



# Ericsson Third quarter 2019

Oct 17, 2019





# Peter Nyquist

Vice President Investor Relations



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This presentation contains forward-looking statements. Such statements are based on our current expectations and are subject to risks and uncertainties that could materially affect our business and results. Please read our earnings reports and our most recent annual report for a better understanding of these risks and uncertainties and please see the last page in this presentation for further information about forward-looking statements. Any forward-looking statements made during this presentation speaks only as of the date of this presentation and Ericsson expressly disclaim a duty to provide updates to these forward-looking statements, and the estimates and assumptions associated with them.



# Börje Ekholm

President and CEO

# Key takeaways



- Increased R&D efforts have resulted in a competitive portfolio – strong momentum across business
- Several important wins improving market footprint for future business
- Faster than anticipated 5G rollout – North America and North East Asia leading the way
- Provision for SEC/DOJ related costs of USD -1.2 b. (SEK -11.5 b.)
- Strong cash flow - solid financial position with a FCF (before M&A) of SEK 11.8 b. YTD and a net cash position of SEK 37.4 b.
- Geopolitical and financial environment creates continued uncertainties

# Q3 2019 in numbers



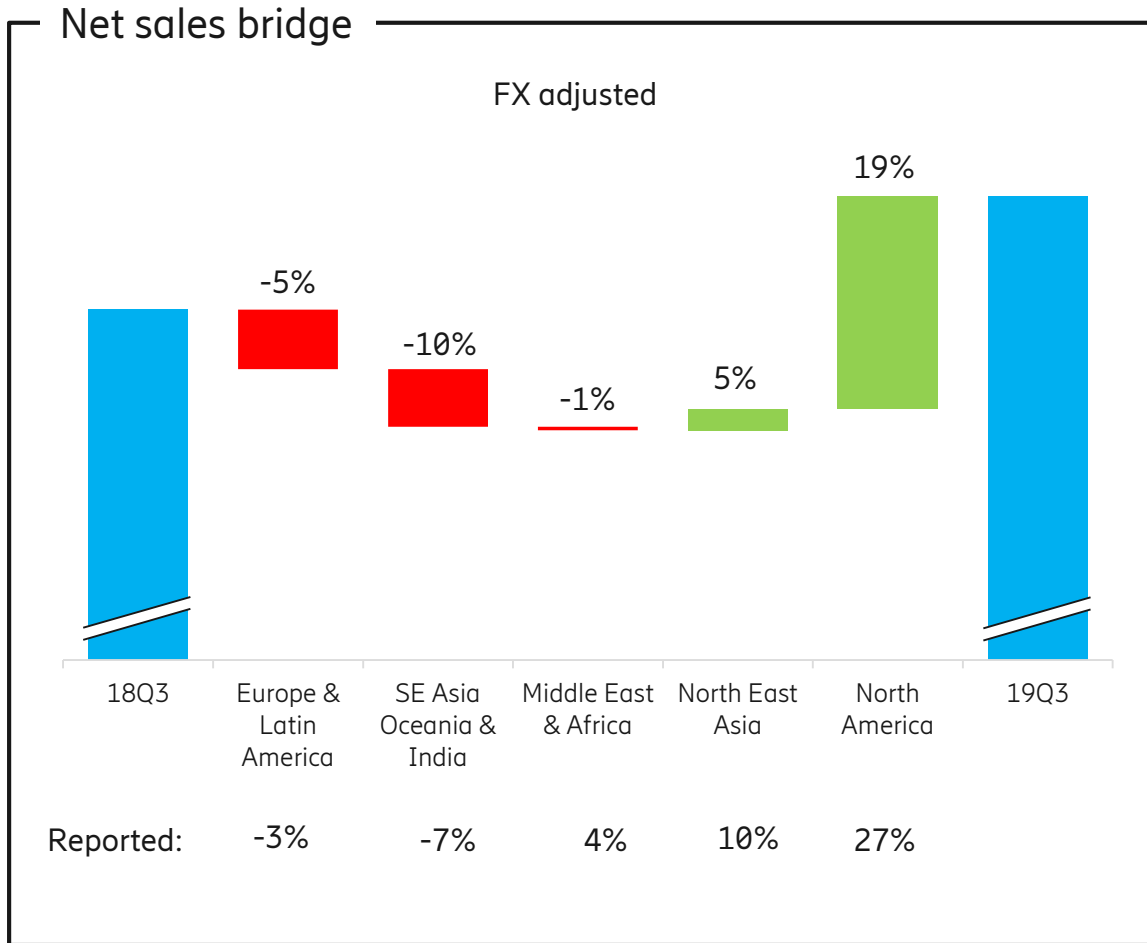
## Financial Performance

Excluding restructuring charges

SEK b.	19Q3	18Q3	19Q2
Net sales	57.1	53.8	54.8
Gross margin	37.8%	36.9%	36.7%
Operating income	-4.0	3.8	3.9
Operating margin	-7.1%	7.0%	7.0%
OI ex. items affecting comp.	6.5	--	--
OM ex. items affecting comp.	11.4%	--	--
Net income	-6.9	2.7	1.8
Free cash flow before M&A	5.5	0.7	2.2

- Free cash flow before M&A SEK 5.5 (0.7) b.  
Net cash SEK 37.4 (32.0) b.
- Organic growth 3% – Reported growth 6%
- Underlying margin 11.4% – improved YoY and QoQ
- Networks – profitable growth, absorbing negative impact from strategic contracts
- Digital Services – significantly improved result
- Managed Services – improved margins
- Emerging Business – growth in IoT
- Items affecting comparability:  
SEC/DOJ cost provision of USD -1.2 b. (SEK -11.5 b.) and SEK 0.9 b. in refund of earlier paid social security costs in Sweden

# Market area sales Q319, YoY



- Europe & Latin America
  - Growth in Europe (Networks and Digital Services) offset by decline in Latin America (large deployments in 2018)
  - Decline in Managed Services from exited contracts
- South East Asia, Oceania & India
  - Strong Managed Services sales
  - Digital Services declined due to lower legacy product sales
- Middle East & Africa
  - 4G and 5G deliveries in key markets
  - Decline driven by contract exits in Managed Services
- North East Asia
  - 5G deliveries in South Korea
  - 4G deployments in mainland China slowed down
- North America
  - 4G and 5G investments
  - Strong Managed Services sales

Ericsson equipment (radio and core) in 19 live 5G networks



# Carl Mellander

Chief Financial Officer



# Q3 2019 items affecting comparability



## Financial Performance

Excluding restructuring charges

SEK b.	19Q3 excl restr. charges	SEC/DOJ provision	Social cost refund	19Q3 adjusted
Net sales	57.1			57.1
Gross margin	37.8%			37.8%
Operating income	-4.0	-11.5	0.9	6.5
Operating margin	-7.1%			11.4%
Op. Income Em. Business & Other	-11.3	-11.5	0.9	-0.8

- SEC/DOJ cost provision of SEK -11.5 b.
  - USD -1.2 b.
  - Handled as non tax deductible
  - Reported as Other operating income and expenses in segment Emerging Business and Other
  - No cash impact in Q3
- Refund social costs of SEK 0.9 b.
  - Refund for earlier paid (2013-2017) social security costs related to pensions in Sweden
  - Reported as selling and administrative expenses in segment Emerging Business and other
  - Positive cash impact in Q3 2019 SEK 0.4 b. after tax deduction

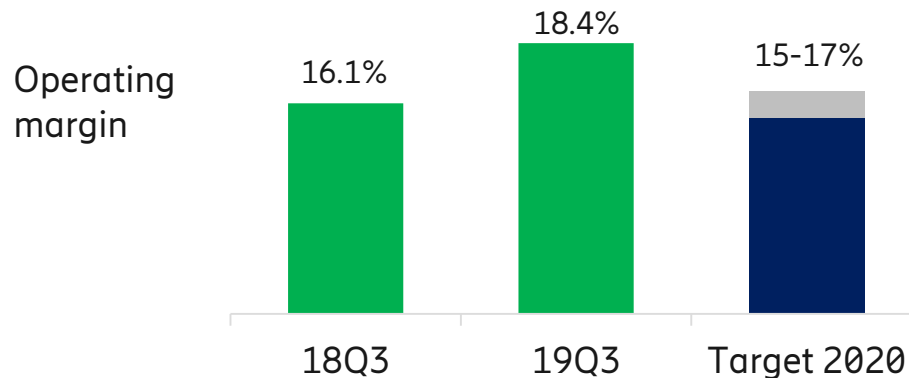
# Networks



## Segment Networks – Financial performance

Excluding restructuring charges

SEK b.	19Q3	18Q3	19Q2
Net sales	39.3	35.9	37.8
Gross margin	41.6%	41.5%	41.4%
Operating income	7.2	5.8	5.7
Operating margin	18.4%	16.1%	15.0%
<i>Capitalization impact</i>	<i>0.3</i>	<i>-0.1</i>	<i>0.4</i>



- Sales adjusted for FX +4% YoY
  - Strong growth in North America – 4G and 5G investments
- QoQ reported growth 4%
- Gross margin
  - YoY flat excluding restructuring charges
  - QoQ the underlying gross margin declined -0.8 percentage points, impacted by strategic contracts
- Operating income and margin increased YoY
  - 5G momentum continues with higher sales and gross margin
  - Underlying margin stable – Q318 impacted by revaluation of Customer financing and Impairment losses of trade receivables
- 27 commercial 5G contracts with named operators

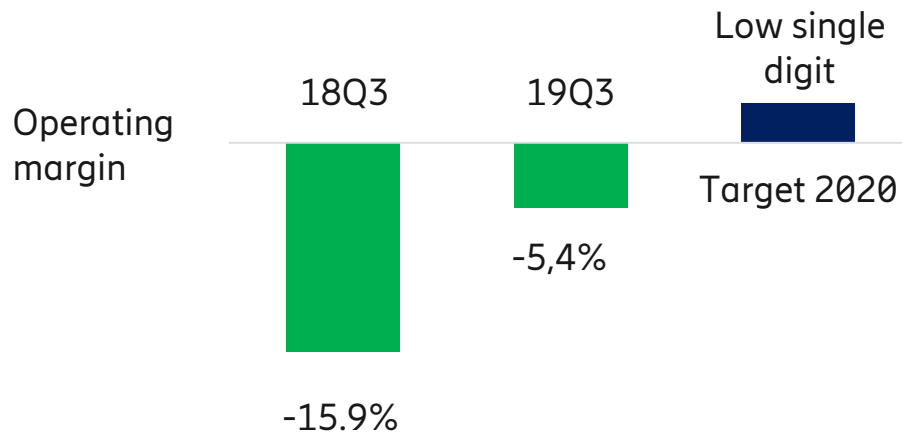
# Digital Services



## Segment Digital Services – Financial performance

Excluding restructuring charges

SEK b.	19Q3	18Q3	19Q2
Net sales	9.9	9.0	9.0
Gross margin	38.3%	36.9%	37.1%
Operating income	-0.5	-1.4	-1.3
Operating margin	-5.4%	-15.9%	-14.6%
<i>Capitalization impact</i>	<i>-0.2</i>	<i>-0.4</i>	<i>-0.3</i>



- Sales adjusted for FX +5%
  - Strong sales in North America and North East Asia
  - Rolling 12 months sales of new products +19%
  - Momentum in 5G and cloud-ready portfolio
- Gross margin improved YoY and QoQ
  - Increased software share
  - Continued cost reductions
- Operating income – significantly reduced losses
  - 29 of the 45 contracts addressed to date (2 in Q3), target to have 75% completed end 2019
  - Execution of BSS strategy progressing according to plan – several new BSS deals won in the quarter
  - Earnings may vary between quarters – tracking towards 2020 target

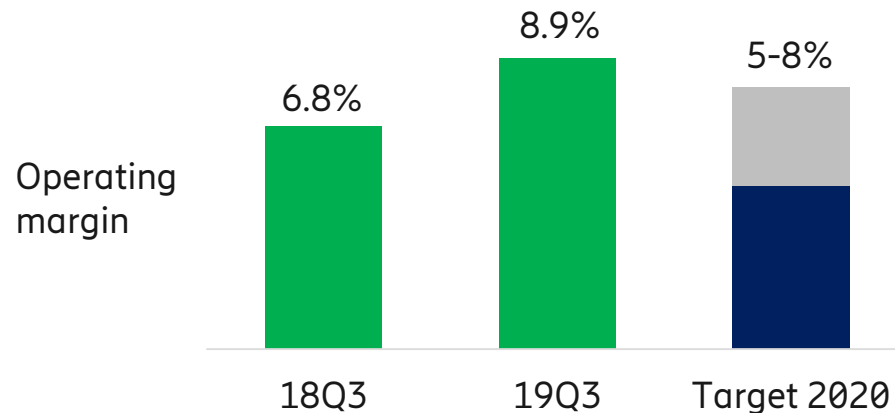
# Managed Services



## Segment Managed Services – Financial performance

Excluding restructuring charges

SEK b.	19Q3	18Q3	19Q2
Net sales	6.4	6.5	6.3
Gross margin	17.9%	12.9%	12.3%
Operating income	0.6	0.4	0.2
Operating margin	8.9%	6.8%	3.2%



- Sales adjusted for FX -5% YoY
  - Lower sales due to contract exits
  - Growth in Network Optimization
- Gross margin increased
  - YoY – efficiency gains
  - QoQ – non-recurring costs in Q2
  - Higher add-on sales
- Operating income
  - YoY and QoQ increase due to higher gross margin
  - YTD operating margin 6.9% (5.4%), excluding provision reversal in Q1 – in line with 2020 target
- R&D investments in automation, machine learning and Artificial Intelligence

# Emerging Business & Other



## Segment EB & Other – Financial performance

Excluding restructuring charges

SEK b.	19Q3	18Q3	19Q2
Net sales	1.6	2.4	1.7
Gross margin	20.5%	32.3%	19.2%
Operating income	-11.3	-1.0	-0.7
Operating margin	--	-41.5%	-42.8%
OI ex. items affecting comp.	-0.8	--	--
OM ex. items affecting comp.	-46.6%	--	--

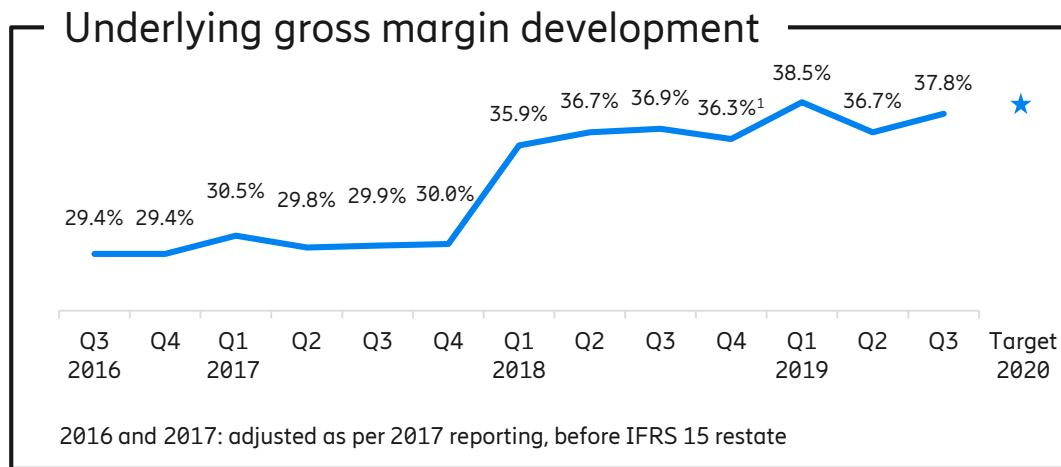
SEK b.	19Q3	18Q3	19Q2
<b>Emerging Business, iconectiv and common costs</b>			
Net sales	1.1	1.0	1.0
Op inc, ex. items affecting comp. in 19Q3	-0.5	-0.6	-0.5
<b>Red Bee Media</b>			
Net sales	0.6	0.7	0.6
Operating income	0.0	0.0	0.0
<b>Media Solutions</b>			
Net sales	0.0	0.7	0.0
Operating income	-0.3	-0.4	-0.2
<b>Items affecting comparability in 19Q3</b>			
Operating income	-10.5	--	--

- Emerging Business incl iconectiv
  - Sales growth in IoT. >4,500 enterprises on platform
  - Increased income in iconectiv
- Red Bee Media
  - Lower project related sales YoY
  - Operating income stable at break-even
- Media Solutions
  - 51% of MediaKind – divested February 1
- 2019 Q3 segment income impacted by -10.5 b. of items affecting comparability



# Gross margin

Excluding restructuring charges



<sup>1</sup>excluding costs for revised BSS strategy

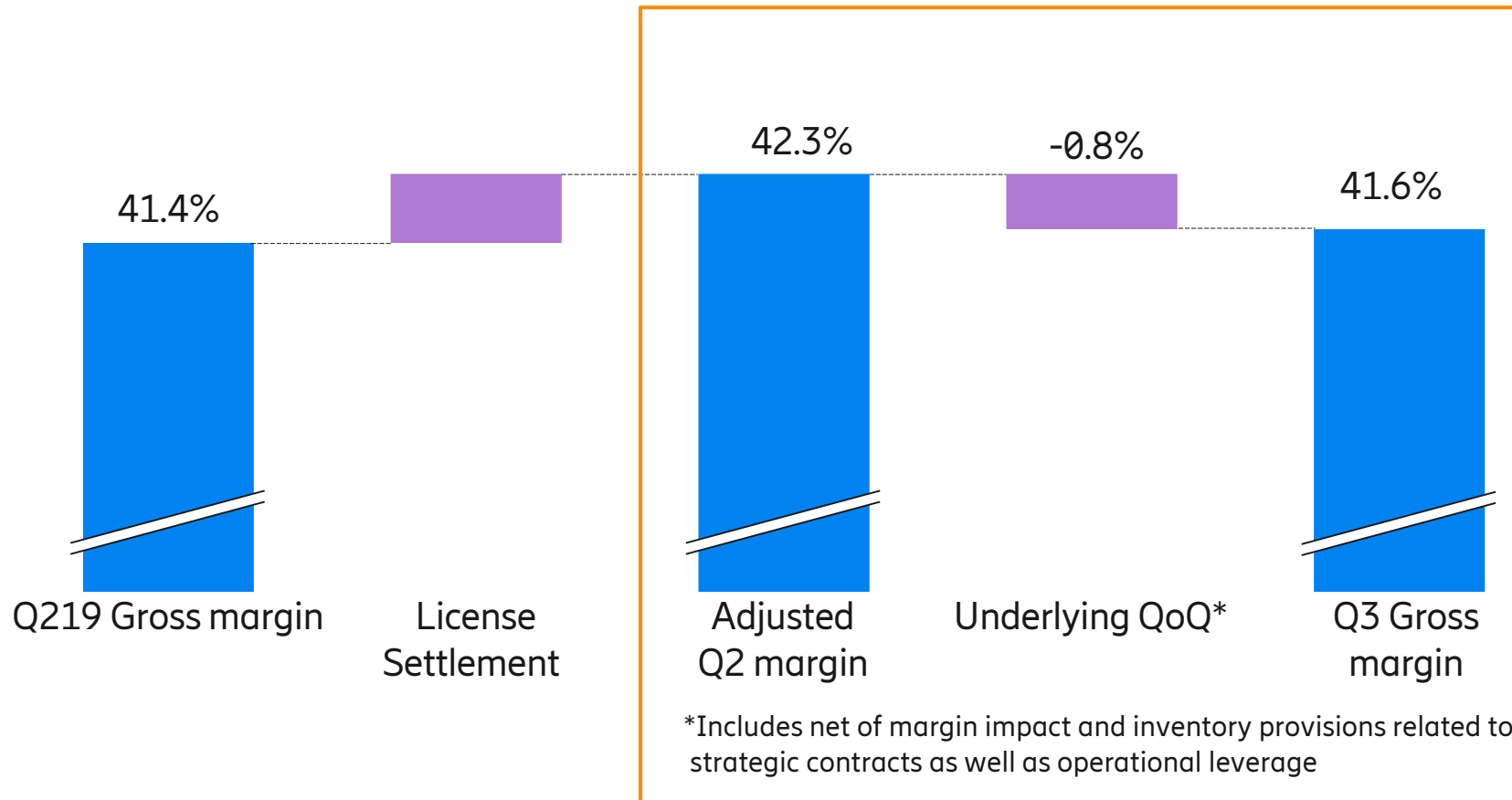
- Gross margin improved QoQ – improvements in Managed Services and Digital Services
  - Managed Services: Higher add-on sales and Q219 impacted by non-recurring costs
  - Increased share of software sales in Digital Services
- Underlying gross margin in Networks reduced with -0.8 percentage points due to dilutive effect of strategic contracts and related inventory provisions
- Gross margin improved YoY
  - Improvements in Managed Services and Digital Services
  - Networks stable, despite strategic contracts
  - Increased IPR revenues

Continued solid gross margin in line with 2020 target

# Strategic contracts impact on Networks GM



Gross margin to be compared QoQ



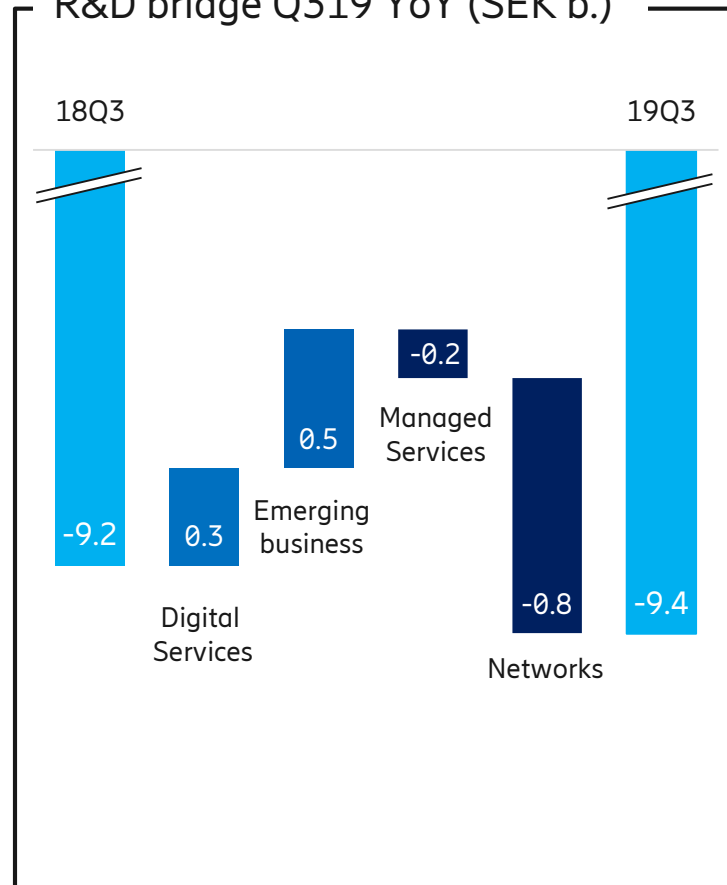
- Some contracts have lower initial margins, however all selected for their value creation
- Competitive product offering and cost structure, enable us to capture opportunities without jeopardizing our 2020 targets
- Will continue to have a negative impact on Networks gross margin, and the dilutive impact may vary between quarters

Strategic contracts expected to have a somewhat increased negative impact on gross margin short term

# Operating expenses

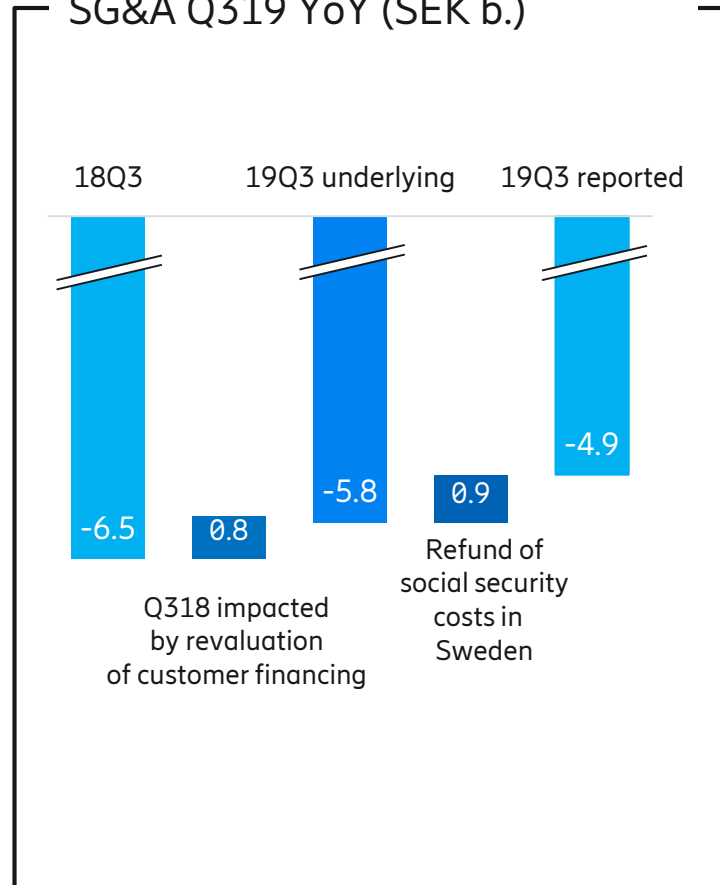
Excluding restructuring charges

R&D bridge Q319 YoY (SEK b.)



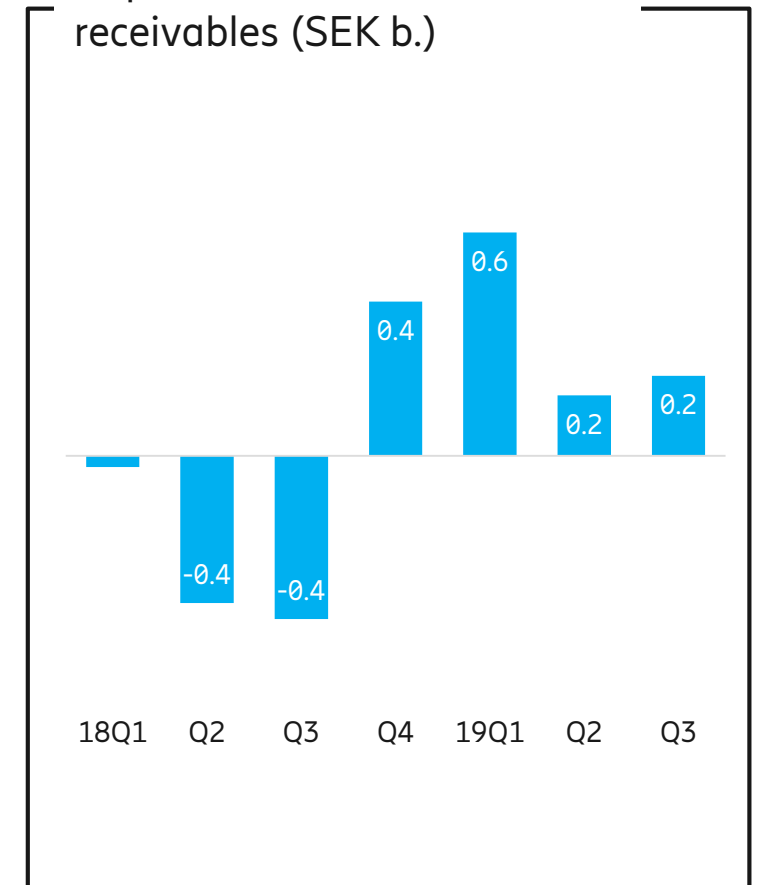
Investments in 5G and AI

SG&A Q319 YoY (SEK b.)



Underlying SG&A expenses stable YoY

Impairment losses on trade receivables (SEK b.)



Methodology for continuous impairment testing

# Free cash flow



## Financial Performance

SEK b.	19Q3	18Q3
Net income reconciled to cash	-4.3	2.9
Change operating net assets	11.3	-0.9
<b>Cash flow from operating activities</b>	<b>7.0</b>	<b>2.0</b>
CAPEX	-1.2	-1.1
Other	-0.2	-0.2
<b>Free cash flow before M&amp;A</b>	<b>5.5</b>	<b>0.7</b>
M&A	0.5	0.4
<b>Free cash flow</b>	<b>5.0</b>	<b>0.3</b>
<i>Net cash end of period</i>	<i>37.4</i>	<i>32.0</i>
<i>Gross cash end of period</i>	<i>76.2</i>	<i>65.7</i>

- Free cash flow before M&A SEK 5.5 (0.7) b.
- SEK 2.2 b. cash out from provisions in Q3
- Majority of the DOJ/SEC provision of USD -1.2 b. (SEK -11.5 b.) is expected to be paid in Q4
- CSF acquired in the quarter, strengthening the iconectiv portfolio
- Strong cash collection

Free cash flow before M&A YTD SEK 11.8 (1.2) b.

# Planning assumptions – summary

Please see the Q3 report for complete planning assumptions



## Market

- RAN equipment market 5% FY 2019, 2% CAGR 2018-2023 (Dell'Oro)

## — Net sales

- Normal seasonality Q3→Q4 18%. Uncertainty of NA operator merger likely to impact spending negatively short term
- Baseline for IPR ~SEK 9 b., on an annual basis

## — Gross margin

- Strategic contracts in Networks expected to have a somewhat increased negative impact on gross margin short term
- Large 5G deployments in China expected to commence in 2020 – investments to increase market share. Initially challenging margins but positive over the lifespan.
- Kathrein - initially negative impact on Networks margin
- Improvements in Digital Services continue, earnings will vary depending on business mix, sales seasonality and impact from the 45 contracts

## — Operating expenses

- Opex typically increase Q3→Q4 due to seasonality

## — Restructuring charges

- Restructuring charges for full-year 2019 are estimated to be 1% of sales

## — Currency exposure

- Rule of thumb: USD/SEK 10% weaker → ~ -5% sales and ~ -1pp OM. For historical FX rates, please see [ericsson.com](http://ericsson.com)

Ericsson

Based on current visibility, assessments and FX rates





# Börje Ekholm

President and CEO

# Closing remarks



- Will continue to invest in R&D and leverage our leading portfolio to capture market opportunities
  - 5G, cloud native portfolio, AI and automation
- Strong momentum in 5G business – will continue to expand footprint where strategically and financially sound
- Confident in reaching 2020 and 2022 financial targets
  - Updated sales ambition for 2020 SEK 230-240 (previously SEK 210-220 b.)
  - Operating margin target for 2020 remains unchanged at >10%<sup>1</sup>
  - Operating margin target for 2022 12-14%<sup>1</sup> (previously >12%)



Investor Update on October 17 at 3:00 – 5:00 CET, on-line only digital event



**Q & A**





# Forward-looking statements

This presentation includes forward-looking statements, including statements reflecting management's current views relating to the growth of the market, future market conditions, future events, financial condition, and expected operational and financial performance, including, in particular the following:

- Our goals, strategies, planning assumptions and operational or financial performance expectations;
- Industry trends, future characteristics and development of the markets in which we operate;
- Our future liquidity, capital resources, capital expenditures, cost savings and profitability;
- The expected demand for our existing and new products and services as well as plans to launch new products and services including R&D expenditures;
- The ability to deliver on future plans and to realize potential for future growth;
- The expected operational or financial performance of strategic cooperation activities and joint ventures;
- The time until acquired entities and businesses will be integrated and accretive to income; and
- Technology and industry trends including the regulatory and standardization environment in which we operate, competition and our customer structure.

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