Infineon Technologies AG, Q3 2022 Earnings Call, Aug 03, 2022 (EditedCopy)

TEXT version of Transcript

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Presentation

Operator [1]

Welcome to the conference call for analysts and investors for Infineon's 2022 Fiscal Third Quarter Results. Today's call will be hosted by Alexander Foltin, Executive Vice President, Finance, Treasury and Investor Relations of Infineon Technologies. As a reminder, today's call is being recorded.

This conference call contains forward-looking statements and/or assessments about the business, financial condition, performance and strategy of the Infineon Group. These statements and/or assessments are based on assumptions and management's expectations resting upon currently available information and present estimates. They are subject to a multitude of uncertainties and risks, many of which are partially or entirely beyond Infineon's control.

Infineon's actual business development, financial condition, performance and strategy may, therefore, differ materially from what is discussed in this conference call. Beyond disclosure requirements stipulated by law, Infineon does not undertake any obligation to update forward-looking statements.

At this time, I would like to turn the conference call over to Infineon. Please go ahead.

Alexander Foltin, Infineon Technologies AG - Head of Investor Relations [2]

Thank you, operator, and good morning. Welcome, ladies and gentlemen, to our earnings call for the fiscal third quarter of 2022. Also in this summer edition, you have the entire Management Board on the call with 1 new but well-known entrant. Let's go through Jochen Hanebeck, CEO; Constanze Hufenbecher, CDTO; Sven Schneider, CFO; Andreas Urschitz, our new CMO; and Rutger Wijburg, COO.

Our procedure remains unchanged. Jochen will open the call with remarks on the market situation and divisional performance, followed by Sven commenting on our key financials. Jochen again will provide the outlook and highlight key messages. The illustrating slide show, which is synchronized with a telephone audio signal is available at infineon.com/slides.

After the introduction, we will, as always, be happy to take your questions. [Operator Instructions] A recording of this conference call, including the aforementioned slides and a copy of our earnings press release, as well as our investor presentation are also available on our website at infineon.com.

As of now, I would turn the call over to Jochen. Please go ahead.

Jochen Hanebeck, Infineon Technologies AG - CEO & Member of Management Board [3]

Thank you, Alexander, and good morning, everyone. When looking at the macroeconomic and geopolitical situation, we see that exogenous headwinds are blowing stronger compared to our last update 3 months ago. Inflation rates are persistently high, leading to more hawkish central bank responses, PMI levels and consumer confidence are dropping.

The ongoing war in Ukraine causes scarcity and surging prices for energy supplies and materials. COVID-19 outbreaks continue to cause disruptions in -- particularly in China. Supply chains remain under stress, while demand in consumer-focused areas like PCs, smartphones, TVs, home appliances and battery power tools is weakening. In this challenging environment, dynamics and fundamentals in Infineon's key applications are still robust. Market conditions for applications like automotive, industrial, renewables, data center and IoT remain supportive. Correspondingly, we had a very strong June quarter with revenue and profitability progressing favorably.

A sign of unabated customer demand for many of our products is the backlog of confirmed and unconfirmed orders. The figure moved up further from EUR 37 billion at the end of March to EUR 42 billion at the end of June. We treat this indicator with very high caution as ordering activity is still characterized by shortages.

Furthermore, currency movement and price changes played a significant role in the sequential increase. Having said this, we see the supply-demand mismatch gradually improving, especially for products manufactured in-house. Constraints are less pervasive, lead times are stabilizing, customer escalation calls are getting less severe. It appears that we are transitioning towards the end of a long upcycle. However, the picture is very differentiated. Some markets have slowed down considerably. Others are showing fully intact dynamics.

And it's by no means clear that all applications will follow an identical pattern only at different points in time. Therefore, careful monitoring of lead indicators and acting swiftly will be paramount. I will elaborate more on this later in my outlook section.

Let's come to the financial performance in our fiscal third quarter. We recorded revenues of EUR 3.618 billion, 10% up compared to the previous quarter and a staggering 33% increase year-over-year. The stronger U.S. dollar provided a tailwind. On a constant currency basis, the quarterly growth rate would have been around 6%, put differently, around 1/3 of the quarter-over-quarter revenue increase is due to currency.

Additionally, the impact from the lockdown in Shanghai at the beginning of the quarter turned out to be less severe than expected, in particular for PSS. Furthermore, we were able to secure some incremental supply from external manufacturing partners and continue to benefit from supportive pricing. These better-than-anticipated factors had a positive impact on our profitability in the June quarter with a segment result of EUR 842 million, the segment result margin came to 23.3% after 23.1% in the quarter before and above the guidance of 21% given in May.

Let's now take a closer look at the divisional performance in the June quarter. The higher sequential growth rate was achieved by automotive with revenues of EUR 1.701 billion. The segment recorded a 14% increase compared to the previous quarter. All product groups within our broad portfolio contributed to this development, in particular, automotive microcontrollers.

The segment result improved to EUR 399 million, causing the segment result margin to progress further by almost 200 basis points quarter-over-quarter from 21.7% to 23.5%. The increase of sales and profitability was driven by the availability of additional supply, including from foundries, positive pricing effects and a favorable U.S. dollar exchange rate.

Overall, automotive production volumes continue to be depressed by material shortages and supply disruptions. A major such issue were the lockdowns in China at the beginning of the past quarter. Once these were elevated, a very rapid recovery of the domestic Chinese car market has set in, driven by public stimulus and demand resilience. It remains to be seen whether other regions follow with a certain time lag.

Lingering supply chain constraints and macro uncertainties, render unit estimates for the global car market quite difficult. The current prediction by S&P Global for light vehicle production of 80.8 million cars in the calendar year 2022 implies some limited upside for the second half of the year. In the near term, the market remains kept by supply rather than by demand.

While shortages are gradually easing, we continue to see instances of incomplete subassemblies, where a so-called golden screw is missing. In quite a number of cases, it is on us to deliver that crucial part. Besides this, content growth remains a strong driver in the foreseeable future. In particular, the fundamentals for ADAS and electromobility are fully intact, providing strong structural growth opportunities.

Infineon is well positioned to capture those as recent design win activity is showing. We were awarded the battery management system business of the electric version of a high-selling model of an established U.S. car manufacturer. Our Profound system understanding on the back of a global leadership position in semiconductors for automotive electrification enables us to provide high accuracy voltage measurement, best-in-class robustness and leading quality.

Also, our automotive silicon carbide business is gaining further traction. As announced earlier in the quarter, we have started cooperating with Vitesco technologies in the field of silicon carbide-based power semiconductors, supporting the efficiency of electric drivetrains with up to 800 volts.

In addition, we are excited about a near final talks with a well-known American OEM about a multiyear multi-model supply of silicon carbide-based onboard chargers with an estimated mid-triple-digit million euro business volume. Our high-value solution is enabling ultrafast charging. Here as well as in other customer engagements, we benefit from our differentiating offering, combining excellence in the device architecture, packaging capabilities, quality and supply security.

Continuing with Industrial Power Control, revenue of the segment amounted to EUR 436 million, slightly topping the high level of the previous quarter. Renewable energy and power infrastructure solutions continue to thrive. Also automation and drives showed robust momentum. On the other hand, decreasing consumer confidence is weighing on home appliances, which constitute only a mid-teens percentage of IPC's revenue. The segment result of IPC declined to EUR 82 million, corresponding to a segment result margin of 18.8% after 21.6% in the prior quarter.

As mentioned during our previous call, the timing of input cost increases and output price adjustment is not fully synchronous. In addition, the COVID restriction in Shanghai and resulting logistical challenges had an indirect negative effect on IPC's quarterly revenue and margin trajectory. We expect this to reverse in the September quarter.

Looking ahead, market dynamics remain positive across most of our target applications. Decarbonization is a strong structural driver for renewable energies and the related infrastructure. In the wake of the Russian invasion in Ukraine independence from fossil fuels has become a further motive driving the green energy transition. Market researchers from IHS Markit predict the buildup of 255 gigawatt of photovoltaic capacities in 2022, followed by 311 gigawatt in 2023, a year-over-year growth of 22%.

Infineon has a leading position in semiconductors for renewable energy applications. This is supported by our strong expertise in silicon carbide for applications with high-growth expectations such as photovoltaic inverters. Energy storage systems and the charging infrastructure for electric vehicles. For industrial drives, we currently see stable demand. While macro uncertainties are looming, CapEx plans are driven by the need to invest in alternative energy sources and smart manufacturing.

In mature markets like home appliances, on the other hand, we expect some softening due to deteriorating consumer sentiment. Now coming to Power & Sensor Systems. The segment for the first time crossed the EUR 1 billion per quarter mark, recording revenues of EUR 1.021 billion. Compared to the previous quarter, this corresponds to a 10% increase, helped by the stronger U.S. dollar and for PSS, fewer delivery limitations caused by COVID containment measures in Shanghai than initially expected.

From an application point of view, we saw continued good traction for enterprise power solutions, solar installations by residential customers and automotive charging. In contrast to this, demand for consumer applications like battery-powered DIY tools, PCs and smartphones was sluggish. On the back of higher revenue, the segment result of PSS increased by 150 basis points to EUR 277 million, leading to a segment result margin of 27.1% compared to 25.6% in the quarter before.

From a general market perspective, long-term underlying trends are intact, but a weaker macro environment causes some headwinds for consumer-related applications. Our differentiated product portfolio helps us balance these conditions. Take our industry-leading silicon microphones as a case in point. Their superior signal-to-noise ratio enables new cases like far field conferencing and studio recording with laptops partly offsetting smartphone weakness.

Another example comes from our server business. Infineon provides best-in-class power density and performance for DC-DC conversions for AI training and machine learning systems. Our power delivery solution is enabling a leading GPU platform for these applications. Such a system needs about 1.5x the semi content of a CPU for servers.

Finally, with a rising number of mobile devices, notebooks and battery-powered equipment, the need for increased charging power in smaller form factors is emerging. Gallium nitride based solutions provide the optimal answer. Anchor innovations, the global leader in charging technology has chosen Infineon's next-generation digital power controller and gallium nitride integrated power stage for fast chargers above 100 watt. This combination is achieving an outstanding system level efficiency beyond 95% and is reducing energy losses by 21% compared to other charging solutions. What the combination also underscores is that gallium nitride market is prone to follow the IDM, the integrated device manufacturing model.

Let's take a look at Connected Secure Systems. Revenue of CSS increased by 2% quarter-over-quarter to EUR 456 million. Overall, demand continues to outstrip supply in several areas, including industrial IoT, identity and payment while decreasing consumer confidence weighs on applications like wearables or gaming. The segment result declined to EUR 84 million, equivalent to a segment result margin of 18.4% after 24.1% in the previous quarter.

As you may recall, we had projected such a development as cost increases and price movements do not happen in sync. Furthermore, continued investments in R&D resources to further strengthen our product road map, constitute a near-term burden. The motive behind these efforts is to harvest the revenue synergies from the Cypress acquisition over the mid and long term.

In this regard, we are encouraged by ongoing design win momentum. Our general purpose microcontrollers and connectivity solutions, in particular, WiFi-Bluetooth combos have been selected for new smart TV models, handheld tools, home appliances and smart home devices by leading OEMs.

New business wins could be achieved for our embedded security solutions supporting wireless charging and IoT applications. Further later, combining our OPTIGA Trust M Express with our CIRRENT Cloud ID, we offer high-end security solution that provides a hardware anchor of trust to connect IoT devices to the cloud at scale.

Specifically, developers can easily and securely provision IoT devices and connect them to the cloud, while enhancing them with robust security right from the production line.

Now over to Sven, who will comment on our key financial figures.

Sven Schneider, Infineon Technologies AG - CFO & Member of Management Board [4]

Thank you, Jochen, and good morning, everyone. Let's start, as usual, with looking at our margin development. In the third quarter of our fiscal year 2022, gross profit came in at EUR 1.564 billion equal to a gross margin of 43.2%, slightly up from 42.9% in the previous quarter.

Excluding non-segment result effects, the adjusted gross margin amounted to 45.4%. This level is unchanged compared to the March quarter, which is somewhat better than we had initially forecast. Key reasons are a good agility in passing on cost increases to customers in an overall supportive market environment, the sooner-than-expected ending of the Shanghai lockdown and the tailwind from the stronger U.S. dollar.

Now to our OpEx numbers. Research and development expenses increased quarter-over-quarter from EUR 447 million to EUR 466 million, in line with our efforts to fund an ambitious technology and product road map. Compared to our revenue development, the increase was lower.

Selling, general and administrative expenses went from EUR 369 million to EUR 414 million, staying essentially flat as a percent of revenue. The net other operating income was EUR 6 million. The nonsegment result totaled minus EUR 152 million. Of this amount, EUR 78 million corresponded to cost of goods sold, EUR 7 million to R&D expenses and EUR 62 million to SG&A expenses. Other operating expense amounted to EUR 5 million.

The financial result for the June quarter was minus EUR 40 million after minus EUR 43 million in the previous quarter. Income tax expense amounted to EUR 134 million for the third quarter of the current fiscal year, equivalent to an effective tax rate of 20%. Cash taxes in the March quarter were EUR 66 million, resulting in a cash tax rate of 10%. For the entire fiscal year 2022, we continue to expect a cash tax rate of around 15% as current prepayments will be trued up.

Our investments into property, plant and equipment, other intangible assets and capitalized development costs amounted to EUR 542 million in the June quarter, up from EUR 494 million in the quarter before.

Depreciation and amortization, including acquisition-related nonsegment result effects, were EUR 422 million in fiscal Q3 after EUR 405 million in the preceding quarter. The free cash flow from continuing operations improved quarter-over-quarter as predicted from EUR 120 million to EUR 440 million, a higher profit and a lower increase of working capital compared to the previous quarter served to overcompensate high investments. Trade working capital moved broadly in line with higher sales volumes. This can, for example, be seen through an essentially flat inventory reach level at 124 days despite headwinds from rising input costs and a stronger U.S. dollar.

Now to our liquidity and leverage figures. Our gross cash at the end of June increased to EUR 3.6 billion, driven for the quarterly free cash flow. Our gross debt amounted to EUR 6.1 billion, slightly up due to the stronger U.S. dollar and corresponding to a gross leverage of 1.6x. Net debt stood at EUR 2.5 billion, equivalent to a net leverage of 0.7x.

Our strong financial position provides us full flexibility to fund our profitable growth path throughout different economic phases.

To close the financial part, let's look at our after-tax return on capital employed. The ROCE for the third quarter of our '22 fiscal year increased slightly from 12.3% to 12.7%, clearly, in excess of our cost of capital.

Now back to Jochen, who will comment on our outlook.

Jochen Hanebeck, Infineon Technologies AG - CEO & Member of Management Board [5]

Thank you, Sven. The geopolitical and macroeconomic situation has deteriorated in recent months, leading to pronounced weakness in several consumer-related applications. At the same time, key markets with strong underlying trends like automotive, industrial, renewable, cloud computing or IoT continue to be underserved.

Broad-based shortages are narrowing to fewer product areas. However, supply limitations remain fairly pervasive. Channel inventories are lean, whereas downstream customer stock levels are showing signs of increases. Having said this, the risk reward relation of holding semi inventory with typically high criticality, little obsolescence risk and constituting a small part of the bill of material appears favorable.

Therefore, we do not see an inventory digestion period in the near term. Needless to say, in such times of heightened volatility, it is of utmost importance to be watchful. Our key markets have different drivers and different cyclicalities. We are constantly and closely monitoring business KPIs in order to react swiftly, should the market conditions worsen from here. Our near-term outlook, however, is framed by strong visible demand and limited incremental supply capabilities. Importantly, in our base case, we assume no major disruptions from a potential cutoff of Western Europe from Russian natural gas exports. We are anyhow tackling this issue very actively.

Shortly after the beginning of the war in Ukraine, we have initiated measures to significantly reduce the usage of natural gas in our manufacturing processes, in particular at our sites in Germany and Austria. At these sites, we are confident to bring down natural gas consumption by about 2/3 by the final quarter of this calendar year. Furthermore, we are in a continuous exchange with the respective authorities regarding reliable energy supply.

First, our outlook for the fourth and final quarter of our 2022 fiscal year. Given the strength of the U.S. dollar against the euro, we adjust our assumed exchange rate to $1.05 from $1.10 before and anticipate revenues to increase further to around EUR 3.9 billion equivalent to a sequential growth rate of around 8%, almost entirely coming out of volume and price.

Since our assumed exchange rate for Q4 is only marginally different from the actual one. In Q3, ATV and PSS should grow around this rate, whereas quarterly growth rate of IPC should be significantly higher. For CSS, we expect a low single-digit percent revenue increase due to supply limitations.

The segment result margin should come in at a level of around 25%. Besides a positive impact from higher revenues, we also see more and more value creation from system solutions, crucially enabled by former Cypress technologies, products and competencies. These so-called product to system synergies contribute noticeably to our profitability improvement.

The outlook for the full 2022 fiscal year resulting from our forecast for Q4 is as follows: we once again raised our anticipated revenue figure from EUR 13.5 billion to around EUR 14 billion. Only a smaller part of the increment around EUR 140 million is related to the stronger U.S. dollar. The majority comes from additional volume and to a lesser extent, positive pricing.

The implied annual growth for the group comes to around 27%. From a divisional perspective, ATV is expected to grow at a slightly faster, PSS at a slightly lower pace. The growth rate of CSS should be in line with group average. For IPC, we anticipate a mid-teens percentage annual growth rate. The segment result margin for the full fiscal year 2022 is expected to land at a level greater than 23%, increased another percentage point from our previous forecast.

Our projection for investments into property, plant and equipment, other intangible assets and capitalized development costs remains unchanged at around EUR 2.4 billion, implying that we expect order equipment to reach us on schedule.

For depreciation and amortization, we continue to expect a value between EUR 1.6 billion and EUR 1.7 billion including amortization of around EUR 400 million resulting from the purchase price allocation for Cypress and to a lesser extent, still related to International Rectifier.

For free cash flow, we now expect a level of around EUR 1.4 billion on the back of higher revenue and improved profitability compared to EUR 1.1 billion guided previously.

Now ladies and gentlemen, it's time to summarize. The past June quarter was a strong 1 with EUR 3.6 billion of revenue at a 23.3% segment result margin and EUR 440 million of free cash flow. The macroeconomic deceleration and geopolitical tensions lead to deteriorating demand in some consumer-facing markets. At the same time, we observed robust dynamics in our main target application areas, automotive, industrial, renewables, data center and IoT. Supply is gradually improving but remains insufficient to meet customer demand.

Consequently, we expect continued revenue and margin expansion for our fiscal Q4 with around EUR 3.9 billion of revenue and around 25% segment result margin. It would be a strong finish to a very successful 2022 fiscal year with around EUR 14 billion of revenue, a segment result margin above 23% and around EUR 1.4 billion of free cash flow.

Vibrant design win activity is showing high customer interest in our value-adding system solutions with silicon carbide and gallium nitride gaining more and more traction. The operating environment is challenging with many products still on allocation. At the same time, we remain vigilant to early signs of cyclical movements in order to react on the OpEx and our CapEx side when needed.

The secular fundamentals for our business remain in place. Semiconductors are indispensable building blocks of decarbonization and digitalization.

Alexander Foltin, Infineon Technologies AG - Head of Investor Relations [6]

Operator, we would now like to open the call for questions.

Question And Answer

Operator [1]

[Operator Instructions] And we'll take our first question from Sandeep Deshpande of JPMorgan.

Sandeep Sudhir Deshpande, JPMorgan Chase & Co, Research Division - Research Analyst [2]

My first question is back again to silicon carbide. And you mentioned here that you had further traction in the silicon carbide market. We've heard the same from other players in the market as well. So how do you see this playing out? I mean, in the IGBT market, you were in pole position in auto electrification, whereas with silicon carbide, it seems to be a clearly multiplayer market rather than a single player dominating it as they did in -- you did in electrification. So how do you see this playing out over the next few years? And what impact would it have on revenue growth, margin, et cetera?

Secondly, because of your and other incumbents not being able to supply over the last couple of years, has that letting other players into the market, which could hurt your position in the longer term, not just your position, but on the peers who lost share to these new players who come -- who have come in suppliers because of being unable to supply?

Jochen Hanebeck, Infineon Technologies AG - CEO & Member of Management Board [3]

Yes, Sandeep, thanks for your questions. The second one, I just wanted to double check with respect to which product portfolio, is that meant your question?

Sandeep Sudhir Deshpande, JPMorgan Chase & Co, Research Division - Research Analyst [4]

Just in general, many other players are now...

Jochen Hanebeck, Infineon Technologies AG - CEO & Member of Management Board [5]

In general?

Sandeep Sudhir Deshpande, JPMorgan Chase & Co, Research Division - Research Analyst [6]

Yes.

Jochen Hanebeck, Infineon Technologies AG - CEO & Member of Management Board [7]

Okay. All right. Got it. Yes, maybe I'll start with that one. Of course, in an allocation situation, there is always opportunities for new players to get in. But I think, in general, with our capacity growth rates internally and externally, we are able to follow here, and I do not see across the bought areas where we really are in danger of losing market share, there might be -- the one or the other product here and there, where competitors were able to deliver better. But then in other areas, we had the upper hand.

In terms of silicon carbide, well, I talked about the actual design wins, which are proof that our value proposition in the market is accepted. I talked about it in the automotive space, in the IPC space also very strong. We will now reach soon the time frame where new design wins will basically come in line with the ramp-up of Kulim, which enables us then to ramp up capacities even more quickly.

So to me, this is still an open end. You know our current position in the market. And I think the final market shares will only be sorted out by the end of the decade. And then we are very well positioned with Kulim expansion, which is on track.

Sven Schneider, Infineon Technologies AG - CFO & Member of Management Board [8]

Sandeep, if I can add to your revenue and margin question. So Jochen already alluded to the revenue. We have given out the target of $1 billion mid of the decade, we're making good progress. We have a very steep CAGR this year. And this is prior to Kulim. The Kulim expansion will give us an incremental and additional -- significant additional revenues later.

On the margin side, as we have said before, the silicon carbide business at IPC is already clearly an accretive business. And if you look at automotive, we are making very good progress here, which is also mirrored in the very good expansion of the overall automotive margins you have seen over the last quarters.

Operator [9]

We will take our next question from Matt Ramsay of Cowen.

Matthew D. Ramsay, Cowen and Company, LLC, Research Division - MD & Senior Technology Analyst [10]

Yes. Thank you very much. Good morning, everybody. For my first question, I wanted to ask a bit on the automotive power business. You guys highlighted as you just mentioned in response to Sandeep's question, some progress in silicon carbide. I was -- we have the dominant IGBT franchise. There was some mention in the script about a new BMS win that you may have coming forward in the U.S.

So I think my question is really about the way the business is being won in automotive power. Are each of these segments being sort of fought with competitors individually? Or is this like a collective business sale that you guys bring BMS and IGBT and silicon carbide and rapid charging to the table, and it's more of a package sale at the customer level? I'm just trying to get an idea of those customer dynamics? And are they different by end customer and OEM? Or are they pretty consistent across the board? And then I have a follow-up.

Jochen Hanebeck, Infineon Technologies AG - CEO & Member of Management Board [11]

Yes. Thanks, Matt. And first of all, thanks for staying in so -- to such a late hour for you. So you are asking about the automotive power business. So I can state that the battery management system is, of course, part of the overall architecture of the car, which we, of course, from our P2S approach also want to understand and here guide the customer to the right solutions. But still, it's somewhat separated from the main inverter. And you know that our main business, of course, there are auxiliaries, but the main business is the inverter.

And here, we do have a very good position in the IGBT part of it, and we are building up the same position in the silicon carbide. We do see long term that, of course, silicon carbide will dominate the inverter, but there will be also substantial part related to IGBT in the entry segment and in the second axle will remain. And we can really here guide the customer what is the best solution also benefiting from our overall position in automotive.

The second most important application becomes the onboard charger. That's why also this design win is noticeable because the onboard charger with fast charging and be directional is increasing in terms of value and becomes also interesting. And again, we will see here IGBT solutions at the beginning, now moving to silicon carbide and ultimately, gallium nitride because this offers an even better power density. So overall, the customers benefit here from the broad experience and competencies of Infineon in these, what you call automotive power business.

Matthew D. Ramsay, Cowen and Company, LLC, Research Division - MD & Senior Technology Analyst [12]

Thank you very much for that. As my follow-up is somewhat unrelated. And anyway, in my investor call, I've observed a lot of, let's just say, imprecise math around what the effects of higher natural gas prices and the power bill for Infineon and given your factory footprint might be. Do you guys were kind enough in the script to give us some details on some of those things went by a little bit quickly, if you wouldn't mind recapping some of the mitigation efforts you're making there and if there's any way to bound for us the absolute sort of euro amount that the power build may have changed. And if there's any government subsidies potentially around that, that would be really helpful.

Jochen Hanebeck, Infineon Technologies AG - CEO & Member of Management Board [13]

All right, Matt. So I hand over first to Rutger, who will explain once again what we are doing in order to save natural gas and then Sven will chip in the numbers.

Rutger Wijburg, Infineon Technologies AG - COO & Member of the Management Board [14]

Matt, so this is Rutger speaking. So of course, semiconductor fabs and particularly our fabs in Germany, have dependency on gas. The other hand, also one should realize that the gas consumption that we have is pretty modest compared to, let's say, other industries like chemicals or steel. Steel, as Jochen already indicated, at the moment of the start of the Ukraine war, we immediately took additional measures to further bring down our consumption.

And like I said, we expect that by -- the quarter 4 of this year, we will be able to reduce our gas consumption in Germany by about 2/3. So what we are doing is actually replacing their gas that's being used for heating, which is the most important aspect of the fab and replace it by oil. So that means that instead of using gas, we are able to continue our operations by heating the facilities by oil. And then also by that, we become far less dependent on any gas.

So I'm pretty confident that is one of the operational issues we're dealing with, that we are able to handle that one, like we have been handling many of the other issues. So I'm pretty confident that we'll be not of an impact to us. Sven?

Sven Schneider, Infineon Technologies AG - CFO & Member of Management Board [15]

Yes. Thanks, Rutger. After this conferencing message also the numbers, the energy bill for Infineon is close to EUR 300 million for this fiscal year. So you see it's not very significant compared to other industries. But if you look at the development then you see the steep increase. Last year, it was EUR 200 million. So there's an increase of 50%. And I don't want to guide now the future, but I think we can expect some further increases unless the situation really comes down. So EUR 300 million, give or take, a little bit above is the number for this year, Matt.

Operator [16]

We will take our next question from Johannes Schaller of Deutsche Bank.

Johannes Schaller, Deutsche Bank AG, Research Division - Research Analyst [17]

You mentioned that some of the constraints on the supply side are getting less pervasive, lead times coming down. And then also the customer escalation costs getting a bit less severe. I was just wondering, in that context, what does that mean for your pricing power going forward? So how should we think about incremental price increases for the portfolio as a whole as we go from here?

And then Mr. Hanebeck, you referred to the infamous golden screw situation. I would probably characterize it as auto semi is currently being restocked where they are available, and that's driving a good amount of demand. And if this golden screw situation is not resolved, then that growth driver of restocking is going to go away at one point. So how do you assess that situation? Do you think in the next few quarters, some of these missing components, I guess, microcontroller is still a big issue are going to get delivered and auto production is going to improve.

So the backlog in the auto industry is being worked down? Or do you think we will stay with the golden screw situation for a while, and that maybe creates a bit of risk around the inventory situation, maybe not now, but say, in 6 months' time or so?

Jochen Hanebeck, Infineon Technologies AG - CEO & Member of Management Board [18]

Yes. Thank you, Johannes. And I have passed on the first question on pricing to Andreas, and I take then the second on the golden screw.

Andreas Urschitz, Infineon Technologies AG - CMO & Member of Management Board [19]

Andreas speaking. First and foremost, we do see a reversal from the typical past always price downtrend pattern. That was a rule in previous history, and that has now been turned around. We believe it's going to be here to, then also stay for the time being. There are several factors behind that trend inversion. The most important one I want to mention is the importance of semiconductors in general in the electronics value chain, creating end customer experience, and so to say, value to customers of our customers has grown substantially relative to the past.

In finance products, in particular, are system relevant in this context, system relevant mostly in the areas around carbon neutral and also digitalization. So we have something in our hands technology and product wise, where some people say it's kind of a new gold in the industry, if you will.

We have been historically a bit slower in average to increase prices relative to the one or the other peer. However, we are on track now to very decisively managed to deploy market prices, which allow us to extract a very fair share of the industry profit pools towards our P&L. And when I fair, I mean fair for both, our customers and Infineon. That's where we stand. Back to Jochen.

Jochen Hanebeck, Infineon Technologies AG - CEO & Member of Management Board [20]

Yes. Thank you, Andreas. And on your second question, the golden screw. Yes, the golden screw is very often related to foundry capacity. So in our case, related to microcontrollers or connectivity components. Now you can assume there is a certain overlap between consumer related capacities at the foundries and those products, but only to a limited extent, most of the consumer products use different technology nodes.

Nevertheless, we see incremental supply in certain nodes. We expect this also others to see. So yes, microcontroller or this golden screws will over time be delivered. There's also the element which I described before already that we do see inventories at the Tier 1s on request by the OEMs to increase, which, in a way, is a good development because those buffer inventories then provide the decoupling, which is required, and we do not see any digestion of this inventory in the near time. And to be very honest, I expect the next allocation to be around the corner, affecting XEV as they are on the same capacities as renewable products. And we see here increased interest by certain customers to protect us from -- to protect themselves from -- or towards supply security.

Johannes Schaller, Deutsche Bank AG, Research Division - Research Analyst [21]

That's a very interesting observation. And Andreas, just maybe coming back on the pricing. So I know you're not guiding for next year yet. But directionally, should we assume that pricing remains a tailwind as we go into your next fiscal year?

Andreas Urschitz, Infineon Technologies AG - CMO & Member of Management Board [22]

Allow me to hand that point over to our CFO, Sven.

Sven Schneider, Infineon Technologies AG - CFO & Member of Management Board [23]

Yes. Thanks, Andreas. Johannes, you already said it. Sorry, we are in the Q4 call. So unfortunately, we cannot guide for next year. But I will add a little bit of flavor to what Andreas very well described. If you look at the fiscal '22, you see that we had a revenue number of EUR 11 million, I'm rounding, now we expect EUR 14 million. So this 27%, if you look at the components, I would say a good half of that is coming from volume and the rest is coming from mix, currency and currency, I think you can calculate very well on the back of our rule of thumb calculation and price.

So you see that the price component was an important driver in this fiscal year. But I would leave it there, and we will guide to the next year and including pricing then in November.

Operator [24]

We will take our next question from Aleksander Peterc of Société Générale.

Aleksander Peterc, Societe Generale Cross Asset Research - Equity Analyst [25]

I have a question on CSS and the sequential growth in the fourth quarter, which seems a little bit lower than the rest of the group. And I would have thought that improved foundry capacity would help CSS obviously to be reliant on external manufacturing. So why do you not see a better momentum in this particular business? And I have a follow-up.

Jochen Hanebeck, Infineon Technologies AG - CEO & Member of Management Board [26]

Yes. Thank you, Aleksander, for the question. I hand it over to Sven helping us on this.

Sven Schneider, Infineon Technologies AG - CFO & Member of Management Board [27]

Yes. Aleksander, you're talking about revenue, right?

Aleksander Peterc, Societe Generale Cross Asset Research - Equity Analyst [28]

Yes.

Sven Schneider, Infineon Technologies AG - CFO & Member of Management Board [29]

Yes. Okay. So I mean if we look at the Q3 number, which is EUR 450 million, it has gone up significantly compared to the beginning of the year and also very much to last year. So you are seeing we are doing everything we can to secure supply. There is incrementally additional supply also in combination with some consumer-related weakness in some markets, and we are trying to get that as much as possible. So now guiding for a number which is below the 8% is all we can do from a demand perspective, we could service much more, but that is based on our current view on the capacity side. But if we can get more, we will take it, we will ship it and we will translate it into revenue.

Aleksander Peterc, Societe Generale Cross Asset Research - Equity Analyst [30]

Okay. And then my second question, maybe it's not the right time to answer it right now, but I still like to share your thoughts on your margin trajectory. So Q4, 25% is well above your through-cycle model 19%. And for the current year as well, I think we're looking at over 23%, to maybe 23.5%. So at what point will you tell us how much of this margin uplift is structural and your through-cycle model needs to be upgraded? Or do you think we're just at a high order cycle and things will be left in the future?

Sven Schneider, Infineon Technologies AG - CFO & Member of Management Board [31]

Okay. I take it as well, Aleksander. So first of all, as you said, there is a very good trajectory significantly above the 19% for the cycle, which we are now guiding to 25%. There are clearly structural and sustainable elements, as we have said in the intro script, if you look at our megatrends, which are contributing. We have the volume and the capacity also from our internal investments, which are coming on stream more and more. If you think about Villach, if you think about Dresden, and there is also the additional component of pricing.

You have said it a little bit already. Yes, we are -- the new team is as well, very committed to a profitable growth path. And without now commenting on the revised number we have said, and I'm happy to repeat that once the markets have normalized and stabilized, we will upgrade this model. And if you look at the drivers or the levers which have been communicated also in the industry, be it price, be it manufacturing productivity, be it portfolio management, be it OpEx scaling, there is no reason why they should not apply to us. But please stay with us, and we will give you more guidance when these conditions have been fulfilled.

Operator [32]

Our next question comes from Sébastien Sztabowicz of Kepler Cheuvreux.

Sébastien Sztabowicz, Kepler Cheuvreux, Research Division - Head of Tech - Equipment Research [33]

I've got 1 on the MCUs. ST just announced a flagship partnership with Cariad, the software arm of VW on MCUs and also on advanced MPUs. Do you see any change in the competitive landscape? And how do you see your own positioning in the MCU market generally speaking, at the large German OEM, which are large customers for Infineon. That's the first question.

The second one is on silicon carbide. Could you provide a little bit some color on the level of your backlog right now? And also following some questions previously -- how do you see the dynamic from the Chinese silicon carbide player that seems to be quite aggressive in terms of investment in this new technology. Do you see new entrants coming to silicon carbide from China?

Jochen Hanebeck, Infineon Technologies AG - CEO & Member of Management Board [34]

Yes. Thank you, Sebastian, for your question. So yes, it was a well marketed design win here. But let's put it in perspective. Our automotive MCU business is going to cross EUR 2 billion revenue next year and will double over the next 5 years. So that's what you have to compare any other design win with. And I think with this, we are holding in automotive microcontroller, a very, very strong position. And this changes only, given the stickiness of the products only very, very -- is sticky for a long, long time.

On the MPU side, we are not engaged. So we are focusing on our -- on the MCU, which we think will be a substantial market in the automotive space. On silicon carbide, I don't think we disclose this one, the backlog. In terms of China, you're right with the observation. It's basically the leapfrog strategy that Chinese competitors, which they also applied in other markets are trying to leapfrog with the new technology. We do see here major hurdles. Of course, there is a wafer bull supply market or players that are trying to establish themselves, maybe that comes in earlier into the picture. On the device side, we haven't seen things that are really, let's say, state-of-the-art here, the non-Chinese players are more the ones that are offering competitive solutions.

Operator [35]

Our next question comes from Janardan Menon of Jefferies.

Janardan Nedyam Menon, Jefferies LLC, Research Division - Equity Analyst [36]

I have 2 questions actually. One is I'm just trying to reconcile your comments on supply easing in some areas and a decrease in escalation calls, et cetera, and weakness in recent times from the consumer side with the ongoing strength in your order book and increase further to EUR 42 billion. So is it that there's an increasing proportion of that from the automotive side? I mean is a proportion from automotive increasing? And can you also give us any flavor you alluded to the potential for shortages moving a little bit away from MCU perhaps more to the EV components? And is it that you're getting a big increase right now on the EV side on your order book? If you could just give us a little bit of flavor on what is driving up that order book would be useful.

And Second question is on the IPC side. When I compare your guidance for full year growth in your Q2 results versus your Q3 results, there seems to be a clear change in IPC, where you were guiding for about 10% growth in IPC in the previous quarter for the full year, and now you're guiding at 15% and IPC also seems to be your strongest area into fiscal Q4.

So is that -- going back to your opening remarks, is that all coming predominantly from renewable energy? And is it that this is a clear change because of the situation in Russia, et cetera, that your customers across the world are significantly ramping up renewable energy investments. And is this something that you would expect to continue into fiscal '23 even if there was more of a macroeconomic slowdown, et cetera?

Jochen Hanebeck, Infineon Technologies AG - CEO & Member of Management Board [37]

Yes, Janardan, thank you for your question. Sven will give you some insight into the backlog and then I take the topic on potential shortage in the power semi and the IPC part.

Sven Schneider, Infineon Technologies AG - CFO & Member of Management Board [38]

Okay. Yes, Janardan, I fully understand where you're coming from. We want to be here very transparent. So we see these very strong markets where no demand weakness is visible at all based on our structural trends, and we have these consumer-related markets where we see signs of weakness.

If we look at the backlog, how does that reconcile? The backlog has increased further from -- by EUR 5 billion, Jochen said it already in the intro statement. This is one KPI we are looking at, but with a pinch of salt, given that other factors like the weaker markets, like the easing of escalation calls is clearly visible. If you look at the backlog per se, in the backlog composition, please always think about the effects which drive it. There are 3 main ones.

On the one hand, of course, the orders coming in from our customers, so the customer wishes, so to say. But then you have the price impact and you also have a currency impact in the reevaluation of the backlog. And just to give you 1 hint in the EUR 5 billion increase quarter-over-quarter, 1/3 of the increase is coming from currency only. So you see that's a pretty significant result and -- or contribution, sorry.

The backlog, again, to your question, to give you more flavor, around 70% of the backlog is up to 12 months. If we now look at short term versus long term, the long-term orders grew -- and I learned that in English, it's disproportionately because overproportionately doesn't exist. So in other words, the long-term orders grew stronger than the short-term orders. And yes, more than half of the backlog is automotive and the backlog and the order book is continuously rolling forward. Now back to Jochen.

Jochen Hanebeck, Infineon Technologies AG - CEO & Member of Management Board [39]

Yes. Thank you, Sven. And I'll start with the IPC part. So IPC was a bit more constrained this quarter due to the Shanghai related logistical challenges, and that's why there is another increase, but you're perfectly right with the assumption that IPC is driven by renewables. Of course, there's an automation and drives business, which is stable, but the growth momentum comes out of renewables. And here, very strong.

On the solar side, we cannot catch up with demand. Is there a link to the Russian Ukraine war, probably likely. On the wind side, we also expect recovery. The wind market is still driven by government subsidies, and we see here governments pouring in more money for next year.

And now you were asking about the shortages potentially there, which I alluded or hinted at. And it's basically those 2 end markets, the xEV and the renewable market meeting because as we speak, it's mainly IGBT business. And in the future, more silicon carbide, and I expect these 2 markets to compete for capacities. And as they are, let's say, partially also new supply chains that are in setup mode across the industry. I -- it's hard to imagine that this disruptive change, if you want, is working completely smoothly. I don't see that but we are preparing and for that also for next year.

Janardan Nedyam Menon, Jefferies LLC, Research Division - Equity Analyst [40]

Understood.

Operator [41]

We will take our next question from Adithya Metuku of Crédit Suisse.

Adithya Satyanarayana Metuku, Crédit Suisse AG, Research Division - Research Analyst [42]

I had, firstly, just a clarification on the natural gas situation. Do you see any effect from any indirect chemical shortages? You said earlier, the chemical companies use a lot of gas. Are there any chemicals that are produced using natural gas, which might be in shortage and hence may impact your production? Any color you can give there would be helpful.

And then Jochen, just a question for you. Since you've become CEO, what have you found the most surprising? Now one of the impressions that investors have is that Infineon has been slow to market with technology transitions. And this has allowed other players to enter, for example, the silicon carbide market. What is your view on this? And do you see any need to make any improvements on the execution side when it comes to technology transitions and time to market?

And then just a clarification for Sven on the last question. On the IPC side, should we expect the run rate where you are guiding for in the September quarter to continue into the next year, given the strength in renewable energy demand?

Jochen Hanebeck, Infineon Technologies AG - CEO & Member of Management Board [43]

Yes. Adithya, thank you for your questions. I'll start with the question to chemicals. Yes, you're right. Of course, the statements we made before that we feel comfortable with our own activity with relate to natural gas replacement does not cover all suppliers. And of course, we are also here dependent on chemical industry. It's a very, very fast network, very difficult to predict whether there is an impact coming. But yes, we, of course, have precursors coming out of this that's remaining risk, absolutely.

You also alluded to that we were slow in bringing innovation to the markets. You hinted at the silicon carbide. I accept that as an example, I think we had also other examples where we were very early in bringing innovative products, think about our power solutions for enterprise, think about microphones, think about automotive products in general, but you are right, one of my priorities is to improve this innovation to customer value journey. And here, I would like with the Infineon, the Board colleagues and the whole Infineon team to get our innovative ideas faster to the market and create customer value. Yes, a priority topic. And now I hand to Sven.

Sven Schneider, Infineon Technologies AG - CFO & Member of Management Board [44]

Yes, Adi. I think I have to be fair to you and the others. So again, I cannot guide for next fiscal year on IPC. But I would say if you take the quarter 4 and the input which you have received from us on the pull-in of the renewables that should give you some, I would say, a reasonable guidance for the increase of IPC going forward.

Operator [45]

We will take our last question today from Didier Scemama of Bank of America.

Didier Scemama, BofA Securities, Research Division - Director in EMEA Equity Research & Head of European IT Hardware [46]

Just wanted to go back to your point on the backlog. So if I understand correctly, the EUR 42 billion backlog is not something that you would rely on. And you also said that around half of it is automotive, so around EUR 21 billion, which is a fair amount higher than your current revenue and your current capacity in ATV. So my question is, if we were to see a halving of the backlog, do you think that you would still grow in fiscal year '23? That's my first question.

And the second one, if you could give us a little bit of perspective on that EUR 21 billion plus backlog for automotive, how much of that is xEV related? And I'm not saying just silicon carbide agilities but also BMS, any microcontrollers you have in the -- and ADAS related. So if you could give us a bit of color on that, so that we can appreciate what might be at risk of being canceled and what might not be at risk?

Sven Schneider, Infineon Technologies AG - CFO & Member of Management Board [47]

Yes. So Didier, sorry, I can't give you the more details on the composition, but I can repeat that it's not half, more than half of the backlog is indeed coming from automotive. That is correct. The question on holding of the inventory, I think, has been answered and to what extent this then translates into stable higher or reduced backlog numbers really needs to be seen. But just 1 word because we are getting used to these ultra-high numbers, we just run the numbers. The backlog is 3x the annual revenue. That's not the sustainable situation. In previous years, we have been much lower. So even if the backlog would go down, I would not take that as a negative signal at all.

Jochen Hanebeck, Infineon Technologies AG - CEO & Member of Management Board [48]

And even 1 step further, even if -- as you say, if it were to reduce by 50%, it would not make me nervous.

Didier Scemama, BofA Securities, Research Division - Director in EMEA Equity Research & Head of European IT Hardware [49]

Okay. Well, that's good because it sounded really bearish during call. So it's good that you clarified that. For my follow-up, I wanted to just ask you a question to Andreas. Can you maybe give us a sense of what you're going to change in terms of the pricing and marketing policies of Infineon versus what was implemented before?

Andreas Urschitz, Infineon Technologies AG - CMO & Member of Management Board [50]

As I said before, it is one of the topics where Infineon will put going forward, even more effort into, namely extracting a fair amount of the value, which are to a good degree, unique and highly differentiating semiconductors and semiconductor-based solutions, including pieces of software are creating amongst our customers. So in other words, we're going to push forward much stronger the topic, value-based pricing that then bottom line truly results then also in probably improving the bottom line, depending on other circumstances. More cross-divisional shall be done, if you will.

So the entire topic of bringing to customer the true value of sytem solutions. So combining, for instance, a microcontroller from Cypress with a sensor like a radar chip, adding a piece of middleware and software on it to create a functionality like presence detection or room segmentation to customers. That is something we consider to be pretty unique in our offering also as compared to competition that shall and will allow us value-based pricing to be the new norm.

Alexander Foltin, Infineon Technologies AG - Head of Investor Relations [51]

Thank you very much, Andreas. I think it's time to wrap up as we have an adjacent press call coming up. I think we have been very comprehensive. So thank you all for your questions. Given that there is still a queue of analysts, it gives the Investor Relations department a nice raison d'etre for today. Please feel free to contact us. Otherwise, we wish you a nice and wonderful summer and a great day ahead. Operator, please close the call now.