KONE Q3 INTERIM REPORT FOR JANUARY – SEPTEMBER 2015

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Katri Saarenheimo: Good afternoon and welcome to KONE's Q3 Results Webcast. Here in Espoo, Finland we have today our CEO Henrik Ehrnrooth and CFO Eriikka Söderström. We will again start with a review of the highlights of our results as well as the recent developments in the market environment. After this we will have plenty of time for Q&A and discussion. So Henrik, let's get started.

Henrik Ehrnrooth: Ok, thank you, Katri. Also welcome on my behalf to our Q3 results call and I'm very pleased to present our results. As we can see, in Q3 our strategy and execution continued to bring good results so we have positive news to tell. I will start with going through our key numbers. After that, I'll go a little bit deeper into the numbers as well as development of our businesses, our markets and then how we developed KONE and finally our outlook.

Let us start with looking at the key numbers. In Q3, we continued our profitable growth and we had very strong cash flow. Our orders received, they grew close to €1.8 billion, growth of about 12% or 3.6% in comparable currencies. Our order book had a strong level of more than €8.3 billion, growth in comparable currencies of about 14% compared to last year. So this naturally gives us a good position going forward from here. Sales close to €2.2 billion, growth of 16.3% or 7.7% in comparable currencies, so we're able to slightly accelerate the growth compared to the previous quarters this year. Our profitable growth continued. EBIT of €326 million and as you can see, our EBIT margin improved slightly from 14.8% to 14.9%. It's a good performance also in this respect. Very pleased with our strong cash flow of €432 million, continued very strong cash conversion, which shows that we have continued to maintain healthy business practices throughout our operations. Earnings per share €0.50 compared to €0.41 last year.

This is Q3; we know one quarter is a short period of time to look at performance, so if you look at it from a little bit longer perspective, for the first nine months of the year we can see, and as you know, we have had a strong development on a broad basis. Orders received in the first nine months more than €6 billion, growth in comparable currencies of 5.2%. Also, continued good sales growth, sales of also more than €6 billion in the first nine months and growth in comparable currencies of 7.2%. a good EBIT, €863 million, an improvement from 13.9% to 14.2% in the EBIT margin, and cash flow for the first time in our history in a nine-month period, we had over €1 billion of cash flow in the first nine months of the year. It's a good performance here. And EPS increased from €1.07 to €1.30. So overall strong development on a broad basis is what we have achieved during the first nine months of this year.

At this stage again we'd like to express a big thank you to all of KONE's employees for the great work they have done for the continued good development of KONE, executing on our strategy and executing our projects which has resulted in the good achievements we have had again in the first three quarters of this year.

So those are the key numbers. If you then go into, starting with orders received, into our numbers a little bit more in detail, orders received, so I mentioned we have a growth of 11.9% or 3.6%. Here the highlight is that we had a slight slowdown in our orders received in China but we were able to accelerate our growth in many markets to compensate for that. We continued to grow our volume business and our strongest growth was in the modernisation business. If we look at our development geographically, we continued our strong growth in North America and we were able to achieve very strong growth in Central and North Europe. That was a good achievement. Also if you look at the volume business, that grew very strongly in Asia Pacific outside of China. So as you can see, a broad-based development and was able to compensate the slight decline that we had in the Chinese market. Price competition continued, particularly in China but elsewhere as well. Despite that, given the improvements we have had in our competitiveness, the focus we have had on pricing meant that we have been able to maintain good margins of our orders received.

Then if we return to sales, here we had a good development in both our new equipment business and our maintenance business. Our new equipment business grew at about 10%, so good growth continued there, and I'm pleased to say that in our maintenance business we were able to slightly accelerate our growth, which is pleasing. We now had 6.7% growth in comparable currencies in maintenance. Modernisation was now seasonally more stable. If you look at the growth regionally, as you know, we have had good growth in orders received in North America for a couple of years already, or more than two years already, and now we can see that this is coming through in sales. So our sales growth in North America was almost 20%. It's a very good growth. And we continued our double-digit growth in sales in Asia Pacific as well. So again here a broad-based, good development.

If we then go to our EBIT, operating income, what is the most important point here is that our profitable growth continues. We had a broad-based, good development in our EBIT driven by strong development in our new equipment business and also good development in our maintenance business. If we look at the development geographically, it was good on a broad basis. So that is something that I'm very pleased about. Exchange rates continued to contribute positively to our results; about €30 million in the quarter came from translation exchange rates, but even if you take out the impact on exchange rates, we can see that we had a good development in our EBIT.

Also pleased that we've been able to significantly invest in the development of our future competitiveness and keep up a profitable growth at the same time, so we have continued to increase the investments in research and development, process development and in IT, and also in North America we're also resourcing our organisation stronger to deliver on the strong growth that we have achieved in orders received over the past years. The, I guess, highlight here is the broad-based, good development.

Then if we look at our business mix and start with sales by business, here we can see a continuation of the trend that we have had for a while already which is that the share of new equipment, of the new equipment business, continues to increase. New equipment, the share of new equipment increased to 57% of our sales. Now, the increase now in the share of new equipment was mainly driven by changes in exchange rates; that is due to the fact that we have more of non-euro sales in new equipment than we have overall for KONE. If you look at geographically, we can see that now Asia Pacific was 45% of our sales, the largest geographic region, and here the change in the mix was both due to exchange rate as well as the underlying growth, and the increase of North America from 14% to 16% is naturally due to the strong growth we have had in the first nine months in the Americas. So overall, as you can see, solid, good financial performance across the board throughout this year.

If we then turn to our businesses and the market development in the various businesses, so first of all new equipment. Orders received in new equipment were stable overall. We grew in the volume business but major projects declined slightly. In the volume business, as I mentioned, we had good growth on a very broad basis in many European countries, very strong in North America and strong growth in Asia Pacific in the volume business, but that strong growth then compensated for the slight decline in China and the decline in our major projects. If you look specifically at China, orders received, if you measure that in units, was stable; and we had a slight decline if you measure that in monetary value.

If you then look at the development of our markets overall, and starting with Europe, Middle East and Africa, here we've continued to see positive development in Central and North Europe, particularly in the residential segment. Middle East also continues to develop positively and South Europe is slightly recovering from a low level. We believe that France has found its bottom and we continue to see a recovery in Spain, although from a low level. North America markets continued their good development, and Asia Pacific, if you look at the volumes overall, they were slightly – declined slightly because of the decline in the Chinese market, although we had growth in other Asia Pacific markets such as India, Australia and some Southeast Asian markets. India continues to grow, not quite as fast as we had predicted at the beginning of the year but at least the direction is the right one.

At this stage as always, we’d also report a little bit and talk a little bit more in detail about what's happening in China. First of all, the situation is very much what we discussed at our capital markets day about a month ago in Shanghai. So overall, the market continues to be challenging as we had expected. If we look at the market overall in Q3, it declined slightly and also if we look at the first nine months, markets declined slightly. We have continued to outperform the market. In Q3, we were stable when the markets declined slightly and in the first nine months also markets slight decline compared to a close to 5% growth for KONE overall.

So if we look at the markets, what do we see there? Well, it’s exactly as we discussed at the capital markets day in Shanghai; they remain mixed. Much better development in the higher-tier cities, particularly tier one and most of tier two cities where we continue to see a good development. Inventory levels are at a pretty good level. We can see a good improvement in the overall real estate market. However, if we look at many lower-tier cities, particularly northern parts of China, we see a much more challenging situation and a situation where inventory levels overall are at a quite high level. The good thing is that the market is large and there continues to be good opportunities in the higher-tier cities. Competition for market share in China remains, as you know, remains intense and pricing trends have continued to be pretty similar in the third quarter as they were earlier in the year.

If we look at our development, we can see that given the improvements, we have continuously been able to drive, in our total competitiveness, we have been able to retain healthy margins in China.

If we look at the segments a bit closer in China, similar trends to what we saw the beginning of the year is that standard residential is declining slightly, affordable housing more stable, and also stable or slight decline in the commercial markets. The infrastructure markets, on the other hand, are growing well due to government stimulus. So if you look at the property markets as a whole, not only our market but the property market as a whole, we see both better and less good news. The good news is that for several months already, we've seen continued improvements in overall transactions in real estate markets, and we've also seen a continuous improvement in the pricing in real estate markets, and this is positive. So we can see that the markets are going forward and developing. On the other hand, when we look at overall real estate investments and new construction starts, we see a more negative picture. And again, we continue to see different situations in different tiers of cities. So the situation continues to be, as we have discussed before, uncertain and our expectation for the full year is that the markets will decline slightly. So that’s a little bit more in detail again on China.

Next I'll turn to our maintenance business. First of all, in our maintenance business, pleased to say that we grew in all geographic regions and we continued to have strong growth in Asia Pacific. Here we are achieving strong growth because of the strong deliveries of new equipment we have had over the past years. The most significant growth continues to be in China where our growth continues to be at about 25% in the service business – continued very strong growth there. If we then look at the maintenance markets as a whole, first of all, Europe and North America, really no change to the market environment. Markets continue to grow slightly overall and markets where we have had a more difficult new equipment market over the past years, we see a more difficult pricing situation. So very much the same trends we've seen before. On the other hand Asia Pacific, also as we've seen before, continues good growth in the service business due to the high level of installations in the past years. So positive growth here, and we've been able to capture that growth in a very good way.

And then modernisation business, first of all our performance, we had good growth in all geographic regions in our modernisation business. Now seasonally, modernisation sales were more stable with slightly better performance in Europe, Middle East and Africa, but overall quite stable sales. If you then look at the markets, North America continues to grow, so similar good trends we've seen before. In Europe – Central and North Europe – the market is growing and South Europe market remains weak. Here we can see a nugget of positiveness through Spain where the market is recovering from a low level but overall, South Europe is weak.

So that's about our markets and our businesses. Then in connection with our quarter results, we usually highlight one area where we have strengthened again our business through our development programs. This time we're highlighting our Preferred Maintenance Partner development program and as you know, one of our important strategic objectives is to strengthen our differentiation in our service business. Here, we have further improved our capabilities to service our customers and drive productivity. We have, during this year, we continue to roll out our next generation, what we call our field mobility device, to our service technicians to improve the connectivity of them, provide them with better information, with faster problem solution times, and that way be able to serve our customers in a more effective way and improve our productivity. As you also know, we have over the past years invested significantly in developing our sales setups, our sales management and also in our customer interactions. Now we have those implemented throughout KONE and now driving benefits of this, and again giving us a better opportunity of understanding customer requirements, offering better services to them, and this way driving a better growth. Again, I think in the maintenance business we have a very strong development agenda and we can see this moving forward.

And then finally our outlook, which is the same that we discussed in connection with the capital markets day in Shanghai recently, slightly specified relative to what we said in Q2. Asia Pacific, we expect the markets to decline slightly in 2015 due to the slight decline in the Chinese markets. Other Asia Pacific markets overall we expect to continue growing. Europe, Middle East and Africa, expect that market to grow as a whole slightly. Central and North Europe to continue growth. The market in South Europe, gradually recover from a low level, a similar trend to we see now, and Middle East continued growth. North America, we expect the good trend will continue throughout this year. Maintenance markets very much the same trends that I talked about earlier, continue to expect to see those – some growth in Europe and North America and continued good growth in the Asia Pacific markets. Modernisation, if you look at Europe as a whole, broadly stable with growth in Central and North Europe and a weaker market in South Europe, and continued growth in both North America and Asia Pacific. So very much the same outlook that we have seen before. If you then look at KONE's business outlook that we have only slightly specified, if you look at our sales, here we have kept our outlook unchanged so we expect our sales to grow between 6% and 8% for the full year in comparable exchange rates. And if you look at our EBIT, here we have slightly specified our outlook. We now expect our EBIT for the full year to be in the range of €1.20 billion and €1.25 million, again assuming that there won't be a significant change to translation exchange rates compared to the average of January-September. Previously we had lower end of the range €1.19 million, so a small improvement in the bottom end of the range.

So with this outlook, what we can see is that we have good confidence that we will deliver strong results for the full year and continue our strong execution and deliver upon our strategy. So with those words, we are ready for questions.

Katri Saarenheimo: Thank you, Henrik. We are indeed ready for the Q&A and unless we have questions from those present here in the room, I think we can go straight and take questions from those listening via the phone line so I am handing over to the operator please.

Operator: If you would like to ask a question at this time, please press the * key followed by the digit 1 on your telephone. Please ensure that the mute function on your telephone is switched off to allow your signal to reach our equipment. If you find that your question has been answered, you may remove yourself from the queue by pressing *2. Again, please press *1 to ask a question. We will take our first question from Lars Brorson from Barclays. Please go ahead.

Lars Brorson: Thanks very much. Hi Henrik, it's Lars here from Barclays. I was a little late on the call so I apologise if you've covered this, but I wonder whether you could give a little bit of granularity on the mix impact on your margins both in the quarter, but also on the orders received. In terms of orders received margins that's been flat since mid-2014. I wonder whether again, if you give some granularity around that regionally, presumably your OR margins in the US are improving quite nicely and probably Europe is or EMEA coming off the lows. Should we think about OR margins in APAC as weighing negatively on that? That would be my first question, thank you.

Henrik Ehrnrooth: First of all, overall what we’re saying is that despite the competition we see, we have been able to keep our margins at a good level. So we continue to have a healthy and a good new equipment business. When we look at the margin of our orders received, we very much look at that still, you know, what we do in the various regions. We have to remember that China is still close to 40% of our orders received so that has a big impact. I would say that where we have seen improvement is in North America. That’s the most positive story. I would say that there hasn’t been any significant changes in other markets.

Lars Brorson: Thank you and then secondly and finally just on pricing in China, can you give us an order of magnitude of how that's declining year-over-year on an apples-to-apples basis? I think in the first half, you talked about pricing in China down some 2-5%. Where are we currently?

Henrik Ehrnrooth: So we are looking at similar trends, I would say 3-5% approximately year over year. That’s the trend we have seen earlier in the year, it’s pretty much the same what we continue to see.

Lars Brorson: And on China, when you look into 2016, you're obviously not giving a formal outlook as just, of yet, but at the CMD you talk about the same trend, which purely means that you are seeing the market down again in China slightly. Otis is obviously talking about a double-digit decline in ‘16 but with different mix there. Can you give a little bit of an update as to what you see? I know it's early days to but based on some leading indicators you talked about earlier, is there perhaps an opportunity to be a little more to optimistic here relative to what you were seeing at capital markets day?

Henrik Ehrnrooth: I think what we said in the capital markets day, as I mentioned in the presentation now as well, the situation we described there is very much intact. So when we look at next year, we will give our formal outlook in January. It’s too early for us to give a formal outlook for that but as I said during the capital markets day, we expect a similar trend to continue and we don’t expect any dramatic changes to the market overall.

Lars Brorson: Thanks.

Operator: We will now take our next question from Erik Karlsson from Bodenholm. Please go ahead.

Erik Karlsson: Hello, thank you very much for taking our questions. I wanted to ask you about the development of the maintenance business. If we think about KONE in the very long term, maintenance is still the biggest value driver in the business and if we look at the local currency growth in the maintenance business, it's accelerated over the last 12 months. Here it was 5.3% in Q4 last year, accelerated to 6.1% in Q1 this year, than 6.4% and now 6.7%. Could you just help us understand a little bit more what is driving the acceleration and how we should think about the maintenance business going forward here?

Henrik Ehrnrooth: Okay. So when we look at what's driving the growth of the maintenance business, well, the most important reason is a growth in number of new conversions. We're converting from new equipment sales to our service business. As you know, we have grown a lot with our new installations over the past years and that we can see coming into our service base, so that's perhaps the most important part of that. We have also been able to be more proactive in our service business, have improved our sales competencies which we can see a slightly better development in pricing compared to the prior year. But still the most important part is the improvement in conversions year over year.

Erik Karlsson: And could you just help us, what is the conversion for the group now?

Henrik Ehrnrooth: So we are, if you look at – I think it's worthwhile looking at China separately because it's such a big market and the dynamics are different there. As you know, if you look at the rest of the world, we are somewhere north of 80% on average, Europe quite a high level, then China conversion rates remain pretty much – has remained pretty stable, roughly 60% for the KONE brand; if you look at KONE overall in China, around 50% ish.

Erik Karlsson: Very good, thank you very much.

Henrik Ehrnrooth: Thank you.

Operator: We will now take our next question from Martin Flueckiger from Kepler Cheuvreux. Please go ahead.

Martin Flueckiger: Yes, good afternoon, gentlemen. Martin Flueckiger from Kepler Cheuvreux. A few questions, I'll take them one by one. First one, I suppose the slight downgrade for the China market, new equipment market, was probably less surprising for most people but considering a further worsening in real estate investment growth in Q3, do you expect a larger decline in the new equipment market growth in China in Q4? That would be my first question.

Henrik Ehrnrooth: So first of all the outlook for the Chinese market, we have the market declined slightly the beginning of the year and that's our outlook for the full year as well. So we don't expect a significant change for the fourth quarter. So pretty much similar trend to what we've seen in the past quarter.

Martin Flueckiger: Okay, thanks and looking at EMEA sales, they were down 0.5% in Q3 at constant exchange rates. Could you elaborate a little bit on the main drivers in terms of markets please? And also if you could mention the acquisition impact on EMEA sales growth in Q3. Thank you very much.

Henrik Ehrnrooth: So acquisition-driven sales growth throughout KONE, it’s small. So it doesn’t have any material impact. Now if we look at Europe, Middle East and Africa and start with Central and North Europe, first of all we have strong orders and see growth, so that’s positive. So we’re building a stronger order book. Now seasonally, we had somewhat weaker sales than earlier in the year; I would more say this is a seasonal matter because we are building up our order book overall if you look at Europe, Middle East and Africa. So this is 0.5% negative in comparable currencies. That’s pretty much the organic development overall.

Martin Flueckiger: Okay, thanks and then finally looking at the financial results and the tax provision, that was significantly higher year-on-year in Q3. Could you explain that in more detail please?

Henrik Ehrnrooth: Do you want to, Eriikka, explain our taxes?

Eriikka Söderström: About the taxes, so our effective tax rate was 23.5% and last year it was 23.3%. So of course the business has been growing. There we have been specifying especially the withholding taxes related to dividends because we are towards the end of the year, and also we have seen growth in our North America business so that is also increasing somewhat our taxes.

Martin Flueckiger: Okay, thanks and the financial result? That was also some €20 million higher year-on-year in Q3.

Henrik Ehrnrooth: Do you want to also address this financial result?

Eriikka Söderström: Yes, sure. So our financial income was stronger now in Q3 due to two reasons. We had dividends coming from Toshiba, where we are having the minority shareholding; and also the other issue was related to the valuation, the FX valuation or the option liability on acquisition and that has been now this quarter slightly positive.

Martin Flueckiger: Okay, thank you very much.

Operator: We will now take our next question from Andre Kukhnin from Credit Suisse. Please go ahead.

Andre Kukhnin: Yes, good afternoon, I've got a couple of questions, so take them one at a time. Firstly, on the maintenance business, operational gearing and related to that pricing, could you just walk us through that, sort of related to previous questions about growth accelerating? And is that yielding operational gearing within the group that is consumed elsewhere given that the margin progression has slowed down a little bit? If you could talk us though that would be great.

Henrik Ehrnrooth: If you look at our maintenance business overall, it has continued its profitable growth. I think we have developed most of our business in a good way. We have – what should I say? We have a good, profitable growth in our maintenance business. The difference in mix hasn't actually changed that much if you take out currencies, a little bit even more still on new equipment. So that's perhaps the biggest impact on our overall margin. The good thing is that both our new equipment and our service business continued their profitable growth both first nine months and also in the quarter.

Andre Kukhnin: Got it. So just to confirm, within the overall EBIT, your maintenance operating profit margin has expanded year-on-year in Q3 with the 6.7% growth, has it?

Henrik Ehrnrooth: Well, we don't, as you know, we don't open up our margins by business and we look at this as a whole. I would say what you can see and what the most important point is that we are, we have been able to slightly improve our growth in the maintenance business.

Andre Kukhnin: Got it, thank you and a couple of questions on broader markets. Just I think when you started coming up next year for elevator equipment and it looks like it's going to be a global standard. Could you talk us through the impact of that on KONE and on competitive landscape as well? It looks like something that's some of the smaller players may struggle to keep up with, and whether you think that the China will actually implement and release the standard?

Henrik Ehrnrooth: Yes, there is a new so-called EN-81 code being implemented. That has some implications on safety devices mainly for elevators and I believe that this could have some impact on the market, but I don't think it will be dramatic. As far as we know, most competitors are able to deal with those changes. China is implementing most of this. Again, I think if you look at the structure of the market, I think many of the suppliers, large suppliers in the market, will be able to resolve it for most players. I don't think that there will be a significant impact from that change.

Andre Kukhnin: Got it, thank you and the last question specifically on a market, on Iran, actually it looks like it's going to be opening up soon. Could you tell us what your position is currently in this market and if it becomes more widely open to international suppliers like yourselves, what would be your plan for that?

Henrik Ehrnrooth: We are of course, as I think a lot of companies, watching the situation very closely. We don't have our own subsidiary in Iran but if the market opens up, I think we are ready to move and following that market and we know who the partners are and we think we can move quite fast if the market now opens up on a more broad basis.

Andre Kukhnin: Got it, thanks very much.

Henrik Ehrnrooth: Thank you.

Operator: We will now take our next question from Manu Rimpelä from Nordea. Please go ahead.

Manu Rimpelä: Okay, good afternoon. My first question would be on maintenance pricing, could you just maybe help us understand a bit better? In those markets where we are starting to see some growth like in the US in the equipment side and maybe some countries in Europe, are you starting to see any sort of improvement in maintenance pricing, and how do you see that working if we see kind of more sustained equipment growth in those markets?

Henrik Ehrnrooth: So first of all you have to remember that even though we've seen a good development now in orders received in the United States, and now we can see more deliveries, the service business comes with quite a delay with that because they are still being delivered to the market and then when you start them, they come off their so-called first service period. So therefore pricing continues to be challenging in this market the same way as it's been before. So we haven't seen significant changes overall.

Manu Rimpelä: So would it be fair to say that if the US market is seeing deliveries now, that maybe 12 months onwards, we should see an improvement?

Henrik Ehrnrooth: Well, let's see how the market develops. We are of course continuously developing our competitiveness and differentiation so that we can have a good development. That is what we can impact. I can't make a prediction on what's going to happen in the market overall.

Manu Rimpelä: Okay and then second question on the GiantKONE revaluation, which I think Eriikka mentioned, was a positive item in the third quarter. So I think that's been a headwind over the last year. So would you be able to give us any sort of a guidance how do you expect that revaluation to impact the financial expenses line maybe this year and for next couple of years.

Eriikka Söderström: Well, guiding that kind of items is not necessarily the right thing to do here but just as a reminder, so on quarterly basis, we have the FX valuation and then at the end of the year we do the whole valuation for the acquisition-related option liability.

Henrik Ehrnrooth: Yes, so Manu, as you know, we don't predict currency exchange rates so that depends very much on those.

Manu Rimpelä: Okay and then final question in the balance sheet, the cash flow remains very impressive. At what point do you start feeling that balance sheet becomes too heavy in terms of the cash position?

Henrik Ehrnrooth: We have a strong balance sheet and we are comfortable. We think that the world has many uncertainties. We have growth ambitions and therefore we think it makes sense to have a strong balance sheet to be able to capture opportunities should they present themselves to the market. That's how we think about it.

Manu Rimpelä: Okay, thank you.

Henrik Ehrnrooth: Thank you.

Operator: We will now take our next question from Phil Wilson from Redburn. Please go ahead.

Phil Wilson: Good afternoon, everyone – Henrik, Eriikka, Katri. It's Phil Wilson from Redburn. I've got a few – three questions, I'll just do one at a time. Firstly, can you quantify the maintenance sales growth in comparable FX that you saw for EMEA and Americas in 3Q? You said 25% for China. What was is for EMEA, Americas and how has that changed during the year. Thank you.

Henrik Ehrnrooth: So we don't break out those sales but as we said, we have grown in all geographic areas so growth has been lower, the growth rate in Europe, Middle East and Africa, and North America overall. So we talk about a slight growth overall in those markets.

Phil Wilson: Thank you. What I was trying to hope to understand that given that EMEA has turned negative minus 0.5%, has that been driven by maintenance slowing sharply or is it just because of the timing of major projects and new modernisation business?

Henrik Ehrnrooth: It's the latter. So pretty steady, the development in the maintenance business.

Phil Wilson: Okay, thank you and then just turning to the US in terms of new equipment, I assume you're seeing double-digit growth. I mean peers are talking about 20% growth. When you look to 2016 and you think about drivers of this good growth, I assume it's things like the shift from single- to multi-family homes, do you think the US will sustain the double-digit growth next year? Just as a sense as to what your thoughts on next year in the US.

Henrik Ehrnrooth: So first of all, the same as with China, we aren't making yet the prediction of what we expect for the Chinese market for next year. If we look at more longer term, I think that there continues to be good opportunities as you mentioned in the shifting patterns of how younger generations live, an increase in single households where only one person lives, all of this is driving a need for more smaller apartments and more multi-family housing over the long term. How it's going to develop next year, I think that we need to come back to in our prediction in January.

Phil Wilson: But we should still think about the US being a growth market next year for you?

Henrik Ehrnrooth: What we expect for this year is a continued good growth market with good trends, and again let's look at next year beginning of January.

Phil Wilson: Thank you and just a final technical question, you talked about the new technology and innovation starting from next year. Can you just scale the incremental costs that we should expect from this, just in case it's material?

Henrik Ehrnrooth: We haven't given a specific guidance, as you know. We have continuously increased our investments in these areas so we are not looking at a step change from this and once we have all of those plans and strategies clear, we may give some more insight into that.

Phil Wilson: Okay, thank you.

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

Guillermo Peigneux: Hi, good afternoon. It's Guillermo Peigneux from UBS. I wanted to ask about credit days and evolution of pre-payment terms in China. How are they progressing as we speak? I have follow-ups but I'll wait for your answer first.

Henrik Ehrnrooth: Okay, so first of all, as you saw and I think the most important sign of that is the continually strong cash flow, which means we've been able to maintain healthy payment terms and healthy business practices, it’s clear that the credit in many parts of the Chinese market is tight and that’s putting some pressure on payment terms, and maybe there's been some small adjustment but no significant changes for us, and you can see through our cash flow that we have been able to have good terms. But there is, given the tightness of credit, that always gives some pressure on it and one has to deal with it, but I think we've been able to deal with it pretty well.

Guillermo Peigneux: Thank you and second, some of your peers in the industry, both local competitors and the international players are in a way suggesting that they may temporarily break the discipline in the market when it comes to returns – regarding China obviously – when it comes to returns and operating profit margins and I'm wanting to understand whether you are ready to walk away when they because irrational on their behaviour or would you compete with them on that, on the same basis?

Henrik Ehrnrooth: First of all, we haven’t seen – yes, we've seen a tight competition for market share but we haven’t seen, on a broad basis, any irrational behaviour. What we are focused on all the time is provide value to our customers, to differentiate, meaning that we have, as we continued to have very strong product competitiveness with good and quality products, we deliver on our promises, which is I think one of the hallmarks of KONE. We believe that we can maintain a good development in markets. That’s what we focus on and that’s how we want to differentiate overall.

Guillermo Peigneux: Thank you and my last question actually. What's, in tier one cities you mentioned, is at the moment looking a little bit more solid when it comes to fundamentals or more solid when it comes to fundamentals, for you what's the best brand, is it GiantKONE or is it the regular KONE brand?

Henrik Ehrnrooth: If we look at the higher tier cities, that's also where we have more of the larger developers, larger customers. That's where KONE would have a stronger presence in these markets.

Guillermo Peigneux: Okay, but there is no aim to try to address that market with maybe a lower price range of products at all, right?

Henrik Ehrnrooth: Well, I would say that of course GiantKONE is also present in there but we have to remember that we have a dual brand strategy and that is with a purpose. We want to have a dual brand strategy and we want these two brands to be differentiated. That gives us a broader market coverage. I think that is what we will continue with.

Guillermo Peigneux: Thank you very much, very helpful.

Henrik Ehrnrooth: Thank you.

Operator: We will now take our next question from Martin Flueckiger from Kepler Cheuvreux. Please go ahead.

Martin Flueckiger: Yes, thanks for taking my further questions. Coming back to the Chinese property market, I've been looking at the latest statistics from the National Bureau of Statistics and I've seen some contradicting signals, at least to my mind, and I was wondering what your view was on this. If we take a look at real estate investment growth, that decline has been accelerating slightly in September. But on the other hand, based on my calculations, the new construction area was up in the mid-teens and I thought that was pretty surprising after quite a number of months now where we've seen some pretty hefty declines. My first question here would be how would you interpret this? Is this just a one-month blip or how do you see this?

Henrik Ehrnrooth: I think with all of these statistics, you may have some differences in national holidays and things like that so just looking at the one month month-to-month figure is not always the best pictures. It always makes sense to look at them over a little bit longer period of time and that tends to give a better picture. But as I said, we have two different messages coming, one is the total sales area that has been sold, number of transactions sales area and pricing that is developing, has been developing for about seven months in a positive direction – and a pretty good positive direction. And then we have, as you mentioned, real estate investment, if you look at Q3 it's slightly negative and continuing negative starts. So there is of course a timing difference between these two. I think it's important and positive that sales there are improving because that's fundamentally what naturally has an impact on the overall inventory and then on the willingness for developers to start new projects.

Martin Flueckiger: Okay, thanks and then coming to my final question on M&A, I seem to remember that KONE has previously argued that M&A continued to be one of the main thrusts going forward and I was – even though in the last few months it's been rather quiet, if I remember correctly. I was wondering what your aspirations here are, whether there has been any strategic shift or changes. How do you see M&A going forward for KONE?

Henrik Ehrnrooth: We continue to be interested in acquisitions and we continue to do a number of acquisitions this year, mainly for smaller independent companies on the service side and also some of our former distributors. That will continue. We want to have high activity there. It's a question of the supply of these opportunities in the market.

Martin Flueckiger: Okay and if I remember correctly, you used to say that you were also interested in bigger players if they were willing to discuss the issue. Is that still the case?

Henrik Ehrnrooth: If there were some bigger opportunities in the market available, yes, we would be interested but you need to have a willing seller to be able to buy something.

Martin Flueckiger: Sure, thank you so much.

Henrik Ehrnrooth: Thank you.

Operator: We will now take our next question from Andre Kukhnin from Credit Suisse. Please go ahead.

Andre Kukhnin: Yes, hello again, it's Andre from CS. Thanks for further questions. I have got couple on –- invariably – on China. Firstly, could you tell us how your own brand versus Giant performed in Q3 and the year to date?

Henrik Ehrnrooth: As mentioned here earlier, KONE is more prevalent in the higher tier cities, GiantKONE perhaps more in the lower tier cities. So based on this, I mean we of course look at China as a whole market but here we see that now the market where KONE operates and the customer base, they are in the better situation therefore the performance of the KONE brand has now been stronger than the GiantKONE brand. But if you go a couple of years back, the situation was reversed and therefore we want to continuously have these two brands so we can address different market situations and this is also the reason why we have a dual brand strategy.

Andre Kukhnin: Yes, absolutely and just on acquiring service portfolios in China, our understanding is that sort of the distributors or sort of – in a layer between you and the customer, they sort of build up service portfolios of up to a couple of hundred units or 500 units and then they are willing to sell. Are you seeing any change in that behaviour at the moment or are you seeing maybe some more of these portfolios coming to the market or those players willing to sell out given the incidents that took place and given the increased scrutiny on the maintenance of the equipment?

Henrik Ehrnrooth: So we have not actively started to buy maintenance portfolios in China. Our organic growth remains very strong and that's what we're focusing on and that's what strategically makes sense to focus on at the moment. So we have been buying maintenance portfolios mainly in Europe, Africa and some Balkan countries, in North America. That's where we are mainly active. China we have not yet become active in buying these maintenance portfolios and there haven't been that many of those transactions. There are some that move hands but not a lot of activity there yet. And again, when you have an organic growth like we have, the main focus needs to be on growing your organisation, building out the capabilities so you can continue to do that with the very good quality that we do at the moment.

Andre Kukhnin: Right, very clear and that not pursuing those maintenance portfolios in China is because of I guess a sheer capacity constraint of how many technicians you have to train to satisfy demand or is there some other reasons? Because I presume there are some of them that contain a lot of KONE elevators?

Henrik Ehrnrooth: As I said, we haven't seen a lot of activity there yet and this may change but currently we are mainly focused on the organic growth in that market.

Andre Kukhnin: Got it. Thanks very much.

Henrik Ehrnrooth: Thank you.

Operator: We will now take our next question from Matthew Spurr from RBC. Please go ahead.

Matthew Spurr: Hi there, yes, it's Matthew Spurr at RBC. Your growth delta over the underlying equipment market in China and referring to the slide 15, your graphic there, perhaps a few percentage points this quarter and previous quarters, it looks – and years – it looks like it's five or more. Do you have any additional insight why you think that slight change was the case, perhaps in terms of talking about segments or large projects? I understand of course the limitation of looking at one quarter in isolation, but anything else you could add there would be helpful.

Henrik Ehrnrooth: Well, first of all I think you said it exactly. It's one quarter. We have to remember that we are the market leader in China, we have by far the largest volume. If we look at the absolute growth, we believe that we have had the strongest growth of anyone in China if you look at absolute numbers. When you have our scale and size, all the time in absolute volume you need to grow so much faster than the others to keep up the percentage rate. So we believe that we have a continued good performance and one shouldn't look at one individual quarter. There are always going to be differences quarter to quarter, very much dependent on how strong the previous year was and so forth. So it's best for us to look at it over a little bit longer period of time. And I believe that we have continued to outperform the market in a good way in China.

Matthew Spurr: And then just in your statement you mentioned that some of the larger major projects were slower. Was that talking then globally or was that specific to China as well?

Henrik Ehrnrooth: That’s globally. If you look at both Quarter 2 and Quarter 3 last year, we had a higher proportion of very large projects. So we have had a continually good activity where we have had even better performance this year, that’s been in our standard volume business, that is still the majority of the business.

Matthew Spurr: Okay, thanks.

Henrik Ehrnrooth: Thank you.

Operator: We will now take our next question from Erik Karlsson from Bodenholm. Please go ahead.

Erik Karlsson: Thanks for taking another question. You mentioned in the report you had good margins on new orders won in terms of your orders, I was just curious to know does that vary by region so that the margins are going up in some regions and down in some and they are stable overall? Or are they stable in most of the regions?

Henrik Ehrnrooth: Of course you always have variation in a business. No business has linear trends in all markets at the same time. As you know, if you look at our margins overall, the best margins we have in our new equipment business is in China, and here we have been able to maintain good margins overall. Where we have had a slight improvement has been in – yes, over already a couple of years’ time – has been in North America.

Erik Karlsson: Very good, thank you very much.

Henrik Ehrnrooth: Thank you.

Operator: We will now take our final question from Phil Wilson from Redburn. Please go ahead.

Phil Wilson: Oh hi, thanks for letting me come back. Just two final questions. Just looking at your maintenance based growth, can you say in Europe and in the US what level of retirement you see from your maintenance base on an annual basis?

Henrik Ehrnrooth: So what we see in developed markets is – it's a very rough number but perhaps one percentage point of the maintenance base gets retired every year. So that's a number of buildings that get taken out of use either temporarily or permanently.

Phil Wilson: And how's that changed – I imagine that hasn't changed much over the last three years.

Henrik Ehrnrooth: That hasn't changed, no, it's stayed pretty constant

Phil Wilson: Okay, great and then just actually changing gears, just going back to China and you talked about the high growth in KONE versus GiantKONE, and I know when you acquired GiantKONE you disclosed a 10% EBIT margin in that business, and I imagine that's gone up a little bit, but given your commentary on overall Chinese profitability that you've made in the past, I imagine that KONE is doing a higher margin than GiantKONE still. Is that the case? And if so, going forward as your orders feed into your revenue, should we are expecting a positive margin benefit from that mix shift?

Henrik Ehrnrooth: First of all, we don't – we haven't disclosed our margins for China for the business. We have a good business in China both for KONE and for GiantKONE. KONE's benefit compared to most of our competitors is we have very good volumes there and yes, we have a good business in China.

Phil Wilson: Are they the same or is KONE higher or lower than GiantKONE? Just a rough sense.

Henrik Ehrnrooth: Again I said that KONE has a benefit compared to I think everyone else given the volumes and the scale that we have.

Phil Wilson: Okay, great. Thank you very much.

Operator: We now have another question from Lars Brorson from Barclays. Please go ahead.

Lars Brorson: Thanks. Sorry, I'll sneak another two in if I can. Just on the affordable housing segment in China, the preliminary numbers we hear is that ahead of the 13th Five-Year Plan that this program will be down some 20-25% in unit terms from the current program. Is that your view too and if so, how are you positioning your business and inevitably your go-to-market strategy for that?

Henrik Ehrnrooth: We don't have any specific information on that so I think we wait and see what government plans are in that respect.

Lars Brorson: And finally, can you give us a sense for how much of your China sales is tier three to five cities, in rough numbers?

Henrik Ehrnrooth: The majority of our sales, well over half, is in tier one and tier two cities, but of course we have important business there in the lower tier cities as well.

Lars Brorson: Understood, thank you.

Henrik Ehrnrooth: Thank you.

Operator: There are no more questions in the phone queue at this time, therefore I would like to turn the call back to the speaker for any additional or closing remarks.

Katri Saarenheimo: Okay, thank you very much. I believe we are ready then to conclude this call so we would like to thank you, everybody, very much for you active participation and wish you a very good rest of the day. Thank you.

Henrik Ehrnrooth: Thank you.