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Q4 2022 Earnings Call

CORPORATE PARTICIPANTS

Natalia Valtasaari
Head-Investor Relations, Kone Oyj

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

OTHER PARTICIPANTS

Lars Brorson
Analyst, Barclays Capital Securities Ltd.

Daniela Costa
Analyst, Goldman Sachs International

Aurelio Calderon Tejedor
Analyst, Morgan Stanley & Co. International Plc

Klas H. Bergelind
Analyst, Citigroup Global Markets Ltd.

Miguel Borrega
Analyst, Exane SA (United Kingdom)

John Kim
Analyst, Deutsche Securities (Pty) Ltd.

Tomi Railo
Analyst, DNB Bank ASA (United Kingdom)

Panu Laitinmäki
Analyst, Danske Bank A/S (Finland)

Martin Flueckiger
Analyst, Kepler Cheuvreux SA (Switzerland)

Delphine Brault
Analyst, Oddo BHF SCA

Rizk Maidi
Analyst, Jefferies International Ltd.

James Moore
Analyst, Redburn (Europe) Ltd.

MANAGEMENT DISCUSSION SECTION

Natalia Valtasaari

Head-Investor Relations, Kone Oyj

Good afternoon and welcome to KONE's Fourth Quarter Earnings Call. My name is Natalia Valtasaari. I'm head of KONE's Investor Relations, and, as usual, I'm joined here today by our President and CEO, Henrik Ehrnrooth; and our CFO, Ilkka Hara.

As in previous presentations, Henrik will start by running through the key highlights of the quarter and the full year, both in terms of our business performance, financial performance, and also what we're seeing in the markets. Ilkka will then follow up with a bit of in-depth review about the financials, and Henrik will end the presentation speaking about our outlook for this year. We'll go into Q&A then, and I would ask you all to limit yourself to one question, one follow-up, so that as many people as possible have the opportunity to ask their questions.

With that, Henrik, please.

Henrik Georg Fredrik Ehrnrooth

President & Chief Executive Officer, Kone Oyj

Thank you, Natalia, and warm welcome to our fourth quarter presentation. Today, we have again a lot of interesting and exciting news to share with you. So going straight into the highlights of Q4, so Q4, we had a solid sales development now, particularly if we look at the market conditions. So, clearly, sales was at better level than it was in Q2 and Q3.

Our service business continued to perform very strongly. That is something we put a lot of focus on during the past year, and we have continued to drive very nice growth in both maintenance and modernization.

The Chinese market was clearly very challenging in Q4, and that had an impact on both orders and cash flow. It's clear that a lot has happened in China since end of Q4, and I would say that signs are much more encouraging now than they were just going back to November, for example.

We continued to successfully increase our prices in all of our businesses, which have been driving continued margin recovery both year-over-year and sequentially. And our board of directors have today announced that they will propose to annual general meeting a dividend of €1.75 per B share, the same level as the prior year.

So what about Q4? I would say Q4 performance was very much in line with our expectations and we did see an improvement in profitability. Orders received at €1.9 billion, down about 11% in comparable currencies. It's clear that Chinese market weakness had a big impact in this. Order book remains at a very solid level of more than €9 billion, and if you look year-over-year, up 5%.

As I mentioned, sales returned to growth. Now in this quarter, just about €2.9 billion and 2.9% growth here. Clearly, services business was the key driver here and regionally was Americas. What I'm also happy about is now our operating income increased 4.3% year-over-year to €367 million and our adjusted EBIT improved from €359 million to €365 million. So a slight improvement here even though margin was still down 0.5 percentage point from 13% to 12.5%.

Cash flow was €33 million in the quarter. Clearly, not something we are happy with. So that is perhaps what was a disappointment in this quarter, and earnings per share the same as previous year. As we always say, one quarter is a very short period of time and now we have a full year to look back to on our performance, and it's clear that 2022 had many different phases. Q1 started reasonably normally. In Q2, we clearly faced the COVID lockdowns in China, which meant that our sales suffered a lot because we almost lost a month of sales because of closure of our factory. And Q3 continue to be challenging, now somewhat better Q4, if we look at profitability wise.

Our orders received in that year, €9.1 billion down 2.5% in comparable currencies, which I would say is actually an okay result in an environment like this. Sales €10.9 billion, down 1.8%. Of course, vary a lot quarter-by-quarter and our return to growth. Operating income down 20% to €1.31 billion and adjusted EBIT down from €1.3 billion to €1.77 billion. This is clearly something we are not happy about and that's why we have such a strong focus on profitability improvement, which we of course could see partly already in Q4. And cash flow €754 million down from an exceptionally strong €1.8 billion before, and EPS €1.50.

Now what I will talk about lot today is where we put our focus last year. And we can see that we made great progress in the focus areas we set for us. That again shows that KONE's team when we set our mind to something we can drive good improvement. That was again a sign of that last year. So, I think the team from that perspective did a great job again.

As I mentioned, board of directors made a proposal of a dividend of €1.75, same level as last year, which means of course, we're paying out now a bit over our EPS, and provides a good dividend yield of 3.6%. But continued strong dividends, this is a bit over €900 million that will pay out again for last year's result.

Now, we know that markets have changed a lot over the last years. It's been about capturing opportunities where they have emerged. And therefore, in a very changing environment, we set our focus on three specific thing during 2022. It was clearly about the improving pricing. We've been talking about that a lot. Then of course, about driving productivity, absolutely critical in an inflationary environment, and an environment where costs are going up.

And then service business growth. Of course service markets have provided good growth opportunities and that's why we have really pushed for growth in that business. So, how do we do it? Well, price increases did go well last year, and it meant that our margins of our orders received improved compared to sequentially and end of 2021. So, when we look at outside of China, we had set ourselves a target of getting our margins of our new orders to a similar level where we were towards the end of 2020. And that is what we achieved. So, great progress there. China clearly more challenging.

Also, in our offering development and in our operations development, we focused a lot on productivity and product cost, both we had clearly better improvement than in prior years. So, again, great results there. And I think which is very clear that we continued throughout last year to have market-leading services growth both in maintenance and modernization.

In maintenance, for example, we can see that our service base grew by 5.4%, whereas our revenue grew by 8%. So, clearly successful pricing. 24/7 Connected Services, all of them contributed to having a sales growth that was 1.5 times higher than unit growth. So overall, that was our focus during last year. And clearly, we're setting a very tight focus for this year to continue our positive development in these areas.

Also what I think is familiar to everyone that the way we measure our longer-term success is through our strategic targets. That's a balanced way of looking at how we're developing all the areas that are important to us. In our great place to work, our employee engagement continued to be clearly above global norms, in a changing environment absolutely critical to have motivated, driven workforce. Most of our customers, we could see that our customer loyalty based our customer loyalty survey continued the upward trend in both of our businesses, both the services and new equipment and very broadly geographically. So what we're doing clearly is delivering positive results from our customers' perspective.

Our third target is to grow faster than our markets. We continued throughout last year to have market-leading growth in services and that is of course where we really put our focus. In new equipment, we really said that the first and most important thing for us is improving our margins, so pricing increases that we did. Now in terms of market share, we were about in line with markets, varied a little bit region-to-region but more or less in line with the markets for last year.

Then our fourth target is to have the best financial performance. It's clear that this we are not happy with. Our current profitability is not something that is okay for us, something we want to improve and we are driving improvement there. And in sustainability, we continued our strong performance in environmental sustainability, in our diversity metrics and safety. In environment, we continued to get a lot of external recognitions for the work we're doing there. So continued good progress for us and, of course, a lot to do going forward. But I would say many good developments, but still on profitability, a fair bit to be done.

Now, the other thing that we announced today is that we are planning to renew our operating model. This is, of course, to improve our competitiveness and be able to react even faster to market changes. So what are we doing? We are simplifying our operating model. As you know, KONE has always had a culture of a strong local accountability. Now we're driving even further accountability to our area organizations and our front lines. And at the same time, we want to continue benefiting from the global scale we have through our global product platforms, services platforms, as well as our supply chain.

So why did we decide we want to do this? Well, when we look at the past years, we can clearly see that the market environment has changed very rapidly and situations have changed in a different way in different regions. Going forward, we believe that that will continue to be the situation. That markets will change and the development in North America will differ from Europe or from Asia. And therefore, we want to drive even more accountability to our area organizations to be able to quicker make decisions, to capture the opportunities as they emerge in order to drive better growth.

Also, as part of this, we are going from five geographic areas to four geographic areas. So two areas in Europe will be combined to one called Europe. And that's part of this change.

Now, as I mentioned already, what we're really targeting with this is to better capture regional growth opportunities. It's, of course, about improving our competitiveness and our profitability. With better growth, we can drive also better profitable growth. At the same time also in an environment that we are, we also want to reduce our costs. So the target of this program is to reduce cost by €100 million, also to support our profitability development. So those are some highlights of our financial performance and how we performed and worked last year, and also the change in operating model.

Let's next talk about our markets, how they developed in Q4. New equipment markets in Q4 globally declined. We can see that markets declined in each geographic area. So it's clear that we could start to see impact of increasing interest rates and lower consumer confidence. And that had an impact on, for example, market for apartments and housing.

North America, which has been, perhaps, the best performing market, now declined clearly in Q4. Same with Europe. There, perhaps, the bright spot continues to be Middle East. China declined by around 20% in Q4 and rest of Asia Pacific slightly, although their bright spot has clearly been India.

Now, on the other hand, services market, we can see a much more positive development. That is why we have been putting so much effort in our services business. We can see that the maintenance markets continue to grow as we've seen before. And with best growth in Asia Pacific and China and modernization market now slightly lower growth than prior quarters but still positive growth which created, again, opportunities which we captured quite nicely.

Now let's dive a little bit deeper into the China market in Q4. It is clear that Q4 was one of the tougher environments in China and pricing competition was very tough. We did see a lot of changes towards the end of Q4 with the abolishment of all COVID-19 restrictions, which had a lot of impact during the quarter. Now, if we look at all the statistics for Q4, we can see that most of them actually were worse in Q4 than the rest of 2022, except for completions. So we could start to see the focus on completing semi-finished buildings, how important that is.

So if we look at China and how I see it at the moment, it's clear that Q4 was a challenging quarter. At the same time, towards the end of the quarter, first, we saw an abolishment of all COVID restrictions, an opening of the market which we believe will have a positive impact now as the country goes through that current infection wave, which very far has done so already.

At the same time, we have seen a lot of policy announcements to improve the situation for developers to enable them to refinance themselves, to get financing, to be able to drive the whole property sector forward. So those have clearly created much more optimism and, therefore, there are encouraging signs for the market.

Before the market really starts to now recover, we still need to see an improvement in consumer sentiment, which would then be a result of markets opening up and starting going better now that COVID restrictions have been abolished. That's what we will say also, you will see in our outlook, we're saying that we expect Chinese markets, yes, to decline for the full year 2023, but to start recovering towards the end of the first half as a result of all of these measures that already have been taken. But I will come back to that. So clearly, if I compare the situation now compared to, for example, in November, outlook has clearly improved.

So that is about our markets and a bit more on China. And with that, I'll hand it over to Ilkka.

Ilkka Hara

Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

Thank you, Henrik, and also a warm welcome on my behalf to this fourth quarter result announcement webcast. I'll go through our financials as normal and start with orders received development for the quarter.

For the quarter orders received was €1.944 billion, down on a reported basis 9.8%, and on a constant currency basis 11.2%. This development was driven by China and the property sector continuing to see difficult environment that Henrik already described. And as a result, Asia-Pacific declined significantly in orders received. Also, Americas declined as well as we saw a slight decline in Europe, Middle East, Africa as well contributing to this development.

At the same time, as we've talked about earlier, pricing has been at the center of our focus in this inflationary environment. And also in fourth quarter, we continue to see our orders margins improving compared to last quarter, but as well as compared to last year. In China, pricing continued to be challenging, but lower commodity costs contributed to this development. At the same time, in other areas, we continued to see good momentum with pricing. And as Henrik already highlighted now with the pricing actions we've taken, we have been able to see our orders margin recovering back to the level where it was at the end of 2020. So very good development there. We've already highlighted the strength in modernization pricing earlier and we've continued to now see good development also in new equipment outside of China. So very pleased to see this continuing in a positive manner.

Then to sales, sales for the quarter were €2.9 billion, on a reported basis 5.2% growth and on a comparable basis 2.9%. From geographical perspective, strong development in Americas, over 14% growth. Europe, Middle East, Africa growing at 4.8% and Asia-Pacific down 3.9%, mainly driven by the development in China there, also China impacting new equipment, which declined 2.4%. But as highlighted already earlier, our services business continued its very strong performance and as a result, maintenance grew 7.6%, and modernization 11.4%, so very good performance on our services business.

Our adjusted EBIT for the quarter was €365 million and the margin for adjusted EBIT was 12.5%. We continued to see positive here. It's been a focus to be able to recover our margins now towards the end of the year. Absolute basis were slightly up, and margin wise, we continued to narrow the gap compared to last year.

The initial results or the pricing actions that we've taken on orders are now visible in the orders we deliver in this quarter that contributes positively. We continued to see the widespread inflation creating cost headwind having a negative impact in our profits and profitability. And also, the mix impact from declining China sales is impacting negatively our profitability.

Then cash flow which for the quarter was €33 million. And clearly, we saw our working capital having a negative impact to our cash flow, down from last year's exceptionally high level of €525 million. As I highlighted earlier, both at the end of last year, but also in conjunction with third quarter results, timing on our accounts payable had a negative impact on cash flow and working capital. And also, overall, the liquidity situation in China is impacting our customers, and accounts receivable were up in the quarter.

Also, I would say that the orders received development in China, which was negative, naturally contributes to our advances and therefore negatively on working capital development. But clearly, this cash flow is not something we're happy about and are expecting that in the coming quarters we would then start to return to a more normalized development in our cash generation for the business.

But with that I'll stop and hand over to Henrik to continue with the market and business outlook.

Henrik Georg Fredrik Ehrnrooth

President & Chief Executive Officer, Kone Oyj

Thanks, Ilkka. So how are we seeing 2023? First of all, let's start with the important China market. We expect that the Chinese market will decline by somewhat over 10% in 2023. Now, as I mentioned already, we expect that recovery will start towards the end of the first half of the year as a result of the stimulus measures that have already been announced.

So we don't expect anything new. We expect just that this will start taking effect, and also when the economy improves see better consumer confidence. Rest of the world market grow clearly in Asia Pacific. Ex-China, of course, driven by India, more stable in Europe, Middle East and Africa, of course, there Middle East better than Europe and declined slightly in North America, of course, from a good level in North America.

Modernization markets expected to continue to see growth in all regions. And maintenance markets, good development that we've seen so far, trend to continue with slight growth in mature markets and of course, good growth in Asia-Pacific.

KONE's business outlook for 2023, we expect our sales in comparable currencies to be at a similar level to the previous year. And we expect our adjusted EBIT margin to start to recover due to better margins of orders received that Ilkka talked about in our orders and also the continued solid development, in maintenance business.

Now this whole outlook does assume that construction activity in China starts to recover towards the end of the first half of the year as a result of the measures that have already been introduced in the property sector. Now, there are a number of things that are supporting our performance. It's of course, the positive outlook for our services. The good development we have there. We have a strong order book and we're having gradually better margins that we deliver from that order book. And of course, the easing commodity headwinds in Asia, particularly China, I would say.

What is burning the result, the rotation, the order book continues to be slower throughout the world because of more uncertain outlook and many developers slowing down their projects or in some markets, still some material shortages. Then of course, the anticipated decline in China's new equipment market. We know that China is by far our biggest market and a very good market for KONE.

Then also, wage inflation will be higher this year than in prior years and component costs are still going up. So we always have for the components that we buy, there's the raw material part and the value-added part. The value-added part because of labor costs and other inflationary trends are driving up those costs still. But I think, many good things and of course, overall expectation is that we will start recovering our EBIT margins.

Now to summarize, there continues to be good opportunities in services that we are focused on to continue to drive the good performance we have had. And we are seeing positive results from profitability actions, particularly when it comes to pricing and productivity. We have a competitive offering and our focus is to continue to drive long-term growth. And then we're also taking action to further improve our competitiveness with our planned operating model renewal.

So with that, we are ready for your questions and comments. Operator, please.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] The first question comes from the line of Lars Brorson from Barclays. Please go ahead.

Lars Brorson
Analyst, Barclays Capital Securities Ltd. Q

Thank you. Hi, Henrik, Ilkka. If I can start maybe on this full year guidance, we have four years history of giving earnings guidance, now you don't. I appreciate there are certain key variables within [indiscernible] (00:26:44) trying to understand how [indiscernible] (00:26:52) raw material [indiscernible] (00:26:54-00:27:10) talk about €400 million headwind over the last two years, this should start to reverse this year. I wonder from a sort of total raw mat and logistics and components cost standpoint, can you help us a little bit on what that number might look like in the 2023 bridge? Thank you.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj A

Yeah. Thanks. Thanks, Lars. First of all, I don't know if was elsewhere, but that line on our end was a bit, a little bad, so slightly difficult to hear your question.

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj A

First was guidance, and then I'll take the raw materials.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj A

Yeah, our guidance, I think, we are being quite specific on our sales guidance, and also that we will start to see a recovery in our EBIT margin. Clearly, there is some uncertainty still in the market that how will the China market – which, we all know is very important to us. It's a good and profitable market for KONE, how that will start taking off. But I still believe that we have a quite a specific outlook there. So, I hope that's helpful to everyone, the guidance we've given.

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj A

Maybe I'll then continue on the cost or raw material/component cost question. And as you said, so we are seeing raw materials, especially in China, having a positive impact. And that is something that we expect for year 2023. At the same time as Henrik was highlighting, that even though the raw material part of the component cost is coming down then we are seeing the inflation, in general, having a negative impact to this, value-added parts or the processing cost to the components. And as a result, raw mats are a tailwind. But then due to this overall inflation, so the component costs are a slight headwind. So it's not a huge headwind. So some tens of millions, but clearly, a headwind still on an overall level.

Lars Brorson
Analyst, Barclays Capital Securities Ltd. Q

Well, thank you, Ilkka, that's helpful. Would it be fair to assume that the €400 million headwind over the last couple of years would reverse, say, over the next three years at which you could get, say, €100 million this year, just to help us a bit for our EBIT bridge for 2023.

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

So first, I guess, if I would know whether, yeah, raw material prices for the next three years would go, I think there's other opportunities and just elevate the business. But...

Lars Brorson
Analyst, Barclays Capital Securities Ltd.

Q

Just assuming current price [indiscernible] (00:29:41).

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

Yeah. Yeah. That's more of a joke, so all in all, in your bridge for 2023 as a result are the component purchases that we're making are a slight headwind. So even though the raw material comes down, then still the cost is a slight headwind for us as a result. So that's the situation in 2023. Now, if it continues to go down the raw material part, then you need to take a view on the inflation. But obviously, if it continues to go down and inflation starts to come down as well, then it will start to be a tailwind as a result. And then, of course, we're taking a lot of action to reduce our own product cost through the offering. And that's, of course, something that is also supporting. So a lot of moving parts here when we look at component costs and then, of course, offering where we are driving some quite positive change.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

And maybe to add to that, as we talked about earlier in conjunction with the earlier results, clearly in this cost environment, also the focus on scrutiny on product cost, for example, has been on a different level, and we've been able to see quite a good development there. So it is something that will contribute positively going forward being able to then counter some of the inflation that we see overall.

Lars Brorson
Analyst, Barclays Capital Securities Ltd.

Q

Briefly. Secondly, if I can, and finally, just on the market outlook, Henrik. I was quite encouraged to see the new equipment [indiscernible] (00:31:12) flat this year and modernization clear growth. I think we were all bracing ourselves, maybe something that was a bit worse, maybe help us understand a bit better what you see in that part of your business. And secondly, within market outlook, negative 10% for China feels a bit conservative if we get a completion backlog pick up that part of your business. Could you help us understand or frame how much of should we say completion backlog is already on the books today versus an order opportunity in 2023 potentially? Thank you.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

This order backlog, I would say magnitude wise and that's always going to be a backlog but let's say that's probably close to a year of volumes in deliveries and half a year of volumes in orders. But how quickly does that come through? So that's uncertain. There's always going to be a backlog. But if we get a better financing situation that could be leave a tailwind. But it's clear it's going to take some time before that starts improving. Therefore, the first half of the year is likely to be more challenging.

When it comes to Europe, it's clearly varies quite a lot. They're quite strong markets in the Middle East in particular, of course with high commodity costs, they have a good situation there. Then within Europe it varies between segments, quite a lot of infra building. So it varies a lot market-to-market but the good thing is that it continues to be opportunities to be to be taken.

Lars Brorson
Analyst, Barclays Capital Securities Ltd.

Q

Helpful. Thank you both.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

Thank you.

Operator: The next question comes from Daniela Costa from Goldman Sachs. Please go ahead.

Daniela Costa
Analyst, Goldman Sachs International

Q

Hi. Good afternoon. Thank you so much for taking my questions. One, is a follow up actually on the margin question and the second one is on the cash flow from operations. But maybe starting by the one this follow up, maybe I didn't fully grasp your answer there, but so you're guiding for your margins to bebe slightly up. Your volumes are flat, raw mats minus components seems like it's not a big driver. So what is – is it some of the €100 million of savings already in that bridge? Is it mix? Is it sort of what do you assume for China margin? If you can re-explain, sorry, to ask again about what drives that margin up because originally, I guess I thought at least it would be raw materials but it doesn't seem to be the case and then I'll ask the second one afterwards.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

And thank you for piece meaning the questions. It's much easier for us. So, yes. So as you said, volume wise we're quite flat with this guidance. Mix wise it's neutral in a sense that we continue to see good opportunities in services at the same time with the orders development that we've seen, particularly in China that is the other side of the coin. Then it's good to note that we've seen increase in orders margins in the last quarters since third quarter of last year. So that's obviously something that we will now deliver and as we go through the order book to new and newer orders, it will have a positive impact to our results this year and some of that will carry over to 2024 as well, where the order book rotation is slower.

Then negative side on that bridge is overall cost inflation. So for example, salary costs are continuing to be on a higher than normal level a headwind. And then yes, there will be some cost benefits from the new operating model but the €100 million we set as a target, the full impact of that is only expected in 2024 but there are some tens of millions that will help also in 2023 as we go through the program and implement new structure.

Daniela Costa
Analyst, Goldman Sachs International

Q

Okay. That's very clear. Thank you very much. And my second question is regarding the cash flow from operations and you talked about the key make up, but looking at the amount of advances as a group, it doesn't look like a huge difference, so I guess is really the receivables. And can you talk about what's going on in China? Is – was it a one-off in Q4? Do you expect to receive a big inflow from these receivables into the beginning of the year? If you could give us some clarity, I guess, sort of what the visibility you have of getting paid in China. Thank you.

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj
A

Well, first, if I think about item by item, the net working capital development, so clearly our payables are coming down quite a bit compared to end of last year – sorry, end of 2021 as well as in the quarter. And that's then normalizing, as I talked about the timing difference of the payables. Then on advances, normally, if we have a growing business in – they're actually contributing positively to net working capital, meaning that it is further negative. And now we don't see that, orders growth in China is the key driver there. Elsewhere, we've seen better development there. And I think on a quarterly basis, as I always say, cash flow will fluctuate. But if you look at the situation, so overall, we've seen a more difficult quarters in China starting from lockdowns in Q2 and the tightness in liquidity overall that is impacting and also having then impact on receivables being the key driver there.

Daniela Costa
Analyst, Goldman Sachs International
Q

Very quickly. So no bad debt increases or is it just a timing?

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj
A

Well, we've reserved bad debt as we see risks, but that's not the driver for our net working capital development.

Daniela Costa
Analyst, Goldman Sachs International
Q

Understood. Thank you very much.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj
A

Thank you.

Operator: The next question comes from the line of Aurelio Calderon of Morgan Stanley. Please go ahead.

Aurelio Calderon Tejedor
Analyst, Morgan Stanley & Co. International Plc
Q

Hi. Good afternoon, Henrik and Ilkka. Thanks for taking my questions. I'll take them one at a time. First of all is around the China market and apologies because I already asked this in the third quarter. And if I look at that slide, you showed that you had slightly underperformed the market. So I just want to understand if that's driven by you not going after every single project or what's been to driver, do you think you're losing market share or do you just think it's a conscious decision not to take orders [indiscernible] (00:38:02) margins?

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj
A

So if I look at – for the full year, in China last year, we're in line with the market or even perhaps slightly above and it varied quarter to quarter as it usually does. In second half of the year, we had quite a lot of focus on pricing and that's contrary to positive in Q3. In Q4, we continued to be very focused on making sure that we take orders that are high quality, i.e., payment terms are in place and also margins makes sense. So that's perhaps the biggest reason. I would say it's quarter-to-quarter fluctuation. We continue to have very strong position there. In end of the last year, particularly second half, the liquidity situation of many of the developers was challenged. And one needs to be very focused on making sure you take orders where you're going to get paid. And that's one of the things we kept high focus on.

Aurelio Calderon Tejedor
Analyst, Morgan Stanley & Co. International Plc

Q

That's helpful. Thank you. And it's probably a little bit of a follow-up on some of the previous questions around raw materials. But if you could confirm what the raw material headwind was in 4Q. Is that €400 million – sorry, that €300 million sort of guidance for the full year that you provided is sort of the number where you ended up? I'm just trying to trying to understand how much of the run rate in 4Q for the margin should we assume heading into 2023.

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

So the actual number for the full year is quite close to €200 million that I've quoted already earlier. And as a result there was a slight, I guess, headwind in fourth quarter but not big enough to be called out individually. And your question on the run rate on fourth quarter, I think it's also good to note, if you look at the seasonality that we tend to have a quite a good margin always in the fourth quarter. And then given the timing of, for example, Chinese New Year and market development in China, so first quarter is a bit different. So you need to also take into account the seasonality in margins.

Aurelio Calderon Tejedor
Analyst, Morgan Stanley & Co. International Plc

Q

That's clear. Thanks very much.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

Thank you.

Operator: The next question. Sorry. The next question comes from Klas Bergelind from Citi. Please go ahead.

Klas H. Bergelind
Analyst, Citigroup Global Markets Ltd.

Q

Thank you. Hi Henrik and Ilkka [indiscernible] (00:40:34). So my first one is coming back on the cost side and looking at the China impact from lower raw mat, you don't have much hedge this year versus the rest of the world, do you see the impact already now? So let's ignore the component inflation for a moment and just zoom in on the raw mat. And if you look at the current spot levels, I guess based around €80 million annual potential tailwind and I guess a component of electronics [indiscernible] (00:40:58) elevated, but the raw mat impact in China, I think is 60% of the total headwind, which is now reversing to the order what they thought in the quarter, is that a number you would agree with? Around €80 million and then you add the €10 million headwind from component cost on top of that? Thanks.

Ilkka Hara

Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

I guess your net-net impact is different than mine, meaning that raw materials plus the inflation is a headwind rather than tailwind. If I understood correctly, you are proposing it to be a tailwind for us. Particularly in China, the raw materials are developing more favorably and maybe also the inflation in overall is a lower impact there. But then in China, we've seen also pricing be more challenging.

So I'm not going to comment area by area this, but dynamic wise, it's a bit different dynamic in rest of the world versus China.

Klas H. Bergelind

Analyst, Citigroup Global Markets Ltd.

Q

Yeah. No, I was commenting on gross impact rather than network pricing, but you might have alluded to network pricing then, Ilkka.

Ilkka Hara

Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

Yeah. In rest of the world, yes, clearly, pricing contributes positively.

Klas H. Bergelind

Analyst, Citigroup Global Markets Ltd.

Q

Yes. Fine. I might circle back on that. In terms of – my second one is on the orders margin where you say that's now back to levels we saw end of 2020, that's around 14%. When we look at the total backlog conversion now with China typically [indiscernible] (00:42:40) maybe 12 months, America maybe 18 months or more. That's 14%. How quickly do you think you can convert that, Henrik? Is that end of 2023, start of 2024? I'm just trying to think about the conversion.

Henrik Georg Fredrik Ehrnrooth

President & Chief Executive Officer, Kone Oyj

A

Well, we haven't quoted any specific numbers on what that margin was. I think, Ilkka was pretty clear in his presentation that when we talk about recovery margin, we talk about outside of China. In China, pricing has to be more challenging, but at the same time, cautious. Or the cost picture is clearly better in China than the rest of the world. So, from margin perspective, it doesn't differ that much but clearly, recovery has been better in other parts of the world. Then we also have to remember mix that China is – continues to be a very profitable new equipment market. So, when that share comes down, that from a mix perspective a little bit – is a negative for us. But with this current rotation, we're going to start gradually more and more this year, get good pricing coming through. But that's going to flow into 2024 as well, particularly, larger projects in Europe and particularly North America.

Ilkka Hara

Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

And it's good to remember that North America has been one of the markets where we've seen pricing developing most positively. So that gives us a good tailwind then into 2024 from that perspective.

Klas H. Bergelind

Analyst, Citigroup Global Markets Ltd.

Q

Thank you.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

Thank you.

Operator: Next question comes from the line of Miguel Borrega [indiscernible] (00:44:14) Exane. Please go ahead.

Miguel Borrega
Analyst, Exane SA (United Kingdom)

Q

Hi. Good afternoon, everyone. Two questions for me. The first one just on your market environment guidance for North America and Europe. Just wanted to dig a little bit deeper on that and your expectations. You said North America, slightly down, flat in Europe. Can you just comment on your exposure in each market? I guess in the US, it's mostly non-resi, which is typically more resilient. So, I was just wondering why you expect the market to be down.

And in Europe, obviously, the resi market is quite weak. It's also a bit surprise you think it's going to be flat. So, just wondering what you're seeing on the ground for each of the Western markets?

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

Okay. So, in North America, clearly there is a lower share of residential, but the residential is an important part of the market. But also, we're seeing a slowdown in the office market there as well. It's clear that many companies are now thinking about their situation, also developers with higher financing cost, there's clearly less speculative construction right now. So that is what is impacting, but I would say it continues to be at the good level of the market there.

In Europe, it varies a lot. If you look at housing, yes, we can see that housing starts and approvals are coming down in most places. But there's still apartment shortage in most of Europe. But what are the sectors that are improving? So when we look at Europe, we say Europe, Middle East, and Africa. So it's clear that Middle East, there are some very strong markets that are actually growing very nicely with a lot of opportunities. So Middle East is clearly the bright spot. Then you can see quite a lot of continued infrastructure construction, and actually some of office continues to be pretty okay in many parts of Europe. So it varies a lot. And I would say really the strength comes from Middle East. It's the big strong part.

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

And then maybe to add just to make clear because we are talking about the same thing. So when we talk about market outlook, we look at the total market for elevators and escalators there with the comment and maybe it means elevators given the volumes. Then we don't guide ourselves our orders received. We only comment on sales, so that's also good to note.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

Yeah.

Miguel Borrega
Analyst, Exane SA (United Kingdom)

Q

Thank you. And then in services, can you give us a bit more color on pricing for 2023? I appreciate the color on slide 6 where you grew your maintenance base by 5% volume, which leaves pricing roughly at 3% in 2022. I suppose if you update pricing by, let's say, last year inflation, so how much are we talking about for 2023 and how easy is it to enforce these price increases? And then lastly, where do you stand on the connected unit? Thank you very much.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

Thank you. So, first of all, it's not that 3% is how much we increased prices because if you think about our portfolio, where we're growing the fastest, it's in Asia, particularly China and India where average monetary value per unit is clearly lower what is in Europe or North America. So that's, of course, making value lower per unit. But then through successful pricing, 24/7 connected services and so forth is actually making it higher.

So I think the gap is actually quite positive there. If you look at prior to 2018, it was always the – almost the opposite, the average value per unit. Now, we are not going to comment so much on pricing yet because pricing for maintenance is happening right now for the year. So we can talk about in the first quarter more results. Only thing I can say it's higher than prior year because of the trends. But then, let's see, we're always very cautious that we don't comment on pricing going forward, but we are just negotiating with customers.

So let's see what the outcome is when it comes. But I would say, I'm quite encouraged there. On connected units, we are now over 20% of all KONE units connected and roughly 15% of our total base is connected. So continuous good growth and that also contributed more than a percentage point to our growth last year.

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

And in the markets where we have maintenance contracts which are tied to some kind of inflation index, Naturally, that index last year did not fully reflect yet the inflation we've seen because inflation was just picking up. So in those markets, the inflation now has been a bigger part and then gave us a good environment for escalations. But as said, we'll come back pricing when we look at [ph] both the fact (00:49:35) what we've been able to accomplish.

Operator: The next question comes from [ph] Jing Zhang (00:49:46) from Credit Suisse. Please go ahead.

Q

Hi. Good afternoon, and thanks for taking my question. I have two questions and the first one is on pricing. Firstly, with China, in the presentation, you mentioned like-for-like equipment prices declined slightly and pricing environment continues to be intense. And I'm wondering if you have observed any sequential signs of improvement or at least stabilization on China pricing. And now with China commodity prices now roughly reversed all the inflation we saw over 2021 and 2022, I'm wondering what's your expectation on pricing environment in China going forward.

And on the same topic more broadly for other regions, would you say that low-teens is a sensible estimate of the price increase in North America and Europe on your equipments? And now with raw materials coming to – raw material almost coming to a tailwind but on the other hand, we observed industry have been lagging its larger peers in building space in terms of pricing action. So that, I'm curious how you see the pricing environment develop in 2023 in North America and Europe as well?

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

I would say, first of all, we're not going to comment on pricing environment going forward. That we don't do because that is something between us and our customers, and then in hindsight, we're going to look at what commercial strategies we deployed.

In China, what we can say is that yes, pricing environment was challenging. Perhaps we started to see some signs of stabilization because it's clear that with – the environment for everyone has been very challenging even though, as you said, that steel prices have declined clearly there. So that is a helpful thing for China market but pricing has been very tough there. So we expect – we have seen some stabilization now. What we're going to see going forward, let's see.

Q

Thank you. That's very helpful. And my second question is on maintenance conversion rate in China. If I remember correctly, you previously mentioned about 60% for KONE owned brand. So I'm wondering, what is the roadmap for conversion rate to develop and to catch up with other [ph] regions (00:52:14) going forward in the mid-term? Thank you.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

So pretty much the same level last year as previously. It's clear that we're taking a lot of action to improve conversions and retentions. We know that the market there is very competitive and a lot of independent players. So through value-added services, through connected services, those are for example ways how we can improve both conversion and retention.

And also we're seeing that where they're starting to deploy condition-based maintenance where you can use more connectivity and you can therefore reduce your visits, that – there is a better situation. But it's still only a few cities that have this and we're going to start to see a gradual increase in that, but that's going to take some time. So those are the actions that are on the table to be able to improve conversion. So I think regulatory environment also is an important factor there.

Q

Got it. Thank you very much.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

Thank you.

Operator: The next question comes from the line of John Kim from Deutsche Bank. Please go ahead.

John Kim
Analyst, Deutsche Securities (Pty) Ltd.

Q

Hi. Good afternoon. Thanks for the opportunity. I was wondering if we could pivot back to China for a second, some color or context on the following ideas or topics. When you think about broad-based stimulus, are there specific programs or initiatives perhaps we should focus on? I'd also be interested to hear about kind of adoption of the newer – or lower ASP product that I think you had mentioned in the Q3 call. I do find that the market is evolving to a lower ASP. And how should we think about that when we think about the market on perhaps a two- or three-year view? Thanks so much.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

Thank you. So when you think about the China market that – what has been important? If you look at last year, the biggest challenge in the market was clearly the liquidity for developers. Three red lines policy was a very strict rule. And therefore developers that had a weaker situation just didn't get financing, and they were unable to refinance or even restructure themselves. That has changed. That is perhaps the most important thing that developers, both private and the ones with state backing, are able to refinance themselves and get financing. They will, of course, first need to get their bonds to refinanced and all that, and then we think the market will start to flow better. But that is perhaps the most important thing.

And it was really in November, the 16-point plan that was announced by the government that had many of these elements in there. And we could also see the importance of three red lines policy has been declining. It's clear that the developers, many of them need to strengthen their balance sheet, but as said, the most important thing is that now they are able to do it. They weren't able to do it during last year.

Before we start to see an upturn, the other thing we will need is consumer confidence for consumers again to have confidence to buy apartments. And that probably is going to take some time when the economy starts to pick up now when COVID policy have been loosened. So there seems to be some encouraging signs now or during Chinese New Year of consumers' propensity to spend and be out there. So I think those are the important things we need to see.

John Kim
Analyst, Deutsche Securities (Pty) Ltd.

Q

Great. And could you touch a little bit about the lower ASP products for the newer products you're introducing?

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

So also, that has been a feature in China over the past years is that perhaps the market that has done better has been the more affordable end of the sector. There are some opportunities also in a more valuable products, but that has been, perhaps, where the highest volumes have been. So yes, we have renewed our offering for lower end and made sure that cost is at the right level. So we start to see good demand for that, of course, in the market context that we have right now.

John Kim
Analyst, Deutsche Securities (Pty) Ltd.

Q

Okay. Thanks so much.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj
A

Thank you.

Operator: Our next question comes from the line of Tomi Railo from DNB. Please go ahead.

Tomi Railo
Analyst, DNB Bank ASA (United Kingdom)
Q

Hi, Henrik, Ilkka, Natalia. It's Tomi here from DNB. Two follow-ups, actually. Did I hear correctly that, Ilkka you said the price increase is going to be higher this year compared to last year?

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj
A

I said very clearly that we are not commenting on price increases for this year. I'm saying – what I did say a little bit of course is that on maintenance side when it comes to annual price escalations that there're encouraging signs.

Tomi Railo
Analyst, DNB Bank ASA (United Kingdom)
Q

Got it. Thank you. It was – actually you who commented that. Secondly, in China, do you see any risk that the customers are starting to ask for lower prices because steel prices are moving down? I know that the market has always been particularly challenging, but any risks that the prices are going down?

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj
A

Well, I can say, first of all that of course, it's a very competitive market and it's where market pricing will set and then of course, everyone need to look after their profitability. So again, I would say what have been encouraging is how costs have improved and that has helped margins sequentially in China. And now what the price is going to be going forward, I think let's see it. To be successful there, one needs to continue to have a very competitive offering, great field operations and service. I believe we are very strong in those points. So, those are the things you need to have in place to capture the opportunities. But again, I'm not going to comment on pricing how we think that's going to go this year. That's – that we have to see then in hindsight.

Tomi Railo
Analyst, DNB Bank ASA (United Kingdom)
Q

All right. Thank you.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj
A

Thank you.

Operator: The next question comes from the line of Panu Laitinmäki from Danske Bank. Please go ahead.

Panu Laitinmäki
Analyst, Danske Bank A/S (Finland)
Q

Thanks for taking my question. I just wanted to ask about EBIT margins in China and rest of the world. Are you able to kind of directionally comment on where China profitability was compared to the rest of the group in Q4 and in the full year of 2022?

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj
A

Yes. China for fourth quarter as well as the full year was accretive to earnings, so its margin was above group level slightly.

Panu Laitinmäki
Analyst, Danske Bank A/S (Finland)
Q

Both Q4 and full year? Okay. Thanks. Can I just ask what about the sales mix? Is it still like 85% new equipment, 15% services, as you've committed in the past?

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj
A

Yes. It hasn't changed from that.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj
A

Yeah. Directionally, it's like that. Yes.

Panu Laitinmäki
Analyst, Danske Bank A/S (Finland)
Q

Okay. That's very clear. Thanks.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj
A

Thank you.

Operator: Next question comes from the line of Martin Flueckiger from Kepler Cheuvreux. Please go ahead.

Martin Flueckiger
Analyst, Kepler Cheuvreux SA (Switzerland)
Q

Yeah. Thanks, gentlemen, for taking my question. I'd like to come back on the raw material price issue. Now, if we could talk a little bit about steel prices in the various regions in 2022, so backward looking. I understand that what you said about the China development of the steel prices. What did you see in Europe and in the States, and what is it that makes you hesitant to fully answer I think the first question of this call which was, at current spot prices, what would this imply in terms of head- or tailwinds for you in terms of raw material costs? That's my first question.

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj
A

I guess – so I guess not – if you were asking about 2023 then, as I said already earlier, so yes, overall raw materials and obviously steel in different formats is by far the biggest one. It is coming down and is contributing positively. At the same time, then the processing cost – because we don't really buy that much pure raw materials, but rather components made out of those. So the inflation has driven the processing cost, value-added part up. And as a result, the component cost is a slight headwind. It's not a huge one, but a slight headwind in 2023.

Martin Flueckiger
Analyst, Kepler Cheuvreux SA (Switzerland)

Q

Okay. I got it. Thanks. And then the other one is also a clarification question. Regarding 24/7 Connected Services, if I understood you correctly because the line wasn't always clear, the contract penetration rate is above 20% now. Is that correct? And I also heard another number like 15%, if you could clarify that please, sorry.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

Sure. Sure, Panu. So we're saying over 20% for KONE equipment. And if you take the whole portfolio, we are roughly 15%.

Martin Flueckiger
Analyst, Kepler Cheuvreux SA (Switzerland)

Q

Okay. Thanks.

Operator: The next question comes from the line of Delphine Brault from Oddo. Please go ahead.

Delphine Brault
Analyst, Oddo BHF SCA

Q

Yes. Good afternoon. Well, thank you for taking my question. I have two, if I may. First, a follow-up question on the working capital. When do you believe you will come back to a more normalized level in working capital? Is it in the course of 2023?

And the second question I have is on your reorganization plan, you mentioned 1,000 job reduction. Can we have some granularity maybe by region and by segment?

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

Maybe I'll start with the working capital and maybe Henrik you want to talk a bit more broadly on the operative model changes. So working capital, well, it depends how you look at normality. We're now roundabout in working capital on 2019 level. So it is quite negative. It just was a lot more negative and now came down. And naturally, we don't guide working capital as such. But what I do expect is that, as we said, there's measures that we expect to be impacting China market. And they will also have a positive impact to liquidity available to property developers. So I expect those to continue to then help to recover the China market from liquidity perspective and then having a positive impact also to our working capital. But after the beginning of the year, I expect more normalized development thereafter in working capital.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

When we look at our renewal of our operating model, as you said, it impacts about roughly a 1,000 jobs globally. That will be – we haven't given a breakdown of that regionally, but it will impact all parts of the world when we are simplifying the organization. So therefore, yeah, it will be a global program for us.

Delphine Brault
Analyst, Oddo BHF SCA

Q

Okay. Thank you.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

Thank you.

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

And may be good to note that due to the legislation, we just gave a number for Finland, which we have to give out, so that's why there's one specific data point but not the others.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

Yeah. So, Finland it's about 150 people and then 850 rest of the world.

Operator: The next question comes from the line of Maidi from Jefferies. Please go ahead.

Rizk Maidi
Analyst, Jefferies International Ltd.

Q

Hi, Henrik and Ilkka. Thanks for the time. Just the first one is a clarification really. So you just spoke on a gross impact, so you said [indiscernible] (01:05:27) said component costs is tens of millions of headwind. Are you able to quantify the easing cost headwinds in China? And also the wage inflation, is that still 1 percentage points faster than normal wage inflation [ph] please, I'll stop there (01:05:44).

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

I guess on the cost headwind part, Henrik, now you're flipping slides as I speak.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

Sorry. Sorry.

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

So the cost headwind, we haven't broken down that to more granular level obviously. China is a big part of the overall manufacturing as well as deliveries, but we haven't commented that on more detail. Then remind me about your second question, sorry.

Rizk Maidi
Analyst, Jefferies International Ltd.

Q

Wage inflation.

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

Of course, that's good. So, yes, we are expecting wage inflation to continue to be higher than normal level and also higher than what we saw in 2022. So we're roughly speaking over €100 million in wage inflation as an extra cost as a result, so instead of 1%, maybe 2-plus percent.

Rizk Maidi
Analyst, Jefferies International Ltd.

Q

The second one is historically, the growth in your order book at the beginning of the year has historically correlated quite well with the organic revenue growth or organic, so the growth in local currencies that you're able to achieve. In this case, you're entering 2023 with 5% growth in your order book, and yet, you are guiding for flat revenue development. Understand that there are some delays in construction sites on both sides of the Atlantic. There's some sort of component issues that refrains you from that, but how can we sort of explain this discrepancy between the way you guide revenues versus your order book growth?

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

I guess the main contributor there, if you just look at our headline number, I agree with you. But as Henrik described, both the tailwinds and headwinds. So on the tailwind side, we are seeing order book rotation somewhat slower in 2023 and it is resulted, so if you think about the mix where we're seeing the growth, fastest rotation in the order book is in China and there we've actually seen a decline in orders received. And then the growth has been especially in North America, where we have the slowest order book rotation, so that's impacting overall then the order book conversion to sales, especially in the new equipment than in larger major projects.

Rizk Maidi
Analyst, Jefferies International Ltd.

Q

Thank you very much.

Operator: And our last question comes from the line of James Moore from Redburn. Please go ahead.

James Moore
Analyst, Redburn (Europe) Ltd.

Q

Hello, Henrik, Ilkka, everyone. There are lots of moving parts behind the EBIT margin this year and I'm afraid I'm coming back to some of them because I had a bad line, maybe just me, but I couldn't [ph] hear a lot (01:08:53). So currency, have you mentioned that [indiscernible] (01:08:58) or so positive last year. Do you expect this €50 million, €60 million negative impact to EBIT in FY 2023 [indiscernible] (01:09:07)

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

It's not that big of a driver in 2023, the currency. That's why we're not calling it out.

James Moore
Analyst, Redburn (Europe) Ltd.

Q

Okay. So sort of small negative.

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

And also remember that now this time, we've normally given maybe more specific guidance. Now, what we're saying is that related to first revenue that it's on last year's level and as well as then on profitability that it improves, expect it to improve in 2023 and the currencies are not having a big impact to profitability. So that's why we're not guiding also currencies as such.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

Basically, with weaker dollar and RMB compared to euro, that's a bit of a headwind from a translation perspective. That's clear.

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

Yeah.

James Moore
Analyst, Redburn (Europe) Ltd.

Q

Okay. And second one is on savings. Could you help me with the timing? I get the message a bit this year, more next year but is it €30 billion this year, €70 billion or is it €10 billion this year, then €60 billion, then a spill of €30 billion in FY 2025? I'm just thinking from a bridge perspective if you could help us with the €100 billion.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

Some tens of millions for this year.

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

The idea is that when you...

James Moore
Analyst, Redburn (Europe) Ltd.

Q

In 2025?

Ilkka Hara
Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

The idea is that this renewal will be completed during this year, which means it should be fully in place from 2024 onwards.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

So you would or you would not expect any impact in the FY 2025 bridge because there's a difference between a running rate at the end of 2024 and all achieved in the bridge in 2024.

Ilkka Hara

Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

So run rate should be full at the end of this year. Yes.

James Moore

Analyst, Redburn (Europe) Ltd.

Q

Okay. So nothing in the bridge in 2025.

Ilkka Hara

Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

No.

James Moore

Analyst, Redburn (Europe) Ltd.

Q

That's great. Thanks. And just lastly, I get the message on raw material and components together. When you've talked about raw material in the past, have you always talked about raw material component together, and are you able to say what the pure raw material gross positive would be this year?

Ilkka Hara

Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

In the past we spoke really focused on raw materials. And it was because the value added part was more stable and it didn't really have a meaningful impact. Right now, it actually has a very meaningful impact. So, therefore, we're now guiding a bit differently because purely that just looking at the raw material doesn't really tell what the impact is to our profits and profitability. So that's why we are now commenting it slightly differently.

James Moore

Analyst, Redburn (Europe) Ltd.

Q

But going back to Klas and others, [ph] NII (01:11:50) had €80 million, that sort of number, if one was to look at the raw material on a standalone, pure raw material basis with a sort of high double digit number, be an appropriate positive. But that [indiscernible] (01:12:02) by a slightly bigger negative on the componentry side.

Ilkka Hara

Chief Financial Officer & Interim Leader - South Europe and Mediterranean Region, Kone Oyj

A

I guess what I was saying was that we have some tens of millions of positive from raw materials and then an opposite inflation item. And as a result, net-net, it's a slight negative, but not big enough to be called out.

James Moore

Analyst, Redburn (Europe) Ltd.

Q

And lastly, if I could, I think there was mention about the adjective flight when it came to margin expansion for FY 2023. Is that an adjective you used or was that from thing that something that somebody injected into that question? I just wondered if there's any way you can quantify the consensus in 110 basis points. Is that broadly in line with your thinking?

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

We're saying very clearly that we're saying this. EBIT margins [indiscernible] (01:12:51) EBIT margin is expected to start to recover as a result of the margins orders received and the good performance of our maintenance business. That's what we are seeing right now.

James Moore
Analyst, Redburn (Europe) Ltd.

Q

Okay. Thank you very much.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

A

Thank you.

Operator: Thank you. There are no further questions. So I'll hand you back to Natalia [indiscernible] (01:13:15).

Natalia Valtasaari
Head-Investor Relations, Kone Oyj

Thank you. Thanks, everyone, for dialing in. Thank you for the questions. I hope you found the call informative, useful. I hope you got the answers that you were looking for. If you do have any follow-ups, please feel free to reach out to the team or to me. We're here to answer them. And otherwise, I would like to wish you a great rest of the day.

Henrik Georg Fredrik Ehrnrooth
President & Chief Executive Officer, Kone Oyj

Thank you, everyone.

Operator: Thank you for joining today's call. You may now disconnect your lines.