KONE Q3 2018: INTERIM REPORT FOR JANUARY-SEPTEMBER 2018
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Sanna Kaje: Good afternoon, ladies and gentlemen. And welcome to KONE Q3 Result Presentation. My name is Sanna Kaje, and I'm the Head of the Investor Relations. I have here with me today our President and CEO, Henrik Ehrnrooth, and CFO, Ilkka Hara. They will together present you the Q3 highlights and how we see the market and business outlook. Henrik, please.

Henrik Ehrnrooth: Okay. Thank you, Sanna. And also, a warm welcome on my behalf to everyone that is on line to have a discussion with us today again about our performance and how we are developing KONE. If I straight go to the highlights of our Q3 performance, we can say that our Q3 was a mixed quarter. There are a number of areas that continue to develop very well. Also, in particular, the fact that our orders received – grew in all geographic areas and grew at a good rate. Also, that our sales grew in all regions and all businesses. What I'm just happy about is clearly our EBIT margin and how it developed and the fact that it's continuously burdened by a number of headwinds. On the other hand, what I also see is, our strategy continues to improve our differentiation. This we can see very concretely from the growth that we're having and also improving pricing. So I feel very good about how we continue to develop the differentiation of KONE, and we'll talk more about that as well during this presentation.

I'll just start with, as usual, let's go to the highlight numbers. And here, we can see, as I mentioned already, that our orders received very good growth of 7.3%. Orders received were a bit over €1.8 billion. In an environment where our markets, particularly in the new equipment side, are more as flat, a continued good growth is a good achievement. Orders received – I'm sorry, order booked continues to be solid, growth of 5.5% over last year. And also, our sales grew at a pretty good rate of 5.6%. That was close to €2.3 billion. Our EBIT was €258 million or adjusted EBIT €273.7 million and we can see that our EBIT margin declined from 14.5% to 12%. It's clear that 12% does not meet our objectives and this is a margin that we clearly want to improve and will improve. Cash flow, €273 million, and earnings per share are 42 cents compared to 49 cents a year ago.

So, if I look at the overall assessment of Q3 as I mentioned, clearly, orders received, a broad-based growth, the fact that we've been able to improve pricing slightly and the broad sales growth, those are the good things. However, EBIT margin and EBIT does not quite meet our objectives. But one quarter is a short period of time. So, if you look at the first nine months, we can see similar trends. Also, orders received for the first nine months have grown to €5.8 billion a little bit more and it's a 6.8% growth in comparable currencies. As I mentioned already, in this environment, that's a good growth rate.

Sales grown to 6.2% in the first nine months up to €6.6 billion and our EBIT is €750 million or adjusted EBIT if we exclude the costs from the accelerate programme, a little bit over €792 million. And also, here the margin was 12% compared to 13.9% a year before. Cash conversion has been pretty good, €880 million from an EBIT of €750 million. And earnings per share of 1.19 compared to 1.41 a year ago.

If we look at the overall environment, we know that our whole industry has gone through a more challenging period and we continue to develop KONE very actively. That is good. When I look at how we're driving that internally, I'm very pleased with how our people continue to do it very proactively. They're engaged by the motivation to continue to positively develop KONE. That, a big thanks to them. And I must say, I am very pleased when I look at the developments on this side.

In order to drive growth and profitability, the key to that is really differentiation. And when I look at the external environment, we can see that there are plenty of good opportunities to differentiate because we can see that the environment is changing more rapidly than it has ever changed before and we can see that that creates new needs and also challenges for our customers.

For example, the changing use of buildings that we have talked about, that the way people live and the way people work is changing fundamentally and quite rapidly. We can also see that people are expecting much more convenience, much more experiences and want to have service that meets their individual expectations. That's about ease and convenience.

Speed is becoming more and more an important factor also for our customers, our new equipment side in particular, because we can see that, in particularly, in city centres, land costs are increasing all the time. We can also see that there continues to be shortages of employees in many parts of the construction trade. So the more we can help our customers speed up their construction, the more we can help them succeed, and we can see that our solutions on this side have taken us very much forward.

If we look at how we are differentiating and capturing opportunities out of these needs, that is really all about our new services and solutions. Those you have heard a lot about in the past, I want to talk about them again because they are so central to how we continue to drive KONE forward.

For example, new KONE Care in the countries where we have KONE Care now – new KONE Care nowadays, that is the way we sell service contracts to our customers, and I continue to see very good development here. When we look at the countries where we have introduced KONE Care already a year or two ago, I see that that is the contracts we sell. And we compare them to the old way, we can see that pick rates are better with customers, customers are happier with this because they can buy something that suits their needs, and also pricing is better. So we can see that it does bring differentiation.

Then of course, our digital services, KONE 24/7 connective services, very important in helping our customers run the buildings more efficiently, but also get more insight in our buildings operate and make them more efficient.

Residential flow is something we start to sell in a pilot mode earlier this year. We now have the first installations and we can see very good development here. I must say, I can see very good improvement in the momentum, how we're selling it, and we are taking to more and more countries now.

And then, finally, our people for planning and consulting services are an essential service that we provide to our customers to help their buildings improve, make flows better in the buildings, make sure the buildings just simply operate better.

All of these are bringing clear differentiation and we continue to develop these services, we continue to drive them out. And I must say that, what I'm most pleased about, when we look at the feedback from earlier adopters, it is very broadly positive. So with that encouragement, we continue to drive these services forward, and I believe that that's central to our differentiation, not only in services but also in our new equipment business. So that is about our development and how we continue to develop KONE going forward.

If you then next turn to the market development, how the external environment is developing. If we look at new equipment markets, they have grown slightly if you look at the number of units in Q3 and North America market continues to be robust at a higher level, growing slightly, whereas we see the small change has been in Europe, Middle East, and Africa, where the markets were now more stable. It's clear that we've seen a slight weakening of the markets in northern parts of Europe and UK, and also it's clear that the Middle Eastern markets have declined now. South Europe, we continue to see some growth opportunities there, our markets growing there. Asia-Pacific, the Chinese market actually grew slightly better that we had expected in Q3. That grew slightly, that was good. And we also have growing markets in the rest of Asia-Pacific, in particular driven by India.

If we look at the service markets on the maintenance side, no changes in credits there, continued growth in both Europe and North America, and good growth in Asia-Pacific. Modernisation, not changes in North America, we've continued a slight growth from a good level, and good growth in Asia-Pacific. In Europe, Middle East and Africa, we have, however, seen now, a stabilisation of the modernisation markets after a long period of growth. And that's particularly Middle East and a few European markets, where we see a more stable development. Although, I would say that modernisation continues to have good growth opportunities, but perhaps we see a little bit pause in the markets at the moment.

If we go more in detail to the Chinese market, as I mentioned, developed slightly better that we had expected, we can continue to see very much the same trends we have seen earlier. What is very good with the Chinese markets is that it's becoming healthier all the time and that we can see through the improving situation of inventories of unsold apartments. Both in absolute and relative terms, they continue to improve, and actually most big cities, they're at quite healthy level at the moment.

On the other hand, we can see that the government continues to have a lot of restrictions in place in more than hundred cities in order to cool down the housing market and we have seen the impact break[?] in higher key cities where markets have declined or being stable now and also in lower key cities we have seen an impact there and therefore, overall more stable markets on this side.

But what is still happening if we look at the development side is that the large developers continued to take significant market share. So they are – overall markets – not growing so much, but with the right positioning, there are clearly growth opportunities in the market that we have seen, that we have been able to capture in quite well now this year and particularly this quarter.

The overall construction markets are pretty stable, even though we can see good growth in real estate investments, but that is mainly due to increasing land cost. And as I mentioned, our markets grew slightly.

So then about our development and the external markets and with that I'm again as usual will hand it over to Ilkka Hara to review our financial performance in Q3.

Ilkka Hara: Thank you, Henrik and also welcome on my behalf for this third quarter results announcement conference call. And as normal, I'll start going through our financials in more detail with orders received.

In third quarter orders received was 1.8 billion and that's a 5.3% growth on a reported basis and 7.3% growth on a comparable basis. And not only did we have a strong growth in the quarter, but also we saw a broad base growth. All regions as well as all businesses contributed to our orders received develop.

If we look at more in detail the large Chinese markets for our orders received, in units we see – so our orders received growing clearly and in monetary value significantly. Mixed at a slight negative impact, but like-for-like prices had positive impact both quarter-and-quarter as well as year-on-year.

And if we look at the overall margin development for our orders received that continues to be stable year-on-year. So the pricing actions that we've taken continues to be there to stabilise our margins compared to increasing raw material price.

Then looking at sales development, we continue to see broad base growth in our sales. And our sales reached 2,289,000,000 and that's 3.6% growth on a reported basis, at a comparable currencies that's 5.6%.

If we look at what are the contribution from our regional perspective to that growth, then the strongest growth was in Asia-Pacific, China at 8.2%, Americas at 6.7% and Europe, Middle-East, Africa grew 2.4%.

From a business line perspective, we saw the strongest growth in modernisation at 8.1%, new equipment at 5.4%, and our maintenance business grew 4.9% in the quarter.

Then looking at our EBIT. Our adjusted EBIT was 274 million in the quarter and our adjusted EBIT margin was 12%. And as said already by Henrik, it is clearly not satisfactory developed. While we continue to see growth contribute in positive to our operating profit, we are seeing the headwinds being stronger than our productivity actions that we've taken.

And the pricing that we've seen in orders received earlier, especially in China is having a negative impact, so profitability, as well as increasing in input cost both the raw materials, as well as cost on the labour side.

Also currencies at 11 million negative impact to our operating profit. So the adjusted EBIT in this quarter, the accelerate programme costs were 15.7 million.

Then lastly, key words about cash flow. The cash flow in the quarter was 273 million and our cash conversion continues to be on a healthy level in the quarter. We look at the key drivers for this operating cash flow, then the decrease in our operating income was the main driver for the decrease compared to the comparison period a year ago. Our net working capital increased slightly, but continues to be a in a good level. With that, I'll hand over back to Henrik to talk about market and business outlook for 2018.

Henrik Ehrnrooth: Thank you, Ilkka. If we look at our market outlook for the full year, we have made a couple of changes. First of all, we have slightly upgraded our view of the Chinese market for the full year. Seems to be, of course, we are – we have three quarters behind us, and we've seen our slight growth. Also, Europe and Eastern Africa, we have actually taken slightly down and we expect it to be stable now and the same thing in modernisation for Europe and Eastern Africa. The new equipment, we expect the Chinese market to be stable and grow slightly in units this year. Although, competition will continue to be very intense. Our estimate in Asia Pacific will continue to grow driven by India. Europe and Eastern Africa, as I mentioned, to be stable this year and North America to continue to be very robust and grow slightly from a good level. Maintenance markets, again, no changes here slight growth in Europe and North America and good growth in Asia Pacific. And in modernisation, stable in Europe continued robust and good markets in North America and strong growth in Asia Pacific.

If we then go to our business outlook, we expect now our sales to grow between 4% and 7% in comparable currencies. Previously, we had – we expected it to be between 3% and 7%. We're simply now nine months through the year, so we have narrowed the range. We expect our adjusted EBIT now to be in the range of €100 million to €150 million. And that assumes that the exchange rates will stay at the level of where we are at the end of September and if they stay at this level, they will impact our result by approximately €45 million negative for the full year.

When we look at our EBIT margin, we expect that the pressure we have seen so far in the year, which have been expected, and that will start to ease towards the end of the year in the fourth quarter. In fact, if we look at this outlook range, we can see that with this, we expect our EBIT margin to be approximately at last year's level or even slightly better. Previously, our – we have our – had our EBIT range to be €100 million to €200 million and then we expect the exchange rates to impact €35 million negative. So, €10 million more than previously. And I think it's familiar to everyone that we have a number of good things that drive our performance, but also a number of factors that burden our results. But of course, we continue to develop KONE proactively going forward to build on the positive performance in order to, of course, offset all the headwinds that we are facing.

To summarise – what I'm very happy about is the continued good growth in orders received, and improved pricing. It shows that we have a strong competitiveness and we are differentiating and driving differentiation in many markets. This is very good. We can see that our differentiation is improving and it's really the key lever to drive improved performance. That is why we continue to roll out and invest in our new services, solutions, and products and we see good outlook for those. So that is really what we are very focused on.

It's clear that the EBIT margin trend has not been favourable this year, so far, but we expect that the trend to improve now in the final quarter and we can see margins to be at last year's level or slightly better. So, with that, we will now have good time for your questions.

Sanna Kaje: Yes, and I believe we can go straight to the lines. So, operator, please. You can take questions now. Thank you.

Operator: Certainly. Thank you. Again, just as a reminder, if you wish to ask a question, it's star one on your telephone keypad. That's star one to ask a question. We can take the first question at this time from Athira Pradeep from Goldman Sachs. Please go ahead. Your line is open. Hello? Please ensure that your mute function is switched off. Hello caller, your line is open. Hello? Your line is open. Okay, we'll just take our second question in the meantime from Andre Kukhnin from Credit Suisse. Please go ahead. Your line is open.

Andre Kukhnin: Yes. Good afternoon. Thank you so much for taking my questions. I'll just go one at a time. Just firstly, on that margin evolution from Q3 to Q4 with the over 100 basis point step-up in the guidance, how much kind of visibility do you have on that? I presume you do see it in the order book and do you have a very good idea on what kind of orders will be rolling into Q4 revenue and at what prices, with what input costs? But I just wanted kind of really check how much you can really underwrite that from the visibility you have in the company.

Henrik Ehrnrooth: Well, as you know, we have an order book and we our service base. So it's clear that we have a pretty good visibility at this point of the year for the last quarter. So we can see what we have. But always, as always, in business, there will be some fluctuations through that. But, yes, we have pretty good visibility for the final quarter of the year.

Andre Kukhin: Right. And if I think about – so your message now is that the backlog margin has stabilised, I just wanted to check what level should you be referring to for that stabilisation. Is this on the last quarter or the last four quarters' average as it has been stabilising through this year?

Henrik Ehrnrooth: If I I first would answer it in a slightly different way, but I'll then answer your specific question that, actually, we have communicated now for a year that we have stabilised our margins. That means that we have been able to slightly improve our pricing constantly, and at the same time, we know that the input cost with raw material and now also labour cost has increased. So with that estimate, we believe that year-over-year, it's pretty stable.

So we can say that the what we have been taking in as orders now compared to what we have been delivering, there is not a big difference between those. So, clearly, if you look at historic highs, we clearly the low, but now we have stabilised and prices are going in the right direction, and that is, to me, important, that the trend there has – it has improved.

Andre Kukhin: Got it. So, essentially, am I – would that be right – that this kind of implies that at the current level of raw material prices, your price versus raw material equation is neutral compared to the current profitability, so that in the years' time or nine months' time, when you come to deliver these orders. And I appreciate there could be variability on what exactly comes overtime, et cetera, but – and there's a whole, then you will have the efficiency improvement and accelerate programme savings coming on top of that and being incremental as long as obviously we don't have the further inflation from raw materials.

Henrik Ehrnrooth: I think that's it – you know, of course, there are many inputs. But if you simplify it, you can say that that, that that would be situation on the – more on the new equipment side of the business.

Andre Kukhin: Great, thank you. And just last one. On labour inflation, as that has become more of a topic for elevated world out[?], our kind of historic thinking was always that labour inflation is almost a net positive for elevated companies because of the price escalate is built into the service contracts and that kind of usually allows you to do more on price when there is labour inflation rather that when there isn't. How would you view the current levels of labour inflation and the trend there, when maybe looking 12 months forward, is that, likely to be a headwind or net headwind for you or not?

Henrik Ehrnrooth: Yes, eventually, in the – particularly in Europe, KONE service contracts will have some kind of inflation or cost index in them, but, of course, that comes, you know, with a delay. From the service side –on the service side, I think that, overtime, it's an ok thing to have some overall inflation in the market that helps use your pricing there as well.

But I think where you probably have got more comments and also a big comment, and more perhaps on the installation side, where there's quite also subcontracting used. And there, we could just see there's a shortage of skilled labour, not only in our industry, I would say the lot of skilled labour for construction trade as whole. You start to see that the particular subcontracting cost would go up.

Andre Kukhin: Got it, thank you, Henrik, I appreciate it.

Operator: Thank you. We can now take our next question from Guillermo Peigneux from UBS, please go ahead.

Guillermo Peigneux: Hi. It's Guillermo Peigneux from UBS. I actually have a question regarding your, your headcount and inflation problem into next year. I was wondering, you, you do have some, around about 3 billion internal weight and other expenses but if I net basically direct labour with your overall headcount levels, I would say that your labour bill is at around, you know, 2.15 billion 2.20 billion. And that obviously – that continues to inflate into next year unless you're able to contain inflation – weight inflation here.

Given that analysis relatively equal at this point in time, that means extra 80 million roughly speaking of cost pressures and I wonder whether your pricing initiatives both actually on the equipment side and especially on the market side are enough actually to offset that inflation alone.

Henrik Ehrnrooth: Perspective here, it is clear that strictly in Asia, we've seen quite high increase in labour cost over the past years constantly and so that is not a big change there if anything perhaps in China that's percentage wise a bit lower that has been in the past years. I think where we start to see an increase in pressure is perhaps Europe and some other Asian country.

This is not a necessarily a new phenomenon but, of course, we constantly need to get productivity, how to work, we do with that happens by doing investor processes, better quality, better ways of doing and that is how we offset and then also pricing is another lever for that.

So when we talk about stabilisation and margins that means that we have been able to increase prices, to compensate for increase in material costs and the labour costs. But in order to get the margin improve further, we will need to do more, that's of course, a clear objective.

Guillermo Peigneux: Okay, thank you. And then second question is – obviously you're giving a clear message as to how great Q4 is, but I'm surprised a bit of how unpredictable Q3 was. And to some extent, I wanted to understand what happened during the quarter that made the quarter look so weak from a margin standpoint? What was unforeseen that happened during the quarter from a margin perspective? Thank you.

Henrik Ehrnrooth: But first, I think we've been quite explicit with the fact that we expected – that we had expected Q3 margins to continue to be under pressure, that is very clear.

I would say this, you know, as always, in business you have variation and fluctuation in businesses. So it's the headwinds we've been talking about that impacted us as well as, you know, prior years and prior quarters that are now being delivered.

And as Ilkka said, given the – particularly increasing cost on the installation side that, you know, we would have had to get more productivity to offset that. So I wouldn't say that there's anything out of the ordinary, you know, as always, you have fluctuation in business and we have always been guiding the full year only not quarter-by-quarter.

Guillermo Peigneux: Thank you. And last question, regarding after market in Southern Europe or services in Southern Europe, or maybe expand that into Europe, could you come a little bit from the competition environment there and how margins are developing from a maintenance point of view in Europe, I mean, alone. Thank you.

Henrik Ehrnrooth: As we have been talking, it's clearly if you look at northern parts of Europe clearly better – demand and pricing situation are better. South Europe as you know, has been challenging for many years because the equipment volumes have been low and many of those markets are quite fragmented, so you have quite a lot of competitions.

So competitions has continued to be quite intense and therefore I would say more stable those markets, whereas our development in some of the central and north, you have a markets from a growth perspective has been better.

Guillermo Peigneux: Thank you.

Henrik Ehrnrooth: Thank you.

Operator: Thank you. Again, as a reminder please press star one to ask a question. Please try to limit your question to one question and we will take follow-ups if time permits.

We can now take our next question from James Moore from Redburn. Please go ahead. Your line is open.

James Moore: Hey, everyone. Good afternoon everyone. Hi, Henrik, Ilkka. I wondered if I could ask a little bit about China and you seem in the last year has done really well compared to your peers on the volume versus price equation and I'm sure you have the ambition to sustain that. But was there any kind of product launch or innovation lead that helped you do that? The first – become a topic comparison of next year or not?

Henrik Ehrnrooth: You see we have in – if you look our adjusted product perspective in China, I'm going to say we have had a continuous improvement how we have improved our product portfolio, but we haven't kind of any step changes. I would say, if I look at why we have done well, you know, it's the large developers that are clearly taking market share. And we have a good market share there. And the way you achieve a good market share with customers such as this that are very demanding, is to be very reliable in your installations, to be a very good partner, to have reliable and good products and provide them with value added services which we are doing. So it's – you know, our overall approach, and you know, in our industry, I think it's very seldom just down to the products, you know, there are a lot of good products out there.

I think we have excellent products out there, but you need to have the whole operation, you need to be a very reliable partner in installation, you need to make sure that you have a very broad and good and strong service base, that's how you create trust with these customers, and build a good business with them. And I think that's what we've been very focused on in not only China, but the rest of the world, and we can see that's yielding results.

James Moore: Congratulations, but we also do hear that large developers are tougher on price. So if that's become a bigger and bigger part of the mix of the market and you're taking share in that, one might have thought that that might have led to greater price pressure, you say, that others get the price pressure, but because of your service offering, you think you can – you can get – basically not suffer as much as others in the large developer price pressure?

Henrik Ehrnrooth: I mean it's clear that the whole China market is a very competitive market, there' not question about that. It's quite a fragmented market with a lot of players. Everyone knows it's the world's largest market, everyone wants to be a big player there, so competition is tough, but you need to constantly, if you can add value to your customers, then you can – everywhere, do good business, it's clear that the competition is very, very tough there and very demanding customers, but that's okay, that's how you know, positive pressure to perform better all that time.

And even that environment, we have been able to slightly improve pricing and yeah, it only happens if you can add value.

James Moore: Thanks, Henrik.

Henrik Ehrnrooth: Thank you.

Operator: Thank you. We can now take the next question from Antti Sutterlin from Danske Bank. Please go ahead.

Antti Sutterlin: Yes, thank you. If I compare you with some of the peers, that have reported, Otis vs Schindler, I think one can say that Otis EBIT margin dropped by about as much as KONE's, while Schindler's didn't it was a flattish year-over-year. Would you say that the simple reason why some dropped, and some don't, is China? Those who are big in China, see a fall in EBIT margin. Can one say that?

Henrik Ehrnrooth: You know, I cannot comment on any of our competitors. I can comment on our business, I can comment on our performance. And it's clear that you know, we'd be very clear that, what has impacted our margins has been the price pressures we've seen in China, we continuously have good margin in China, but they used to be even clearly higher. So that is the clear biggest impact on our side. I can't comment on the rest.

Antti Sutterlin: Yeah. And after all these, let's say, pressures, that we have seen over the past years, is it really so that you are still having a higher margin in China than in the world outside China?

Henrik Ehrnrooth: We have very good margins in China, that's a good business for us, that's why it's a good market, important market. I think we're performing well there.

Antti Sutterlin: So higher than elsewhere?

Henrik Ehrnrooth: Not everywhere, but it's – most of it, business there is higher than average, yes, I think the new equipment side.

Antti Sutterlin: Yes, okay. Thank you.

Henrik Ehrnrooth: Thank you.

Operator: Thank you. We can now take our next question from Glen Liddy, from JP Morgan. Please go ahead.

Glen Liddy: Hi there. Just coming back to your input cost in raw materials. Are you getting any impact from tariffs for things like steel purchases in the US? And also, on your sort of raw materials, if we start at the beginning of the year, 100 and raw materials have gone up by X, how much of that X have you recovered just in pricing so far, not productivity, because you seem to be able to improve that on a continuous basis, just on a pure pricing basis, how much of your raw material hit have you know recovered?

Henrik Ehrnrooth: Well, two-fold, first, if you look at the raw materials, we've been consistent throughout the year, that we were estimating the raw material impact to be around 100 million for the year, and we continue to be there. And I guess, your second part was about the tariff impact, so that includes the impact of the tariffs for us.

Then at the same time, I have commented – sorry?

Glen Liddy: But have you recovered that? I mean I appreciate you've not changed that 100 million, but have your price increases for your new business today, recovered half of it, three-quarters of it, rather than just looking at the margin being similar, you know, for incoming orders and where you are at the moment, because that includes productivity improvements as well, presumably.

Henrik Ehrnrooth: Yes, so I was trying to get there, so bear with me. But if we look at what we commented on our pricing development, so when we look at our margin of our orders received, we've been consistently saying that it is – it's stable for this year, for the first three quarters, and that means that we've been able to stabilise compared to the previous year, our margin.

Glen Liddy: Okay, but is that just raw material price rises, and your price rises equalling each other out?

Henrik Ehrnrooth: Well, it's the net of everything, because we do also include our productivity actions for new equipment, manufacturing installation there.

Glen Liddy: Yeah, okay. Okay. Thank you.

Henrik Ehrnrooth: Thank you.

Operator: Thank you, we can now take our next question from Athira Pradeep, please go ahead, your line is open.

Danielle: Hi, this is Danielle[?] actually here, from Goldman. And good afternoon, everyone. I wanted to ask three quick things. One, can you update us sort of – accelerate – I know prior to this, you have said, not much impact in 2018, but you started it in September '17, show – and I think you were 50% through the action. Shall we expect the largest chunk of the first impact of that to come in the first half of '19? Is there any sort of seasonality how that comes to '19?

The second thing I wanted to ask you about is China payment terms, some of your competitors have talked about in their calls about that getting tougher. You've already commented extensively on pricing, but I was wondering what's – with large developers taking share, what's happening on payment terms.

And the third thing is just on US market share. You had a few years of very successful market share wins in the US, has that continued? What's the situation there in your view? Thank you.

Henrik Ehrnrooth: Why don't you start at least the two first ones with acceleration in China?

Ilkka Hara: Yeah. So first, let's start with accelerate. So we've said that it has minor impact in 2018, some impact, but that's included in our guidance as such. And we continue to see the programs working through in 2019, so some of them will continue. We will develop them during that period as well, so the impact of P&L continues to be increasing throughout the year, but at this stage, I wouldn't comment half or on a quarterly level yet. We'll come back to that at the later stage when we guide 2019, more detail in January.

Then on the payment terms for China. So as Henrik was talking about earlier, that there are – larger developers are taking share, we're also growing with them, and yes, they are demanding customers, and price is one component, but also commercial terms, including payment terms, are also there. And we've been able to overall have stable payment terms, good payment terms in China as well.

So there continues to be pressure, but we've been able to also then push back on that one. So that's the status on payment terms in China.

Henrik Ehrnrooth: I think your final question was related to US market share. As you know, we don't disclose market share throughout the year because it can fluctuate quarter to quarter. Overall, I would say that we have been able to grow our orders received in North America and US in particular this year, continued to have good performance there. So overall, I'm quite pleased with how we're doing there. Now this quarter, growth was slightly slower, but you know, as we all know, they fluctuate quarter to quarter, and overall, we're doing quite well.

Danielle: Thank you.

Henrik Ehrnrooth: Thank you.

Operator: Thank you, and we can now take our next question from Andre Kukhnin from Credit Suisse. Please go ahead.

Andre Kukhnin: Great. Thanks so much for taking my follow up. It was just more a broader question on China and the evolution there, of construction – statistics. We've seen this sort of continuous ramp up and starts now for turnoff years, and at the same time, completions are completely diverging from that. So I just wanted to get your opinion on what's driving that, how long this can continue forward, which where you think that eventually plays out what we should be kind of looking out for when we're tracking that? Thank you.

Henrik Ehrnrooth: I think a very important number to crack all the time is the real estate investment. That tells usually quite what about the activity. And we have to remember that we don't come really the earliest in the cycle, particularly on standard projects. So there is a divergence between these two when we see a current activity, when you look at two construction activity and volumes, that they are pretty stable in those places. So that is what we continue to focus on and I don't have a clear crystal of how this will play out over the coming year or so.

Andre Kukhnin: Got it. And can I just ask a follow-up? Looking at your China business for next year or next kind of 6 to 12 months, you've now had four, not five quarters in a row of orders in China printing into – in kind of a mid single-digit or even towards high single-digit positive in value terms. When we think about these orders rolling out into revenues over the next 12 months, should this drive actually growth of your revenue in China or are these more kind of longer lead orders with i.e. that order book is not the usual sort of 9 to 12 months lead time? And maybe that growth is not actually – the order is not translating growth and revenues?

Henrik Ehrnrooth: I don't see any big difference in the –

Ilkka Hara: We haven't seen any big changes in order book growth basis[?]. So as such, the 9 to 12 months is a predicted proxy.

Henrik Ehrnrooth: Yeah.

Andre Kukhnin: So if you print Q4 – sorry.

Henrik Ehrnrooth: In China, of course, we have large projects, but the vast majority of the market is standard, more volume business and we haven't seen any relationship between the two would be – that there will be a significant difference.

Andre Kukhnin: Got it, thank you. So if you print Q4 similar to, say, Q3 in terms of orders in China in value terms. And I know it's kind of, say, it's my assumption, then when we come to modelling 2019 we shouldn't do anything different to what we're doing a year ago i.e. take that and mostly imply that for the new equipment part of your Chinese revenues? I'm just trying to think what may prevent it from growing next year.

Henrik Ehrnrooth: We don't give outlook on our orders. What I would say is that we had a very good quarter with, you know, as Ilkka mentioned, value terms, it was in a double-digit. So that's very, very good in the current market. But, yes, what we're ordering – what we get in those orders now is something is that I think the volume business, by and large, will be delivered next year.

Andre Kukhnin: Great. Thank you very much to both of you. I appreciate the time.

Henrik Ehrnrooth: Thank you.

Operator: Thank you. We can now take our next question from Lucie Carrier from Morgan Stanley.

Lucie Carrier: Hi and good afternoon, gentlemen, and then thanks for taking my question. The first one, I was wondering if you could maybe comment on your services business and the digital offering. Because from what I understand, you are saying you are trying to raise the prices in your maintenance service contract, your kind of contract inflation. And I was wondering that with all of your new offering, are you seeing maybe a faster renewal of grade of your maintenance contract at the moment because of all this new offering? And are you able, as a result, maybe to step up prices a little bit faster than what would have been previous in the past? So that's question number one.

And then secondly, it's a follow-up on the many question on China. So I think understand with order up in China in '18, we should see China revenues up in '19 with normal conversation. But those orders being up above the market, have you gained market share also possibly versus some of the smaller players? And with the challenges that the industry has shown over the last few years, do you think that maybe the number of the smaller players is finally starting to reduce?

Henrik Ehrnrooth: Ilkka will take the second while I take the first one.

Ilkka Hara: Can you just repeat the first question? Sorry.

Henrik Ehrnrooth: I'm getting the first question. You take the – it was mostly about maintenance. And if you take the China small players, that is awesome.

So if I look at our new services that we have now been rolling out over the past roughly a year or so, the first countries where we're in with many of these services were – many countries in Europe. And in those countries, yes, we started to see a slightly improved growth. It's clear that we are very much at the beginning and clearly that is an objective that we have additional new values we can sell to our customers. We can their buildings function better, we can help them manage their buildings in a better way, and we believe that that's an area where we can help them perform better and that we believe will generate extra revenues.

Earlier on, as I mentioned from the early adopters, news is positive. And when we also look at our KONE Care in the countries where we're earlier on with this, we're seeing a slightly better growth rate there. But, again, we have to remember that the renewal of contracts in our industry is quite slow, which is a good thing. But when they are renewed, then we can see the improvements from this.

So the long answer is the summary of it, is that, yes, over time.

Ilkka Hara: And to the second question on China market share, so our focus in China has been more the value than the volume clearly in a market situation where it's been price pressure. Raw materials had been a headwind to us. We've been really focused on gaining share in more the value than on the volume side.

And if we look at our execution so far, it seems that we've been successful making some shared gains. But obviously, we look at it in a context of a year, not on quarter-by-quarter basis, but that's how it seems to be.

Henrik Ehrnrooth: And I think you also asked about what happens to the smaller players. We can see that many smaller players have lost market share, but we haven't seen a big change. There are some mid-sized players that have actually done pretty. But overall, I think many of the large players have taken market share out of it from the really smallest ones.

Lucie Carrier: Thank you.

Henrik Ehrnrooth: Thank you.

Operator: Thank you. We can now take our next question from Rizk Maidi from Berenberg. Please go ahead.

Rizk Maidi: Hi. I just have a couple of questions. Number one, we're hearing that some of the real estate developers are holding back on first stage[?] completions as there was an expectation in the market that China will stimulate the property markets. Is this something you're hearing from your customers?

Henrik Ehrnrooth: There can be different approaches to province-to-province, but we haven't seen that that would be something that is happening on a larger scale.

Rizk Maidi: Okay. And maybe on the accelerate programme, you talked about a minor impact in 2018. Can you just help us on the phasing there between Q4 and whether you had in Q3, please?

Ilkka Hara: Well, on the raw mats, we've said the 100 million pretty evenly split between the quarters throughout the year so there's no big difference, it's quarter-by-quarter.

Rizk Maidi: I was thinking about – mentioned the accelerate programme.

Ilkka Hara: Sorry. Can you repeat the question?

Rizk Maidi: Just accelerate programme, and the minor impact in 2018, what is the impact in Q4 versus Q3?

Ilkka Hara: We haven't been so particularly on that one. It's a small impact but it's within the guidance, so it's not that material yet.

Henrik Ehrnrooth: Yeah. We're not talking about a huge amount. We're talking about – as always, you have some – I would put that it's a little bit more than continuous improvement that we tend to have a little bit more, but it's not the major number still this year.

Rizk Maidi: Okay. And then perhaps as we're getting closer to the yearend, can you just give us just an early indication on how do you feel about the Chinese market next year, at least in the first half of it?

Henrik Ehrnrooth: I think we have to still see exactly what's going to happen next year. Much will depend on the government policy on restrictions and also financing availability. So let's how that develops. Because a very big impact on the market is the fact that there are restrictions in more than 100 over large cities and also the very tight liquidity situation for developers. So let's see how those develop and that will tell a lot about the market next year.

Rizk Maidi: Thank you.

Henrik Ehrnrooth: Thank you.

Operator: Thank you. We can now take our next question from James Moore from Redburn. Please go ahead. Your line is open.

James Moore: Thanks for the follow-up. I've got two, maybe one for Henrik and maybe one for Ilkka as a guest. But thinking of your comments from your US friends, is Korea an important region for you? And if so, could you size the percentage? And basically, are you seeing any weakness there?

And the second question is, you've already said back at the capital markets day that you see a negative FX, a more material impact in 2019. Is there any chance you could say anymore about the impact relative to what you are going to see this year given current rates or is it too early for that?

Henrik Ehrnrooth: I'll take – will take the very simple one, Korea. We see nothing because it's 0% of our sales.

James Moore: Okay.

Ilkka Hara: Maybe I'll then get the effects. The second point of the question on raw materials on FX impact for 2019, so well this has many parts still moving when it comes to get into '19. But first, from a raw materials perspective, we continue to be where we are right now. We are seeing that the raw materials will continue to be a headwind in 2019, but less of headwind than within 2018.

And also currency, there is a slight headwind that there will be for next year if we continue to be on this level on the exchange rate.

James Moore: Did it wage inflation? Is it a bigger percentage next year versus what you see this year? Is that an important topic? Another player believes it is. I don't know if that's the same for you though.

Ilkka Hara: I guess we've been now saying also that the late of cost of inflation is picking up and that's – it's basically I would say Europe, some parts of Asia where it's picking up compared to where it has been and that's something that we need to take into account.

James Moore: Thanks so much, guys.

Henrik Ehrnrooth: Thank you.

Operator: Thank you. We can now take our next question from Guillermo Peigneux from UBS. Please go ahead.

Guillermo Peigneux: Small follow up for me. Thank you very much for taking my question. You mentioned service business as means of going to the market for acquisitions. Maybe two if I may. One is the size of deals. I guess you've changed a little bit your tone from the market will invest from consolidation to, you know, we're looking to every single segment for consolidation along the large players and then now is the focus is narrowing to the service businesses. I was wondering whether this scope of acquisition is getting smaller for you in your daily number.

And then second in terms of services business which regions are you most interested in acquiring services business and is China part of that opportunity? Thank you.

Henrik Ehrnrooth: I don't think we've changed our focus on acquisition so, you know, we will continue to do them. Just this year perhaps we've seen less attractive opportunities than in the past year. So that's definitely something we continue to do buying smaller service companies.

And if you think about what we have been acquiring over the past many years is the principally company service side or few of our distributors in market such as Israel and few other markets joined KONE, of course, a bit different case.

But the focus continues to be very much the same and we continue to think that consolidation in this makes sense. Whereas the highest activity been usually has been in Europe, part in North America.

China we still see such good organic growth in the service business that we have not yet started acting, looking for acquisitions there but let's see in the future by the moment is not high focus area for us.

Guillermo Peigneux: Thank you.

Henrik Ehrnrooth: Thank you.

Operator: Thank you. We can now take our next question from Tom Skogman from Carnagie. Please go ahead.

Tom Skogman: Yes, this is Tom from Carnagie. I was wondering about potential to do cost cutting in China when the margin obviously is down like [inaudible] there on the equipment by the minute to see any significant change in the setup to get down as opposed so that given you have such a still amount factors compared [inaudible].

Henrik Ehrnrooth: I would say it was now – Tom, your line was a bit breaking, so it was difficult to hear your whole question.

Tom Skogman: Yes, I was wondering about potential for cost cutting in China given the margin pressure. I mean, the accurate programme is rather about developing KONE than really improving the efficiency.

Henrik Ehrnrooth: So if I look at, we have a lot of people in China, but if I look at our efficiency there, it is at pretty level, but of course there's always room to improve and, of course, we look all the time at how we run the operation most efficient way. But if I look at our China operation, I think it's actually quite deficient, quite need an efficient.

Ilkka Hara: Maybe to that, if we look at productivity gains in China, so actually one of the reasons why we have a attribute business from a profitability perspective in China is been that we've been consistently able to make good gains in productivity starting from manufacturing but all the way to installation site, so that's been something that we've done throughout the time.

Tom Skogman: Then my second question is about the maintenance margin in European countries that I've enjoyed, you know, good equipment in there now in the last five years. What is happening to the underlying maintenance margin in these countries?

Henrik Ehrnrooth: No – you know, usually that's a pretty good level.

Tom Skogman: But, I mean, you said you got couple of years ago that it's improve – the maintenance margin is improving in the US some years after the equipment markets start to improve and now we have had, you know, quite few years with good demand in equipment in Europe. So I just wondered if it's a similar trend in Europe –

Henrik Ehrnrooth: I mean it's really very for growth perspective. What drives growth for the market is clearly historical new equipment deliveries, that's what growth to service market and therefore we're seeing in many European markets, we're seeing better growth than usually than there's also more space forever in growth with better pricing. So yes, we can see it improving in many areas there.

Tom Skogman: Okay, thanks.

Henrik Ehrnrooth: But in the fast growing markets.

Operator: Thank you. We can now take our next question from Mustafa Okur from Bloomberg Intelligence.

Mustafa Okur: Hi, Henrik, Ilkka. Thank you for taking my questions. Just two please. First one on the new services. Would you say that your margin would be even lower without offering these services like 24/7, your KONE Care. Did they much really contribute to your margin in the quarter?

And second question please. Your order intake in China jumped from about 5% in the first half to 10% in Q3. Did something specific happened there? Did your, maybe, price increases start taking hold or did you receive a large order? Thank you.

Henrik Ehrnrooth: So first of all as I mentioned, new services, yes, they have a good margin although we have very much at the beginning so they don't have a material impact from KONE overall so I would say still the impact from them, our bottom line is very small so that's been having an impact really either way.

In China, it's usually not about single orders because it's so much driven by the large standard volume business there. Just that we have a good performance. We have been very focus on serving our customers well and we continue to do that and outward[?] our focus, that's what we are doing. And there was nothing out of the ordinary I would say here.

Mustafa Okur: Sounds good. So you wouldn't say that perhaps the price elements wasn't more prominent in this quarter versus the first half it was on the similar trajectory, should we say?

Henrik Ehrnrooth: Yeah, about [inaudible] we had a slight positive impact to the growth number, but also we have to remember that growth rates, they do fluctuate quarter-to-quarter so one quarter is quite a short period of time to look at, but if I look at the first nine months of the year overall, we have perform well in China this year.

Mustafa Okur: Okay, thank you.

Henrik Ehrnrooth: Thank you.

Operator: Thank you. We can now take follow-up from Lucie Carrier from Morgan Stanley.

Lucie Carrier: Hi, thank you very much for taking my follow-up. Just one question on the service business in China. I know it is quite small versus, you know, new installation and historically that the margin as well was made year being impacted by a bit of what I call lack of scale or lack of density. As you are saying this business services both maintenance and with innovation continuing to grow, are you seeing improving momentum also on your profitability in business in China?

Henrik Ehrnrooth: Profitability on that businesses is quite good. It's similar to the new equipment there. I would say density has not been the major issue there because it tends to have quite of our buildings together so you can actually get pretty high service density early on. But clearly, as we expand the business, we are looking to get all the time better efficiency there, adding more value to our customers and that's why improve the margins. So that is where we focus mainly, but density is perhaps not the biggest driver in that market, not as much as it's in a market such as Europe or North America.

Lucie Carrier: Thank you.

Henrik Ehrnrooth: Thank you.

Operator: And as a final reminder, that's star one if you would like to ask a question. We have no further questions in the queue at this time. I'd like to return the call back over to you for any additional or closing remarks.

Sanna Kaje: Many thanks again for all the good questions. We look forward to continue in the discussion over the coming months. And with this, we wish you a good rest of the week. Thank you.

Henrik Ehrnrooth: Thank you.

Ilkka Hara: Thank you.