Thule Group

Thule Group Interim Report Q2/2018

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Interim Report Q2/2018

Magnus Welander

Chief Executive Officer, Thule Group

2018/Q2 – Strong Performance in Europe

Good morning everybody, and welcome to the second quarter report for the Thule Group in 2018. I am happy to say another strong quarterly report to report on. If we go to the first page we can see that if we take it from the top line our net sales grew to SEK 2.155bn which is then about 10% growth. If we look in a constant currency it is a growth of 7%. The growth was driven by Region Europe & Rest of World. I will get back to a little bit more commentary to what has been going on there and why we are doing so well there. While we saw a small decline in Region Americas, I am also going to comment on that later on specifically.

If you look at our EBIT performance, we had a strong EBIT margin in the quarter with 24.3% despite spending significant funds on our product development in the quarter as we enter the busiest period we have ever had in terms of preparing and launching new products. A strong, solid EBIT performance and a strong net income follows that of course.

I am also very happy to announce, as has been announced with press releases, that we do have a long-term financing in place with a more flexible setup and a more cost-efficient setup than the old agreement with its five year contract with the banks. We feel very good with that.

2018/Q2 and YTD – Net Sales and Underlying EBIT Development

If we look at the growth numbers by quarter, a 7% organic constant currency sales growth means that we year-to-date are at 6.4% in constant currency topline growth. We had a stable high margin in the quarter, which means that over a rolling 12-month basis we are now at 18.8%. For the first six months we are at 22.1%, which is then 700bps better than the 21.4% we had in previous first half of the year in 2017. Overall a strong financial performance.

Region Americas – US Market Still Challenging

Looking then at the regions and going to the next page looking at Region Americas, you can see that we still have a challenging situation in the biggest market in that region, being the US. The US is the dominant market, followed of course by a big market like Canada, Brazil and the rest of Latin America. If we look at sales for the quarter the sales were in decline at 4% or 4.2% to be exact. The decline was caused also this quarter by the known OE contracts that we are phasing ourselves out of. We have spoken about these many times but they are worth repeating that we have a number of contracts with car manufacturers for some pickup truck accessories. We do also have two major OE programmes for bags and cases as a supplier to OE. These contracts are all lower-margin contracts that we are continually phasing out. They will continue to also affect us in the coming four quarters.

What we were not 100% happy with, we were hoping we would see a bigger growth in the rest of the business because the decline in this OE business was something we had forecast. We had an okay quarter in the rest of our business but we did not grow as much as we had hoped. The main reason being that the US market's bricks and mortar retail sector is still under challenge. We have seen a number of store closures and a continued wavering confidence level, I would say, in how the markets have performed. We do believe that there is a market in terms of consumer desire although not as strong as in Europe. However, the retail sector is still balancing itself out and that affected the second quarter as well.

We see nice growth in luggage and our backpacks for everyday use, which is of course very key because we still see and will continue to see a decline, especially in the US in what we call the legacy products. The US market has been the market where we historically sold the most of tablet folios, CD wallets and other smaller cases under the Case Logic brand. These categories are continuing to decline rapidly and therefore the growth in more high-margin, future-focused categories like luggage and backpacks is very important. It is nice to see that we are now growing in those nicely in the US and in Region Americas.

In the Region, we have a very small sales of RV products and this is, as we have communicated in the past, due to the fact that in the US market there is a relatively small interest in higher quality, higher priced products. There are however some niche categories, more in the smaller van segment and we are very happy that in those small, niche categories we have had a very strong growth in the quarter. Still a very tiny product category for the region but growing nicely with the right type of products.

Within Active with Kids we are also performing well, stable and growing, as we should expect. That is also positive. In the region the two other major markets, Brazil and Canada, are continuing to be strong. The challenges we face are the US retail, the combination with the OE phasing out and the relatively larger amount of old, legacy products that we still do have in the US. However, we believe that we will see a better performance going forward in the coming period from Region Americas.

Region Europe & ROW – Very Strong Q2 with Growth Across the Region

If we then turn to the strong-performing Region Europe & Rest of World on the next page, I am very happy to say that the trend, which has been very strong for a long period, continues and we grew with 11.7% in constant currency, which is of course very strong. One of the reasons was already hinted at in our quarter one pool where the late spring in Europe also affected, like it did in the US, some of the selling-in of bike carriers and also our bike trailers for kids, like the one in the image. When the spring is late these type of products normally will be sold during the spring anyway but they might be sold a few weeks later and thereby falling rather into the beginning of the second quarter rather than the end of the first quarter. That is something that we saw so we saw a strong effect of picking up these sales in the second quarter and doing very well in both those two categories.

On top of that we continued to grow very strongly in our roof box category with the Thule Motion XT product line, which was launched in 2017 that has been multiple design award and test award winner and has continued to take market share in the market. As I already mentioned the bike trailer, I can also mention that within Active with Kids we have had a very strong growth momentum with our updated Thule Urban Glide stroller. This all-terrain stroller is really targeted to the active parent. You can jog with it but you can also use it as a very practical normal stroller walking around in the city. We did an upgrade in terms of design and tweaked it a bit ahead of the 2018 season and that has meant a very positive momentum of sales for this in Region Europe. That is of course a very positive signal as we will be now in the coming weeks launching more strollers that we already have a strong momentum.

Within the RV product category that is significantly bigger in this region, the market continues to be strong. We estimate the market growth rise to be just below or around 10%. This is of course a combination of actual registrations going on in the marketplace but it is also how much manufacturers are manufacturing new things and how much of these new vans and motorhomes are being bought to be put on the lots at the dealerships. A combination of actual registrations, which were slightly lower in the quarter, but we still believe the market grew around 10%. I am also very happy to confirm that we continue to outgrow the market by taking market share, so a very strong RV product also in the second quarter.

If you have been watching and looking into other companies in the category, I think you have seen something of the belief that that might cool down slightly in the second half of the year and we do share that opinion. We believe that the market will continue to grow but maybe not at the double-digit pace anymore, but more a mid-single-digit level of growth for the market.

Within packs, bags and luggage we have had a solid start to the year. We still also, to a lesser extent than in Region Americas, have a declining legacy product but we are growing in our growth categories of luggage, smaller backpacks for everyday use and sports bags like technical backpacks. Especially the successful launch of our first-ever hydration backpack, the Thule Vital, with the very innovative and patented hose system for the drinking, has been a huge hit and has meant that we have picked up big listings in that category. Overall, very happy with the performance in Region Europe & Rest of World.

With that I will leave it over to Lennart to discuss a bit about more the details in the income statement.

Q2/2018 Financials

Lennart Mauritzson

Chief Financial Officer, Thule Group

2018/Q2 – Reported Income Statement

If we look at slide six, income statement, gross margins were flat in the quarter with prior year, only 2.2%. However, including unfavourable currency effect of 0.3pp. The improvements then in the gross margin of 0.3pp were driven by a positive product and customer mix, combined with our normal price increases that we are doing, mainly within sport and cargo carriers, dispirited by continued headwind from commodity price development.

Looking at financial nets, as Magnus said, we were going into a new financing arrangement. In the quarter we had to post the one-time hit of the dissolved old financing cost of SEK 4m. Good to see that we could offset that by a positive FX effect on the revaluation of FX accounts involving cash in local entities, which means that we had minus SEK 30m in financial nets, versus the prior year of minus SEK 12m.

As noted, our selling expenses are higher than prior year, approximately SEK 25m. Those are driven by higher product development, as we had communicated, and we are now at this 6% LTM ratio sales. We also have a lot of marketing activities during this quarter due to the upcoming Q3 product launches. Finally, looking at taxes in the quarter we had an efficient effective tax rate of 24.5% versus prior year 24.7%.

2018/Q2 – Operating Working Capital and Operational Cash Flow

If we turn the page to slide seven we are looking at the operational working capital and operational cash flow. This quarter we ended with approximately SEK 1.5bn in operating working capital, which is 24.3% of last 12 months of sales versus 22.3% prior year. The increase in absolute number is SEK 157m but if we adjust it for currency the increase is SEK 95m whereof accounts receivables stand at almost SEK 22m, which is driven by the sales growth. Looking at net increase in inventory and accounts payables that is SEK 74m and the increase in inventory is because we have a slightly later ramp-down in high seasonal production this year. A little bit more importantly, as we are preparing for the Q3 key product launches.

That means that for the operational cash flow we saw, as expected, an up-sequence since the Q1, which always is a little lower, but slightly less than prior year in Q2, which is all related to the change in working capital I just mentioned.

Targets and Outlook

Magnus Welander

Chief Executive Officer, Thule Group

Preamble

I think it is key to note that of course it is a very fresh inventory we are holding. As Lennart mentioned, it is a lot of inventory related to the ending of the season coming slightly later this year, in the summer season, and some very exciting product launches that we are just about to do. We feel very good with having that inventory on hand.

2018/YTD – Performance vs. Financial Targets

If we go to the next page summarising our performance versus the financial targets, we are year-to-date growing with 6.4% versus our target of minimum 5% every year in constant currency excluding acquisitions. A good start to the year. In terms of our tracking towards our above 20% EBIT margin target we were for the first six months at 22.1% but more importantly looking at the last 12 months we are running at 18.8%, tracking well towards that target. We are at a net debt/EBITDA leverage of 1.7x and as announced previously, there was an approval at the AGM of an 87% dividend pay-out of the net income. Overall we feel very good about how we are tracking to the financial targets.

Focus Areas for Coming Months

If we go to slide nine and talk more about what is happening in the coming months, I often say this, that we have some of the most exciting periods and I can assure you that internally in the Thule Group we will have the most exciting months ever since I joined the company, in the coming months. The reason is simple. We are in a very busy normal season because this is still peak season. Busy times and good to see all the positives of the products we have already launched to the market. However, we are also doing a very big launch of the Thule Sleek city stroller which is shown in the image. Rolling it out to major retailers around the world during the quarter. This is of course very exciting. I have announced a number of times that we will not judge the performance of a stroller in how it does in the first quarter. That you can do after one full season and it is more so by the end of 2019. It is still very important to get the first steps right when you launch something. Getting it into all those key retailers in all those markets, getting the market reception, getting the media attention is of course something that we are very excited about.

We are also going to a number of key fairs in the coming few months where we will display the products which will be up for sale in 2019. Especially in our traditional sporting cargo carrier category, this will be by far the most exciting launch year ever with some very large, key announcements taking place in a few weeks' time. Exciting times also for the products to hit the market in 2019.

On top of that, we continue a very focused approach, of course making sure that we can deliver on time in full for a very strong season, especially looking at what we have seen in terms of growth numbers in Europe in being able to meet those type of growth numbers. We are in the new factory that we finalised at the very end of last year in Pila in Poland in a full production ramp-up for the Thule Sleek launch, which is of course a big undertaking and very exciting. We are also finalising a major investment and layout for production set-up change in our Swedish roof rack plant, which is also being finalised this quarter. We are well into the building works of an expansion of our Eastern European distribution centre with the growth we have seen in Eastern Europe over the last few years. We are now taking the step to expand that distribution centre actually one year earlier than anticipated, to be able to serve those markets and the expected continued growth.

We are of course, as any company at the moment, tracking and working very closely and staying on top of what is a still volatile raw material market. In that it is obvious that also some of the statements being made by the Presidency in the US in terms of what potential duties will be hitting on various products is something that we are tracking closely. It is to early to be able to say what the effect will be exactly but we are working very detailed on it to see what the final outcome will be truly decided in the US.

Then as we are spending, as Lennart commented on, around 6% of sales now on product development it means that we have more people than ever and more projects than ever underway. Some being finalised for launches as we speak, many being from products that will hit the market in 2019, and some for 2020 and 2021 even. Very exciting times for all those efforts, as well.

Q&A

Daniel Schmidt (Danske Bank): Good morning, Magnus and Lennart. I wanted to touch on two subjects, the Americas and then RV. You talked on the call today about that you were a bit surprised about not having stronger growth in the more regular areas that you expected. When you look back at what you said in connection with the Q1 report and the fact that many retailers went into Q2 with very low inventories. You were quite sure that they would need to restock and I also got the impression that the portfolio pruning that you are conducting would be slightly less visible in Q2 versus Q1. Still you are ending up with the same organic deterioration year-on-year. Could you shed some more light on what happened with the retailers? You sounded a bit more optimistic by the end of April. What gives you the confidence that you will perform better in the coming quarter or quarters?

Magnus Welander: I would not say surprised. I said disappointed. There is a subtlety in that word so I will go back to it. The disappointment is actually not in those retailers we mentioned, which did have low inventory and which we have grown with. The disappointment has come from the fact that some of the retailers that were less performing already in the previous period have been closing down stores and struggled more than we expected. We have a number of retail customers that we have grown nicely with, exactly due to the reasons we expected; that is, they had relatively low inventory, and we have a strong portfolio we have been growing with them. However, we have been hurt by a number of retailers, that especially focus a lot on bricks and mortar stores that have taken decisions and communicated late in during the year to close down further stores. As soon as that is being done there is all the limited stockholdings because we have physically large products in stores. It still means that there is a little bit of pipeline depletion when stores like that stop taking orders. That is the disappointment, not the actual general performance in those categories where we do our core business. There has been some of the legacy parts of the business and some of our more low-end categories where there have been store closures. That has affected us.

The second part was that we hoped and believed that we would see a better pick-up of the bike and paddle sport industries in the US than have been seen in the marketplace. Generally the paddle sport category, which is globally relatively small but in the US relatively bigger, has really had a very weak first half of the year. We were expecting that to pick up a bit more in terms of market. Overall, I would not say surprised. I would say disappointed. If you look at what the effect of the category of those OE, we do say all the time that it should have a certain effect. Sometimes they also do worse than expected so already knowing they were going decline, they sometimes decline even more. That was the case in the quarter. Although we do have some insight into the ordering of these large OE contracts they can also change their ordering pattern, and the fact was that the decline in that group was even bigger potentially than we had expected. That was also difficult. Not a huge disappointment in terms of EBIT because they are not contributing a lot on that and we know we were phasing them out. However, the effect was bigger in the quarter than expected. Those were the main reasons.

Due to that we still have a more positive view on the second half of the year in Region Americas or specifically the US than we have for the first-half. However, I do not think, as we already said in Q1, that it will go from a decline to a fantastic growth. We do expect this to grow and now the key challenge will be to prove that in practice, making sure that we do see the pick-ups of some of those key launches we are doing. Of course a launch of a new stroller, a category where we are adding a product into a four-wheel stroller will be pure additional growth so expectations are more positive. However I am also convinced that Europe will still have to be the engine in the second half of the year.

Daniel Schmidt: Have you seen any signs of any improvement? It has been a very short period into Q3 so far but is there anything you want to comment on with regards to the Americas trend?

Magnus Welander: It is too early to tell, actually.

Daniel Schmidt: The second subject which you touched upon yourself and RV is of course maybe a concern in general. It is not a big exposure for you guys but I think you said in your opening statement that you do expect a slowdown in the second half versus the first half. If I read you correctly when you say that the market growth has been 10% and registration data seems to be up by around 3% for the second quarter in some of the bigger markets, at least in Europe. Then you combined that with the manufacturing pace that you have seen in the quarter. Does that mean that there is some sort of inventory build-up in RV in Europe going into the second half? Is there any risk if growth slows but still grows that there will be some sort of inventory correction in the coming months? Have you seen that during the quarter?

Magnus Welander: First of all, the underlying market trends in terms of a consumer group with younger consumers than ever buying RV vehicles and buying smaller vehicles, more like vans, that is a positive, underlying market trend with motorhomes growing. The caravan market is not growing but the motorhomes market, especially the lower-price-point smaller vehicles, is growing. There is a positive underlying trend. What we saw and that you need to be careful a little bit with the registration data because the June data is not in. It is up to May and there can be fluctuations. We commented to some of those fluctuations which were a bit abnormal in Q1 in the beginning due to legislation on emissions. There can be similar things going on sometimes with seasonality things and package deals, also in a specific quarter. We therefore think that there is not a huge inventory build-up in Q2. There might be some inventory build-up which is why we are estimating that overall market could or probably would not grow with a double-digit in the second-half.

We of course discuss with a lot of manufacturers and a lot of players in the industry. and we have a general feeling, which is ours. Our interpretation is that it is more of a mid-single-digit type of growth in the second half of the year. It is still a nice growth so I do not see a huge challenge for the category. I am quite optimistic about RV category but sometimes you have to just be realistic that when you go from 12/13% growth, 6/7% sounds terrible all of a sudden. It is not. It is still a very nice growing market. Therefore, we do not foresee huge corrections. I think there will be specific dealerships and specific manufacturers that might have overstretched in their efforts to win market share this year but that is more a normal thing in the market. It is a market where players have to commit very early and there is always somebody making a mistake. If they do not make the mistake to leave money on the table by not ramping up, somebody will have to make the mistake of having done a little bit too much and ramped up too much. I think some natural correction but that is included in our assumption of a mid-single digit second half of the year.

David Schmidt: Does it entail in any way a higher volatility in your sales to this industry if we would see some corrections here and there when it comes to the inventory and the underlying demand, do you think?

Magnus Welander: No, we do not think so. If we look at it, we have a very broad customer platform so even if one dealership or one manufacturer of a specific brand struggles a little bit thanks to our very strong position in the niche categories we are in we supply them all more or less. Therefore for us, it has less of an impact than maybe it will have for some other brands since we are much more an aftermarket player as well. We are not therefore 100% depending on manufacturer A being successful versus B because we play with them all. Therefore I do not see it having a major impact. We are seeing a growth continuing in our expectation. We are running our production accordingly. We feel very comfortable with inventory levels we have in this category.

Gustav Sandström (SEB Equities): If I might start off with a follow-up on the inventory, up 21% in local currency. It was also up, if I recall, high single digits in Q1. Obviously you state clearly that this relates mainly to new launches but could you please give us a break-up of how much of the inventory actually stems from the new baby stroller category and luggage please, and how much is something else? On top of that, if possible could we get a geographical breakdown of where this inventory is specifically located? Thanks.

Lennart Mauritzson: The answer is no actually, Gustav. We will not disclose details on the categories because it would be slightly too indicative, only on separate products. What we can say is that as we are planning to sell thousands of these strollers over the coming months it is quite obvious as we are ramping up that it is a very significant amount. If you add it together we can say the majority of the growth is by far in the new launches. If we would take away the products that we are launching this autumn from our inventory holdings we would not have been growing.

Secondly, if you take it by geography since we are manufacturing all of the strollers in our Polish factory and since we are just into the mass manufacturing if you looked at the closing of Q2 all the inventory was held in the European part of the business geographically. However, since we do not report that set-up specifically. However, physically, geographically the majority of the build-up is physically located at the end of Q2 in Europe. It is being shipped to some parts as we speak, to the US markets and other markets around the world. However physical location wise it was associated with plants in Europe.

Gustav Sandström: Thank you, that is very clear. Regarding retail listing on Thule Sleek, first if you can give us some comment on development there with your discussions with retailers? Secondly, if you could give us some hint on when we should anticipate some second launch within this category? I would assume that maybe something without the stadium seating varieties is something to expect.

Magnus Welander: First of all, extremely happy in terms of listings. Listings is not sell-through though so you always have to be a bit cautious with this. However, it is the first step to being able to achieve sell-through to consumers. The listings have been won with all the key retailers in all the key markets so we are feeling very comfortable in terms of having the right retailers showing the product to consumers. We are feeling very good stepping into it therefore. Then it still is we need to convince consumers that when they go to these world market-leading juvenile stores where there is a very competitive reality, as all you analysts and we ourselves have commented on several times, we still need to win the battle in the stores and on the online platforms. The reality is at least we will have very good listings to be able to fight the battles there. I feel very good about the listings.

If we then take the second comment on, will there be more strollers? No doubt, there will be coming more stroller models but as this model, as we knew, would only be really starting to roll out as of Q3 this year, we are talking about future years, not in the near present. The focus will be on the Thule Urban Glide 2, which is growing fantastically, as an all-terrain stroller and for the Thule Sleek which is just about to go to sale in terms of sell-out in the coming 18 months. If you look in the future, yes, we are product developing additional strollers as we speak.

Gustav Sandström: Lastly, some consumer product peers of yours have experienced a bit of a shortage on the logistics side of the business with truck drivers' strike and so forth, in the quarter. It does not seem like it has affected you but have you seen any things like this in your business or do you expect any hurdles going forward of this nature?

Magnus Welander: I think that you are right because one of the biggest challenges that we see globally is that there is a huge overall global challenge in the last mile. It is not about the logistics of sending large quantities between plants to each other in large trucks or on ships. That part is relatively mainstream to solve but there is a more and more growing challenge of reaching that last mile to the small retail shop or even directly to the consumer in terms of finding the small van deliveries for the last mile and making it both cost efficient enough but actually simply finding the volume there. It is something our logistics team is working incredibly hard on. I think we are doing it better than many. We will have some challenges and as we also sell to 140 countries we have to be realistic.

At times there are striking issues, like there was recently. There has been a big strike in Brazil in all the harbours. That hurts our Brazilian business, no doubt, as it does anybody else shipping into Brazil, for example. Last year, there were some issues in the US harbours and generally you can say it is not easy. I do not think anybody will claim it is easy logistics at the moment, with more and more parcel shipments and more and more pick and pack and more and more consumer demands of getting it home to their front door. I think it is a natural challenge that all us consumer goods companies just have to work through. I do not think any of it is big enough to dent our numbers but it sure makes us work hard, that is for sure.

Peter Reilly (Jefferies): I have got three questions, please. Firstly, I was interested to hear you talk about sport and cargo carriers having the most exciting year ever for new products. You have launched quite a lot of new products in that market recently, so maybe you can give us some more colour about what is coming and why you are excited about it?

Secondly, I would love to know a bit more about what is happening with the Urban Glide 2, particularly in the States. You talked about it being very successful in Europe but is it going well in the States as well? Who is buying it? Are these traditional over-achievers out jogging or are they normal people? Therefore, is it positioning you well for the Sleek?

Then lastly on packs, bags and luggage you said earlier this year you still hope to grow the business in 2018. I think that is probably looking a little bit more challenging now given what has been happening. Do you reckon you can still grow PBL for the full year?

Magnus Welander: Thank you for those questions. I have to disappoint you on the first one because we have not shown it to retail yet. There will be, I can tell you, at the morning of the big shows a significant PR event with all the people from that industry. Trade media will be there, because there are some huge launches. You will see it on our home page when we announce it to the marketplace but they are very significant launches that really shape the category going forward. I am sure you will be happy to see them when they come.

In regards to the second one on the Thule Urban Glide 2 it is performing well in the US as well. Historically we have from a historical perspective outperformed in the US versus Europe on the Thule Urban Glide first generation. The reason was that you are absolutely right Peter that there in the US it was an over-achiever. It was the training people. It was the people doing their triathlons, their runs and really it was being used very much as a jogging stroller. That category has been big historically. There was a competitive product which was called BOB and they had a big marketplace. We came in and grew the market taking significant share very quickly in the US. We continue, if you look at it in the US, to see that stroller mostly being seen as a jogging stroller.

The success we have had in Europe where we have had a very, very fast growth in the last nine months, especially in the first six months of this year as we launched the Thule Urban Glide 2, is the positioning is different. It is being sold much more as an all-terrain, very easy to use, comfortable stroller for everyday use. Partly that is our positioning, where we did a black and black model and we tweaked it a bit, making it easier to put in the bassinette. We made it easier to use as an everyday stroller. However, partly it is also that consumers have found how super-practical it is even on cobblestone streets or just walking on the beach or something like that. In Europe it is more positioned as an urban stroller for everyday use. It is also growing much faster as we have gained more listings of that kind. Therefore by default you are right in that it is helping us more in Europe as being positioned already as one type of urban stroller. Now we get a second type with the Thule Sleek, where you are going to find them next to each other in similar juvenile stores. Therefore a slightly easier ride in Europe. Also, specifically the type of stroller we are targeting here with a sibling, stadium seating, premium stroller is more of a European type of product anyway. In our expectation we should sell a lot more of the Thule Sleek in Region Europe than we should sell in the US.

Then thirdly on packs, bags and luggage, you are right. There is always, if you have not grown in the first half, as we have seen, a more rapid decline in the legacy categories and a more rapid decline in some of those OE contracts for packs, bags and luggage. They are definitely holding us back more than we thought, both of those two things. We are therefore by default putting significantly more pressure on how much we can grow in the growth categories of luggage and of everyday backpacks. I am not sure that we will grow. We have an ambition. The ambition is definitely more difficult and you are absolutely right, truly mathematically we will have a bigger challenge of how much we will need to grow it. Slightly less optimistic. Very optimistic on growth in the second-half but can we fully overcompensate for the decline in the first-half? That is still to be proved.

Peter Reilly: If I can come back on the sport and cargo carriers? I understand you are not going to tell us before the product launch, but it sounds like it is very material in terms of the breadth of products you are talking about. It is not just a couple of niche products here or there. Is that a correct assumption?

Magnus Welander: It is the correct assumption. As it is categories where we are already very, very strong and absolutely global market leaders I do not think so much our focus is not on immediate pick-up of additional sales. It is that we are redefining the platform for us to build on for many more years to come and be the undisputed market leader, as we are today, also in years to come. That is why we are not talking so much to you as investors and analysts about, 'This is going to do fantastic things for us in pick-up of sales.' It is just more importantly redefining and repositioning us even further ahead of our competition in the categories where we are undisputed market leaders.

Peter Reilly: This is very much a 2019 and 2020 story, I guess, a bit like the fact that the growth you are seeing currently is a product that you launched maybe two years ago.

Magnus Welander: Yes. That is really the effect. You are right.

Per Johansson (S&T Asset Management): Magnus, your thoughts about the US; has that made you change maybe not your strategy but maybe more short-term where you want to put in your resources? Maybe put them more into the Europe & Rest of the World market. That is my first question.

My second question, maybe more on insourcing, spare parts and things like that for your strollers. Do you see any problems with getting these products to your assembly line in Poland? That is my second question.

My third question is, all these operation focuses on Pila, on Hillerstorp and so on, will that enable you to maybe increase your gross margins a bit more in the coming years or in the coming period as we have seen lately? Thank you.

Magnus Welander: If you look at the first one, I think we have the strength and capability of focusing on Europe & Rest of World like we already are doing. We do need to focus on the world's biggest market for us, which is the US anyway. It is not changing our view on where we should focus resources, money or efforts. We need to continue to do both. Of course we share best practices across the world. For example, at the moment the biggest fair in the industry is happening next week. We have our biggest annual sales meeting over in the US as we speak and we have some of our European colleagues that are over there to speak about different ways we have done things over here that might help the US team to get things more going. I do not think it has changed our view at all. It is just that we need to acknowledge the fact that the market has been stronger in Europe and we have been outperforming Europe. We need to do it in both regions.

If you take on the second part of insourcing and ensuring that we can take care of everything what it takes into account of a stroller with all the accessories and spare parts and everything. It is a big undertaking, no doubt. It is a complex product the stroller. We sell a lot of accessories. If you are a premium stroller company you expect to have a significant share of sales in additional components and accessories. You should of course not hopefully, if you manufactured the right type of stroller, need too many spare parts initially but we already manage that type of spare part handling for other products so we are not worried about how we would set that up or how we would do it. We feel we have that well under control.

If you take the third question about our investments in the plan, it is a type of investment that is actually a two-fold. One is very much the capacity into new product categories. We are investing in a factory in Pila in Poland where we are both doing strollers, which we never manufactured ourselves historically, and where we will be doing hard case luggage which we never manufactured. That is capacity expansion into new categories, strategic and capacity. If you look at the Hillerstorp plant it is major investments for future efficiencies. If you do future efficiencies right and you combine it with top-line growth it should long-term help you to get better margins. However, I would not say that any of these major investments are of the type where you will see a step-change to our margins. It is more of a continuous, you can call it almost boring, nitty-gritty work of every year trying to squeeze out a little bit better margin, which is part of our long-term 20% EBIT margin growth.

Stellan Hellström (Nordea): I would like to ask about sporting cargo carriers in North America. I reckon there were tough market conditions in this quarter but if you could comment maybe? It is obvious that your performance in Europe you are taking quite significant market shares continuously. How do you feel this is developing in North America?

Magnus Welander: All the data that we have and the information we are getting from our retail customers is that we continue to take market share also in North America. Not at the same pace as we are taking it in Europe actually but we are taking market share also in a much tougher market in North America. In Europe we have had a number of very key trends that are helping us. There is a trend generally that in sporting cargo carriers to move to carrying your bags much more on the back of the car at the tow bar with therefore more expensive and more practical solutions, tiltable with back lights and everything. That is perfect for us at Thule. A heavy e-bike which is much more difficult to load on than an 8kg bike because with 23kg with batteries etc., you need to technically have a much better product to convince a consumer that they can load it in the right way or several of those heavy bikes.

That trend of heavier bikes, more expensive bikes, more moving to the back of the car and with the very tricky thing of applying that to a spherical tow ball has meant that the trend fits us. We are simply much better than everybody else doing that and therefore we are picking up more market share. In the US there is a similar trend to move to the back of the car but they have a significantly technically easier solution because they have a square hitch hole, as they call it. Technically it is easier to do a square thing that you put in a square hole than catch a round, spherical thing. I do not want to go into the technicalities but it is easier for other brands to compete, to do an okay solution. We still have the best ones there as well but not with the same distance, I would say, to competition. There is a little bit of that going on and then there is the general market trend is less positive. However, we do take market share also in US.

Stellan Hellström: Maybe a question also on your OE business. You have discontinued some for the pickup industry, truck industry. Can you shed light on the remaining OE business in sports and cargo carriers and RV? Is that more attractive, and are your market positions better?

Magnus Welander: Yes, the main reason is, similar to what I just mentioned, if a product is technically more complex to do really well you can position yourself also to the large OE manufacturers with a technical competence of building something, developing and manufacturing something that is complex. If you can do that and they can still benefit, sell it and make nice profits because it is a more expensive product you should be able to withstand and hold up to a better margin, so a higher margin performance. We are the number one provider both in the North American market and in the European market to premium car manufacturers that want to have these type of OE solutions. However, when it is more advanced solutions because to be honest those pickup truck accessory solutions were very basic type of accessories, if you do a very basic type of accessory you will be under completely different type of pressure from the purchasing organisation because you add relatively little value with your strong competence. In the other categories we are adding significant value. We have insights that none of these manufacturers have about these products. We have test records, we have proven performance things, we can really coach them how to do it better. They therefore think it is worth paying for it and we can have better margins. That is the big difference.

It is more about the complexity of the product rather than having done the right negotiations or anything like that. It is the reality that as we go with the business and that is why we are phasing ourselves out of these businesses, we need to play and capture where people are prepared to pay for quality and competence. If that is then an OE player or if it is a retailer or even if it is a consumer we want to capture it where the skill set and product development competence is getting paid.

Stellan Hellström: Then finally on the launch here of Thule Sleek, I take it that you have great expectations for this product. Is there any chance or should we expect that the launch costs will rise as a percentage of sales even for the Group in the third quarter?

Lennart Mauritzson: No. I would say that if you look at it a lot of these costs have already been seen in Q2 because similar to an inventory build-up in terms of preparing all the marketing material, the displays, dressing up shops and all of that, since it is happening in the next few weeks we have taken the major efforts of those costs already. No, it will not continue to grow. It will be relatively higher in terms of product development cost but specifically launch costs, no you should not see it pick up in Q3.

Daniel Schmidt: Coming back to product development spending, you write and you also said at the call that you are at 6% of sales now. Could you update us on how we should model this cost item in the second half of 2018 and also to the start of 2019? I know that you have said that this is the peak year and so on but is it going to go above 6% in Q3 for instance or is it the opposite? Some guidance on that to start with.

Magnus Welander: At the guidance, we said that the full year 2018 you should expect us to be on a 6% level. That means by default if we are trailing 12 months at 6% you should see it being similar to what you have seen. We are going to maintain it around 6%, not exactly but around those levels. Not going down fast or not increasing, it is going to be kept around a 6% level for a rolling 12 months, for the full year as well.

When we go into 2019, what we have said is that over time it will slowly move downwards. As revenues grow in those new categories where we are spending a lot of money. That does not happen over one month or one quarter. It will take some time so it will be slowly going down from the 6%. You will not see a rapid step down. What we are saying is more that it will not grow and if anything it will slowly start to move downwards after we go into the 2019.

Daniel Schmidt: Then also a follow-up on RV again. When it comes to the aftermarket what is your experience going back in history if we would see a decline in the OE business? Has the aftermarket been able to hold up or has it been gradually affected also by the slowdown in the OE? What is your experience?

Magnus Welander: We saw the big decline in 2008 so that is pretty easy to go backward. That is the only time it has declined in the last 15 years. There it was a very rapid decline. Let us remind ourselves that at that huge decline for the RV category it was a combination with the financing from consumers not being able to secure financing. That is not what is worrying people so much for this downturn. There is still a underlying consumer trend that is more positive. There is an underlying consumer financing that still looks more positive. An adjustment this time is not of the same size, not nearly in anybody's expectations.

It is not even of the same kind because the likelihood of an adjustment, if there is one, is that what will happen is that some manufacturers have overextended their manufacturing, tried to push out too many of their models to specific dealerships. By default some dealerships will then be sitting on too many vehicles. When that happens there are two things that can happen. One is they are trying to get rid of their vehicles that they now sit on and that are tying up significant funds on their lots. A typical way that that happened last time was they start to throw a lot of accessories extra on and say, 'You get a fantastic deal if you take it off my hands.' A little bit like a business package with the extras on a car when they are trying to get rid of them from their lots.

That is easier to do in the RV industry than it is in the car because in the car you more get what you get. However, on an RV they can add things to it afterwards. You get this and you get the bike carrier. That means that our type of industry is less immediate than if you would be, for example, something like a toilet or something that is more installed with the vehicle. By default if you look at what happens with a manufacturing trend, as a manufacturer has a more, I would say, defined production planning set-up, normally their decisions are more binary. You are saying, 'Am I going to hold open my vacation production or am I closing production for four weeks?' What happened in 2007 and 2008 was dramatic longer closures of manufacturing facilities where they said, 'We are going to have a Christmas break this year and the break is nine weeks and we are not going to produce anything.' It becomes much more binary. While the dealership will continue to sell in an aftermarket world in a slower, more grey type of decline than that binary.

If you are a supplier to a lot of brands and manufacturers even if one of them is binary maybe the whole market is not binary. It actually became the whole market in 2008. The whole market grew binary for a long time and then it declined binary for a period of time. I do not think that will happen now. I think we will see some manufacturers and some dealerships starting to hold back but it will not be the same effect.

Daniel Schmidt: You are basically saying if there is no heart attack to the system the aftermarket will do better and the OE could be impacted to some degree, like you said earlier today.

Magnus Welander: Yes.

Peter Reilly: I wanted a few issues to talk about please. Firstly, I am wondering if you can give us an update on the headcount in your factory in Poland. I think you said at the last call you had 100 people working there. I am interested to see where you are with that.

Secondly, I would love to know more about what is happening with Subterra, how that product is selling and whether there is anything you can add about the Revolve range. I know it does not go on sale until early next year but whether there is any additional colour you could add.

Then lastly, you mentioned that you are launching some niche RV products in the US and I am curious to know what they actually are. If you would not mind sharing that with us?

Magnus Welander: Absolutely. If we take first one, we are roughly 60 people more than we were last time when we discussed so 160 now in Poland in that specific factory. That gives you an idea about how many more we are at currently in Pila. The Subterra luggage collection continues to sell well, continues to gain listings and continues to be doing well in both department stores and airport stores. It is being sold in more than 85 countries and in more than 70 international airports. It continues to sell through well which is of course key in terms of confidence.

That confidence has helped the type of listings we are getting, for instance, for our new hard cased Thule Revolve range that, as you said, is coming at the beginning of next year. In many of those, not all of them but in many of those locations we will have also the Thule Revolve range. We will have the Thule Revolve range in some locations where we do not have the Thule Subterra range and in some cases they will both be coming at the same time as we become a more complete supplier with two types of collections with both hard and soft in the beginning of next year. Once again, as we have said many times, listings is only one thing. It is actually sell-through that is key. However, in terms of listings for the Thule Revolve that looks very promising after the fairs and after our retail meetings.

Then finally the niche products that we are doing in RV products is in the core category that we are very strong at. What has happened in the US market over the last few years is you have seen a growth of the smaller vans. What would normally have been ridiculously small for a US motorhome buyer has started to grow as a motorhome category also there. We are then doing both our awnings and bike carriers. Then on top of that we have launched a type of awning for the US market in a category which does not really exist in Europe, which is this overland vacation where you take your big SUV, you drive it out, you bring your bikes and you bring your stuff, and you do 1-2 nights out in Utah to go motorcycling or something like that. What that then means is you use your normal very large American SUV but as you are going to have it for maybe two days out there you want some shade, you want some stuff to throw out your big Yeti cooler with your icebox in it and some stuff. There we have actually launched a specific model of an awning that is being applied to large SUVs. In the bordering country, so to speak, between a sporting cargo carrier customer of ours buying those products and an RV customer. Those two categories are doing very nicely but they are very small niche categories.

Peter Reilly: Are you selling those as aftermarket products or as OE products?

Magnus Welander: They are sold as aftermarket, so if you look at it for the last product we mentioned, the one that is more put on your SUV that is a pure aftermarket product. If you talk about the first one it is actually a combination of an OE product with one of the large US manufacturers and an aftermarket product.

Since that was the last question, I then want to wish you all a fantastic summer vacation with tremendous use of Thule products. We will speak to you after the Q3 report. Thank you.

[END OF TRANSCRIPT]