

# **Siemens Energy AG (SMEGF) Q3 2024 Earnings Call Transcript**

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**Body**

Siemens Energy AG (SMEGF)

Q3 2024 Earnings Conference Call

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Christian Bruch - President & CEO

Maria Ferraro - CFO

Conference Call Participants

Vivek Midha - Citigroup Inc.

Sebastian Growe - BNP Paribas

Akash Gupta - JPMorgan Chase & Co.

Max Yates - Morgan Stanley

Gael de-Bray - Deutsche Bank

Ajay Patel - Goldman Sachs

Alex Virgo - Bank of America

William Mackie - Kepler Cheuvreux

Ben Uglow - Morgan Stanley

Phil Buller - Berenberg Bank

Andrew Wilson - J.P. Morgan

Malte Schmitter - Petrus Advisers

Sean McLoughlin - HSBC

Presentation

Operator

Once again, a wonderful good morning, ladies and gentlemen. Welcome to the Siemens Energy Q3 Fiscal Year 2024 Analyst Call. As a reminder, this call is being recorded.

Before we begin, I would like to draw your attention to the Safe Harbor statements on Page 2 of Siemens Energy presentation. The conference call may include forward-looking statements. These statements are based on the company's current expectations and certain assumptions and therefore subject to certain risks and uncertainties.

At this time, I would like to turn the conference over to your host today, Mr. Michael Hagmann, Head of Investor Relations. Please go ahead, sir.

Michael Hagmann

Thank you, Franci. Good morning and a warm welcome to our Q3 conference call. As always, all documents were released at 7 o'clock on our website. And here with me are our President and CEO, Christian Bruch, and our Chief Financial Officer, Maria Ferraro. Christian and Maria will take you through the major developments of the last quarter and this is expected to take about 30 minutes. Thereafter, as always, Christian and Maria are available to answer your question. And for the entire call, we've allowed about an hour.

And with that, Christian, over to you.

Christian Bruch

Yeah. Thank you very much, Michael, and good morning everybody also from my side. Thank you very much for joining us for this conference call today. We are on track to meet our guidance and to reach our objectives for the full fiscal year. We saw a healthy order intake, good growth and profitability in line with our expectations, and we are making progress at Siemens Gamesa. The market for electricity remains strong and we continue to see strong growth in pretty much all our businesses and in the different regions of the world.

As we discussed before, we see that the rapid buildout of data centers fuels additional growth in electricity consumption. For us, this means customer interest in generation equipment, grid infrastructure, and what we call electrification solutions. We see a lot of discussions happening at the moment. Orders will then come more and more in the next years.

Order intake was healthy at EUR10.4 billion this quarter, even though it was down year-over-year due to the low order intake at Siemens Gamesa. It represents a book-to-bill of 1.2. Orders for Gas Services and Grid Technologies were just shy of EUR9 billion, which means that they are, after nine months, already roughly at last year's full-year level.

As a consequence, our order backlog passed now EUR120 billion and I am pleased that with the growth, also our backlog margin quality continued to improve. This provides us with an excellent foundation on our future path to improve profitability of the company.

Revenue rose close to 20% in the quarter and 12% during the first nine months. In Q3, we did not only see strong growth at Grid Technologies and transformation of industry, but we also saw strong growth at Siemens Gamesa, driven by offshore. Profit before special items came in at EUR49 million in the quarter and this was in line with our expectations even though the results were hold back by one-time effects from legacy effects.

Maria will shed a little bit more light on it also to -- that you really understand it because that is not related to technology or products, but it's legacy items. This means that after nine months, we are at just over EUR400 million profit before special items, reflecting a margin of just under 2%. So even if you consider that profitability in the fourth quarter tends to be the lowest in the year, we are well on track to reach our guidance.

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The losses at Siemens Gamesa in the quarter were around EUR450 million and roughly at the run rate of the first two quarters, resulting in a loss of EUR1.3 billion for the first nine months. You may also recall that we update the statistical models utilized for the evaluation of the entire wind turbine fleet once a year. It is a comprehensive exercise in which we review failure rates, cost assumptions across the whole fleet and review our potential agreements with customers.

Driven by changes in cost inflation assumptions and variations and failure rates, our assumptions have been updated with the latest information. All changes were well within our expectation in respect to the assumptions for the quality cost of the platforms in 4.X and 5.X. The change to our assumptions was overall not material with the P&L impact below EUR20 million.

Let me also confirm that we are on track for the reintroduction of the 4.X before the end of this fiscal year and the 5.X during fiscal year 2025. Based on the good development during the first nine months, we raised our cash flow guidance from up to EUR1 billion before to a range of EUR1 billion to EUR1.5 billion, and we confirmed the guidance for the full year for all the other group KPIs.

Parallel to our activities to improve the profitability of the company, we are driving measures to satisfy the growing demand for our products, and during the last quarter, we have been announcing further capacity expansions, which will allow us to capitalize on the growth cycle in our industry.

For our Gas Services business, we inaugurated the new gas turbine combustion burner factory in Budapest in May, and like the other examples from this quarter, this is in addition to an existing operation which allows us to make the most efficient use of capital for building up capacity.

And the fast growth in Grid Technologies is supported by further factory capacity expansions. We had already announced a new high-voltage transformer factory in the US and India during quarter two. In July, we now broke ground at our Austrian transformer site in Weiz to increase our capacity, and a day later, we broke ground in Nuremberg in Germany where we're expanding our capacity for DC switches.

These steps include the joint venture -- including the joint venture with Koncar will allow us to industrialize project execution of HVDC projects. We also have commissioned our vacuum interrupter tube production in Berlin, which adds in-house capabilities to provide our customers with SF6-free switchgear. I am proud that after the development efforts, this product now lands successfully in the market. As you know, SF6 has 25,000 times the global warming potential of CO2 and therefore will be gradually phased out in the European Union from 2026 onwards.

Moving on to Siemens Gamesa, you have seen strong revenue growth in offshore over the last quarters, which reflects the ramp-up in our factories. We are progressing to improve productivity, and with that, our output. I still see room for improvement, particularly when it comes to blades, given that we intend to almost double our output from fiscal year 2023 to fiscal year 2026. Here you can see a picture taken in Aalborg where we are ramping up the production of blades for the SG 14236, our most powerful turbine.

Like in every quarter, I would like to give a brief update on some project highlights for this quarter. In Gas Services, which absolutely stands out, our record high order intake was supported by the order in the Kingdom of Saudi Arabia, and Saudi Arabia is currently in the process of really transforming its energy infrastructure, which offers opportunities for us not only in gas, but also in other businesses which we do.

Taiba and North Qassim will be two of the world's most efficient gas-fired power plants with a capacity of 2 gigawatts each. Each plant will be fitted with a total of three HL-class gas turbines, steam turbines and generators, and reduce CO2 output by 60% against the prior solution, and they can be fitted with carbon capture and storage facilities at a later point in time, and in this regard, a very, very successful project launch.

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Siemens Gamesa successfully installed the first 11 megawatt wind turbines at the Borkum Riffgrund project, Germany's largest offshore wind park, with 913 megawatt. The project is a milestone in the industry because it is the first offshore wind project globally without governmental support.

In Grid Technologies, one highlight this quarter was a contract in Denmark. We are grateful for the trust which Energinet is putting into Siemens Energy to support the acceleration of the energy transition in Denmark with a contract award of around EUR1.4 billion. The connection and transport of renewable electricity around the country will require 50 new or reinforced 150 KV high-voltage substations, which will be built or upgraded over the next eight years.

I'm also very pleased to see that we could secure a contract for a 280 megawatt electrolyzer system from our customer EWE in Germany. The plant in the German city of Emden is expected to go into operation in 2027 and will provide up to 26,000 tons of green hydrogen annually for various industrial applications in the regions. Seeing that the green hydrogen takes off much slower than people were expecting, I'm very pleased with what our teams are doing and that they are able in a tighter market to secure lighthouse projects and I'm confident that we will be able to build this business up step after step.

And with this, I would hand over to Maria to walk us through the detailed numbers.

Maria Ferraro

Thank you, Christian. Good morning, everyone, from my side. I'm very pleased to share with you our Q3 financial results. Maybe getting right into it on the next slide, please. Looking at Siemens Energy orders, overall orders came in at EUR10.4 billion. As mentioned by Christian, Gas Services orders more than doubled year-over-year. We did have some decreases in other parts of the business due to a high level of comparison, mainly at Grid Technologies, and of course, Siemens Gamesa, as expected.

If you were to exclude Siemens Gamesa, we would be plus 30% orders year-over-year versus minus 30%. Book-to-bill was healthy at 1.18, driving the order backlog again to new high of EUR120 billion. And I'm also very pleased to say that the margin quality in the backlog continues to improve. More on that in a moment.

Revenue for the group grew by 18.5% on a comparable basis. Grid Technologies and Siemens Gamesa leading the way, including transformation of industries, all generated growth between 20% and 30%, and revenue of Gas Services was also up slightly also due to a high level of comparison. Service grew around 16% comparable and new unit sales grew even greater at 19%.

Profit came in at positive EUR49 million due to the strong growth at Grid Technologies and transformation of industry. Siemens Gamesa was in line with expectations. There were puts and takes in the profit, of course, as per usual. This also includes this time a one-time legacy effect, impacting Gas Services and also a legacy project effect impacting transformation of industry.

Special items amounted to positive EUR69 million, and this is driven by a reversal of a write-down relating to a pending sale of an asset. Of course, this is all part of our overall divestment program. As a result, this brings us to a profit for Siemens Energy for the quarter of EUR119 million and net loss of EUR102 million.

Free cash flow pre-tax improved to positive EUR727 million. This is reflecting higher profitability and strong order momentum, particularly in Gas Services and Grid Technologies who showed very strong cash flow contributions with each just over EUR400 million. The cash flow at Siemens Gamesa was in line with our expectation.

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Moving on to our order backlog, again, a new high of EUR120 billion and I'm very pleased across all businesses, the order backlog quality continues to improve, and of course, this is important as this trend continues to support our midterm targets. 50% of the overall backlog is now service, and what's also important is we're seeing strong growth and solid margin improvements in the backlog of our new units business. Again, new units help us grow the installed base and to build the base for additional service revenue in the future.

Now let's take a closer look at our liquidity status and cash bridge as of the end of Q3. On the next slide, given our strong cash flow, our cash position improved again in the quarter. So looking at the cash bridge above, you see at the end of Q3 EUR6.1 billion in cash and cash equivalents. At the end of Q2, it was EUR5.8 billion and EUR3.8 billion of financial debt, of which EURR3.3 billion is long term. This is stable.

This brings us to a net cash position of EUR2.25 billion, up from the net cash position of EUR1.9 billion at the end of Q2. This is again in line with our clear target to maintain a net cash position throughout the year. Also of note, there were no material cash-ins beyond free cash flow pre-tax of EUR727 million. The main outflows relate to financial interest and cash tax. Net cash adjusted for pension obligations then amounted to EUR1.7 billion at the quarter-end. This is an improvement of roughly EUR2.5 billion versus the end of last fiscal year.

As you know, as just a gentle reminder, in February, we refinanced the existing revolver credit facilities for one facility of EUR4 billion with a maturity of five years. So overall we now have an even stronger balance sheet in comparison to the end of second quarter of fiscal year '24. As mentioned, this is absolutely in line to our firm commitment of a conservative financial risk profile as well as an investment grade rating profile.

So now let's take a look at our business area starting with Gas Services. Gas Services booked record orders this quarter of EUR5.3 billion. This is more than double the level of orders we booked in the third quarter of last year. Book-to-bill was strong at 1.9. The order backlog rose to EUR45.3 billion and the backlog quality continues to improve.

From a regional perspective, as mentioned by Christian, the main orders came from Middle East and Asia. In Q3, we booked 26 gas turbines greater than 10 megawatts; therein, 12 large gas turbines and 14 industrial gas turbines. The market for gas turbines was strong in Q3, and we reached a market share for gas turbines greater than 10 megawatts of approximately 47%.

Revenue in the third quarter was up slightly, plus 1% year-over-year on a comparable basis and came in at EUR2.7 billion. Growth in the service business compensated for a decrease in the new unit business, which resulted, like in the first quarter, in a favorable business mix. The decrease in the new unit business is mainly just due to timing effects.

Profit came in at EUR186 million versus strong prior quarter. This reflects a margin here of 6.8%. In this quarter, we did have one-time legacy effects impacting GS. The impact is a mid-double digit amount. If you look on an underlying basis, the margin is seasonally lower compared to Q1 and Q2 and had, like in last -- Q3 last year, we had a very profitable service quarter.

So just to repeat for GS, we had an impact of a legacy item, which is one-time in nature. If you include, in prior year we had a very strong transactional service quarter, and of course, the regular seasonality that occurs for GS in the next -- in the second half of the year. If you take out the one-time topic, then we're approximately at 9% for GS for the quarter and this is absolutely in line with our expectations.

So now moving on to Grid Technologies, on the next page please. GT, here orders in the third quarter were lower than prior year due to an exceptionally large order for offshore grid connections in the North Sea in prior year. However, the overall level for GT came in strong at EUR3.5 billion, and of course, this is on the back of strong growth in product orders. The book-to-bill came in at 1.54 and the order backlog went up to a record EUR31 billion. Again, also very important is the quality of the backlog in GT also continues to improve.

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Revenue stand out 30.5% year-over-year on a comparable basis growth, coming in at EUR2.3 billion. From a mix perspective, we see solutions at 35 -- just over 35% that grew faster than products, but still products at 25% growth, both at double digit growth. Profit before special items came in strong at EUR237 million. This reflects a margin of 10.3%. Again, the improvement here is driven by the higher volume and comparatively higher margin in the processed order backlog.

Turning to transformation of industry, in the third quarter, for orders, we booked EUR1.1 billion. This is a decline versus the prior year. This decline is absolutely reflecting timing effects in the order intake and a high basis of comparison with a large project book last year, mainly in the electrification, automation, and digitalization business. Book-to-bill therefore came in at 0.86.

But looking at the different businesses within TI, we see continuous positive market momentum. In our sustainable energy business, the electrolyzer business, we do see some temporary slowness, but as Christian mentioned, we're faring well. We're close to booking more orders subject to the grant of course of subsidies.

Revenue in TI grew significantly by just over 23% year-over-year on a comparable basis with all four independently managed businesses, we call those IMBs, at or above prior year's quarter level with compression business at plus 27% and electrification, automation and digitalization or EAD just shy of 27%, really showing the highest growth rates. Of course, SES grew by 32% as well.

Revenue growth was supported by the execution of order backlog [Technical Difficulty] TI, a continuous service momentum. Service revenue in the quarter increased by approximately 25%. New units also grew by 23%, just over 23% versus prior year's Q3. The service share has now reached around 45% year-to-date running, well ahead of our target.

Profit for TI came in at EUR103 million. This is a profit or margin before special items of just shy of 8% at 7.8%, particularly strong in STG or steam with a margin of 12.7%. This is up 310 bps and compression with a margin of 9.4%, also up just over 200 bps. Of course, benefiting from increased volume, but like I said earlier, in a very nice mix with service business and better pricing.

Now let's go to Siemens Gamesa. Overall, Siemens Gamesa is developing in line with our expectations. Looking at orders in the quarter, as expected, sharply down from prior year, and came in at just EUR0.7 billion. Onshore orders continued to be impacted by the temporary suspension of sales activities for the 4.X and 5.X onshore turbines.

As expected, the offshore and service business did not receive any large orders this quarter. In the same quarter in prior year, we had a very large single offshore order in the US worth EUR2.3 billion. Order backlog overall as per the end of the first quarter decreased to EUR37.4 billion, excuse me.

Revenue rose by just over 25% in Siemens Gamesa, comparable as led by onshore and service. Profit before special items came in at negative EUR449 million. As you know, the reasons here, of course, are the project margins burdened by the higher than planned costs due to the known quality issues as well as increased product costs and ramp-up in the offshore area.

As Christian mentioned, we had the annual update of our statistical models, which is used to evaluate the entire wind turbine fleet with respect to failure rates, cost rates, cost inflation assumptions, and we reviewed our agreements with customers in major projects. Again, this is an annual exercise.

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Maybe just as a friendly reminder, in prior year -- it is in Q3; in prior years before that, and this year it's in Q3. Previously it was conducted in Q1. This review overall resulted in a headwind of approximately EUR100 million in the quarter, which is well within expectations and again is not cash effective. This brings me to the financial outlook please for the year on the next page.

As already mentioned by Christian, everything remains the same. There is two important changes. One is the adjustment of our assumptions for Siemens Gamesa. We now expect losses at Siemens Gamesa of up to EUR2 billion compared to around EUR2 billion before. And with respect to free cash flow, we now expect free cash flow pre-tax in a range of EUR1 billion to EUR1.5 billion compared to up to EUR1 billion before.

So thank you very much for listening. With this, I now hand over back to Christian to explain our key priorities. Thank you.

Christian Bruch

Yeah. Thank you very much, Maria, and I will keep it very short because it's a repetition of what I always said quarter over quarter. They are the key three priorities which we are following this year; deliver profitable growth that is obviously linked to profitability, but also making sure that we continue to invest wisely for the growth which is to come; fix the wind business, and obviously maintain a solid financial foundations. We are fully focused on that. I am very grateful for the contribution of all the colleagues at Siemens Energy. We continue to be well on track and we'll continue to do our homework in order to stay on track.

And with this, I would hand back to Michael for the Q&A session.

Question-and-Answer Session

A - Michael Hagmann

Thank you, Christian. Thank you, Maria. We are good on time. As I mentioned earlier, we've allowed about an hour for the call, but we do have a lot of questions already. So I would please ask everybody to stick to one question. If there is time at the end, we will, of course, do a second round. [Operator Instructions] The first three questions go to Vivek Midha, Sebastian Growe, and Akash Gupta. So please, Vivek, go ahead.

Vivek Midha

Thank you very much, Michael, and good morning, everybody. My question is on the very strong cash flow in the quarter. Would you mind giving us a bit more color on the drivers of this? And in particular, I noticed there was quite a large contribution from the change in other assets and liabilities line this quarter. Is there anything to be aware of around this? Thank you.

Maria Ferraro

Thank you, Vivek. Good morning and thank you for the question regarding our free cash flow development. So maybe just to take a step back, the development, of course, of our free cash flow is heavily linked to our volume development. And as you can see, in the first nine months of the year, we booked quite a lot of orders. This is reflecting even a book-to-bill of 1.4.

And after three quarters, we now stand with respect to free cash flow at EUR0.9 billion. And we are expecting a positive free cash flow in Q4, again, driven by the continued strength in orders as well as our typical seasonal effects. I think it's important to see that in context, we also -- of course, maybe one other point is regarding cash outflow from Siemens Gamesa, the quality provisions. That also remains small, right? So this is just as a reminder.

With respect to the change in other assets and liabilities, this is a bit of a mixed bag, but let me just try to shed some light. Of course, our regular employee-related accruals reside there; change in market value in derivatives. So for example, the SIL (ph) option that we talk about and actually have additional information on, the SIL option is there. Those two effects and then, of course, we have sales tax and VAT receivables etc. Those two to three effects really do account for the majority of the change in other assets and liabilities.

Vivek Midha

That's very helpful. Thank you very much.

Maria Ferraro

Thank you.

Michael Hagmann

Thank you, Maria. And the next question goes to Sebastian Growe. Sebastian, please.

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Sebastian Growe

Thanks, Michael. Hi, Maria. Hi, Christian. I also have a question around free cash flow and it's around the guidance. So you have updated the guidance, but still the quarter four only implies around EUR100 million to EUR600 million in quarter four free cash flow. The seasonal working capital release typically has contributed alone EUR0.7 billion to EUR1.5 billion in September quarter. So again, the backdrop, may I ask to walk us through the key building blocks here behind the new guidance, and with that, may I also ask you to provide an update on the project pipeline across sectors. Do you feel comfortable with the EUR10 billion run rate? So leave it there.

Maria Ferraro

Hi, Sebastian. Hi. It was a little difficult to hear you, but I think I got the gist of the question, I think. Of course, as we go into Q4, as mentioned earlier, I mean, we now stand at EUR0.9 billion, right? So we have that already. We're expecting positive free cash flow in the fourth quarter. We put the range there, of course, to say between EUR1 billion and EUR1.5 billion. And I think that it's suffice it to say that of course in the mid-range is where we would expect at this point in time. I hope I captured the question. I didn't hear it.

Sebastian Growe

The question was rather you had typically a very, very strong tailwind from working capital alone, which was between EUR700 million and EUR1.5 billion in the last four years. So I'm a bit struggling with only seeing then EUR100 million to EUR600 million in quarter four as per your guidance. And when you say the mid-range, we're talking EUR300 million, EUR400 million, which looks like a flash in the pan against what typically the seasonality would have allowed for.

Maria Ferraro

Okay. Now -- and we can hear you a little better. So no, I appreciate that. I think there is one distinctive difference. Of course, in the past, we had quite a large order intake coming from Siemens Gamesa, and that actually did have a very strong seasonality of Q4 actually even in the last month of the fiscal year. So of course, with the tempered expected, but reduced order intake there, that also is effect that you should take into consideration. Thank you.

Michael Hagmann

Okay. And then the next question goes to Akash Gupta. Akash, please.

Akash Gupta

Yes. Hi. Good morning. Thanks for your time. One question I have is on Gas Service, and that is related to how to translate the gigawatt opportunities into dollars. So in the quarter, you announced 4 gigawatt order in Saudi Arabia, which includes long term service contract and the value is around EUR1.5 billion and this would translate into roughly $400 million per gigawatt in terms of revenue opportunity, including service.

Is this a fair calculation to convert the gigawatt volumes into monetary value, like $400 million per gigawatt or is there anything related to scope or geography that might complicate the math from one region to the other? And secondly, on the same gas turbines topic, can you also update us on where do we stand on demand and supply given the strong demand that we see also at your competitors? Thank you.

Christian Bruch

Yes. Hi, Akash, and thanks for the question. I would say it's probably a little bit more complex in the overall math of doing it to apply it to an overall order intake. You also have to keep in mind that's a mixture between gas turbines, steam turbines, generators, and then rest of the scope. Services normally is booked then only partly or then later. So I think it's a mixed bag and I would be very careful, and I have to admit from the top of my head, I could not give you a breakdown equation like this, but it's very, very different in the different projects. And also then the regions, obviously there, I would be careful.

In terms of your second question, you have seen our H1, right, on Gas Services in terms of order intake, which already underlines how strong it is. And I continue to be optimistic also on the order side of that. So we are busy, definitely. This is also why I flagged up that we are extending certain capacities. I've announced one thing in Gas Services, and I think the whole industry is pretty busy. We all look forward to continuous market momentum going forward simply because of the higher-than-expected electricity growth. As I said when we've met the last time, we will update everybody in the market with the quarter four results in terms of our future outlook on Gas Services because obviously that is in very, very positive momentum, what we see here.

Akash Gupta

Thank you.

Operator

Thank you. And the next three questions go to Max Yates, Gael de-Bray, Ajay Patel. Max, please go ahead.

Max Yates

Thank you. I guess if I had to ask one, I guess I just want to come back to this legacy item that you mentioned in the Gas Services. So I mean, would you be able to give us kind of any more color or any more detail? And I guess some of the questions that we're getting kind of this morning, you mentioned it isn't a technology issue. Was this a sort of delay on a project that took longer because of supply chains?

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Is that project kind of now fully handed over to the customer and signed off? I guess, just how would you sort of give us kind of increased confidence sitting in our seat that we can kind of draw a line under this and completely attribute it to one-off? How -- is there anything you're able to sort of help us get comfort with on that? Thank you.

Maria Ferraro

No. Thank you. Maybe just to reiterate, and please understand that there is not much more we can say at this time. It's really one-time in nature. It's a legacy item. It has nothing to do with a project or customer requirements not being met, not at all, and it's not technical in nature. I mean, that's all we can share at this point in time, but again, I think it delineates the topic well.

Michael Hagmann

Thank you, Maria. Gael, over to you.

Gael de-Bray

[indiscernible] to statistical model review for Gamesa. If I heard correctly, you mentioned EUR100 million headwinds in total this quarter, out of which only EUR20 million related to the 4.X and 5.X, but with this EUR100 million headwind in mind, so does it mean the underlying operating loss is now trending closer to maybe EUR350 million on a quarterly basis? And could you also help us understand the implications of this model review for the longer term margin outlook in service as well as for the near-term margin development in new equipment?

Michael Hagmann

Gael, unfortunately, for the first 30 seconds or so, you were still on mute. Your line wasn't unmuted. If it was material, if you could repeat the beginning of the question. Otherwise, we will try to answer the remainder of the question that we actually all heard.

Gael de-Bray

Let me repeat. I am not sure what you missed, but I was just saying that if I heard correctly, the impact of the statistical model review was EUR100 million in total in the quarter, part of which only EUR20 million related to the 4.X and 5.X, but does it mean that with this EUR100 million total headwind, the underlying operating loss is now rather trending around EUR350 million a quarter?

Maria Ferraro

You will start. I can certainly go ahead.

Christian Bruch

As you like. I can -- you can take it, I can take -- I mean, first of all, I think with the -- I would, at this point in time where we have so many puts and takes, be a bit careful to go on a simply quarterly mathematics because we'll continue to have puts and takes between the quarters. This is what you have to be aware. And as we work through the different matters, this is obviously what you see.

What I just wanted to comment on is your point around the service margin. We continue to obviously believe on this continuous improvement in the service margin. We also have no reason to believe that fundamentally something is changing in terms of the level of the margin. It will go step after step because obviously we are digesting through some of the legacy items, which you will see in the margins, but fundamentally, there has nothing changed in the principal outlook to the margin profile on the service side. Maria?

Maria Ferraro

No, absolutely. Maybe just to add to that again, of course, as Christian mentioned, we're working through all the challenges and we do experience that normal volatility in both directions because, of course, we're still in transformation in some areas, optimization mode in Siemens Gamesa on the back of last year's issues.

However, I think, Gael, it's really important to see that we had three rather stable quarters between the lines of EUR400 million negative to EUR450 million negative, and again, with nine months under our belt and solid visibility for this fourth quarter, that's why we have adjusted the outlook for Siemens Gamesa to say that the negative EUR2 billion now marks end of our expectations.

But I think also, just remember, in Q4, the absolute amount of revenue is the highest. So the higher the revenue, especially with legacy contracts, then of course, the higher the negative P&L impact or the losses. So just to put that into context and just to underline what Christian said, it's not so easy just to take this EUR100 million headwind and say we're now at EUR350 million. I think that's not correct. Thanks.

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Gael de-Bray

Okay. Thanks very much.

Michael Hagmann

The next question goes to Ajay Patel at Goldman. Ajay, please go ahead.

Ajay Patel

Good morning, and thank you very much for the presentation this morning. My question's on wind. So I just wanted to understand the profile of the margin. So if you look at slide 22 in the presentations, you can see like you have a quite heavy negative WT margin that is moving to minus 5% in Q3. And if you look at the service margin, it really does accelerate into being quite a high negative, like minus 60%, and I just wanted to understand what that profile represents or any detail that can make us understand why those numbers would move in such a fashion. And then just the follow-up to that is, could you give us an indication of how much your onshore order backlog you would have worked through in '24?

Christian Bruch

[indiscernible]

Maria Ferraro

Yeah. Onshore backlog.

Christian Bruch

Yeah. Would you want to take that?

Maria Ferraro

Yeah. Absolutely, I can do. So as mentioned at the beginning of the year, we said we had just over EUR3 billion in onshore backlog that we're working towards or actually converting into this year and into next year again because the execution of that backlog then, of course, secures the fiscal year '26 breakeven, a goal that we have for Siemens Gamesa on target. So as a result, we do expect that a good, let's say, EUR1 billion to EUR1.5 billion of that backlog to be executed this year with the remainder next year, again, with '26 supporting a very small tail end of that into '26 to support the breakeven approach for Siemens Gamesa.

Ajay Patel

And then just on the margin over the quarter, in terms of how it evolved, could you maybe explain that shape a little bit more?

Maria Ferraro

Yes, I can do. And I think this is actually important to understand also with respect to the EUR100 million headwind that we mentioned earlier with the annual update. I think it's important to see the relationship on how that works, and we also indicated that we had puts and takes, if you'd like, both positives and negatives.

Of course, when it comes to the quality issues, service is the one that takes the burden, if you'd like, of most of those quality issues where it comes to additional costs etc. At the same time, and this is something that we've been working very diligently on in the last quarters, is talking to our customers, optimizing costs wherever possible, and that you see actually impacting positively on the WTG profit margin in Q3. So as a result, you have a bit of a mix issue there, if I may, for Q3. What we would expect, of course, is that normalizes into the future, specifically on the service side, as we continue to work through the quality issues. Thank you.

Ajay Patel

Thanks.

Michael Hagmann

Thank you, Maria. The next three questions go to Alex Virgo, Delphine Brault and William Mackie. So Alex, please go ahead.

Alex Virgo

Thanks very much, Michael. Good morning, Christian and Maria. Hopefully you hear me okay. My question was just on the free cash flow profile in Grid Tech. It's been very, very strong, probably a bit stronger than I thought it would be, although I appreciate the strength in the underlying business. Given the sort of seasonality comments in Q4, I'm just wondering if you can help us out with a little bit of the color of what's going on under the hood there and thinking about that, I guess, into 2025 as well, particularly as we think about the margin improvement in the backlog. Thank you.

Maria Ferraro

Thanks, Alex, for the question specifically related to Grid Technologies. As I mentioned, overall, the free cash flow of EUR727 million for the quarter was underpinned by both Grid Technologies and Gas Services. Of course, for Grid Technologies, and you see that actually quarter-over-quarter, that's very strong momentum in the order intake line, and that of course, comes with advance payments etc., from customers, but please don't forget we also have a very strong, now third quarter in a row, double digit profit for Grid Technologies, which is also helping that cash.

With respect to the profile, as we continue into Q4, of course, we still expect the order momentum to continue, and this also then translates into, let's say, strong cash conversion expected for the rest of the fiscal year. Of course, when it comes to next year, Alex, as Christian mentioned, stay tuned. We'll provide that guidance at the end of the year accordingly. Thank you.

Alex Virgo

Okay. Great. Thanks, Maria.

Michael Hagmann

Thank you. Next question goes to Delphine. Delphine, please go ahead.

Maria Ferraro

Delphine, we cannot hear you.

Delphine Brault

Okay. Can you hear me now?

Christian Bruch

Yes, we can hear you.

Maria Ferraro

Yes, we can.

Delphine Brault

Okay. Thank you. Thanks for taking my question. Did you see any issue with your supply chain? I'm thinking notably about the Grid Technology division and the strong growth that you have to manage there.

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Christian Bruch

Thanks for the question. And the answer is yes and we anticipated it over the last quarters. I mean, we see simply a busy supply chain, and we have been investing already more than a year ago at some suppliers into their extension of capacity. You have maybe seen that we are establishing a joint venture with the supplier to extend capacity. This will continue to be something to watch carefully on how to build out smartly capacities.

What you have to see at the same time that this EUR120 billion order book obviously unfolds over quite some time. And this is, you have to put into perspective. But we are working on all ends; own capacity, but also suppliers' capacity. And obviously we see it also, I think, generally in the industry that the delivery times increase. And this is why it will continue to be an area of our focus, but we are focusing on it since quite some time now.

Michael Hagmann

Thank you, Christian. Next question goes to Will Mackie. Will, please go ahead.

William Mackie

Good morning. Can you hear me? Good morning. Can you hear me?

Michael Hagmann

Yes, we can.

William Mackie

Okay. Good morning, Christian, Maria. Thank you for the time. My question is directed towards Gas Services and specifically new unit production outlook and capacity. Against the backdrop that you're highlighting of an improved demand for electricity created by these new demand centers including data centers and the specifics that you've highlighted about increased demand, how would you describe the capacity utilization across the gas turbine new unit production currently? And are there bottlenecks that you see ahead that need to be addressed and what sort of medium term capacity expansion might be needed? Thank you.

Christian Bruch

Yeah. Thanks, Will. It goes into a bit the last question. First of all, on our side, because if I look on our main factories there, I think that is something which we can manage where we can also manage the growth. That is obviously a lot of assembly work where you can work through shifts through different operational models. The big thing we are watching in Gas Services are the blades and vanes, and that is partly obviously our own facility, but obviously also supplier's.

And this is where I said we already some time ago started with one of our key suppliers to invest into extension of their capacity, but it will continue to be an area to watch in terms of building up this capacity. And that is also the reason why delivery times go up because the blades do not come fast enough. This depends a bit and this is why you have to carefully watch it, what type of turbine you're talking about. It's a different infrastructure, a different supply chain, if you talk to the big or to the smaller turbines.

So that is something which differs a bit, but generally that part of the supply chain is constrained and it will not go overnight to extend it. However, I mean, we had to -- that we had a very conservative look on the Gas Services type of development in the last capital market day, and this is why we also said in the next -- with the final full fiscal year quarterly results, we're going to give you an update. We look positive into the outlook. I believe we can manage the capacity in line with what the market is doing. It just means work.

Michael Hagmann

Thank you, Christian. The next three questions go to Ben Uglow, Phil Buller and Austin Earl. So Ben, please go ahead.

Ben Uglow

Brilliant. Good morning, Christian, Maria and Michael. Hope all are well. My question is really a high level question about the customer dialogue, the customer conversation. I mean, if we go back, you basically had orders and book-to-bill coming in at 1.4 times for 12 straight quarters, which is a very long run indeed.

And when I look at some of some of -- some other industries, not necessarily gas power, we're beginning to hear about project pushouts, deferrals, and I think even your US competitor talked a little bit last week about some kind of order slowdown in the second half. I think they were specifically referring to wind.

Really, Christian, I guess what I wanted to know, when you're sitting around the table, do you sense any hesitation at all? Is anybody talking about pushing things into 2025? I mean, obviously it doesn't look like it by this quarter, but what is your sense from the customers at the moment?

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Christian Bruch

Yeah. Thank you very much, Ben. Very good to hear you. And maybe put it into perspective because I think we have to differentiate a bit the situation on wind, particular offshore wind, where you have a special discussion. Fundamentally, I would say I'm not seeing that. I mean, I'm seeing a, let's say, very positive dialogue.

Obviously what we have to take into account that the planning phases are much longer than they used to be. And this is why we see reservation agreements. On future capacity discussed, we anyway try in all our areas to have a little bit more strategic discussions with our customers to be able to plan longer term. And this goes well in line with what we always wanted to do [Technical Difficulty] the volatility as much as possible (ph), let's get a little bit better and planning [Technical Difficulty]. And this is what I see happening. So I do see still obviously a good momentum in these type of markets. However, the delivery times are longer and obviously do require special relationships.

What I see in wind, particularly in offshore wind, obviously the whole industry is at the moment trying to understand how can you make it profitable also seeing the auctions coming. And there, absolutely, we see a discussion also our customer says it's difficult sometimes to compete in an environment where the profit pools are not entirely clear. I think there is a full understanding also for the suppliers that they also need to earn money on the supply chain.

However, at the same time, with increased financing cost, it is very difficult to make certain projects in some countries fly. We always have, in offshore, planned relatively conservatively with the outlook. We never took the sum of the commitments and planned on that. We considered a much lower number, but that is something what I see and it will be extremely, extremely interesting now to see the auctions coming out, the results in the UK, in US, in Europe, in terms of how does this play out.

However, on the renewable side, that is definitely something which we need to watch simply because it's so influenced also by the increased financing cost. And I think the overall cost inflation which we had seen in this industry on GS and GT, I would see that slightly different also because in a lot of areas, GT is regulated, build out in terms of the commitments, but wind is definitely something which we also watch very carefully on close contact with our customer on how to face that challenge, but we, at the same time, and I hear that from our customers, everybody is convinced you will need it; we will need that industry, but it might be not as cheap as some people believe.

Ben Uglow

Understood. Thank you.

Michael Hagmann

Thank you, Ben. And the next question goes to Phil Buller. Phil, please go ahead.

Phil Buller

Hi. Thanks for the question. Obviously well done on the cash flow. I know this isn't a company where you want to run with leverage, but is there anything to consider with regard to the guarantees in the context of potential shareholder distributions? I guess I'm wondering if you plan to propose a dividend at some point to be paid in 2025 or if there's a reason that can't or shouldn't happen at this point. Thanks.

Maria Ferraro

Hi, Phil. Thank you for the question regarding the bond guarantee. I think it's well known the restrictions on that that is placed upon us as a result of that bond guarantee. I think it's important to state that we are utilizing the facility now. This is something that, of course, is required on the back of some of the growth, but of course, anything relating to '25 and beyond, as we mentioned, we will give indications with -- in line with our year-end call and that's where of course we'll give a proper update. Otherwise, I would say, with respect to how things are going on a quarterly basis and our necessity for guarantees, the ability for us to obtain guarantees, all of that is actually quite well in hand.

Phil Buller

Thanks.

Michael Hagmann

Thank you. And the next question goes to Austin Earl. Austin, please.

Unidentified Participant

Hi. My questions have been answered. Thank you.

Michael Hagmann

Thank you, Austin. So the next couple of questions go to Andrew Wilson, Alex Hauenstein, and Malte Schmitter. Andrew, if you please go ahead.

Andrew Wilson

Hi. I have to be honest. I must have dialed that by accident. So I don't actually have a question. Apologies for wasting your time.

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Michael Hagmann

Thanks, Andrew. Okay. So the next question goes to Alex Hauenstein. Alex, please.

Alex Hauenstein

Yes, hello. Alex Hauenstein. Thanks for taking my questions. I would like to come back on SGRE. You wrote about the reintroduction of the X.4 is on track and you wrote about solid progress on the X.5. Can you provide us a bit more color on the project execution, especially on the legacy project part? Overall, with regard to these three items, I mean, can you give us some examples what has been done since we spoke last time?

And maybe a follow-up very quickly on SGRE. Do you have a feeling that especially in Germany and the EU, in particular, the approval process and the bureaucracy generally is somewhat tackled at the moment and are things somewhat improving? Or is it even getting worse in terms of time to install and time to get the approvals etc., etc.? Thank you.

Christian Bruch

Yeah. Thank you very much for the question. On the project execution, and that is obviously particular also looking on the 5.X, because that has been the bigger amount of projects under execution, where for the 4.X, there has been the bigger amount in turbines in the field. And we continue to do so. We also continue to hand over, and keep in mind, if you discuss the 5.X elements, let's say a lot of these turbines are operating and generating power for customers and continuously also with the investigations, we continue to improve also the availability in the field step after step.

This will still take some time to get it there where we want to have it, but you have seen an improvement and you also have seen continuous handover -- since the last time we spoke, continuous handover of projects to customers, which obviously is a sign also that this was not a stopped activity. I would, if I say right from the top of my head, think that more than half of the project we had under executions are -- have been handed over and we continue to execute on this while at the same time we identify the implementation of the -- of, let's say, quality packages for the next years to come.

On the approval process, because you mentioned in particular Germany, I think it has improved. I mean, it's probably a better question to our customers, but we always have to be clear that the German process is a special one. There is a, let's say, relatively time-consuming upfront approval process, which is then also implying already the technical solution. So that is a more time-consuming process compared to other European countries. So I think there is room for improvement. Generally we have seen certain upticks in onshore. Obviously, for us, it will now be interesting to see how this plays out when we start to re-enter the market, but I think that's a bit too early now to comment on.

Michael Hagmann

Thank you, Christian. We have time for two more questions as we have a hard stop. As I previously mentioned, next one will go to Malte Schmitter, and then the very last one will go to Sean McLoughlin. So Malte, if you please go ahead.

Malte Schmitter

Yeah. Thanks for that, but I think there seems to be a technical issue. I also did not register for a question. Apologies for that.

Michael Hagmann

Thank you. So the last question then goes to Sean McLoughlin. Sean, please.

Sean McLoughlin

Thank you for squeezing me in. I suppose then just because we haven't asked about it, just on transformation of industries, obviously slightly disappointing order intake. You've talked about a much longer or slower market, particularly around the SES side. I mean, how are you thinking then about, I suppose, capacity allocation -- or CapEx allocation here to this segment and I suppose how quickly could this become profitable?

Christian Bruch

Yeah. Thanks for the question. First of all, just also to put it in perspective, we flagged up, let's say, a bigger project there which is not reflected yet in the order intake of the quarter. You would see it in the next quarter, which obviously gives us load for the factory here, but we also always have set our interest at the moment. And I would say in the next 15 months to come is to keep some load in the factory, but also to practice to have the quality assurance, the supply chain assurance to get ready for really the full volume. So it was not the intention to really have it fully ramped up.

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The market is slower than we originally anticipated, probably I would say delayed by a year or one and a half years, my guess, also driven by a change in the IRA schemes in the US. But at the same time, there was a reason also why we have set up this factory here in Berlin together with an industrial partner, Air Liquide, which is a good partner to do this who co-invested with us into the factory to keep some balance in there. So we definitely will be very careful with our cash burn on this business, but at the same time, we need to keep a focus on commercializing it really and building up the supply chain.

I don't see big investments on our side to keep the system running, but because as I said, I believe the market is somewhat delayed, but also keep in mind that we always said that's going to be a commercial business by the end of the decade. And I would repeat this. I think the expectation to that business has been far too positive. It will take time. We are, I believe, on track what we set and I'm pleased also if I look on our factories, on what the guys are doing in terms of really stabilizing all the processes and getting ready for the market, but it's still some time to come.

Sean McLoughlin

Thank you.

Michael Hagmann

Thank you, Christian. That brings us to the end of the Q&A. Apologies for the noise earlier. It was not possible to hear it from where we were. And if there was anyone that couldn't hear, please do reach out to the Investor Relations team. As always, we are very approachable. And with that, I would hand over for very last closing remarks to Christian. Thanks, everybody.

Christian Bruch

No, and I would just convey my thanks to all of you for spending the time with us, to be interested in our company. I look forward for the quarter four call where we give you an outlook for 2025 and then really stay healthy, stay tuned and look forward to speak to you soon. Thank you very much.

Maria Ferraro

Thank you.

Operator

Ladies and gentlemen, this concludes today's conference call. Thank you very much for participating. A recording of this conference call will be available on the Investor Relations section of Siemens Energy website. The website address is www.siemens-energy.com/investorrelations. Have a good day. Good-bye.

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