KION GROUP AG

Q3 2017 Preliminaries Conference Call

Conference Call Transcript

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Dr Thomas Toepfer (CFO)

Gordon Riske

Thank you. Good morning, and welcome to Kion Group's Preliminary Conference Call for Q3 2017. As a basis for this call, we'd like you to use the short presentation which is available at Kiongroup.com, under Investor Relations, in the Presentations section. Right now, I'm in the presentation, on page two. We have published our strong preliminary Group financials for the first nine months of this year, and at the same time, slightly adjusted our overall guidance. We are presenting a strong set of results from January to September 2017, with order intake and revenue of €5.7 billion, and an improved EBIT margin of 9.9 per cent.

While growth in order intake and revenue for the segment Industrial Trucks and Services, was stronger than anticipated, the segment Supply Chain Solutions did fall short of expectations. We have adjusted the outlook for both segments accordingly, which results in a slight downward revision of the outlook for the entire Kion Group.

The agenda for this call is as follows; we will start with a review of the preliminary financials Q1 to Q3, 2017, and then specifically the third quarter of this year. We will go on to explain some of the developments within the segment, and we will close the call then with our adjusted outlook for the full year 2017. So, let me hand it over to Thomas Toepfer, our CFO, who will present to you the Q3 preliminaries on the following pages.

Thomas Toepfer

Thank you very much, and also a very warm welcome from my side to this call. I'm on page three of the presentation, and you see our key financials. Let me start with the first nine months of the year; our order intake and revenue grew to €5.7 billion for that period, and our adjusted EBIT grew to €562 million, which will present a margin of 9.9 per cent. And this margin is above the previous year, despite material cost headwinds and FX transaction effects that we were facing.

The net income, as you can see, came in with €230 million, and is also above the previous year, despite the PPA effect from the Dematic acquisition. What you don't see on this page is the free cash flow, which came in at €120 million, compared with €65 million in the previous year, and you have that in the table of the press release that we have published. So, overall, we saw continued profitable growth between January and September, and that is also confirmed if you look at the numbers for the individual Q3, at the bottom of this page, so the order intake and the revenue grew to €1.8 billion, our adjusted EBIT grew to €195 million, which represents a margin of 10.5 per cent, again clearly above the previous year level, and the net income was €80 million, also above the previous year. Again, let me remind you, we saw a strong set of results also in Q3, despite some headwinds that I was just mentioning.

If you turn the page, on page four you see the key preliminary financials for the segment, Industrial Trucks and Services; the order intake value grew by 5.2 per cent, to €1.4 billion, in the third quarter, and the growth rate is below the growth rate for the order intake in units, which was 11.3 per cent, but that is due to product and also country mix. And we will provide further details on that, and on the market development, during next week's update call.

If you look at the revenue number, that number when up by 6.2 per cent, to €1.3 billion in Q3, and the adjusted EBIT grew by 6.1

per cent, to €153 million in the third quarter, which represents again a margin of 11.5 per cent.

So, at the same high level as last year, despite headwinds on the material costs side, which are especially related to steel and rubber, as well as foreign exchange headwinds, which are related to the British pound transaction effect, and so we were able to maintain the margin, as I said, on the very high level of Q3 2016. Overall, I would say we saw normalised growth and a stable EBIT margin in the ITS segment.

Now let me turn the page, to page five, and that explains to you the outlook adjustment for specifically the order intake in the segment, Industrial Trucks and Services Compared with the order intake in Q1 through Q3 2017, the implied order intake for Q4, or as we would call it, the year-to-go, based on our outlook for the year, would have been between €1.17 and €1.32 billion, and therefore would be lower than any of the previous quarters in 2017 that we've seen so far. And therefore, the adjusted outlook increases the upper and the lower ends of the order intake guidance by €200 million each to reflect the higher than anticipated momentum that we see across the regions.

What you don't have on this page, but you will see later in this presentation, the outlook for the revenue of this segment is increased similarly, by €150 million at the upper and the lower end of the guidance ranges, and the outlook for the adjusted EBIT remains unchanged, due to the material cost headwinds and FX transaction effects that I was just mentioning.

If you turn the page, you see the same set of numbers for our Supply Chain Solutions segment, which again are preliminary.

As you can see, the order intake was €493 million in Q3 2017, and thus above the order intake in Q1 and Q2, however it was at a lower level than we had anticipated. The revenue was at €514 million in the quarter, and the adjusted EBIT at €59 million in Q3, therefore resulting in an adjusted EBIT margin of 11.4 per cent. And this margin step-up shows that the segment is benefiting from a good project mix, and also the fact that the Monterrey ramp-up is progressing well. And, as I have stated previously, we are absolutely on-track to complete the ramp-up during the course of this year.

If you turn to page seven, the graph on that page explains the 2017 outlook adjustment for the order intake in the segment Supply Chain Solutions. So, again, compared with the order intake that we have seen in Q1 through Q3, the implied order intake for Q4, or again, as it is called year-to-go, based on our outlook for the entire year, would have been €0.9 billion and €1.2 billion, and therefore significantly above any of the previous quarters, and therefore the adjusted outlook lowers the lower and also the upper ends of the order intake guidance by €450 and €550 million respectively, so that the year-to-go order intake now is expected between €494 million and €694 million. This is definitely more in line with the previous quarters in the space, on a very detailed review of the project pipeline and direct customer discussions that we have had, and we will provide more detail on the underlying reasons on the next page.

Again, let me say that the outlook for the revenue for the segment is lowered, similarly by €250 and €400 million at the lower and the upper end of the guidance range, and the outlook for the adjusted EBIT is lowered by €25 and €35 million at the upper and the lower ends of the guidance due to the lower topline growth for the segment.

And with that, let me turn it back to Gordon Riske, who will provide you with more in-depth reasons for the adjustments that we have made.

Gordon Riske

Okay. I'm on page eight, and we're highlighting some of the key reasons for the outlook adjustment in Supply Chain Solutions. This analysis is preliminary and indicative; today we have this special call for this purpose, but it sheds light on the three main reasons we've identified for the difference between our initial outlook and now the adjusted outlook. So, the first one; most notably, we are seeing some hesitation to invest at our US retail customers, that is customers in the verticals, as we call them, general merchandise and apparel.

Secondly, we do see some delays in project decisions by customers, which push out signing of orders into the next quarter, perhaps also into the year 2018. We will only book an order intake if the project is formally signed. Third, we have lost some orders, among others, due to repercussions from late deliveries out of the Monterrey plant we acquired before Dematic. This is certainly the smaller part of it, but we have now taken our customers to Monterrey, to show them that the ramp-up has taken place, that the fixes have been implemented, and things are going as planned.

So, to summarise the Supply Chain Solutions segment, we have seen nice double-digit revenue growth in this segment year-to-date, so the company is growing. Comparing its performance with pro forma financials for the first nine months, 2016, we definitely see this double-digit growth. We have set ourselves very ambitious targets, based on our visibility into the activities at our customers, and we have had to adjust our outlook as I just explained. Nevertheless, and this is most important, we are benefiting from the growth drivers such as e-commerce, and the megatrends, such as automation and digitalisation and, thanks to Dematic, and our new Supply Chain Solutions segment, we are very well-positioned to profit from these growth opportunities.

If we want to sum all that up in one page, here on page nine, the complete picture of the adjusted outlook for the full year 2017, so for the Kion Group order intake is now expected to be between €7.550 and €7.900 billion, previously it was €7.800 to €8.250 billion. The target figure for consolidated revenue is in the range of €7.400 to €7.700 billion, previously it was €7.500 to €7.950 billion. The target range for adjusted EBIT is between €715 and €765 million, previously this was €740 to €800 million. The implied margin would be then 9.7 to 9.9 per cent, previously it was 9.9 to 10.1 per cent.

The free cash flow is expected to be in the range between €320 and €380 million, previously it was €370 to €430 million. And the target figure for return on capital employed is in the range of 9.0 to 10.0 per cent, previously it was 9.5 to 10.5 per cent.

Going through the segments individually, Industrial Trucks and Services order intake is expected to be between €5.650 and €5.800 billion, so previously €5.450 to €5.600 billion. The target figure for revenue in the range of €5.450 to €5.600 billion, previously €5.300 to €5.450 billion. And the target range for adjusted EBIT remains unchanged, at €605 to €630 million, so the implied margin range would be 11.1 to 11.3 per cent, previously it was 11.4 to 11.6 per cent.

And for the Supply Chain Solutions segment, the order intake is expected to be between €1.900 and €2.100 billion, previously it was €2.350 to €2.650 billion. And the target figure for revenue is in the range of €1.950 to €2.100 billion, previously it was €2.200 to €2.500 billion. And the target range for the adjusted EBIT between €170 and €195 million, previously it was €195 to €230 million, which implies a margin range of 8.7 to 9.3 per cent, previously it was 8.9 to 9.2 per cent.

This outlook is based on the assumptions that material prices will not increase any further, and that the exchange rate as it is in the moment, the environment remains stable. To put this, then, all into context, if you look on page ten we are showing the relative magnitude of the change in the guidance for the Kion Group that means, as a Group, order intake, at the upper and lower ends of the guidance ranges, is adjusted slightly downward between three and four per cent, revenue slightly downward between one and three per cent, and adjusted EBIT slightly downward between three and four per cent.

So, before we end the presentation, if you look on page 11 you will see our financial calendar. We will, as planned, present the full Q3 2017 results on October 26th, and the regular Q3 call will also take place on this date next week. This is where we can discuss Q3 trading and, of course, the final results, in more detail. This is a call today on preliminaries. And with this, we'd like to close the formal part of the update call and turn it back to the operator so that we can take your questions.

Operator

Ladies and gentlemen, at this time we will begin the question and answer session. Anyone who wishes to ask a question may press star followed by one on your touchtone telephone. If you wish to remove yourself from the question queue, you may press star followed by two. If you are using computer equipment today, please lift the handset before making your selections. Anyone who has a question may press star followed by one at this time. And one moment for the first question, please. And the first question comes from the line of Philippe Lorrain of Berenberg; please go ahead.

Philippe Lorrain

Morning, gentlemen. Philippe Lorrain from Berenberg speaking here. I've got a couple of questions actually, so I will start and ask them one after another. The first one is just on your topline guidance for the ITS segment; the question here is, you still keep the same kind of amplitude between the low end of the range and the high end of the range compared to the previous guidance that you were mentioning, but you are just moving up basically the trench. I am just wondering here, why do you keep the same amplitude for the range, is there any weaknesses that you are expecting in the market, or is it just the way you are guiding, which is quite conservative, and you don't want to disappoint on that side? So, that's the first question.

Thomas Toepfer

Well, I think on this one, I think there's no particular thought behind this; we just think that a range which is €150 million is sufficiently narrow for a business that is close to €6 billion. I think there is no uncertainty, or anything else, implied with that; we just feel that the magnitude of the range is the right one for a business of that size.

Philippe Lorrain	Okay, thank you. Then I move on to Supply Chain Solutions; my question here is could you give us some more light, actually, on the FX translation effect that you might have had in your topline, especially in Q3? I mean, that has been a slight headwind here on the order side, and probably also on the safe side, due to the fact that your business is around, if am not mistaken, around 17 per cent exposed to the US dollar.
Thomas Toepfer	I think, Philippe, just for the order of magnitude, our translation effect for the entire Group, if you look at the year-to-date numbers, is some rough €25 million that we have seen, and I think you can roughly guess from the split that of course the main US dollar exposure is to Supply Chain Solutions, but I think I would like to answer that question on a Group level, and I think €25 million is the right ballpark number here.
Philippe Lorrain	Okay, thank you; and I assume that's probably also the same magnitude, then, on sales, so orders and sales?
Thomas Toepfer	Absolutely; yes, you can take that number for both.
Philippe Lorrain	Okay, perfect, and then another question I had was actually on the slide eight that you showed; and you mentioned basically three factors for your adjusted outlook now on the orders and sales at Supply Chain Solutions. The first one is hesitation to invest, the second one delayed projects, and the third one lost orders. Mr Riske already mentioned the lost orders are actually the smallest part, how much confidence do you have here that actually the customers are coming back to you after the successful ramp-up in Mexico? That's the question.

And secondly, could you shed a bit more light on how to understand the guidance cut, and put in numbers what is going into the first factor, the second factor, and the third factor, just to have a rough representation here.

Gordon Riske

As I said, the last one is the smaller factor; my confidence is boosted in the past couple of months, we have seen some customers come back. I would say the punishment, as I call it, for mis-performing in 2015/2016, if you can imagine a $50 million warehouse being six weeks late, that's painful, and so customers are rightfully upset. And as I said in a previous call, Monterrey we fixed, in good shape, we will be through with all of that this year, and customers, the first ones, have come back. They have placed orders with some of our competitors, we know that, but it seems yes, we were late, but when we deliver, the stuff works. And some others may not have been late, but this whole concept of working around the clock, it seems not to be so easy around the world. So, I do have a good level of confidence that many of these customers will come back, and we're seeing some of that now.

Now, regarding the bucket one and two, that's hard to say; certainly the project pipeline, some of these delays, we have some big projects that are sometimes in multiple pieces, so you get one part of the warehouse, and the second and third part comes later, so that has happened on some of the bigger projects. And the first one, which is also an important factor, in that segment, you know, we're not talking about all segments, we're talking about general merchandise and apparel, we have noted that in the e-commerce business, there are some big players, and I think everybody knows who the biggest players are, that have made some very aggressive moves. And so if I look at some of these customers, which are also our customers, they're re-calibrating some of their strategies to compete with some of the biggest players in the market on how to address those aggressive moves that they've made. But, as I said, the last one is certainly the smaller part.

Operator: The next question comes from the line of Sven Weier of UBS; please go ahead.

Sven Weier: Good morning; a couple of questions from my side. So, just coming back on the last point you've mentioned, I understand it in a way; it's a kind of a cannibalisation, on the one hand Amazon invests, the other ones are losing market share, but wouldn't their response also be to automate more? So, do you think this is just a delay, or is this an ongoing cannibalisation that you see there? The second point is on what you said, that some of the contracts take longer to negotiate; how does that impact the profitability of that contract? Does it mean some of the bigger clients are also taking a tougher stance on the pricing? And the last point would be on if I look at the high end of your SCS guidance, basically suggesting flat sequential sales in Q4 for the SCS business, which I thought was seasonally rather the low point of the year, and at the same time the high end of the margin guidance signals the decline of the margin from 11.5 to eight per cent, so why would there be such a margin decline sequentially if revenues were flat? Thank you very much.

Gordon Riske: So, cannibalise, you're right, there is some of that as the top players are very aggressive; but I'm not saying it's going to prevent some of these companies from investing more, they will invest probably differently, in even more automation, even more robotics, but that's a process we have to go through. I think some of the very small competitors, if I just look at…you go through the US and you see some of the malls, and how empty they are; there's a reason for that, and some of those customers will certainly have to re-think their strategy. So, projects that take longer, it doesn't necessarily mean, at all, that the profitability is less, actually it means in some cases it's higher. We have seen some particular cases with, as I said, multi-phased projects, and I know the orders are coming because the first part of that site is already ordered, and we're doing the engineering work. But sometimes as these things progress, and you do the engineering work, you do have customers that change it along the way. And especially bigger projects, I'm talking €30, 40 million and higher, up to €100 million, there's a lot of room there to make some changes. So, it does not have an impact that the customers are, at this point, taking a tougher stance on pricing, and just waiting to get the lowest price.

Now, regarding the fourth quarter; we took the company over on November 1st, 2016, and the fourth quarter is traditionally a slower quarter, so that is perfectly in line with what we have been saying all along, that the fourth quarter is traditionally somewhat slower, because after Thanksgiving, the Christmas stuff, everything has to be in and running. And customers are less thinking about putting new things in, or installing things; it has to be working at that point.

Operator — The next question comes from the line of Ben Uglow of Morgan Stanley; please go ahead.

Ben Uglow — Morning, gentlemen; thank you for taking the questions. A couple. First of all, on the subject of the SCS margin guide, unless I've got my maths wrong, at the mid-point, for the fourth quarter we're looking at something like €30 million of adjusted EBIT, and at the mid-point as opposed to the high point, which some people seem to be looking at, you're actually guiding at four to five per cent type margins. What scenarios, or on what basis, did you want to guide to that at the mid-point? I guess what I'm curious to know is beyond any operating leverage or FX effects, are you building in any provisions, any charges, any write-downs? Or is there anything more significant happening on the pricing side that would actually have that outcome? Or is it just undeniably conservative? That's question one. Question two; at the second quarter stage this year we talked about double-digit margins for SCS, and I remember the conversation quite well; how quickly do you feel that we're going to be back on a double-digit margin trajectory for SCS? Is that something that we can reasonably expect in the first half of 2018?

Thomas Toepfer

Well, Ben, let me answer both questions. First of all, the implied margin for Q4, I think there's nothing specific behind, except for the seasonality that Gordon was just mentioning. Let me just remind you, it's a project business, and remember the margin for November/December last year, which we have published, was 3.9 per cent, so I just think that underlines that Q4 is, from a seasonal perspective, the weaker quarter, and therefore I think there's nothing specific in terms of negative development that we see for Q4. And the second answer is that if you look at the implied margin for Supply Chain Solutions for the year, we're talking about 8.7 to 9.3 per cent, so I think we're making good progress. You also see that through the ramp-up of Monterrey, on a quarter by quarter basis, we're making good progress. So, I think we're absolutely on the trajectory that we have outlined, where we said both segments will contribute to the double-digit margin for the Group.

Operator

In the interests of time, please limit yourself to two questions only. And the next question comes from the line of Sebastian Growe of Commerzbank; please go ahead.

Sebastian Growe

Good morning, gentlemen; thanks for taking my questions here. The first one is on the outlook, so taking it a little bit to a higher level than just looking at 2017, well knowing that this is a call on the quarter three prelims, but given what has happened now in the first nine months of 2017, can you just help us with understanding your expectations going into 2018 now? It would be very helpful to give us eventually an order backlog figure for Supply Chain Solutions as of end of September. And, from today's point of view, are you comfortable with your earlier indications that the SCS business should grow in double-digits also into 2018? And then, secondly, a follow-up to the currency impact and sensitivity; you've been alluding to the fact that your guidance is based on current exchange rates, but going into 2018, can you help us understand what the sensitivity is in a one cent change in the euro-US dollar, that would be very, very much appreciated. Thank you.

Gordon Riske

So, on the first question, 2018, again we have preliminary numbers today for Q3, we have a call next week, when we have the full set of numbers available, and it would be unusual now, in October, to give guidance for 2018, although I know that's of big interest to everyone, especially to us. However, the statement of double-digit growth in this segment is very viable; we are 100 per cent confident that this business in the Supply Chain Solutions will grow double-digits. That has not changed in any way, but now to say what the full guidance is, we're a little bit ahead of the game there.

Thomas Toepfer

And maybe in terms of the dollar sensitivity; talking rough numbers, I would say 20 per cent of our business is in the Americas, and business mainly in North America, so we're talking about roughly €1.5 billion if you take full year numbers, and therefore if the dollar exchange rate varies with one dollar cent, the impact on the revenue is anything between € ten and 15 million, but please remember, this comparison position does not hold true relative to 2016, because at the time we didn't own Dematic. So, this is of course including the exposure that we now have through the Dematic business that we own.

Operator

As a reminder, in the interests of time, please limit yourself to two questions only. And the next question comes from the line of Felicitas Bismarck of Deutschebank; please go ahead.

Felicitas Bismarck

Yes, good morning, everyone. I have two questions, then. The first one is a follow-up; so when you are so confident of double-digit, could you please tell us how much your new guidance on Solutions is actually implying in terms of organic growth? So, how much are you growing in this business right now? And the second one is actually a clarification; is the difference between hesitance to invest and delayed projects that the former is longer-term, and the latter you expect to come through in the next quarters?

Gordon Riske

Could you repeat the second one again?

Felicitas Bismarck

Yes, the question for me is, is the difference between the hesitance to invest as the reason for the shortfall for orders, right, the hesitance to invest, the difference between that and

	delayed projects that the former is longer term, and the second one, you would expect in the next quarters?
Gordon Riske	Yes, certainly there's some basic logic to that, because in the delay, that's customers that we are actively working with some of these projects, as you know, in the early stages.
	By the time you start the process to where you have a formal order, that can be three months, but it can also be nine months, or even 12 months, but we know the customers. On the SCS double-digit growth, I know we don't have the full pro forma financials for the year, we don't, but we have seen double-digit growth revenue year over year if you look at those internally. So we have shown on the revenue side that we have grown double-digit, and if I look at current order pipeline discussions with customers, there's no reason for us to question that at all.
Felicitas Bismarck	But is that organic growth that you are double-digit growing right now?
Gordon Riske	Yes, yes.
Felicitas Bismarck	Okay, thanks.
Operator	The next question comes from the line of Omid Vaziri of Jefferies; please go ahead.
Omid Vaziri	Yes, good morning; thanks for taking my questions. There are two questions, one on ITS first of all; if I take your new guidance for orders and sales, take the mid-point of that, and work out what the implied Q4 figures are for orders, it implies negative 1.5 per cent growth year over year in the quarter, and for sales, one

per cent growth, positive one per cent growth. Now, Q4, typically for the forecast, has been the strongest quarter and acknowledging that Q4 16 was also quite a strong quarter for the company, is this pointing to growth moderating in the forklift space much faster than we had expected?
And the second question is in relation to the SCS segment; based on what you've provided as the explanation for weak orders in SCS, would it be fair to say that Dematic's exposure today is to the customers that are a little bit slower in spending versus the likes of Amazon, some of the more aggressive spenders within warehouse automation?

Thomas Toepfer

Omid, let me take the first question. First of all, you're right, we do see some moderated growth. We don't see the growth terminating, or slowing down even further, but definitely Q3 and Q4, as we've always indicated, we would be expecting some moderated growth. The second factor to this is simply the translation effect because we're calculating the average exchange rate; the full effect then is reflected with the difference of the full effect to the new average rate as reflected in Q4, so I think there's also, let's say, some caution baked in due to that effect, which is reflected in the guidance.

Gordon Riske

Your second question, are we exposed to customers that take longer? Perhaps, but you always have to look at the relative size; Dematic is certainly, especially in this market, e-commerce, by far the largest one. So, when other competitors maybe have higher growth rates, but it's also a question of where's your baseline? What are you starting with? A €50 million order for a smaller company is a huge upside, for us, it's not that big of an effect.

That's one point, the other point is if I look at the leading companies, without mentioning any names, in the e-commerce, we are probably the main supplier for these things. So, yes, we have more exposure to bigger orders than most of the competitors because there are very few companies in the world that can handle a complex project in a three-digit order magnitude.

Operator

The next question comes from the line of Markus Almerud of Kepler Cheuvreux; please go ahead.

Markus Almerud

Hi, Markus Almerud from Kepler Cheuvreux here; I'd like to come back to slide eight, please, and the explanations for the projects. If I read you right, one of the keys for hesitation at least is general retail is just re-strategizing how to meet e-commerce, and the death of retail not all that, is that also the reason for the delayed projects? Are they among the same type of customers? And related to that, how much of your business is towards e-commerce, and how much is towards general retail, and that is in the US in particular? And secondly, I would assume that there are no risks for write-downs on the back of this? Thank you.

Gordon Riske

The second one, as I said previously, the question from Felicitas, Deutsche Bank, the delays in project decisions are customers that we currently are working with, or have engineering contracts with, and the final order, or the order changes that we have anticipated are not fully booked. So, that's a little bit different case; that's also something that, in my view, will sort itself out faster than the first one. And this is more of a US topic with general merchandise and apparel, and everyone knows who's dominating those industries at that time, so some of those competitors do have to re-think what they're going to do. On the write-downs, no.

Thomas Toepfer

I think if you want to have a specific revenue split by industry, I think you will find that in our investor relations presentation on our website, on page nine, where you see 13 per cent is pure e-commerce, but please keep in mind that also general merchandise, which is 20 per cent of the wholesale, 14 per cent is of course driven by the underlying development towards e-commerce, so that's like big players in the United States who have a multi-channel operation, do put automated warehouses in place in order to be able to also deliver into the e-commerce channels, so I think it is probably the biggest driver of the business, but you have the exact split on page nine, as I said, in the investor relations presentation.

Markus Almerud

Okay; can I just ask a quick follow-up, if I may? So this hesitation, what has changed between let's say the beginning of the year and the mid-year and now? Has this hesitation that you've seen, has it in any way accelerated? Or if you could just elaborate on how you've seen your discussions evolve throughout the year, would be helpful.

Gordon Riske

I wouldn't put that big of a statement that it has accelerated; I would say that as we have, since November 1st, when we purchased the company, we said this is a project business. This is a lumpy business, as I've said to some of you on roadshows that I've accompanied you, we have to learn how to manage the expectations in this business, and to understand it better.

This is a lumpy business, there are months when things go very quickly, there are months, I can think of two or three customers that I'm engaged with personally, these things take some time, but there is not really an acceleration as a structural effect. Maybe we have three customers right now, at this time, that are working on it, next year it changes completely because we have more of a customer that you've worked with for ten years. It's not that everybody buys the same way every year; it is a project business, it is a lumpy business, and as we said from the first day, it's a learning process also for us, of how to communicate, when to communicate that to the public markets.

Operator — The next question comes from the line of Martin Wilkie of Citi; please go ahead.

Martin Wilkie — Thank you; it's Martin from Citi. A couple of questions; so, the first one is on the mix in North America; as you've mentioned, you've given us the split between e-commerce and the other areas, but compared to your competitors, are you relatively higher market shared in traditional markets, and relatively underweight e-commerce? Just to understand that mix. And then, related to it; when you look at what you've been selling into North America, obviously you have a broad range of products from systems like conveyors that are presumably somewhat slower growth, all the way up to automation systems and software, presumably higher; when we look at what's happened so far this year, has it been one area, for example traditional conveyor systems and so forth that has really dragged this down? Just to understand a bit more about that. And the second question was just about your longer-term margin guidance; it sounds like you still have the same view on the underlying market growth rate being double-digit, but obviously you've re-set to a lower baseline. In your 2019 to 2021 margin targets for Supply Chain Solutions, had you assumed a certain level of volume, or does this reset make us think a little bit differently about how you're thinking about margin targets from 2019? Thank you.

Thomas Toepfer

Well, let me maybe take the last question; the long-term margin target that we have communicated, what we have said is that for that we do expect some mid-single-digit growth for our ITS segment, and we do expect double-digit growth for the Supply Chain Solutions segment, because we expect the market to grow double-digit in one or two outgrow, and we still want to out-grow the market, and continue to out-grow the market. And so, as Gordon Riske already said, we haven't published the numbers, but our revenue growth this year, in the SCS business, is double-digit, so I would say we're absolutely on-track to achieve the long-term margin growth, and thereby also the long-term margin target that we have communicated for 2019 to 2021. I think the guidance that we've given has not changed.

Gordon Riske

And regarding market shares, market shares are not so easy in the Supply Chain Solutions comparisons as it is in forklifts, where we have a real common statistic, the WITS statistics, but if you try to break it down into players that are addressing general merchandise, e-commerce, and so forth, and maybe not so much making small systems, or other parts that are not part of a larger system, then Dematic is by far the market-leader in North America.

Now you saw the split in our corporate presentation, the double-digit part of our business in e-commerce, we are one of the leading suppliers in the E-commerce, but in North America, Dematic is by far the market-leader. So, when you do have some issues with customers taking more time, it probably affects the market-leader more than it would affect the other ones.

Operator

The next question comes from the line of Frederik Bitter of Exane BNP Paribas; please go ahead.

Frederick Bitter

Good morning, thank you. So, the first one would be, despite the positive macro-economic backdrop, and also industry backdrop, I should say, why are customers in fact hesitant to place orders, and delay orders? And, in that regard, where do you think we stand on the demand cycle on the warehouse automation equipment and solutions business? And the second one would be if you could give us an indication for, because we have now done all the discussions, SCS, as you obviously said in your presentation, with your customers, the project pipeline, so how should we think about the quarterly order run-rate in Supply Chain Solutions going into 2018? Thank you.

Gordon Riske

Quarterly run-rate, difficult to answer for 2018 as we're having a preliminary call right now for the numbers 2017. But, this whole demand cycle; we have seen now a number of years of high growth in North America especially, in e-commerce, and if you look at the industry, and who the leading players are, I'm repeating myself a little bit, there are some very strong, very dominant players that are going even deeper into the sales channels of other, more traditional type of stores, especially when I talk about apparel, and these types of things. And so I think all of these companies are reviewing how they combat the one or two giants out there that are taking part of their business.

But I wouldn't see that as a demand cycle change at all, it's just changing to perhaps fewer customers, or fewer players in this market that are customers, taking a bigger share of it. So, I'm glad we are the leading supplier to the top two or three in this space, but we have no change in our view of the demand cycle; we see it as before, as a double-digit growth market, and there is absolutely no indication that that has changed.

Operator — The next question comes from the line of Richard Schramm of HSBC; please go ahead.

Richard Schramm — Yes, good morning. Just a question on Supply Chain Solutions; so, taking into account that you confirmed your guidance at the end of July, with the H1 figures here, are now saying that Supply Chain Solutions did not perform in Q3 as good as expected, and also the outlook has changed; should we draw from this that your visibility for this segment is even below one quarter? Which would be a dramatic low number, yes, so I'm really puzzled that visibility is even not reaching for a quarter in this business. Thanks.

Gordon Riske — Again, this is not a business like producing widgets, 1000 per day, and you have stock orders, this is a project business, and when you have projects of between €50 million and €100 million, all you need to do is have a couple of small delays and you're in another quarter. So, it's not a question of visibility, of knowing the pipeline; of course we know the pipeline, of course we know the discussions with the customers, we know where everythign is at, but sometimes to get a final order is a process that takes longer than anticipated. So, it's not a question of we don't know what's out there, or visibility, it's simply a lumpy project business.

Richard Schramm	Yes, but you should have a certain backlog; we have no backlog numbers here, but even at the end of a quarter, you should have a certain backlog, giving you an idea about what you will be able to invoice in the next quarter, right?
Thomas Toepfer	Of course we do have that, and I think this is also reflected in the fact that the adjustment for the net sales of course is significantly lower than we adjusted for the order intake, but, as you can imagine, some of the order intake that we would have expected in the second half would also have generated revenue, so I think this is just the natural relationship that we have in this business. And, as Gordon Riske said, it is to some extent lumpy, and that is true for both the order intake on a quarter by quarter basis, but it also has some effect on the revenue. But, as I said, the guidance range is much narrower, and the reduction is also much lower for the revenue, because we do have a higher visibility here.
Richard Schramm	Okay, thanks.
Operator	The next question comes from the line of Jasko Terzic of Metzler; please go ahead.
Jasko Terzic	Yes, the first one is also on visibility and backlog; I was just wondering with the book to bill implicitly guided to 1.0x, how should we deal with that figure in case that you are expecting a structural growth rate of ten per cent for 218? So, should we assume that the visibility of around six months, as we learned right now, that the order intake in the first half of 2018 has to soar to achieve those growth rates? And the second question is more a confirmation; can you confirm that you have organically

grown double-digit in order intake in 2017, and if you also can confirm it for 2016, it would be very helpful.

Thomas Toepfer

Well, let me take the last statement; what we said is the revenue growth in Supply Chain Solutions organically was double-digit in 2017, the number for order intake is lower than that, but the revenue growth was clearly double-digit. And we have not given any numbers for the previous years, so I think that was the statement that we have made. I'm not sure I understood your question 100 per cent with respect to 2018, because we haven't given any guidance for that year yet, and we will come out with that, of course, as we publish our annual report. But, as we speak today, the long-term view that we have, which is that the market is growing double-digit and we should out-grow the market, that is something that I think at this point we can clearly confirm.

Jasko Terzic

Okay, but book to bill, for me, indicates of 1.0x that you only have a stable sales performance in case of the orders will be translated into sales next year, so, when you say you are growing double-digit, and above market, this would then imply that the orders have to soar to accelerate the sales momentum then.

Thomas Toepfer

If you take it mathematically, I think you're absolutely right, but again our guidance is more over a longer-term horizon, until 2019, and you will of course, just because it is a lumpy business, on a quarter by quarter see that the book to bill ratio is fluctuating, but we are probably looking at a short-term effect and, mathematically, I wouldn't contradict what you have said.

Jasko Terzic

Okay, thanks.

Operator	The next question comes from the line of Bjoern Voss of Freiburg; please go ahead.
Bjoern Voss	Yes, good morning. Just a follow-up question on the SCS segment; I'm actually curious if the issues you have, the hesitation of customers and delays of projects are really limited to the US, or if we also see some issues in EMEA or Asia. That is my first question, thank you.
Gordon Riske	Mainly US.
Bjoern Voss	It's mainly in the US, okay. And secondly…
Gordon Riske	It's by far the bigger part.
Bjoern Voss	Of course, but still one-third, I think, is in other markets. And, secondly, when it comes to the reduced guidance for the ITS segment, the margin guidance, which is down a bit, this is really just due to some material headwinds as it had steel and rubber, and the translation effects, no other issues like mix or pricing?
Gordon Riske	No; as you have correctly said, it's purely due to the material headwinds and, of course, also to the effect of the British pound that we have seen if you compare to 2016.
Bjoern Voss	Okay, that's it. Thank you.
Operator	And the next question comes from the line of Philippe Lorrain of Berenberg; please go ahead.

Philippe Lorrain Yes, thank you, gentlemen, for taking my follow-up. I just wanted actually to know a little bit more if we had as well in your order intake development a, let's say, shift from orders with a high portion of your own value-add versus perhaps larger orders as well with a less significant portion of your value-add? If we have some mixes here at stake, or perhaps the resource effect actually from one year to the other, which would explain why you have this very lumpy development, so that's the question here.

Thomas Toepfer No, we don't see that. We have alluded to some mix effects for the ITS business, and in terms of country and product mix, but we don't see a shift in mix for the Supply Chain Solution business.

Philippe Lorrain Okay, thank you. And then just a follow-up, again on this, not hesitation of customers, I think that is understood, on the delays regarding your orders; I think you were mentioning some price discussions that you have with clients, can you indicate if it's really affecting these delays, which means that you have already done some engineering work for these guys, and now they are trying to push down a little bit the price, which is affecting the margin profile? Or the question would be also if you have now perhaps, even if the contracts are not booked, as Mr Riske said, but perhaps already you have agreed with the clients on these contracts, if you have already lots of letters of intent?

Gordon Riske I didn't mention that we're having price discussions; that, I did not mention. Normally it's more of a technical discussion, because once you have part of the total project as an order, and the customer has an add-on, or a change, or a significant new component that has to come in, that's more of an engineering question, and agreeing on the solution. The price basis is done already, with the first orders, so we don't have the case where okay, we negotiate something, then we make a project, we get an order, and then the customer comes back and says well, I want 30 per cent more value for the same price. No, that's not the case.

Operator

And the next question comes from the line of Peter Murdoch of Morgan Stanley; please go ahead. Mr Murdoch, your line is open.

Peter Murdoch

Yes, hi, Gordon, hi Thomas; sorry, I was on mute there. Just a follow-up to Ben, three very quick questions. On cash flow, the revision on the free cash flow number, is that purely just an effect of the lower EBIT number, and I guess lower order number, and hence pre-payments in Supply Chain Solutions? That's just question one there, question two is on the trucks business; is it possible you can give a margin number x the raw mats, and x the FX, just so we can kind of see what the operating leverage is there, and whether it's changed throughout the year? And then the final one, I know it's not the biggest issue that you highlight of the three reasons for SCS and the lower order intake, but you highlight Monterrey and the loss of orders there, but you also say Monterrey, among other reasons as well, on that comment on page eight; could you just elaborate on that if you can, please?

Gordon Riske

Let me start with the last one, Monterrey, and again it's a little bit repeating what I said before, is we have had cases where we have made commitments for start of production dates that we did not meet, or previously, before we owned the company, it was very significant in 2015, that have not been met and customers just made a decision. So, once a factory like

Monterrey has an issue, it affects everything, and how the engineering work is done, you have so many changes that you have to make to try to compensate for some of the time in the factory, so we don't have another particular effect for that, the main effect is we have had delays in go-live, and customers have punished us for some of that. We have fixed the factory, and by the end of the year that is all done.

And I expect, and we have seen some of that, many of those customers come back, because, as I said, at the end a delay is one thing, but a working system that works continuously around the clock is another thing, and we've always proven that our systems do work, and are very robust, And I think that's the biggest argument we have.

Thomas Toepfer

So, on the other two questions; first, I think cash flow, you are spot-on, it's exactly the two effects, one is the EBIT reduction, and the second effect is the lower pre-payments, and therefore the effect on cash flow is higher than on the EBIT line. With respect to the qualification of the FX effects and the headwinds from purchasing; I think what we have said is we have seen negative headwinds for material costs which were high single-digit for the first half of the year, I'd say that number has probably doubled by the end of Q3, and I'm expecting again the same additional incremental effect in Q4. So, I think that just gives us the order of magnitude what this could be, and I would say the British pound transaction effect that we're seeing this year is also similar in size to that effect; I'm a little bit reluctant to exactly quantify it, but it gives you the order of magnitude for those two effects and therefore also the margin impact that his has on the ITS business.

Peter Murdoch

That's perfect, Thomas, I can do the math. Thank you.

Operator	I'll hand back to Mr Gordon Riske for closing remarks; please go ahead, sir.
Gordon Riske	Thank you for all participating in this call today; again it's preliminary numbers, we do have another opportunity next week, when we release all the numbers and engage in more detailed discussion. Again, we'd like to close this part of the presentation, and welcome you all back when we have our call.