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Q4 2018 Outokumpu Oyj Earnings Call

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PRESENTATION

Operator

Good afternoon, ladies and gentlemen, and thank you all for standing by. Welcome to today's Outokumpu Full Year Results 2018. (Operator Instructions) I must advise also that this call is being recorded today, Thursday, 7th of February 2019. And without any further delay, I would now like to hand over the call to your first speaker today, Tommi Järvenpää. Thank you. Please go ahead.

Tommi Järvenpää ***Outokumpu Oyj - VP of IR***

Thank you. Good afternoon, and welcome to Outokumpu's Full Year 2018 Earnings Webcast. My name is Tommi Järvenpää, I'm the head of Outokumpu's Investor Relations. With me here today are also our CEO, Roeland Baan; and our CFO, Chris de la Camp. We will be referring to the presentation that can be found on our website. As always, please pay attention to the disclaimer in the presentation as we will be making forward-looking statements.

With these remarks, I'm pleased to hand over to our CEO, Roeland. Please go ahead.

Roeland I. J. Baan ***Outokumpu Oyj - President & CEO***

Tommi, thanks. Welcome to the call. As always, we will start with the vision to be the best value creator in stainless steel by 2020. Just to reiterate, we do have a target of EUR 750 million in 2020. We reiterate that this is the target that we are confident we will achieve. And, of course, as we said during the CMD, given the market circumstances we have seen on our baselining of 2015. Major deviations up or down will have deviations on the number. But then if you look at the underlying business there is nothing that makes us, at this moment, to reconsider those targets.

Go to the results for the year in 2018. And clearly, 2018 was an extraordinary year. With the 232 tariffs implemented by the U.S. We have seen a major disruption of trade flows, resulting in a very large deflection of volumes from U.S. into Europe. And on top of that clear jockeying proposition of Asian exporters into the European market. The safeguard measures -- the temporary safeguard measures that were announced in July of last year have only partially helped due to a number of design flaws that we have talked about before. The main design flaw being that there was a so-called shipping clause that allowed material that was notionally already destined for Europe to come in without adding to the quota.

On top of that, you have seen very clearly as well that in first half of the year, when the commission has already announced the investigation into safeguards, everyone in this [dock] tried to get as much volume into Europe, leading to import volumes of up to 110 tonnes, 115 tonnes per month, and a 33% share of consumption by imports, something that we haven't seen before. And with that, of course, came significant erosion of prices in Europe. Conversely, in the U.S., we have seen prices strengthened; however, not as much as we had hoped for because ultimately there is still the arbitration going on between the higher pricing in the U.S. and the lower pricing in the U.S. and China varies at 25%. So the ability to price up has always been curtailed by that arbitration.

Overall, in absolute sense, we ended the year with EUR 485 million of EBITDA. And if you look at bridge to 2017, the main blocks there that influence the difference was deliveries, slightly lower; overall, pricing and mix slightly better, mainly because of the mix and high prices in the U.S. We have been very successful in Europe to move a mix of high added-value products, up by probably a sort of 40% from

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about 8% of our portfolio volume to about 12% to 13% of our portfolio volume at significantly better prices and margins.

Further hedging was slightly negative, basically it is 0. The biggest issue that we all have been talking about were the input costs. Cost of electrodes, cost of ferrosilicon and specifically in the U.S., the cost of freight has been a very big negative impact on the results. Ferrochrome, we had lower prices compared to '17, partially compensated by higher volumes, but sales were negative and altogether that accounts to EUR 485 million.

So if you then have a look at how the different parts were influenced in the business. In Europe, where the biggest impact came from the pricing, we have seen a significant drop compared to 2017 to EUR 250 million. Still given the fact that we reached base prices of as low as EUR 750, the mitigation effort that we have had in Europe has been extraordinary and shows how robust the business there is.

In the Americas, and I come back into detail to it later on. In the Americas, we have made breakeven, slightly disappointing. We had hoped to have a better year in 2017, but again a number of elements that has -- have pushed the performance down, mainly again cost -- input costs have gone up. And I'll get there in detail in another slide later on.

Long Products had an excellent year, almost EUR 10 million improvement over last year, good volumes and good margins on both sides of the ocean. And then ferrochrome, as said, slightly lower prices, but extremely good operational performance leading to record productions.

Before we talked about the prices. Here, you see them a little bit better spelt out. In Europe, we had lost about EUR 200, EUR 220 per tonne on the base price; on our volume of about 1.6 million tonnes, so you can do the math. And you can see as well how much we have been able to mitigate. The U.S. price change is about $90 up, but far not enough to compensate what happened to Europe and, of course, with the lower volume as well comparatively not a total hedge for the European business.

Nickel prices have been trending up over the year. They are reaching peak by about mid-year and then trading off very significantly. So a few -- a bit of volatility as far as the metal effects are concerned, but throughout the year, pretty neutral.

And then ferrochrome prices, EUR 0.11 lower on average. And as you know, every EUR 0.10 is about $10 million a quarter. So there is about $14 million a euro effect.

Coming back to the import pressures. Already said that the temporary measures were not effective. And you can see this very clearly, where in 2017, on average, we had import penetration of about 27%, 26%. That has gone up to peak in the third and second quarter of '18 of 31%, and is still pretty high at about 30%. You see here, 28% for Q4, which is only up to November. We don't have the December numbers yet. We do have the feeling though that if you look into December and the month afterwards, January, that imports are trading off into the year.

Into the U.S., you see the opposite where we have gone from 22%, 23% import penetration, even 25% in '15, but take 2017, 22%, 23%. We have come down to about 19% for the rest of the year. So there we have seen a significant takedown of imports. What we do see, however, is currently that the imports are on the rise again. Then, of course, we have significant effect on the pricing, already discussed that. You see here the pricing in Europe, Germany and almost dropped down. And when you thought that you were basically at the bottom in Q3, we had enough pushdown in Q4, which has persisted into the first quarter as well. In the U.S., we have seen prices tick up, as we saw before. And currently, we have a little bit of tick down, but stabilizing at the current levels in the U.S. as well.

Transactions, and I think this is important to see as well. Transaction prices have come down significantly due to the drop in the second half of the year of, first of all, nickel, but then towards the end of the year as well start dropping in ferrochrome. And as a result, as far as in the U.S., the alloy surcharge has been trending down for seventh consecutive month, which had a big impact on the volumes that we saw as the distribution sector was destocking their high priced inventory.

I have been complaining sufficiently about the temporary safeguards. And I think of the commission has been very open to listen to our criticism or our proposals for improvement, let's put it that way. And we have now, as of February, the permanent safeguards in place.

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And there are a number of very good things there. One is that the period on which the import quota are being based is 2015 to '17, which if you look at it were relatively -- '15 and '16 relatively benign import years. '17 was getting already pretty high, but the average would take down the quota significantly. The other thing which is good to mention is that the quotas are for the large exporters, representing 75% to 80% of the imports, are country specific. So the issue that we had were countries are jockeying for position and just trying to beat the quota barrier. That has now been replaced by a more manageable country-specific target.

And then last but probably the most important is that it is now calendarized, it's being measured on a quarterly basis. Whereas in the temporary measures, it was free for all for the whole quota for the whole period. So now the clock resets every quarter, any residual will carry over to next quarter, but still it's in far more manageable position and you will not have the whiplash that would come with the old system.

We expect, as you can see from the left graph, that the imports that were running at, let's say, about 400,000 tonnes historically, should come down to about 330,000, which is 20% down from the imports that we saw in '18. So a very high level of imports will come down. And we said this before, if you do the math on this, you will probably get to a import penetration share of 23%, 24%, even if you include the 5% reset that has happened in February when the new quota were announced.

Two more points. One is that there is potentially an increase of 5%, again in June. However, after we have intervened with the commission that is not necessarily automatic. We have argued that why would you have relaxation of quotas in line with market development if you don't know what the development is. So it will be reviewed in the revision period in June. And the same goes for Indonesia, Indonesia has been left out of the quota. The commission has put into investigation period first half of 2018, which is the only thing they could do on the WTO as the second half was not yet done. In the first half, Indonesia still was able to get under the radar screen and under the 3%. In June, they have already committed to looking at the period -- the full period of 2018 for Indonesia and then review the developing country status. And we know for a fact that for full 2018, both in hot rolled and on cold rolled Indonesia is comfortably above the 3%. So we expect them to be included in the quota as from July this year.

Chris, over to you.

Christoph de la Camp ***Outokumpu Oyj - CFO***

Okay. Thank you, Roeland. Good morning -- good afternoon, ladies and gentlemen. Moving to Slide #11, take a quick look at the group key financials. I think the first thing that stands out here, on the first slide, that our deliveries in the fourth quarter were very low. They were not only lower than in the previous 3 quarters, but also lower than the fourth quarter of last year. And this was driven partly by seasonality, of course, that we will see in the fourth quarter, particularly in Americas, but also because we found distributors having very high inventory levels going into Q4. And with falling prices for nickel and ferrochrome and therefore, lower pricing, there was quite a significant destocking effect that caused distributors to hold back and not buy as much as we were expecting and hoping.

So overall, a very low volume result in the fourth quarter. And that actually then also lead to us not being able to get beyond the deliveries in 2017. We felt just short of that, if you like, in the fourth quarter because of that very weak quarter.

If you go further down, the EBITDA is EUR 89 million, higher than in the fourth quarter last year, but obviously somewhat lower than the 3 quarters we'd seen prior to that in 2018, where we were around the EUR 130 million mark. I will come back to the key drivers behind that decline. Net income is still positive in the fourth quarter and positive for the year as a whole. But here in the fourth quarter, a further deferred tax asset booking of about EUR 20 million helped the results somewhat. So that was much lower than the previous years, but nonetheless we were able to take an additional benefit in the U.K. and Italy.

If we then move down, we saw the capital expenditure, and this is accounting rather than cash capital expenditure. Cash capital expenditure was lower, came in at EUR 104 million. So that's quite a high amount when seen against the CapEx -- accounting CapEx for the year as a whole. This was because a lot of the projects were completed at the end of the year, and hence quite a lot of backloading of that expenditure in 2018.

ROCE is still a little short of where we wanted to be. We were obviously targeting 12%. We were at 7%. We have some way to go there.

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And overall, staff headcount costs broadly flat. The increase in 2018 caused by the acquisition of the Fagersta in Sweden that became part of Long Products in Q2.

Moving on to Slide #12. You can see here, on the left, the development of our EBITDA in 2018. And I think certainly during the first 3 quarters, we achieved much more stability in our results. But the fourth quarter in some ways a very difficult and somewhat unusual as well due to some of the factors that we'll go through. The broad bridge items to get from the Q3 results to the Q4 results were, first and foremost, I think, deliveries where we saw, as I said before, significant destocking by distributors, and therefore significantly lower volumes than in Q3 in both main business areas. Both Americas and Europe struggled severely here, and in Long Products also took a hit on deliveries here. So across the board lower sales.

As we said before, lower prices did happen in the fourth quarter, but we managed to negotiate better raw material prices and costs. We also worked very hard on our product mix, particularly in Europe and that substantially offset the further decline that we saw during the fourth quarter in pricing. And there was a negative timing and hedging impact. And clearly, as you know, we saw a nickel and ferrochrome prices fall into the fourth quarter and that then led to this negative timing and hedging that we're seeing here.

In the fourth quarter, again, we did a significant amount of maintenance work in Tornio at the end of the quarter, about EUR 20 million impact there. That's the big block predominantly that you see on the cost side here. And then ferrochrome much stronger in the fourth quarter substantially, of course, helped by the payment of a reinsurance claim -- of an insurance claim, but also because of higher deliveries that we achieved. So those are the key items how we moved from the Q3 results to the Q4 results.

Let's take a look at each business area that we have in turn. So starting with Europe. I think the chart on the left shows -- gives a very good pictorial sort of indication of what happened during the course of the year with the high level of imports coming to Europe, that Roeland has already outlined, so the results are very much tracked, that is we saw high levels of imports coming in the second and third quarter and having a very, very strong impact on pricing. So here very clear reflected in the quarterly results. And the bridge item from Q3, again Europe heavily impacted by lower deliveries. That was one of the big pieces. We did manage to get an improvement overall in pricing and mix for the quarter in Europe. And in Europe, we also saw a little bit of -- compared to the previous period a negative on the timing and hedging. The Tornio maintenance costs I have already referred to; however, we also saw higher electrodes costs and higher -- other higher input costs in Europe in the fourth quarter and the third quarter as electrode, ferrosilicon, refractories, fuels were all more expensive.

And then in the other what we had here was a benefit from a German pension plan adjustment. So we spent significant amount of time during the course of the year working up on our pension obligations in Germany and rearranging some of the plans there. And that resulted in the fourth quarter in a small benefit that we were able to book to improve our results there. Overall, that was EUR 33 million for the quarter.

If we look at the Americas, the results was not so good. As you can see here, deliveries made a very large negative impact. We do have the seasonality in the U.S. anyway with 2 public holidays -- extended public holidays with distributor destocking being a common feature. But this year, it seemed to be unusually strong, so this had a significant impact through the fourth quarter. We also saw pricing, mix and margin effects come down, bringing the results down and the timing and hedging results had a big impact versus the third quarter. So overall, it was 0 actually in the third quarter, we benefited from about EUR 10 million positive timing and hedging impact which didn't return in the fourth quarter. And costs were slightly up. So that led overall then to result of minus EUR 22 million.

If we look at the Long Products business on Slide #15. Very good trend in development up to the end of the third quarter with a significant decline then in the fourth quarter, again, some destocking led to lower deliveries. We were impacted more so in the fourth quarter than in the third quarter by the effect of Section 232 in U.S., particularly on the imports of slabs and billets particularly that were moving from the U.K. into the U.S., which we had to absorb some of the tariffs that were relative to the previous quarters from smaller negative timing and hedging impacts and costs also went up. The biggest item here is the other blocks, and this is related to medical plan charges in the U.S. where we had a benefit in the third quarter that did not recur in the fourth quarter. But also in the fourth quarter, we saw a change in legislation -- pension legislation in the U.K. that forced us to take a EUR 3 million charge there. So the combined effect -- bridge effect is represented here in this block and led to that significant decline, that's the biggest contributor in the decline of

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the Long Products business in Q4.

And then we come on Slide 16 to the ferrochrome production results. Ferrochrome had a have very, very good production result. It was a record for the quarter. That's shown here, as you can see deliveries also went up. And that mitigated together with a small cost improvement, the decline that we saw on ferrochrome pricing. So overall, despite lower prices, we actually managed to mitigate that through better deliveries and better cost management. The big, big story, of course, in the fourth quarter in ferrochrome was the reimbursement of an insurance claim. This referred back to the furnage 3 outage, which we reported on extensively in 2017. And that caused us a lot of losses in 2017, and we successfully managed to get an insurance claim for that during the fourth quarter. So that was EUR 32 million that had a positive impact. So even if you take out the EUR 32 million insurance claim we would still have ended up the fourth quarter with a record results for the year. So overall, then a very stable underlying result for that business during 2018 and not just a stable but also a very, very good and strong result.

Then move on to the next slide, and to cash flow, which I think overall was a disappointment. You can see here the bridge of how we get from our EBITDA result and this is reported rather than adjusted EBITDA EUR 496 million to a cash flow before financing activity. So this is before we pay that dividends and bought back shares of minus 14. I'll start from the right here and talk briefly about the investing activities. This is our CapEx, but we also bought the remaining part the Fagersta business in Sweden that we did not already own. So that was a EUR 14 million cash out, if you deduct that, we actually ended up with cash CapEx out of EUR 215 million, which is well within the guidance that we provided of EUR 220 million for the year. So no big surprises there.

Then if we look at the EUR 170 million, this was made up predominantly, of course, interest costs, other financing costs associated with refinancing activities that we did during the course of the year. Derivative and hedging costs, there were some smaller tax payments that we have to make and we also have to make some payments to top-up pension plan and had to payout against accruals that were made against restructuring in the past. So that represents EUR 170 million cash out.

And then we had an increase in working capital of EUR 112 million. Now maybe just to go to that a little bit. If we look at it for the year as a whole, I think this is the area where we're most disappointed about because we were really aiming for reduction. But I'll explain what happened here. So the biggest thing is that the accounts receivable and the accounts payable actually generated cash. We saw lower AR at the end of 2018 versus 2017 and higher APs. What really increased during the course of the year was the overall value of our inventory. And here, we saw a small build in the overall volumes, as inventory that we keep at a very significant increase in the value of that inventory. So during the course of the year, we saw an increase in electrodes, ferrochrome, ferrosilicon, refractories, fuels. We also saw like-for-like, an increase in nickel and ferrochrome pricing. And all of that is reflected in the higher inventory value that we had. So the specific value with each tonne of inventory actually went up during the course of the year, which led to this increase in inventory and hence an increase in working capital overall.

This is an area that we will focus on, but probably next year. That's clearly, we cannot see so much -- this year -- sorry in 2019 this year. That's clearly, we need to try to get a inventory, a value down and this is the biggest goal for -- that we'll be targeting in 2019.

You can see on Slide #18, the development of our net debt and predominantly the working capital increase here led to an increase in the overall net debt, which ended the year at EUR 1.21 billion. The gearing, as a result of that increased to 45%. So in both areas the first increase in 3 years and also a pickup in the leverage on the right here of 2.6. There are things we will be doing around , inventory management, working capital management, more generally but we also have some non-business assets, land from previous mills in Germany that we'll be looking to monetize during the course of the year to push that level down significantly.

And with that, I'm going to hand back to Roeland to give more color about the Americas results.

Roeland I. J. Baan ***Outokumpu Oyj - President & CEO***

Thanks, Chris. Yes, so going back to the Americas, disappointing year for the Americas. But if you put it into perspective, then we have had operationally still a strong year, and we have had some headwinds that mitigated negatively those good performances from an operational point of view. So if you look at that bridge, first of all, deliveries were slightly up year-on-year. But it's a story of 2 different tales. The first half of the year was very strong in volumes, driven by, on the one hand, optimism around the Trump measures, both the

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Article 232 which led to a lesser imports, but as well the whole euphoria around the tax reduction which was full to boost the economy led to increases as well in commodity prices and in a restocking cycle which we wrote in the first half of the year.

Pricing and mix. And sorry -- and of course, the conference happened in the second half of the year where, as I said, 7 months of continuous falling of the alloy surcharge, volumes came down significantly to a very, very low level of 155,000 tonnes in Q4. If you look at pricing and mix, pricing improved. You saw that the $90 as I mentioned in one of the earlier pages year-on-year, but on the mix as well we have been able to put a significantly larger portion of cold rolled into our mix. So where we have been saying for a while now that we want to get rid of the low added-value product, especially black hot band and to a certain extent some of the white hot band and put more cold rolled into market, we have really succeeded to do that this year and have virtually eradicated any sales of the low and -- of black bands.

There was a slight positive on the timing and hedging, but then the very big negative comes from the freight cost about EUR 30 million and then other inputs another EUR 10 million plus that we have not been able to fully offset. And then as a bitter fact we had last year a release of EUR 6 million in accrual, which does not repeat and that brings us just below breakeven.

So operationally, actually a stronger year than 2017. Result wise, you can't see that because of the increases in the input costs.

So a few points there that I do want to keep on hammering. Our operational performance there is excellent. We have clearly the lowest cash conversion cost per tonne in the group coming now out of the Americas. We are still working on the last stages of the restructuring in Mexinox and the reliability of the plant is really, really good. So where it has been probably most disappointing is that we have not been able to commercially fully take advantage of the opportunities that were in the market. And secondly, we have made a judgment error in the second half of the year where we were expecting higher volumes than actually materialized. By the way, you can see that as well, our volumes dropped but our market share stayed at the same. But this has led to a lot of inventory bought to cater for a market that wasn't there. And that is part of the story of the higher inventories that we had, with the higher inventories in the U.S. versus lower inventories in Europe.

So in Q4, we said we'll do a deep dive. We have put up a task force combined of European group and the Americas management team and the rest of the team done a deep dive, come up with a number of improvement areas that we are going to tackle specifically around the supply chain area. And I come back to a few of the specifics. And we have decided to strongly strengthen our commercial capabilities. We have taken our lead from the commercial leader in -- that we had in the Americas Steve Letnich. And we have as per 1st of January Olli-Matti Saksi, the Global Head of Commercial and the architect of our European commercial success. He has moved to the U.S. and he is now taking charge of both the sales side as well as the supply chain side in the Americas.

His mandate is clear. Is fix a number of the issues that we found in the supply chain and supply chain interface with sales was a sort of [SNLP] process, fix those, reorganize the sales site as well, beef up the capabilities and start avoiding the leakages that we have seen in 2018.

And the last point, we have, in December, we brought an investment proposal to our board to do a significant investment in ferritics capability for about EUR 40 million price tag that had been approved. We already have placed our first POs. We are in vendor selection. We have reserved production capacity. We have pushed some of the long lead time items. And we are going full steam ahead with an investment in order to unlock the 37% of the market that currently we cannot reach because we do not have the ferritics capabilities.

So those are the specific actions that we have for the Americas. And I'm happy to answer more questions about that as we get into the Q&A.

That brings us to the outlook. The stainless steel market is expected to remain changing due to high inventory levels and especially, if you look into Q1 that has -- is still there, that's destocking still taking place. Stainless steel deliveries of course, are expected to be higher than the fourth quarter of '18. But Americas performance, we expect to remain weak. Firstly, because still volumes were not returned to the same levels as we have seen in other Q1s but as well because of, as I said earlier, the overhang of raw materials of input materials that we have bought at relatively high prices will depress the result in Q1 as it works its way through the production cycle.

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And something that everyone, of course, has already seen is that the lower ferrochrome benchmark price will lead to lower ferrochrome price as a result. So we expect the adjusted EBITDA for the first quarter to be lower than the fourth quarter. So lower than EUR 89 million.

Tommi Järvenpää ***Outokumpu Oyj - VP of IR***

Thank you, Roeland. Operator, we are now ready for the questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from the line of Seth Rosenfeld.

Seth R. Rosenfeld ***Jefferies LLC, Research Division - Equity Analyst***

Just a couple focused on the U.S. business. And I recognize, you've already spoken about this some, but I think that everyone in the call would appreciate a bit more color. Given what appears to be an inability to make attractive returns even during the time of unprecedented trade projection and with very high base prices, I think investors are very concerned about the ability of Outokumpu to make this asset work. Can you perhaps walk us through some of the past initiatives you talked about on past conference calls, is freight improving? How much has been mixed enhancements actually improved your margins? Why was there such discrepancy in your cost base in the back half of the year, following up on the discrepancy in contract basing the first half of the year? And ultimately, are you considering not retaining this asset and selling it to another operator, who might have a better foothold in the U.S. business right now? I'll start there.

Roeland I. J. Baan ***Outokumpu Oyj - President & CEO***

It was a good start, Seth. So if you look at -- the broader question, will we be capable of making this asset a profitable one. I'm sure we can. We -- the first step we had to do was bring this asset operationally to maturity, and we have succeeded in that without -- literally without fail. So we now have an asset that is operating well, that is turning out quality product in time and exactly what the customer wants. Customer response is very positive. We still see our share in the high end of the market growing, especially if you look at appliances where we have taken a major share of wallet. So we are moving very well operationally. Where we have failed to really capture the value that you said yourself, unprecedented protection. You have seen the results of other operators in the U.S. market, the unprecedented protection has not really resulted in unprecedented returns, not for us, not for others either. So there are other area elements that played a role there as well. But we have made mistakes. We have, in the first half of the year, not captured a lot of the price increases, as you know, because we eagerly contracted in December at extremely low prices and missed actually the run up of pricing after 232 went live. In the second half, I don't think we have missed that much commercially in terms of sales or capturing pricing. But what we had wrong there is our forecast on the sale in the market. Again, we are not alone in that. But it does hurt, and it hurts because you have these high inventories that will have at high prices, that will have to work that way through the system. So I would say a lot of that is self-inflicted. If you look at some of the initiatives, freight, we are getting the freight cost down. We have moved into renting a warehouse in the Midwest. We are now bringing motor coils in there and distributing by barge and distributing from there that will help. We're putting much more on the rail and using less truck. We are renegotiating truck products. So I expect that aspect to improve. I expect not that there will be a full mitigation because the stock market and the freight market remains tight. And again, that's a general issue. Let's see what are the -- yes, so I think those -- all those points address the 4 points that you had. So if there is anything else, just go ahead.

Seth R. Rosenfeld ***Jefferies LLC, Research Division - Equity Analyst***

I think just one last follow-up on the U.S. business. It seems like last year when some extreme weather impacted your ability to access raw materials. There was a bit of talk about whether or not the company in past year has a very aggressive working capital management and actually -- perhaps cut working capital a bit too tight. Recognizing the challenge in late 2018 to manage working capital, is there any question of whether or not there's a structural challenge here where you have to rebuild inventory just to operate on a normal basis? Or do you really think it's the temporary Q4 phenomenon because of apparent customer demand?

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Roeland I. J. Baan ***Outokumpu Oyj - President & CEO***

Yes. This has nothing to do with the structural necessity. We are over inventorized. We are sitting at inventories of over 100 days in the States. Whereas at the end of -- the contrast to Europe where we are below 80. So if you take that whereas the Europe is a more complex business, more different products, more different inputs. So clearly, we have a lot of leeway there. And ultimately, if you look at the disappointing cash return that we have had in 2018 that links very much into our performance in the Americas business. And specifically on how much working capital we have been building, specifically in the Americas. The good news is that we can take it out again, but it is still disappointing that it happened.

Operator

Our next question is from the line is from Luke Nelson.

Luke Nelson ***JP Morgan Chase & Co, Research Division - Research Analyst***

Couple from me. Firstly, just on Q1 deliveries that you've guided to be high in Q4. Can you just give us a sense of what sort of delta that will be relative to normal seasonal patterns? And secondly, just the comment on hedging and timing effects, the sort of level of that, that will continue to flow into Q2 and beyond? And then my final question, just on the balance sheet, given the guidance commentary around EBITDA, sort of rough calculations get to over 3x net debt to EBITDA as of the end of March on the last 12 months basis. So I'm just trying to build a bridge to your year-end '20 target of less than 1 times. And as things stand, absent a big -- a material change in stainless pricing. I'm struggling to get this. So maybe just to -- again to just highlight what of that is you're assuming in terms of market versus internal measures and maybe some high-level sensitivities around the balance sheet that have changed in top-line pricing.

Roeland I. J. Baan ***Outokumpu Oyj - President & CEO***

All right. So I will take the deliveries. Chris will talk more about the hedging and the balance sheet questions. Deliveries, specifically in the U.S. where the drop-off of the surcharge went still all into the first quarter. We expect there is relatively low for Q1, relatively lower deliveries. Definitely higher than Q4, but lower than what you would seasonally expect. Europe is more in line with what you would seasonally expect, slightly lower but not that much. In general, and I think that is important, we do not see the underlying markets change. We do have -- we do -- if we talk to our direct customers, we do have good direct demand. There is -- there are no big negatives on the horizon. We don't see any of our segments grinding to a halt. Automotive, as we have said before, has been slow. It's not slowing down further. We see some crewing shoots here and there. So I'm not that concerned on deliveries going forward into the year.

Christoph de la Camp ***Outokumpu Oyj - CFO***

On hedging and timing in Q1, we still have quite a bit of inventory that was produced on the higher nickel and ferrochrome prices last year. So we will see negative timing effect in the Americas as a result of that work and space of the system. In Europe, we have rather less inventory left at high inventory costs, so we expect the results from hedging and timing to be not particularly negative at this stage. On the hedging, it all depends a little bit because obviously, hedging is very sensitive to the movement of prices. So generally, we had certain hedging positions which we can offset to underlying positions, to a large extent. But generally, hedges tend to -- if you just -- tend to be mark-to-market. So in a rising environment you tend to have a negative hedging effect, offsetting your underlying gains. In the falling nickel environment, you tend to get a gain. At the moment, we're seeing nickel prices go up. They've gone up quite significantly since the beginning of the year. So generally, we would expect a little bit of a negative hedging result for the quarter if prices remain at the current levels or continue to go up.

Moving on to the leverage question. I think very clearly the answer to your question is yes. Leverage will move up in the first quarter. There'll be 2 key drivers behind this. The first is that there has been an introduction of a new accounting standard IFRS 16, which requires leases to be put on the balance sheet as pure debt. That has an impact on our overall net debt position of EUR 130 million. It's not a cash debt, if you like, but it will have an accounting impact and we count as part of our net debt going forward. So that will drive up the overall net debt position. Just as a result of that change or the implementation of that new IFRS standard and also we typically see an increase in working capital in the first quarter. So fortunately, we're seeing a pickup in deliveries from the fourth quarter so that will pick up AR. We should be able to see an increase in payables that will help. But at the moment, we're also seeing our inventory value increase a little bit as nickel and ferrochrome -- nickel prices in particular going up that will be reflected. So overall, we expect as a result of better business, we like higher volume of business and higher nickel prices potentially the net working capital to go up. And those 2 will be drivers for a high net debt position at the end of Q1, and therefore a higher leverage as well.

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So to recall the last question, I guess is -- and how do we then push it down to get to a lower leverage and the target that we set ourselves for the following 21 months or so. Clearly, structurally, we need to work. We're putting in place a program to work on structurally getting our working capital levels down, but that is, in particular, our inventory levels. It will address some aspects of our payment terms as well. And as I said earlier in the call, we have in the past had assets in Germany that have been sitting on land that where we have closed the assets. That land has been refurbished to some extent and can be sold and it's not an insignificant amount of potential cash in. So we're expecting significant boost to reducing our net debt from some of that. And the rest will have to come from better EBITDA through 2019 and '20 as we're expecting as mentioned by Roeland before.

Roeland I. J. Baan *Outokumpu Oyj - President & CEO*

And maybe just one extra remark because -- so we have -- as you know, the way we work our strategic cycles in the company, we have our vision for 5 years, and then every year we have a specific mission. And we shared these missions in the past with you and what they are. In every year's mission puts a plus for me to jump on for the next year. For this year and this was set already back in December, the mission is concentrating on just one single item and that is to bring down net debt. So the focus of the company for 2019 is to aggressively work on a reduction of net debt. And there are a number of levers that we can talk about but that is what the whole company is geared to doing.

Operator

(Operator Instructions) Our next question is from the line of [Sandeep].

Unidentified Analyst

I have couple of questions. One on maintenance CapEx. So do you -- so your maintenance cost that was in Q4, do you expect the same going into 2019? And second question is, what are your expectations on working capital for the full year 2019?

Roeland I. J. Baan *Outokumpu Oyj - President & CEO*

So I'll put to Chris. CapEx, that's just seasonal, Sandeep. So in Q4, in the Nordics, we just closed down and do the bulk of our maintenance. Our maintenance -- typical maintenance budget CapEx for the year is EUR 60 million to EUR 80 million and that was the case in 2018 and it will be the case in 2019. Chris?

Christoph de la Camp *Outokumpu Oyj - CFO*

Yes. On the working capital, the -- there are things that you can influence in terms of reducing your inventory levels, the quantity of those and on your payment terms both with your customers and your suppliers. On that basis, we are targeting to get the working capital down -- underlying working capital down by 10% to 20%. However, let me qualify that, if nickel or ferrochrome shoot up and move to much, much higher levels that would be an offsetting effect. And there comes a point where you can no longer reduce your working capital levels without significantly impacting your operations. So this is on the assumption that raw material prices stay, broadly speaking, the levels that we have seen recently. There is a significant jump and that would have an impact. And I cannot tell you where those are going to end up. But on the assumption that we're going to see a broadly similar level for raw materials, we should see a 10% to 20% reduction of our working capital.

Unidentified Analyst

Just one follow-up question. So we saw Tornio maintenance shutdown during the Q4. So is this a regular occurring event or how should we think about it?

Roeland I. J. Baan *Outokumpu Oyj - President & CEO*

That's yearly event. It happens every year. Last year, it was there. It was actually slightly more cost about EUR 30 million. This year, it was EUR 20 million. So it is a yearly event.

Operator

Our next question is from the line of Cedar Ekblom.

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Cedar Ekblom ***BofA Merrill Lynch, Research Division - Analyst***

Just some follow-up questions on the U.S., please. So first of all, on the release, you said that there's been a misalignment between sort of the production and the sales function. And can we interpret that as your sales team is battling to get the right orders in order to run the mill efficiently?

Roeland I. J. Baan ***Outokumpu Oyj - President & CEO***

No. What it is here it's easy to one question at a time. What it is, is that, as I explained, our sales forecasts were far higher than the -- what came out ultimately because of the significant drops on the -- in the alloy surcharge. And as you know, 80% of the market is distributors and distributors speculate. If they see prices go up, they restock. If the alloy surcharge comes down, they get a hell lot of dodge and they destock. So there was significantly lower than forecasted sales volume, but we have meanwhile both in the raw materials for the forecasted sales volume and that's -- this connector was there. There was no process to timely have the feedback loop to stop the further buying process. And as a result, we have built too much, too high priced inventory in raw materials in the U.S.

Cedar Ekblom ***BofA Merrill Lynch, Research Division - Analyst***

Okay. That makes sense. And then just a follow-up on that question. Is there any in read across in terms of ATI ramping up into the stainless market in the U.S. that we should sort of infer that that's also part of the reason why potentially you are moving volumes not as quickly as you would think? Or was it -- is it just a destocking issue at distributors?

Roeland I. J. Baan ***Outokumpu Oyj - President & CEO***

As our market share has actually increased, that cannot be the issue.

Cedar Ekblom ***BofA Merrill Lynch, Research Division - Analyst***

Okay. And then the last question, you're talking that you're quite hopeful that the safeguards in Europe will have a meaningful impact on improving the supply-demand balance. Just in terms of what happened -- has happened in the U.S., we've obviously had trade protection in place in the U.S. for nearly a year, and we've had steel prices go up and then go down, essentially round flipping. When we look at the European example, is that the fact that you're confident because the mechanism is different in Europe in terms of a quota rather than the tariff as it is in the U.S.? Or why having looked at the U.S. not being that effective on the safeguards or when import barriers basis actually resulting in price increases, why do we have the view that in Europe it's going to be a significantly different outcome?

Roeland I. J. Baan ***Outokumpu Oyj - President & CEO***

I think the -- there are a few differences. First of all, the U.S. is -- as I said, is a very high priced market. So it's open to arbitration, whereby if you look at in Chinese market and the European market which, at the moment, by the way, are almost at similar levels. And there is much less arbitration possibility. So you virtually would not be capable of absorbing as an exporter, absorbing the 25% tariff beyond the quota. So it is much more likely that the import into Europe will be limited to the quota. Don't forget the flipside of the low pricing in Europe is that some of the European producers are becoming much more competitive with the Asian imports. In other words, the door is relatively closed to Asian imports on a net back basis. Whereas to U.S., you have the arbitrage where you could, in some cases, you even paid the 25% and still net back more than when you would probably put it into Europe.

Operator

Our next question is from the line of Bastian Synagowitz.

Bastian Synagowitz ***Deutsche Bank AG, Research Division - Research Analyst***

I have got, firstly, one question on the inventory situation, which you outlined on the U.S. I guess, what you say is you're running too much high cost inventory here. That means that there should be a lot of scope to release inventory from this asset alone, but then you're telling us that working capital is going up from an already high level in the first quarter. Could you please quantify this extra effect of inventory. And then also, how long do you expect for this inventory direct on your cost structure to unwind? Is this something which actually is dragging into the second quarter alloys or something which you will be have fully absorbed in the first quarter? That's my first question. And I have one more, but I will stop here.

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Roeland I. J. Baan ***Outokumpu Oyj - President & CEO***

All right. So I would say that the bulk, 90% will be absorbed in the first quarter. It's still small bit that goes into the second quarter, but the bulk is gone. So the other end where you say, okay, but how do you then explain it to the increasing working capital. That has a lot to do with as well the inventory in Europe, so the European inventory, as Chris said, has got rid of the more expensive stuff. So as now the nickel prices go up and with that potentially our input prices then you will see a rise there.

Bastian Synagowitz ***Deutsche Bank AG, Research Division - Research Analyst***

Okay. And -- but could you quantify the effect from essentially this additional inventory load in the U.S or is it actually not that meaningful in terms of actual value, it's more meaningful in terms of cost?

Roeland I. J. Baan ***Outokumpu Oyj - President & CEO***

It's not that meaningful in that sense. No.

Bastian Synagowitz ***Deutsche Bank AG, Research Division - Research Analyst***

Okay. Okay. And could you able to quantify the impact on your Americas numbers in the first quarter. I mean, is this like -- it like a EUR 10 million or EUR 20 million number or is it actually less than that?

Roeland I. J. Baan ***Outokumpu Oyj - President & CEO***

It's, let's say, EUR 10 million to EUR 15 million.

Bastian Synagowitz ***Deutsche Bank AG, Research Division - Research Analyst***

Okay. Okay. Okay. And then just again on the balance sheet and also on your cash flow. Chris, probably one for you. Could you please quantify the amount of non-cash assets or the amount of assets which you aim to monetize in the course of the year? I think you mentioned that earlier. And then secondly, I think you have been guiding for cash requirements of around EUR 320 million to EUR 330 million in the last calls, I think you confirmed that at some point. Now if I look at the waterfall bridge, you have been spending around EUR 220 million on CapEx and then another EUR 170 million for taxes, which means we would actually be much closer to EUR 400 million. You mentioned there was some one-off items in there. Could you please quantify those and maybe also just update us again on what the actual cash needs are?

Christoph de la Camp ***Outokumpu Oyj - CFO***

Yes. We would stick to about the EUR 330 million, EUR 340 million. I have talked about in the past. Let me just come back to your first point on disposals. I mean, the assets that we have on our balance sheet are very significant double-digit amount, right, high double-digit, millions. So to see if it's sort of indication of where we are, that's what we're targeting for disposals. In terms of the other items, our interest costs makes the -- or this year will be lower because we obviously did some refinancing activity between 2018 and that only had a half year impact. We'll have a fuller impact in 2019. So that's going to be lower interest costs. The guidance for EUR 220 million of CapEx spend, so that's the same. We did have some one-off costs in financing during 2018. For example, the refinancing of the bond was one that came into there, and we also did some work around CO_2 emissions. So what happened here was that we had derivatives in place for the requirements -- actually excess requirements on CO_2. Those -- we exercised and then converted them into physicals during the course of the year. We sold the excess of significant profit and that's reflected in the EBITDA, and we discussed in the previous quarters. And -- but we still retain some of them. So we have, if you like, pre-board our CO_2 requirements for the next 3 years that are now sitting on the balance sheet. And that should also help and that is also in the one-off costs that will not repeat in 2019 and beyond. And also, in addition to that, I should add, we do have small tax payments. We always said they are low, but they are there. In some countries, we have minimum taxes. And we are in the taxpaying position countries, such as Mexico. And we have minimum taxes in Germany and the U.S. And then the other item is that we have to fund, in particularly, in the U.K. a pension deficit as well, which was in aggregate of about EUR 20 million.

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Bastian Synagowitz ***Deutsche Bank AG, Research Division - Research Analyst***

Okay. Just on the CO2 component, which you mentioned, could you just let us know roughly how much that was? And I think just -- I would have thought -- and sorry for my lack of knowledge here. But I would have thought if you buy CO2 credits for future period, you would basically capitalize those i.e. it's basically an asset swap but you wouldn't expense those, but it's easily been just -- so you -- or you don't carry them in cash equivalents is basically the answer?

Roeland I. J. Baan ***Outokumpu Oyj - President & CEO***

No, you don't have them in cash equivalents, but to buy them you have to -- sorry, I thought you meant the cash out you have to. Finally, we have to pay cash to buy them. So that's in the block that you see there of the EUR 170 million. So because we have a surplus, when the price went up we sold cash. And the cash-in from those sales is reflected in the EBITDA number. So it will be to purely cash here and not accounting.

Operator

Our next question is from the line of [Charles].

Unidentified Analyst

My question is a point of clarification regarding the outlook for Q1 and the guidance. So obviously, in Q4 '18, the EBITDA, excluding the insurance claim is about EUR 57 million. With the commentary that you provided to us, it sounds like Q1 is going to be relatively soft. So we understand the guidance for EBITDA in Q1 to be lower than $57 million or lower than $89 million?

Roeland I. J. Baan ***Outokumpu Oyj - President & CEO***

We guide for Q1 lower than in Q4 and Q4 is $89 million.

Operator

Our next question is from the line of Luc Pez.

Luc Pez ***Exane BNP Paribas, Research Division - Stock Analyst***

Two remaining questions, if I may. I hope you can hear me well. I'm losing my voice. So first one on the ferrochrome, which prices now only under $1 per pound and maybe some risk into the Q2 benchmarks. Aren't you afraid that this maybe a headwind into your results and ability to reach the 2020 target. And second question related to that. Is there any room for you to rethink the timetable for the investment at Kemi expansion honored? And the last question with regards to the CapEx guidance for '19. I'm not sure I got the answer right, it was asked before?

Roeland I. J. Baan ***Outokumpu Oyj - President & CEO***

All right. So the ferrochrome benchmark was set at EUR 1.12. When the prices in China were around EUR 0.80. They are still around EUR 0.80, EUR 0.81, EUR 0.82. So there is absolutely no reason to think that it will go lower. In the end, look, I think the most important thing here is, we are in the top 10% of most efficient ferrochrome operations. So at the sort of EUR 0.80 that you see in China, over 50% of the market is losing money, cash. So the likelihood that it goes lower is extremely low. I mean, everything can happen, but it is very unlikely. Holding the Kemi investment, that will be shooting ourselves in the foot because it's not to expand the mine, it is to make sure that we are into the next layer of the seam so that we can maintain production beyond 2023. If we do not to that, you will see the ore production taper off. And then by the time you are then ready to restart your mine production or your mine expansion, you would run the risk that you do not have enough ore available anymore to feed the smelters. So as you can see from the results, the return that we have on ferrochrome is extremely attractive and although EUR 250 million is a high investment, the payback time of it is about 1.5 years.

Luc Pez ***Exane BNP Paribas, Research Division - Stock Analyst***

CapEx '19?

Roeland I. J. Baan ***Outokumpu Oyj - President & CEO***

EUR 220 million is our guidance there.

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Operator

Our next question is from the line of Harri Taittonen.

Harri Taittonen ***Nordea Markets, Research Division - Senior Director & Sector Coordinator***

Couple of quick questions. It's been a long call already. On the impact from the European safeguarding measures, I was wondering is this sort of the final decision or is the industry possibly still kind of working to amend the continuation and the implementation of the measure, that's one thing. And then the other question is about the sort of the volume outlook, I know that destocking has been a key driver for deliveries to go down. But as you said, nickel prices have been moving up. And can you see a scenario in which sort of higher nickel prices would start to trigger opposite direction in the inventory cycle? Those 2 questions, please.

Roeland I. J. Baan ***Outokumpu Oyj - President & CEO***

So safeguards, and don't get me wrong if I haven't -- if I gave the wrong impression. We are actually very satisfied with the safeguards. We do think that they will make a substantial difference in the market. We have put our -- all our thoughts into the commission and the commission has taken 90% of them into the design of the new safeguards. The only thing left, as far as I'm concerned, is Indonesia. Now don't forget Indonesia is relatively unimportant at the moment even though they are very high in their imports into Europe. It is like hot band and there is only one customer for it, and no one else re-rolls. So and it doesn't change the market. There is the one re-roller that somebody has access to more material from Indonesia. Cold rolled is still negligible in terms of the imports into Europe and as well as in terms of capability of Indonesia. And then the second, I can't even read my own handwriting here.

Harri Taittonen ***Nordea Markets, Research Division - Senior Director & Sector Coordinator***

Scenario in which there is sort of nickel prices which have been moving up and is that sort of in any way..?

Roeland I. J. Baan ***Outokumpu Oyj - President & CEO***

We can clearly see volumes improving. If we look at the order book, we see our order book is currently full until April. And so we see a stronger order book. We see as well stronger pricing coming in already. So that bodes well for the future. And as I said, with these, if you just take the mathematical numbers, imports would drop to about 22% -- 23% of consumptions versus the 29% that they were. So yes, I think, this will be very supportive.

Operator

There are no further questions at this moment, sir. Please continue.

Tommi Järvenpää ***Outokumpu Oyj - VP of IR***

Thank you very much for attending our earnings call. As a reminder, we will host a site visit to Calvert on April 2. More details can be found from our website. Hope to see many of you there. And our first quarter 2019 results will be published on May 7. Until then, thank you, and goodbye.

Operator

So that does conclude our conference for today. Thank you all for participating. You may all disconnect.

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