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Drägerwerk AG & Co. KGaA (DRW8.DE)

Q3 2024 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, welcome to the Drägerwerk Q3 2024 Earnings Call. I'm Sergin, the Chorus Call operator. I would like to remind you that all participants will be in listen-only mode, and the conference is being recorded. The presentation will be followed by a Q&A session. [Operator Instructions] The conference must not be recorded for publication or broadcast.

At this time, it's my pleasure to hand over to Stefan Dräger, CEO. Please go ahead, sir.

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

Good afternoon and thank you for joining our conference call on our financial results for the first nine months of 2024. I have with me Gert-Hartwig Lescow, Group CFO; as well as Tom Fischler and Nikolaus Hammerschmidt, both Investor Relations.

We would like to take you through the results with a presentation that we made available on our Web page this morning. Following the presentation, we will open the floor to your questions.

Let's get started on page 5 with the business highlights. In the first nine months of 2024, we successfully paved the way to our annual targets with continued good demand, robust net sales, and higher earnings. At €2.4 billion, order intake slightly surpassed the high level of the prior-year period. Net sales at €2.3 billion almost reached the high prior-year figure which, at that time, was positively influenced by an improvement in delivery capacity and a surge in demand for ventilators in China. Both in terms of orders and sales, we were able to grow in all regions except APAC.

Our safety division performed better than the medical division which was affected by the challenging market environment in China. Our EBIT in the first nine months increased to over €80 million. This growth was driven not only by our operating business, but also by onetime effect totaling around €32 million. Among others, this included the sale of a non-core business activity in the Netherlands and the sale of land in the US in the second quarter with a total amount of €20 million, as well as the sale of a building in Spain in the third quarter, which contributed around €10 million to the earnings.

After the first nine months, our EBIT margin was slightly above the prior-year level at 3.5%. Our focus remains on improving profitability.

Regarding our FDA warning letter, there have been no relevant news since our last conference call at the end of July. We are still waiting for a response from the FDA to conduct the necessary reinspection of our site in Andover. Actual timing and scheduling of this inspection is at the FDA's discretion.

As communicated two weeks ago, we confirmed our annual guidance. In expectation of a strong year-end business, we continue to forecast net sales growth in the lower half and EBIT margin in the upper half of the previously forecasted ranges. I will come back to this in our outlook at the end of the presentation.

With that, I turn over to Gert-Hartwig for a review of the financials. Gert-Hartwig, please.

Gert-Hartwig Lescow

Chief Financial Officer and Executive Board Member-IT & Vice Chairman-Executive Board, Drägerwerk AG & Co. KGaA

Thank you, Stefan. I would also like to welcome everybody to this conference call of our results for the first nine months of 2024. Please turn to page 7 for a review on the Dräger Group. As usual, I will be stating currency-adjusted figures whenever referring to growth rates. As Stefan said, we continued to see good demand for our Technology for Life. Overall, orders in the first nine months of 2024 increased by about 1.4% to around €2.4 billion, driven particularly by growth in Germany and positive development in EMEA and America. However, orders in APAC decreased mainly due to the reduced demand for ventilators in China compared to last year and the current challenging market environment in China, which is leading to subdued demand affecting all Western medtech suppliers.

Net sales in Q3 and in the first nine months almost reached the prior-year level, despite the mentioned base effects. After the first nine months, net sales were only 0.4% lower at around €2.3 billion.

In both reporting periods, our safety division outperformed the medical division. Due to the good margin of the safety division, our group's gross profit margin increased by 0.4 percentage points to 44.4% at the end of the first nine months. Our functional costs decreased by 0.4% in the first nine months of 2024. This was mainly due to higher other operating income as a result of onetime effects.

As Stefan said, the onetime effects contributed around €32 million to earnings in the first nine months. Around €31 million of this amount is included in the functional cost. With around €18 million of total onetime effect, the impact in our safety division was stronger than on our medical division with around €14 million.

In the third quarter, the onetime effect amounted to around €12 million for the group, of which €7 million in medical and €5 million in safety. In the second quarter, we sold our fire alarm system business in the Netherlands to focus our activities on our core business. Additionally, we sold an unused plot of land in the US. These onetime effects contributed around €20 million to our EBIT. In the third quarter, we sold the building in Spain, which contributed and added the additional €10 million. The building was owned by our subsidiary, Dräger Hispania, which decided to move to a new location for rent.

Including this onetime effect, our EBIT in the third quarter was approximately €24 million, compared to around €29 million in the prior-year quarter. Our EBIT margin stood at 3.1%, down from 3.7% in the year before. However, in the first nine months, profitability improved with EBIT increasing from roughly €77 million to around €80 million. Consequently, our EBIT margin rose from 3.3% to 3.5%. Additionally, the rolling 12-month DVA improved to around €30 million.

Let us now take a closer look at the development of the two divisions, starting with the medical division, on page 8. In the third quarter, order intake was below the prior-year level. Growth in EMEA, APAC and Germany was offset by a decline in the Americas region, which was primarily due to the light high level of the prior year when we would see major orders from Mexico for workplace infrastructure.

In the first nine months, order intake decreased by around 2%. This was mainly due to the significant decline in APAC in the course of the missing ventilator demand and the current health care reform in China, which is slowing down health care orders throughout the industry. While net sales in the third quarter were still slightly lower than the prior year's figure, the gap is much lower than in the previous quarters since much of the base effect is related to the first and second quarters.

Overall, net sales in the first nine months were around 5% below the prior-year level at around €1.3 billion. Mainly due to currency effects and higher expenses from inventory adjustments in production, the gross margin in Q3 decreased by 2 percentage points. After nine months, it was only 0.7 percentage points below the prior year's margin.

Functional expenses decreased by roughly 2% in the year-to-date. In the third quarter, EBIT amounted to minus €4 million after €0.3 million in the prior-year period. The EBIT margin decreased to 0.1% to minus 0.9%. In the first nine months, EBIT amounted to some minus €28 million after minus €2.3 million in the prior-year period while the EBIT margin decreased from minus 0.2% to minus 2.2%.

As mentioned, onetime effects contributed around €13 million to [indiscernible] (00:18:31). The rolling 12-month DVA was significantly lower at minus €67.7 million, coming from minus €41.6 million, mainly due to an adjustment of the weighted average cost of capital, reflecting a changed interest rate environment.

I will now turn to our safety division which delivered another good performance. We are now on page 9. Our safety business continues to grow. In the third quarter, order intake rose significantly by roughly 12%. Orders for services and customer-specific orders recorded a disproportionately high increase. In the first nine months, order intake rose by roughly 7% to around €1.1 billion, thanks to a higher demand in almost all product categories, especially occupational health and safety equipment, as well as respiratory and personal protection equipment.

In both reporting periods, Germany was the main driver with an increase of almost 37% in Q3 and 17% year-on-year. Year-to-date, EMEA also performed very well. In the third quarter, net sales were roughly 1% below the prior-year figure. This was due to the decline in EMEA and APAC, which offset the growth in Germany and the Americas. In the first nine months, however, net sales increased by roughly 6% to just over €1 billion, thanks to growing sales in all regions.

The gross margin went up by 1.4 percentage points in Q3. During the first nine months, it rose by 1.5 percentage points, thanks to effective price enforcement in particular. Functional expenses were around 2% higher than in the prior-year period, mainly due to higher R&D expenses and higher sales costs in the region.

In the third quarter, EBIT and EBIT margin remained quite stable at €28.3 million and 8.4% after €28.9 million and 8.5% in the prior year. In the first nine months, however, EBIT increased significantly from some €79 million to roughly €108 million, thanks to the improved operating development and positive onetime effects of around €18 million. The EBIT margin consequently rose from 8.2% to 10.7%.

The rolling 12-month DVA also improved significantly by around €31 million to around €97 million, coming from €66 million in the prior-year period. All in all, a very positive development in our safety business.

Let's move on to some key ratios on page 10. In the first nine months of 2024, we recorded a significant improvement in the operating cash flow. Next to slightly higher earnings, also working cash flow investment contributed, especially with improved payables and receivables management. Furthermore, the sale of our business in the Netherlands also contributed to a higher free cash flow. Free cash flow after nine months is clearly back in positive territory. Following our normal CF seasonality, we expect to see a further improvement in cash generation in the fourth quarter.

Net financial debt was further improved during the quarter, so had net financial debt to EBITDA and with a leverage of 0.7, it is on a healthy level. Net working capital was around 6% below the prior-year level and just below €700 million. The significant improvement in the 12-month rolling EBIT and the decrease in capital employed as at the reporting date also led to an improved 12-month return on capital employed of around 11%, compared to 8.4% in the same period of the prior year. The positive business development next to other things has also resulted in a further increase in the group's equity position. As at September 30th, the equity ratio was almost 48%. Next to other things, this was mainly due to the adjustment of the calculation parameters for pension provisions.

Now, I hand back to Stefan Dräger for the outlook on page 12.

Stefan Dräger

Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

Ladies and gentlemen, with our markets being intact, good overall demand, robust net sales and improved earnings, we have successfully paved the way to reach our annual targets. Some onetime effects helped us to compensate for a prior-year tailwind. At the same time, we saw some bright spots in Q3, such as the significant year-on-year order increase in our safety division.

Q4 is always our strongest quarter. This would be no different this year. The remaining net sales gap is not without challenges, especially since we are still not seeing any sign of improving in the Chinese market. Nonetheless, we confirm our full-year target. For 2024, we continue to expect, as previously guided, net sales growth of 1.0% to 5.0% of net currency effects and an EBIT margin of 2.5% to 5.5%. At the same time, we continue to expect net sales growth in the lower half and EBIT margin and DVA in the upper half of this forecasted range.

With this, I would like to end the presentation and hand over to the operator to open the line for your questions, please.

QUESTION AND ANSWER SECTION

Operator: Ladies and gentlemen, we will now begin the question-and-answer session. [Operator Instructions] We have the first question coming from the line of Christian Ehmann from Warburg Research. Please go ahead.

Christian Ehmann
Analyst, Warburg Research GmbH

Q

Hello and good evening. Thanks for taking my questions. So, I have two at the moment. The first would be regarding your, let's say, feelings toward Q4. As usual, you need the – [indiscernible] (00:25:18) most of the earnings for the year in Q4, depending on what kind of guidance one has in its model. And I would like to ask you to give me some of your parameters which contribute to your confidence for the Q4. And the second would be regarding the safety and medical division. So, I appreciate that safety is very much better than medical. What kind of structural – what kind of effects for the positivity in safety are structural and what kind of are seasonal? And what kind of effects for the negativity in medical are structural and what kind are seasonal? Thank you very much.

Gert-Hartwig Lescow
Chief Financial Officer and Executive Board Member-IT & Vice Chairman-Executive Board, Drägerwerk AG & Co. KGaA

A

Perhaps let me start with the question on the fourth quarter. Firstly, let me repeat that, the seasonality and I think you said so much in your question, that is in fact typical over an extended period. The fourth quarter is, by far, the strongest quarter in particular on the medical side of the business. And this year makes no exceptions. And the basis for the assumption that this year will be similar is from a regional point of view, the sound development that we have already seen in North America, as well as in South America where some order tenders will be delivered in Q2. And the continued good development in Germany, for example, in South America, we had received large orders in Mexico, and they will partially be delivered in the fourth quarter. They will contribute. Let me also reiterate we do not, at this point, expect or have factored in any strong or quick recovery in our Chinese business.

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

And that is, now Stefan Dräger speaking, leading to your second question on the both the medical and the safety division, what are seasonal effects and what are structural elements that could be behind. Well, firstly, I would say, and for both divisions, there are no, say, special seasonal effects other than the ones that Gert-Hartwig already mentioned that are typical for other Dräger business as we had quite a number of the government bodies as the – say, our customers because they ask – many of them are still in the [indiscernible] (00:28:06) system, and it is spending the budget towards the end of the year. So, that is why it is – as the overall Dräger business for both divisions has this structure.

Now, on the structure side, for the medical – sorry, start with the safety division, we decided in around like 2017, I think, or 2018 that we wanted to invest more in specific capabilities in the sales organization, specific competencies. And that's what we did. And this is now paying off, as we have enjoyed very good increase and development in the fire gas detection systems business.

And so, we have the new products coming to the market for the firefighter communication and location system, and also for the mining industry, for the oil and gas industry. And so, it is supported by the – it's a competitive state-of-the-art product portfolio. But the general underlying reason is that we invested – a couple of years ago, we decided to invest in specific capabilities in the sales organizations. That strengthens mainly the safety business because it is so diverse, so many different markets that we serve that is actually around 30 different single markets. There is no such thing as a safety market.

For the medical, there – which is, of course, a little bit disappointing that it has, as I said, downturn overall. There's one single very big factor, that is the situation in China, which for us, the large contributor to our medical business in the past. And then, it has a very [ph] weird (00:30:27) development in this current year. And as we Gert-Hartwig pointed out, we have not expected that it'll recover quickly. So, that is the greatest single effect. Without this effect, then we wouldn't have this discussion. It would look reasonably well overall. And there are some smaller effects, for instance, in Korea that is still ongoing strike of the doctors in the health care system. So, that is also muting the investment for medical equipment.

And then, there we have – in addition, had a big boom in the corona times, you remember the ventilation. So, we quadrupled the output of our production, and that continued until well after the pandemic. So, that is the reason why it is not as strong as the safety business, plus the product architecture in the portfolio, as I said before, we are still working on the last steps of replacing the – the current architecture goes back to the year 2003 when it was decided the architecture for the therapy systems. So, that has now happened for the last couple of years, a major effort. And so, we're looking forward to harvesting the fruit in the years to come. In general, the market outlook is as positive as for the safety business.

Christian Ehmann
Analyst, Warburg Research GmbH

Q

Thank you. A couple of follow-ups, if I may. When I look at the – so, you said that the Q4 is, as we all know, particularly strong for the medical side. Given that we see a weakness this year, do you see any indication for the Q4, especially given the development we saw up until now? And if I sum it up correctly, your confidence for Q4 comes mainly from the safety division and from the good order book from North, South America and Germany?

And my second question would be to the structural effects in the safety business. So, is it reasonable to assume, and I'm of course looking at 2025, that the good growth rate you saw for the safety business overall for 6.5% year-over-year, is this something you – one could expect to continue in 2025 and even might be – maybe even beyond in 2026? Thank you.

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

Yeah, in general, it is rather safe to assume that safety continues on a good development. However, please mind that some of the growth, in particular in 2023, came from the improved price [indiscernible] (00:33:48). So, we were able to increase prices significantly. And so, that effect was even slightly greater than the volume increase and the pricing increase will probably not continue at the same slope. So, this factor will continue, as you know, everyone that's around the organization how important that is, in particular as we put profitability first. However, it will probably go back to a slightly lower rate of improvement for the price defense. So, besides on that, it's safe to assume that it will continue on the positive development.

Your point before, the good outlook for the Q4, no, I would say it's not only the confidence based on safety and some regions because we also expect a good Q4 for the medical side, as Gert-Hartwig pointed out, there are larger orders in the mix for the regions that he mentioned. And there is – other than in China, there is no – and it was slightly extend in Korea, there is no fundamental problem that would prevent a similar, say, ratio of the quarters as we typically has [indiscernible] (00:35:19), so it's – that's on that part.

Christian Ehmann
Analyst, Warburg Research GmbH

Q

Thank you very much. Very helpful.

Operator: The next question comes from the line of Alexander Galitsa from HAIB. Please go ahead.

Alexander Galitsa
Analyst, Hauck & Aufhaeuser Lampe Privatbankiers AG

Q

Good afternoon. Thank you for taking the questions. I'll have several, maybe starting the first set of questions related to medical division. First, whether you could remind us why last year in Q4, the gross profit margin was the lowest throughout the year, despite much higher revenue. I presume that maybe the hospital infrastructure orders that you saw last year from medical played a role, but whether you could clarify that. And then, related to that question is now looking at sequentially higher volumes, obviously in Q4, and current mix you have in the backlog, would you expect your gross profit margin in Q4 this year to improve sequentially? That would be the first one.

Gert-Hartwig Lescow
Chief Financial Officer and Executive Board Member-IT & Vice Chairman-Executive Board, Drägerwerk AG & Co. KGaA

A

So, firstly, the Q4 gross margin overall was lower since we wrote down our factories for the FFP masks.

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

That is in safety.

Gert-Hartwig Lescow
Chief Financial Officer and Executive Board Member-IT & Vice Chairman-Executive Board, Drägerwerk AG & Co. KGaA

A

That's for the safety division. But that is, across the group, the largest factors. We, at this point, see no comparable write-down either in the medical or in the safety division. And you're correct, we had a higher share. The larger orders that I mentioned, for example, in Mexico, they are more coming from therapy. So, there should be a similar hit on profitability.

Having said that, it is not unusual that large orders in particular also are executed with a larger discount to the customer, obviously. But we do not expect a steep hit on the gross profit margin, but in fact a significantly higher net sales overall in safety and in particular on the medical side of the business in the fourth quarter.

Alexander Galitsa
Analyst, Hauck & Aufhaeuser Lampe Privatbankiers AG

Q

Okay. Can I just clarify this Mexico orders? Because if I understood correctly, last year in Q3, you had also big order in, I think, in the category of hospital infrastructure. So now, we're talking about Mexico orders in Q3 2024. Is that – are those different orders? Or if you could clarify, do we have big order last year and big order this year, or is it the same?

Gert-Hartwig Lescow
Chief Financial Officer and Executive Board Member-IT & Vice Chairman-Executive Board, Drägerwerk AG & Co. KGaA

A

It's quite right. It's actually different orders. [indiscernible] (00:38:26) to similar health care group, but it's a different orders. We had a larger share of workplace infrastructure, and we have a higher share of therapy devices this year.

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

And last year, so that's – some therapies business as well, in Russia, this is now more or less diminishing.

Alexander Galitsa
Analyst, Hauck & Aufhaeuser Lampe Privatbankiers AG

Q

And just to confirm with – in terms of profitability, my understanding was always that workplace infrastructure carries lower margins than the therapy devices. Is that also the case with this Mexico fitting of the hospital in Mexico?

Gert-Hartwig Lescow
Chief Financial Officer and Executive Board Member-IT & Vice Chairman-Executive Board, Drägerwerk AG & Co. KGaA

A

Generally, right. On the gross profit margin you refer to, there are also, of course, trigger few expenses. But on the gross profit, you're quite right. And that's also [indiscernible] (00:39:24).

Alexander Galitsa
Analyst, Hauck & Aufhaeuser Lampe Privatbankiers AG

Q

Okay. Thank you. And then, moving on to safety, a couple of questions here as well. I wonder why Q3 top line in safety was flattish in Q3 year-over-year despite you basically having a better year-on-year book-to-bill in Q2 that you carried over into Q3, which should have been helpful. And then, simultaneously also in Q3, order intake and safety was also on a good level. Just wondering whether there is anything specific you could call out as the reason why Q3 top line was softer despite the rather positive, I guess, backdrop in terms of order intake.

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

That's a good question. I really cannot call on anything specific. And it is the nature of the business. If you break it down to a lower time in the order – you go down today, it is becoming more statistically, say, up and down. So, I wouldn't think too much about it.

Alexander Galitsa
Analyst, Hauck & Aufhaeuser Lampe Privatbankiers AG

Q

Okay, fair enough. And then, whether you are – just wondering whether you're confident to having seen this sort of a small blip in Q3 in terms of flattish revenue, whether you're confident to return to revenue growth in Q4, considering that also, it seems that Q4 comparable did not really have the benefit last year from the book-to-bill that you have in this year? I guess the question ultimately is what's your confidence level to return to growth in Q4?

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

Well, it is – it's reasonably good for both the medical and the safety division.

Alexander Galitsa
Analyst, Hauck & Aufhaeuser Lampe Privatbankiers AG

Q

Okay, perfect. And then, if I may, just to squeeze additional one in terms of order intake in safety, I think throughout the first three quarters of this year, there is a divergence in performance between regions, I think Germany and the EMEA consistently growing while Americas and APAC are more muted. I just wonder whether you can stick to this divergence, what is doing well in Europe and why are you much less successful in Americas, APAC? And what are your expectations for this trend going forward?

Gert-Hartwig Lescow
Chief Financial Officer and Executive Board Member-IT & Vice Chairman-Executive Board, Drägerwerk AG & Co. KGaA

A

Okay. So, for APAC, also on the safety side, there is a weakness in China. So, that's a key driver for the weaker development. And as far as and...

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

And also in Japan, so – and Korea, there is, say, that is challenging, so there's no, say – there is not much to do with the rest the world because it's a individual sales in this market.

Alexander Galitsa
Analyst, Hauck & Aufhaeuser Lampe Privatbankiers AG

Q

And in the US in particular, I mean, you obviously have now benefits from the intensified, I guess, sales and marketing activities in Europe, are you expecting – has something changed in the US and whether you are expecting to see similar maybe uptake in the business you have witnessed in Europe for safety division?

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

Yeah, to be honest, I think that's a good question [indiscernible] (00:43:05). And so, we are, say, deeply looking into that [indiscernible] (00:43:11) from our point of view, necessary ingredients for growth. And then, we need some, say care to find out, to the life that's going as it should.

Alexander Galitsa
Analyst, Hauck & Aufhaeuser Lampe Privatbankiers AG

Q

Okay. And then, very last one, the currency, you mentioned currency headwinds and higher expenses for inventory adjustments having an impact on profitability in medical division. Could you maybe quantify that? And also, what are these inventory adjustments? And yeah, thank you.

Gert-Hartwig Lescow
Chief Financial Officer and Executive Board Member-IT & Vice Chairman-Executive Board, Drägerwerk AG & Co. KGaA

A

Why we have not broken that out on individual basis and the inventory adjustment is really a side effect of the lower production in the medical. So, when you think about it, it's not so much, if you will, the write-down of the inventory, but it's higher inventory cost due to the fact that we have lower utilization in our production on the medical side. And it's – actually if I – if you compare, say, the, the realized margin based on, if you will, what's realized in the market, the lower margin in the medical is actually mainly due to these FX effects and the low-capacity utilization.

Alexander Galitsa
Analyst, Hauck & Aufhaeuser Lampe Privatbankiers AG

Q

Okay. And the FX effects the headwind is stemming from what currencies in particular and whether you're expecting based on current, I guess, trends in this respective currency, whether you're expecting much of the headwind in the coming quarter?

Gert-Hartwig Lescow
Chief Financial Officer and Executive Board Member-IT & Vice Chairman-Executive Board, Drägerwerk AG & Co. KGaA

A

So, the second part is a bit difficult. We regularly assume that currencies are what they are. We do have some, but we do not – it's very difficult to make a forecast on the individual currencies and it's really across the portfolio [indiscernible] (00:45:22). There is not, as of today, a huge impact. But overall, on the net sales side for the group, the impact is about 1 percentage point, 1.5 percentage points or so on the net sales.

So, all in, it's not even anything that I would call a large FX impact. Of course, it is noticeable in particular on the medical side since the relative profitability is already on a rather low level.

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

And to your further and to the – single most important, the currency in the US dollar versus euro, please keep in mind that we have a pretty, say, comprehensive natural hedging as we have cost expenses. And so, as a source, say, in our supply chain about as much and as we have income in US dollars.

Gert-Hartwig Lescow
Chief Financial Officer and Executive Board Member-IT & Vice Chairman-Executive Board, Drägerwerk AG & Co. KGaA

A

Not quite.

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

Go ahead.

Gert-Hartwig Lescow
Chief Financial Officer and Executive Board Member-IT & Vice Chairman-Executive Board, Drägerwerk AG & Co. KGaA

A

Sorry for jumping in. In fact, the US dollar is an unusual currency, we have even higher costs, albeit including material...

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

[indiscernible] (00:46:30).

Gert-Hartwig Lescow
Chief Financial Officer and Executive Board Member-IT & Vice Chairman-Executive Board, Drägerwerk AG & Co. KGaA

A

...in the US dollar. So...

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

Okay.

Gert-Hartwig Lescow
Chief Financial Officer and Executive Board Member-IT & Vice Chairman-Executive Board, Drägerwerk AG & Co. KGaA

A

So, for almost all currencies, we are, of course – not of course [indiscernible] (00:46:38) at the non-euro currencies. So, a stronger currency is positive for us on the bottom line. For the US dollar impact, in weaker US dollar is, if you will, harmful on the net sales and on the profit contribution from the country, but positive for the EBIT for the group due to the fact that many materials that we use in safety and medical are denominated in US dollars and the one currency where we are almost balanced out across both medical and safety is the British pound, which is due to the fact that our SCBAs on the safety division are manufactured in the north of England. So, in addition to the contribution from the market business in the UK, we have a counter-position from manufacturing the SCBAs in – for the global market.

Alexander Galitsa
Analyst, Hauck & Aufhaeuser Lampe Privatbankiers AG

Q

Okay. Thank you so much.

Operator: The next question comes from the line of Jean-Marc Müller from JMS Invest AG. Please go ahead.

Jean-Marc Müller
Founding Partner, CEO & Portfolio Manager, JMS Invest AG

Q

Yes, thank you for taking my question. I have a question on cost management. I mean, I look at Dräger since many years and obviously cost management has never been the [ph] fore to (00:48:06) of the company. And this year, again, I must say, it's rather disappointing how costs are being managed given the lower top line development. If I adjust the functional cost for the one-offs, the positive one-offs, the costs are up over nine months by around 3% on a top line, which in euro is down 1%. And that on a base which is already super high, I mean, you're overspending on R&D and on other functional costs and still the cost go up any further. Also, you mentioned in medical, pretty poor capacity utilization because of the weak sales development. I mean, when are you willing to address these issues and really take a look at the structural costs, the capacity utilization, et cetera, and maybe make adjustments which will lead to a sustainable, different margin profile for the company, especially in medical?

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

Yeah. So, our primary focus is on profitability and the cost is a factor that is important for that, and I mean probably expenses. And so, I mentioned in my previous answer one of the reasons why we spent the significant amount in R&D in particular in the medical division to catch up from the legacy of the previous architecture, which is ongoing. And to make a long story short, when are we willing to make significant cuts in the expenses. At the moment, we do not believe any longer in the future and we would do it.

Jean-Marc Müller
Founding Partner, CEO & Portfolio Manager, JMS Invest AG

Q

But you have been overspending now for many years. I mean, eventually we should see the benefits of this extra costs that have been burdening the P&L now for, for many years. And I don't see it. The gross margin medical is still subpar. And I don't see it in – if you overspend on R&D, that's fine. But eventually one should see a great product coming out of all this, which will then lead to higher volumes and higher margins because it's potentially the better product. And I've seen neither of it.

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

Yeah, you are right. And it symbolizes a [indiscernible] (00:50:49) act and it's also disappointing for us and in particular myself, that it takes longer than expected to see the benefits and to harvest the fruits. However, we still believe that [indiscernible] (00:51:04) that's going to come. Otherwise, we wouldn't do it, on the R&D side. On the capacity underutilization, we are aware that, that is a burden, and we are working on reducing the capacity in the medical production side. So, that's not something that we somewhat decline in general, but we do it after we do a thorough reflection of the pros and cons.

Jean-Marc Müller
Founding Partner, CEO & Portfolio Manager, JMS Invest AG

Q

Okay. And on the EBIT level, I mean, obviously upper end of the range, I mean, no surprise given that you have €32 million of one-offs in there. How do you see 2025, given that you have now this very high base effect on the EBIT level? Do you think that there is a chance that you can overachieve 2024 results in 2025? Or will it not be possible to compensate for the €32 million one-offs that you had?

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

Well, there is a chance, if we do the calculations that we might overachieve in this year. However, the general overall goal is, as we, say, indicated previously, the key [indiscernible] (00:52:28) profitability steadily by 1% point per year and to have a figure that is for the time being above the same as the last digit in the current calendar year. So, this year would be a 4% target. And for next year, it would be a 5% target.

And yes, we had the onetime effects this year. It is not completely excluded that we have more onetime effects in the future. However, it is not that we have these because we need to kind of, say, make our result a little bit – look at little bit nicer. We are in, as I said, for the long term, the goal and the profitability goals, and we are working on several, say, aspects continuously that continue to improve the profitability in the future, including next year. So – and also to complete the picture and being completely honest, the environment, it's not making it really easier given the geopolitical changes and the general economic, say, environment in particular in Germany. However, the goal is still intact and we go for it.

Jean-Marc Müller
Founding Partner, CEO & Portfolio Manager, JMS Invest AG

Q

Okay. No, I understand that the, that the environment is not easy. I mean, I understand that. And there's not much you can do there except really manage your cost base hard. And I don't see that happening.

[indiscernible] (00:54:19)

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

...as we have a great diversity, there are so many things to do and we are addressing. Given one example, so we are seeing, you might not be aware and it's not probably, normally even worth mentioning is we are reducing the number of [indiscernible] (00:54:40)...

Jean-Marc Müller
Founding Partner, CEO & Portfolio Manager, JMS Invest AG

Q

Okay.

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

[indiscernible] (00:54:42) currently about in half that from what is I think 16 locations down to around 8 or 9, and further reduction to come. And there is about more than 1,000 people who live in these places are affected. So, it's not that we are not doing anything. It's not that – it is only that we are not, say, making provisions for the Big Bang that probably you would expect.

Jean-Marc Müller
Founding Partner, CEO & Portfolio Manager, JMS Invest AG

Q

Okay.

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

That's not going to happen.

Jean-Marc Müller
Founding Partner, CEO & Portfolio Manager, JMS Invest AG

Q

And I mean, I think you get this question quite often, but I mean, could you split the business, the medical and the safety business? Or are there I mean, do you see substantial synergies having those businesses together?

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

We do, we do. So, if we would grow for the short term, then we would split them and sell them both individually. However, as Dräger, overall serving many different stakeholders in particular and internationally, we have to make the experience that one Dräger company in a certain country be it France or say India, where I have just returned from a trip, that is why [indiscernible] (00:56:02) there it is greatly beneficial for Dräger to have a one company opposed to per country and legislation only one organization that has all the generic functions can be combined and that it's a lot more efficient. And it makes us track – much more effective as an employer and we get better people can give better service to our customers and then we can afford that, I mentioned earlier, you might remember the more specific capabilities in the sales channel in the countries based on this approach, it would be difficult if we split and then the individual entities become too small and are typical.

Jean-Marc Müller
Founding Partner, CEO & Portfolio Manager, JMS Invest AG

Q

Okay. Okay. Thank you.

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

You're welcome.

Operator: We have now a follow-up question from Christian Ehmann from the line of Warburg Research. Please go ahead.

Christian Ehmann
Analyst, Warburg Research GmbH

Q

Thank you. I was wondering about the effect of the silence from the FDA. How much how is the impact on your planned product launches for next year? Does this postpone any of your plans? Thank you.

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

Oh, there, currently, we do not see any impact on the product launches. And the lifting of the warning letter, unfortunately, it has to wait. To our information, the FDA is undergoing a heavy reorganization in itself, and that is why they can't be – we do not get answer to all our inquiries. So, very senseless to, say, setting up and scheduling dates for reinspection. There is no answer because they are busy with the reorganization.

Gert-Hartwig Lescow
Chief Financial Officer and Executive Board Member-IT & Vice Chairman-Executive Board, Drägerwerk AG & Co. KGaA

A

In fact, if I may add, for some of our approval processes that were in line with the warning letters we have received or have received positive replies with – we should know that to make that in terms of business impact. But it's a positive indication and it's one of the factors that gives us optimism that we will receive a positive answer, since on the product level we do – we have received over the past few months positive feedbacks on at least some of our approvals that we are with the FDA.

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

A

And there is no negative indication as such. As you said, there is little bit silence.

Operator: Thank you. We have another follow-up question from Alexander Galitsa from HAIB. Please go ahead.

Alexander Galitsa
Analyst, Hauck & Aufhaeuser Lampe Privatbankiers AG

Q

Yes, thank you for taking the follow-up. And just a housekeeping, on your interest expenses, I think your guidance is €20 million to €26 million. We've seen €12 million as of nine months and roughly €4 million per quarter. Just wondering, given that net debt also went down as of Q3, is there a reason why interest expense should increase substantially in Q4? Or you just are still being conservative, not adjusting the base part of the guidance?

Gert-Hartwig Lescow
Chief Financial Officer and Executive Board Member-IT & Vice Chairman-Executive Board, Drägerwerk AG & Co. KGaA

A

Mainly the latter. But please keep in mind that the interest expense also includes the interest expense for the pension obligations which are really set, if you will, to a regulatory type of mechanism. And they have not gone down significantly over that period.

Alexander Galitsa
Analyst, Hauck & Aufhaeuser Lampe Privatbankiers AG

Q

Okay. Understood. And just a quick one on the – I guess the further one-offs potentially in 2025. So, is there – generally should we expect more divestments of buildings? Or how big is the scope stoop for this sort of a clean-up, if you will, where you sell idle facilities, et cetera?

Gert-Hartwig Lescow A
Chief Financial Officer and Executive Board Member-IT & Vice Chairman-Executive Board, Drägerwerk AG & Co. KGaA

There are no comparable plans at this point.

Stefan Dräger A
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

Yes. As I previously said, there is no [indiscernible] (01:00:18) that could take into account. However, that does not mean that wouldn't be here [indiscernible] (01:00:23).

Alexander Galitsa Q
Analyst, Hauck & Aufhaeuser Lampe Privatbankiers AG

All right. Thank you.

Operator: [Operator Instructions]

Stefan Dräger
Chairman-Executive Board & Chief Executive Officer, Drägerwerk AG & Co. KGaA

Okay. If there are, at this moment, no further question, then in the interest of everybody's time, I ought to say thank you to all of you for being with us and for lively discussion that we had on the subjects, also from our point of view, that really matter. Thank you very much and have a pleasant afternoon. Thank you, and goodbye.

Operator: Ladies and gentlemen, the conference is now over. Thank you for choosing Chorus Call, and thank you for participating in the conference. You may now disconnect your lines.