



C: Dr. Rolf Breidenbach; HELLA GmbH & Co. KGaA; CEO and President
C: Bernard Schäferbarthold; HELLA GmbH & Co. KGaA; CFO
P: Christoph Laskawi; Deutsche Bank AG, Research Division - Research Analyst
P: Henning Cosman; HSBC, Research Division - Analyst
P: Raghav Gupta-Chaudhary; Citigroup Inc, Research Division - Analyst
P: Christian Ludwig; Bankhaus Lampe KG, Research Division - Analyst
P: Julian Radlinger; UBS Investment Bank, Research Division - Equity Research Analyst
P: Manuel Tanzer; Pareto Securities, Research Division - Research Analyst
P: Sascha Gommel; Crédit Suisse AG, Research Division - Research Analyst
P: Jüergen Pieper; Bankhaus Metzler, Research Division - Research Analyst
P: Ralf Stromeyer; Allianz Global Investors

COMPANY EDITED TRANSCRIPT

Operator

Thank you all for standing by, ladies and gentlemen, and welcome to today's HELLA investor conference call. (Operator Instructions) Please be advised the call is being recorded today, on Friday, 11th of January 2019.

I would now like to hand the call over to your speaker, Mr. Bernard Schäferbarthold, CFO. Thank you. Please go ahead.

Rolf Breidenbach

Yes, good morning, ladies and gentlemen. This is Rolf Breidenbach speaking. First of all, allow me to wish you a Happy New Year. I hope you had a good start into 2019. Also on behalf of our CFO, my colleague from the board, Mr. Schäferbarthold, we both would like to welcome you here to the HELLA investor call on our half year results.

Before I lead you through the highlights of our first half financial figures and before Mr. Schäferbarthold will give you an overview about the financial results in detail and I comment on the outlook, allow me at the beginning of this call to make some general remarks with regards to the -- to our industry, the development of our industry in the last months, our perspective how it's -- how this development will go on in the future and about the general positioning of our company.

First of all, I think it's fair to say that the 6-months period that lies behind us has been very dynamic compared to our last investor call end of September. And I remember the intensive discussions about the sales development, growth perspective and so on. The environment for the entire automotive

industry has become even more challenging due to several reasons. First, we are facing a general decline in the globalizing vehicle production. Second, and this is from our perspective even more important: especially China, one of the most important markets, is currently recording negative growth rates for the first time in decades, so a totally new situation. Third, the transformation of the entire automotive industry towards major market trends like autonomous driving, electrification has to be driven forward resulting in even higher R&D expenses. And fourth, on the costs side, and we also discussed this in the last investor call, we continue to see a general increase in labor and material prices worldwide. So from the HELLA perspective, a real challenging and very dynamic market environment.

And despite this very demanding environment, we continue to anticipate a positive business development for the current fiscal year 2018/2019 and confirm our current company outlook assuming that the auto market will not suffer any additional weakening in the second half of the fiscal year.

What does this mean in detail? For the whole fiscal year 2018/'19, we expect that our currency- and portfolio-adjusted sales growth will be at the lower end of the given forecast range from 5% to 10%. Concerning the earnings and before interests and taxes, adjusted by restructuring measures and portfolio effects, we expect that the adjusted EBIT will be in the lower half of the given forecast range from also 5% to 10%. And with regard to the adjusted EBIT margin, we still expect a value approximately equivalent to the value of the prior year. And this means we are slightly more confident with respect to our future EBIT development. This, of course, has a lot to do that we have more possibilities to impact the EBIT directly with a very consistent cost control program, for example, which we have already implemented and which works, from our perspective, very positive.

Looking to the next quarters in more detail, we expect the following development, and this, of course, is also included into our guidance. Q3 will be very challenging. We expect that the headwind from the market will continue to increase in the months to come. Thus, we clearly see a further decline of our sales growth in Q3, especially the Chinese market will be very challenging. This is, from our perspective, absolutely clear. Of course, we talk to the different forecast institutes, but also, we -- of course, we talk to the Chinese officials, to our Chinese managers, and it's absolutely clear. Especially until Chinese New Year, nothing will change. And also after that, for the first quarter, we are not optimistic with regard to the development of the Chinese market. For Q4 of our fiscal year, we at least see a kind of stabilization for the growth dynamic worldwide. Assuming that the automotive market will not suffer any additional weakening in the second half of the fiscal year, we therefore anticipate in total a quite positive business development for our fiscal year 2018/'19.

Looking beyond this horizon, let me also stress one point. Despite all temporary market challenges, the overall HELLA strategy still is valid, and we will follow this strategy with no compromises. So we are innovation leader in many areas and we are benefiting from major market trends like autonomous driving and electrification, and therefore, we will continue to invest into these areas. We are globally positioned with a strong product and development footprint in all major growth markets, and we will continue, of course, to strengthen our global footprint. For example, we -- in the last 6 months, we opened our activities now in Lithuania for electronics. The same is true for Mexico. And this kind of strengthening of our global footprint will go on.

We have a strong focus, of course, at the same time, on operational excellence as well as on stringent portfolio management. And I think it's fair to say that we have a proven track record and an effective cost control management, something which is, especially in these times, very important.

Yes, having said this, as a kind of introduction into our investors call, allow me to comment on the results of the first half of our fiscal year. Our currency- and portfolio-adjusted sales increased by 7.3% to EUR 3.5 billion in the first 6 months. This is mainly attributable to the following aspects. On the one hand, the Automotive segment once more has been the main growth driver and supported our group-wide sales increase. On the other hand, profit from our international presence in core markets of our automotive industry in North, Central, South America, for example, we achieved a significant sales plus, which compensated regional market volatilities so far.

With regards to our results. Our adjusted gross profit margin improved by 40 basis points to a level of 28%. And this shows also that with regards to our, let's say, cost control program, we are quite effective, let's say it in this way. Our adjusted EBIT improved by 5.5% into EUR 302 million. And thus, our adjusted EBIT margin is now at a level of 8.6%., so more or less at the same level compared to the previous year.

We are also -- or we continue to be satisfied with the development of our free cash flow. Our adjusted free cash flow from operating activities increased by EUR 45 million now to EUR 152 million. Of course, we increased our adjusted net CapEx by around EUR 30 million. But for example, our working capital consumption decreased by around EUR 70 million, our trade payables increased by EUR 176 million, so we feel quite comfortable in handling our working capital and, yes, continuing the improvement of our cash performance, which I think you all know this is a special topic of our CFO. And he is here deeply and personally involved into that.

To sum it up, I think all in all and against the background of a challenging market environment, we are quite satisfied with our half year results. However, of course, it's also important to mention that we saw a decreasing growth dynamic in the second quarter and of course, this will also continue for the third quarter, what I already mentioned.

With regard to our adjustments of our growth performance, allow me to shortly comment on Page 5. You see the reported growth is now at a level of 2.8%. This, of course, is related to the sale of our of our wholesale business. Our adjusted growth rate is at a level of 7.3%. And as I said, of course, this is a mix of our high growth in the first quarter and the reduced growth of the second quarter of our fiscal year. The adjustments with regards to FX are in the first half year very limited.

Yes, with regard to the different segments. As I said, the Automotive segment is and will remain, of course, a growth engine. 8.1% was the growth rate in the first half of the fiscal year, especially, on the one hand, the demand for advanced lighting systems but also for our energy management products and radar solutions were main reasons for this performance. But also, the development of our Aftermarket business, knowing, of course, the different market dynamic at a level of 4.5% is, from our perspective, quite satisfying. And the same is true for Special Applications. You know we have closed a plant in this area in Australia. It was the OE plant. It was reported in the sales figures of Special Applications. Without this effect, we also see a very, let's say, - solid growth rate of around 6.2% in our core Special Application business. So overall, all the different segments contributed to our growth performance, which, of course, is good and makes us quite positive also for the months and quarters to come.

At Chart 6 you, as always, can see how we performed with regards to growth rates in the automotive sectors compared to the market. Overall, we were able to outperform the market in the first half of the fiscal year by around 10.6%. Especially the outperformance in Europe and North and South America is at a 2-digit level, 11.6%, and in -- yes, both in North America and in Europe. In Asia, we at least were able to grow stronger than the market by 6.8%, yes. So overall, we could achieve our target to, of course, significantly grow faster than the different markets. And yes, this also shows that, in the end, the business model of HELLA works and that we can make a difference with regards to our growth performance compared to the market development.

Yes, having said this, allow me now to hand over to my colleague from the board, our CFO, Mr. Schäferbarthold, who will give you more details about

our financial results for the half -- for the first half of our fiscal year 2018/2019.

Bernard Schäferbarthold

Thank you, Mr. Breidenbach. Also from my side, good morning. Before jumping into the presentation on Page 8, please allow me also some initial remarks to our half year results and also the outlook.

First of all, to the result, I have to say that overall, we are pleased with the outcome. It's in line what we internally also predicted when we talked last time some months ago. It's a little bit different. If we look at the regional distribution, we have seen slightly better performance in North and South America for us. On the other hand side, China was by far worse than our expectation. Overall, the predicted slower growth in total was roughly at the amount we predicted for Q2.

On the results, especially on adjusted EBIT, what really was good is that we see that the cost control programs we already started at the beginning of our fiscal year shows that we are able to stabilize overall the result. And also what is good that with these efforts, we also have been able, so far, to compensate also higher personnel cost and also material cost as of end of November.

On the other hand side, we were more positively 3 months ago if it comes to Q3. There, especially the market reduction will have also an impact on our growth in Q3. As Dr. Breidenbach said, we do not expect before Chinese New Year, which is in the second week of February, that the market in China will change, and so that impacts our Q3, which ends end of February. For that reason, we predict even a slower growth compared to Q2 in terms of total sales, where, if we look at numbers, it could even be at the end flat if we compare to previous year.

Q4, we then expect certain normalization especially coming out of all 3 regions if we look at overall market expectations and also our feedback from our management in the different regions. As said, on EBIT, on adjusted EBIT, we continuously intensively work on our cost control measures so that we are more optimistic also in our margin expectation so that this substantiating guidance we have given we feel more comfortable because there we have also a lot in our hands really to influence that.

Second remark comes to -- if we look at the numbers yet is that the wholesale business is now sold, so the vast majority now of this sale is reflected now in the numbers. Only our Norway business will be then shown in Q3 numbers, but these are no big numbers, so the biggest effects are now reflected. With that, we are showing a book gain of that transaction of EUR 255 million, which is then reflected in our reported EBIT numbers. This brings now our net

debt position more or less close to 0. And that is even including the finance lease position we have now taking in with the IFRS 16 implementation, where we have taken EUR 135 million of debt in our books.

With that wholesale transaction, we have also changed or adapted the reporting. If you look at the segmentation of our Aftermarket, so the numbers you will see are like-for-like. So from now on, without also in comparison to prior years, without showing wholesale numbers, so the like-for-like comparison is valid here.

So having said that, I will shortly comment on the slides, starting with Page 8. So on gross profit, an absolute improvement of EUR 75 million. All 3 segments contributed to that improvement.

In Automotive, we had positive volume effect. In addition, we also mentioned before several productivity measures which positively contributed to that growth. And with that, we were able to compensate, as mentioned, higher raw material prices and also an increase in personnel expenses. This trend will be difficult to hold especially with a slower growth I mentioned also in Q3. But overall, we're intensively continuing to work on that.

Also a positive is the trend in our gross profit margin in Aftermarket and Special Application. In Aftermarket, we have seen a positive product mix here, especially with higher sales in our diagnostic product with the good growth in that area. Special Application, a further good development in our agro and construction business, which positively contributed. And that good development also has to be seen despite the fact that we closed our Australian plant in the first quarter of this year, which had also an impact on top line and on our results.

On Page 9, you see the development of our R&D. As mentioned by Dr. Breidenbach, we continue to invest in the future trends of the automotive industry. So with that, our R&D expenses are increasing. And as mentioned also in several calls before, these expenses follow basically also the project acquisitions we had in the past and, hence, also supports actual launches but also future launches in the next periods. With a slower growth especially also in Q2, the ratio increased to 9.6%.

On Page 10, the SG&A development overall, a proportional increase to our sales growth. Certainly, on one hand side, we invest or continue to invest in our system landscape especially and in our efficiency of our organization and processes. On the other hand side, certainly, the already mentioned cost control programs certainly addresses especially these SG&A-related areas so that we are cautious here in expenses we are doing. And that certainly will also be the case in the upcoming period.

On Page 11, the adjusted EBIT and EBIT margin. We see improvements in our adjusted EBIT to EUR 302 million. Our EBIT margin, at 8.6%, is close to previous year, overall, a slightly better gross profit margin. But on the other hand side, higher R&D, as mentioned, where we continued our -- basically, implementation of our strategy.

On Page 12, we illustrate here further financial numbers down to net profit. Most important here, as we already mentioned, a book gain of EUR 255 million from the sale of our wholesale companies, especially in Denmark and Poland. And this leads to our reported EBIT of EUR 537 million for the first half of this fiscal year and a net profit of EUR 444 million overall.

On Page 13, we show the different development in sales growth and adjusted EBIT margin for Q2 only. In Automotive, our growth is down to 5.3% in Q2. On a year-on-year comparison, we see that the growth basically reflects the change in market growth if you would compare it with IHS numbers. Market in Q2 was shrinking, minus 4.6%. And in comparison to last year Q2, we had a growth of the market of plus 1.9%. Lower growth dynamic overall in Automotive in combination with the continuous higher R&D investment influenced our adjusted EBIT margin, which, at the end, was at 9.3% compared to 10.4% previous year.

Aftermarket, as mentioned, without wholesale shows a growth of 2.1%; EBIT profitability of 6.7%. Q2 in our Independent Aftermarket business was a little bit weaker than expected especially due to demands coming out of Turkey but also Middle East due to the political situation in this area. Very positive, as already mentioned, was the demand and development in our area of diagnostic products.

Special Application shows a negative growth in Q2 of minus 7.7% due to the closure of our production plant in Australia. Without that effect, we would have shown a growth of 4.2%. Profitability shows a very nice and decent positive development with good improvement also compared to previous year.

On Page 14. Free cash flow improved to EUR 152 million. Here, we can see that our cash improvement program shows achievements. Our working capital ratio improved by 1.3% in comparison to the beginning of the year. On the other side, in the first 6 months, our free cash flow here was also supported by the sale of our inventories in Poland in the context of our exit in the wholesale business, in total, EUR 44 million. On the negative side, we had in the first 6 months higher tax payments but also the severance payments coming out of the closure in Australia. Overall, that impacted our free cash flow by -- with roughly EUR 40 million.

Looking at the segments on Page 15. The Automotive segment shows a growth of 8.1% in the first half. Growth was relatively slightly higher in our electronics business compared to lighting. Profitability is slightly down at 8.5%.; main reason, as mentioned, probably higher R&D expenses despite improvement in our gross profit margin.

On Page 16. Aftermarket growth is at 4.5% in first half; good demand, as mentioned, in diagnostic products; slower growth in Independent Aftermarket, as mentioned; and EBIT margin, on a comparable level to previous year.

And Special Application, negative growth, as mentioned, but solid trends in our core business; examples, agro, trailer, construction. So here, taking out Australia, 6.2% growth in the first half and, as already mentioned, a very solid development also in our profitability.

Having said that, I hand back to Dr. Breidenbach with the outlook.

Rolf Breidenbach

When we look at the general economic outlook, it weakens according to the IMF data, and it's indicated that we will see also a further weakening in the months to come. I think all the risks we know, the trade conflicts, high level of debt of several countries, so overall, the economic environment is, of course, not supporting the development in the automotive industry. According to the IHS data, of course, the environment has significantly worsened.

Now for our fiscal year, which I think you all know this starts in June and ends in May, we see now a global market development of minus 1.4%; China, minus 4.1%; NSA, plus 2%; and Europe, minus 2.6%. These are the official IHS data. We see China a little bit weaker and -- but overall, of course, we are using these data also for our forecasts. But as I said, China, I think IHS is still a little bit too positive.

Yes, with regards to our guidance, I already said the current perspective. Although we have a lot of challenges, like the development of the Chinese market, the WLTP topics but also these overall economic elements, we are still very positive. We continue to anticipate a positive business development also for our fiscal year '18/'19. Of course, in the end we do not know what will come in the weeks and months to come. But trying to really forecast on a conservative basis, especially the development in the Chinese market, we are very confident to grow exclusively FX and portfolio effects at the lower end of the given forecast range; so in sales growth, between 5% to 10% but lower end of the given forecast range. With regards to the adjusted EBIT growth, here, the growth excluding restructuring and portfolio effects, we see it in the lower half of the given forecast range. So here we feel a little bit more comfortable with regard to the adjusted EBIT margin. And this has, of course,

a lot to do with our cost control program. Excluding restructuring and portfolio effects, we approximately will achieve the same (margin) level compared to the previous year.

Yes, allow me again to sum up. And so far, we are very satisfied with the development of HELLA in the first half of the year. We are very positive to continue this development, knowing, of course, that the general market conditions will not support this and that the headwind, especially from the market, especially from the Chinese market, will continue.

Yes, having said that, we are now open for your questions

Q&A

Operator

Your first question, it's from the line of Raghav.

Raghav Gupta-Chaudhary

Q. Firstly, a quick clarification on sales growth. You said in your commentary that you expected deterioration in Q3. If I heard correctly, you said you expect it to be flat. And subsequently, was that guidance for organic growth or -- and overall growth, just to clarify, please?

Rolf Breidenbach

A. Overall -- so like-for-like?

Raghav Gupta-Chaudhary

Q. That's right. Okay, so organic.

Rolf Breidenbach

A. Like-for-like, we see a flat development in Q3. And this is included into our guidance.

Raghav Gupta-Chaudhary

Q. Sure, okay. So does that indicate significant slowdown in your top line outperformance, which obviously held up very well in Q2 despite the fact that China was down double digit in kind of October and November? And just wanted to try and understand what you're seeing. Is that due to kind of various programs that you have launching or coming off -- or is that simply kind of 3 quarters of China being very weak? Because I would have expected Europe would perhaps start to improve a little bit. And so that's my first question.

Rolf Breidenbach

A. Let's see how our development will be compared to the market. We currently see the markets, especially in China, for our Q3 worse than the general, for example, IHS data, yes. So we are not so positive with regard to

the development of the Chinese market. And therefore, we are also quite positive with this flat development that we will at least for a significant degree, also outperforming the market. Of course, it's difficult to assess, but we are not so positive for China, especially for our Q3. And with regards to the, let's say, general event, of course, we will launch a lot of products. This will support here and there the sales development. But the main reason why Q3, why we expect such a, yes, slowdown of our growth dynamic is, from our perspective, very weak market development in China for our Q3.

Raghav Gupta-Chaudhary

Q. But it's fair to say then that you're expecting your outperformance to deteriorate. I mean, it's held up remarkably well in Q2, I would say, and so just kind of confirming that. And it's -- and you're suggesting that it's entirely China driven and nothing really to do with various programs that are launching, that you might be annualizing. Sorry to belabor the point, but just wanted to get that clarification because of -- and because of the outperformance was so good in Q2, I just wanted to check if my thinking is right.

Rolf Breidenbach

A. In the end, for us, it's difficult to now forecast the outperformance because the outperformance will be a result between our -- it's clear, between our growth rate and the market development. Therefore, please do not -- please allow me not to now come to -- into, let's say, yes, thin water. As I said, we are not optimistic for China. With regard to the market development, we see a kind of outperformance also for Q3, but let's see what's coming up. Like allow me to say not more because I would now start to speculate, and this is -- I will not -- would not like to do, okay?

Raghav Gupta-Chaudhary

Q. Okay, very well. And in terms of the free cash flow generation, you obviously saw a step-up and you've -- and kind of outlined some of those reasons. We talked about payables and the majority of the improvement, and it kind of looks to be kind of from working capital. How should we think about the sustainability of that particularly in light of, I guess, kind of the soft macro outlook, and the payable days have expanded quite a bit? How do you and how should we think about the sustainability of that?

Ulric Bernard Schäferbarthold

A. In general, it should be sustainable overall. And I think there are certainly positive and negative elements in it. What -- where we see -- what's our still highest levers is continuously on the payable side, and this we are also quite optimistic that this will continue. On the inventory side, still also if we look at end of November, also with the slower growth and especially on the inventory side, we have not basically stopped as quick the material inflow. So there are certainly also some potentials are still possible. So also there, I do think that it

is sustainable also to predict that we can also improve also in the future. On the receivables side, there we -- on one hand side, we see in some areas also the possibility of improvements. Especially on China, there it's getting more challenging. What we see is that on the customer side, we also feel that liquidity gets short. And that it's getting more critical and a much more intensive discussion to really get the payments off the customers and especially also off the local customers. So that there -- now exactly in these times where the market is shrinking and is in a difficult situation, we are spending a lot of management efforts also in pushing our customers. So that's really hard work. But overall, I'm still confident if it comes to the overall program, looking at the improvements we are tracking, trying to realize. And I would overall sum up that we are on track.

Raghav Gupta-Chaudhary

Q. Super helpful. On the payables if I can just kind of push you in a little bit more. Is that being kind of expanded or managed better globally or in particular regions? Your comments on China receivables was interesting. It kind of -- are you matching payables with the kind of the longer receivable days or in China -- just in China or is this something that's going on globally?

Ulric Bernard Schäferbarthold

A. The program is set up globally. On the payables side, I still think that we need to push more in China. We are, I would say, too much German if we look in China what is basically possible in a market. This is addressed, and we are working there. But they are still basically to adapt in line with the behavior of our customers and to do the same also on the supply side. And this we need also to -- there is still, I would say, a lot of potential. And this is addressed. Same accounts for especially Mexico, where we have a very large business there. It's very comparable also there. Lot of potential is still there. In Europe, we already have realized a lot of improvements, but still there also we are not at the end. We can do more.

Raghav Gupta-Chaudhary

Q. Very well. And my final one is just on raw materials. You obviously mentioned it as a headwind to EBIT margins. Can you just remind us what you have written into your contracts with customers in terms of kind of the pass-through of raw material price changes?

Rolf Breidenbach

A. These, let's say, raw material clauses, we have for metals like copper. But for us, plastic is also very important, and here, we have no problem.

Raghav Gupta-Chaudhary

Q. On the clause on copper, sorry, is that 100% pass-through? Or...

Rolf Breidenbach

A. Yes, yes, yes, copper is -- metal, we have covered between, let's say, 75% to 100%. So this is not a concern for us. But of course, when we look at resin, this is much more important for us.

Operator

The next one is from Henning Cosman.

Henning Cosman

Q. Please can I just clarify as a first question what the base is for the EBIT growth? I believe it's EUR 552 million, which excludes 3 quarters of wholesale. Can you just confirm that, please?

Ulric Bernard Schäferbarthold

A. Yes, confirmed.

Henning Cosman

Q. Okay, great. Then the second bucket is on the market more. With respect to China specifically, can you please clarify if you're incorporating potential incentives in your weaker expectation also beyond the Chinese New Year? Secondly, in that bucket, if you could talk a little bit about December specifically, how that was? I'm conscious that Germany was down, for example, 22% in terms of production. If you could say what you've been seeing? Is December just as bad or even worse? And finally, maybe in the market bucket on WLTP and how you see inventories. I think 3 months ago, we were still talking about a catch-up effect maybe in the calendar Q1. I think that tone has changed. But if you could please share your view? So just basically overall elaborate on the market a little bit.

Rolf Breidenbach

A. With regards to incentive in the Chinese market, we do not expect incentives in the Chinese market. This is all information we got from our Chinese partners, our own employees. So of course, we ask this question frequently. But from our perspective, there will be no incentive in the Chinese market, also after Chinese New Year. With regard to December, China was very weak. We have no concrete figures with regard to the market. But for us, China is -- it was just at a weak level we, of course, in November, expected. And as I said, this will not change. So I have no concrete figures, as I said, for the market. But for us, it was very weak. With regard to WLTP, we only see one OEM who will now accelerate in the first quarter of 2019 its sales because you now has WLTP under control, for all the other of our customers, this WLTP topic was more or less finished within calendar year 2018. Of course, there are exceptions, but when you look at the volume, car types, WLTP was more or less finished end of December, with the exception of one, of course, important OEM.

Henning Cosman

Q. Sorry, just to clarify on China and the incentives. So you basically disagree with its recent spokesperson's comments of the National Development Committee that has indicated there would be incentives. Your local people, they disagree with that. Is that right?

Rolf Breidenbach

A. Yes, our local people see no sign for incentives.

Henning Cosman

Q. Okay, great. And finally, from me, on the debt level now and maybe continuing portfolio rearrangement, are you looking to increase that debt level, again, maybe via external growth? Or are there no such plans at all?

Rolf Breidenbach

A. Both. We -- on the one hand, of course, we will continue to invest into our own activities, be it technologies, products or footprint. On the other hand, as we always say it, of course, we are now -- will be continuously looking also to be more active in the M&A area. And it's now for the first time, from our perspective, that the prices for companies, step-by-step, come to a reasonable level, where our, let's say, business cases for these companies pay off. So yes, of course, we will invest into our own activities. And -- but also with regard to M&A, we will continue to find the right targets for us. And this, of course, would then have an influence on our debt level.

Operator

The next question, it's from the line of Manuel Tanzer.

Manuel Tanzer

Q. I basically have one question left. So can you give us an idea how did your sales development in Q2, how did it develop towards the end of Q2? Like was there a notable deceleration in sales growth? And how did December start out? Just to get some idea. You were commenting on a very difficult Q3. So just to get some idea is that a run rate we could imagine for the rest of Q3, what we saw in December? And if you were commenting on a potentially flat Q3 that would, even at the lower end of the guidance, imply some, I'd say, north of 8% growth, organic growth for the Automotive segment to reach the lower end of the guidance for Q4. Could you confirm that? Because that would actually be a pretty strong growth, again, and a solid revival. And one add-on on the JVs. I was actually surprised to see the strong -- pretty strong JV performance of around EUR 50 million. Can you just shed some light on how come that JV has performed so strongly again?

Rolf Breidenbach

A. Yes, thank you. Let's start with the sales development. Yes, we saw in Q2 month by month, week by week, a declining of our growth rate, which comes

to an end in December. So we expect a very flat development now for the weeks to come. And as I said, our, let's say, bottom line assumption for Q3 is that we develop on a more or less flat level, perhaps a little bit positive but no significant growth. And due to our, let's say, launch portfolio on the one hand and the kind of normalization on the market side, we come to our overall guidance.

Ulric Bernard Schäferbarthold

A. So on the joint ventures, half year certainly is slightly better. So overall, EUR 2 million better. And in Q2 only, it was significantly better. But there are also, the prior year was very weak. There is no, I would say, special one reason on that. And I think overall, what we have seen is that all our joint ventures in Q2 performed a little better in comparison to last year. So summing that up, overall, we had a much better performance overall in half year. Certainly, sometimes there are also some volatilities on quarter-to-quarter. But we are coming back, I would say, to slightly better result. But as mentioned, last year was also very weak if it comes to our joint venture results.

Operator

The next one, it's from the line of Julian Radlinger.

Julian Radlinger

Q. Just 2 or 3 for me, quick ones. First one, the EUR 90 million-or-so free cash flow in the quarter, there's a positive item in there of -- I think you mentioned it, Mr. Schäferbarthold, of EUR 40 million or EUR 44 million. In your quarterly report, you called this a repayment of the financing of the corporate operations. Can you just elaborate what exactly that is, please?

Ulric Bernard Schäferbarthold

A. Yes, with the sale of our Polish company in wholesale, we have been paid for the branches and the inventories. And that was EUR 44 million, basically what we there got back. Besides, basically, the transaction, where we realized, I would say, the equity value also on that business. So that's on the EUR 44 million I mentioned. And then on the negative side, especially also in Q2, we had the severance payment of the closure of our plant. And we had partially, that is not only Q2, also related to Q1, significantly higher tax payments in comparison also to the previous year. So overall, more than EUR 20 million more taxes, which is overall related to higher prepayments on taxes, especially in Germany but also in some other Eastern European countries. But overall, I would say in comparison to last year, if you sum both up, severance payments, especially, and tax, it comes also to EUR 40 million. So that -- yes, these are the major, I would say, differences.

Julian Radlinger

Q. Okay. So just to clarify. You're basically saying on the one hand, you did have this repayment related to the sale of your Polish wholesale business, around EUR 40 million. But you also had higher taxes amongst others that you didn't adjust for in your adjusted free cash flow number, and so that kind of offsets essentially. And the clean -- or clean adjusted free cash flow really is around EUR 90 million in Q2. Am I understanding that correctly?

Ulric Bernard Schäferbarthold

A. I'm not saying that clean adjustment. I'm just saying what are the highlights within our adjusted free cash flow. And on one hand side, we have a positive effect; and on the other hand side, we have some, I would say, significant negative effects also. So if you take both, which more or less -- we'll not say it's onetime, but it's in a certain way onetime. On the comparison, especially in Q2, it's special, I would say, to understand the number.

Julian Radlinger

Q. Okay. No, that makes sense. Then second question. Talking about the net working capital consumption. We already talked about it now in the Q&A a little bit. I'm struggling still to see in the financial statements an actual improvement because as a percentage of sales, the net working capital is still around or is around 17% to 18%, if I'm not mistaken, right now. About a year or 1.5 years ago, when you first said that you want to improve net working capital by 300 basis points over the next 3 years, that ratio was at 16%. So it's actually gone up since then. But in most quarters, especially this one and the last one, you've actually said there's been an improvement. So I can't really reconcile those comments. Can you just kind of help me with that a little bit?

Ulric Bernard Schäferbarthold

A. Yes, mostly it's related to the changes in IFRS 15, where basically, the projects related tools are now shown in the inventories. So that is an amount where with the adoption of IFRS 15 overall, with the entry booking of that change, we had -- that is in the half year's numbers now, EUR 200 million of these tools in the inventories and, in addition now, additional project stocks, which are also related to ongoing work in progress of current projects we are working. So additional EUR 20 million. So overall, we are talking -- if you look in comparison to prior year number, around EUR 230 million of additional inventories more or less related to tools, which if you look now at when we started this cash improvement program, this normally you would have to take out. It was before in the assets. So that is an accounting change. And if you take that out, then you come to that improvement I mentioned.

Julian Radlinger

Q. Okay. That really explains it. And then just a last question also of free cash flow, more or less. CapEx. Is my understanding correct that you are -- of the 6 or 7 plants and plant expansions that you undertook starting about a year ago, a

little bit more, that you outlined at your last Capital Markets Day, I think you're at the point where you opened all those plants apart from I think one that you said would launch at the beginning of calendar 2019. Is that still the case? Or are there new plant expansion plans you have over the next 1 to 2 years at this point? And what does it mean for CapEx for full year '18, '19 and for next year? Is it right in assuming that you should trend somewhere between 6% to 7% net CapEx to sales rather than above that because you're not expanding capacity anymore in the next 18 months or so?

Rolf Breidenbach

A. Let's say, with regard to our core business, we currently see no, let's say, building up of a new plant in the next, let's say, 12 months. What I cannot assess today is whether we invest into new areas, for example, in the field of energy management, and then, yes, needs to build up a new plant. But as I said, when we talk about our core business, at least in the next 12 months, I see no new plants. And of course, then this also means no CapEx investment into that. But please have in mind that also a huge amount of our CapEx spending is related to project costs. And based on our, let's say, ambition, of course, to continue our growth path, when we have the opportunity to get new business in, we will acquire it. And this means -- this can mean additional CapEx.

Julian Radlinger

Q. Okay. And then just very finally, again, so there is one more plant opening in the next 2 to 3 months, if I'm not mistaken. Is that right?

Rolf Breidenbach

A. That's correct.

Operator

Your next question, it's from Sascha Gommel.

Sascha Gommel

Q. The first one would actually be on your cost control which has been quite strong in the first -- in the second quarter, sorry, given the slowdown. How confident are you that given the incremental slowdown now coming in your third quarter, that you can find incremental cost measures to protect your margins? And what would that be? And are most of the cost measures you did in Q2 sustainable? And then a couple of small ones on your financials for clarification. So the change in provisions in your cash flow statement. This is still related to the Australia closure, is that right? And then the last question on the financial is: You have a restructuring charge in your distribution expenses. Can you explain that, please?

Rolf Breidenbach

A. Yes, starting with the cost control program. Of course, when -- assuming we would become flat in Q3, then of course, it's very, very difficult to work

against -- with our cost control program. So we would assume a slight decrease of our margin. On the other hand, of course, we see still a very good potential on this side. And we will continue to implement very strict and hard measures.

Ulric Bernard Schäferbarthold

A. On the provisions. Yes, it's right. A big part of it is related to the severance payment. And what was exactly now your last question to the distribution?

Sascha Gommel

Q. In the quarterly report, there is a EUR 9-point-something million adjustment on your distribution expenses. I was wondering if you could explain that. What is behind that? It's on -- it's in the Aftermarket.

Ulric Bernard Schäferbarthold

A. That is related to restructuring we are doing in the Aftermarket related to the reduction of our overall business coming from basically the disposal of the wholesale. So we are now doing reorganization of our global overall setup in the Aftermarket business. And these restructuring costs overall are assumed to be in the area of EUR 8 million to EUR 9 million. And this is fully now taken in, in our results and has been adjusted.

Operator -

A. The next one, it's from the line of Ralf Stromeyer.

Ralf Stromeyer

Q. Just a short one on Special Applications. What has driven the strong EBIT margin - increase there in the second quarter?

Rolf Breidenbach

A. On the one hand, a good market development in the agriculture and construction market; and a good cost management.

Operator

Next question is from Christian Ludwig.

Christian Ludwig

Q. Couple of quick questions from my side as well. First of all, coming back to your cash situation. You mentioned that you are looking at M&A. But if you're not successful there, is it possible that you may increase your dividend payout ratio or actually pay a bonus dividend once to basically also have shareholders participate in the gain of the sale? Second question. Could you tell us a little bit on any new orders you received during the quarter? Maybe, you don't want to report an order intake. But maybe, you can give us some indication what kind of new orders you were able to win. And the last question. In your balance sheet, you now show contract assets and contract obligations. I assume I

haven't read full of it, but is that due to IFRS changes. But maybe, you could tell us very quickly what that's about.

Rolf Breidenbach

A. Starting to answer the first question with regards to the dividend, I think this will be decided at the end of our fiscal year. So, so far, I have no perspective on that. And then in the end, here also our shareholders' council, I think, will make a strong proposal. So this is not discussed to the end, and no decision is made so far. With regard to orders. On the one hand, of course, we, again, could acquire additional segments in the area of -- for example, battery management system. Also our radar business is working quite good. In general, DC/DC -- in general, energy management products are running in this dimension very well. So we also booked new additional business in the area of DC/DC, converters, 48 volts. So from the electronic side perhaps. And with regard to lighting, on the one hand, we see, yes, addition -- interesting new orders in the field of Car Body Lighting on the one hand, so illuminated grills and so on. And also in interior lighting, we see a lot of additional new businesses due to the fact that our customers have the tendency to pay more and more attention on the design of the vehicle with regard to interior, especially when we talk about -- not only, but especially when we talk about e-vehicles. Just perhaps as an example. And overall, we are very satisfied with the current status of our order book.

Ulric Bernard Schäferbarthold

A. Contractual assets and obligations we mentioned are in the context of the change of the IFRS 15, which has now been taken into account now from Q1 onwards. As I mentioned and also in the context of the inventories, we discussed there is also basically a change what had to be shown in the inventories. Basically, it's related to the accounting of our tools but also our R&D spend. And basically, the agreement we have with the customer is how this R&D is then contractually -- basically specified how it is then sold to the customer, how this has to be shown then in the balance sheet. It's explained also in in more detail in our notes of our half year report, how this accounting method has been changed. And if you have further question, Mr. Ludwig, please feel free then to contact me directly, so I can give you much more details also to explain it to you.

Christian Ludwig

Q. Great. And I'll have a look at the notes and may give you another call.

Operator

The next one is from Jürgen Pieper

Jürgen Pieper

Q. I usually don't say it in a call. But I must say this is a great performance and a great first half in a very tough environment, and congratulations for these relatively very good results. Two questions remaining after the long discussion. Question one is on LED lighting. If you -- if one compares your comments with some other companies' comments, like especially Osram, there's this great discrepancy. And I don't expect you to comment on Osram. But would you say that, at least, you expect still stability from here in the LED lighting market or even some kind of growth? And secondly, we've talked a lot about the weakness in the overall market and your view, your expectations concerning the market in the next couple of months. What is your view on the electric vehicles market? Is it growing by a 30%, 40% or so globally? Is it in line with what you expected? Or is it somehow better or worse than that?

Rolf Breidenbach

A. With regards to LED, I think this trend to LED functionality is continuing. So when we look at functionalities and volumes, we still see a very good growth potential. And fortunately, we also see that the number of LED suppliers is increasing. And therefore, the competition we had in this field is also, yes, from our perspective, of course, developing into the right direction. And therefore -- so we are very positive with regard to the LED market. And this is not only true for headlamps. Also when we talk about interior lighting and other functionalities I mentioned, I think the trend to LED will continue. With regard to the general market development. As I said, we are very pessimistic for China for the, let's say now, first, let's say, 2 to 3 months. Then let's see what's going on. Perhaps, a kind of stabilization will come but not much. We see NSA still quite stable on a low-growth level. And Europe is very difficult for us to assess and to forecast. But in general, we see that premium remains very strong. And you know our business depends on around 50% on the premium car manufacturers. And when we go into the different markets, on the one hand, we see this tendency to SUVs, nothing new, but we also see, also in difficult markets, premium is developing more positive from our perspective than, for example, segments, like the A segment or something like that. Yes, with regard to electrification, we see still an increase with regard to the dynamic of development of the e-vehicle market, which now, step-by-step, will also be seen with regard to the number of launches. I think we all notice. But due to the, let's say, latest decision, for example, with regard to CO2 values in Europe, the investments into the e-vehicle technologies and car parks have even accelerated although there was a great dynamic already there. And with regard to China, this, of course, is only our very subjective perspective, we see a strong focus of the Chinese car industry and the Chinese government on e-vehicles with regard to basic investments, infrastructure and so on. So for these 2 markets, we are very positive with regard to the e-vehicle development. This, of course, is not comparable to NSA. Here, I think the dynamic will be significantly lower.

Jürgen Pieper

Q. Okay, so when one can say that your growth in this with your products here, in this EV market is similar to the market growth of, let's say, something like 30% or so. Is it correct? Or is it -- would it be exaggerated to talk such a figure?

Rolf Breidenbach

A. This is now difficult for me to calculate here on spot, but as a quick guess, it's best in line with the development of the e-vehicle market.

Operator

We still have one question more. It's from the line of Christoph Laskawi.

Christoph Laskawi

Q. It's really only one left and also relating to something that you mentioned on the Q1 call, where you said that visibility in Europe with regards to orders coming in and actually what's -- relates to call updates it's very tough to predict in the coming ones. I'd like to know if that situation actually improved over the quarter and visibility improved. And on the back of that, would you expect a sequential improvement in January and February, knowing that December was very weak?

Rolf Breidenbach

A. So still, Europe is as difficult to assess because there are so many discussions going on with regard to regulations, with regard to trade conditions. And this does not improve the mood and the positive assessment of the end customer. And therefore, we still, let's say, are very unsecure how Europe will develop. It's for us not so clear. And it's very comparable to the situation in Q1.

Christoph Laskawi

Q. So the volatility in the order book that you commented on with the last call is essentially as high as it was back then. And you expect it not really to improve going forward? Is that the correct take?

Rolf Breidenbach

A. No, you really have to distinguish between the order book on the one hand and the market development on the other hand. So my comments were related -- if I got your question wrong, my comments were related to the market development. With regard to the order book, we are very -- very good position also in Europe.

Operator

And there are no further questions at this time. Please continue.

Rolf Breidenbach

A. Okay, it looks as if there are no further questions. Therefore, again, thank you very much from Mr. Schäferbarthold and my side for participating in that call. Thank you very much for all the questions and your time you have spent in this call.

Thanks, and all the best, and have a nice weekend when it will come. Thank you.

Operator

Thank you. That concludes our call for today. You may all disconnect. Thank you all for participating.

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