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Full Year 2019 Draegerwerk AG & Co KGaA Earnings Call

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PRESENTATION

Operator

Good afternoon, and welcome to the conference call of Drägerwerk AG & Co. KGaA, which is now starting. At our customer's request, this conference will be recorded. You can listen to the recorded conference for the next 7 days by dialing +49-30-868-757-330 for German or +49 30-868-757-360 for English menu navigation. The PIN code for the replay service is 651270#.

The management presentation for the following conference is available on the Dräger homepage, www.draeger.com. Press Investor and there, you will find the presentation under Financial Calendar.

May I hand you over to Mr. Stefan Dräger, CEO of Drägerwerk AG & Co. KGaA, and the moderator of this conference.

Stefan A. Dräger ***Drägerwerk AG & Co. KGaA - Chairman of the Executive Board - Drägerwerk Verwaltungs AG***

Ladies and gentlemen, good afternoon, and a warm welcome to everyone joining us today on the phone or via the webcast online. I have with me today Gert-Hartwig Lescow, CFO; Tom Fischler, Investor Relations; and Peter Müller, Financial Communication. We would like to guide you through the presentation covering our final 2019 full year results, which we made available on our home page this morning.
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In January, we had already published preliminary results and our guidance for the current year. I will start the call with a high-level review of the main developments in 2019 and elaborate on key changes we implemented concerning the organization. [After this] we'll then go into the financial details of the group and the regions. Following the presentation, we will open the floor to your questions. Out of respect to everybody's time, we will end this conference in 1 hour.

So let's get started with a brief high-level overview on the business development last year on Slide 4. 2019 was a year in which the economy was struggling with high uncertainties. Again, the world economy grew at a lower pace than the year before. Nevertheless, we can keep our confidence look forward. Our markets are robust even in such an environment. Again, they have proven their resilience in terms of high uncertainties.

Net sales increased by some 6% and were even stronger than originally expected. Growth in 2019 was well balanced. All 3 regions and both businesses, medical and safety, contributed to this strong net sales cost. The development in safety was again exceptionally good with higher net sales coming from all product areas. This good development is also a result of the higher investments into specific sales capabilities over the last 2 years even if these investments currently still burden our profitability. Our full year EBIT is within our guidance. But in light of the higher-than-expected top line volume, our earnings development is a bit disappointing. Our profitability remains too low for Dräger's quality business.

Next to the low profitability, especially our order development in medical is disappointing and a lowlight in 2019. The America business remains our area with the biggest challenges and the focus of our restructuring activities. Unfortunately, we had a setback on the regulatory side with the FDA warning letter issued in January of this year. The warning letter relates to an FDA inspection that was conducted from August through September 2019 at the Dräger facility in Andover in Massachusetts. The letter is specific to the patient monitoring business unit and addresses the approval process we historically used in product changes. It refers to a specific regulatory filing process errors and lists deviations found in our quality management system.

It is not a warning against the use of a particular device, nor was a specific product found unsafe. No patients were harmed. The issue is receiving the highest attention from our side. We are in close coordination with the FDA to fully resolve all findings and concerns. We have provided a plan with corrective and preventive actions to address all issues outlined in the warning letter. The FDA will only consider the issues closed when we have concluded the agreed-upon actions and a reinspection has been successfully completed. At this point, we have no insight in when these activities will have been concluded. From today's perspective, we do not expect any adverse financial impact, which is not covered by our current guidance for 2020.

Despite this setback, we have made good progress in 2019 with innovation in our MEDICA business on our way to rejuvenate our product portfolio, which we consider a key on our way to improve profitability of the (inaudible). We successfully launched our new anesthesia family, Atlan, which is very well received by our customers. And quite recently, we took another important step and launched our new Evita ventilators. A big series of activities was the reorganization we finalized during the year, something I will explain in more detail on the following page.

Now on Page 5, sometime ago, at the beginning of 2016, we already went through a change in our governance model, giving more power to the regions and countries with one single person responsible and in charge for each unit and shifting much of more decision power to the region, empowering the local entities to operate as entrepreneurs. This has proven to work well. Therefore, we are keeping the One Dräger global sales organization structured according to the existing regions: Europe, Americas and AAA. Clearly assigned responsibilities lead to high customer orientation, dedication and entrepreneurship. The only aspect we have changed here is that now all 3 regions are reporting to one Chief Sales Officer on the Board level, Reiner Piske.

Next, to the global sales performance. Additional responsibilities are allocated here, like the global key account management and other sales-enabling functions. This is the first pillar of the new Dräger organization. The other 2 pillars, our medical and safety, to strengthen our organization at our headquarters in Lübeck regarding our medical business and our safety business. Here in our headquarters, we have become too remote and to disconnected from our customers and business needs. We have, therefore, introduced -- reintroduced business responsibilities for our medical and safety business, both divisions headed by a Board member, Toni Schrofner, heading the medical division; and Rainer Klug, heading the safety division. The divisions have full responsibility for the product. Product marketing, product development, their respective supply chain and the quality assurance are all in the sole responsibility of the medical or safety division. What they do not have is the sales and service responsibility. These resources are allocated to the first pillar, the global sales and service organization.

Now on Page 6. To allow the divisions to deal with the different nature and diversity of their respective customer base, we have chosen to slightly -- 2 slightly different structures for medical and safety. On this slide, we have illustrated the structure of the safety division.

In our safety business, we are serving customers from many different markets and industries, each with specific customer requirements. We have, therefore, defined 3 business fields that each have similar set of requirements when it comes to preferred sales channels, business mechanics, supply chain and key products they require. The first business field is processing industries. It combines customers from industries like oil and gas, chemical, pharma and others. These customers are often multinational, global industrial companies that share the same demanding approach towards safety. They see safety as a relevant and integral part of their operational strategy. They are interested in safety outcome in general, not only in a mask or in a single device, and avoidance of operational downtime as well as a very broad safety approach. No occupational accident disease or harm is of interest. Many of them are following a Vision Zero approach. That means designing their processes and workplaces to reach a level of 0 accidents. These customers require high-value service offerings even with outsourcing and OpEx-oriented business model. Many of these customers are served best directly through a global key account management organization with high consulting expertise.

Product-wise, the gas detection business, mobile and fixed gas detection, is the most relevant for these customers. We have, therefore, given this business field the responsibility for managing these products.

The second business field is manufacturing industries. This cluster is characterized by a broad range of industries that look at safety more from a compliance perspective. Often, these customers are small and medium-sized enterprises. They want to make sure that they meet the safety regulations, e.g., the requirements regarding personal protection and equipment needed for a specific job. Easy access and fast availability are key success factors to meet this requirement. In many cases, indirect distribution through channel partners is the best choice, but also digital distribution channels will become more important in the future. Product-wise, PPE, personal protection equipment, and licensing protection are managed in this business field.

Last but not least, the third business field is emergency and rescue services, a combination of customers from fire services, mining, defense and law enforcement. These customers are predominantly public authorities like fire departments or police authorities. Sourcing by these customers is often financed from governmental public buckets through tender processes and within standard fiscal budgeting frames. So for us, that means to focus on norm and regulation-driven technical requirements. Product-wise, heavy breathing equipment is one of the key products for these customers and, hence, these products consequently will be managed in this business field. The safety division is best served with continuing the functional setup in R&D, production and quality assurance, therefore -- and to minimize complexity, these responsibilities will not be included into the management of the business field.

Now I turn to the medical division on Page 7. In the medical division, we basically have only one vertical segment, the hospital with focus on acute care. One thing is a top priority of any hospital, patient outcome. Hospitals aim for providing the best medical outcome for their patient. But too often, the clinical teams cannot access all the information that is required to make the right decision for the planning and execution of therapy. If important medical information is missing, this can lead to clinical errors, which can have catastrophic consequences. The reason for the limited availability of the necessary data are the missing standardization and the limited security of communication protocols.

We at Dräger are always thinking about improving acute care, and we envision a future in which medical devices are connected as a system and are interacting with one another and enabling new clinical applications like visualization of data, remote control, decision support and ultimately, automation in a safe and secure environment. That's why in the past couple of years, we invested in the implementation of a new network-based communication protocol and data infrastructure that securely connects medical devices and clinical information sources.

indiscernible], the roof of IEEE as a standard setting board, a family of communication protocols for medical devices was introduced.

SDC, service-oriented device connectivity, and Dräger contributed significantly to the development and introduction of this new standard. The main purpose of SDC is to enable manufacture independent medical device-to-device interoperability. With this secure connection of medical devices and with the access to clinical data, we will develop software applications for clinical decision support and algorithms for the automation of therapy to reduce the risk of medical errors and to reduce the stress and burden of the clinical test. We will also provide the infrastructure and tools to access our products remotely to continuously monitor their conditions, keep their software up-to-date and thus guarantee uptime and highest quality along the entire life cycle.

Now on Page 8, where we're still in the medical division, in the mid 2019, we have reached a big milestone on our path to offer devices with connectivity, that is the launch of the anesthesia family, Atlan. The Atlan is an ergonomic can-do-all anesthesia workstation. The Atlan family is well received by our customers. And this is our first device with built-in SDC capabilities.

Beginning of this year, we took the next important step on our journey to rejuvenate our product portfolio. We launched our new Evita ventilators with V600 and V800 and the VN versions for neonatal marks. Over time, they all will be using SDC as the protocol to include connectivity functionalities. The Atlan anesthesia product family and the Evita ventilators demonstrate our continuous efforts for improving clinical outcomes and patient safety by connecting medical products and software-based tools to smart solutions in acute care. These and other solutions are part of our road map that we will be focusing on in the coming years. I am convinced that these additional investments we are making into our innovation road map will bear fruit and drive our market success in the years to come.

On Page 9, the medical division. The medical division will operate in 5 business units. Each business unit forms a group of employees that are fully dedicated and passionate for their product and the customer needs associated with the type of business. The largest business unit, in terms of net sales and employees, is the business unit therapy. This BU combines our traditional core business, the business with anesthesia devices, ventilators and thermoregulation equipment. This is an area where we have strong market positions and long-standing business relationships. The unit operates from our allocations in Lübeck, Shanghai and Telford in U.S.

In patient monitoring, we currently do not have the same strong market share like in the other therapy product areas. So here, the challenges are different. That is why we are organizing the management of this business in a separate business unit. Patient monitoring is an essential part of our hospital strategy. It will be focusing on driving forward network systems in close cooperation with the business unit therapy and also with the business unit IT and systems, the next business unit on the chart.

The BU IT and systems will be focusing on developing and marketing new digital and data-driven services. That means software applications and system products that work on or with our therapy devices as well as pure software solutions. This is a business that, today, does not have a similar net sales share like the other business units, but it is a strategic growth area, which will build new business models, asset-light and technology-intensive, as the interface of devices to IT systems. This business unit will operate in Lübeck and over in Telford.

The business unit WPI, workplace infrastructure, combines supply units, medical lights and gas management systems. This is predominantly project business with special business mechanics as the result, becomes part of the customers' real estate. Therefore, it makes sense to manage this business separately. Next, to the operations here in Lübeck. The business unit will also use our plant in Shanghai and our facility in India to better cater for the needs of customers from emerging markets.

And finally, the business unit, hospital consumables and accessories, focuses on the fast-turning business with device-specific and generic consumables and accessories. The requirements from customers in this business are very different compared to the device business. Fee for being successful is an efficient supply chain to guarantee high availability. This is also one of the reasons why, unlike to the structure and the safety division, we have included the full responsibility for the supply chain into the business units.

Management of the business unit has full decision power to design the supply chain according to the needs of their respective business. To sum it up, we believe that the setup chosen for our medical and our safety business together, the one sales and service organization, is the best solution for Dräger. It will facilitate the improvements that we are working on, and it will enable us to achieve the goal of being first choice for our customers by having the right diversity and specific channels to serve our customers and market and still benefit from synergies and scale effects where diversity does not add value.

In the headquarters in Lübeck, we are introducing a clear allocation of responsibilities, small patient groups that are driven by a responsibility for a defined product area and a high degree of identification across the various functions within the respective unit. Teams with clear goals, increased visibility of individual contribution and team success will reinforce customer focus. In the regions, we are keeping the empowerment, which we introduced in 2016 and which has proven to work well.

Now I would like to turn it over to Gert-Hartwig Lescow for more color on our financial performance. Gert-Hartwig, please.

Gert-Hartwig Lescow ***Drägerwerk AG & Co. KGaA - CFO, Executive Board Member for IT & Vice Chairman of Executive Board - Drägerwerk Verwaltungs AG***

Thank you, Stefan, and good afternoon, everyone. Please note that my comments today will be on numbers net of currency effects whenever I refer to growth rates, as usual. Let us start with a quick review of the Q4 development of the group.

As in prior years, the last quarter of the year was the strongest quarter in terms of net sales volume and profitability. Order entry increased by 2.1%, driven by higher orders in safety. Medical was slightly negative on the back of a very high order entry in the prior year's quarter. Driven by a strong development in Europe, our group net sales increased by roughly 1% over the record Q4 last year and reached EUR 882 million. Both medical as well as safety reported high net sales volumes. As usual, the fourth quarter also had the highest earnings contribution of the year. But despite the roughly EUR 20 million higher time volume in the quarter, EBIT stayed below last year's level. Slightly lower gross margin and the increased cost base below gross profit led to a lower Q4 EBIT of just below EUR 70 million compared to last year's EUR 104 million.

The higher cost base is very much driven by some one-offs during the last quarter. I'll get to that in a minute.

Changing the view to the full year results now. Order entry for the full year increased by 2.8%. Order growth was continuously positive throughout the quarters, but order growth stayed behind the very strong net sales development throughout the year, which increased by just below 6%.

Looking at the quarterly seasonality, the first quarter sticks out with a very strong net sales growth rate of more than 20%. Our growth rate in Q1 was significantly impacted by a weak comparable basis in Q1 2018 when we had some delivery disruptions. Orders on hand are only slightly above the prior year's level. This is also one reason why we are somewhat more cautious on our growth expectations for the current year. The currency-adjusted net sales growth of 5.9% translates due to some FX tailwinds into nominal growth of 7.2%. The euro lost value against the U.S. dollar during the year, which has a positive impact on the top line but a negative impact on Dräger's earnings. The euro exchange rate developments towards currencies from emerging markets was diverse, so that in total, currency fluctuations in 2019 had only a minor relevance for Dräger's EBIT. The positive top line development translates into an increased gross profit contribution. The gross profit margin was stable at 42.7%. Our functional expenses increased at the same rate as net sales. I'll provide some details on this in a minute.

The other financial result of minus EUR 4.4 million had a slightly negative impact of about EUR 1 million in the year-over-year comparison. As a result, our full year EBIT of EUR 66.6 million is roughly only on the level of the prior year's EBIT. The margin was stable at 2.4%.

Coming to the P&L below the EBIT line. The interest result declined year-over-year by roughly EUR 6 million, which was mainly driven by IFRS 16, and the tax rate was slightly lower at 31.8%. As a result, net profit is just below EUR 34 million. The primary metric with which we steer our business is the Dräger Value Added, the DVA. The DVA at the end of the year was negative at minus EUR 32.7 million, a decline by EUR 6 million. The only slightly improved EBIT faces a more pronounced increase of the capital cost. 2019 capital costs were up relative to the prior year as a result of the higher average capital employed, the strong increase of the average capital employed of some EUR 145 million is primarily due to the first-time application of IFRS 16.

On the following slide, Page 12, we provide details on the key development of the financial expenses. On a nominal basis, our functional cost increased at the same rate as the net sales by 7.2%. Currencies had an unfavorable impact on the cost base. On a currency-adjusted basis, our functional cost increased by 6.4%. Functional expenses include some one-offs in the amount of roughly EUR 15 million. The one-offs include some EUR 6 million restructuring charges and close to EUR 10 million write-offs of receivables from the Middle East region. Excluding these, the cost increase is just below 5%.

Looking at the development in the different functions. Sales and marketing expenses are up by 3.9% over the prior year. In several countries, we are implementing new go-to-market strategies that require upfront investments into personnel. Hence, the increase is driven by our investments into specific sales capabilities and capacities in countries like China or the United States. These investments will put us in the position to better exploit the potential of these markets in the coming years. In line with our guidance, our R&D expenses increased by 3.3% to roughly EUR 264 million. The R&D ratio improved slightly to 9.5% of net sales. The expense growth for R&D will possibly go up in the current year. We are ending with an R&D budget of between EUR 275 million to EUR 290 million. The highest expense increase is in the administration functions, which increased by 10%. But this cost increase includes aforementioned one-off costs. We do not expect any further restructuring charges during the current year. Excluding the cost, the admin cost increased in line with net sales. The SG&A ratio has slightly improved to 30.3%.

As communicated before, we have negotiated an agreement with our labor representatives to limit the further cost increase through a salary waiver for the next 3 years for the German workforce. This agreement will reduce the personnel cost. If we use -- review this period, of course, the German workforce will not immediately receive the collectively agreed salary increase. Instead, the salary of these employees will return to the collectively agreed salary level in 2023 only. Depending on the success of the current restructuring and Dräger returning to higher profitability levels again, employees would receive an additional variable compensation for accepting the salary waiver for the period of 2023, '24 and '25.

Moving on to some key financial ratios for last year. Cash generation in 2019 was much stronger than in the prior year. Dräger managed to improve free cash flow by more than EUR 162 million, delivering a positive free cash flow of some EUR 102 million. A high cash flow from operating activities is the key driver with an improvement of some EUR 160 million. Operating cash flow delivered an inflow of roughly EUR 165 million versus a cash inflow of some EUR 4 million 1 year ago. This positive development was supported by an improvement in DSOs. Receivables have remained stable despite the substantially higher sales volume. In the prior year, receivables had increased by more than EUR 40 million. Also, the increase of inventories was below last year's level with positive effects on cash flow. Next to that, the introduction of IFRS 16 had a positive impact on the operating cash flow of roughly EUR 30 million.

Cash outflow for investments was the largest level was mainly related to replacement investments. Also, in the current year, the guided investment volume between EUR 85 million and EUR 95 million comprises mainly replacement investments. Liquidity has increased by some EUR 17 million, mainly to the positive free cash flow and amounts to close to EUR 200 million. Net financial debt has increased to EUR 88.7 million, corresponding to a net financial debt-to-EBITDA ratio of 0.5%. Leverage of the group remains uncertain.

The implementation of IFRS 16 had a strong effect on net financial debt. And the strong year-over-year increase in the net financial debt of some EUR 45 million has mainly to do with the different treatment of leasing contracts under IFRS. On a comparable basis, net debt would have improved by more than EUR 60 million compared to the same period last year. The equity ratio decreased by close to 3 percentage points. The main factor was the extension of the balance sheet triggered by IFRS 16, responsible for roughly 2 percentage points of the lower equity ratio. The second effect comes from the adjustment of the interest rate used for discounting pension liabilities from 1.75% to now 1.5 -- 1.1%. The equity ratio at the end of the year stood at just below 42%. Under the assumption of full distribution, the earnings per share for the common share is EUR 1.38 after EUR 1.42 in 2018. The EPS of the preferred shares is EUR 0.06 higher at EUR 1.44.

On the next 3 pages, we take a look at the development within the regions, starting with the region America on Page 11 (sic) [14]. First, let's take a look at the Q4. Order entry in the region Americas was slightly negative with minus 1.2%. This must be seen in light of a very demanding comparable figure. The same is true for net sales. Net sales development in Q4 2019 is nearly 10% over the last quarter and the prior year. This comes from both areas, medical and safety. In line with the lower volume, gross profit also declined by a similar margin. When we now shift to take the full year view, we can see that the full year figures are more favorable than the Q4 development. For the full year, the entire region Americas showed currency-adjusted top line growth of some 1.5% for order entry and some 6% for net sales. Due to the FX tailwind, the nominal development is more positive. On a normal basis, order entry increased by some 5%, and net sales in the region Americas increased by close to 10%. Both business areas, medical as well as safety, developed favorably in terms of net sales.

Slightly different picture with order entry in medical orders -- in medical, orders declined by 1%. But to be fair, the comparable figure order and growth in the prior year was quite high. Important areas like anesthesiology and ventilation had increased by some 10% in 2018. These growth rates could not be repeated in 2019. On the safety side of the business, orders increased in nearly all product areas, resulting in to total growth rate of 7% for the full year. Due to the strong net sales increase compared to the prior year, the gross profit in the region Americas increased by close to 11%. The gross profit margin increased as well by 0.4%, with only slightly higher functional expenses. Their profit contribution -- or the EBIT of the Region America improved by some EUR 16 million, but EBIT remains in negative territory. It was minus 14.2% -- EUR 14.2 million at the end.

Moving on to the region Europe, the region that, from a volume perspective, is our largest region by far, accounting for more than 50% of group net sales. Hence, the development of Europe is of higher importance for the business performance of the Dräger Group. Fortunately, we have the quite success -- we've quite a successful year in the region. Again, let me start with some comments on the Q4 development.

The region Europe had a very strong year-end business. Order intake in the fourth quarter increased by more than 7%. Both medical and safety contributed. Net sales development was similarly positive with an increase of 6%. The development in Germany was particularly strong. For the full year, the top line improved by some 5%. Orders are up by 5.5% and net sales increased by 5.1%, whereby safety developed more favorable than medical. In medical, especially order entry for our anesthesia devices was favorable. Europe is a market where we have already introduced the new Atlan anesthesia family, which is very well received by our customers.

Total orders in the medical business increased by about 2% for the region. Safety increased its order entry by an impressive rate of more than 10%. Order growth for Dräger's safety offerings was particularly strong for gas detection systems and business we have invested into in the last 2 years. But also, all other products areas increased their order volume compared to the year before. Despite the higher net sales volume, profitability has declined. The slightly lower gross profit margin and higher functional expenses overcompensate the effects from the higher net sales volume. Higher functional expenses are in light of the investment into marketing and sales. For example, in Germany, Italy or the U.K., EBIT declined by roughly EUR 40 million to EUR 68.5 million, which corresponds to an EBIT margin of 4.6%.

Coming to the purchase region AAA, Africa, Asia and Australia, first, as -- previous to the view on the development in Q4. In the prior year's Q4, in 2018, AAA region had a very strong performance. Order intake, an increase by some 20%, especially on the medical side of the business. Net sales at that time was -- were very strong as well. In light of this very demanding comparable basis, order entry in Q4 declined by some 6% year-over-year. Also, net sales only reached a slightly lower level than the year before. Let's take the view at the full year. Due to the weaker year-end business, currency-adjusted order entry of full year 2019 declined by 1.6%. From a geographical point of view, for the second year in a row, China was the main growth contributor. On the other side, demand from some countries in the Middle East overcompensated this impact. Within the region, it was, again, the safety area that demonstrated a very solid order growth with some 11% higher orders. Nearly all safety products contributed, with particularly strong demand for our gas detection solutions.

In medical, orders stayed below the high comparable order figures of the prior year, quite a different picture when it comes to net sales development. Both areas, safety and medical, increased volume. Medical grew by some 5% with nearly all product areas contributing to growth. In safety, net sales increased by an impressive 13.5%. Both areas combined add up to some 7.6% growth for the group in AAA. The high net sales volume resulted in higher profit contribution and also the improved gross profit margins. Working against a more pronounced increase in profitability is the fact that AAA is the region with the highest increase in functional expenses. In line with our investment program, we have increased investments in our -- into our marketing and sales organization, especially in China. In addition, as mentioned before, we had some write-downs on receivables in the Middle East region, broadening our Q4 earnings. In consequence, despite the higher net sales volume, EBIT only slightly improved to EUR 12.4 million.

From this year onward, we will be reporting the business development according to the newly formed medical and safety divisions. Please note that we have extensively reorganized department in light of the introduction of the medical and safety divisions, while in the last couple of years, a large portion of costs were allocated via net sales key to medical and safety. The cost allocation now is much more direct, more accurate. Unfortunately, this limits the comparability of year-over-year figures below the top line. Please have this in mind when analyzing the year-over-year developments.

So let's now take a look at the 2019 business figures according to the new divisional structure, starting with the medical business on the next page. Order entry in medical slightly declined year-over-year. The decline is mainly due to the lower demand from the AAA region where especially, some countries in the Middle East have placed substantially lower orders compared to the prior year. The region America is slightly below the prior year as well. In Europe, we were able to increase our order volume by some 2%.

A more favorable picture when it comes to net sales. Medical sales increased by some 5% year-over-year, all regions above the prior year's level. Also, nearly all product areas have increased net sales, especially strong development in the area anesthesia and thermoregulation as well as in medical services. The gross profit margin slightly improved. Nominal functional expenses increased at a slightly lower rate than nominal net sales. In consequence, medical EBIT improved to EUR 13 million corresponding to a still quite low EBIT margin of below 1%.

Moving on to safety. 2019 was a very strong year for safety. Order entry increased by more than 10%. All regions contributed to this very solid growth rate. Only the Americas region grew by a somewhat lower margin, but this has to do with the exceptionally strong prior year's growth of more than 50%. Looking at order growth from a product angle, growth was fueled by very strong demand for our gas detection products and also for respiratory and protective systems, like SCBAs, but all other product areas contributed as well.

A similar picture for net sales development, growth in all regions and in nearly all product areas. Only engineered solutions did not contribute to the growth, but engineered solutions is a project business, which can be quite lumpy. The gross profit margin was slightly lower than last year. Functional expenses were up quite strongly by some 10% on a nominal basis. This is the result of our investment program. In several countries, we have been investing into our sales capabilities and capacities, especially on the safety side of the business. These higher expenses have burned the profitability so that EBIT has slightly declined year-over-year. We remain confident that with our very competitive product portfolio and with these investments into our sales force, we will be able to grow the business and return to higher profitability in the future.

That's it for the financial overview. Back to you, Stefan.

Stefan A. Dräger ***Drägerwerk AG & Co. KGaA - Chairman of the Executive Board - Drägerwerk Verwaltungs AG***

Thank you, Gert-Hartwig.

Coming to our dividend proposal and outlook. Our dividend policy is to distribute at least 10% of group net profit to our shareholders and participation certificate holder. Consequently, we will propose to the Annual Shareholders Meeting in May, EUR 0.13 for a common share and EUR 0.19 for a preferred share. The dividend is on the same level as last year.

Before we get to the end of the presentation, we share with you our outlook and the guidance for 2020. At this time, I want to comment on the current impact from the coronavirus on our business. In an economical sense, the coronavirus results in chances and risks for Dräger. On the risk side, there are potential disruptions of our own operations in China and beyond. We have more than 800 people working in China and have 2 development and production sites. Next to that, there is generally also the risk of disruptions in the supply chain if suppliers can no longer deliver material we require. So far, these risks are still manageable. Our facilities are operating, and shortages from our suppliers are mitigated. In addition, there is the risk of a global economic downturn that will not go unnoticed for our business.

The coronavirus also offers opportunities for Dräger. They are mainly in 2 areas. Demand for light breathing protection is currently very strong and exceeds our production capacity. This can be considered windfall profits. However, the product lines affected are only a small portion in our safety product portfolio. The demand for intensive care ventilators has increased, especially from our Asian customers. We consider this demand largely as advanced spending planned for the coming year being pulled forward and not sustainable. So in total, the economic effects for the first quarter will be positive but definitely no reason to change the view on the full year. It helps to mitigate the downside risk coming from the regulatory side. We, therefore, reiterate and confirm the guidance we communicated in January.

Economic uncertainties around the world remain a key risk. Dräger markets tend to be quite resilient against economic downturns, but the modest economic outlook makes us a bit more cautious when it comes to the expected demand development for the current year. For 2020, we expect net sales growth of 1% to 4% net of currency effects. From today's perspective, we do not expect a relevant impact from FX. Nominal growth should be on a similar level as the currency-adjusted growth rate this year.

We do not see big improvement potential for the gross profit margin in 2020. Only after new products gain more volume, we should be able to see an improvement in the gross margin. Hence, we expect the gross margin to remain on the 2019 level, plus/minus 1% point, around 43%.

We expect the full year EBIT margin to be in the range between 1% and 4%. You can find some additional guided figures like investments, R&D budget, et cetera, in the appendix of our presentation. All guided figures are based on the assumption of stable currency exchange rates at the beginning of the year.

With this, I would like to end the presentation and open the floor for your questions. Please, the floor is yours. Ask your question now.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And we have the first question. First question comes from Mr. Oliver Reinberg from Kepler Cheuvreux.

Oliver Reinberg ***Kepler Cheuvreux, Research Division - Head of Med Tech Equipment & Services Research***

Can I actually just expand a bit on the coronavirus discussion? I was a bit surprised that you said like you so far only see ventilator demand from Asia. I think the U.S. just actually made budgets and funds available for purchase. Can you just provide a certain outlook like what kind of global demand do you expect? And so what kind of ability do you have to increase your capacities here?

My second related question, do you see any kind of -- as part of this crisis, any kind of effects where hospitals are going to delay investment decisions because, obviously, the focus is currently on the corona challenge?

And final question, I mean, so far, it's mostly probably in Asia, but is there a risk that your service business may be impaired by the fact that your people can't walk into the hospital [that it's on]? And if that is the case, how will that actually work financially? Do you have a kind of contract in place where you get fixed revenues anyway? Or would this kind of a lost service hours impact the business?

Stefan A. Dräger ***Drägerwerk AG & Co. KGaA - Chairman of the Executive Board - Drägerwerk Verwaltungs AG***

We'll start with the last question. The -- we are continuing with our service in all parts of the world including China and the most affected regions. Our people work day and night to keep up our products and equipment in like Wuhan. We see it exposes our responsibility and also an opportunity to, say, strengthen the trust that our customer has in us to support our customers in saving people's lives that have become seriously ill with lung diseases. So -- and we protect our people that are providing the service in these areas with the respective protection equipment that we both manufacture ourselves, in some parts, we buy in. So the -- there should be no negative impact on the service business.

Your first question was on the -- on the U.S. sales pressure of ventilator, that we have to look in what it actually is. So I'm not familiar with the details to -- at this point in time. In general, there is -- so not much room to increase the capacity for the production. It's already at this point in time, running at a much higher pace than it usually does. And that -- so the bottleneck is in, say, testing equipment that cannot be increased on a short notice. So that would take for, I would say, almost 0.5 year to 1 year to increase that capacity.

And also the supply chain, you would not be able to sustain even the current rate for a prolonged period of time. So -- and that is, you can safely assume the same with all manufacturers worldwide. So -- and even more, say, a clinical capacity situation, as you are I'm sure you're fully aware with light breathing protection, where our production capacity is limited by the respective machinery. And new machinery has like a lead time of a year. And all machines are running at full capacity and the production is sold out until August. So -- and to your second question, Oliver it was...

Gert-Hartwig Lescow ***Drägerwerk AG & Co. KGaA - CFO, Executive Board Member for IT & Vice Chairman of Executive Board - Drägerwerk Verwaltungs AG***

Delay from investment (inaudible).

Stefan A. Dräger ***Drägerwerk AG & Co. KGaA - Chairman of the Executive Board - Drägerwerk Verwaltungs AG***

Yes, investment delays, that might happen. We don't see that yet. It might very well happen later in the year. It is still very unclear at this point in time. It would further, say, development of the disease will be when it will peak in what part of the world. So we have seen models from -- that has been developed on similar scenarios already some years ago that predict that the peak maybe as late as 300 days after the beginning. So we will see.

Oliver Reinberg ***Kepler Cheuvreux, Research Division - Head of Med Tech Equipment & Services Research***

Great. That's very helpful. And can I just ask -- can you remind me the general service structure or the nature of this contract? Is this actually bid by -- or do you have a kind of framework in place where you have a kind of annual fee and that actually covers all services?

Stefan A. Dräger ***Drägerwerk AG & Co. KGaA - Chairman of the Executive Board - Drägerwerk Verwaltungs AG***

Well, several different models exist. We have to bill by the hour. We have service contract. And then we also have managed services that includes, not only our devices, but all medical equipment in the respective hospitals. So different models exist.

Operator

And the next question comes from Mr. Aliaksandr Halitsa from H&A.

Aliaksandr Halitsa ***Hauck & Aufhäuser Privatbankiers AG, Research Division - Equity Analyst***

Maybe just again on the virus outbreak-related ones. What is your best guess? I guess, you should have pretty good visibility in terms of revenue -- incremental revenue you're going to generate in respiratory masks, given that the capacity is fully booked? And also maybe more on the ventilator side, how -- what is the situation with the capacity there and if you also see it's fully booked? And if so, what is then the incremental revenues that come in on top of revenues you generated in 2019? That would be the first one.

Stefan A. Dräger ***Drägerwerk AG & Co. KGaA - Chairman of the Executive Board - Drägerwerk Verwaltungs AG***

Well, to give you a rough figure. The share of the light breathing protection, it's actually, we're talking about the so-called FFP mask or filtering face pieces. Last year, it was 0.3% of Dräger revenue was with this product line. So even if you assume it doubles this year, then there is a very limited effect on this one.

The ventilation is probably the opposite side. This type of ventilator that is currently in high demand for these markets in Asia that require support that has a built-in turbine, that it does not require a central gas supply system from the hospital, this line of ventilator has a share of approximately close to 3% of our annual sales. So that's probably as high as any product would get in Dräger.

No other product has more share of our revenue than 3% that's why we have this great diversity that have -- makes us very resilient in times of crisis. So it also limited the upside effect we have as the capacity is -- as I described in the answer to Oliver in his question, already so -- at the limits now and cannot be expanded short term. It's not possible to convert other production lines if there's a reasonable effort and time frame to become ventilator lines.

Aliaksandr Halitsa ***Hauck & Aufhäuser Privatbankiers AG, Research Division - Equity Analyst***

So if I -- do I understand it correctly, last year, you would make 3% of revenue, so roughly EUR 80 million with those ventilators? You're saying is that in 2019, despite higher demand, you couldn't squeeze out more than that, assuming that the prices remain stable?

Gert-Hartwig Lescow ***Drägerwerk AG & Co. KGaA - CFO, Executive Board Member for IT & Vice Chairman of Executive Board - Drägerwerk Verwaltungs AG***

No. Let me -- that's not what we meant to say, but thanks for the opportunity to clarify. Firstly, of course, as Stefan Dräger said, our overall net sales from ventilation product is higher than the 3%. We are focusing here on those type of products, which are relevant for the customer in the situation at hand. And we will see an increase in that category.

And given that we are starting from a base of about 3% of net sales, there could be a double-digit increase within that category, and that translates into a similarly increase for the group. So it could mean for the group, but then if you take the rate, it could mean for the group a contribution to growth, which could be up to 1% or even 2 percentage points for the group. But that has to be kept in mind against the other risks that we also talked about.

Stefan A. Dräger ***Drägerwerk AG & Co. KGaA - Chairman of the Executive Board - Drägerwerk Verwaltungs AG***

That the risk affects 100% of the revenue.

Gert-Hartwig Lescow ***Drägerwerk AG & Co. KGaA - CFO, Executive Board Member for IT & Vice Chairman of Executive Board - Drägerwerk Verwaltungs AG***

Again, why we did not add 1 or 2 percentage point to the net sales guidance for the group. Of course, you could do that a few -- I mean, if you add the math, you could add up the chance to get it from 1% to 4%, but it is included also in our chance to get to the high end of our guidance in spite of the risks we see not only from corona -- supply chain is the key word here -- but also from other areas like the pending approval of some of our products in the U.S.

Stefan A. Dräger ***Drägerwerk AG & Co. KGaA - Chairman of the Executive Board - Drägerwerk Verwaltungs AG***

One other thing is, I think, worth mentioning here, the prices at what we sell. So despite the other, say, news spread in the conventional media they remain stable so -- and I am very sure that the other investment goods manufacturers have no -- are not different, not any different here. So the best -- what happens is that we sell at list price with no discount, we don't double or triple the prices here. And we do have higher freight expenses because it's more difficult to get the product out to China at this point in time. It also cost more to get air freight space.

Aliaksandr Halitsa ***Hauck & Aufhäuser Privatbankiers AG, Research Division - Equity Analyst***

Okay. Understood. And then maybe to follow on. You mentioned that you're going to be spending more on the IT infrastructure as compared to last year. Is that a meaningful amount more? Or is it not as material?

Stefan A. Dräger ***Drägerwerk AG & Co. KGaA - Chairman of the Executive Board - Drägerwerk Verwaltungs AG***

IT?

Aliaksandr Halitsa ***Hauck & Aufhäuser Privatbankiers AG, Research Division - Equity Analyst***

Higher IT cost?

Gert-Hartwig Lescow ***Drägerwerk AG & Co. KGaA - CFO, Executive Board Member for IT & Vice Chairman of Executive Board - Drägerwerk Verwaltungs AG***

It's not a meaningful amount up and beyond. I'm not sure what...

Stefan A. Dräger ***Drägerwerk AG & Co. KGaA - Chairman of the Executive Board - Drägerwerk Verwaltungs AG***

you exactly refer to from -- it does not say -- we don't break our head on that. That's nothing special.

Operator

(Operator Instructions) One more question coming from Mr. Aliaksandr Halitsa.

Aliaksandr Halitsa ***Hauck & Aufhäuser Privatbankiers AG, Research Division - Equity Analyst***

Sorry, one follow-up, if I may. Maybe on the 2020 outlook, in general, given that it has been provided with preliminary results and since then, a lot has happened. If back then, the midpoint was kind of your base case outlook, how do you assess the current situation?

Are you now leaning more towards the lower part of the range? Or maybe the opposite is the case that you are more optimistic on the intake that you are seeing in products relevant for the outbreak? And then you say that maybe now the odds are actually the upside, if you could give any comments on that?

Stefan A. Dräger ***Drägerwerk AG & Co. KGaA - Chairman of the Executive Board - Drägerwerk Verwaltungs AG***

Yes, so intentionally, we gave you a wider bandwidth this time because there is more uncertainty, and we can't tell and we don't know.

Gert-Hartwig Lescow ***Drägerwerk AG & Co. KGaA - CFO, Executive Board Member for IT & Vice Chairman of Executive Board - Drägerwerk Verwaltungs AG***

If anything, if I compare the situation today, I would probably say, the standard deviation is higher than -- or at least appears higher than it would have appeared, certainly 12 months ago and even 2 or 3 months ago and the impact on the expected value is not significant compared to that.

Aliaksandr Halitsa ***Hauck & Aufhäuser Privatbankiers AG, Research Division - Equity Analyst***

Okay. And maybe lastly, on the currencies. We have seen that over the last -- quite recently, some major export market currencies have spiked, so basically you lost in value compared to euro. If that persists as this dynamic, what would you expect the, yes, the influence would be on the Dräger Pac earnings? And maybe you could, in this context, update us on your current hedging situation.

Gert-Hartwig Lescow ***Drägerwerk AG & Co. KGaA - CFO, Executive Board Member for IT & Vice Chairman of Executive Board - Drägerwerk Verwaltungs AG***

So given on the current situation, the impact would still be negligible. So we're talking 10, 20 basis points or so on the EBIT margin. What we do is besides the natural hedge, which we have, due to our own sales and service infrastructure, summarizing, we are, of course, long most currencies with the exception of the U.S. dollar, where we are on an EBIT basis short and the British pound, where we are roughly balanced.

The remaining exposure, we hedge on a case-by-case basis. Most currencies, typically currencies with a cost of carry between 5% and 10%, we do hedge around 80%. Across currencies with a cost of carry in excess of 10%, ee only hedge on a case-by-case basis. For example, the Argentinian peso, we do not hedge because it is -- we deem it excessively expensive. And that leads to an overall hedging situation of the exposure of roughly 50% to 60%.

Operator

Mr. Oliver Reinberg Kepler has one more question.

Oliver Reinberg ***Kepler Cheuvreux, Research Division - Head of Med Tech Equipment & Services Research***

Actually, coming back to the ventilation discussion. So basically, what you're saying is you only see increased demand for one of your ventilators, but the majority of your ventilator portfolio at this stage does not see any benefit? Is that correct? And if that is the case, why is that actually the case? Is it simply because Asia just buys lower or value equipment? In fact, I think when the would not.

But in theory, in other parts of the world also the demand for the rest of your ventilation portfolio should be stronger. Is that way of thinking correct? Any color would be appreciated.

And then I heard from one of your competitors that they basically hold of you -- I mean, I would not speculate this, but that they say this crisis, to some extent, may trigger certain rethinking. So we have seen over the last decade a certain investment backlog in Europe overall. So now this crisis, to some extent, shows the limitation that even the developed healthcare system in Europe actually face.

So probably early to say, but the discussion is could that actually, overall, increase to somewhat higher in spending into hospital CapEx infrastructure? If you have any thoughts on that, it would be great.

Stefan A. Dräger ***Drägerwerk AG & Co. KGaA - Chairman of the Executive Board - Drägerwerk Verwaltungs AG***

Yes. So the first part on the ventilators. Yes, there is some positive effect on all types of ventilators, but the grade and the very significant, its effect is on this one particular line. And that's a technical differentiation because this ventilator has a built-in turbine and -- so and works from any, let's say, power outlet with electric power. And if power failure, then run on battery, and does not require the hospital to have a central gas supply for compressed medical air.

And in such situation, where you are in this -- a hospital where that is built in 2 weeks in containers in China or as that has to take additional patients beyond the normal capacity, that is a good feature that the ventilator can work rather independently. And this is why that is mainly concentrated on this type.

So your other point might take crisis trigger rethinking. I would think, yes, but not so much in the, say, in the investment behaviors of hospitals. That will still be very much budget-restrained and constrained. However, in the disaster preparedness of countries around the world, we know from many countries.

I think Austria is a publicly known example that they bought a huge amount of FFP mask many years ago actually from Dräger and the administer who then worked at the end, let go because bought too many masks. And now all these masks have been scrapped and they have none, which is a very bad situation. And in the future, I think there will be continued preparedness to a greater extent than what we have today. There will be a rethinking in that area.

Oliver Reinberg ***Kepler Cheuvreux, Research Division - Head of Med Tech Equipment & Services Research***

But overall, in terms of equipment capacities, do you think that there could be kind of renovation happening?

Stefan A. Dräger ***Drägerwerk AG & Co. KGaA - Chairman of the Executive Board - Drägerwerk Verwaltungs AG***

To some extent, there may be authorities that they, say, prepare a certain capacity of ventilators like there is already in the U.S. Historically, they have some centrally prepared staff in the -- that the government administers. And so -- but that to a limited extent, because it's just -- the most countries can or will not afford this.

Operator

Mr. Dräger, Mr. Lescow, there are no further questions in the queue.

Stefan A. Dräger ***Drägerwerk AG & Co. KGaA - Chairman of the Executive Board - Drägerwerk Verwaltungs AG***

Oh that's, it's a -- well received because we are already beyond our time that we promised a couple of minutes. So we thank everyone for being with us online today for your participation, for your interest in Dräger and for your questions. So we look forward to hear from you, see you at another time. And for now, thank you very much and goodbye, and have a pleasant afternoon. Bye-bye.