DER AKTIONÄR Executive Board Interview

Softing AG – WKN 517 800

Interviewee: Chief Executive Officer Dr. Wolfgang Trier

Softing CEO Dr. Trier: "We must create a positive narrative"

Dr. Trier, Softing was forced to significantly lower its EBITDA guidance for 2017. Was this development already apparent during the third quarter?

Dr. Wolfgang Trier: No, it was unforeseeable, as our operating results for the third quarter were largely in line with expectations. Even if our third-quarter performance had been better than planned, our full-year earnings would have been unable to compensate for this individual payment of around EUR 2 million expected in the fourth quarter for the sale of rights for non-capitalized development services, which counts fully against EBIT. This was quite a blow for us, and there was no alternative but to make an announcement.

Your ad-hoc announcement says that "revenue recognition for a completed product development ... will be delayed". Having expected this figure to contribute to revenue and earnings in 2017, do you now expect to be able to realize this contribution during the 2018 financial year?

Dr. Wolfgang Trier: Yes. In fact, we assume that we will recover the vast majority of this figure in 2018. The customer has already paid us a high six-figure sum. We will only lose our rights to the IP once the balance has been paid, either as a lump sum or in several installments. While this has affected us significantly in the short term, there is no doubt that it is merely a delay that will have a positive impact on our 2018 figures.

Your announcement also stated that foreign currency translation effects reflected in the balance sheet would have a negative impact on your earnings for the year. Why don't you hedge your currency risks?

Dr. Wolfgang Trier: This is primarily an accounting effect arising from the measurement of internal loans in accordance with IFRSs, and makes up the majority of these translation effects. It is simply impossible to hedge against this. Operationally, this only affects the translation of our US subsidiary's results. Although it is possible to hedge this, doing so would incur significant costs. As the positive and negative effects of currency fluctuations will largely cancel each other out over the medium term, expensive hedging does not make good business sense.

Apart from the two aforementioned non-recurring factors, how satisfied are you with the company's operating performance so far this year?

Dr. Wolfgang Trier: The results of operations in the Automotive segment in 2017 have already been discussed at length. The first two quarters went extremely well in the Industrial segment, even though the business exhibited weaker growth in German-speaking markets. However, the US business in particular regained its former strength. Our IT Networks subsidiary also experienced good to excellent growth. Growth has been and remains our primary focus whenever we are in the black. The third quarter did not match these rates of growth.

You mentioned the fact that German-speaking markets are currently weakening while the US Industrial business has regained its former strength. What measures have you taken in response to these developments?

Dr. Wolfgang Trier: In our German-speaking markets, we previously brought together two businesses with very different market characteristics. The first is a traditional business primarily comprising hardware products for the manufacturing and process industry. The other, Data Intelligence, is a new range made up almost exclusively of software-based products. This business is evolving much faster and has to hold its own in a completely different competitive environment. To ensure the success of both businesses, we will form two independent groups, each of which will be geared to meet its particular objectives across all activities and roles.

The operating loss generated by the Automotive segment is having a negative impact on consolidated profit. When do you expect to break even in this business and what innovations do you have in the pipeline?

Dr. Wolfgang Trier: As we have already announced, we have begun to significantly reduce costs by the end of the year, which will also reduce the cost base for 2018. We expect that this, combined with the level of business expected, will return the business to profit. During the next year, we will launch at least two new products with over-the-air features. Together with one of our partners, we strive to offer services that allow users to retrieve data from vehicle fleets in a cost-effective way, which is one of the hottest topics in the automotive industry at present. We can use our diagnostics expertise to our advantage in this area.

You are also reporting potential orders totaling several million euros that are currently under negotiation. Are these negotiations now simply a matter of price? How significant are these orders for Softing?

Dr. Wolfgang Trier: We are currently in negotiations about several projects that are extremely interesting both strategically and commercially, with products and services based around our core diagnostics expertise. We first need to secure these key projects one by one, at which point we will announce them. Any premature announcements would put both the projects and our credibility at risk.

What do you expect in the fourth and final quarter of the year?

Dr. Wolfgang Trier: The fourth quarter is traditionally the strongest for Softing, and this will be the case again in 2017. As a result of both this and the gradual reduction in external costs, we expect to reach our latest earnings forecast for the year. All the signs are currently pointing towards a strong final quarter.

At an investor event in September, you provided a very optimistic outlook for 2018. Do you still stand by this assessment?

Dr. Wolfgang Trier: Yes, absolutely. In some areas, you can still expect to hear news of completed transactions this year that will provide us with milestones for 2018. While this means that our earnings will be moving in the direction of our fundamental expectations, we do not believe our core objective of consistently double-digit EBIT margins can be achieved at a stroke. Reaching this target will both depend on restoring profitability in the Automotive division and on changing our business model from non-recurring income to recurring annual revenue with a stronger emphasis on services. The initial steps will inevitably involve a shift from the first year to subsequent years.

There has been very little news of potential acquisitions. Have you failed to find suitable targets or do you require available funds for investment and product development?

Dr. Wolfgang Trier: We were ultimately not convinced by several acquisition targets that we pursued until the due diligence phase. We have put several topics on hold, and are taking matters into our own hands when it comes to one of the biggest opportunities in the field of mobile data. We will provide further details as soon as these plans have been finalized.

The recent profit warning was a blow to investor confidence. How are you planning to regain this trust in the coming months?

Dr. Wolfgang Trier: We must and will fight to win back this trust little by little by capitalizing on the opportunities I have already mentioned. There is no sense in speculating; we need to deliver and, by doing so, create a positive narrative. It will also be important to use regular IR work to communicate much more intensively - and that’s exactly what we’ll do.

Dr. Trier, thank you very much for the interview.