the

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delivery potential for Ocean in the coming years? You are saying that your backlog covers '27, large part of '28 going into '29. But do you see that your deliveries in Ocean can pick up in '27 and '28, and is it possible to reach a revenue level well above SEK25 billion-plus, or are we capped because of the shipyard constraints for the coming years? Thank you.

Tom Erixon

I think we are under delivery pressure into 2027. I think our invoicing -- on our side, the -- in the supply chain, our issue is not the manufacturing capacity, it's the commissioning capacity. And commissioning of new ships, especially on advanced equipment with new yards, with inexperienced staff, the demands on us are very high.

So, we have a major effort at the moment to ensure that the commissioning can follow the -- what we see as the current yard production schedules. Now, so I think we will fulfill our part of the equation, but I think Klas was on to this earlier.

Sometimes we see that when the delivery schedules are very tight at the yards, and especially we see new yards coming on stream, they sometimes fall behind their delivery schedules that are planned.

So, I think we will have to see how it effects, but I still believe that net-net, we will have a higher production capacity and the global yards in 2027, and most likely, it will result in some tailwinds for the invoicing side on Marine. I don't know if you want to

Fredrik Ekstrom

No. I think that covers it well.

Andreas Koski

Yeah. Thank you. And then just on the margins in Ocean, you refer to, say, a negative mix and under-absorption. But can you give us an idea maybe of the year-to-date margins in Ocean, excluding pumping systems, or maybe talk a little bit how much of the, say, sequential margin decline that we saw in Q3 was related to the mix of maybe less pumping system sales, more other equipment sales, and how much was related to the to the under-absorption?

Fredrik Ekstrom

Well, I mean, I first of all, I don't think we have many units in the Marine division or manufacturing units to the Marine division that have an under-absorption in the factories. The load is good, and we have a good planning horizon on that. So, that's not where we have -- that's where we're not have -- that's not where you find the reason for the lower level of margin compared sequentially. However, this is well in line with where we expect to be when it comes to the margins in the Ocean division.

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I would also add that, you know, the mix is the biggest component of it, and we have discussed this before, that we were going to have quarters where pumping systems wouldn't be as dominant, together with a very high degree of service revenue. When you have those two together in a quarter, you very well get the 24% and 23% margins that we have seen over the last past quarters.

Now that we see that the revenue starts to have a larger component of the traditional Alfa Laval portfolio and a lower component of service and pumping system in this particular quarter, well, then you have the effect that we come down to the level that we are now, which is plus 21%, which is still a fantastic profit margin for the Ocean division.

Andreas Koski — Okay. So all of it is mix-related, you could say. That's understood. Thank you. And then lastly, on capex, so with the higher capex plans now for '27-'28, do you see that -- maybe, yeah, do you see that capex levels can come down post-'28 at the same time as you have now or will now have invested for the SEK100 billion revenue target in 2030?

Tom Erixon — Yeah, I think, you know, when we have completed the capex program 2028 then we are geared for what we need to do 2030. There will not be any new decisions that will in a meaningful way impact our capacity into 2030. So our best estimate is that this is the peak.

We actually thought that the SEK3 billion was going to be the peak before, so we we've been wrong in our crystal balls on a number of dimensions, but I think, we just feel it's been a long run now of positive industrial growth since the start of COVID and through all this period.

And I think my stomach tells me that, at some point in time, this positive business cycle will also come a little bit to an end, and so I just doubt that we will see this thing continue to, you know, just the industrial machine in the Western world, and it will continue to develop in line with the last 8 years.

So, the SEK100 billion plan, we feel comfortable with at this point in time, and capacity-wise, we will be there by 2028 and return to a more normal capex program. That's our best estimate. That's was a long-term forward-looking comment.

Fredrik Ekstrom — It was indeed, but that's our ambition, that we do return to a lower level, yes.

Andreas Koski — Thank you very much. Thank you.

Operator — The next question comes from the line of Anders Idborg from ABG Sundal Collier. Please go ahead.

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Anders Idborg

Hi. Morning. Thanks. Could you just talk a bit more about the service business in Ocean? It's been another quarter with sort of flattish demand. I suppose, can this go on indefinitely as long as there's just high pressure to keep or high incentives, you should say, to keep ships sailing? And how is profitability developing and mix within services in Ocean?

Tom Erixon

The service business in Ocean division is negative in the quarter, so we are down high single-digit in volume compared to last year. There's not so important changes in the service mix and the service margin, so we're not concerned with that.

They are, you know, why is service declining? It is partly a guess work on our side. We have stated that the one fact that we know is that around 4,000 ships are sanctioned, under sanctions and are out of our service scope, and this is typically ship classes that we are working with. So, obviously, we're taking out part of our customer base from the service, and I would say that's the main structural shift that we see in the service business.

I have a hard time to see that will continue, in the sense that out of this merchant fleet of 60,000 ships, there's a limit to how many can be put into the sanctions regime and how many are needed in that part of the global trade, so we don't expect that to continue to rise and, consequently, will be a neutral factor going forward until the war in Ukraine is over.

The other side is a bit of a guess work for us. Normally, when ship owners are making a lot of money, also the service business tend to grow. At this point in time, we have the feeling that extremely high utilization rates and need for shipping capacity keeps the ships running a bit more intense than normally, and we see a delay factor in the service business.

That's our best estimate for the situation. And as long as the pressure is on, that will continue a little bit. But obviously, service intervals to some degree are needed, and they are given cycles on that, so, I think we will see better conditions and a trend shift coming at some point in time. I will not predict it by the quarter, but reasonably short-medium term, we ought to see a return back to growth.

Anders Idborg

Okay, that's clear. And just a follow-up on energy and LNG. It's been an active market out there. I didn't see any mentioning of it or your cryo business in this release. Maybe I missed it, but could you just tell us what happened and what the pipeline looks like in that segment?

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Tom Erixon

Yeah, the pipeline is obviously complicated by the warlike conditions in the Middle East. And so, new projects there are obviously a bit unclear, and that's one of the big LNG markets. We booked a good order in the US for large LNG installation in the quarter, and we see generally speaking, quite a good trend not only for LNG, but for industrial gases that are used in a number of areas, including space flights.

So there is a good underlying demand on the cryo side, and we have a positive view compared to when we acquired the company of our abilities to grow both in terms of market and market share.

Anders Idborg

Okay, thank you.

Operator

The next question comes from the line of Sebastian Kuenne from RBC Capital. Please go ahead.

Sebastian Kuenne

Yeah, thank you for taking my questions. First, I would like to understand a little bit better the underlying margin in Energy. You speak of good utilization, but you are still also aggressively ramping output for the data center related heat exchangers. But then the margin also improved.

So, I try to understand how much of ramping costs or one-off costs or extra costs you still have within Energy that at some point will fall away when this business matures and then leaves just, the underlying business without any one-off.

So, I try to understand whether the 17% is now your end point, or whether there is more to come simply because you ramp up and have ramped, and then production goes more smoothly, if that makes sense. Thank you.

Tom Erixon

Well, the problem is there's going to be 20 factors affecting the margin going forward on and the scaling cost is just a small part of everything that goes into the equation, and that's why we typically are a little bit cautious in terms of predicting the plus and minuses on all the dimensions.

I think what the best guidance we can give you on the specific number on the ramping is the fact that, in any capex program, it consists of both capex and opex. And I guess, Fredrik, that opex share on the current program is around 20%?

Fredrik Ekstrom

Yeah.

Tom Erixon

Something like that.

Fredrik Ekstrom

Yep.

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Tom Erixon

So, if you look at the SEK3 billion or SEK4 billion, consider about 20% of that dropping down into the P&L, and when it goes away, it goes away. I would still caution you to use a model where you have a 20% profit improvement just because of that. Input costs, material costs, load, pricing, etcetera., will mix. Service will play huge part.

The other but -- the guiding comments I will give you is that we thought that the Energy margin in last in Q2 was a bit depressed. So, this was not the Q2 was not a normalized level. We indicated we want to see this division at 17%, 17%-plus. So the quarter was not exceptional in our point of view.

Fredrik Ekstrom

If I could just add to that, and to everything Tom has said, the ramping costs, I mean, we have had them now for a long time related to investments, so I think you can almost say they are a normalized part of the costs.

What's really different, I think, in this quarter is that we have really, it's really come up now that we have a better balance in the in our manufacturing, the use of our manufacturing assets, particularly for those going into the HVAC industry.

And then there's a mix shift. I mean, there's a lot of transactional business and service in this quarter, which is good, and that's the level we expect it to be at. We would like to see, of course, good projects business come through, as well.

Sebastian Kuenne

Yeah, understood. Thank you. And for Food & Pharma, you seem to get a bit more projects now, and I would guess there's also projects in the pipeline for biofuels, especially. Should we see this as an indication of mix going down a bit because you have more engineering hours, more project-related business?

Or is this priced at the level where Food & Pharma is now because it's higher demand, it's incremental business, and you can you have some leverage on the pricing? Maybe a comment there. Thank you.

Tom Erixon

Mix will affect, and the difficulty with projects is that we do not know exactly where they are going to end until they are commissioned and ready and paid for and invoiced, and all that. So our forward-looking comments are a little bit less clear when it comes to the mix impact.

What I think is important in this is that our transactional business is running extremely strong. We are growing with 10% in the quarter, and the service business in the Food & Pharma division is growing by mid-high single-digit numbers, as well, and expected to continue to do so.

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So, there is a, -- against an increase in product orders, there is a fairly large transactional business that is growing at a good rate. So, I do not think even in a slightly stronger project environment, we will have a big negative mix effect from the project growth. That would be my estimate.

Fredrik Ekstrom

Yeah. And I would agree with Tom. I would just add to the fact that, of course, now when we get more project business, we are utilizing engineering hours and that capacity, which then offsets the dilutive nature of a project business margin compared to the transactional one. So, it balances out.

Sebastian Kuenne

Yeah. A last question briefly, outside of data center, marine, and food, offshore, petrochem, nuclear, could you give us in some indication of what the market is doing at the moment? Thank you.

Tom Erixon

I think I will be very quick on that. Nuclear is going to be important in in the future. We believe that we cool a lot of reactors, and we have important relationship with some of the reactor technology suppliers.

So, as it grows, we will follow with it, but of course, it's many years of implementation of the new reactors, so the it doesn't hit our invoicing very quickly.

On offshore, I think we will see more of a short-term effect. As I indicated, the transparency of the lead pipeline is quite good, and we see it strengthening. So, we believe, in 2027, we will see a stronger year for offshore than before. And I think the energy resilience and security issues are going to highlight this in a substantial way in the years to come.

Sebastian Kuenne

Perfect. Thank you so much for your help. Much appreciated.

Operator

The next question comes from the line of Carl Deijenberg from DNB Carnegie. Please go ahead.

Carl Deijenberg

Thank you very much. Good morning, Fredrik and Tom. So, two questions from my side. And first of all, Fredrik, if you could help us a little bit on the sales bridge in the Energy division.

I thought that or I see that the structural impact is almost 18% here in Q3, and I thought that the cryo business was included from the beginning of Q3 last year, i.e., the organic sales figure for this year.

So, first of all, that, if you could share some color on that. And maybe also with regards to the currency impact on the same division here for Q3, as well, would be interested to hear about.

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Fredrik Ekstrom

Sure. When you look at the structural part of it when it comes to the sales bridge for the Energy division, it is primarily related then to the acquisitions that we have in China from a structural point of view when it comes to the sales bridge. There is also an element of movement of businesses, and that's also affecting the structural part of it.

The currency, well, there is the exposure that you have at the at any given point in time. We have a lot of invoicing now going to the US. We've had a marked movement of the dollar versus the versus SEK, and, of course, the euro has also gained ground on the SEK, and both of those have a negative impact here when you look at the sales bridge.

Carl Deijenberg

Okay, very well. And maybe secondly to that, as well. I mean, would it be possible to say on that 18% the structural impact, is it roughly the magnitude of those Chinese acquisitions, is that half-half or just to get a ballpark sense of what the impact was here in Q3?

Fredrik Ekstrom

Yeah, I think that's a fair assessment on that.

Carl Deijenberg

Great. Secondly, I also wanted to ask Tom if you could share some more color on your views of the heat pump market here. I mean, obviously, you had a couple of quarters with underutilization and the inventory drawdowns that followed the previous upcycle, and so forth.

And now we're seeing gas prices coming up in Europe, and so forth, again. And we seem to be heading into winter here with a yeah, a quite stressed energy situation, which could be favorable for heat pump adoption. So, what are you hearing from the OEMs out there, and do you see that demand already now is being positively impacted by those factors?

Tom Erixon

I think when it comes to the external factors, I think the situation will be a little bit less clear. While we see higher gas prices, we also see the risk of high electricity prices in Europe, so I think the balancing between the different sources of energy may perhaps is not affecting so much the implementation of heat pump solutions in in Europe this winter.

The growth in the heat pump business has been going on now for quite some time. We are, I think, four to six quarters into the growth period. We are in running rate, maybe 30%, 40% below the peak where we were in 2023. And so, and at that peak, we know now afterwards that part of that was actually an inventory buildup. So, the market is getting back to a reasonably healthy level.

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Our best view of this is that we will continue to see, you know, a steady organic growth climbing. We don't expect another peak. Should we have one, we are pretty well supplied with pressing capacity since the last peak, and so we are ready to go.

But I think we will not see we don't expect to see the same type of rapid growth that we had at the last cycle. It was your business at the time, maybe you have a further comment on that.

Fredrik Ekstrom — No. I think, as you say, we're catching up to the growth trend we had pre-invasion of Ukraine.

Carl Deijenberg — Okay. Very well, thank you guys.

Tom Erixon — Okay, and I think with that, we are done for this time. I remind you, in a couple of weeks, we have our digital Capital Markets Day. We will do a couple of interesting deep dives in a number of, for us, very important business verticals, so I encourage you to spend the I think three hours together with us in November and otherwise we will meet in early February for the report and Q4 earnings call.

Fredrik Ekstrom — Thank you very much.

Tom Erixon — Thank you.

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