

# **DEUTZ Aktiengesellschaft (DEUZF) Q4 2023 Earnings Call Transcript**

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**Body**

DEUTZ Aktiengesellschaft (DEUZF)

Q4 2023 Results Conference Call

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Company Participants

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Timo Krutoff - CFO

Conference Call Participants

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Stefan Augustin - Warburg Research

Jorge Gonzalez Sadornil - Hauck & Aufhäuser

Roland Konen - Value-Holdings

Presentation

Operator

Ladies and gentlemen, thank you for standing by. Welcome and thank you for joining the DEUTZ AG conference call on its full year 2023 results. [Operator Instructions] I would now like to turn the conference over to Christian Ludwig, Senior Vice President, Corporate Communication and Investor Relations. Please go ahead, sir.

Christian Ludwig

Thank you very much, operator. To all, a very warm welcome from my side to our fiscal year 2023 earnings call. Please note that this call is being recorded and a replay will be available on our website at deutz.com later today. Your participation in the call implies your consent with this.

Joining me today are our CEO, Sebastian Schulte; as well as our CFO, Timo Krutoff; and our Head of Finance, Oliver Nord. Also on board today is my successor, Mark Schneider as this is going to be our last earnings call for DEUTZ. As usual, Sebastian will walk you through the highlights of the performance of the group, and then head over to Timo who will provide some more details on our financial figures. Sebastian will close the presentation with our current market outlook and our guidance.

After this introduction, we will be happy to answer your questions. Please note that management comments during this call will include forward-looking statements, which involve risks and uncertainties. For a discussion of risk factors, I encourage you to review the disclaimer contained in our annual report and this presentation. All documents relating to our full-year 2023 reporting are also available on our website. And without much further ado, I'll hand over to Sebastian.

Sebastian Schulte

Thank you very much, Christian, and also from my side, welcome to our 2023 full-year earnings call. And well, as the picture here -- the initial picture shows obviously 2024 is for DEUTZ an most important year as we're celebrating our 160 year anniversary. But today we want to focus obviously looking back on the numbers and the results we achieved in 2023 because '23 was again a year of a very profitable growth for DEUTZ. Let me walk you through some of the highlights before going into details. So in terms of growth, we grew or we grew on many, many fronts. And the growth in numbers of engines sold was 3%. So in our Classic segment, we sold eventually 186,718 engines.

What we particularly are pleased with is that we managed to further grow our service business, our very profitable service business by 7.6% to an end year figure of €484 million. So that's a really, really solid development of this important business segment for us. And the group revenue grew again by almost 8% to a level of €2.1 billion. We'll hear later particularly when Timo is running you through the numbers that these €2.1 billion includes also the discontinued operations Torqeedo but we'll show later on the numbers also for continued operations in more detail.

But one thing is growing top line, the other thing much more important is growing bottom line as well. And on the group level, so including discontinued operations, we have -- we achieved an EBIT margin of 5.7% which translates into €120 million EBIT, which is an increase of 35% over the already successful numbers of 2024 -- 2022.And if we look at our continued operations business, so excluding Torqeedo, we achieved a level of 7% EBIT margin translating into €144 million E-B-I-T.

And let's bear in mind that a couple of years ago, we introduced our 2025 mid-term targets where we said in terms of profitability, we would expect by 2025 an EBIT margin level between 6% and 7%. So in terms of continued operations, we are already there in 2023, which is a great success at this for the time being. Classic business, our profitable sort of bread and butter business, we achieved an EBIT margin of 8.8% in the year 2023. Also very important, if we're looking back on the last years, '21, '22, and now also '23, we delivered what we promised.

So we're very proud of that that we build up credibility towards the capital market as well. So in '21, the guidance we gave in terms of unit sales, revenue, EBIT margin, and free cash flow, we gave a guidance we delivered.

In '22, we gave a guidance, we delivered. And in '23, the latest guidance we gave was in unit sales, a range of 185,000 to 190,000. We achieved 186,718 engines. We promised a revenue level of roughly €2.1 billion. We delivered €2.1 billion. We promised an EBIT margin range between 5.3% and 5.8%.

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We delivered at the upper end, 5.7% And bear in mind, continued operations, we delivered 7.0%. And last but certainly not least, free cash flow, we promised a mid double-digit million amount, we delivered €56 million free cash flow before M&A. So we know and we have always been convinced that DEUTZ as a company has a lot of potential and now we are able to show that we are able to use it, to utilize it and to unleash it. Looking now on the development of order intake. That has been to be frank in Q2 and Q3 a little bit of a point of concern because order intake has decreased, book to bill went down in particular in Q3 and also still in Q4. But we see a positive trend moving now into Q1.

Order intake goes up again. And now we've explained that several times and most of it -- in actually all of our capital market communication, we had some let's say special effects, special developments in the last years. You may remember when the market demand was so strong, particularly for our business sub-4 liter, we introduced the so-called fixed-volume program where our customers were able to reserve limited capacity against paying a premium.

And that let -- and that program was actually taken very, very strongly from our major customers in that range. And obviously, that led to a bit of a early booking effect at the beginning of this program. And now this has been normalized or normalizing over the last months.

And also in '22 and first half of '23, we still saw a lot of instability in the supply chain. The supply chain is now despite ongoing crisis at the Suez Canal is getting much, much more stable. So obviously we have not here -- we don't have the situation anymore, that customers ordered significantly more than they actually need and use. So orders on hand are now in the level of 3 months to 4 months. We had -- we were much higher before, 6 months to 8 months but 3 months to 4 months is a level which we also saw prior to the various crisis of the last 3 years. So that's again showing a level of normalization.

And what's a very important observation wouldn't surprise most of us, the U.S. remains the most dynamic region also going forward and I will elaborate on that later when I talk about the outlook '24. And it's very important that we as DEUTZ are growing strongly in the U.S. that we decided actively to put a lot of our focus on the U.S. rather than other geographic regions which are not developing that well. And last but not least, we see now positive trend in new orders for the first quarter. Let me now give a bit of a recap when it comes to our strategy, the DEUTZ Dual strategy.

We introduced that January '23. And I'll just walk you through briefly. Most of you know us pretty well. So I'll keep it short. We introduced the pillars, DEUTZ classic, DEUTZ green, and DEUTZ service with all with a very relevant significance for us.

DEUTZ classic, it's really important that we're growing that business, that we're making it performing stronger, performing higher and we achieve growth also by market consolidation. So here, the focus is both profitability and growth. When I move on to DEUTZ's green, here, the focus is very clear, to build the green ecosystems with products and technologies which may focus on the drivetrain but will may also go into ecosystems around the drivetrain. So here we're talking about investments, growth, and in particular, long term profitability. Here, we're building the long term future of the company.

And last but certainly not least, our DEUTZ service business where we are already strong, we're already highly profitable, but because we are that strong and because we are that profitable, we decided actively to further and stronger push the growth with a particular focus on the U.S. and Europe. So here, it's about really increasing the absolute profitability via growth organic as well as inorganic.

If we look at -- one thing is developing a strategy, finding it, bringing it on some nice PowerPoint charts. The other thing is really the consistent implementation, the consistent execution of the strategy. And here, on all aspects, classic, green, and service. And what we show when looking back at the results '23, how our strategy execution begins to pay off very nicely.

So we started with an adjusted EBIT in '22 at the level of €89 million which in the grand scheme of DEUTZ performances over the last decade was already a very, very good year, a very good starting point. It was in fact, one of the top results of the company's history. So now if we walk through what was achieved last year and Timo will go through that in more detail later in the financial part, but we grew the classic business, we grew the classic E-B-I-T by margin as well as growth.

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We grew the service business by margin as well as growth, through the acquisitions as well. In terms of EBIT, we had an adverse effect of green because we did spend more on R&D, particularly in the area of hydrogen. And by the way, we do not capitalize our green R&D. We put it all in the P&L to be fully transparent on what we do here, but that's our investment in the long term viability of the company.

And we've signed an agreement to sell our loss making Torqeedo business. And when we bridge it here from adjusted EBIT '22 to adjusted EBIT continued operations '23, we already take this result out in that bridge. So coming up and summing all that up together says in terms of continuous operations, we were able to improve EBIT by more than 60% to €144 million which equals a margin of 7%. But even without that Torqeedo effect, we would have achieved €120 million adjusted EBIT '23 which even without that effect, that would have been the most successful EBIT of DEUTZ in recent history.

Let me start now with walking through the individual segments. Let me start with our highlights in the classic segment.

So in classic, we're focusing on both partnerships and also focusing on improving performance. And in both aspects, we made progress, significant progress. When I talk about strategic partnership, we did clearly initiate an active role in market consultation. And it's not just a statement, it's actually showing that we're showing actions here. We want to establish DEUTZ as one of the top 3 independent engine producers by 2030.

And we did initiate the first partnerships, one with Daimler Truck for their heavy duty and medium duty engines for the off-highway use with the DEUTZ. And that's a bit of a longer shot implementation. And thus, top and bottom line is only going to start by the end of the decade around '28. But as a second step with a much more immediate effect, we agreed in principle with Rolls-Royce Power Systems that we are already taking over the sales activity for these Daimler engines heavy duty and medium duty for the off-highway sector much earlier. At the moment, we're looking here at the beginning of the second half of '24. So here, we are on good track in making this happen. So that's the second great puzzle piece of our market consolidation.

But also, in our organic business, performance improvements have taken place and begin to pay off. We have continued throughout '23 our very successful pricing campaign of '22. Really fixed a lot of accounts, which used to be problematic, to say the least. So here we are. We made it.

We made sure that we healed the revenue quality significantly. Also in production, we enhanced efficiency significantly. We introduced more automation in particular in the main production site here in Cologne. And we also shown that we are able to flexibly manage capacity. We established a third shift, a night shift here on our Cologne site on the production line, which runs for the sub-4 liter engines in summer '23, when the demand was so incredibly strong that we had no other choice than doing that.

And we managed also to reduce it swiftly in February '24 by the way, all with temp labor, so that made it actually very, very flexible to react here.

So that's been a successful way of managing capacity. And in '23, before the tide turned a little bit when it comes to the power battle between customers and suppliers, obviously our suppliers also tried to face us with partially significant price increase requests. We were very good in fighting back on a broad front. And now in '24, we'll actively target our suppliers to reduce material costs because again, the tide has turned and that's one of the important aspects of cost control for 2024.If I move on to service and looking back to like the last 10 years in a way, we show already that we have grown the service business significantly with a CAGR of give or take 7%. But since 2020-2021, we really increased speed here. We grew from 2020, €348 million to €421 million to €450 million, and now to €484 million.

And we are well on track supported by specific measures to achieve our mid-term target of €600 million service revenue in 2025.How are we doing that? On the one hand, we are further developing our existing business. That's going to be a key driver. We're expanding our service center network, particularly in the U.S. That's also part of the very successful growth in the United States that DEUTZ has achieved in the last 3 years.

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And we're using particularly there also innovative approaches such as the Technician in a Van, so to bring the business closer to the customer, and not force the customer to travel to DEUTZ. And there's still so much potential out there in the market, which we're actively approaching right now. But we also work here with inorganic, with M&A in the -- '23 was the first year where we saw in the full year contribution of our previous acquisitions in Ireland, South Coast Diesels, and in the Benelux countries, and AUSMA. And as you know, last year, we closed 2 more acquisitions in Scandinavia DEUTZ Nordic. It used to be Diesel Motor Nordic. Now renamed as DEUTZ Nordic.

And in South America particular Peru and Chile, the long term DEUTZ dealer Hochschild. We didn't don't see the full year numbers yet in our figures because the closings happen in the second half of the year. But they give us a solid basis for further growth in '24. Let me move on to green. And before going on the growth area of DEUTZ green, let me spend a few words on the sale and the divestiture of Torqeedo. So we sold Torqeedo or we are in the process, in the final steps.

I will tell a bit more in a minute of Torqeedo to Yamaha Motors. And we truly found your best owner for the company. It's a very professional experienced company and we believe Torqeedo is in best hands with Yamaha Motors. And we're very, very happy to have found this agreement.

And the sale of Torqeedo has really been or is a very important step in our ongoing process of repositioning and focusing our green segment because we want to ensure that the resources we have, the resources we are willing to spend for the green transformation, and that I will -- we will see that later is a substantial part of our resources but we need to ensure that we really focus them in the markets we are currently working in and the customers we're currently serving.

So that we really focus here on areas where we have a right to play and most importantly, a right to win. Let me give you some key aspects of the transaction.

So Torqeedo in '23 lost approximately €23 million. So EBIT was more or less give or take minus €23 million. So we signed the transaction with Yamaha Motors in January '24. And we expect the closing to occur shortly after Easter. So the vast majority of preconditions have been met.

There's just one merger control clearance still missing, but that's rather a formality. So sometimes it takes a bit time but we're very optimistic that we're going to get this done shortly. We do expect as of closing or with closing a cash in to DEUTZ in a high double digit million range. And we also do expect a book gain out of that transaction in the low double digit million range. So but let me conclude on Torqeedo. The divestiture of Torqeedo, the sale is really an important step in refocusing our green segment. And it also shows, it also proves that it will significantly improve profitability for the company.

But there are also other highlights than green than just optimizing the portfolio. We have put a lot of money and efforts and dedication in the last years into research and development in our green projects, in our green technologies, both hydrogen based as well as battery electric based. And we can't talk about all of those projects because many of them are actually under confidentiality clauses with our customers. But let me just guide you through 2 projects in particular. The one, and we are particularly fond of that is the first serial order for hydrogen engines as part of power generation, decentral power generation. We received in October '23 the first major order for 100 hydrogen engines -- hydrogen gensets to be more precise from China.

And we started now the serial production of this DEUTZ TCG-7.8 H2 engine here in our facility in Cologne. We've been one of the first to develop a hydrogen combustion engine, and we certainly are one of the first, if not the first, who is able to produce such a product on their serial production line, which obviously helps us incredibly fast gaining here scale effects and getting actually this product into the market also at competitive prices. First engines are already being shipped. So here, we're well on track. Another example -- another project example I'd like to share with you is the example with Karcher. As I said, there are many other projects ongoing, but this is something we are able to talk about.

And with Karcher, we agreed to deliver in the first step, GEN2 batteries, GEN2 E-DEUTZ batteries for sweeper vehicles, 39 kilowatt hours capacity. We're starting this year with 3 prototypes, but we do see the potential for more than 200 units and not only focusing on the battery but potentially going further, including also the drive. And it's important, green transformation takes time and also money to an extent. So we continue a high level of future investment. We continue to allocate a significant part of R&D into green, particularly into hydrogen. So to give you some numbers in '23, we spent a bit more than €100 million in R&D and out of which I think is 36% on the green business.

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So that is a clear sign that we'll take the green transformation seriously but we want to do it more focused and less using a scattergun approach than in the past. So that's why the sale of Torqeedo has been one of the fundamental bases to get that done properly now. And as I said earlier, R&D costs for green are expensed rather than capitalized. So the numbers you see, the EBIT you see with DEUTZ, they tell you the truth, and it's not hidden somewhere in capitalized balance sheet positions, which may be of questionable nature.

But before handing over to Timo to walk you in more detail through the numbers, I would like to give a first outlook on what is important for DEUTZ, for the DEUTZ's management team for the strategy implementation for '24. Because one thing is clear, we will continue to execute our strategy with a required tenacity to be successful also in '24 and beyond. On the classic side, that is obviously the integration of the Rolls-Royce Power Systems business. We do expect this to boost our earnings from mid-'24 onwards.

We want to continue to implement and further implement the performance focus in the organization. I mentioned some of the aspects earlier, material cost reduction, capacity optimization through more flexible shift operation also in other assembly lines than the one for sub-4 liter. So in a volatile environment, being flexible pays off immediately. And more mid- to long term, we want to continue play an active role in the market consolidation. We do screen. We continuously screen acquisition targets to be able and to be able to be ready when there is the opportunity there, and then we will inform whenever this is the case.

And very importantly as well, for our products larger than 4 liters, we need to win more new customers, and our sales team has really done a fantastic job in repositioning themselves, getting very, very many new qualified people aboard. So sales is really the biggest change we've seen with the DEUTZ before 2022.On DEUTZ green, important implementing the China hydrogen genset order, expanding other orders and customer projects, both in the field of hydrogen as well as battery electric products.

Obviously, closing the sale of Torqeedo, the M&A and really then focusing stronger with a new organization on green. Last but certainly not least, we will continue our growth path in service organically as well as inorganically, further M&As are in preparation. We'll work here, let's say, a little bit not in the shadow that is sounding too negative, but we don't want to publicize big things before they're ready. So we're working here very well on service, M&A.

And we also want to expand into new business models like telemetrics, which opens up another revenue and thus profit pool for DEUTZ.Having said that, I will now hand over to Timo to give you more than a glimpse of financial year '23 numbers.

Timo Krutoff

Yes. Thank you, Sebastian. And good morning to everyone. I'm very happy to now be able to give you some more details on this, again, a very successful year in our financial numbers. Let me start with one special topic from a financial perspective. I would like to clarify this right at the beginning.

We've heard Sebastian talk a little bit about it already. But for the financial numbers, it's really important that you understand the difference here between our continued operations numbers and discontinued operations numbers. So if we talk about continued operations, we talk about the DEUTZ business without Torqeedo the way it is supposed to be in the future. So to give you an idea of what that means, we start out here with a comparison of both main numbers. If we look at unit sales, for example, yes, there is a significant change if we take out the Torqeedo numbers because we roughly sold 36,000 engines for Torqeedo. But if we then look at the revenues, we see that revenue decline is only 1.9%.

So not a very, very big difference here from a revenue perspective. The biggest and by far, most important part is then if we look at the EBIT. The EBIT for the -- including the discontinued operations was €120 million already. That is already a very, very successful number again for us. But if we then take out the losses from Torqeedo, we end up at €143.6 million. That leads us to an EBIT margin of 7.0%.

And many of you might remember that we had a guidance out for 2025, where we said we are going to aim for a margin between 6% and 7% by 2025. Well, if we are now looking at the new setup of DEUTZ, we already achieved this number in the last fiscal year. So from now on, I would mainly focus on the new setup, just the continued operations, and give you now a comparison between 2022 and 2023. So yes, order intake went down a little bit compared to the very high numbers of the year before and without especially the special topics we had because of the disruption in the supply chain. But in general, 11.7% lower from today's perspective is not a bad number. Looking at the unit sales. And then on the other side, yes, we did increase sales by 3.2%, selling 187,000 DEUTZ engines.

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And then if we look at the revenue side, and this shows very well again how good we did on our pricing initiative. Revenue grew by 9%. So unit sales, 3.2%, revenue, 9% is a clear indicator of what we do on the pricing side, especially since we did so a little bit more on the sub-4-meter engine segment, which in general is a little cheaper. So that was a very good level. If we look at orders on hand, we are now at a normal level of €450 million. Again, this is roughly what we had before the after-corona special effect.

So a very typical number for DEUTZ with 190,000 unit sales, €400 million, I think is a healthy amount for us. Now I would like to focus a little bit on the service segment because it is really a very, very important segment for us, not only from a margin perspective, where it is very healthy but also from a volatility perspective because we know that the service business, it doesn't really matter what's happening elsewhere is a very, very stable business, especially in times where the engine sales might be a little more difficult.

This really gives us some significant leverage on the revenue and especially on our EBIT side. So we were able to grow this business again, which, of course, is our clear strategy to get to €600 million by 2025. So last year, we increased it from roughly €450 million to €484 million, so an increase of 7.6%. And also the order intake in this segment is higher than the year before. So this is in line with the revenue with 480%. As Sebastian already said before, the two acquisitions we did last year were in the second half of the year, so we didn't really make a big difference on the sales side, but they will be fully included, of course, then in 2024 and also how it should help us with the growth and reaching our target of €600 million.

Some details on the revenue break down, first by region and then by application segment. So the first big thing for us on the regional thing is that we did grow in all regions. You always see here the different regions and the percentage of sales of DEUTZ below that and the sales volume in absolute numbers and then the growth compared to the year before. So we can see that Europe and Germany, yes, we're growing nicely but not with huge amounts, Europe with 3.9%. Germany with 5.3%. And then if we look to the bottom left side, we see the Americas, which grew by 16.4%.

So a clear push from this region. And now the Americas is exactly 1/4 of our sales volume, which from a diversification perspective also helps us. Asia Pacific is almost flat on, again, a very low level. We don't see any downside there anymore, but hopefully some upside potential for the future when this market is going to pick up. Looking now at the applications. On the right side, our -- the two ones where DEUTZ is often known for the construction equipment segment was flat similar to the agricultural machinery segment, which was a little bit declining.

But in general, these two, again, didn't change much. On the other hand, we saw the two very important segments which are service, again, 7.6% increase, but also material handling where we saw a 31.7% increase and is now with almost 1/4 of our business, helping us also on the growth path. EBIT in general was, yes, €143 million, very, very, very successful. We're very happy with this number, but also if we look at the development over the year. In general, we saw that we had a very stable EBIT. If we look at absolute numbers around €36 million every quarter.

So not much deviation here stability on the EBIT side, if it goes in the right direction that we like, of course. But we can also see the improvement compared to the year before. The last quarter always is a weak quarter because December and the Christmas holiday always leads to lower sales and usually also to lower EBIT. But here, if we compare the last quarter of 2024 to the last quarter of 2023, we see an increase in the margin of 1 percentage point. And this is also very nice to see if we look at the absolute numbers. The Q4 of last year was even the strongest quarter of the whole year, which, of course, carries then into the beginning of this year and it gives us some very nice starting position.

The improvement in general on the EBIT side, yes, came first from the service business. I've already mentioned that, but also, of course, from the pricing initiative. And this is very important now in times that we're not just looking on the pricing side or can't look as much anymore, but from the cost measurements where we go do a very strict cost management here at DEUTZ. There is one thing, if we look at the EBIT margin, we are talking about the EBIT before, exceptional items. We do have extraordinary items in the last year of €20 million as a negative effect. That was mainly an impairment on some of the older R&D projects that were capitalized.

This also, of course, is never very nice for the single year, but for the future, it does also help us because there's no depreciation anymore. And in general, we have now reached a very low amount of capitalized R&D costs which is good for the future. Consolidated net income, therefore, because of the special item is €82 million, a little higher than the year before, and the earnings per share at €0.66 also stable. R&D spending. Yes, we are still investing very heavily in our future. That is great.

We see that. If we look at the left side, 4.7% of sales is 0.2 percentage points higher than the year before and also in absolute numbers, roughly €30 million more than the year before. And Sebastian already mentioned that almost all of that goes into the bottom line directly, so no burden for the future here. Capital expenditure was a little special. If we look at the IP and license fees we acquired from Daimler last year. But on top of that, you see that in the dark red part, we are also investing here, especially in improvements in our production.

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And on the working capital side, not much change, a little bit on the inventory side on the receivables, a little less factoring. So just operational issues in line with our sales volume. Cash flow, of course, the very positive thing on the very left side here is the operational cash flow, which increased by over €81 million. That did give us a strong push, and we then -- that also leads to a much better free cash flow before M&A. Here is the one exception to the other numbers we show also here on the left side, the numbers, including Torqeedo, which then ended up in €56 million positive free cash flow. If we then also take out Torqeedo, here you can see that Torqeedo is not only EBIT negative but also cash negative.

Then we end up at almost €73 million positive free cash flow. Net debt didn't change much a little bit because of the dividend payment and the M&A projects. But in general, we are very well positioned here. And this, we can also see if we look at equity and equity ratios, we already had a very good stable level in 2022 with 45.3%. We were able to increase that even a little more to 46.7%. Net debt to EBITDA, also on a very good level, very far away from any issues with any covenants or something like that.

So from these numbers, you can see that we are very well positioned for further growth, either on the organic or inorganic side. Dividend per share, we -- our proposal for this year's payment is €0.17 per cent. So again, a €0.02 increase compared to the year before also, I think, something that is a positive information for our shareholders. Quick look because we do have the 2 segments, and there is one -- some change in the green segment, especially here, we are looking at the classic segment. These numbers are very much in line with what I've presented to you already. So I would just like to focus on one last number.

And this is the EBIT margin and absolute EBIT in the classic segment. You see here that we have €180 million EBIT with an 8.8% margin. So this is everything without the green segment. And this, I think, also in the benchmark compared to other companies, we are very good on track. Now the bigger change, if we look at the green segment, of course, if we take out Torqeedo, which was the bulk of the green business, then the numbers, especially on order intake, new orders, and revenue are significantly lower without Torqeedo side. But the important part here is if we look at R&D and on EBIT adjusted, then you see that, yes, we do invest €31.4 million in R&D, and this is mainly in hydrogen, but also, of course, in the electrification.

And then you also see the effect on the EBIT adjusted, which is almost only the R&D costs, which then leads to €37 million negative effect on our EBIT. Okay. That's all from my side for now. And I would hand over to Sebastian to give you an outlook for this financial year.

Sebastian Schulte

Yes. Thank you very much, Timo, for the detailed view on those really fantastic numbers for '23.I'll give you an outlook for '24. If you look at the end markets, we are present in the main end markets, agri, construction, and material handling in the 3 regions, EMEA, Americas, and APAC, we see, overall, let's say, a slightly weaker or stable situation in '24 than '23. And that doesn't come as a surprise, neither to us nor to any other market observance because it's not a surprise that agri development is a little downhill, a little more, let's say, more conservative.

Construction depends on the market, on the country as well as on the segment. So it's -- in Americas, for example, we see it on a very stable level, material handling.

You'd be surprised, initially, I thought we would even see a green arrow here in material handling in Americas but actually, it comes from a very, very high level and the demand in the U.S. in the last 2 years was actually too -- so strong that we weren't even able to fulfill it. So that's why we're saying slightly weaker or stable. But overall, let's say, a mixed picture, but certainly with a positive trend in the recent numbers, which we see already. But one thing is obviously the overall market situation. And the other thing is how we, as DEUTZ look into '24.

And our guidance, which we published today is in unit sales reflects the lower demand that we are now seeing a range of between 160,000 and 180,000 DEUTZ engines are to be achieved in the fiscal year '24. We see revenue on a stable level, €1.9 billion to €2.1 billion. And we see EBIT margin, and that's actually for us, let's say, the most important aspect to mention also, let's say, on a stable level, 5.0% to 6.5% because we do have now a significantly more robust pricing after all the initiatives we've taken and also the cost structure where we've worked a lot over the last years. And now, as I said earlier, we'll put an additional focus, particularly on material cost programs, and we expect this improved cost structure also to offset lower unit sales volumes. And let's not forget one thing. We continue to grow our service business, right?

The service has such a high profitability. And the more service we sell, the more parts we sell, the more robust is here our bottom line performance. And also if you compare it with revenue levels 4, 5 years ago, where we were also at some point in the range of 1.8, 1.9, I mean, back in the days, the share of service in the total business was in the range of 17%, 18%. Now it's 27%, 28%.So already, that shift in mix from new engines to service supports here really the strong development and the higher resilience of our bottom line performance. And as Timo said earlier, we're coming actually from the Q4 with a fairly strong momentum.

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Our Q4 result was great, was the best EBIT in the year and also over many, many years. And what we see at the moment, our Q1 is not over yet, of course, but we see particularly on bottom line that this momentum, we seem to be able to carry into '24 as well. So we are still fairly optimistic looking in this year '24 despite a little more challenging market environment than what we had in '23. But before closing the presentation with the outlook, it is the

presentation focusing on '23. So we do take a lot of pride in looking back. '23 was the year for DEUTZ with a strong performance in a still volatile environment.

We have the new orders going down a bit to €1.8 billion. That's been explained. Unit sales has been up 3% to 186,718 units and revenue up by almost 8%. So here again, we see the development also of pricing in our portfolio, revenue of €2.1 billion. And most important is the bottom line, €120 million plus €31 million of the adjusted EBIT, EBIT margin, 5.7%, and considering the continued operations, which again is the basis for the future, we were at a level of 7% already having achieved the upper end of our mid-term guidance that we announced a few years ago for '25.Free cash flow, we're able not only to be profitable.

We're also keeping more cash in than spending, €56 million. And dividend, €0.17 per share, even slightly below our communicated payout ratio. But it is important for us that we are showing very clearly we want to -- despite the fact that we are in a transformation, we want to ensure that our shareholders receive their fair share also of ongoing payments via dividends, and we want to continue this dividend policy. We want to continue keep or grow the dividend year by year. We've made significant strategic successful moves with selling Torqeedo in the first place. And growing the business via the partnerships with Daimler Truck and Rolls-Royce Power Systems, and that led us to the guidance for '24.

But we take pride in looking back in '23. On the other hand, this is just the beginning. So we're going to be excited to lead and guide this fantastic company through the next years and phases of our transformation. Thank you for your attention. And as usual, we're now available for questions.

Christian Ludwig

Thank you, Sebastian. Thank you, Timo. Operator, please open the line for the Q&A.

Question-and-Answer Session

Operator

[Operator Instructions] And the first question comes from Tore Fangmann from Berenberg.

Tore Fangmann

Two from my side. First would be on general pricing. How you see it into 2024, do you see pushback starting from your customers that also want to take a bit of the share of the lower input costs that you see now? And the second question is, this time, you do not have the slide on the '25 guidance. In general, you mentioned it a little bit.

But how do you feel about the '25 guidance given that you would need from the midpoint of the '24 guidance a further 25% increase in '25 to reach the revenue goal?

Sebastian Schulte

Right. Yes. In terms of pricing, good question. Let me first state, we will not be able to continue increasing prices on the levels we've done in '22 and '23. I think the market dynamics is different.

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We still have a very sort of selected approach in some products with some customers where we may be in a niche or where we have a very unique situation. And there where we are still able to adjust prices a little bit. On the other hand, there are a few customers already requesting reductions. But so far, we were able to keep prices on the stable level. Obviously, we need to always look that it's in sync with also our cost situation. So in the end, if prices do not increase further, it's important that we reduce the costs from our material and component suppliers.

And so far, it's looking good that we'll manage to play that game, to ride that wave in a different shape than we've done it in the last 2 years. But so far, it seems like that we're actually here on good track. Yes, your question on the '25 guidance is a good one because we still -- we believe that the top line is in principle, achievable, obviously, with a couple of M&As coming in. I mean, the one -- and the transaction I mentioned several times, the Rolls-Royce Power Systems business.

When we announced it in December last year, we explained that the top-line revenue is €300 million on an annual basis. So obviously, in this year, we won't see the full year because although it starts materializing in the second half of the year, next year is going to be the full year effect in combination with further growth in M&A -- in service for the M&A and service. We're well set to get to the guidance.

Obviously, it all depends a little bit on what is the top line with new engines. But in principle, if we are in a level of today slightly above maybe then for '24, adding up the Rolls-Royce business, adding up further service growth, actually, we are on good track. So we see no reason to adjust that guidance, neither downwards nor upwards in terms of top line. In terms of bottom line, we need to see how the market develops. So maybe we can come up with the positive surprise later this year.

Operator

And the next question comes from Stefan Augustin from Warburg Research.

Stefan Augustin

Some questions. So the first one is actually on green. When I'm looking at the segment, let's say, in 2022, we had losses in green on a continued basis, roughly on the scope of the R&D expenses. And in '23, this is a little bit higher than the R&D expenses. And if I look in the forward-looking statements of the annual report, you expect roughly losses in green to be stable in '24 versus '23.

So where is this additional investment actually coming from? And when we go into '25 if I extrapolate this amount, this is a bit higher than the initial €100 million you wanted to spend in the segment. So can we expect that, for example, in '25 or so, we see a little bit less investment and this is currently the peak you're looking for when it comes to the green investment, will be my first question. I take the other one later.

Sebastian Schulte

Yes, you're right. I mean, first of all, the green continued operation loss is mainly attributable to the R&D. That's very clear. We do not see a significant reduction in the R&D next year. We see rather refocusing.

And then we're setting up -- as stated, we're setting up our green business in a new way where we'll also get aboard a dedicated leadership position to manage that green business a bit more. I wouldn't say standalone, that's the wrong word, but with a more focus and less integrated into the classic engine business because it just requires different focus, different processes, different speed in particular. And with that team, we are, at the moment, setting up the business case for the green business with specific targets, top line, and bottom line, starting '25, '26, '27. So -- and also including a bit of a refocusing. So we may -- when we look at H2, obviously, is a strong focus. That's for us something where we've got a right to play and right to win.

But for example, with the battery electric technology, we will look into are we continuing to put as much money in the low-voltage products or are we rather focusing on the high-voltage products. So there may be a room for focusing a little bit. But in principle, we will not cut the spendings on our -- on green R&D significantly. We'll just refocus.

Stefan Augustin

And then when it comes to your statements on Q1 versus Q4, can you outline a little bit on which verticals actually the demand is picking up or is it not so much coming from the verticals, but rather, as you explained from pre booking and other normalities. And the second is when you reflect on your indication for the bottom line development, the starting point is I just want to make sure the 6.7% margin you showed on the continued operations on Q4, right? So this is, let's say, actually, the idea that we should -- that we would be in Q1 rather on the upper end of the guidance range when it comes to profitability.

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Sebastian Schulte

Yes. I mean, when we look at Q1, obviously, it's very -- we will not talk much about Q1 because we cannot give you an indication or a glance on that. But we see at the moment, not surprisingly, still a very strong pull from the U.S. in particular. And then in other areas, it's not yet that clear where it comes from because we only have 2 months booked, and it's very difficult, particularly with January.

January is always a special month because some of the customers only just open a factory after first 7 or 10 days. So I would not be willing to be able to or willing to give too many details for top line, for break down of top line numbers. But what we see is at least January, February, and I won't say more than that, the strong momentum and profitability we had in Q4 is certainly seems to push us also into the first quarter at the moment.

Stefan Augustin

And you also indicate that you rather would be rethinking mid-term targets around 2024 in your outlook statement on the -- so when we -- when should we expect that, rather in the second half of this year?

Sebastian Schulte

Sorry. I didn't catch it exactly. So you meant the Rolls-Royce --

Stefan Augustin

In the outlook statement of the annual report, you mentioned that you will reframe the mid-term targets also when it comes to green and that would be due during 2024. So is that rather in the second half or --

Sebastian Schulte

Yes, we would. We are currently planning to organize the Capital Market Day in autumn, probably around September. And that's the point in time when we have good progress, when we will have good progress made on reestablishing here or establishing our green business, including the person who's leading it. And part of the agenda for our Capital Market Day in September is going to be a focus on the business plan for green or the outlook for green. And then we will also see whether we can then specify the '25 targets or even come up with new mid-term targets because '25 is -- by the end of '24, '25 is not mid-term anymore.

Stefan Augustin

And finally, one, if I look at your free cash flow guidance, it feels a bit conservative to me. If I recall that correctly, the Rolls-Royce business has a lower working capital bound to Torqeedo was free cash flow negative in the business. And let's say, all things more or less equal, we could imagine that the free cash flow generation also when you spend a little lower on the overall R&D, if I saw that correctly in the outlook statement. So it's -- is there a missing point here to me that I'm overlooking some CapEx spending or so?

Timo Krutoff

I know there is no -- it's a very good analysis I can say. There's no special topic you're looking at, but we gave an EBIT guidance, which has a fairly wide range. Depending on where we end up in the range, of course, it also has an effect on the free cash flow side. So mid-double digits is also a wider range in general. Let's see how the year progresses, where we end up at the EBIT side, and when we are actually going to book the business from the Rolls-Royce side. But maybe there are some additional changes.

Operator

And the next question comes from Jorge Gonzalez Sadornil from Hauck & Aufhäuser Investment Banking.

Jorge Gonzalez Sadornil

First of all, congratulations, Sebastian and Timo for this strong result. I have a couple of questions. The first one is also regarding the free cash flow. I was wondering if you can clarify how much is spending of the payments for the original Daimler Truck deal. I know that you were planning to pay through 2 or 3 years, but I don't know.

If the pending payments are relevant or not, just to understand the net debt levels at the end of '23. And for '24 following also the question of my colleague, can you please give us some indication in terms of the working capital that you are expecting once Rolls-Royce Power System distribution of Daimler Truck is included? That I think is going to be very helpful. That will be my two first question, please.

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Timo Krutoff

Yes, let me start with the second part of the question. The Rolls-Royce deal that should be roughly a zero game on the net working capital side. So -- but of course, we are not even yet in the signing phase. So it's a competitor. Therefore, we need to be very cautious on what we've seen so far, and not everything is open on the contractual side.

So again, on our business plan, we are very cautious with these numbers, and I can't give you any details on that. On the Daimler Truck side, Daimler Truck is a total spending of €30 million, which is -- we are spending over a 6-year period with roughly very similar numbers every year, so you won't have much changes year-over-year on this one.

Jorge Gonzalez Sadornil

And then my last question is regarding the delay on the emission regulation for heavy-duty vehicles in the European Union. I was wondering how do you see this for your business. Obviously, it's giving more years of life to the diesel platforms, but it will be also interesting from your strategical approach to the new technologies. If this could mean that you could delay some of the investments or that could delay the consolidation of the sector or not. I will be very interested in your view.

Sebastian Schulte

Yes. As always, if you have a moving target, that's at least for planning purposes, less than ideal. On the other hand, back when the emission regulations were updated more frequently, it obviously led for companies like us and competitors to sometimes Shell difficult decisions, how much money to spend for a new engine platform. And this decision -- these decisions, we are currently, let's say, not -- we don't have to take under high time pressure. So if you look at our portfolio, we have a very, let's say, good and well established and well-respected portfolio with our customers in the sub-4 liter range.

We've got our cash cows, the 3.6. We've got a fairly new development, the 2.9 and the brand-new development of 3.9. So for this, at least, we know we have products in our portfolio, which we can easily use in our customers -- with our customers for 2, 3, 4 years longer should the emission guidelines not been updated, yes, earlier than what currently is foreseen.

And on the portfolio of the larger engines, we do have with our sort of brand new 5.2-liter engine, a state-of-the-art product, which is achieving start of production soon. On the other hand, the deal with Daimler Truck and also then subsequently with Rolls-Royce Power System, it gives us pretty much a maximum flexibility, particularly the combination of those partnerships. Because with Daimler Truck, I mean, initially we were focusing on getting them access to the medium-duty and heavy-duty engines in a new emission platform, whether it's going to be from '28 onwards or from '30 or from '32.

But now with the second puzzle piece, the Rolls-Royce Power Systems business, I mean, we get access to the engines as they stand right now. So for us, it really doesn't matter in this field when the switchover is because we will have products for both.

So that's actually quite positive for us, but mainly because of the combination of those 2 transactions. So yes, sure. On the other hand, we are looking at the moment in a dedicated project to the future of our product portfolio, and we will see whether there are other areas where we may or may not develop a new product by the end of the decade, but other than that, we're actually well positioned right now in the power ranges we're offering today.

Jorge Gonzalez Sadornil

So the research and development costs should remain at similar levels now -- than now?

Sebastian Schulte

Yes, I think that's what I would -- if I were you, I would reflect that in my model.

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Jorge Gonzalez Sadornil

And just a last follow-up. On U.S., this is not the case, no? The emission regulations are still expected to arrive before, no, the end of the decade.

Sebastian Schulte

Yes, they are. I mean we expect this to arrive at the end of the decade, but it's never sure. It could also delay a year or two. So at the moment. And that's, by the way, whenever this happens, we would then -- we will try to then bring a product into the market which is then already fit for the U.S. regulations and even potentially a little better than the current regulations in Europe. So we would then be a little bit like the front runner because we don't want to work with too many different products at the same period of time, at least between the U.S. and Europe.

Obviously, with other jurisdictions, it's a bit -- it can be a bit more complex because other countries like China, like India, obviously also follow a different approach. It's not always 100% aligned, but we see with our development paths that we'll look for maximum alignment particularly between Europe and the Americas -- to U.S. I'll be precise.

Sorry, not the Americas.

Jorge Gonzalez Sadornil

And sorry for my colleagues here that are in the line. Just last one that just came in top of my head. Can you give us some feedback on SANY in China? How the year ended and how is -- how the year started for the joint venture?

Sebastian Schulte

With the joint venture with SANY, we concluded the year with roughly 10,000 units.

Jorge Gonzalez Sadornil

And are you expecting any improvement in '24?

Sebastian Schulte

Slight improvement. That's what we hear from them. Let's say, not a major uptake, but a slight improvement. We do expect SANY is obviously also a customer in other areas. So for example, in India, we are selling more engines to SANY India for port material handling to the SANY Marine business.

But in China itself, we should expect a slight increase, but we do not expect that's a major growth at the moment.

Operator

And the next question comes from Roland Konen from Value-Holdings.

Roland Könen

Just for clarification on your guidance, could you elaborate a bit on the inorganic effect of the Rolls-Royce deal? You mentioned roughly €150 million for the half year and also the full year effect on the acquired service businesses. And the second part of the question also on the guidance on Page 26 of your presentation, you talked about the positive EBIT effect of the Torqeedo sale. So the book gain of this deal would be in your EBIT guidance of 5% to 6.5% and the operating loss of the first quarter will be in the discontinued operations. Maybe you could clarify that.

Sebastian Schulte

Yes, sure. So first of all, you're right. You correctly stated the annual effect of the Rolls-Royce Power Systems business is about €300 million. We do not have completely modeled it in, let's say, from the beginning of the second half. So I would roughly use €100 million to €150 million as a range in terms of top line, that will fit pretty well.

And the Torqeedo -- sorry, then another question was on the top line effect on the service acquisitions. And we'll see here for the -- from the 2 acquisitions we did last year -- sorry. From the service business, from the acquisitions we've taken last year in the Nordics as well as in Chile, we do expect here roughly, from the services, it's roughly €20 million, €25 million revenue on the service side because there's also a new engine business on top. And then you asked about the effects of the Torqeedo sales. So the book gain, we would not include in the EBIT guidance because the book gain, we would classify as a special item. So that's going to be adjusted.

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However, the loss of Torqeedo in the first quarter prior to closing will then be shown as discontinued operations. That is correct.

Operator

There are no further questions at this time, and I hand back to Christian Ludwig for closing comments.

Christian Ludwig

Well, thank you very much, operator. Thank you very much for listening to our full year call. If you have any questions left, please contact us at the IR department. And the next point or touchpoint we will have is on the 30th of April when we will report the Q1 figures that will not be with me. That will then be Mark Schneider, my successor.

So for me, also time to say goodbye. Thank you very much for the great discussions we've had and hope to see you around at some point in the future. Goodbye.

Sebastian Schulte

Thank you.

Timo Krutoff

Thank you.

Operator

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

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