Airbus SE (OTCPK:EADSF) Q4 2022 Earnings Conference Call February 16, 2023 1:30 AM ET

Company Participants

Helene Le Gorgeu - Investor Relations
Guillaume Faury - Chief Executive Officer
Dominik Asam - Chief Financial Officer

Conference Call Participants

Daniela Costa - Goldman Sachs
Robert Stallard - Vertical Research
Doug Harned - Bernstein
Olivier Brochet - Redburn
Chloe Lemarie - Jefferies
Tristan Sanson - BNP Paribas Exane
Milene Kerner - Barclays
David Perry - JPMorgan
Harry Breach - Stifel
Christophe Menard - Deutsche Bank
Ian Douglas-Pennant - UBS

Operator

Ladies and gentlemen, thank you for standing by. Welcome to the Airbus Full Year 2022 Results Release Conference Call. I am Melanie, the operator for this conference. [Operator Instructions] At this time, I would like to turn the conference over to your host, Guillaume Faury, Dominik Asam and Helene Le Gorgeu.

Helene Le Gorgeu

Thank you, Melanie. Good morning ladies and gentlemen. This is the Airbus full year 2022 results release conference call. Guillaume Faury, our CEO and Dominik Asam, our CFO will be presenting our results and answering your questions. This call is planned to last around 1 hour and 15 minutes. This includes Q&A, which we will conduct after the initial presentation. This call is also webcast. It can be accessed via our home page by clicking on the dedicated banner. Playback of this call will be accessible on the website, but there is no dedicated phone replay service.

The supporting information package was published on our website earlier today. It includes the slides, which we will now take you through, as well as the financial statements. Throughout this call, we will be making forward-looking statements. I invite you to refer to our safe harbor statement that appears in the presentation slides, which applies to this call as well. Please read it carefully.

And now over to Guillaume.

Guillaume Faury

Thank you, Helene, and good morning, everyone. Thank you for joining us early this morning for our full year 2022 results call. I am happy to be today here in Toulouse with Dominik to run you through our results. Again, in 2022, we faced an adverse operating environment. On the 1 hand, last year, resoundingly confirmed that people want to fly and they do so even at higher ticket prices. Airlines have returned to long-term fleet planning and are preparing for long-term growth.

In this context, with the reconfirmed long-term visibility on demand, we decided last month to ramp up our A320 family to a monthly production rate of 75% in the middle of the decade. On the other hand, 2022 has also been a year of multiple disruptions, mainly driven by the cumulative impacts of COVID and the Russian invasion of Ukraine, international sanctions, the energy crisis, aggravated already existing tensions on logistics, materials, components and also skilled workforce.

Our supply chain, facing these other severe circumstances, did not recover at the pace we had anticipated. As a consequence, we had to adapt our operations and the associated production plan for the year, eventually leading to our December announcement. I have to say the situation has been quite frustrating last year. Obviously, we were not satisfied with the number of aircraft we deliver in the end. As you know, in Q4, we delivered 226 commercial aircraft taking our full year 2022 deliveries to 661 aircraft. While this represents an 8% increase compared to 2021, this is about half the increase we had initially planned. As you will see when I come to our guidance, this means that it will take us 2 years to achieve what we had planned to do in one.

Nevertheless, we met our financial targets. For the full year 2022, our EBIT adjusted stood at €5.6 billion. Our EBIT adjusted reflects our deliveries, but also our efforts on competitiveness and further benefited from the overall positive impact of non-recurring elements. Our free cash flow before M&A and customer financing stood at €4.7 billion, €4.7 billion and has been supported by a favorable foreign exchange rate environment as well as a strong positive phasing impact from working capital. These solid financial results with a net income of €4.2 billion and confidence in our future financial performance underpin our dividend proposal for 2022 of €1.80 per share. As we enter 2023, we see strong demand in all areas of our business, while at the same time we are facing persisting supply tensions.

This year, we expect our commercial aircraft delivery profile to be backloaded again. In light of ongoing geopolitical and macroeconomic turbulences, risks of further disruptions remain. Before we look at our commercial environment, let me mention that the 3-year provision period under the terms of the deferred prosecution agreement with a French so-called Parquet National Financier, the UK SFO in the U.S. Department of Justice. This has ended on the January 31, 2023, a couple of weeks ago. We are awaiting the formal determination by the authorities that Airbus has complied with the terms of the GPAs and to close the prosecution against Airbus in line with the requirements of each country. Airbus will continue to meet its obligations under the consent agreement, extended until October 2023, as mutually agreed with the U.S. Department of State.

Let me say as well that over the past years, we have implemented company-wide a strong culture and governance with respect to ethics and compliance, which we will maintain and continue to develop going forward. Let's now look at our commercial environment. In 2022, commercial air traffic continued to recover with domestic and regional markets leading the way. International traffic has progressively been closing the gap, strengthening our confidence in the widebody segments outlook. Air travel demand came back even faster than we expected during summer, and the trend was confirmed by the strong activity around the end of the year, where global traffic was already trending close to previous levels. The recent reopening of China is proving to be a strong positive driver for air traffic as it progressively recovers. All regions should now converge towards normalized levels.

Let me remind you of our orders and backlog for the year. We booked a total of 1,078 gross orders, of which 222 in Q4. On widebodies, we booked 63 orders including 24 freighters and further progressed on the remarketing of our aircraft concerning the increasing commercial momentum on widebodies. We saw 258 cancellations, of which only 49 in Q4. The cancellation in the year were already largely anticipated and embedded in our backlog valuation as of year-end 2021. As a result, net orders were positive at 820 aircraft, and our backlog in units amounted to 7,239 aircraft at the end of December 2022, including 6,093 A320 family aircraft for more than 6,000 for this family.

Our net book to be significantly above 1, illustrates the strong appetite of our customers for our well positioned and diversified portfolio. This was once again evidenced by the large Air India order. We were honored to receive earlier this week, which is obviously not yet reflected in our order book as of the end of December 2022. So, really honored by this honor. At book level, our backlog in value increased to €449 billion to close to €450 billion in 2022, mainly reflecting our book-to-bill above 1 as well as the strengthening of the U.S. dollar. Our robust and diversified backlog would support the company's resilience in case macroeconomic conditions were to deteriorate.

Looking at helicopters. In 2022, we booked 362 net orders compared to €414 million in 2021, with a book-to-bill above 1, both in units and in value, orders that – sorry, orders are well spread across programs and include 12 H160s for which we secured customers on all targeted segments. 2022 was a solid year, I should say, a good year with ongoing market recovery and positive momentum on both civil and military markets.

Finally, in Defense & Space, 2022 turned out to be a difficult year in a complex geopolitical and macroeconomic environment. Russia's attack on Ukraine had consequences that spread to many sectors and businesses. One of the direct consequences is the loss of access to the Russian Soyuz launches. At the same time, Ariane 6 is experiencing further delays and Vega C is temporarily grounded, sorry, following the launch failure in December. All in all, in 2022, Europe has lost most of its capacity to access space. This is also directly impacted. This also directly impacted our Space business. In addition, across our Defense & Space division, the rising inflation impacted our long-term contracts, in particular, the A400M program, and we are not immune to disruptions in the supply chain.

Still, we also had some successes, important ones. The Airbus built ESM, European service modules successfully bought NASA's Orion spacecraft safely around the moon and back home, and we secured important orders, such as the FCAS future combater system demonstrates our Phase 1b and Eurodrone, two important difference programs for the decades to come. they will be critical for Europe's security and strategic autonomy. We also booked orders other orders, which will as well play an important role in our future of business, such as the contract to deliver 20 latest-generation Eurofighters to the Spanish Air Force as well as the renewal of two contracts for the in-service support of the Spanish fleet, the order by the Republic of Indonesia for 2 Airbus A400M services, becoming effective, which makes Indonesia the tenth operator of this aircraft and the contracts to provide two high-performance optical Earth observation satellites and services to. This confirms the confidence of our customers in our company and products and takes our order intake to €13.7 billion, corresponding to a book-to-bill of around 1.2.

Now Dominik will take you through our financials.

Dominik Asam

Thank you, Guillaume, and good morning, ladies and gentlemen. Our fiscal year 2022 revenues increased to €58.8 billion, up 13% year-on-year mainly reflecting the higher number of commercial aircraft deliveries, higher contributions from our divisions and the appreciation of the U.S. dollar. Our fiscal year EBIT adjusted increased to €5.6 billion up from €4.9 billion in the prior year. The year-on-year improvement in our EBIT adjusted is mainly driven by the commercial aircraft delivery increase, partially offset by a slightly less favorable hedge rate versus fiscal year 2021. It also includes some non-recurring elements. As you might recall, in the first 9 months, we recorded a non-recurring positive element of €4.4 billion related to retirement obligations, partially offset by €0.1 billion negative impact resulting from international sanctions against Russia.

In Q4, we made progress on our compliance-related topics, which allowed us to release provisions for an amount of €0.3 billion, while the loss of 2 Pleiades Neo satellites resulted in a negative impact of €0.2 billion. While we continued to benefit from our assets and competitiveness, the investments in preparing the future, in particular, our decarbonization efforts and ramp-up are now materializing in our cost base. This is particularly visible in our R&D expenses, which stood at €3.1 billion in 2022 versus €2.7 billion in 2021. Our fiscal year earnings per share adjusted stood at €5.15 based on an average of 787 million shares. Our fiscal year free cash flow before M&A and customer financing was a record €4.7 billion, supported by working capital upside and the appreciation of the U.S. dollar.

Now on to the next slide regarding our profitability. Fiscal year 2022 EBIT reported was €5.3 billion. The level of EBIT adjustments totaled a negative €0.3 billion, including €308 million positive impact from foreign exchange mismatch and balance sheet revaluation, of which minus €41 million in Q4, 28 million related to the A380 program of which minus €5 million in Q4, minus €477 million related to A400M of which €258 million negative in Q4, minus €82 million related to the Aerostructures transformation in France and Germany, of which minus €34 million in Q4 and minus €79 million of other costs, including compliance costs, of which minus €35 million in Q4.

Earnings per share reported includes minus €250 million of financial results. It mainly reflects minus €232 million of net interest result, it also includes a negative impact from the revaluation of financial instruments and a positive impact from the revaluation of certain equity investments. The tax rate on the core business continues to be around 27%, the effective tax rate for net income is 19%, including a net release of deferred tax asset impairments. The resulting net income is €4.2 billion, with earnings per share reported at €5.40.

Turning to our U.S. dollar exposure coverage, as a reminder, the forwards portfolio and the euro conversions are presented altogether, both in terms of volumes and associated rates. The mark-to-market figures on the other hand, are only associated with the Forward instruments. There's no mark-to-market associated with euro conversion deals, we have entered into. In fiscal year 2022, $20.3 billion of forwards matured with associated EBIT impact and euro conversions realized at a planned rate of 1.22 versus 1.21 in fiscal year 2021. This volume includes $6.2 billion in the fourth quarter at a blended rate of 1.23.

In fiscal year 2022 also implemented $16.4 billion of new coverage at a blended rate of $116 million of which €3.5 billion in Q4 2022 at a rate of 1.07 mainly for the years 2023 through 2025. As a result, our total U.S. dollar coverage portfolio in U.S. dollar stands at $93.9 billion with an average lended rate of 1.24 as compared to $98.3 billion at 1.25 at the end of 2021. Our portfolio is currently being adjusted by implementing some rollovers to reflect the latest ramp-up trajectory and our delivery target for 2023.

Now let's look at our cash evolution in fiscal year 2022. Our gross cash from operations of €5.5 billion mainly reflects our EBIT adjusted. Our working capital has decreased by €1.4 billion it includes a positive phasing impact from the timing of receipts and payments, including PDPs and is supported by a strong U.S. dollar. The A400M continued to weigh on our free cash flow, but less so than fiscal year 2021. Our fiscal year '22 capital expenditures amounted to around minus €2.5 billion versus minus €1.9 billion in fiscal year 2021. We expect our capital expenditures to slightly increase in 2023.

Free cash flow reported was plus €4.3 billion. It includes M&A activities for minus €210 million mainly reflected related to the acquisition of ZF Luftfahrttechnik [indiscernible] while customer financing cash flow amounted to minus €146 million. You might see additional usage of cash going forward, even though overall, the aircraft financing environment remains solid with sufficient liquidity in financial markets for our products. The 2021 dividend of €1.50 per share or €1.2 billion in total was paid in Q2. On our pensions, we contributed €0.6 billion for the full year 2022. The net pension deficit taking the surplus in our UK schemes into account stood at €2.9 billion as of December 2022, a €4.2 billion reduction during the course of 2022, mainly driven by the increases in interest rates.

We're currently benefiting from the higher interest rate environment to reduce the sensitivity of the pension deficit to interest rates, but also to other parameters such as inflation, credit spreads and volatility in equity markets. Our net cash position stood at €9.4 billion as of the end of December 2022, and our liquidity position further strengthens to €31.6 billion. Looking back at the last 3 years, we have managed to weather multiple challenges to our balance sheet, including the pandemic and the DPA payments, closing the year 2022 with a net cash position exceeding our net pension deficit by €6.5 billion.

On that positive note, back to Guillaume.

Guillaume Faury

Thank you, Dominik. On to commercial aircraft, in 2022, we delivered 661 aircraft to 84 customers. Looking at the situation by aircraft family, on 220, we delivered 53 aircraft, we continue to ramp up and are still on track for rate of 14 that we envisaged by the middle of the decade. On 320, we delivered 516 aircraft, of which 264 A321s. To match supply, we have adapted the ramp-up trajectory. We are now progressing toward a monthly production rate of 65 aircraft by the end of 2024, and 75 in 2026. We continue to progress on the ground work to secure rate 75 and all our sites are now A321 capable, including our [indiscernible].

On the XLR, we expect the entry into service to take place in Q2 2024, no change. On widebody, we delivered 92 aircraft of which 32 A330s and 60 A350s, on A330, we increased our monthly production rate to around 3% at the end of 2022 as per our plan, and we now target to reach rate 4 in 2024. On A350, we are now at a rate of around 6 aircraft per month in order to meet growing demand for widebody aircraft and after a thorough feasibility assessment with our suppliers, we have now decided to target a monthly production rate of 9 A350s, which we plan to reach at the end of 2025. We're also pleased to have reached an amicable settlement with Qatar Airways, which will enable us to move forward and work together as partners again. This includes an agreement on terms for the delivery of 50 A321neos and 23 A350s.

Let's look at Airbus commercial financials for 2022. Revenues increased by 15% year-on-year, mainly reflecting a higher number of deliveries and the strengthening of the U.S. dollar. The EBIT adjusted increased to €4.6 billion from €3.6 billion in 2021 reflecting the increase in deliveries and supported by some non-recurring elements, partly offset by a less favorable hedge rate compared to 2021. Non-recurring elements included positive impacts from retirement obligations and compliance-related topics partly offset by the impact resulting from international sanctions against Russia.

Looking at helicopters, in 2022, we delivered 344 helicopters, 6 more than in 2021. Revenues increased 8% year-on-year to €7 billion, mainly reflecting growth in services and a favorable mix in programs. EBIT adjusted increased by around 20% year-on-year to €639 million, non-recurring elements, including the positive impact related to retirement obligations. As a result, the profit margin stood at 9.1% in 2022. I'm pleased with the solid performance of the division and the strong program execution, well done helicopters.

And let's complete our review of 2022 with Defense & Space. Revenues increased 11% year-on-year, mainly driven by higher volume in military aircraft and Eurodrone. The decrease in EBIT adjusted mainly reflects the impairments related to the loss of 2 Pleiades Neo satellites in December, as Vegas and to the delays on Ariane 6 as well as the impact of rising inflation. This is partly offset by higher volume in military aircraft ramp up in Eurodrone and a positive impact related to retirement applications booked in Q1.

On the A400M, we delivered 10 aircraft in 2022. We continue with development activities towards achieving the revised capability roadmap. Retrofit activities are progressing in close alignment with the customer. In 2022, an update of the contract so-called EAC estimated at completion has been performed and an additional charge of €4.5 billion recorded. This mainly reflects updated assumptions including inflation and risks related to the remaining SOC3 contractual development milestones that remain to be achieved. Risks remain on the clarification of technical capabilities and associated costs on aircraft operational reliability, on cost reductions and on securing export orders in time as per the revised baseline. Overall, for Defense & Space the external environment remained challenging, leading to disappointing results in 2022, a lot of headwinds.

Turning to our guidance, and let me read our guidance. As the basis for its 2023 guidance, the company assumes no additional disruptions to the world economy, air traffic, the supply chain, the company's internal operations and its ability to deliver products and services. The company's 2023 guidance is before M&A. On that basis, the company targets to achieve in 2023 around 720 commercial aircraft deliveries, an EBIT adjusted of around €6 billion and free cash flow before M&A and customer financing of around €3 billion.

This guidance reflects the adjusted growth trajectory of our commercial aircraft business, taking into account the phasing of pre-delivery payments the investments we are making to prepare our future and the adverse operating environment we continue to face. This now brings me to our key priorities, which, by the way, haven't changed. This year, more than ever, our main priority is to ramp up commercial aircraft production, including single-aisle aircraft as we progress towards rate 75 now in 2026.

Again, in this adverse environment, we will closely collaborate with our suppliers to match our production with supply. In parallel, we will continue the long-term transformation of our company. That becomes more short-term and mid-term now to digitalize and decarbonize our processes, our products and our services, the geopolitical disruptions of 2022. First and foremost, the war at Europe's doorstep, has clearly demonstrated the need for a strong and sovereign Europe, in particular, in defense and high-end technologies. We are proud of contributing to Europe's ambition by taking a leading role in major defense programs, notably the Eurodrone, the [indiscernible] and the future combat air system which all made significant progress last year. When it comes to sustainability, as highlighted at our last Airbus summit, we endeavor to set the sustainability agenda for the aerospace sector. This is our priority. That's my priority.

Our focus is now to transition together with a broader industry ecosystem ambitions to actions. Last year, we defined near-term reduction targets for Scope 1, Scope 2 and Scope 3 emissions. I'm happy to announce that our target have now been approved by the SBTi, the Science Based Targets initiative. This is an important milestone as these objectives going forward will influence decision-making at all levels of our company. And I will tell you more on this topic during our annual press conference just after this call. So stay tuned.

Last year, we also made concrete progress on our road map to achieve these objectives. Let me mention some of the highlights. On SAF, sustainable aviation fuel. We continued our efforts to drive the production and use of SAF as illustrated by our landmark partnership with Qantas and our recent MOU with Neste, one of the largest SAF producers in the world. On hydrogen, we continue to make sure our innovative technologies in preparation for entering to service of a hydrogen powered aircraft by 2035 in the frame of our so-called ZEROe program we announced the development of a hydrogen-powered fuel cell engine. In parallel, we signed a partnership agreement with CFM to test a direct combustion engine fueled by hydrogen.

Having said that, in the short-term, decarbonizing aviation starts first by replacing thousands of older aircraft with our latest generation fuel-efficient aircraft already enabling airlines to significantly reduce their emissions and use SAF in large quantities. Those aircraft are already certified for the use of 50% of SAF. Decarbonization is not only a challenge. It is, for us, a very important opportunity.

Before taking your questions, let me finish with a few words about Dominik, Dominik has been a real pleasure and privilege to work with you in the last 4 years. And I think the numbers of 2022 in spite of all the challenges, speak for the very important and crucial contribution you made to this company and bottom line, it's been a real pleasure to work with you. So I wish you all the best in your future job at SAP. But in the meantime, we will run the road shows together. This being said, a bit emotional about it – sorry for that. I hand over, I guess, to you, Helene.

Helene Le Gorgeu

[Operator Instructions] So Melanie, please go ahead and explain the procedure for the participants.

Question-and-Answer Session

Operator

Thank you. [Operator Instructions] The first question comes Daniela Costa from Goldman Sachs. Madam, please go ahead.

Daniela Costa

Hi. Good morning. Thank you very much for taking my question. I wanted to focus on the free cash flow guidance with two related questions to that. And first one, if you could just elaborate a little bit sort of what are the headwinds and the tailwinds that make up the €3 billion this year, given it is a little bit below where the market was expecting is whether there are any one-offs or anything that we should – that the market might have forgotten there. And then relates somewhat related to that, but I think in the past, you have mentioned that once you've reached the situation of net cash potentially around €10 billion that you would consider extra distribution to shareholders in the form of potentially buyback, I wanted to understand if there were any updates regarding that thinking, given, I guess, sort of where your balance sheet is now and the cash you expect to generate this year sort of might put you in that situation? Thank you.

Dominik Asam

Thank you, Daniela. Maybe I'll have a step at the headwinds on free cash flow. I think you always have to look at this in the context also of 2022. Recall that initially, we thought in 2022, we will reach a lower number. So we now exceeded the initial guidance by €1.2 billion. So we had a strong tailwind there especially on contract assets, but also very favorable timing of accounts payable. So, each of these two items accounted for a positive €3.3 billion in 2022. And now you see a little bit of a flip side in that. So if you look at the kind of cumulative of the 2 years, it's actually quite close to the cash conversion of one. And we stick to our commitment that over the 5-year planning horizon from 2022 through 2026, there will be a cash conversion of 1 as we've stated already on the Capital Markets Day. So that notoriously difficult and volatile swing in working capital, of course, also not made any easier with the kind of deferral to the right of some deliveries on the PDP side.

Guillaume Faury

Thank you, Dominik. And when it comes to the – reaching the €10 billion of net cash, Well, we are at 9.4% in the first half of the year, and there will be the payment of the dividend. You see what we expect for 2023 in terms of free cash flow. So I have to repeat what we said. I think earlier last year, that's a discussion we expect to have more in 2024 than 2023, and we will have a discussion when we close that bridge. But I'm happy of the – of the results of 2022 because that was a much stronger free cash flow and net cash position at the end of the year than what we thought at the very beginning of the year.

Daniela Costa

Very clear. Thank you very much.

Guillaume Faury

Thank you.

Operator

The next question comes from Robert Stallard from Vertical Research. Sir, please go ahead.

Robert Stallard

Thanks so much. Good morning.

Guillaume Faury

Good morning.

Robert Stallard

A couple of questions from me. First of all, Guillaume, on your revised ramp target. Given all the challenges that you've had in 2022, how confident are you that you and your supply chain can now deliver on this revised plan. And then secondly, there have been some reports that it's not just a supply chain that's having some challenges, but also Airbus internally having some process difficulties. So I wonder if you could comment on that as well. Thank you.

Guillaume Faury

Yes. Good morning. Robert. So indeed, we had to update our ramp-up plan, taking the lessons and just facing the hard facts of the supply environment we're in. In 2022, to be clear, the situation has been mainly, if not solely, driven by the very complex and bad supply environment. So that's really what we had to face. And we now I mean in our target to deliver 720 by the end of 2023, which means we will have taken 2 years to do the ramp-up we had anticipated in 1 year when we entered into 2022. So that's not something we like. But that's the fact, and we have built the plan for 2023 based on the facts and today's situation and all the headwinds we see in the supply chain, and we believe this situation should ease progressively moving forward, but we have designed our ramp-up for 2023 based on the today's situation of supply, and therefore, we believe in that trajectory, that's a trajectory that is facing the brutal fact of the very bad environment within.

On the second point, I don't know exactly where things came from on those reports. We need to deliver in spite of the adverse environment we're in. And that's basically the situation we're in. Yes, of course, we have to compensate a lot of the supply problems by adapting ourselves, by reorganizing when we have a crisis here and there when we have suppliers of small or very large equipments that tell us they won't be able to deliver what they have planned in a given quarter. So it's a lot of adaptation work, and if the problems are not necessarily coming from internal operations, we have to find the solutions internally. And – and that's what I shared with my management earlier this year, and that's maybe what triggered some comments outside, but us just facing the fact that it's a difficult environment. And therefore, there is a lot of work to be done to compensate, to be creative and to find solutions to constantly adapt our production plannings to the crisis that are popping up here and there. That's what we've done in 2022. We have ramped up by sort of 50 aircraft more in '22 than '21. And what we anticipate for 2023 is a bit of the same kind. We are targeting 60 across more, a bit less than 60 compared to what we have done in 2022. And we really believe that's feasible in the current environment. So it's a bit of a long answer, but that's probably the most important question when it comes to our guidance in 2023.

Robert Stallard

That's great. Thanks very much.

Operator

The next question comes from Doug Harned from Bernstein. Sir, please go ahead.

Doug Harned

Thank you. Good morning. I wanted to continue on the supply chain issues on the A320. First question is – if you look at last year, during much of last year, engines appeared to be the main issue with respect to production and delivery delays on the A320 family. Our understanding is that shifted now and there is a more diverse set of suppliers that may be an issue in Europe. So the first question, if you could help us understand how you're dealing with the supplier environment right now given that it may be a little bit different than you saw for much of last year. And the second question is that with high demand for the A220 family. We would assume that when you've got some delays now that this pushes back the timing of deliveries and may put sort of you may have escalators that are frozen or some penalties for customers some compensation. Can you help us understand if there is any material issue there with respect to margins tied into delays?

Guillaume Faury

Okay. So thank you. When it comes to the supply situation in 2022, we had indeed a lot of delays on the delivery of engines in the first half of the year with all engine manufacturers. And that has led us to revise the production planning several times, and to have very difficult Q2 and Q3 in terms of deliveries as we were really missing engines. In Q3, Q4, mainly in Q4, engine manufacturers came back to this revised planning. So we had stability in the second half of the year. But we had issues across the board. We had issues with the supply chain coming from the lack of supply of electronic components very low in the supply chain, impacting a lot of our Tier 3, Tier 4 suppliers and therefore, indirectly us at a later stage with a lot of issues with onboarding workforce after COVID finding the skills and competencies, delaying the ramp-up of a number of suppliers, we have issues with logistics around the world, supply of raw material, there is a long list of problems that impacted all the supply chain, not only engine makers. And that's what led us to revise the planning several times in the year to come back to the market with a revised guidance twice and the number you saw at the end of the year. This has rather stabilized. I'm not saying the supply chain environment is better. I'm just saying, I think it has stopped degrading, and we think it's going to improve progressively moving forward, but we don't count on a complete recovery of the supply chain in the short-term, and we will continue to face problems in 2023. That's what we have factored in our guidance, including on engine.

Yes, we have to very actively managed the backlog when we face difficulties and challenges on the delivery. As you have seen, we now see reaching rate 65 by end of next year, which is 1 year later than what we were targeting when we entered into 2022. And we continue to invest in CapEx all around the world to prepare our production systems for rate 75, all A321 capable that's happening now. We have the opportunity to have a visit yesterday in Toulouse on the new A321 file in the Jean-Claude building, and this will be achieved by 2026. So we continue to do the work to ramp up to rate 75 as soon as we can. We count on the supply chain to deliver as per our plans this year, and these are revised plans that make it much, much easier, but there are constant negotiation and discussion with customers to replan and to be able to do it in a way that works for us. Maybe Dominik, you want to say a few words on the matter.

Dominik Asam

Yes. I mean, of course, because of the deferral, there are discussions, I mean the key question, which is to be answered case-by-case is what is exclusively land we talked about engine delays, which are really excusable delays. So this is the part of the current year and a really focused item this year to readjust the recall that we have been asked by customers to re-phase big time in 2020 because of COVID and have accommodated these requests. And now we have to kind of cope with the consequences on the supply chain of the COVID impact and the Ukraine crisis later on.

Guillaume Faury

Thank you, Dominik.

Doug Harned

Thank you.

Operator

The next question comes from Olivier Brochet from Redburn. Sir, please go ahead.

Olivier Brochet

Yes. Good morning, Guillaume. Good morning, Dominik. I have two questions. The first one on the Chinese final assembly line, the deliveries were extremely low in December and January. How do you think of the improvement path? And when do you expect a return to a normal situation on this one? And the second is on the 321 final assembly line extensions that you mentioned is now being done. When do we have the entry in service for the various lines in Mobile, in Toulouse and Tianjin, please?

Guillaume Faury

So when it comes to Tianjin, you probably have in mind that we have converted the line from A320 to a flexible A320, A321, we have stopped the assembly line for some weeks to do – more than weeks, by the way, a couple of months to do this conversion. So I'm not very accurate in my answer, but we had to do this transition and this has led to some disruptions. On top, we had some COVID events when the – I mean, the zero COVID policy of China was lifted. So it's been quite turbulent, but there are no specific issue that we anticipate in changing when it comes to deliveries. So that's not something that is critical on my own agenda. When it comes to ramping up the A321 capacity in the new files around the world, Mobil is moving forward as planned. I think its first delivery plan in 2024, '25. I don't have it top of my mind. And when it comes to Toulouse, the new A321 file in Toulouse will deliver its first aircraft, the very first by end of this year. So we are moving forward as planned, and this will support the capacity of accelerating the ramp-up of the A320, A321 family next year very significantly.

Olivier Brochet

Thank you.

Operator

The next question comes from Chloe Lemarie from Jefferies. Madam, please go ahead.

Chloe Lemarie

Yes. Good morning, thank you for taking my questions. I have a first one on the EBIT bridge from 2022 to 2023 because 2022 performance reflected a number of one-offs. I'm thinking of the catch-up as a positive headwind recording in Defense and Space. So could you shed a bit more light on the key moving part going forward, notably aircraft contribution, cost ramp and inflation? Second question, is on the A350 ramp. It's lower volume than [indiscernible], but arguably much faster. So are there any specific pressure points that you're watching within the supply chain that could slow this, I'm thinking of titanium, but maybe some other products as well? Thank you.

Dominik Asam

I will have a step at the bridge from 2022 into 2023. So first of all, there is, of course, the increments on aircraft. And don't forget that on that increment, it's not all kind of high-margin A320. There is also a very significant increment from A220s. So that is important to take into account. There is a little bit of a step-up, but really marginal, I would say, very low triple-digit million on investment in the future. The R&D has already reached a very high level as ramp is already very expensive in '22. So that's not a big delta, slightly better ForEx, a couple of hundred million, I'd say. You mentioned some nonrecurring items we had, I think, of the pension past service adjustment of €400 million, but there was also €0.3 million negative on Ukraine. We had €300 million on compliance and then there we get to see a couple of hundred million loss so that gives you a net of minus €0.4 billion because the net was positive in '22 and will turn to zero next year. And that pretty much gives you the bridge. So this is how you can quite easily bridge and there is, of course, all kinds of smaller puts and takes, but not material in the overall context se there – there is some negative inflation impact, but we are trying to compensate that.

Guillaume Faury

When it comes to the widebody ramp up, actually, when you look at our numbers, the products where we have the steepest ramp-up are the 220 and the widebody. But of course, in volumes, the A321 probably is the one that dominates the supply chain agenda. As we say, once bitten twice shy, we are very prudent on the widebody ramp up, and we spent a lot of time with our supply chain assessing the capabilities, there are a number of critical items, small to large engines will be something we will be monitoring very closely. And that's something that is probably on the critical path. But we have as well a number of equipment and systems. When it comes to titanium, that's something we're managing and there is no volume risk as long as we can continue to source. So, that's not something that we believe is going to be a big problem for this year. So again, yes, it's still compact on widebodies, a very strong demand. That's something we saw coming already at the beginning of last year. You remember, I started to flag the fact that the demand for widebodies was really coming back and now we see it in the bookings and in all the campaigns and therefore, we prepare our own production system for this new situation.

Chloe Lemarie

Thank you very much.

Operator

Your next question comes from Tristan Sanson from BNP Paribas Exane. Sir, please go ahead.

Tristan Sanson

Yes. Good morning Guillaume. Good morning Dominik. Thank you for taking my question. The first one would be to regain on the management of the ramp-up of aircraft production. Can you tell us whether there are specific actions that are being taken to address the issues that you faced in Q3, Q4 in terms of monitoring of the supply chain or increased control incentives, whatever that would show a slight change in your approach of these it difficulties, or does it look same as last year? And the second question is a follow-up on the cost inflation. You described at the Capital Market Day in September of last year, how escalation was predicting over time, the activity from the volatility of your cost base have been that there could be temporary headwinds. How is it unfolding versus that plan in terms of evolution of energy remarks and salaries, you don't really seem to be so stressed about it for 2023, but a bit more granularity would be quite interesting? Many thanks.

Guillaume Faury

Good morning Tristan. Well, indeed, we are spending a lot of time and efforts managing the supply chain situation. We have already a very high level of visibility and transparency when it comes to the supply chain, and it's something we have kept increasing and improving over the course of 2022. What we are improving as well is the ability to anticipate and manage crisis much faster than we did earlier, going deep into the supply chain faster than, than we were used to do. That's something we have organized as well with some of our Tier 1 suppliers. So, that's probably the more collaborative and accelerated way of understanding the situation, finding alternatives. We have also invested in the applications and the resilience of the supply chain. We will continue to do this in 2023. So, there is a long list of actions that we keep running and we have so-called lessons and exercise of 2022 in a very structured way to keep improving the way we are managing this other new and very adverse situation of supply chain that we have not experienced in the last what decades probably. So, we are adapting to that situation, and we have also adapted our own planning. As you see, we are now anticipating to ramp up in a much slower way than what we had targeted beginning of 2022. That's also our lessons learned of the environment. Now as we see the environment improving and we see some signs that this is happening, we will adapt again and prepare for '24 and '25. Dominik on the next question.

Dominik Asam

Yes. Maybe on the inflation topic, yes, there is actually a negative, let's say, a couple of hundred million in the bridge from '22 to '23, that's a net. And the way it works is we have a very significant increase in cost, but to some degree, you can offset it by our escalation clauses, which on the one hand, are capital, on the other hand, applied to the entire revenue base of commercial. And some of the inflation-related topics, especially on contracts, which are so-called estimated completion contracts have actually been embarked already in our financial statements in 2022. So, this is why it's still a burden on us. So, it's not something that you take easily, but it's not a huge item in our '22 to '23 bridge. But as it will remain the case in compounds, which is of course, not our current expectations given what's happening in the market. But in case of compounds, it can become, of course more material, and this is what we continue to have out here.

Tristan Sanson

It's very useful. Thank you for your comments.

Operator

Your next question comes from Milene Kerner from Barclays. Madam, please go ahead.

Milene Kerner

Yes. Hello. Thank you for taking my question. I have two, please. Guillaume, you pointed that you still expect challenges in 2023, in your view, how long will it take the industry to be back to levels of productivity you had in 2018. And then my second question is for Dominik, and I will echo what Guillaume said, it was a real pleasure interacting with you over the years. My question is that you had close to €24 billion of gross cash at the end of December. What is the benefit of the rising interest rates environment on your interest expense going forward?

Guillaume Faury

I will take the first one. You are putting the finger on a difficult topic, which is the productivity of industry. And actually, the productivity today is much lower to say the least, and much lower than what it was before COVID. We have still not recovered from COVID from that perspective and from many angles, and that's something we are focusing very much on this year. It is coming from many different sources. This very disruptive environment that is making us very inefficient, to be honest. And that's also the large renewal of the workforce on jobs that are technical, and it takes time to onboard people to find the skills, but also to train them and to have people back to what we experienced before COVID in terms of highly skilled, highly trained manual and intellectual schemes of people. That's something that is maybe less material with the large OEMs, the large companies than it is in the supply chain, the smaller companies have a lot of difficulties to manage that situation. We have still the impact of lockdowns, teleworking, which that has been taken and not completely recovered from. So, it's a complex picture in terms of productivity and efficiency of large industrial sectors. And that's something we are still recovering. So, your question of when will we be back to 2018 levels of productivity, Honestly, I don't know. That's the jury is out, but we want to work hard on those topics because that's very much driving our performance. So, that's a topic which is high on my own personal agenda and the one of my team, but it's a sectorial issue. Dominik?

Dominik Asam

Interest rates, yes, you are right in mentioning that in a certain way, higher interest rates purely on the kind of treasury side are positive for us. You mentioned the interest on our large cash balance, but don't forget we also have swapped some bond liabilities. And so the gross amount of €24 billion is not what you should look at. You have to deduct the liabilities, we carry the financial liabilities and then also in the €24 billion, there is, I think €6 billion, €7 billion of bond portfolio is relatively short, tenure of 3 years to 5 years, which is also not one-to-one reacting, but there is a benefit there. But the most important benefit is actually on the pension liability, where you have a very long-duration portfolio. And this is why over the last couple of years, you have seen that pension deficits going down to now €2.9 billion from formally €10 billion. We are now starting at higher interest rates to start hedging, and we have already made good progress in our financial statements. You can look at the sensitivities of our pension deficit to interest rates, and you will see it has already reduced. We are continuing that de-risking, and that's actually the biggest lever we have on the interest rate side in the treasury.

Milene Kerner

Thank you.

Operator

Your next question comes from David Perry from JPMorgan. Sir, please go ahead.

David Perry

Hi guys. Good morning. Guillaume and Dominik, good luck in your new challenge. I m sure it won't be as exciting as the aerospace [ph]. Two questions for you, please, Guillaume. You have given us delivery guidance 720 planes for 2023, but that leaves a much bigger step up now to the kind of numbers you were aiming for in '24 and '25 back at the CMD. So, I just wondered if you could talk a little bit about how you see the journey and what gives you confidence of accelerating production over the next few years? And I guess related to that, the second part is there is a line in the press release, we talked about the longer term transformation of the company, but you haven't really elaborated on it in your speech. So, maybe you could talk about some of the plans you have, I think the two are linked probably. Thank you.

Guillaume Faury

Thank you, David. And I really like your comments on Dominik's future challenges, I agree with you that there is nothing comparable to aerospace. Yes, when it comes to the more sales point you make on the acceleration of the ramp up moving forward. Well, actually, we have a target for 2023, which is 720 planes. That's the objective we had for last year. So basically, we have lost a year on moving out of COVID-19 and reaccelerating. But when it comes to the mid-term target, reaching rate 65, and reaching rate 75, we have pushed them out also by a year because beginning of last year, we said we wanted to reach rate 65 by end of 2023. Now, we say end of 2024. Basically, we have more reasons to believe that this is going to play out appropriately as we know where we are in the manufacturing of the new production systems of the new funds. We have made progress on those funds. We have done the same job with our suppliers and supply chain. So, we have a much better understanding of what's going to happen in 2023, but also in 2024 and 2025. And therefore, this acceleration of the ramp-up in '24 compared to '23 is substantiated by a lot of activities we have completed with our suppliers. And we see also at their end, the effect of the investment they are making, the recruitment, the CapEx, they are spending on preparing for that ramp up. That's also something we have done with our widebody suppliers referring to the question that was raised before. The long-term transformation, well, that's basically what we have done or what we have initiated last year with the reorganization of our production system. That's probably something we are not discussing too much around those calls, but it's a major for Airbus to have decided that aerostructures we make, that we deploy our digital solutions across the board, including in what we call now our Airbus Atlantic, Airbus Aerostructures and AI on detailed parts. And that's the work we are doing on the ecosystem for the digital and decarbonization transformation. That's also what we are doing on all sustainable addition fuel activities. You see that we have been approved by SBTi on our scope 1, scope 2 and scope 3 objectives. And that's something where we are working very closely with a lot of external stakeholders to succeed in this decarbonization of the planes, but also the operations, including the use of those new fuels. So, that may be something we could address at a later stage, and our team is very much available to do this. We are driving a transformation plan that is relying on four pillars, which are mainly people, products, production systems and what we call the ecosystem, meaning all those players around us that have a big impact or will have a big impact on the speed at which we will decarbonize addition, and that's some, I mean high-level factors of what I mean by driving the more mid-term and long-term transformation of our company.

David Perry

Okay. It's helpful. Thank you and good luck.

Operator

Your next question comes from Harry Breach from Stifel. Sir, please go ahead.

Harry Breach

Yes. Thank you for taking my question and good morning Guillaume, Dominik and Helene. Just my two questions, and please forgive me if I missed something earlier. Maybe Guillaume, in terms of sales campaign activity, the order intake last year was clearly very good, clearly, a significant upturn. In terms of the level of activity, how do you see it at the moment in terms of the level of interest and demand out there in the market? And then maybe one, maybe a little bit more for Dominik. Dominik, with defense and space, it's become a little bit of a difficult business for us to try to forecast from the outside of Airbus probably from the inside to last year with the impact of the situation with Russia, the Pleiades charges, the cost inflation, the Ariane 6 delays. When Dominik, when can we think about the science in space getting back to the old margins of around 8%, 8.5%. Can we get maybe halfway back by this year? Should we think about that, or can you give us some help to think about that? Thank you.

Guillaume Faury

Okay. Thank you for your questions. I will indeed let Dominik answer the interesting second one. I will take the first one and the first one, the answer is quite easy. The market is very dynamic. We have a lot of demand for our products, a lot of ongoing campaigns, not only for widebodies and freighter, but as well for the single-aisle products. So, you will see a lot happening this year again. That just highlights the need to further accelerate on our ramp up. That's why we are putting so much time and energy on the supply chain, on our own investments at Airbus because the need for the demand for the product is really not getting weaker moving forward. And we have started the year with this Tata India and success both on widebodies and single aisle. And I anticipate that we will continue to see 2023 playing out on the same note. Dominik on the margins of defense and space?

Dominik Asam

I mean as you have mentioned yourself, 2022 was a little bit of a halo [ph] for defense and space with a lot of exogenous shocks that were really non-recurring in nature, and they had to digest. So, I would say, of course, the kind of €3.4 billion return on sales in 2022 needs to be de-polluted to funded. And that means there should be, let's say, some upside. We had a 6.8% in 2021. I don't think we will recover that entirely, but there will be a good move back we anticipate in 2023. Now, with regards to the 8% aspiration, I have to say, that is a kind of more long-term grinding target. So, it's moving out towards the outer years of the forecast horizon of 5 years and the slope at which you can do that is really structural improvement grinding similar to the slope you might see on Helico, where you see also we have some margin every year. So, don't expect any miracles. I think there is a good snapback opportunity in '23 because of the non-recurring nature of the '22, not all of which was an adjustment, as you might have seen. But – and then there will be more heavy lifting to be done over several years.

Guillaume Faury

Maybe if I may complement Dominik, I think a lot of that situation comes from the way historical contracts were structured and we are working hard on the new contracts to prepare a different picture for the future. This will take time to be visible in our numbers because those contracts are very long-term contracts. But when I think of the FCAS or the Eurodrone, they are structured in a very different way to avoid the situation we have today, where headwinds have a very direct and brutal impact on our numbers.

Harry Breach

Thank you both and best of luck to Dominik.

Dominik Asam

Thanks.

Operator

Your next question comes from Christophe Menard from Deutsche Bank. Sir, please go ahead.

Christophe Menard

Yes. Good morning. Thank you for taking my questions and also good luck to Dominik and you new role. The two questions, the first one is on the free cash flow bridge, again, 2023, should we expect some PDP down payments to have shifted to 2024, because you are in effect, lowering the number of probably expected deliveries you had in mind initially. And also, still on this, is any type of settlement cash payment included in that bridge for 2023, or was it already in 2022? And the second question is more on the transformation of the company. You mentioned a few elements. I was wondering whether you have thought also or you are considering quite obviously a more regional supply chain going forward because it's something that we have seen in other sectors like the automotive or cap goods and probably a way to address was, I mean the issues that you had in supply chain in our – that was last year.

Dominik Asam

Okay. May I start on the free cash flow. So, first, I think there are two different buckets in this discussion with more operational discussion about the phasing of PDPs versus the rent. Of course, as you have already seen in 2021, when we shift orders or deliveries to the rise is an impact on PDP, the famous €3.3 billion net PDP flow in contract assets and liabilities in 2022 will not repeat, but will go down. But we are not giving PDPs back. I think you imply that we might repay PDPs. It's really a phasing question about future PDPs payable. You mentioned one legal case here. I don't want to comment on any specific numbers because we have agreed confidentiality on that. It is actually – the one thing I can say, it's to be paid in '23, but I am focusing more on the overall kind of bucket of non-recurring items. You know there are other headwinds, temporary headwinds in free cash flow. We have mentioned before, there is still the A400M to a certain degree. There is still some long end stuff from business partners. And that's also a reason why in 2023, we have a certain headwind, but it's not the major item. The major item is really from the working capital phasing of payments and receipts.

Guillaume Faury

On your question on the transformation, I think we had the opportunity already in previous calls last year and many interactions to explain what we are doing in terms of resilience of our activities, and basically de-risking the supply chain in the sense of multiple sources of supply, reducing the number of what we call single points of failure, and that leads to a more regionalization of the supply chain. So, we do more local for local and less global buy and logistics. That's something that goes progressively and we don't do it as a policy, but more on a case-by-case analysis of the exposure. So, that leads to more regionalization Indeed, that's the consequence. That's not the aim per se. And we don't put it as part of the transformation on what we call the transformation of the company that's more the way we run the business and the way we constantly adapt to the reality of the world. But basically, yes, we do it, and that's also something we can explain more in detail. And you are right in saying that, that's something we see in industries, and that's something we see also in many companies, large companies operating in aerospace.

Christophe Menard

Thank you very much. That's very clear. Thank you.

Operator

Your next question is from Ian Douglas-Pennant from UBS. Sir, please go ahead.

Ian Douglas-Pennant

Thanks for taking my question at the end. I just want to think about margins for a little bit, please, and specifically margins beyond 2023. Can you – I mean firstly, can you give us any directional commentary here or just anything vague. But more in detail, could you give us a sensitivity to inflation here? If inflation comes in at 2% or 5% or 8%, can you give us some indication of the timing impact of how that might impact your margins? And then secondly, on the widebody production increases, can you help us think about the marginal profitability of those programs as they go forward? My understanding is they are roughly breakeven today. I mean maybe you could correct me on that and just give a commentary on how a 50% increase in A350 production volumes impacts profitability of that line? Thank you.

Dominik Asam

So on inflation, I mentioned that on our current assumptions for '23, we see a couple of hundred million net impact. And that's a kind of year-on-year deterioration. If you assumed a similar environment going forward, every year would pick up that order of magnitude that may be compounding. I mean if you compound stuff it's tending to grow exponentially. But it all depends on the inflation itself in the market. And as you see in the capital markets for inflation-linked products, there is actually in anticipation of mean reversion back to levels of 2.5%. If we were on such a trajectory, inflation would not be a topic for us to be blunt. So, I hope that this is where we are going. And I cannot give you any more details, but because, again, these inflation caps are super sensitive topics in commercial debates with customers. In terms of production increases, feeding through to margin, yes, I can confirm that we actually brought both widebody programs to a breakeven situation, which was a great success and really heavy lifting, but there is more upside coming. And we can see of course, a certain upside as we ramp production. And the other thing I always remind people to do is we have quite some volatility in deliveries overall and clearly on the A220, there is not much impact on margin because they are still kind of a zero contribution margin more or less. But on the other programs, when you look at the way the deliveries change and then you look at the kind of EBIT and depollute for non-recurring ForEx. And if you then take averages, you get some feeling of where these contribution margins lie. But I don't want to go into details there, either because it's also a very sensitive commercial topic with our customers and competitively.

Ian Douglas-Pennant

Thank you.

Helene Le Gorgeu

This closes our conference call for today. If you have any further questions, please send an e-mail to Philippe Gossard or myself, and we will get back to you as soon as possible. Thank you and we are looking forward to seeing you or speaking to you again very soon.

Guillaume Faury

Thank you, everyone. Have a good day.

Operator

Ladies and gentlemen, the conference is now concluded and you may now disconnect your telephones. Thank you for joining and have a pleasant day. Goodbye.