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PRESENTATION

Hanna-Maria Heikkinen - *Valmet Corporation - IR*

Good afternoon ladies and gentlemen, you are warmly welcome to this news conference for Valmet's Q1 2014 results. My name is Hanna-Maria Heikkinen, and I'm in-charge of Investor Relations. Today our CEO Pasi Laine, and our CFO Markku Honkasalo will go through our Q1 results. After the presentation, there is a possibility to ask questions. We will start from here, Keilasatama and then it's time for international questions.

Please Pasi, let's get started.

Pasi Laine - *Valmet Corporation - CEO*

Okay. Thank you, Hanna-Maria. So welcome to the first quarterly result review of Valmet, new-born Valmet. So as a starting we are saying that we had very strong development in orders received and like you have been reading our reports, then profitability needs still a lot of focus from management and from the whole organization.

So what I will have together with Markku, the agenda today is to brief our results, then how the business lines have been developing. Markku, will go through the financial development. I will continue with the guidance and short-term outlook. And then we'll have the summary after the questions and answers.

So in a nutshell I would say that first quarter was of course very successful in orders received in capital business. So orders received increased in Pulp and Energy. I will go to that through more in details later. Orders received increased in Paper as well net sales declined compared to last year due to the low order intake in last year.

We had stable development in services, stable orders received and stable net sales compared to last year. Our order backlog increased from the last year's level a lot. So it went up a little bit more than EUR570 million compared to end of the last year. And of course that's very good development for Valmet.



Then our results EBITA was not close to the targeted level. So it needs to be still improved a lot in coming quarters and coming years. So the profitability was under the targeted level. It improved compared to end of the last year despite our net sales was lower than last quarter last year.

Our profitability improvement programs has been progressing as planned. I will have couple words about that one as well. And then of course to continue to improve the profitability, we have to continue with our quality and procurement and many other activities. So the profitability continues to be on the management's agenda on -- as a very important topic.

And then of course our strong balance sheet continued to be strong. So net debt was EUR-39 million and our gearing -5%. So we have very strong balance sheet currently. And the cash flow which was provided by the operating activities was EUR43 million.

So the same in numbers -- so orders received was in the first quarter EUR1.1 billion. And last year it was EUR500 million. So of course this is very good order intake for whole Valmet. And in -- in recent history, I don't actually remember as good quarter. So it's very good quarter for us in order intake.

And because of that good order intake, our backlog grew from EUR1.4 billion to almost EUR2 billion. And of course now, it's -- in the longer run, it will give work to almost all of our units, and we will have a normal situation with this backlog in second half of the -- of this year. Of course now the situation is very much better compared to the end of the year in all the respects.

Net sales was still low EUR519 million, and like you will remember order intake last two quarters last year was quite low, and then of course resulted at the backlog for the quarter was so low, and then -- and the net sales was low as well. We generated EBITDA EUR4 million. And that EUR4 million is lower than you have been expecting, and it includes EUR10 million accrual, cost accrual for one major pulp project where we had negative development, and it's the same project we had negative development in the -- in the last quarter, in 2013.

So even if last time I said that reserve was everything that was needed, that was my best understanding then, and I made a mistake. And the best understanding currently is that that this EUR-10 million is still needed.

EBITA after restructuring was EUR-8 million, from net sales it's -1.5%. Our earnings per share was negative \$0.04, return of capital -2%. And like I said, cash flow from the operations was EUR43 million and gearing at the end of the period was -5%. So all in all good order intake. Now, good backlog, profitability needs to improve.

Here you'll see the trend in our orders development. So you'll see that the -- of course EUR1.1 billion is a lot of more than in many other quarters. So we are very, very happy with that. And the good thing is that the order intake came from several segments. So paper was stronger than last year, pulp was stronger and Energy was stronger. So it was not coming only from one -- from one big project which is important for us.

Services, a little bit disappointment, but almost at the level of the last year. Then when you look at the area perspective here, the Asia Pacific was of course high and that was because of this one big OKI project that we booked in Asia, in Indonesia, otherwise it was active area as well. And then what is positive is that Europe grew from last year a lot. And our order intake in Europe was EUR400 million, almost EUR440 million.

So somehow we see a lot of more activity also on capital side currently in Europe than we have seen for at least for a year like you see from [the past]. So Europe has been positive also in -- as a capital market to us. So, good development in Asia Pacific and Europe.

Then when you look our backlog, like I said, it's now one -- almost EUR2 billion, and it went up by EUR570 million compared to last year. And now, it starts to be at the healthy level. We are estimating that about 70% of the backlog is currently expected to realize as net sales in 2014.

And here I want to remind you that we have been saying all the time that Q1 is a challenging quarter for Valmet. And we have been saying that quarter two is a challenging quarter for Valmet, because of the low order intake in last year.

So the backlog starts to help us more in quarter three and quarter four. So -- and more towards the end of the year. So it takes -- in this big project business it takes sometimes six months before -- after the order, before it starts to hit your operation and sometimes even nine months.



So the order intake will help -- will not help as quickly as maybe somebody might assume. But quarter three and quarter four, we will have better utilization of our organization already. And we are saying that 20% of the order intake is -- or the backlog is for services and the rest is for capital.

Here's the trend of the quarters. So here you see that the net sales was a lot of lower than in previous quarters, EUR519 million. And even if it was so much lower, then we were able to make positive results. So this EUR4 million and 0.7% like I said, it's not satisfactory result and it's not good but that shows that our profitability improvement actions have been taken place so that our breakeven point has been lowered quite considerably. So now with EUR500 million net sales, we are still on positive side. And then of course, it's a positive sign that the profitability has improved compared to end of the last year.

Then, how we continue with the profitability in more couple details, first, about the profitability improvement. So, on the right side you will see the SG&A. So Sales, General and Administration expenses in the company, and they are now at the level of EUR100 million. And last year they were about 12 points higher in the first quarter, which shows that the actions, what we have been saying that we are reducing the costs in SG&A that will in line with the plans what we have been saying early.

Gross profit improved percentage wise even we have that one -- EUR10 million problem in that one project, so gross profit has been going up. And of course in the longer run and during the year, the thing is that we have to be very careful with SG&A and to make sure that the SG&As don't start to grow. And then the other one is that we have to continue to improve our gross profit by improving our procurement, improving our quality and of course now with the help of the better backlog, we will have better utilization for the organization as well.

So the target is of course to improve the gross profit and keep the SG&A as current level, and by that those actions then improve the profitability of Valmet also in the future.

Then if we go through the business lines -- so Services, order intake little bit lower than last year. I wouldn't say it is a disappointment because the decline came all from North American market. So it's only one market where we -- where we saw a little bit lower activity in the beginning of the year. Other areas, Europe, Asia, China, South America have been -- have been performing like earlier.

From business units, it was also the same that the other business units have been performing at the same level. But then we saw some declining in especially North American Mill Improvements. Last year, we had two -- one big MMO, Mill Maintenance Outsourcing case which we booked in the beginning of the year, and that has an impact on that. But -- so that's mainly causing the difference currently. But decline in North America, Mill Improvement otherwise very stable development in our services.

Net sales declined, it was because of the last year's low order intake in Q4 and Q3. And the quarter one was little bit lower than we were expecting. But all in all we would say that the Services business line continues to develop as we have been saying. It's stable roughly about EUR1 billion business. And currently we don't see any change in the market itself.

So we see that the long-term -- or mid-term activity is the same as what we have been saying that it's on satisfactory level. And mill operating rates by our customers have been reasonably good. And we have opportunities to keep services at the -- at the same level where it has been earlier. So we have been saying that satisfactory market and our activities are like they have been earlier.

Then pulp and energy, strong orders received, EUR622 million. And that's of course a record, partly it's coming from one order EUR340 million from this OKI. But it's almost EUR280 million, other capital projects booked as well.

So we have been successful in many energy project and also in pulp mill projects. So the activity and order intake in Pulp and Energy has been of course very good in the first quarter. And what is important here is that we have been successful in many segments of the business lines. So it's not coming only from one product line. So it's good for our workload.

Net sales was low, EUR181 million. And of course from this picture you see that last year order intake was so low that it was expected that net sales in the beginning of the year is on the lowest side.



Then Paper business line also positive thing. So orders received EUR212 million. Last year the total year was -- if I remember correctly EUR460 million, EUR470 million. And now we got in the first quarter EUR212 million. So of course it's good improvement.

We received orders in North America, Europe, Asia Pacific. Activity in Board and Paper was better than last year like we said when we increase the outlook for Paper and Board in beginning of this year. And that has resulted now to good or a lot -- a lot of better order intake than last year. And it's important also to say that the good level in order intake in Tissue continued from the last year as well. So I would -- I'm happy also with the Paper business line order intake development.

Then of course, sales declined compared to last year because of the low order intake in the end of last year. But all in all I think Paper business line shows also positive development currently. And it's developing as we have been saying in the last conference call.

Then customer activity, we are saying that it has increased compared to last year. So OKI has been mentioned couple times, but still a little bit more about the details. So we sell the -- with deal with the key technologies for one pulp mill project. So it's a technology delivery, it's not EPC delivery.

We deliver two pulp dryers, two power boilers, two gasifiers and lime kiln], and it's a very, very big project for us. And of course it's strengthening our -- as a leading supplier for this segment. And of course we are very proud of that order.

Then we announced the letter of intent for Klabin pulp mill project where the value is between, is typically between EUR150 million and EUR200 million for that size of orders. And it's two pulp drying lines. And this order is not included in the Q1 order intake. So it will be then later on but it's not included in Q1.

And then here you see the list of the other projects what we have been announcing. So we have -- we got prehydrolysis system in Netherlands, multi-fuel boiler in Finland, recovery boiler and power boiler upgrade in Sweden, Bulgaria, paper machine rebuild in Austria, steam generator in Sweden, bleach plant rebuilt in Portugal, wood-chip heating plant in Finland, container board line in Vietnam, tissue production line in Mexico, cooking plant in Sweden, waste to energy boiler in Sweden and then after the quarter we have announced also the -- one tissue production line in Turkey. So activity has been actually -- it has been good or our success has been good in order intake now in capital side in quarter one.

So after this I will let Markku to go more in details with the financial development.

Markku Honkasalo - Valmet Corporation - CFO

Okay. Thank you, Pasi, and good afternoon on my behalf as well. My name Markku Honkasalo, and I'm the CFO of Valmet. Just as a reminder, year 2014 figures, they are actual and all comparison figures, they are carve-out figures. So please remember this one.

We are in good start for the year in terms of the cash flow generation. So cash flow before investment was EUR43 million positive. Our gross CapEx was EUR11 million and net CapEx was EUR8 million. Our depreciation was EUR13 million. So our CapEx is less than the depreciation.

Net working capital at the end of the year was minus EUR193 million. And at the end of the first quarter, it was minus EUR257 million, but it is 10% of the rolling 12 months net sales.

At the end of the Q1, we had EUR39 million more cash and cash equivalents, than we had net interest bearing debt. So our gearing was minus 5%. Our equity ratio was 40% and the group equity declined quarter-on-quarter EUR40 million. And biggest impact gain from the dividend decision EUR22 million, EUR9 million was relating to the hedge accounting, EUR4 million translation course and then EUR6 million came from the negative net profit.

Then our loan portfolio -- so basically no change since the year end. So our main financing sources are coming from the two term loans. It's both maturing in 2016. And then we had EUR33 million of short-term loans. And then we have two back up facilities. EUR200 million, domestic commercial paper program, out of which we drawn some EUR9 million at the end of the Q1. And then we have EUR200 million syndicated revolving credit facility which was totally undrawn.



So the average maturity of our long-term loan portfolio at the end of the Q1 was 2.8 years. And the average interest rate was 2.9%.

Then I will give to Pasi.

Pasi Laine - Valmet Corporation - CEO

So our guidance and short-term outlook. So we have kept our guidance for Valmet. So Valmet estimates that net sales in 2014 will decline from 2013 level, and EBITA before non-recurring items will increase in comparison with 2013. So it's the exactly the same guidance than earlier.

Then short-term outlook by which we try to say to you how we see the coming six months. And we see that services continues to be satisfactory like it has been up to now. In pulp, we see satisfactory development as well. In energy, we keep the satisfactory rating which we improved last quarter. In board and paper, we keep the satisfactory rating and the same story we improved it last time. And in tissue, we see that the demand continues to be in satisfactory also in coming six months. So we are keeping the guidance, we are keeping the short-term outlook at the same level where they were in the beginning of the year.

So as a summary, of course order -- success was that we got so much orders in the -- in the first quarter. And that is of course the big news for us. Stable development in Services, and we see that the market continues to be like it has been. So we don't see there any big variations.

Now, we have good order backlog. Now it's time to start the work with that backlog. And then of course the profitability was not at the level where we expect it to be. So the profitability improvement continues to be top of the agenda of the management. And of course we are -- we are pleased that our balance sheet is so strong. And we generated positive cash flow as well.

Hanna-Maria Heikkinen - Valmet Corporation - IR

Thank you, Pasi and Markku. If you could kindly come here, now it's time for questions.

QUESTIONS AND ANSWERS

Sampsa Karhunen - DnB Markets - Analyst

Yes, good afternoon. It's Sampsa from DnB Markets. Just two questions I'll start with. Pasi, you stated quite clearly that the Q2 is kind of a problematic quarter for the company in the sense that the orders last year lack and then Q2 is weak. Are we seeing Q2 being the kind of trough quarter in the sense that it is going to be weaker than the Q1 both on sales and the profitability? Is that what you are indicating?

Pasi Laine - Valmet Corporation - CEO

No, I'm -- no, actually not -- that's not what I'm saying. And we of course not telling our guidance for Q2. But what I want to make sure that now when you see that our order intake has increased, that your expectations for the net sales recognition is not too high that you all think that in our type of business it takes some months before the revenue recognition starts. So that's what I want to make sure that all of us are on the same page.

Sampsa Karhunen - DnB Markets - Analyst

Very good. That answers the question pretty well. Secondly on the services business, you were mentioning that there has been a decline in the North America. I take it as a kind of indication of the kind of maybe declining production rates in the North America as well or am I misunderstanding it? And just to continue on the same subject, basically when you have recently or basically sold new equipment and new installations over the past years, and it typically as I understand takes a couple of years before you start to see related service sells going into the direction. What year '15, '16



should we see increase in the services based on this quite recently installed base or is this newly or recently installed base only replacing the service sales and the volumes that are disappearing in other markets?

Pasi Laine - Valmet Corporation - CEO

[So] first the operating rates. So to my knowledge the operating rates in US have been -- have been reasonably good, and I probably [starting with that and okay] I'm not saying it. But North America our customers are doing well. They has some difficulties with weather conditions in North America, and that took their attention somewhere else. And we see that the market continues to be good and the market activity continues to be good. But there were some seasonally challenges for our customers in North America.

And then the other one was that last year we had exceptionally good order intake in North America in the first quarter, which then now is maybe more in the -- more in the normal level without any big startings of mill maintenance outsourcing cases. So I'm not worried about North America.

Sampsa Karhunen - DnB Markets - Analyst

So it's not basically you're saying that it's not kind of related to a structural decline --

Pasi Laine - Valmet Corporation - CEO

No, no, no.

Sampsa Karhunen - DnB Markets - Analyst

And the second question is what is the --

Pasi Laine - Valmet Corporation - CEO

Yes, installed base. I think our history has been all the time that our capital business has been cyclical. So -- and with that 50 years cyclical business we have created the installed base which we are serving. So I don't see that this peak in order intake would be seen in two years in service order intake.

So it's more that we are serving 2,500 customers already now. And then if in some years, some will of course disappear because the installed base is decreasing. And then we will have new installed base. So I don't see that there's a big change in the order intake because of these new orders what we have currently.

Sampsa Karhunen - DnB Markets - Analyst

Yes. And I'm talking also about the kind of some plants that have been installed over the past couple of years. So do you basically -- I'll restate my question, are you seeing that the service business is not going to grow that much that it's going to be around EUR1 billion that you've been referring to quite many times?

Pasi Laine - Valmet Corporation - CEO

Our target has been to grow services, the history has been that the growth rate has been about 4% -- and now, Hanna-Maria has to help me, about 4%. And then we have been saying that to continue to grow the service, we have to improve our market share. So don't expect too much, but we of course continue to work on our offerings so that we continue organically to grow our services in the future as well.



Sampsa Karhunen - *DnB Markets - Analyst*

Very good. Thank you so much.

Elina Riutta - *Evli Bank - Analyst*

Hello. Elina Riutta, from Evli Bank, two questions please. First on the EUR10 million costs overrun the pulp project. Can you comment a bit on what's causing that and is it over and done with [is the lead on]? And then related to that still, is it the kind of issue that could crop up in other pulp projects as well?

Pasi Laine - *Valmet Corporation - CEO*

Yes. First of all, the main reason is to say that like I have been somewhere saying that we under estimated the challenges to build that mill in that location, and that continues to be so. The EUR10 million is now the best understanding what we have. So that's the best understanding what we currently have.

You can't draw any conclusions from that project to the other ones. So our track record in Latin America and in pulp mills is actually has been such that normally we have been able to improve our margin. And in this one it goes to the other way.

We have some other EPC projects in Latin America. But like I said, track record has been that we have been able to keep our [as sold] margins, and this is an exception. Then like I said, this big order in -- for example in OKI, is not an EPC contract, so its equipment and services. And then of course the risk profile is different as well.

Elina Riutta - *Evli Bank - Analyst*

Thank you. And then the other question on the cost savings. You say in the report that in the first quarter, SG&A expenses were down by EUR12 million. How much of the total EUR100 million savings did you get in the first quarter or how much are you expecting to get in absolute terms in 2014?

Pasi Laine - *Valmet Corporation - CEO*

No, we keep what we have been saying that the full impact is seen by end of the year. And then we have been saying that a little bit about one-third is coming in SG&A. And we keep the statement still. So of course if you multiply now, that 12 with 4, then it's more than one-third, but -- so we keep the statement what we have been saying that by end of the year, you will see the full impact then.

Elina Riutta - *Evli Bank - Analyst*

Is that then the run rate that the run rate would be EUR100 million at the end of this year?

Pasi Laine - *Valmet Corporation - CEO*

Yes, by end of the -- by end of this year, we have -- we have EUR100 million cost savings on yearly basis, yes.



Elina Riutta - *Evli Bank - Analyst*

Okay. Thank you.

Antti Viljakainen - *Inderes - Analyst*

Hello, everybody. Antti Viljakainen from Inderes. I would like to ask about pricing. How do you see pricing environment in project business right now?

Pasi Laine - *Valmet Corporation - CEO*

That's a good question. So of course, pricing has been -- our pricing has been tough. So the competition continues to be tough. Now, when we have better backlog now in the future might be that we can be more selective. But the price continues to be an issue all the time in the sales projects. And our competition is also active. So we haven't seen any dramatic change on the competition behavior in last half a year.

Antti Viljakainen - *Inderes - Analyst*

Do you see differences between segments?

Pasi Laine - *Valmet Corporation - CEO*

No.

Antti Viljakainen - *Inderes - Analyst*

Okay. Thank you.

Hanna-Maria Heikkinen - *Valmet Corporation - IR*

Do we have further questions from Keilasatama? If not, then we will start with the questions from the lines.

Pasi Laine - *Valmet Corporation - CEO*

(Inaudible).

Operator: And your first question comes from Antti Suttelin from Danske Bank. Please ask your question.

Antti Suttelin - *Danske Bank - Analyst*

Thank you very much. I will have two items that I'd like to talk about. First of all, the sustainability of the -- of orders, if we look at Valmet and Metso Paper historically we know that the demand is very cyclical, especially on the pulp side. The upside goes then to last a couple of years, and then orders have may fall quite notably. How do you see this? How long will this strong demand face last in pulp and also paper this time? Thank you.



Pasi Laine - Valmet Corporation - CEO

So we are now giving the guidance for coming six months. And we keep the guidance at the same level where it has been -- has been so satisfactory. I think of course quarter one was very good. So you cannot estimate that we will have quite many that kind of quarters in a row.

So we think that now the order intake has been good, we say that the market activity is still satisfactory in pulp. It's in Energy and Board and Tissue satisfactory, Services as well. And then of course in our management system we have to be prepared for the cyclicity.

So we have to be prepared all the time to the situation that there will be two quarters when the order intake is low. And that's why we have to make -- we have been reducing the capacity cost with this EUR100 million cost. And we have to make sure that we are not increasing our capacity cost now when the -- when the market has improved.

So one of the -- one of focus is of course to get the orders, then the second focus is to make sure that our capacity cost is not increasing, so that even if the market would turn down like it in cyclical industry it will, that we are not suffering the profitability in that case. But the clear guidance to you, Antti, to say that how long pulp activity continues, I cannot say except that you might have noticed that there are customers who are talking about investments and may be even more all the time.

Antti Suttelin - Danske Bank - Analyst

Yes.

Pasi Laine - Valmet Corporation - CEO

And in board side, paper board side, we increased market activity to satisfactory level. And we still keep it at the satisfactory level which means that we see that there is -- there is -- there are activities on the customer side.

Antti Suttelin - Danske Bank - Analyst

Okay. But basically my question was that [is if] there any reason to believe that the cyclicity would have -- would have gone away or is this more of the same that this continues to be a very cyclical industry, there are up times and then there are down going cycles?

Pasi Laine - Valmet Corporation - CEO

It continues to be cyclical, and that's what we all have to remember. So it's a cyclical industry in capital business.

Antti Suttelin - Danske Bank - Analyst

Okay. Thank you. And then my second question is relating to your efforts to improve the gross margin. Now, my concern is that even if you do good work on gross margin side, what is the impact when these pulp orders that you have now taken in, when they start to be coming through the P&L, how will that improved gross margins?

Pasi Laine - Valmet Corporation - CEO

No. So we haven't of course told the gross margin levels in capital business and services separately. But I think it's obvious for all of us that the gross margin level in services is higher and capital is lower. And then when the share of the -- of the -- share of the capital business is increasing, then it can dilute gross margin percentage. But of course we are fighting against that, and our intention is of course to work towards the 6% to 9% goal what we have said. And not depending on what is the -- what is the cycle in the capital business.

And we have a lot of actions ongoing. So I've been saying this, quality and procurement. But of course we have a lot of other things to improve our internal efficiency to make sure that the -- to make sure that the gross margin is improving. And then one thing what affects is that once you have -- once you have workload, then of course your under absorption rate will start to decrease which has an impact to gross profit as well. So there are many leverages from the workload which can affect positively the gross margin.

Antti Suttelin - Danske Bank - Analyst

Okay. But my concern is to put this frankly, I'm afraid that the pulp gross margin is kind of an alarmingly low. Is this -- is this a wrong assumption?

Pasi Laine - Valmet Corporation - CEO

I'm not commenting on that. So I said that the price fight continues to be there. And we do our best to get the deals with as high price as possible. And once we have got the deals, then we continue to work hard on procurement quality and many things to improve us from that as sold margin. But specifically I'm not saying that is it alarming or is it not alarming.

Antti Suttelin - Danske Bank - Analyst

Okay. Thank you very much.

Operator: Your next question comes from the line of Alexander Virgo, from Berenberg. Please ask your question.

Alexander Virgo - Berenberg - Analyst

Yes. Good afternoon gentlemen. So a couple of questions please. The first one just on services and I want to -- kind of go through the outlook there and what you've actually seen in Q1, because obviously you said that at the Capital Markets Day that you were targeting on average growth in emerging markets, and services is 5% per annum, but down at eight or so in Q1 on the revenue side probably indicates a little bit, less than [five up].

So can you talk to us a little bit about how that's developing? Where you're seeing the growth come from and where not? And a little bit more color than you've provided so far?

Pasi Laine - Valmet Corporation - CEO

Yes. Now, I'm not sure where from you took the numbers. But services growth of course we are setting higher expectation for services growth in growing markets -- growth markets. And I think it's of course because of the capacity has been installed there and it's aging and it gives us services opportunities. I don't remember that we have said specifically the growth target to service.

Markku Honkasalo - Valmet Corporation - CFO

No, I think -- sorry, sorry, can I -- can I just to -- yes, just to clarify that Alex, actually you are referring to the fact that what we have said is that on average the services market is growing some 5% in emerging market countries. And the total market which is roughly EUR 7 billion. The -- annual growth is about 2%. So I think that Alex is referring to that one.

Pasi Laine - Valmet Corporation - CEO

Yes. Yes.



Alexander Virgo - *Berenberg - Analyst*

Right. Which given you were expecting to at least hold your market share if not grow market share, then you should be growing at 5% or more in emerging markets, right? I mean, I guess -- I guess the -- that the bit is quite difficult to reconcile is you've got services orders down 5% in Q1 and you've got services sales down at 8% in Q1 and also appreciate you don't want to disclose the divisional profitability, we know that services is the driver of EBIT.

So I'm just sort of trying to understand why you think that that satisfactory in that context?

Pasi Laine - *Valmet Corporation - CEO*

So like I said, the decline is coming from North America, and the other ones haven't been declining. So -- and then like I said, order intake was affected by these -- by one big order in North America, and then maybe some challenges what the customers had in North America. And we don't see that in North America, the market would have change in any way.

So our expectations for the future have been stayed at the same level where they have been earlier. Then in Europe, we see actually positive development like we see in capital business. But we see also that European production rates have been improving, the activity level in Europe has increased, some small signs of improvement also in growth markets.

So we are -- we see that the market environment in services hasn't deteriorated. So we can continue to work with the same market. At the same time we also have to remember that we took -- we took some capacity away also from services.

So we have of course more flexibility in services organization as well compared to last year, which helps us of course with the profitability if there's a situation that volume is dropping a little bit. I think we announced that we took about 200 heads.

Markku Honkasalo - *Valmet Corporation - CFO*

Yes, 200, yes.

Pasi Laine - *Valmet Corporation - CEO*

200 heads away from services organization as well.

Alexander Virgo - *Berenberg - Analyst*

Right, okay. So the profile that you saw last year the service business strengthening in Q2, Q3 and Q4 from the level of Q1, you'd anticipate that happening again this year?

Pasi Laine - *Valmet Corporation - CEO*

We -- of course we are not giving that direct guidance. We are saying that the market is satisfactory and it continues to be satisfactory.

Markku Honkasalo - *Valmet Corporation - CFO*

Yes. Can I comment that one? Actually it's -- typically it's 55% of the orders will be received during the first half of the year. And then 55% of the net sales will be recorded at the second half of the year in our services business.



Pasi Laine - Valmet Corporation - CEO

[I know] but that's what he's now challenging that if that phenomenon is this year through as well, then order intake in services will go down. But I don't -- I don't see that that phenomenon is as mathematical as it has been last two years.

Alexander Virgo - Berenberg - Analyst

Right, okay. And then the last question just on this accrual. Again, I mean, given Suzano is up and running, what is it that's driving this 10? Is it -- is it penalty -- payment penalties for not being on time or I'm just trying to understand what that 10 is for?

Pasi Laine - Valmet Corporation - CEO

It's -- so big project that -- there are several reasons for the over run. So some are related to our activities, some are related to customer activities, some are related to sub-suppliers and even tax authorities. So I'm not going to -- more in details but like I said, the challenge has been to build up so complex plant in that location, and we underestimated the challenge. And that's the root cause in that -- in that project.

Alexander Virgo - Berenberg - Analyst

All right, okay. Thank you.

Operator: Your next question comes from the line of Jake Thomas from Odey. Please ask your question.

Jake Thomas - Odey - Analyst

Hi there, good morning. I just had a couple of questions. Firstly really regarding the operating leverage for the new business and what you've been doing to your breakeven rate. As I try and understand how the increased in your capital orders translate into profits latter of the year? That's the first question.

The second [or we -- or we get] second question.

Pasi Laine - Valmet Corporation - CEO

No. I -- Markku, can you help me?

Markku Honkasalo - Valmet Corporation - CFO

Okay. I will try to -- I didn't fully understand the question. But as Pasi said in his presentation that it takes a while before these new orders will turn into the net sales. So typically it's three to six month lag. So the -- your assumption is correct that second half of the year from the capacity utilization point of view will be -- will be easier in our business.

Jake Thomas - Odey - Analyst

And what is your utilization at the moment?



Markku Honkasalo - Valmet Corporation - CFO

We are not giving any specific details. But we have utilized this possibility here in Finland to temporary lay off people. So we have a certain flexibility within our organization.

Jake Thomas - Odey - Analyst

Okay, all right. So given the 12% reduction in headcount [ratio] that probably equates to 12% reduction in capacity, fair enough. And then in terms of your breakeven point, in terms of your reduction in the breakeven point, where was it and where is it now given that reduction in headcount?

Pasi Laine - Valmet Corporation - CEO

I think -- of course we are not saying exactly the breakeven point. But you can of course assume quite correctly if we make EUR519 million net sales and we made EUR4 million profits. So it's not too far away from breakeven with the current service and capital sales distribution.

Jake Thomas - Odey - Analyst

Right, yes, okay. So how should I understand the operating leverage and the incremental margin if you're at roughly breakeven now, and you expect to kick off in the second half of the year.

Pasi Laine - Valmet Corporation - CEO

So like somebody was asking here, of course we have different margin level in capital business and services level. And we are not speaking that --

Jake Thomas - Odey - Analyst

I'm asking for just the degree [there].

Pasi Laine - Valmet Corporation - CEO

--speaking that -- telling that publicly. And of course -- of course we -- if the services sales is growing more, then of course you get more gross margin. And then the capital side there you have to have bigger volume increased to gain the same Euros in the -- in the profit -- in the bottom line. But exactly we are not telling the numbers.

Jake Thomas - Odey - Analyst

There was a comment you made in your earlier release that with the increase in orders you expect your divisions to reach more normalized state of operations. Should I consider normal to be the long run average?

Pasi Laine - Valmet Corporation - CEO

What I meant is that if you look what has happened in Valmet last two years, so we have had several very big layoffs in our organization. So we have reduced the total personnel I think close to 2,000 people in 18 months or two years. It's of course has caused a lot of insecurity to our personnel and organization. Last year we reduced headcount by 1,400 heads.



We restructured, we start -- we made the de-merger, we build up new head-office, new organization structure, many other things. And now we are in that kind of situation that we start to have work. And then on top of that, we continue to have some temporary layoffs like Markku just said. And now we start to be in the situation that we have almost enough work or enough work in any parts of the organization. And people can work five days a week, and they can have a normal working life.

So I think -- I think from that perspective, we are in the normal situation that people can feel more safe and secure, and they can focus on their job and we don't have to focus on temporary layoffs and that kind of things. I'm sure that that will bring a lot of more effectivity and efficiency in our organization in the latter part of the year.

Jake Thomas - Odey - Analyst

Okay. Thank you. And then just lastly for me, I mean, regarding your comments on competition and the pricing environment, given that you and your competition, all reducing cost is in this environment that you expecting to share the benefits of their cost reductions with your customers, if your competitors are also doing that?

Pasi Laine - Valmet Corporation - CEO

So, of course, we try to keep up big part of the cost reduction as our benefit. And there's -- the market -- the market fight of the market competition, of course, where our competition is reducing cost as well. And then, what is important for us is that we try to develop all the time new technologies by which we could differentiate and earn a little bit more money by that way, as well.

So, the tactic to improve the profit has to be to introduce new technologies to the market, and then at the same time to have as effective organization as possible for execution. And that's what we are developing and we are working. And I think that we are on good part [that] to be more competitive than our friends.

Jake Thomas - Odey - Analyst

Okay, brilliant. Thanks so much for your time.

Operator

Your next question comes from the line of Jan Kaijala from Nordea. Please ask your question.

Jan Kaijala - Nordea - Analyst

Hi, this is Jan Kaijala. Just a couple of questions please, on this topic, we already discussed this capacity utilization within your group after you've had such a good run of strong orders. I would like to ask, what's the situation now? You said, that everybody should be busy by the end of the year. And if you look at different pockets within the company on the paper side, I'm thinking more of would you still strongly need orders here and there or would you still have pockets of with too low operating rates even after these orders?

Pasi Laine - Valmet Corporation - CEO

In our type of company where we have many technologies then, of course, we have in some way a pocket where the utilization is not totally full but we have. And by the end of the year we have few of them anymore. And then what we have been doing during the consolidation, is that we -- or during the restructuring that we have reduced active locations, consolidate the manufacturing to fewer the locations. And we are using those



locations for bigger variety of production, which means then of course that the load from several businesses is actually giving work for the same production unit.

So, we have been doing a lot of work to centralize our operations and that will give benefit during the years. So, all in all I think that capacity utilization by end of the year is -- could be actually to the other direction that in many units we have too much work.

Jan Kaijala - *Nordea - Analyst*

Okay. Then I have a second question on this very strong order growth in the pulp and energy of EUR620 million, and you state this EUR340 million is the one big pulp then you have some EUR280 million other. I mean, of that remaining EUR280 million I would be curious to know -- I mean, if there is one other single big order? And secondly also and that how would that go divided between power and pulp that remainder, that EUR280 million?

Pasi Laine - *Valmet Corporation - CEO*

And from this 340 part is power as well. So, there are two power boilers and two classifier. So, part of -- part of the OKI project includes power projects as well. We are not telling exactly that how much is pulp and how much is power because especially in that organization, we can utilize the same personnel to make pulp recovery boilers and to make power generation boilers. So, from the capacity and engineering point of view it's actually the same units. So, these orders keep good work for them.

Then, we have announced the values for the contracts for part of the -- part of the deals that we have announced. And part of them we haven't announced. But here is the list of the recent sales activities where from you can of course see that we have been very successful in energy sites. So, multi-fuel boiler in Finland, boiler upgrade in Bulgaria, boiler in Sweden, heat plant in Finland, energy boiler and waste to energy boiler in Sweden. So, a lot of boiler activities.

Jan Kaijala - *Nordea - Analyst*

Okay. Thank you. Just one more question on this pulp mill project and the cost overrun. And do we or can we expect any timelines in the future after which we can completely relax about this and not expect anything from there or not be at the risk of receiving anything more? Will there be some points when the project is completely accepted by the (inaudible) warranty period, so whatever discussions may be going on currently? When are we out of the risk area completely?

Pasi Laine - *Valmet Corporation - CEO*

We are saying that these EUR10 million is now the best of our understanding and that's the best understanding what we have. Typically the warranty period for our -- in our type of industry is 18 months, 24 months. And then typically you have some warranty costs and of course in our type of company we make warranty reserves in our projects as well. So, I think -- but I'm not going to this pulp mill project more in details.

Jan Kaijala - *Nordea - Analyst*

Okay. Thank you. That's all for me.

Operator

Your next question comes from the line of Johan Eliason from Kepler. Please ask your question.



Johan Eliason - *Kepler Cheuvreux - Analyst*

Yes, hi. This is Johan at Kepler Cheuvreux, just coming back to these Jan's questions on the order intake. Obviously, it was very strong above mine and the market expectations. And I was just curious is this sort of any big order that you haven't announced during the quarter that's part of that order intake or is it just so that maybe we are underestimating the value of these orders that you have announced but not given the real value for?

Pasi Laine - *Valmet Corporation - CEO*

That's a -- I think we have tried to announce everything what we should announce according our policy. So, maybe the question is that or the answer is that because not all the customers accept that we tell the cost -- the order value, then it's little bit difficult for you to estimate that what is the value of the order. And we are sorry that we can't always announce order value. And then the other thing is that we get of course that kind of smaller orders, let's say, under EUR10 million, which we are not announcing or I don't remember exactly the figure.

Anu Salonsaari-Posti - *Valmet Corporation - SVP, Marketing and Communications*

Under EUR6 million.

Pasi Laine - *Valmet Corporation - CEO*

Under EUR6 million, we are not announcing them at all. And then, for you, it's very difficult to know that if we have been getting those orders. But if we start to make announcement of those ones as well, then you get even more confused because you get even more announcement without order value.

Johan Eliason - *Kepler Cheuvreux - Analyst*

Yes. No, that's true. So, I mean part of the equation question could be that you have a lot of smaller orders than that we obviously don't see. But -- so for these announced orders, there's not been a shift towards larger sizes because your supply full scope solutions et cetera, something that could sort of impact the value when we estimate it using a historic numbers we have seen.

Pasi Laine - *Valmet Corporation - CEO*

No, no, there's not that kind of change. And then I would actually even claim that an average boiler order is now smaller than it is used to be some four years ago, five years ago.

Johan Eliason - *Kepler Cheuvreux - Analyst*

Oh, okay. Now, that's my questions. Thank you very much.

Hanna-Maria Heikkinen - *Valmet Corporation - IR*

Do we have more questions from Keilasatama?

Operator

So there are no further telephone questions at this time. So, please continue.



Hanna-Maria Heikkinen - Valmet Corporation - IR

Okay. Thank you everybody. Thank you for the activity and good questions. Our Q2 result will be published on July 31. It's in the middle of the hottest season even here in Finland, but we have here nice harbor. So you can maybe take a boat and come here. So hopefully we will meet then.

Pasi Laine - Valmet Corporation - CEO

Okay.

Hanna-Maria Heikkinen - Valmet Corporation - IR

Thank you.

Markku Honkasalo - Valmet Corporation - CFO

Thank you.

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