

KION GROUP AG

Q2 2024 Update Call

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Rob Smith

Thank you, Francy. Good afternoon, ladies and gentlemen, and welcome to our Update Call on the Second Quarter Results. Please refer to our presentation on the IR Website for the call.

I shall start off with a quick summary on the second quarter results, and I'll give you a business update. And then Christian's going to take you through our detailed financials and our outlook for 2024, which we have not only confirmed today, but we've also narrowed the guidance ranges following the good performance in the first half and our updated view on the market. Then I'll come back and take you through our key takeaways, and we'll move into the questions and answers.

So let's start together on page 3. Group order intake at €2.6 billion and reflects a seasonal improvement in the ITS segment and the ongoing lumpiness in the SCS segment.

KION had another solid quarter with revenues at €2.9 billion, and our adjusted EBIT at €220 million and the adjusted EBIT margin at 7.7% both increased year-on-year, driven by improvements in both of our operating segments.

Both segments continued to benefit from our measures to improve operational and commercial agility. Material availability continued to be strong, and we monitor diligently and track the situation of our suppliers and their supply chains, allowing us to put mitigation actions in place in good time.

Free cash flow came in at €137 million positive, driven by the improved adjusted EBIT and almost stable net working capital, and earnings per share were €0.52 from €0.54 in the second quarter of last year.

Let me give you some insights into our latest business developments on slide 4. I'm proud to report that, for the 12th time, our brand STILL has won one of the coveted awards, the IFOY Award. Many of you know this is the International Intralogistics and Forklift Truck of the Year Award. And STILL once again impressed the international jury with its EXV iGo automated pallet truck, winning first place in the "Mobile Robot" category.

STILL's EXV iGo is STILL's first automated vehicle to be produced in series production at industrial scale and based on a thoroughly modular concept. The central idea is fast availability and maximum scalability for our customer solutions.

Thanks to industrialized production and modular system parameters, our EXV iGo is quick to be put into operation using our commissioning software iGo easy.

Service and maintenance are also fast and flexible, thanks to our new digital service concept, allowing our service technicians to access the machine's digital twin for each of our individual vehicles for diagnosis and troubleshooting even before getting on site.

Another innovation this quarter is Dematic's launch of the Noise Reduction Portfolio, with comprehensive solutions that cure our customers' noise problems in their operations. Our portfolio reduces noise at source by up to 15 decibels, creating a quieter work environment that supports employee productivity, employee safety, and overall well-being.

Furthermore, only Dematic uses 3D noise mapping audits across our customers' facilities to pinpoint noise and measure sound levels before and after the retrofit, so our customers can feel, hear, and see the differences.

Another highlight in the quarter was on the sustainability front, where KION Group was named one of Europe's Climate Leaders in 2024 by the Financial Times in cooperation with Statista. We're proud to be recognized for our sustainability efforts and our commitment to reducing our emission intensity.

Christian is now going to take you through the detailed Q2 financials and our outlook for 2024. Christian?

Christian Harm

Thank you, Rob. So let's go to slide 6 for the key financials of the ITS segment.

Order intake of nearly 64,000 units was up both sequentially and compared to the prior-year level. In money terms, new orders declined slightly due to a higher share of APAC and class 3.1 warehouse equipment in the new business mix and despite a 3% growth in the service business.

Overall, the order book remained at a robust level and supports approximately 6 months of new business revenue. Margin resilience of the order book remains solid despite a mix skewed toward APAC and warehouse equipment in recent quarters.

Revenue at nearly €2.2 billion remained on high levels, driven by a 3% growth in services.

Adjusted EBIT remained at a healthy level of €231 million and continued to benefit from high production levels and the 2022 price increases. As expected, the adjusted EBIT margin at 10.7% remained in the double digits but declined slightly sequentially, reflecting a higher share of APAC and warehouse equipment compared to the first quarter.

I continue now on page 7, which summarizes the key financials of SCS. Overall, order intake continues to remain lumpy and is impacted by customers' hesitancy to sign new contracts due to macro uncertainty and postponed expectations on interest rate cuts.

Accordingly, Business Solutions orders were down 27% compared to the prior-year quarter. Service orders were down 16% due to the record level booked in the prior-year quarter.

You may recall that, in the first quarter, we talked about approximately €100 million of expected orders slipping into later quarters. About two-thirds of the spilled-over projects from the first quarter were signed in the second quarter.

This quarter, we once again saw good activity from the pure play e-commerce vertical with a share of 61%.

As mentioned in the last two Update Calls, the order book as of the 1st of January 2024 was adjusted due to a change in the presentation of the Customer Services business that we have aligned to the methodology applied in ITS. The slide which explains and quantifies this change is again included in the appendix of this presentation.

Overall, revenue remained close to prior-year and prior-quarter levels. The service business continued to grow at 11% year-over-year, while the project business declined by 3%, as expected, reflecting the lower order intake and the higher share of orders with longer lead times throughout last year.

We continued to make further progress in working through the legacy projects. The adjusted EBIT at €24 million and the adjusted EBIT margin at 3.2% reflects this and the higher share of service business in the revenue and is in line with our view of a better second half of the year.

Let's quickly run through the key financials for the group on page 8. Order intake reflects the seasonal recovery in ITS and the continued lumpiness in SCS. The order book includes the change in the presentation of the service business in SCS and continues to provide good workload for the next quarters.

Revenue benefited from the solid ITS new trucks business and the resilient service business in both segments, which more than compensated for the slightly softer SCS Business Solutions revenue.

KION Group improved the adjusted EBIT and the adjusted EBIT margin year-over-year, driven by both operating segments.

Page 9 now shows the reconciliation from the adjusted EBITDA to group net income. Depreciation and amortization followed the usual quarterly pattern.

Nonrecurring items of minus €14 million mainly include the conclusion of a multiyear legal dispute related to an acquisition

that Dematic undertook in 2015, which was before KION Group acquired Dematic. Nevertheless, our full-year expectation for NRI remains unchanged at minus €10 million to minus €20 million, as we had positive NRIs from the release of some provisions in the first quarter of this year.

PPA items in the quarter included a €22 million goodwill impairment for KION ITS Americas, which we had preannounced on July 10th. This was driven by the stronger-than-expected decline in the Americas market in the first quarter.

With the impairment, we have written off the entire goodwill related to KION ITS Americas, which stemmed from the foundation of KION Group back in 2006 or 2007, when the industrial truck business of Linde AG was sold to private equity.

The increase in the adjusted EBIT was more than offset by the two described effects in NRI and PPA, resulting in pretax earnings of €118 million in the quarter.

The tax rate in the quarter was negatively affected by the nontax-deductible goodwill impairment. Excluding this, the tax rate would have amounted to approximately 34%. We have therefore increased our full-year 2024 effective tax rate indication to 30% to 35% from previously 29% to 34%. As always, you'll find the slide on the housekeeping items in the appendix of this presentation.

Net income attributable to shareholders amounted to €68 million in the quarter, corresponding to earnings per share of €0.52.

Let's now continue with the free cash flow statement on page 10. Free cash flow in the quarter reached positive €137 million due to the strong improvement in adjusted EBIT and an almost unchanged net working capital.

The triple-digit free cash flow was achieved despite high tax payments of €120 million relating to the improved financial performance in the fiscal year 2023 and high tax prepayments for fiscal year 2024.

The positive free cash flow did not lead to a decrease in net debt, mainly due to the dividend payment of €92 million in June and the complete unwinding of on-balance-sheet factoring.

Page 11 shows the development of net financial debt and our leverage ratios. As mentioned on the previous slide, the positive free cash flow did not lead to a decrease in net debt, mainly due to the payment of the dividend and the completed unwinding of on-balance-sheet factoring. In fact, net debt at the end of June 2024 increased by €51 million compared to the end of March 2024.

Accordingly, the leverage ratio on industrial net operating debt increased slightly quarter-on-quarter by 0.1x to 1.5x despite a further improvement in the last-12-months EBITDA. Due to lower net pension liabilities, the leverage ratio on industrial net debt remained sequentially stable at 1.8x.

We remain committed to improving leverage metrics further to defend our two investment grade ratings, as we believe they are supportive to our business model.

Slide 13 lays out our updated 2024 view on our respective markets. For the industrial truck market, we now expect orders in units to remain on the prior-year level. While we continue to expect growth in the APAC region, the Americas region is showing a stronger decline than previously expected. EMEA is now expected to remain flat compared to our earlier view of slight growth.

In the Supply Chain Solutions market, we now expect revenues in 2024 to decline slightly due to ongoing macroeconomic uncertainties. We originally expected the market to grow slightly this year.

Slide 14 lays out our guidance. The good performance in the first half of 2024 and our updated view on our markets lead us to narrow our guidance ranges for the full year.

For ITS, we have taken down the upper end of the revenue guidance range by €300 million based on our updated view on the industrial truck market and the recent order intake development.

For adjusted EBIT, we have narrowed the guidance range by €20 million in each direction, taking into account both the solid performance of the first half 2024 as well as the reduced upper end of the revenue guidance.

You can see that we are guiding towards a lower second half of the year profitability in ITS, as already indicated in the quarter 1 Update Call.

Given our recent order intake pattern, it would not be advisable to extrapolate the first half of the year adjusted EBIT margin for the remainder of the year. In addition, certain cost increases, especially with regards to labor, will start being effective only in the course of the year. We expect to remain above the 10% adjusted EBIT margin mark across the second half of this year.

For SCS, we have increased the lower end of the revenue guidance range by €100 million due to the revenue development in the first half of this year. Our updated view on the Supply Chain Solutions market has not impacted our revenue expectations for this year.

Based on the achieved results of the first half, we have also increased the bottom end of the adjusted EBIT guidance range by €20 million euros.

For KION Group, this results in a narrowed guidance range for revenue between €11.3 billion and €11.7 billion and for adjusted EBIT between €830 million and €920 million. The corresponding narrowed ROCE guidance range is now between 7.7% and 8.7%. The guidance range for free cash flow remains unchanged.

Now I hand back to Rob for our key takeaways.

Rob Smith

Thank you, Christian. Let's turn to page 15 together for our key takeaways. KION delivered a solid second quarter 2024 with continued year-on-year improvements in adjusted EBIT and adjusted EBIT margins in both our operating segments.

As observed by many in our sector, the anticipated market recovery is taking longer than we originally expected. As a result,

we've updated you with our view on our respective markets today. We now expect the ITS market this year to remain on the prior-year level in unit terms. And our expectations for the SCS market, we expect it to decline slightly in revenue compared to last year.

We've confirmed our outlook today, and we narrowed the guidance ranges based on our solid performance in the first half and our updated market view.

This concludes the presentation. Let's move to the Q&A together. Francy, would you open the line, please?

Operator

Yes, of course. Thank you very much. Ladies and gentlemen, we will begin now with the question-and-answer session.

Akash Gupta

Yes, hi, good afternoon, everybody. Thanks for your time. I got two, and I go one at a time. The first one I have is on industrial trucks. So when I look at your first half run rate of order intake and also your market outlook for rest of the year, we get to around €8 billion-ish order intake for the year, while revenue guidance at the midpoint is going to be €8.6 billion.

And when I look at the IR presentation that was updated today, you expect 4% to 6% average growth rates in ITS new units beyond 2024.

The question I have is that -- I know you won't guide on 2025 today, but conceptually, looking at current order run rate and revenue guidance, is it fair to assume that revenues at some point in the next 12 months should see some decline before returning

back to growth, or is there a scenario where you can avoid year-on-year decline in revenues? So that's the first one.

Christian Harm

So, Akash, it's Christian. Thanks for your question. The point that you're looking at in terms of the market and the order intake, as you rightly point out, we don't guide for order intake right now, and we don't talk about 2025 in this particular call, in the Second Quarter Call of 2024.

I think in the equation that you're setting up or so, there's an element missing actually that I think is very important to look at as well because there's also a service segment which is in the order intake, which is in our revenue. So I would not necessarily come to the conclusion that you are lining out when you look at the overall picture.

Akash Gupta

Thank you. And my second question is on SCS business where, given the lack of new order recovery in H1 and your reduced market outlook for the full year, which may limit revenue growth next year in the segment, can you please talk about the levers you have to improve your profitability further in the segment versus 2024?

Rob Smith

Hi, Akash, good to hear from you, and appreciate your question. Look, as we pointed out earlier, we updated our SCS market outlook today, and it's the pushed-out expectations on interest rate cuts and the ongoing macro uncertainties that are the main drivers behind the ongoing hesitancy of customers to sign new orders.

Having said that, Akash, irrespective of the current market situation, our Supply Chain Solutions business has shown

sequential improvements in the adjusted EBIT over the past quarters and is set to continue to do so.

You see that in our narrowed guidance range. We lifted the lower end of the revenue, and we lifted the lower end of the adjusted EBIT. And what you're seeing is the effect of the implemented measures we've taken to improve our project management and our execution. And this enables Supply Chain Solutions to continue its margin improvement further, even with the volume growth being delayed.

Clearly, when the volume growth comes, that will have an additional uplift on the margins. But, Akash, our Dematic business, we've done our self-help homework, and it's making excellent progress fixing the machine. And the underlying trends that are underpinning the automation, global trend driving automation, are very strong and very much intact. And so the macro -- the market will be coming back macro wise. At one point in time, it will be coming back, and when it does, our Dematic business is ready, and we'll be running at stronger margins when the market's coming back.

So we're really pleased with the performance and the progression in that business, and probably the next year and a half of volumes, one way or another, we're able to deliver increasing profitability with that great improvement in the execution in the business.

Akash Gupta

Thank you.

Sven Weier

Yes, good afternoon. Thanks for taking my questions. The first one is regarding the market outlook you've given. And I

remember, previously, we were kind of thinking that the second half, especially on the warehouse automation side, should see bigger, stronger order pipeline conversion.

What you tell us today, does it mean that we should basically see a steady second half in both divisions, right, that there will be no uptick whatsoever when we think about it sequentially against the second quarter? How should we understand that? That's the first one.

Rob Smith

Yes, Sven, don't be drawing too many conclusions there, but the SCS order intake is, remains, and will go into the future as lumpy order intake.

The pipeline is good. The conversations with our customers about active projects that they're getting ready to start is well progressed with a lot of different projects. And they're pushing the starting button to start projects. There's some hesitancy still there. That's going to go away as the macro uncertainties clear over time, but they're still there. And so guiding on order intake we're not doing. I wouldn't take particularly the conclusions you've got because it's lumpy.

Sven Weier

The follow-up I have is just also coming back to the point about the truck business. And I guess another factor that we haven't discussed is the backlog in terms of your revenue generation in '25. Would you say that, by the end of the year, the lead times are kind of as low as they get, so you can't reduce the lead times any further as one potential to have a positive impact on revenues? Is that concluded by the end of the year, or do you think the lead times can go even lower?

And I was just also wondering. It's an industry phenomenon. It's not just you. What do you think about price discipline? Do you think, once we reach the point where backlog lead terms are back to normal, that we see more pricing aggression from your peers?

Rob Smith

Hi, Sven, good questions. Look, the backlog, as we've been talking about it over many quarters now, was quite high coming out of COVID. Kind of the long-term healthy backlog run rate or order coverage is probably 4 months plus or minus, and we're still probably over 6 months plus or minus, depending on which model line you're looking at and which machine.

But as we move back towards probably 4 months plus or minus, there's still some order backlog work to go prior to getting back to that 4 months plus or minus level.

Our observation's our pricing decisions are rational. Our observation's that the market is working with rational pricing decisions too. And we expect to remain rational, and that's our expectations in the market too.

Sven Weier

That's clear. Thank you, Rob.

Martin Wilkie

Thank you. Good afternoon. The first question I had was on the North America business in ITS. Obviously, you've lowered the market expectation there, but also, the goodwill impairment you've done, that, as you mentioned in the opening remarks, was goodwill from a long time ago, potentially 15 years ago, and also, that cycle's been through lots of ups and downs over that period.

So what drove the goodwill write-down now as opposed to during other cyclical weakness? Has anything in particular happened to the business this quarter that we should know about? Thank you.

Christian Harm

Yes, so, Martin, I take the question on the goodwill impairment on the ITS Americas business here. As you said, we went into this year with actually an expectation that the North American market -- in particular out of the Americas region, the North American market on the ITS side will actually face a reduction, a volume reduction, into the year.

You know that we get the market information and market statistics with a 3-month delay. We got the market information then for the first quarter, and actually, the reduction was way more significant than our initial planning was with that.

So we had to, and as a consequence of that, we were updating our own plannings going forward, and we had to say that the recovery out of the trough that we were seeing from the market will eventually take longer than the reduction that we have seen at the beginning of the year.

So as a consequence of this and as a matter of principle, the goodwill impairment test that was triggered, right, came to the result that we would actually have to write it off as we go. It stems from way back. You're right. It's from the original carve-out of the KION Group there, but a reflection of the view in terms of how long it will actually take for our ITS business to actually recover out of the very significant reduction that we have seen at the beginning of this year.

Martin Wilkie

Okay. Thank you. And if I could just have a second question, obviously, as we go into the second half of the year, there's lots of focus on elections and the potential for tariffs. And I know that, next time around, tariffs may not be quite the same as they were in 2018, but when you think about your SCS business, which is obviously very overweight in the US, is your footprint very different than it was back then, how you think about tariff risks in terms of the components that you may still buy in from China? Thank you.

Rob Smith

Martin, thank you for that. Look, I don't foresee for our SCS business -- your question is a North America question is my understanding. I don't see a substantial impact in our SCS business coming from potential tariff changes in North America.

A good deal of our technology in North America is coming from North America, and it's part of our overall strategy to be able to engineer and source and manufacture in region, for region, and to source between regions as appropriate as well.

We've got a good supply chain in the Americas, and our expectation is, as geographic or geopolitical changes may come, we're well positioned to serve each of those different scenarios in a fashion that is a sustainable fashion. So I would not have the concern that you were just describing and for those reasons.

Martin Wilkie

Great. That's very encouraging. Thank you.

Gael de-Bray

Thank you very much. Good afternoon, everybody. I have two questions, please. The first one is about the French market. France is a big market for you, obviously. So have you started to see any early signs that the political issues there have started to

impact the business locally? So that's question number one, and I'll get back later for question number two.

Christian Harm

So then just to answer the first question, Gael, no, we have not seen sort of any ramifications on our business coming from the circumstances you're describing.

Gael de-Bray

Okay. Cool. And then so the second question is about SCS. With the prospect recovery being pushed to the right, let's assume the business doesn't grow next year. So theoretically, what could be the margin profile of SCS if we only take into account the full ramp down of the legacy backlog and the benefits from your recent cost cutting actions? Will the margin be trending around 5%-ish or possibly already higher?

Rob Smith

Gael, as Christian pointed out, you're at the second quarter results call in 2024 talking about 2025 already. I don't jump in your boat saying let's assume it's going to be flat next year. We're not talking about next year until we get a bit closer.

But what I said before, let me just underscore. SCS has put some very significant self-help improvements in place, improving our project management processes and improving the project execution. We've been working through the legacy projects and closing those off one at a time and have made very good progress on that.

So the SCS business has demonstrated successive improvements in profitability over the last several quarters and will continue to do so.

And as much as the market comes back, that will bring more volume. And for probably the next 6 quarters, the profitability improvements in SCS is not market recovery dependent. The profitability improvements are our self-help measures coming from improving the project management, and I expect you'll continue to see profitability increases in the quarters to come.

Gael de-Bray

Okay. Maybe can I try in a different way? With the aftermarket business, with the service business within SCS growing pretty strongly at the moment -- I think 10%, 11%-ish -- so the margin should be quite good, right, for the service part within SCS? Is it still around 10% or above, just on service?

Rob Smith

Gael, we don't comment on explicit service margins, but your general understanding that service business is often at indeed good margins is clearly an appropriate understanding, and you're understanding that that's a growing part of our business. That's true in SCS. That's true in ITS. That's true in KION. Service is a growing and important good profitability part of our business, and it's in many cases recurring and sustainable revenues because it's over longer-term contracts.

Gael de-Bray

Okay. Thank you very much.

Sebastian Growe

Hi, good afternoon. Thanks for taking my questions. The first one would be on IT&S, and it's to further discuss the self-help levers you might have if and when orders would remain at the €2 billion run rate per quarter.

So more specifically, I would be interested in the discussion around potential tailwinds from the sale of entry-level trucks. So I think you stated in the past that these are around €150 million,

€200 million close to at least in '23. You were striving for €400 million over time. So could you just confirm that this is still alive and kicking?

And the second question around this one is how we should think around the outlook for services because you alluded to this as a growth engine in an earlier answer to Akash's question. I would especially be interested in your commentary around aftersales.

And the third element that would be worth, I think, discussing is around the potential expansion of existing leasing contracts, as new trucks are obviously relatively pricey compared to the past. So it would suggest that there is a good sort of interest from clients to renew those contracts.

And then I would have another three bridge questions around SCS, but if we could start there.

Christian Harm

Maybe I'll start in reverse side from your questions. So indeed, on the ITS business, offering our trucks in the connection with the leasing contract is an integral part of our business model. And the share of trucks that we are offering with leasing contracts is actually increasing, and we continue to do so, and that gives us the ability to our business model, as you rightly assume, as it brings also trucks back.

So that's part of the whole notion of a growing service business, is continuing the further increase of the penetration of the new business attached with leasing contracts on that side. So that already partially answers the outlook for the services because that is an essential part of the services.

Now leasing is also a driver for actually driving the services next to the pure fact that the installed base is growing. And the increased shipments that we had been bringing to the market after we last year then finally overcame the supply issues, and now the continuing to prolong the production volumes actually into shipments, that drives the installed base, and the installed base actually comes with aftersales. In addition to that, leasing is driving the contracted services and gives an additional stability to the business model.

The first point, frankly, I did not really get. So if you don't mind we could actually handle that through IR offline. I would appreciate that very much.

Sebastian Growe

No problem. Then on SCS, I think, also there, the framework, would be interested, when we talk about the price quality on new orders, so apparently, you had the broad range in terms of the gross profit margin ranging from between mid-teens levels to up to 24% at the peak of the cycle. Would you be comfortable with a 20% plus gross profit margin at this point, and especially when considering the right sizing that you have been undertaking, i.e., cutting the workforce?

The second thing that comes to my mind is the legacy contracts, if you could update us on that, how far you have been through with the legacy contracts.

And then the third point, solutions obviously have come down quite dramatically from €3 billion-ish in terms of revenues to now below €2 billion. So when will this kind of fire back in the sense that the service growth should slow meaningfully? So yes, if you could comment on those aspects, please.

Rob Smith

Yes, let's start with the pricing, Sebastian. By the way, it's good to hear from you. And the question on pricing, look, the pricing that we're taking new contracts at in our Supply Chain Solutions business, as you know, those projects can go over 3, 4, 5 years. And I confirm that the projects that we're taking into our order books now are coming in at margins that are supportive of returning our Supply Chain Solutions business consistently growing the profitability in it and taking it past 10% profitability in 2027. So the margin, the as-sold pricing is good pricing and supportive of that projection and that progression.

In terms of business solutions and the size of the business solutions business, it's a function of the order intake. We've been talking about lumpiness. We've been talking about people hesitating to take on new projects. At one point, that's going to turn around, though, and the macros are going to turn around.

The underpinning trends in that market are very, very strong. And as I was describing before, when they do, our team is ready because they've done the self-help homework, and the machine is ready to be executing projects with good margins as the volumes are coming back.

I think the element to the service business is one for both our segments I and appreciate the question on it. The service business is very good business and also in both our segments and as it brings good profitability in it and very good customer attention because customers in both segments are focused very much on total cost of ownership and very much on uptime and availability of their facilities.

And as we're driving more and more of our service offering to include telemetry capabilities and benefiting from the digital twin of our individual machines as well as the emulation, simulation, digital twins of our warehouse automation installations, you can do a whole lot of that offsite. And it improves first-time fixed rates. It makes the service technicians more productive and more efficient in their handling the service calls. And it's good for those customers.

So it's quite good business and quite sticky business. And that's the nice thing about having both in the portfolio. The services are growing well, and the market will be coming back on the business solutions businesses. Less uncertainty prevails in the market.

Sebastian Growe

And would you mind commenting on the legacy contracts and how much is left here?

Rob Smith

Sure. Thank you, Sebastian. Didn't mean to skip it but was working on the other questions for you. Look, we're making very good progress, continuing to work off the legacy contracts and projects. We expect that most of those are completed by the back end of this year.

There will be a handful that go into next year and one big one that goes even into the year after that, but the amount of those as a proportion of our business has consistently been decreasing and will have less and less influence going forward, which is quite a bit an important part of the margin recovery in addition to the execution capabilities and consistency in the business.

Sebastian Growe

Okay. Thank you very much.

Lucas Ferhani

Hello, thanks for taking my questions. I'll have two as well. We can do them one at a time. For the first time, just on the free cash flow guidance unchanged, you had a decent start to the year. I'm wondering whether you're expecting any headwinds into H2 on free cash flow.

If you take a similar performance to what you delivered in H2 last year, that should drive you towards the upper end or even above the guidance range. So are there any specific things we should watch out on the free cash flow into kind of H2 and also on working capital, especially the inventory? You said there was more to go in terms of reducing that. Is that still something that's going to happen?

Christian Harm

Yes, Lucas, thanks for asking the question on the cash flow. There's no particular headwinds that you are alluding to that we would consider in the second half of the year.

It continues to be our priority to actually work on the cash -- sorry, not on the -- well, of course, also on the cash flow, but on the working capital in particular, as a constituent of the cash flow for an improvement in the second half of the year.

But that sort of is reflected in our guidance that we maintained for the free cash flow for the year. But there's no particular event, no particular headwind that we would look at for the second half of this year.

Lucas Ferhani

Perfect. Thank you. And the second one is just on the margin in ITS. So there's an impact from mix. You talk about more kind of higher share of APAC. I'm just wondering. Is that a short-term phenomenon because you have lower growth in kind of EMEA

and North America, and so kind of APAC is trending, or is there a strategy to kind of really increase your share and grow more in that region?

And my point is, are you able to deliver kind of similar margin in APAC kind of longer term? Obviously, it's a different market. It's generally more competitive, a bit more kind of price focused, and there's local players, and I'm talking here specifically about China.

And just on the guidance for H2, I think you highlighted obviously previously that you'll be kind of below H1 and still above 10%. You've delivered many years of kind of 11% EBIT margin in ITS historically. Is that still something that you can get to, like you can deliver consistently, or you're happy with kind of 10% plus margin near term and even medium term? Thank you.

Christian Harm

Yes, thanks for asking the question. So yes, I can confirm that we over the last 4 quarters have now consistently achieved more than 10% in the ITS segment, and will remain committed for this one as well. And also, for the second half of the year, we're looking at that, and that remains our strategic aspiration for the segment.

Like it is for the other segment, just the difference is, with ITS, I think we have already shown that over the last 4 quarters and we continue to look at that. That already includes, obviously, the relative weight of the different regions.

We do not comment on margins in the different regions. But the weight, the mix of the regional mix or so is well reflected in the

actuals but is also well reflected in the way how we're looking forward in terms of the updated guidance.

Lucas Ferhani

Perfect. Thank you.

Alexander Hauenstein

Yes. Hi, Alex Hauenstein. Thanks for taking my questions. Looking to ITS, you said that you're targeting for the second half of the year more than 10% margin. Any comment from your side how this could look like in the development path from Q3 to Q4?

Are we seeing the trough probably in Q4, I guess, or is there, due to the matter of components including in this somewhat slightly going-down trend in margins, i.e., for example, the personnel cost side, do you expect this potentially to slipping also into Q1, maybe Q2, so that the trough in ITS margin, as far as you can see, might not be in Q4? That would be the first question.

Christian Harm

So as I said, we are looking at the double-digit margin in the ITS segment in the second half of the year, and there's factors that will come into play in each of the quarters. So I would not necessarily look at the trough in the fourth quarter in that context.

Alexander Hauenstein

Okay. So that means or kind of a follow-up, it might also be a very high single-digit margin number in Q4 actually but still be within your guidance of more than 10%? So that is not excluded, right?

Christian Harm

Yes, so again, we're guiding for a double-digit margin in the ITS segment in the second half of the year. And I think we are confident that we will see that. And I think that's how you should look at that.

Alexander Hauenstein

Okay. Okay. Thanks. Yes, and coming back to SCS, I know it's a bit tricky to look into the next year, but what I see from what you say and when I look into consensus and roughly seeing a consensus for SCS on the revenue side for next year, implying a 10% growth, I'm wondering whether this is something that is providing you some headache. At least for me, it does provide some headache.

And I'm wondering whether the Supply Chain Solutions earning side will kind of double. At least this is what consensus is believing for next year. So apart from everything what you have said so far, can you distract these headaches that I have here in the one or the other way on top of that?

Rob Smith

I suggest you go get some aspirin for the headache. Look, we're describing an SCS business that's done a real good job doing its homework, is doing a good job delivering improving margins. They are improving consecutively. I expect and the SCS business expects to continue on that good glide path.

In terms of revenue next year, too early to call. In terms of order intake, we don't guide, but we did talk about the market, and basically, it's just taking longer for the recovery than I think anybody anticipated. But it's going to come, and when that recovery comes, it's going to bring volume with it.

The self-help measures are driving margin increase on muted revenues. And the self-help measures get that engine real -- that machine real nice and healthy. So as then market-driven volumes are coming back with the macro recovery, the business is very well positioned to be executing those that continue to be increasing margins.

Alexander Hauenstein Yes, absolutely understood, but I think, as you said rightly, that we all are looking for the macro kind, let's say, interest rate-induced kickstart and to get this running again in terms of order intake.

And I'm wondering whether this will most likely be a gradual movement starting coming in quarter-by-quarter or whether you see from what you hear from your customers that, as soon as we have, let's say, a material and feelable step down in the interest rate, that a lot of the projects would come at one point of time, or would it be a gradual improvement very slowly?

Any idea about the way of or the number of projects that are potentially lining up in the back end? We don't see them yet, but you are currently potentially in the discussion at least on an operational side of that, not maybe financially but operational wise.

Rob Smith Sure, I appreciate that thinking. And I think a good way to maybe capture the message there, Alexander, is there is a good solid pipeline of active project discussions and solutioning going on with our Supply Chain Solutions team and their customers as we're speaking.

It's the starting point of -- when the customers kick off the new project, that's when the pipeline starts to turn into order entry. And it remains lumpy, and we will see how it develops. Making too detailed projections and predictions isn't an appropriate thing to do when the underlying trend is a bit lumpy as they come in.

I think the underlying trend, though, it shall get better over a period of time. And we've all heard the messages, and we're all anticipating that it's going to. It's just taking longer to get there than we expected earlier this year.

Alexander Hauenstein All right. Good. So looking forward to see this. And yes, I wish you all the best for your internal measures for the legacy projects. But I think and I understand that you're making good progress there. So at least this is the basis for this.

Rob Smith Thanks very much.

Tore Fangmann Yes, hello, good afternoon. Thank you for taking my question. I got two as well. The first one is a clarification on the first question from Akash today. So I have to go a few minutes back. Sorry for this.

I got a bit confused here. It sounded to me like there was like a mix up in that a few of the services are not included in the orders, but they're then included in the revenues. And this is why it's not fair to look at orders to forecast revenues, but could you just please clarify what your answer was to the question? I didn't quite get it. Thank you.

Christian Harm No, so not sure I get your question now but I give it a try. There's a difference in order intake in units. And then the reference was made to order intake in money terms. The order intake in money terms also includes the service business. So actually, that's a broader measure as a KPI, is a broader measure than the order intake in units. I hope that clarifies the question.

Tore Fangmann

Yes, thank you. That clarifies it better. And my second question would be just, in general, if we currently look at the pricing and cost environment, do you receive any major pushback from clients against your price increases from earlier this year? And then in addition to this, how are currently your raw material, energy, personnel cost, like your overall imposed costs developing? Thank you.

Christian Harm

So on the price increase that we have done at the beginning of the year, that was implemented as planned. The personnel costs, right, obviously, there is still a follow-up in terms of increases from personnel costs out of the inflationary periods that we have seen over the last periods of time.

Material costs actually are flattish, some of the commodities going down, some of the commodities actually risen. They have gone up again. Overall, I would see a flattish development. And the energy prices are actually at this point in time not a particular concern for us.

Tore Fangmann

Okay. Perfect. Thank you.

Christoph Dolleschal

Yes, hi, good afternoon, everyone. Also, two questions from my side, on A&D and ITS. So the first one is that, if we look at ITS mix, the IC and E trucks actually look quite good in the second quarter. And also, here, it was flat in terms of volumes, and still, you talk about negative mix effects. So did the APAC effect overcompensate both Europe, IC and E, or am I getting something wrong there?

Christian Harm

Yes, there is another element that probably is missing in the equation here, which is actually that the warehouse equipment

was up. So it's not just the question of regional mix that we are alluding to. It's the regional mix piece and that there is also mix between the product groups, warehouse and then the E and the IC or counterbalance. So it's the combination of those two mix effects.

Christoph Dolleschal

Okay. Then the next one is on the volumes in EMEA in ITS in the first half. You were at about 79,000 units in total, and now you expect a flat market in EMEA. So does that imply also, for your own -- so not for the overall market, but your expectations would then also point to a similar magnitude of volumes in the second half with the same seasonality that we've seen in the past. Is that your hypothesis for now?

Christian Harm

So again, I just have to repeat myself, I really don't guide on order intake or so, but I'm sure you are aware of the usual order intake pattern that is applicable here or that we have seen. You know historical as well on the ITS side, which particularly alludes to a strong fourth quarter when it comes to order intake. So I think that's the reference point that you probably want to take into consideration.

Christoph Dolleschal

Yes, that is what I meant. And also, obviously, if you think the whole market is flat, then I would just assume that then you have a similar assumption for your own units. So I take that as a mild yes for now.

Then on SCS, I think what I'm a bit puzzled with is, let's say, that the baseline order intake that is coming in, I think, so far, at least myself and probably a few others were thinking about like, say, a baseline order intake number in the region of €700 million, €750

million. But now if we look at, say, the second quarter, this rather points towards €600 million.

So I was just wondering what a baseline number is. Should we be thinking at a baseline? If the market does not recover -- let's put it that way -- should we be looking at a baseline of rather €3 billion or rather €2.5 billion if we don't see any market recovery?

Christian Harm

I think you are trying to do the same thing on SCS like just on the ITS side. I think, again, the one thing is that sort of order intake in the particular quarter and then from quarter to quarter, that will remain lumpy.

You have seen the pattern last year, right, where we had very strong quarters comparably, but there was also a weak quarter in the beginning and then in between. And that's the nature of the whole business, right, in the whole segment. And that will continue to be so, right? I think this notion of the baseline order intake in that context of a lumpy order intake actually is not necessarily the right way to look at it.

Christoph Dolleschal

Okay. Thanks.

Philippe Lorain

Yes, good afternoon, everybody. I've got like one question with regard to generally the SCS market maybe more than the ITS, but like everything, like if you kind of want to comment on that. So since the recovery seems to take longer than expected, but the pipeline looks healthy, how do you think about maybe seeing more growth coming when the recovery starts because of pent-up effects and therefore, again, more volatility in order intake for both segments over the coming 2 to 3 years?

Maybe a correlated question as well is, when you comment on the pipeline being healthy, is it relatively unchanged versus what you've seen in previous quarters, or is it trending slightly up or slightly down? Thank you.

Rob Smith

Hello, Philippe. So actually, the pipeline has been growing over time. The order intake happens when the customers start the orders. And so you could even perceive there is a bit of a backlog building in terms of customers getting closer to needing to start an order, but they haven't done it yet. And it does remain lumpy, like Christian said.

I think, though, that at any given one point snapshot in time, trying to call the trend, and is there a catch up effect, etc., etc., the better way to look at it, I think, is our expectations and our demonstrations in our IR pack that we expect the SCS market to be growing at 9% or better on a CAGR basis over our strategic planning period.

And I think that helps take into any year 1 year or 1 quarter being up or -- and over time, that's the kind of a growth that we expect and you should expect.

Philippe Lorain

Okay. Perfect. And if you don't mind like asking really a quick one, you made a comment as well on its on SCS previously with regard to potential impacts from tariff increases in the North American region. Would you mind commenting as well quickly on what you would expect there for ITS?

Christian Harm

I think the same applies there. The former Trump administration has put tariffs in place. The Biden administration actually continued those tariffs and kept them in place. At this point in

time, we would not look at however the election turns out to have a particular effect on this situation.

Rob Smith

In addition, we put a very good investment into North America a couple of years back, and that factory is ready to roll too. And the North American market will chew through the stock that's in the network over a period of time. And as that market's coming back, we're very well positioned for it.

Francy might not give you another question next time, though, Philippe. Let's see if she does or not. And I see that Timothy's still got one. We'll give him that one too, Francy.

Philippe Lorain

Thank you very much.

Rob Smith

Go ahead, Timothy.

Timothy Lee

Hi, great. Sorry about that. So really quick question on SCS. So I think some of the industry players were actually commenting about like the sequential developments of the order development or pipeline development is getting a little bit better in the second quarter, like rising business appetite for the second quarter. I'm not sure whether you are seeing similar pattern or as long as you're pushing back a little bit of the expectation of recovery in the markets, but how about the sequential development you're observing for the market for the second quarter? That would be helpful. Thank you.

Christian Harm

So maybe, Timothy, I take the question that comes back to sort of also what Rob was alluding before. I think what we are seeing -- and probably that goes along the lines that you're referring to -- we see a pipeline that actually has become better over the

recent time. And so the point is just that pipeline actually turns into the order with the signature of the customer. But the pipeline actually has grown. So I think that goes along the lines of what you were referring to.

Timothy Lee

All right. That's helpful. Thank you.

Operator

And that was our last question for the day, and I will hand back to Rob for any closing comments.

Rob Smith

Thank you very much, Francy, and thanks for all of you joining our call today and your very good questions. We wish you a real good summer break. We'll be at the different conferences in September. We look forward to having those discussions over the coming months, and we expect to see you on our call at the end of the third quarter. Have a good summer, and thanks for your time today.