



Transcription

Knorr-Bremse AG – Q2/H1 2021 Conference Call

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13 August 2021



Knorr-Bremse AG – Q2/H1 2021 Conference Call

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PRESENTATION

00:00:00 Operator

Dear ladies and gentlemen, welcome to Knorr-Bremse AG's conference call for the second quarter financial results. And our customer's request to this conference will be recorded. As a reminder, all participants will be in a listen only mode. If any participant has difficulties hearing the conference, please press star key followed by zero on the telephone for operator assistance. May I now hand you over to Andreas Spitzauer, head of investor relations of Knorr-Bremse who will lead you through this conference today. Please go ahead, sir.

00:00:34 Andreas Spitzauer

Thank you, operator. Good afternoon, as well as good morning ladies and gentlemen. My name is Andreas Spitzauer, Head of Investor Relations of Knorr-Bremse AG. I want to welcome you to Knorr-Bremse's conference call for the second quarter results of 2021. Webcast and conference calls will be recorded, and they are available on our homepage www.Knorr-Bremse.com in the investor relations section. Here you can find today's presentations and later a transcript of the call. It is now my pleasure to hand over the call to Dr. Jan Michael Mrosik, our CEO and Frank Markus Weber, our CFO, please go ahead, Dr. Mrosik.

00:01:15 Dr. Jan Michael Mrosik

Thank you, Andreas. And welcome everybody to today's conference call. Today's focus is primarily on the business figures for the second quarter, as well as on our outlook in an environment that remains challenging before we look forward to your questions and comments. In the second quarter 2021 we continued our recovery from the corona pandemic and again, increased order intake, revenue, earnings, and free cash flow, in some cases even significantly. In the second quarter 2021 Knorr-Bremse generated revenues of 1.7 billion euros using an increase of 21% year over year and an EBIT margin of 14.1%, up to 100 basis points. We continue to see a very strong performance from our truck division. DS was the key driver in the second quarter, which in revenues of 879 million euros, an increase of 52%. EBIT margin came in at 11.2% after 3% in the previous year. The rail market globally is still meaningfully impacted by the pandemic. RVS, as expected, generated revenues of 849 million euros stable versus previous year, and an increase as promised versus the prior quarter by more than 5%. EBIT margin came in at 18.4%. In terms of corporate governance, which is an ongoing focus topic at Knorr-Bremse, we managed to shorten our reporting time by one month versus second quarter 2020 and rolled out an employee share program all 30,000 employees globally in July. Moreover, I would like to take the opportunity to cordially invite you to attend our capital markets day on 29 November 2021. We will come back to this topic at a later point.

Based on the overall good results in the first half of 2021, we confirm our guidance for full year 2021. Have a look at the current market situation and business outlook for both divisions on chart 3. Last year, the rail market was moderately



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affected by the pandemic and this year, the recovery is still slow and more protracted. While general market fundamentals are considered to be intact, and long term growth drivers remain unchanged we see ongoing lists of projects, both in OE and aftermarket. We expect this development to remain during the year. Corona persistently results in less rail traffic and fewer trains on the tracks, which affects the whole rail aftermarket business. We saw last year that ridership levels recovered with decreasing infection rates but at this point in time, it is difficult to forecast when we will return to normalized levels again. Nevertheless, we do not have to record any cancellations. Overall 2021 is another Corona year for rail. We believe quarter 1 should have been the weakest quarter for RVS. In Q2 we slightly recovered already. The degree of business improvement should speed up gradually in the second half of this year. Proof of this are very good all the intakes announced by our OEM customers for the past quarter, which will also reach us with some delay.

Overall, we are not happy but also not concerned about the rather slow recovery in the first half of the year due to the promising long term growth drivers of the rail industry. Additionally, we also expect long term that global investment programs supporting rail infrastructure and covering losses of rail operators will mitigate the negative impacts of Corona. On the truck side freight markets have continued to be strong and utilization rates of trucks remain on high levels. Demand is high but truck OEMs have seen several production disruptions and production capacities are limited due to the ongoing supply shortages, predominantly in the field of semiconductors. However, due to the fact that the production of semiconductors has not improved yet, and distributors inventory levels have deteriorated, we expect the situation to remain tense in the second half of the year, and truck production rates, especially in Europe and North America, while China, after several months of very strong growth, started to normalize on a solid level. Truck production rates for 2021 will depend predominantly on the development of the supply side. However, market research companies currently mirror the strong underlying demand by forecasting significant increases in Europe and North America overall in 2021. We share this opinion.

Let me continue with chart 4 and the operating highlights of both divisions. We have reached a very important milestone in our climate strategy already by the end of 2021. We expect to become CO2 neutral. Thanks to our climate action measures and supported by high quality green energy certificates we're going to increase the proportion of electricity from renewables that we use which is why Knorr-Bremse has signed an offsetting agreement with the Berlin based Climate Protection organization, Atmosphere GmbH. This is an important step on the way to reduce our CO2 emissions in absolute terms by 50% until 2030. After two decades of worldwide use, Knorr-Bremse celebrated the 100,000th delivery of the world's bestselling Metro brake control system Cube Control. Also in June, we celebrated the official start of our steering production in Thailand. The new plant is an important step to match rapid market demand in Southeast Asia, and increased KB's presence in the Asian region. Just recently, we announced that KB and Alstom extended their framework agreement of hydraulic brake systems for Citadis trams for another five years. Getting started in the last quarter of 2020 KB is supplying braking as well as entrance systems for 69 Citadis light rail vehicles. The extension marks another joint achievement in the long standing partnership between Alstom and KPA on the Citadis platform. UC, Alstom sticks to our long standing partnership even after they made two smaller acquisitions in the field of rail braking.

Now, coming to our new the newest acquisition, Evac. Evac is a world leading supplier of sanitary systems for regional and high speed trains with over 100000 installed units worldwide. With the acquisition we expand into an attractive market segment in rolling stock and enhance our position as a global systems provider. Evac has clearly a USP as quality leader, which is reflected in solid EBITDA margins above 10% on adjusted level. Its business model is based on



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an asset light strategy, like KB's strategy, and Evac enjoys a high aftermarket share of 40% of revenue. We expect this market segment will be characterized by above average growth opportunities in the coming years. Reliable integrated sanitary systems are an operationally critical component for train operators and necessary for train availability. I guess all of us have had the experience in this regard when it doesn't work. Evac fits very well to KB's business model, and we can leverage its global reach under the bigger umbrella of RVS. This, I would like to hand over to my colleague Frank.

00:11:08 Frank Markus Weber

Thank you Jan, and a warm welcome from my side as well. Thank you for joining us today. Let's talk about briefly our numbers of the first half year 2021 on page 6 before diving into the details of the second quarter. Despite ongoing global uncertainties due to the corona pandemic KB's overall performance and resilience was once more proven by very good financials. During the first six months of 21 revenues came in at 3.4 billion euros, which is 12% higher year over year. The EBIT margin reached 14.5%, an increase by 150 basis points. The free cash flow of 108 million euros was more than 120 million euros better than last year and led to a cash conversion rate of 31% in the first half year.

Let's have a look at the quarterly results on page 7. Overall, our revenues and profitability were even better than our first quarter results of this year. Compared to the previous year, order intake increased significantly by 58% to 1.8 billion euros. The order book grew once again by 18% to a new record level of almost 5.2 billion euros. Revenues increased by 21% to 1.7 billion euros and EBIT margin grew by 200 basis points to 14.1%. Free cash flow could be improved to 131 million euros in quarter 2, resulting in a very solid cash conversion rate of 77% intra-year. We dive deeper into our order intake and order book on chart 8. Compared to the same period last year, order intake on group level increased significantly by 58% to 1.8 billion euros in quarter 2, 2021. On an organic basis, the increase was even higher at around 65% as we were facing again, FX headwinds of nearly 80 million euros. Accordingly, the book to build ratio was again above 1, like in the first quarter 21 reaching 1.04. The development of the order book at the end of the second quarter was particularly pleasing as it rose for the fourth quarter in a row. It grew very strongly by 18% to 5.16 billion euros. This new record figure provides good confidence and is the foundation of our continuously positive outlook. The increase of order book was strongly driven by CVS, which almost doubled its backlog over year over year.

Let me continue with the revenue development on chart 9. Revenues on group level in the second quarter 2021 increased by 21% to 1.73 billion euros. Organic growth was even better with an increase of 25%. Europe continued its growth path and posted an increase of 35% year over year with a 47% share, it still accounts for the biggest part of our total revenues. North America strongly rebounded and revenue in this region increased by 38%. The revenues in the APAC region slightly decreased year over year after strong demand in the second quarter of 2020. The reduction was basically driven by China.

Let me continue with the development of our profitability on chart 10. Our EBITDA margin improved by 90 basis points year over year to 18.1%, driven by good operating leverage, despite headwinds from Corona related costs in CVS, and less contribution from the attractive APAC region in RVS. The aftermarket revenue share decreased year over a year by three percentage points to around 35%, mainly driven by the stronger OE business in our CVS division. Nevertheless, in absolute figures, our aftermarket business increased by more than 50 million euros or 9% to 599 million euros. The



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overall EBIT increased by over 40% net to 244 million euros, despite continuous FX headwinds. The EBIT margin came in at 14.1% after 12.1% in quarter 2 2021. An outstanding increase predominantly benefiting additionally from a very disciplined fixed cost management with even slightly decreased depreciation levels. At the same time, our earnings per share rose by 60% to 1.02 euro in quarter 2, driven basically from better financial results and a reduction of minorities. Let's continue on chart 11. In the past quarter, we continued our investments in future technologies, increased capacity where it is needed, and in maintenance. Nevertheless, we managed carefully and in a disciplined manner, our investment projects. Absolute capex therefore remained on a stable level in quarter two versus previous year. In relation to revenues, capex decreased from 4.7% to 3.9%. At the end of June, networking capital stood at 1.13 billion euros. This is a slight decrease compared to the previous year, despite a 20% increase of our revenues. This was only possible due to our stringent networking capital management, as we were able to reduce the scope of days by 15% from 70.5 to 59.3 days. In the current fiscal year, we expect that networking capitals should be on an overall higher level again in absolute terms, due to the expected sales growth. Annualized operating ROCE significantly improved by 20% from 22.2% to 26.7%. This strong improvement was supported from the before mentioned profitability and is slightly burdened by additional M&A fixed assets that we took on board as the unjust outline.

Let me give you a short overview of the development of our strong balance sheet KPIs as of June on chart 12. Considering the uncertain economic environment, we focused on maintaining a high level of stability and flexibility. Nevertheless, by the end of the second quarter, we had already repaid 100% of the 750 million euros bilateral credit lines that we had drawn because of Corona in the year 2020. Therefore, on a year over year basis, we were able to reduce our gross debt by 34% to 1.8 billion euros. Net debt slightly decreased to 202 million euros. As a consequence of those de-leveraging measures, the good cash flow and our dividend payments, which was contrary to previous year one month in advance, our group's liquidity was only 29% lower, reaching 1.6 billion euros. The very strong resilience of our balance sheet and the good development of our business activities also continuously confirmed by the rating agencies: Moody's rates as A2 and Standard and Poor's with A.

Let me continue with our free cash flow on chart 13. Free cash flow in quarter 2 nearly tripled and came in at 131 million Euros, which is roughly 84 million euros better compared to the previous year's quarter, and 154 million euros higher than in the first quarter of this year. The good development is driven by good earnings as well as disciplined working capital management. We consider this performance as remarkable and see this as proof that our focus and effort regarding cash flow management are bearing fruit. Consequently, the cash conversion rates defined as the free cash flow before M&A divided by profit after tax nearly doubled and improved significantly from 41% last year to 77%.

Let's move on to the divisional view starting with RVS on slide 14. In the second quarter of 2021, order intake of the rail division was at 737 million euros, a decrease of 7% in total, and a minus of 4.7%, organically year over year. Quarter over quarter order intake was up 3% as expected. Relatively slow recovery of order intake was driven by the ongoing impact of the pandemic on the rail market overall. We still face postponements of projects, but strong order intakes by our customers as Jan pointed out, will lead to a better development in future quarters. Considering the lead time for RVS that we usually have, the lion's share of the shift currently occurred in China, high speed trains and aftermarket as well as Metro in the APAC region overall. Europe and North America are developing on a solid basis, both in OE and the aftermarket business. Europe continues to be our strongest and most stable rail market with large orders in the second quarter 21. In our home region rail operators benefit from a number of government and municipal support measures which will also have a positive impact on us. We expect RVS will gain significantly more orders in the second half of



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2021. As we have already pointed out, Q1 should have been the weakest quarter in 2021 with a slight recovery in the second quarter, while half year 2 should see further recovery. Book to bill ratio in quarter 2 consequently came in slightly lower at 0.87 compared to 0.93 a year ago. The order book on the other hand increased marginally to 3.5 billion euros.

Let's move to chart 15. In the second quarter of 2021, RVS recorded revenues of 849 million euros, stable year over year, organically it increased by 2%. But this improvement was offset by FX headwinds. Compared with the first quarter 21 the division as forecasted achieved an increase of 5%. As mentioned before, we strongly believe that the first quarter 21 was the weakest for RVS, followed by a better quarter 2 and further improvements in Q3 and Q4. RVS recorded stable revenues for OE and aftermarket business in the second quarter of 21 year after year. The driver for this development was Europe, which grew at double digit rates in both OE and aftermarket North America and APAC, on the other hand, had to record declines. The aftermarket shelf revenue was stable year over year as well as quarter over quarter as almost 45%. Nevertheless, the stretch of maintenance cycles in China also remains due to ongoing restrictions following Corona. Host operators still have a lower number of trains in service, respectively a much lower utilization since the beginning of the pandemic, and therefore currently need less service and spare parts. The key markets are affected to different degrees, strongly depending on the respective situation. Europe has seen a pleasing development driven as well by some catchup effects, with a year over year growth of 15%. Overall, this region accounted for more than 50% of RVS total revenues in the second quarter of this year. Europe is continuously our stronger region in terms of revenues. Asia, the second largest revenue contributor of RVS is still not back to normalize levels due to the ongoing impacts of the pandemic. The biggest impact came from China, where we had to record declines, especially in the high speed and the metro sectors. The Metro segments year over year revenue decline in the second quarter was a lot as large as the positive development in the first quarter a clear sign of the lumpiness in the rail industry when it comes to quarterly figures. In North America, we see positive signs in terms of freight rail traffic and decreasing number of rail vehicles in depots, but it will take some time before this will have a positive impact on our business. Accordingly, we still had to record declines in OE and aftermarket in the second quarter. Even though the revenue recovery in the second quarter was somewhat smaller than expected, this trend should accelerate in the second half of the year, driven by the OE business and a rather stable share of aftermarket business. The profitability of RVS decreased versus previous year's quarter, which had benefited from an immediate and very effective Corona countermeasures with a volume of roughly 20 million euros as well as negative effects. Please also keep in mind that our second quarter 2020 was driven by strong pull in effects and was profitability wise also one of the best or the best quarter of the year 2020. The third driver was the revenue decline in the APAC region, which is usually margin accretive for RVS. Based on that, EBIT of RVS came in at 156 million euros in the second quarter 21, EBIT margin decreased from 19.9% to 18.4%. The EBITDA margin decreased from 24% to 21.8%. Compared with the first quarter of 2021, EBITDA margin improved by 10 and EBIT margin by 40 basis points.

Let us continue with the development of our truck division on slide 16. Incoming orders CVS were once again outstanding, a clear highlight of our second quarter results overall. At 1.07 billion euros, the overall figure basically was tripled compared to the previous year, driven by extremely strong underlying demand. In the past quarter, demand continued to be strong across KB's key regions on the back of high transport volumes and high freight rates. The demand in Europe and North America should stay strong, but it will be presumably more impacted by supply chain issues in the quarters ahead. APAC saw a flat development driven by as we told you before, for example, the China6 regulation and therefore respective pre-buy effects. In China, demand was strong in Q1 and at the beginning of Q2. However, both May and June volumes already slowed down. As expected Q1 should have been the best quarter for



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CVS in 21. Q2 was always also very strong, but supply issues should have a greater impact on demand in the second half of the year. We expect the second half to be significantly below our H1 figures. The order book of our track division amounted to 1.66 billion euros at the end of June, which is remarkably 88% higher year over year. The order book of CVS therefore ranges well above our pre Corona levels. As a consequence, book to bill stood at 1.22 in the past quarter.

Let's move on to slide 17. CVS posted 879 million euros in the in revenues in the second quarter 21; compared without last year's figures, this is an increase of 52% on an organic level even plus 59%. CVS saw a positive development in all channels, such as OE business and aftermarket business in all three major regions, e.g. Europe, North America and APAC. The share of aftermarket sales decreased from 29% in the previous year to 25% driven by the extraordinary growth in our OE business. Nevertheless, in absolute numbers, aftermarket was up by 50 million euros or 31%. In the second quarter of this year, CVS achieved an EBIT of 98 million euros, which is significantly higher than a year ago. The EBIT margin or return on sales amounted to 11.2% compared to 3% one year ago. Besides this strong development, profitability was basically burdened by higher Corona related costs for freight and higher material cost for semiconductors. In total, these costs amounted to around 20 million euros in the past quarter. For the full year 21, we currently expect these costs to move up further.

Last but not least, I would like to give you an update on our guidance. For full year 21 on group level, we confirm our guidance given in March and continue to expect revenues between 6.5 to 6.9 billion euros and EBIT margin between 13 and 14.5% as well as an EBITDA margin between 17.5 and 19%. Normally there are good reasons to reduce these bandwidths at this point of the year, however, as outlined, several uncertainties, e.g. due to Corona are still high in both business fields, as well as in the respective revenue channels. Also, the experience of the development in the second half of last year teaches was rather to be cautious. We expect the following divisional full year development in 21 compared to the prior year: for CVS, a significant revenue growth with a significant margin increase; for RVS, a slight revenue growth and margins almost stable compared to last year's level. With this, I hand over back to Jan.

00:31:21 Dr. Jan Michael Mrosik

Thank you Frank. Let's move to slide 19 of the presentation. And as mentioned at the start of the presentation already, we will conduct the capital markets day at the end of the year to give you an update on our strategy, or divisional priorities, and a deep dive of our value drivers. We cordially invite you all also on behalf of my colleagues on the executive board to this event on the 29th of November, in which format this event will be held we will decide in the next few weeks. We hope for a physical exchange, but have to follow the Corona situation very closely. Health and Safety remain key priorities for KB. Either way, it will be possible for you to participate virtually, we all look forward to the event.

Let's called conclude our presentation on page 20. Q2 21 was overall a solid quarter. We achieved these good results under ongoing challenging conditions. I would like to take this opportunity to thank our employees for their contribution, their hard work has paid off. We will continue to need a motivated hard working team in the coming months to master all the other challenges that lie ahead. We look forward to that. This year and maybe even beyond we will still be faced with a pandemic and as a consequence we also assume that the tense supply situation will continue to accompany the truck division for some time. We as KB feel strongly positioned and are ready to react quickly to all market conditions. We also



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benefits from having two divisions that are active in businesses with different economic cycles. PVS has demonstrated its robustness and strength with continuous market outperformance and well managed business operations, despite headwinds from the supply side. In addition, underlying demand remains very strong. RVS is right now impacted more by Corona, especially by weaker market conditions. Our market trends of green mobility and urbanization are fully intact. With that, I'll turn the call back to the operator to begin with a Q&A session. Thank you.



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Q&A

00:34:18 Operator

Dear ladies and gentlemen, we will now begin our question and answer session. If you have a question for our speakers, please dial 01 on your telephone keypad now to enter the queue. You can ask the question. If you find your question has already been answered you can dial 2 to cancel your question. If you're using speaker equipment today, please lift the handset before making your selection. One moment please for the first question.

00:34:56 Arsalan Obaidullah (Deutsche Bank)

Hi, good afternoon, everyone. Thanks for taking my question. Just one thing and I hope I am not reading too much into this, you talked about last time sort of seeing a recovery in sort of ridership levels. I think you gave the figure of sort of 2023. But you sort of I think the message here is things remain more uncertain. Is that sort of now a shift in sort of looking at things a bit more bearish or negatively on sort of rail ridership globally? Or hasn't really been things haven't necessarily changed?

00:35:34 Dr. Jan Michael Mrosik

Yes, thank you very much for this question which is quite an important one, since it drives and determines to some extent, what happens in the aftermarket. So the picture there is quite different. If you look at, for example, France, their ridership is already back to normal. If you look at other countries, like, for example, and I'm currently looking at Germany, we have minus 10% right now, in the UK, for example, the levels are more around minus 15%. So that tells you that the situation is very, very different in the different countries very much dependent on how the COVID pandemic develops and unfolds. And, yes, that's the current situation. And, you know, at the end of the day, that's something that pretty much determines how our ridership in the future is going to look like, obviously, vaccinations, they also play a role. So that's the overall picture that we're seeing here.

00:36:47 Arsalan Obaidullah

Okay, but you're not necessarily ... your view hasn't sort of changed on that in terms of, since you last came in terms of your seeing things to be stretched out in terms of recovery? Or has that changed last few months.

00:37:01 Dr. Jan Michael Mrosik

Yes, we said that, that things might take a little bit longer to recover, we're seeing countries that are faster now in terms of their recovery. And just, you know, to mention as one example, France, but also Germany, where it's pretty close to



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free Corona situations. But in other countries, like the United States, by the way, is another one -15. So their recovery went quite strongly. UK is a little bit lagging behind. So I would say things are moving towards pre COVID levels with some, let's say low degree, two digit numbers below.

00:37:51 Arsalan Obaidullah

Thank you, and then just sort of staying on the topic of rail. My second question, looking into sort of China and this sort of competitive dynamics there. How are you sort of seeing that both again, on the high speed and the metro and how you sort of seeing yourself placed for that sort of going forward?

00:38:13 Dr. Jan Michael Mrosik

Yes, if you if you look at China, and our business in China, it should be noted that our business in China has moved in the last couple of years already from a very much high speed driven kind of market participation into something that's pretty much more leaning towards the metro business. So if you look at its high speed, our current percentage of business it is more in the range of a little bit more than a low single digit number, so to speak, Metro is already in the range of roughly 40% and aftermarket 40%. That means that a very strong part is really driven by a quite robust aftermarket business. And Metro, as we all know, is also business that's pretty much decided on by provincial governments and this centralized decision making is an important part there. So that's kind of the structure that we have in our Chinese markets in our Chinese business at this point in time.

00:39:42 Akash Gupta (JP Morgan)

Yes, Hi, good afternoon, everybody. I have two questions as well. The first one is on rail. And I guess you are guiding for some recovery in the second half and do you I think we should be able to finish the year with one times book to bill, or given some push out in China and given some travel restriction there and recently because of COVID outbreak, do you think there is any risk that this this book to bill might come down below one time for rail business for the year?

00:40:25 Frank Markus Weber

Thank you. Frank speaking, I will take your question. We do strongly believe at this point in time that we have good chances to reach a book to bill that is on the level of one, this is what we are of course currently targeting. And we should, as we outlined already in a qualitative manner, we should see good order intakes in the second half of the year, significantly above the levels of the very first half of this year. And with increased revenues, we should be able to come



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to that level for the full year in the book to bill that you were asking. So my answer was based on that question, full year book to build above one.

00:41:18 Akash Gupta

Thank you. And my second question is on second half margins versus first half margins. If I look at last 40 years, then on an average second half margins around about 90 to 100 basis points higher than first half. I don't know whether there is any seasonality there. But looking at this year and given these raw material headwinds that started coming in Q2 and might be lasting in second half. Can you comment on second half margin improvement versus first half? Could it be possible or are we more likely to see stable development on profitability levels? Thank you.

00:41:57 Frank Markus Weber

Akash, thank you. I mean, you're mentioning already the right point. I think in this year 2021, we have a slightly different situation, given explicitly the topic that you mentioned, we do think that we will see uncertainties on the semiconductor side influencing our revenues on the CVS side in the second half of the year, which would mean that we can't achieve the operating leverage that we had in the first half of the year. So due to that fact alone, we see a slight pressure on the margins on the truck side. And the second point is also that those special costs that I referred to, like increased freight costs, as well as material costs for semiconductors that we to a large extent at this point in time purchase from brokers should also be higher in the second half of the year, as they basically only occurred in the second quarter in the first half year. So it should be higher in the second as well. And then you also have to see that especially the second quarter in 20 ... but you're asking only about 21. So those two major aspects, I would say, are the driving forces behind the situation that we see a rather lower margin on the second half of the year from today's perspective.

00:43:52 Lucie Carrier (Morgan Stanley)

Thank you, ladies and gentlemen, and thanks for taking my question. I have two question. I will go one at a time. And the first one is, to some extent a bit of a follow up on Akash's question, but maybe in slightly more general terms: when you think currently about the dynamic in your backlog, so kind of what have you been, you know, executed to now? How do you think in terms of the balance of raw materials, supply chain constraints, potential delays that then you could see maybe in CVS is a supply chain constraint or kind of continuing? Especially and I guess my question brings us a little bit more as we go into 2022. How do you assess the quality of the backlog versus maybe what you have seen the previous years?



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00:44:43 Dr. Jan Michael Mrosik

So, I think, first statement is and then Frank might want to add to that, is that in our outlook, we have a very balanced view on opportunities and risks and these risks also contained the quality of backlog. And let's say supply chain challenges that we might, or that we will continue to face in the second half of the year. And therefore, this commitment and the clear view that we stick with our guidance here contains both elements, the opportunity, and the risk thereof. Talking about 2022 I think it's kind of common sense in the automotive market as well in the CVS market worldwide, that the semiconductor shortages will probably continue to accompany us for the next couple of months and probably even beyond the end of this current calendar and fiscal year, because the capacities on the semiconductor side cannot quickly be updated and increased on the supply side, and therefore we will have to live with shortages in the medium term.

00:46:19 Frank Markus Weber

And may I continue? Basically, we are not seeing a change of the underlying demand that is out there on the truck side, we do believe that the market is intact and that basically Europe will grow when it comes towards levels of 2022; from a TPR point of view, North America should be able to grow, we think Japan should be able to grow, India should be able to grow. And the only region that potentially is supposed to be going down even slightly further is China, as we discussed already also several times, we do think that the book to bill ratio that we would achieve on the CVS side should be significantly above 1, but below the levels that we saw in the second quarter. So that overall gives us quite confidence that the major market growth is intact. Needless to say, we do somehow assume that some of the orders that we saw and see in the year 21 already might be some safeguarding some pull ahead, orders from some of our customers in order to be well stocked, so to speak, but the general trend, we think is very healthy.

00:47:56 Lucie Carrier

Thank you for that, so if I just can have a quick follow up on the on the backlog quality more on the obvious side than in regards to the mix. How do you see the mix evolving, you know, versus the previous year? Because I seem to share the sense and that you expect kind of Europe to continue to be growing much faster? Probably the mix? And I'm just curious about what's the potential impact on profitability level?

00:48:24 Dr. Jan Michael Mrosik

If you look at the TPRs, and I assume that this is the rationale behind your question.

00:48:37 Frank Markus Weber

Lucy, were you asking in regards to CVS so to rail?



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00:48:42 Lucy Carrier

No, to rail, on the rail side.

00:48:47 Frank Markus Weber

Lucie, look, the thing is that I mean, we have outlined so to say that currently we see is rather stronger in relation an original prospective, rather stronger growth rates in the European business, than on the APAC business, as we just presented and given that, so to speak we do see that on the order book side there is a slight positive trend for the European share. We do know that they also said that the APAC business is basically accretive. But it's not that dramatically so to speak that you would have to have for future use out of our existing order book a significant fear of that, but we see that shift towards Europe. Yes. And yes, the Asian Pacific business is rather accretive compared to the European one.

00:49:50 Dr. Jan Michael Mrosik

And maybe just one addition going forward. We have to also keep in mind that that currently the aftermarket business is pretty much on the rail side affected by the COVID pandemic. Since ridership is still affected, despite the recovery that I was just talking about, and therefore maintenance cycles are stretched, and overall train utilization is lower. So this aftermarket business is therefore a little bit drawn back in terms of the underlying and with COVID disappearing, that that should also, you know, make its way out of all of the numbers and patterns, it obviously depends on the way the pandemic evolves.

00:50:38 Lucie Carrier

And it's just thank you very much. And my second question was more related to comments you maybe have made this morning during the press calls regarding the M&A strategy and saying that in the future, you will be more prudent around this and a strategy. Are you able to kind of explain, you know, precisely what you mean by a bit more cautious?

00:51:06 Dr. Jan Michael Mrosik

You know, at the end of the day, I would like to remind again, that, as we all know, we've in the past, and we will put in the future very strict KPIs to any M&A activity that we will execute. And this is around value creation. So it needs to create any kind of activity in that regard needs to create value for our shareholders and for the company as such, and therefore, this is the major point, while we also refrained from the opportunity that we have been evaluating in the recent past, because it didn't meet our requirements, as far as value creation is concerned. And therefore, going forward and Evac is probably a very good example of what we have in mind as the first priorities for M&A, which is acquiring companies that have a close vicinity to our current business, and add value in terms of high margin as a strong



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aftermarket business component, and kind of a sticky business that really, you know, fits well with our business models. So that's obviously our first priority. And, you know, we will obviously look for opportunities that present themselves but always under this kind of kind of KPI precondition that opportunities would have to meet in order to be seriously considered from our side.

00:53:09 William Mackie (Kepler Cheuvreux)

Good afternoon. Thank you. Three areas, pricing, productivity, and a follow up on M&A. On pricing: Could you just give us a sense of how to what extent you're able to compensate for the pressures on the cost side on the various issues you've highlighted with better pricing, either around OE in CVS and RVS, or particularly in aftermarket? And also, given the pressures that we've discussed around semis and logistics and also more materials in many areas? To what extent are you able to adjust or accelerate productivity actions to further compensate? It's always historically been a very strong point of the company. So that's those two and then on M&A. A couple of things. Where you are on the arbitration processes with Bosch and reaching an agreement on the purchase of the minorities that are outstanding, which I think you're now have an obligation to purchase? And what is the pipeline for M&A looking like alongside the recent deal that you've announced? Thank you very much.

00:54:36 Frank Markus Weber

Thank you, William. Let me start with the first question. Yes, you're right. We have currently certain issues and basically, one is the high freight cost that we are having which is also a headline consisting of additional freight costs per se container freights, etc. Some coming out of kind of uncoordinated processes in these semiconductor times like special airfreights and stuff like that, you have certain inefficiency as a next topic. Of course, the increase in running the plants, you can't always predict when the respective shifts should happen and whether they can be happening on time. Sometimes you have to run extra shifts over the weekends on a Saturday and Sunday, with some additions then to the salaries. To mention three here and, and the other is raw material, we start from the back. Raw material as Jan just outlined, we do have, fortunately, good guide clauses, basically in our contracts with the customers that allow us to basically spill over the respective cost increases that we see in our profit and loss. Towards the customers, this at some time, has, as it's called sliding clauses until a certain threshold is reached for several weeks or sometimes several months, you have the cost sitting in your accounts. And this is a rather minor amount that we are facing this year, really minor one. The bigger one is the freight costs and the additional costs for the semiconductors. And they are the measures. So the countermeasures, on the one side, would be the glide process that would allow us to spill this stuff over in regards to raw materials, or for the other costs, we are discussing with our customers in order to that the customers also pay their fair share, those negotiations are running, we have seen the first results already in the second quarter. In the last month of June, we already got the first reimbursements. But we expect, so to say more to come. And of course, also more cost to come. And as I said, it's maybe from customer to customer different, whether the one assumes a fair share to be 50%. The other would say maybe 40 to 60, we have a certain assumption for full year. And we are striving very, very hard with our procurement and sales department in order to reduce on the one hand side the cost for the purchasing colleagues, and on the other hand, to get more reimbursements in on the customer side; this is, I



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think one important thing. In order to nevertheless whatever is the net in our books, at the end of the day, in order to compensate for that we are running additional productivity programs on the one hand side on the more production oriented areas, as well as on administrative areas, in order to best possibly compensate for all those issues that we are having. And as you rightfully said, this costs discipline and the running in these kinds of cost measures is one of the strengths of KB. And this is what we're currently doing. Can everything be offset? I don't believe so there will be a net amount at the end of the full year 2021 that we will be having in our books. That is what we currently assume. And that's what's baked in, in our guidance, of course already.

The second question is in regard to Bosch. And the fact is that we have not reached an agreement. You maybe know for my (pause 59:01) you know from our statements in March, that we had to get into talks with Bosch in order to find a solution. And the fact is that we have not finalized these talks with a positive ending. So there is a second arbitration proceeding that was just started in July in regards to the 379 million euro, which we have in our books as a liability.

00:59:38 William Mackie

Thank you very much and the pipeline of additional deals either in CVS or RVS, a feel for how you're developing the bolt-on strategy?

00:59:52 Dr. Jan Michael Mrosik

What are we currently having in our pipeline is indeed targets that would exactly fit into what you just call bolt-on strategy. So that's what we're primarily currently looking at.

01:00:13 William Mackie

Okay, thank you. Sorry, one final follow up which relates to China RVS. Can you just sorry to come back to this, can you just share your thinking on the development of revenues for RVS China in H2 around Metro high speed and aftermarket?

01:00:32 Frank Markus Weber

Yeah, thanks for the question, obviously a detailed one. We do from today's point of view, rather think that the revenue development half year one to half year two is somehow on a stable basis. This is what we currently anticipate. And we also do think that this is also true for the region in regards to profitability. So no change in profitability for the region, but somehow stable revenues half year one compared to half year two.



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01:01:23 Alfred Glaser (ODDO BHF)

Yes, hello. Thank you for taking my questions. I have two as well. My first one is on the track division CVS. Could you explain a bit more what you expect in terms of revenues in the second half of the year, compared to the second half of last year? What are the different factors? And what kind of growth rate would come out of this? And I will ask my second question afterwards, please.

01:01:59 Frank Markus Weber

Thanks. I think our current plan is to at least somehow be on a similar level, like we have had in the quite good and progressing quarter three, quarter four of last year 202. It should be slightly excessive. And this is what we currently think with all the uncertainties that are around there in regards to the supply chain, as I outlined, but you see that it's significantly lower than the first half year.

01:02:48 Alfred Glaser

All right, and how would you see business in Europe and North American for CVS in the second half of the year, compared to last year?

01:02:58 Frank Markus Weber

I would say in Europe would be rough roughly seeing that on similar levels, similar levels roughly. North America on higher levels. That's basically the biggest ... and I mean, Asia, Asia Pacific region, as well on somehow similar levels.

01:03:29 Dr. Jan Michael Mrosik

I think I would like to make one comment from an overall meta perspective. We see that as, and you're probably all aware of that, that there was a kind of pre-buy effect in China, starting with Q3 last year and extending its way into at least Q2 the beginning of this year. And we'll see the TPR in China in quarter three and quarter four, coming back to normal levels, still good levels of production, in principle as far as the demand is concerned, and then positive market dynamics in both Europe and the United States. So that's kind of the macro picture that we are seeing on the demand side. What kind of the demand can be fulfilled is obviously dependent on the semiconductor supply situation. So that we have to take these two factors in principle as a multiplying fact into account.



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01:04:42 Alfred Glaser

Thank you. So for these additional comments. I have another question, which pertains to M&A. There has been actually a bit announced on Schaltbau sale in the rail space. What is your take on this? You think that Schaltbau might have a fit with KB? And what do you think about the proposed price for this takeover?

01:05:08 Dr. Jan Michael Mrosik

As I understand it, in the last couple of days, it has been announced that the buyer is identified and that the deal is in fact done. That's according to what I know. And what we heard out of the market in the last couple of days, so that would be my take on it. I think it goes to private equity, if I'm not mistaken.

01:05:38 Alfred Glaser

Yes, it seems but maybe it's not the final saying in that story?

01:05:48 Dr. Jan Michael Mrosik

Yes, that's, that's what we what we know about it.

01:06:01 Iris Zheng (Credit Suisse)

Thank you. Good afternoon, everyone. And thank you for taking my questions. I've got three, two are on the rail division. And the third one is more housekeeping questions. And I guess I will go one at a time. So my first question is on your comment about still delays in large orders for rail? And maybe could you give a bit more color on do you mean, the slower orders more coming from the OEMs customers that you have, or slower from the rail operators, or maybe it's because of the different geographic mix because compared to your European OEMs customers, then you have a higher exposure to acer pack and it looks like it's relatively small in that region, I think it will be very helpful for you to give a bit more additional color just for to reconcile the different order dynamics that we are seeing from you and versus some of your European rural OEM players. Thank you.

01:07:03 Dr. Jan Michael Mrosik

Right, so the large orders, delays that mainly comes from Asia Pacific, and there is order shifts on the high speed side as well as on the metro side in China as we're seeing it right now. And then another area where orders are being shifted out is India, which is obviously very strongly affected by the pandemic. So that's all pertaining to the OE side, obviously, other shifts here and there throughout the world that are somehow in connection with COVID. When it comes to



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aftermarket business, that's something that is sometimes OE business, if the aftermarket business goes through the OEI, but it's in some cases also the end customer meaning the rail operators, that would be directly ordering the aftermarket businesses, the service business with us. Kind of a mixed picture there.

01:08:16 Iris Zheng

Very helpful. And maybe again, on the rail division and on the on the revenue side for the full year I prefaced that before your guidance hadn't been changed, but I think in early this year, the guidance or the comments for the rail division revenue growth is for it to be like higher OE growth versus a flattish aftermarket growth picture. And do you think it is still going to be the case as you see it now for the full year? Because from what I can see of that, the OE and aftermarket developments year to date isn't too different was even a slightly higher decline in OE than aftermarket?

01:08:57 Frank Markus Weber

Thank you for that question, Iris, you are indeed right that in my speech just some 30 minutes ago, I did give you a qualitative picture of how we see the remainder of the year, or the full year. And this differs from what we have told you in March, as we know it better now. We are some four months more into the year. And we said for rails so far that we expect solid growth. That's what we said in March, solid growth and only slight margin improvements. And now we rather think about a slight growth, which is 0 to 4.something percent, and on the stable rather stable, almost stable margins. So this is a changed situation that we think as Jan also pointed out in his speech, that we see the recovery on the China side slower than initially expected. But at the same time, what I also did mention, we changed the forecast so the qualitative guidance for CVS upwards, we talked about solid growth and solid margin improvements. And now we're talking about significant growth and significant margin improvements, which is, according to our definition, well above 10%. And on the margin side, this means more than 1.5 percentage points of profitability increase.

01:10:48 Iris Zheng

Thank you for the color. It's very helpful. And my last question is on the ERP system because I record that there has been an ongoing, long, ongoing program. And can you give us an update on how is it going and when it's going to be finished?

01:11:05 Frank Markus Weber

Now, thank you. Thanks for such a question as well. It's running well, I would say, we have some months ago until Easter of 2022. We will be going live; this plan has not been changed over the last 14 months that I'm now with the company. So it's really running well. The colleagues at KB are doing a good job. We are in budget with our spending and



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time and quality, I would say and we have chosen to the migration efforts the weekend, the Easter weekend of 2022 always to be to have the go live.

01:12:10 Alexander Hauenstein (DZ Bank)

Yes, hello, I have two questions left from my side. First of all, with regard to your comments on this influence on the first half of 2022. I mean, is this going to be read from our side as a message that 2022 consensus expectations of 1.4 billion EBITDA are probably too high? I mean, how comfortable are you with this kind of consensus on what's your way of thinking? I know you're probably not giving a guidance yet. But is this a hidden message maybe that we might have to look into our assumptions on that front? Or how should we think about it? And the other question would be more general on M&A, I mean, based on your experiences during the HELA process, what are your key takeaways and learnings for your future M&A plans here, which could you share with us, please? Thank you.

01:13:15 Frank Markus Weber

So let me start maybe with the first part of your question, not 100% sure whether I got the message completely right. Let me try. And then you tell me whether I'm totally mistaken. My let's say indications in regards to the semiconductor situation that this will linger on somehow it might also link on to 2022. And the book to bill a situation I described somehow and the TPRs that I mentioned to be expected. Not in any kind of meaning had the intention somehow to say adjust your estimates for the year 2022. Not at all. Not at all. No, not at all.

01:14:18 Alexander Hauenstein

This was exactly the question whether this was a kind of a hidden link to getting people rethink about that estimate for next year. But it seems not to be the case. That's good to hear. Thank you.

01:14:24 Dr. Jan Michael Mrosik

I found that as far as the second question is concerned, let me comment on this. I think the key learning for us is that we need to communicate and explain our M&A strategy and also maybe our strategy overall better to the capital markets. Our approach here has been always a value based M&A strategy, a value generating based M&A strategy, and as also in this process, that you're referring to being always a value based M&A strategy and evaluation. And that's why at the end of the day, you know, having first assumed value generation, in this particular opportunity refrained from further pursuing it, because it did not meet our expectations in that regard, and therefore, we are going to invite you to this capital market day on 29 November in order to explain to the capital markets and the community, our M&A strategy and our strategy in general in a greater level of detail. And of course, on the way there we will continue to communicate with



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the financial community in order to make it ongoingly clear how we strategically move. And that's, I think, the most important learning that's you've been asking about.

01:16:03 Alexander Hauenstein

Okay, thanks a lot, looking forward to the event.

01:16:09 Andreas Spitzauer

Hey, so thank you very much for all your questions. We hope you have a lovely summer time and looking very much forward to talking to you thereafter. So have a nice weekend and thanks and bye-bye.