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Kone Oyj (KNEBV.FI)

Q4 2024 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Natalia Valtasaari

Vice President-Investor Relations, Kone Oyj

Good morning, everybody, and welcome to KONE's Fourth Quarter Earnings Call. My name is Natalia Valtasaari. I'm Head of Investor Relations here at KONE. And I'm very pleased to be joined by our CEO, Philippe Delorme; and our CFO, Ilkka Hara.

So, as usual, Philippe will start by talking through the highlights of the year and about our strategic developments. And then, Ilkka will continue going through the markets and the financials.

With that, Philippe, please.

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

Thank you, Natalia, and welcome back on board the IR team. So, let me start, we have a technical glitch to start with, which will be solved in a moment. Thank you. Very good. I couldn't see the slides anymore. That was slightly complicated to talk to you about our story, though we knew it very well.

So, a very good morning, everyone. I'm very pleased to be here today presenting our results for 2024. So, let me start again, as usual, by summarizing the highlights, this time focusing on the full year 2024. It goes without saying that, one of our most important achievements last year was the launch of our new strategy, Rise. And I'm really pleased that we've gotten off to such a fantastic start in terms of strategy execution.

Another key highlight was the excellent momentum that we had in Service and Modernization throughout 2024. Together, these two businesses account for 90% of our profit. So the strong sales growth we've seen makes KONE a more resilient company than ever. From a strategic – from a geographical perspective, we saw good order growth in Americas, Europe, Asia-Pacific, Middle East and Africa. In China, as mentioned before, the construction markets have been under significant pressure and this has impacted our New Building Solutions business, while the Service and Modernization continued to make good progress there.

As you know, profitable growth is very high on our agenda. So it has been very good to see that our disciplined approach to driving financial performance has resulted in the eight consecutive quarters of profitability improvement. So, based on KONE's performance, the board is proposing to the annual general meeting a dividend of €1.8 per B class shares, which represent a dividend yield of 3.8%.

Now, let's have a look at all of this in more detail in the context of Q4. So, in terms of orders received, we had a solid quarter. Outside China, order growth was over 10%, and it was especially good to see modernization order growing nicely in all areas. The headwinds in China continued, which was visible in both orders and sales. Orders received declined by over 20% in China and sales by nearly 15%. Despite this, our overall sales increased by 5.1% at comparable currencies. Here, of course, the highlight was, again, our double-digit growth in both Service and Modernization. This gave us a more favorable business mix, which was a key driver of the 20-basis-point improvement of our adjusted EBIT margin.

And finally, as usual, cash generation in the fourth quarter was very strong. As we discussed in previous quarters, cash flow has been an area of particular focus this year and it was very good to see this paying off very well. So, all in all, I would say that we had a great finish of the year.

Now, probably my favorite page which is customer exciting reference with you. So, starting with services this time, where we recently won a contract to maintain the elevators at the InterContinental Hotel in Madrid. I actually had the opportunity to sit down with the hotel manager last week and it was great to hear that he highlighted our reputation and our digital offering as the key reason they opted to partner with us.

Second reference is the Henry B. González Convention Center modernization in San Antonio, Texas. We've been maintaining the elevators and the escalators at this site since 2012 and have completed another modernization project for the same customer a few years back. So this is a great example of how important longstanding customer relationships are for winning in modernization.

And finally, and I find this one really exciting, New Building Solutions will be supplying our next generation high-rise technology to the world's tallest residential-only building in Dubai. Actually, if we look at the top 10 tallest buildings currently under construction, 5 out of 10, I repeat, 5 out of 10 are going to feature KONE's equipment. And I think it's something we can be very proud about in terms of our leadership in the most demanding application.

Hopefully, this slide should look quite familiar to you by now. But let me just take a short moment to remind you about our ambition, which is very simply to lead the industry by being the number one choice for our employees

and our customers, by leading in innovation, leading in innovation and sustainability, and by leading in growth and profitability.

Since its launch, I visited many KONE locations all over the world, and it has been really great to see how well this ambition resonates with our employees and also with our customers and other external stakeholders. There is a lot of excitement in the year. Despite being early days, we have excellent progress to report in each of our four strategic shifts.

In digital, approximately 35% of our service base is now connected, and we've done really well in rolling out solutions for smarter service operation to new countries. In modernization, we are focused on enhancing our offering, particularly within partial modernization and continue to work on industrializing our value proposition. We have also successfully accelerated the sales of our regenerative drive, which help customer to cut carbon by reusing the energy generated when the elevator breaks.

We haven't talked so much about win residential before, so let me share an example with you which I really find exciting. We've recently launched the renewed MonoSpace 100 DX in Europe to improve our positioning in the low-rise residential market, which is very important segment. It leverages our global supply chain operations to improve cost competitiveness without compromising, of course, on quality and reliability. And I'm especially proud of the speed with which we were able to bring this solution to the market with only six months from initial decision to deployment, and I'm glad that we really see a good commercial traction here.

Now, moving on to my last slide, sustainability. We made great progress toward our sustainability target in most areas last year. I would like to especially highlight the reduction in Scope 3 emissions, which accelerated visibly last year. A big driver of this improvement was the increased share of regenerative drive sales, which I mentioned actually in the previous slides. I was also happy to see over 2 percentage point improvement in the share of woman at director level, our key diversity metric. Unfortunately, we didn't make progress towards our safety target and this is something we'll be paying special attention to in 2025.

Then, a new development to share with you: as of this year, we start to measure our performance with the KONE Sustainability index. It builds on many familiar elements with the addition of cybersecurity which is very important. This is really about simplifying how we track and report performance to create better clarity on how we are progressing vis-à-vis our ambitions.

I'm glad now to hand over to Ilkka, who will go through the market development and financial. Ilkka, the floor is yours.

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

Thanks. Thank you, Philippe. And warm welcome on my behalf to this fourth quarter result webcast. Let's start by taking a look at how our markets have developed during the past few months. Market trends in the fourth quarter were quite similar to what we've seen previously in the year. In the New Building Solutions, as already mentioned by Philippe, the construction market in China continued to be very difficult, declining again significantly in the fourth quarter. In the other regions, activity was more stable or growing.

In Services and Modernization, the market environment was very positive and we saw growth in all areas. From a geographical perspective, Asia-Pacific, Middle East and Africa continues to stand out with a strong demand in all businesses.

Let me next go through our financials in a bit more detail, and I have some good news to be shared. Starting with our orders received, we were very pleased to see, again, orders growing three of our four areas. Overall, our orders received grew by 2.6% at the comparable currencies in the fourth quarter. Modernization grew at a healthy pace, while New Building Solutions came down slightly due to the significant decline in market in China. Our margin of orders received was slightly down year-on-year, with a decline in China and a more stable development in the rest of the world.

Then to sales, we had a very good end to the year. Our sales grew overall by 5.1% at the comparable currencies in the quarter. From business perspective, New Building Solutions declined by 2.9%. This was very much driven by China, where delivery volumes continued to be low. On the positive side, services sales grew by staggering 10.5%. A key driver was the growth of our service base, which now stands at well over 1.7 million units. Pricing and value-added services also contributed to the sales growth.

In modernization, sales started to reflect the strong orders received in previous quarters and grew at a very good rate of 12.8%. Geographically, our sales in Greater China decreased by 14.8%. The order book rotation continues to be slow, which of course relates to challenging market conditions, but we also continued to manage delivery historically to secure cash flow. Outside of China, we grew our sales by over 10% at the comparable currencies. This is a very good outcome in the quarter.

Then moving to adjusted EBIT and profitability. Our adjusted EBIT margins continued to develop positively. And in this quarter, we improved 20 basis points year-on-year. This took our adjusted EBIT to €387 million. Our operating income was €333 million in the quarter. The difference here mainly relates to restructuring costs booked in China, where we have taken more meaningful actions to adjust to the weak market conditions.

Looking at the profitability improvement more closely, the main driver continues to be favorable business mix. We also did see contribution from improved margins in the modernization business. On the negative side, the inflation was a challenge. But, as in previous quarters, the biggest headwind for us was the margin decline in China. So, overall, as highlighted by Philippe, it is really good to see the consistent profitability improvement. And we have actions in place to secure continued progress going forward towards our mid-term targets.

Finally, to our cash flow. So let me start by saying that while one quarter is a short time to measure cash flow, our cash generation in the fourth quarter was particular highlight for me. Cash flow increased to €534 million in the quarter, mainly driven by working capital and also the profit improvement. We actually saw quite a broad-based improvement in various working capital items, but I was especially pleased to see collections contributing positively as this has been a particular focus area for us. The strong end to the year brought the full year cash flow to a healthy level of €1.589 billion.

Let's then look at how we're thinking about year 2025, starting with market prospect. Demand trends are overall very much in line what we saw in the fourth quarter. We continue to see interesting opportunities in all parts of the world with stable or positive outlook in 11 of our 12 end markets. Modernization markets are expected to remain very active and we expect services markets to continue to grow in all regions.

In the New Building Solutions markets, we expect conditions in China to remain difficult. Elsewhere, we expect stable development in Europe and a slight growth in North America. And in Asia-Pacific, Middle East and Africa, we continue to see very good opportunities also in 2025.

Then to our business outlook. We enter to the year with a healthy order book and we expect strong growth to continue in both services and in modernization. Also, the ramp-up of our performance initiatives will also start to

contribute to our performance. China continues to be the main headwind. Here, as said, markets remain under pressure, and we will be delivering orders which were booked at the lower margins. So, with this in mind, our guidance for the 2025 is for sales to grow slightly at the comparable currencies and we expect profitability improvement to continue. This puts us on track to meeting our mid-term financial targets.

Let me now hand back over to Philippe to close the presentation before going into Q&A.

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

Thank you, Ilkka. So, before summarizing, let me take a moment to talk about what we are prioritizing this year, so that we can deliver on our strategic ambitions. First of all, I firmly believe and I think I've said it many times that innovations have a very important role to play in how we succeed with our strategy. We want to be quick in bringing new solutions to the market, and we need to ensure that we focus and align our resources and effort on our new strategy and, I guess, our priorities are very clear.

In service, we will push for higher connectivity and a more rapid rollout of digital services solution to drive customer value and productivity. And in modernization, we'll continue industrializing our offering and developing our sales approach. Bearing in mind the market conditions in China, cash flow is our number one priority, and we also continue to pursue growth opportunities in Service and Modernization to drive a more balanced business mix in that part of the world.

And finally, we'll be more focused than ever on what we can do to secure continuous profitability improvement. Here our initiatives to drive sales and operational excellence and improve procurement efficiency are very key. So, to wrap it up, we have again demonstrated our business resilience in 2024 with great progress on many fronts. We've gotten off to a great start in executing our new strategy, Rise, and maintaining momentum here is key. We see very exciting opportunities in Service and Modernization. These are our main profit pools and we are fully focused on securing growth in these businesses.

And finally, we have clear priorities heading into 2025, and our guidance show that we are on track to delivering on our mid-term targets. I would like to thank again all the teams at KONE, who showed again an outstanding commitment.

And I would like to thank you, all, for your attention. And propose that we now move to your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] We will now take our first question from Daniela Costa of Goldman Sachs. Your line is open. Please go ahead.

Daniela Costa

Analyst, Goldman Sachs International

Q

Hi. Good morning, everyone. Thank you so much for taking my question. I have one question and then sort of just a follow-up on the clarification on the accounting. But my question relates to the margin guidance [ph] for it to be up (00:18:40). And can you help us understand the various moving parts in terms of how do you still model in that China OE positive next year? How much of the improvement is a mechanical mix impact versus tailwind from the actions that you're implementing and which ones are the critical ones?

And then just on the R&D write-off that you did, what have you discontinued? Sort of can you elaborate basically exactly what that was and how we should think about, maybe as you restructure the business further actions like that?

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

Yeah. Maybe on the China part, and Philippe, you can also talk about it, what we're aiming to do there. So, in the fourth quarter, in China, focused our business in line with the market and the new strategy moving to Service and Modernization-focused business. And as a result, where we saw the restructuring costs hitting our fourth quarter as the measures were being taken then. And we do expect those to contribute positively. But, as already said, so we also do see the NBS business continuing to decline in the fourth quarter. So, it's more towards aligning our business to the market reality we see as a result. I'll come back to second question if you want to comment on China.

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

A

No, I think, China priority is very clear, cash first. Cash first. And we believe, actually, we have made further progress in Q4 to be even more disciplined in cash. And in the end, really pick the customers that we believe are going to pay us going forward, because there was cash tension, especially in Q3 in the market, margin, and we are very intentional to – in new construction, picking the customers where we think we have the best margin upside or margin capabilities in the full life cycle and pivoting our business to as much as we can a bigger share of modernization and service. And that leads to adapting our forces because it's a significant change in the way we are dealing with our business in China.

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

Then on your second part of the question, Daniela, on – so the restructuring part of it, the majority was related to China, but also the global teams were impacted as well. And there, we were looking to align our global teams towards the new strategy we laid out in our Capital Markets Day. And as a result of that, in the fourth quarter, we had restructuring done and restructuring costs, including the development teams. So it's all restructuring cost, but it's two different parts of the organization that were impacted. And as a result then, we had the €54 million of restructuring charges for the fourth quarter.

Daniela Costa

Analyst, Goldman Sachs International

Q

Just on the first question, on the answer, just make sure I understood, you're saying that China OE is still profitable or just at a cash level?

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

No. It is profitable both in P&L as well as – actually, as you saw in the cash flow, also China contributed positive. A very good development in the fourth quarter.

Daniela Costa

Analyst, Goldman Sachs International

Q

Got it. Thank you very much.

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

Thank you.

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

A

Thank you.

Operator: And we will now take our next question from Andre Kukhnin of UBS. Your line is open. Please go ahead.

Andre Kukhnin

Analyst, UBS AG (London Branch)

Q

Good morning. Thank you very much for taking my questions. I'll just go one at a time and maybe follow-up on the margin drivers for 2025. Firstly, on restructuring, could you give us an idea of what amount of savings can we expect from that €50 million of restructuring? Is it kind of more of a traditional 1:1? And related to that, are there any other measures to kind of trying to bucket this in terms of what's being done on footprint on sales and procurement? Could you give us some idea of the sizes of those initiatives and what they can contribute in 2025?

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

So, mainly, if I look at the restructuring, so China was about restructuring to the market reality. As said, we expect China margins still in 2025 to be somewhat under pressure given the difficult market, but we're realigning the teams to the market reality as such. And then, in the rest of the world, we are taking measures to align the teams to the new strategy. And then on top of that, as we talked about, we have performance improvement initiatives, especially related to procurement as well as then sales and operational excellence. So how are we organized on the lowest level of KONE to be able to deliver the best possible delivery organization towards our customers.

And what I said earlier is still valid, so we expect the performance initiatives to have more impact towards the end of the year, but still continue to ramp up all throughout towards our mid-term targets with an increasing speed towards the end of the period. And with the measures that we took now in the fourth quarter, we've included those

to our guidance and we expect in China, as I said to Daniela already, that there continues to be a margin pressure in China, but these are measures to counter that. And there are some benefits for the costs, but not that – some benefits for the global teams that are visible in the 2025 as well.

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

A

If we take a broader perspective...

Andre Kukhnin

Analyst, UBS AG (London Branch)

Q

Right.

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

A

...I guess that you've noticed the margin bridge we've shared in the Capital Markets Day, which is a guiding principle for us, so it remains. So I think we were showing the different blocks and the size of the different blocks. What I can say that, both on procurement and sales and operational excellence, we've been extremely diligent, precise and disciplined on working on these to ramp up our measures. I see the opportunity, though things take time to materialize, but we are very diligent and precise in executing this.

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

But we see in turn also...

Andre Kukhnin

Analyst, UBS AG (London Branch)

Q

Thank you.

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

...both the Service and Modernization mix continuing to improve in 2025, contributing positively. We will see some benefit in the margin bridge already for the performance initiatives towards the end of the year. And of course, we are very focused then also see a positive contribution from fixed cost leverage of the business.

Andre Kukhnin

Analyst, UBS AG (London Branch)

Q

Very helpful. Thank you. If I may, just one on cadence of first half/second half, would you expect the margin to show further improvement in the first half already or should we think about second half primarily?

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

So, if you think about what I said about the whole period all the way to mid-term targets, we are continuing to accelerate our margin improvement. But, definitely, we aim to improve margins quarter-by-quarter throughout the year.

Andre Kukhnin

Analyst, UBS AG (London Branch)

Q

Right. And is the service margin itself improving as well in 2025 as a standalone?

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

So, I guess, we have not guided that closely into the dimensions more given the total number. But, as we said in the CMD, so the measures we have taken on digitalizing the service business are actually something where we see good opportunities to drive margin improvement going forward. One – clearly, number one is that customers actually visibly, it will differentiate us. But then secondly, we also are driving with digital productivity improvements. And actually, as we are now ramping up country by country the digital offering, we see that materializing. But it will take some time to see that in the P&L as it will. First, you need to implement; then you need to learn the new way of working, and then you start to be able to reap up the benefits from profitability and productivity point of view.

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

A

And we're working on our pricing.

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

Yeah.

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

A

So the bottom line is in service and that's where we really have the highest attention. We work on one side to be smarter in our pricing; on the other side, to get more productive with digital technology.

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

Yeah.

Andre Kukhnin

Analyst, UBS AG (London Branch)

Q

Really helpful. Thank you very much for your time.

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

Thank you.

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

A

Thank you.

Operator: Thank you. Ladies and gentlemen, kindly be reminded that to limit yourself to one question and one follow-up. Thank you. We will now move on to our next question from John Kim of Deutsche Bank. Your line is open. Please go ahead.

John Kim

Analyst, Deutsche Bank AG (UK)

Q

Helpful. Thank you. Good morning. Could we unpack the slight margin decline in the Q4 order intake? Would be helpful to understand whether this is still the way to timing NBS or whether you're seeing any sort of evolution on margins in the modernization, again, looking at China?

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

So, in China, the modernization margins, as I've said earlier, that is the highest margin business for us. It's still a smaller part of the business and the most – the fastest growing business. And we actually see good development, good opportunities going forward in the modernization, especially the partial modernization part of it is very compelling part of it. But let's see. Right now, it looks quite good.

John Kim

Analyst, Deutsche Bank AG (UK)

Q

Okay. Helpful. And can you comment on service margins, price inflation versus [indiscernible] (00:29:20) for this year?

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

So, our service margins were more stable in 2024. And, yes, labor inflation was there. And also, as normally, we escalate the prices based on that. But more stable development in the service margins. And really, to me, the key focus there is that we are able to grow it fast. And now with the more than 10% growth in services, to me, it is a fantastic number to be able to get the double-digit growth in services.

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

A

And a number on which we've been extremely consistent in the past quarters. So we had many questions in CMD, but when you look back in the past three, four quarters and what we've delivered, again, 10.5% in Q4, very, very consistent growth delivery.

John Kim

Analyst, Deutsche Bank AG (UK)

Q

Yeah. Well done. Thank you.

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

A

Thank you.

Operator: Thank you. And we'll now take our next question from Vlad Sergievskii of Barclays. Your line is open. Please go ahead.

Vlad Sergievskii

Analyst, Barclays Capital Securities Ltd.

Q

Yeah. Good morning. Thanks very much for taking my two questions. I'll start on the [ph] adjustment to EBIT (00:30:33). And apologies for laboring point. On my numbers, it looks like this was the highest quarterly adjustment KONE has ever had. If I take away [indiscernible] (00:30:42) this €18 million development cost adjustment, can you explain what those exactly are and how the accounting worked on those €18 million? And have you done similar development cost adjustments before?

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

Can you just summarize again? The line is bad so on your actual question. I was losing one out of the three words on this end.

Vlad Sergievskii

Analyst, Barclays Capital Securities Ltd.

Q

Absolutely and apologies. So €18 million cost adjustment, what exactly that was related to? How the accounting worked? And have you done similar €18 million development cost adjustments before?

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

So, all of the cost, the €54 million are related to restructuring. Both – China was the biggest part, the €30-plus-million, and the rest were related to global teams, including our development teams to align the actions towards the strategy and how we want to deliver. On the development part, these are costs that related to fourth quarter, which we then discontinued the activities and they were part of restructuring cost.

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

A

And if we take maybe a broader perspective, I didn't – I mean, we've talked a lot about innovation. But I think reflecting back on 2024, there is one thing on which I'm very proud, which is we've very strongly realigned our innovation engines to what are the clear priorities of the company, and we pushed speed. Like this example of the Mono 100, six months to develop a new innovator to market that, frankly, the market was expecting for many years. So, yes, we made choices and we decided to stop some things. I feel very strong with it and I think KONE, with this, is a more agile company, a more nimble company and a more focused company, and I feel very good with that.

Vlad Sergievskii

Analyst, Barclays Capital Securities Ltd.

Q

Thank you very much. That's very clear. Last question, would you expect any additional adjustments for 2025 or restructuring costs at this point or not?

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

Of course, we continue to evaluate both the market as well as how we deliver our strategy. But I do not expect right now any restructuring costs that are meaningful in the 2025.

Vlad Sergievskii

Analyst, Barclays Capital Securities Ltd.

Okay. Thank you.

Q

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

Thank you.

A

Operator: Thank you. And we will now move on to our next question from Klas Bergelind of Citi. Your line is open. Please go ahead.

Klas H. Bergelind

Analyst, Citigroup Global Markets Ltd.

Thank. Hi, Philippe and Ilkka. Klas of Citi. First, on the composition of service growth. It seems like organic units grew mid-single digits clearly, and then, the [ph] ISPs (00:33:34), again, added another 1.5% and that leaves 4% price mix, which is higher than I thought, especially as you probably have a negative geographical mix there out of China still. Can you try and break that down a little bit? What I'm trying to gauge really is if digital and 24/7 contributed more this time to the organic growth in services? Thank you.

Q

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

Well, I see, you're seeing then on the penetration, so we continue to penetrate quite nicely with our connectivity. But I think, this time, I would call out more the overall services contributing to the value. So, yes, 24/7 and the added value is there, but I think we saw broad-based services positive development and especially, the western markets standing out, both Europe as well as more broadly. And those have been standing out in terms of growth in the fourth quarter. Doesn't mean that 24/7 didn't, but I wouldn't call that out as a main driver for that.

A

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

And if I would single one point that explain our growth in service, I would say our people. And the fact that on the ground every day, we try to differentiate by being committed with our customers, and the world of math actually helps us a lot. Example in Madrid, why did we took that contract? Because of our reputation, because of our people and then technology.

But it's hard to copy a culture. I think we have a culture of commitment with our customers and they see it and it's about experience. When you take an elevator, you want to be safe. And our people take it very seriously. And I think that's a big part of the explanation of why we are growing faster than others.

A

Klas H. Bergelind

Analyst, Citigroup Global Markets Ltd.

Thank you. Makes sense. My second one is on the margin development, first on modernization, Philippe. You improved this margin from COVID levels by 4 percentage points. That was the message at the Capital Markets Day. What about the quarter? Let's see if you can answer this. But, roughly, year-over-year in the quarter, just to get a feeling for the magnitude.

Q

And also, if I can just confirm that you said that you intend to improve the mod margin further in 2025, but with the service margin likely to be stable and for that to come further out and I'm obviously talking beyond the restructuring in China. I'm talking about the sort of...

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

A

Yeah.

Klas H. Bergelind

Analyst, Citigroup Global Markets Ltd.

Q

...ex-China business, if you like.

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

A

Maybe I clarify first on what I've said. So, so far, I have not said on service margins going forward anything I comment in 2024. But then looking forward with digitalization and so forth, of course, we expect the margins to improve in the longer term. And on the supporting performance, I was more highlighting the fact that as long as we continue to grow Service and Modernization as fast as we are doing, of course, that provides us a mix positive contribution to profitability.

And in modernization, all I would say that, I continue to be very happy with the steady growth of the profitability of the business as we're scaling it up. And let's see, it is a function, of course, the speed we can scale up, but also it is also one where how we deliver to our customers is critical in terms of how we can differentiate and command a pricing premium and impacting then the margins. But I have to say that the modernization team has done a good job.

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

There is – on that slide that I'm showing here, there is one word which is very important, which is industrialize our approach. Largely speaking, this industry is taking modernization as an artisan business because every case is different. And where I think there is a lot of opportunities in making it modular and simple so that, actually, it's simple and fast for our customers and it's simple and fast for our people. And by doing this, which takes actually a lot of innovation, we should increase our margin.

Klas H. Bergelind

Analyst, Citigroup Global Markets Ltd.

Q

Just final thing, the reason I'm asking is – I get the mix shift, Ilkka. The reason I'm asking is that you improved the modernization margin this quarter. Again, I think that, for some people, there was a feeling that all of the self-help would be quite back-end loaded and that is why I'm asking whether there is a chance to improve the mod margin in absolute terms and get the mix shift also in 2025?

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

Is there a possibility? Definitely, there's a possibility.

Klas H. Bergelind

Analyst, Citigroup Global Markets Ltd.

Okay.

Q

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

You've gone very far.

A

Klas H. Bergelind

Analyst, Citigroup Global Markets Ltd.

Thank you. Thank you.

Q

Operator: Thank you. And we'll now take our next question from Miguel Borrega of BNP Paribas. The line is open. Please go ahead.

Miguel Borrega

Analyst, BNP Paribas SA (London Branch)

Hi. Good morning, everyone. I've got two questions. The first one on maintenance. Grew 9.5% in 2024. I believe you said previously that you would expect a similar development in 2025. So wondering if you could shed some light on the moving parts regarding portfolio growth, scope, pricing and mix. Correct me if I'm wrong, but I think in 2024, you said 5% portfolio growth, 2% scope, 3% price offset by 1% mix. So, with inflation coming down, do you think you can maintain that level of pricing?

Q

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

Well, I guess, what we said about services is that we aim to grow that over cycle towards our mid-term target closer to 10%. And I stick to that target and, hopefully, that is consistently then also our target and ambition every year. And we continue to see good opportunities in growing units. Of course, with NBS market now being more difficult in the last years, we've been seeing modernization contributing positively to the units. And so far, we've been growing quite nicely our units as well.

A

And then market for acquisitions, these small maintenance companies continues to be very active. We have a good pipeline, so the aim is to be able to continue to add also from there. But, of course, it's a smaller part of the growth.

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

It's a disciplined approach.

A

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

Yes. With a smaller part of that growth formula as such. And then, yes, we do aim to also increase the value both from pricing, but also continuing to drive, for example, spare parts and so forth positively. So, we don't guide that in detail individual businesses. But I think the recipe from 2024 is not that different for 2025 or 2026 going forward.

A

And, yes, we do see opportunities to improve pricing even though the inflation is down. It's a part of the sales and operational excellence work we're doing.

Miguel Borrega

Analyst, BNP Paribas SA (London Branch)

Q

Thank you. That's very clear. And then just to follow up on the service margin. As you mentioned, in 2024 was stable despite the 10% growth. Usually, labor is offset by price and you mentioned productivity and value-added services. So, in other words, what prevented your margins from growing in 2024, and why should it be any different in 2025? Thank you very much.

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

Well, many of the things we're aiming to deliver to our customers with digital will actually be the key way to improve the profitability. And, of course, we do have right now, a mix negative shift with still fast growth in China contributing negatively to the profitability. So that's one negative on that side. But it is something where the scaling and getting the profitability up, not only growing, but improving profitability is at the heart of the strategy. So we expect that to be better going forward.

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

A

And on pricing, I think we are working in much more detail on understanding where these are pricing – where there is more value and, therefore, more price and we think we can do better. We started to clarify a couple stuff in 2014 and, hopefully, this starts to impact our 2025 level of profit in service.

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

Did we lose the line?

Operator: No, Miguel is still on. He's probably on mute.

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

Okay.

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

A

Good. We had 10 seconds of oh my God! We are by our self.

Operator: Right. Since there are no further response from Miguel, let me just move on to our next question from Benjamin Heelan of Bank of America. Your line is open. Please go ahead.

Benjamin Heelan

Analyst, BofA Securities

Q

Yeah. Thank you. Morning, guys. I just wanted to have a quick follow-up on some of the margin commentary for 2025. So you talked about the backlog margins being down slightly in 2024. Do you have a view on where that

will end up in 2025? Are you going to be able to offset cost inflation, et cetera, [ph] in 2025 just to (00:43:26) kind of order margin? How can we think about that progressing over the next 12 months?

And then just a quick one on the market outlook. You talked about a more positive outlook in North America. I think one of your competitors last night said something similar. So can you talk a little bit about what you're actually seeing on the ground? Are you starting to see the orders improve? Is it more just kind of qualified leads? Just help us understand a little bit what you're [ph] adjusting on (00:43:55) kind of day to day in the North American business? Thank you.

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

I'll start and then maybe you comment the market. But I would say that we still have double-digit growth in orders in America. So it's a quite a good market and has been for the full year. But, on the order margin, so trying to be clear and concise on your question, so I comment orders booked in fourth quarter and the margins we expect those to have when we deliver them going forward. So, in China, our margins are down for those orders and the margins we're booking for China are below the ones we're delivering. So there's clearly a margin pressure in China.

In rest of the world, the margins are more stable and there's a slight positive. So the orders we're booking are slightly positive towards the ones we're delivering. So a slight tailwind there. So that's on the orders margin.

And we do expect with that comment to continue to drive actually very product cost reductions. And in 2024, we had historically high product cost reductions, especially in China. But, of course, the pricing environment has been quite tough there as well. And the goal for 2025, we continue to see good opportunities to drive overall the product cost down with actions we're taking as such. But maybe on Americas, you want to comment?

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

A

Yeah, the momentum in America is building. It's been always very dynamic in modernization; bit less in service but positive. We've seen and we're expecting H2 to be better from a new construction standpoint than it was. And we see month after month more optimism, more construction even in new construction, so it's a great market to operate. We have a great team. We actually have a great business momentum on our three business lines. I'm very impressed by the work we are doing, especially in modernization, where our growth is really fantastic. So we are optimistic about the Americas.

Benjamin Heelan

Analyst, BofA Securities

Q

Okay. Very clear. Thank you.

Operator: Thank you. And we'll now take our next question from Panu Laitinmäki of Danske Bank. Your line is open. Please go ahead.

Panu Laitinmäki

Analyst, Danske Bank A/S (Finland)

Q

Hi. Thanks. I have a question on the sales mix in China. So, how much roughly was new equipment out of sales in 2024 and then modernization and services?

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

So two-thirds new equipment and one-third modernization and services, and the same rule applies there, two-third services, one-third modernization. So that's the mix. And like Philippe said, we expect that to continue to move in favor of modernization and services, where we see good growth opportunities going forward.

Panu Laitinmäki

Analyst, Danske Bank A/S (Finland)

Q

Okay. Thanks. And then just to clarify, when you talk about margin decline and further pressure on margin in China, does that only apply to new equipment or also on Service and Modernization?

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

That is mainly an NBS comment.

Panu Laitinmäki

Analyst, Danske Bank A/S (Finland)

Q

Okay. Thank you.

Operator: Thank you. And we'll now take our next question from Tomi Railo of DNB. Your line is open. Please go ahead.

Tomi Railo

Analyst, DNB Bank ASA (United Kingdom)

Q

Hello. It's Tomi from DNB. Can you just comment a little bit on the lowered outlook for China service from the third quarter? Clear growth to fourth quarter, slight growth.

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

Well, we are seeing the impact of the slower NBS market in earlier quarters and years impacting the growth in services, so less units being added to the service base, and therefore, the growth we expect for the market to be now a slight growth rather than a clear growth. So, no big drama there and as such.

Tomi Railo

Analyst, DNB Bank ASA (United Kingdom)

Q

Makes sense. Thank you. And just maybe on the comment – continued comment that 90% of the profits come from Services and Modernization. Was that different in the fourth quarter alone or was there kind of a deviation compared to the full year and fourth quarter?

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

No, not that different. I think the message is very clear that that's where we make our money.

Tomi Railo

Analyst, DNB Bank ASA (United Kingdom)

Q

Thank you.

Operator: Thank you. And we will now take our last question from Mikael Doepel of Nordea. Your line is open. Please go ahead.

Mikael Doepel

Analyst, Nordea

Q

Thank you. Thank you. Hello, everybody. Just a question on China, really. So, if you look back at 2024, we saw quite significant volume pressure in the new equipment business there and we also saw quite significant pricing pressure as well, if I remember correctly, being down double digits. I'm wondering what kind of the delta you expect on the pricing side for new equipment in 2025 in China? And also, if you expect to see any mix change in your business there, please?

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

Well, first, our outlook for the market was significantly down in units. We [indiscernible] (00:49:51) or I don't see that you can comment forward-looking pricing, but let's put it the competitive nature of the market is expected to continue in China. And we continue to see our business mix from these two-thirds, one-third to continue to be moving towards closer to the market. And the market value for China is 50/50 roughly in terms of new equipment versus modernization and services. So the mix shift towards Service and Modernization continues in our businesses also looking forward.

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

A

And I repeat our China priorities. Number one, cash. And we think we are very disciplined and we are doing rather well. Number two, margin. Number three, pivot to, let's say, 50/50 directionally. That means that really in NBS and modernization, we are much more intentional and structured in the customers we want to go after to protect our cash and protect our margin.

And the market is a market. We've clearly decided in the course of 2024 to adapt the way we are dealing with our business in China. And actually, we see better output out of this now. It's still a tough market from the new construction standpoint. But I really see our teams being very focused on where there is the biggest or the best compromise volume, margin, cash opportunity.

Mikael Doepel

Analyst, Nordea

Q

Okay. That's very clear. And if I just could squeeze in a final one on the margins, which you managed to improve your group margins by 30 bps last year and you expect to continue to improve this year. We talked a bit about the, let's call it, puts and takes for the year and how things are going to develop. But would you say that this is a good ballpark in terms of what to expect in terms of the improvement for this year given what you have previously said that it's going to be a bit more back-end loaded to get to your size?

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

A

Well, I will leave some work for you guys as well. We will definitely – as I said, we aim to improve our margin – continue the improvement our margins going forward and that's the goal.



Mikael Doepel

Analyst, Nordea

Good. Thank you very much.

Natalia Valtasaari

Vice President-Investor Relations, Kone Oyj

Okay. Thank you, Philippe. Thank you, Ilkka.

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

Thank you.

Natalia Valtasaari

Vice President-Investor Relations, Kone Oyj

And thanks to everyone who joined us listening in and participating with the questions. Great to see active dialogue, as usual. If you do have any follow-ups, please feel free to reach out to me or the team. We're happy to help.

And I guess, we've come to the end of our session then. So, thanks and have a great day.

Ilkka Hara

Chief Financial Officer & Member-Executive Board, Kone Oyj

Thank you.

Philippe Delorme

President, Chief Executive Officer & Member-Executive Board, Kone Oyj

Thank you so much. Bye.

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