Rheinmetall AG
Investor Relations
Conference Q3 2022
Transcript

Publication: 14:00 am CET
Conference Call: 10 November 2022, 14:00 – 14:53:10 pm CET

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Rheinmetall AG Conference Call

00:00:01 Operator

Good afternoon, ladies and gentlemen, and welcome to the Rheinmetall AG conference call regarding the third-quarter results 2022. At this time, all participants have been placed on a listen-only mode. The floor will be open for your questions following the presentation. Let me now hand the floor over to Helmut Merch.

Helmut Merch

Thank you for your kind introduction and a warm welcome to all participants to our Rheinmetall Q3 2022 earnings call. Before I have the pleasure to walk you through our Q3 presentation, I would kindly ask you to take note of our legal disclaimer on the following page.

Let's now start with the highlights on page number three. The third quarter was in line with our expectations and showed already good progress for the year-end rally. Group sales grew by 12% to roughly 1.4 billion Euro and operating profit rose by EUR11m to EUR117m compared to last year. Operating margin slightly advanced from 8.1% in Q2 to now 8.3% in Q3. The operating free cash-flow improved sequentially and accounted for minus EUR37m despite the continuing strategic working capital build up.

Additionally, the first ring swap agreement with Czech Republic has been signed and we are expecting more countries to follow similar agreements with Germany paying for it. In October, we also took an important step in our ongoing strategic reorientation. We signed the sales purchase agreement with Koncentra Verkstads AB Group located in Gothenburg, Sweden, for our large bore piston business.

Last but not least, we confirm our full-year sales and margin guidance for 2022.

Please turn now to page 4.

Our portfolio transformation made an important step with the signing of the sales purchase agreement for the large bore pistons business in late October. It was our aspiration to leave our pistons production operations in good hands and we are convinced to have achieved this step with the Swedish group Koncentra Verkstads AB. The transaction covers roughly 290 employees on sites in Germany, the US and in China with an annual sales volume of around EUR80m. We expect to close the deal beginning of 2023.

The sales processes for our minority shareholdings in the Indian company Shriram and in our Chinese joint venture with our Japanese partner Riken are also on a good track. We also continue the disposal process for the remaining small bore business and we will inform you on the progress.

Please follow me to the update of the German market on page no. 5.

Despite the political commitment to the „Watershed era“ and the strong military, economically and political support of the Ukrainian people, the German government has not been very clear on the speed of its defence spending ramp up. This brings near-term uncertainty and lower visibility. We have clearly to realize that the process to transform political statements and wishes into actual orders is slower than expected in the first half of this year.

But we are in close contact with the German customer and we are making good progress in our negotiations. However, the immense size of the created demand apparently stretches the procurement resources. Additionally, new factors like the high inflation in general and particular in raw materials and energies have recently put a strain on the EUR100billion fund. This led to a reassessment of some projects on the customer side, mostly affecting navy and air force projects. Therefore, it is now certain that some orders that we expected for 2022 will slip into 2023. The scope of the projects however remains basically unchanged to our present knowledge.

On the “Schwerer Waffenträger”, that is a boxer with a Lance turret, we are working on a government to government deal for 100 systems together with Australia to deliver those directly from our running production in Australia to the Bundeswehr. A decision is expected in course of H1 2023. The negotiations for the German Soldier Systems are on a good way. We expect the first orders and sales already for Q4 2022. The associated framework contract is anticipated for the first half of 2023. Puma upgrades for the first lot are confirmed and expected to be signed before year’s end. The current discussion around the Marder-Successor for the new medium forces if it might be a wheeled solution, which is a Boxer or a tracked solution, which is the Puma is still continuing. This does not have a material impact on us since both vehicles are from us and the overall budget remains unchanged. On the truck, we expect a decision for a framework contract also in H1 2023.

There is now eight months of war in Europe. Despite several deliveries to Ukraine, the *Bundeswehr* has not ordered a significant amount of ammunition. A further increase of the ammunition budget from around EUR1billion to EUR1.5billion is currently under discussion. And this would be clearly beneficial for Rheinmetall. We expect an ammunition framework agreement to be signed also in H1 2023.

In a nutshell, we think there is still up to EUR30billion order intake potential in Germany within the next years. Despite the delays, we are still not concerned and continue to do our best to deliver on the order intake from Germany. And our growth story is therefore totally intact.

Now move to page no. 6.

Our two commonwealth home markets remain dedicated to increase defence spending and strengthening their defence capabilities. Both have increased their defence spending for the next years!

Our won Land programs in Australia continue to progress according to schedule. We are still expecting to see an announcement of the Land 400 phase III before year’s end or at the very latest in Q1 2023. Due to the already advanced time of the year, it is however unrealistic to expect any signing until year's end. Commercial negotiations will only start after the winner has been announced. We remain pretty confident that our chances are good. Further potential for Australia will arise from still outstanding tenders of the rearmament program for example for the naval protection systems and others.

The UK seems to consider a heavier focus on wheeled tactical vehicles, which offers a good perspective for the Boxer, with already more than 500 vehicles under contract and a potential of almost doubling this to around 1.000 vehicles with orders coming in 2023 and 2024. And we see additional potential from the UK for an ammunition framework contract.

The first ring swap agreement has finally been signed with the Czech Republic in October. This contract design provides for a replacement of soviet era vehicles sent to Ukraine with NATO standard equipment. Germany is paying for the vehicles from industry stock, namely Rheinmetall stock. So we are going to deliver Leopards, armored recovery vehicles, infantry fighting vehicles like the Marder for Greece and trucks to the nations participating in the ring swaps. First vehicles were already delivered in Q4 2022. And the total volume for the ring swaps will be roughly EUR450m with majority of the sales in 2023.

Follow me on page no. 8 to the financials. Please be reminded that all figures apply to the continued business activities only unless stated otherwise.

Group sales of roughly EUR1.4b grew by 12.5% including a positive FX and M&A effects. Despite the pressure from the inflationary macro environment, we were able to repeat our strong last year's margin level from Q3 2021 by reaching 8.3%. This lifts operating profits to EUR117m.

Reported earnings per share from continuing operations increased from EUR1.69 to EUR1.76 in the third quarter of 2022 compared to the prior-year period. Q3 did not report any special result effects.

Please continue on page no. 9.

Operating free cash flow from continuing operations in Q3 accounted for minus EUR37m and was on level with the amount of minus EUR34m in Q3 2021. The operating free cash flow was again influenced by the ongoing, but slower working capital build up. Higher customer payments mitigated this effect.

The main driver for the increased capex in Q3 was the purchase of our existing air defence production site in Rome, which we formerly rented.

Let's have now a look at our strong balance sheet on page no. 10.

The equity ratio rose to 35.7% as of end of September, well at the upper end of our target range of 30% to 35%. Net financial debt from continuing operations declined to minus EUR958m at the end of the quarter, compared to positive liquidity of EUR118m in December 2021. Main drivers for this decline are the continued working capital build up, payments for acquisitions and the dividend.

One short comment on our pension obligations: The positive effects from the further increased discount rates especially in Germany and Switzerland continues, reducing our pension provision to now EUR484m. This figure is the lowest number since 2009! At the end of the quarter, we reported a cash position of EUR196m and securities held for trade with a value of EUR132m.

Moving now on to the divisional performance on page no. 11.

We saw again a strong sales growth across all our divisions. Vehicle systems grew at a lower pace compared to the two other defence related divisions and reported sales of roughly EUR470m, representing a growth rate of 8.1%. Due to the good operating leverage, the division showed a strong margin of 9.7%. Cash situation was mainly impacted by further inventory build up.

The division Weapon and Ammunition expanded its operating margin to a remarkable 12.8% in Q3 benefitting from its top line growth of nearly 25%. This translated into an improved operating free cash flow growing by EUR15m.

Electronic Solutions delivered an excellent sales growth of around 18%, driving the operating result to EUR25m, which included, however, EUR1m start-up losses from our acquired EMT drone business. Cash flow was helped by the receipt of milestone payments for air defence projects. Sensors and Actuators increased sales by roughly 15% in a quarter with further market recovery, but was faced with challenging market conditions especially regarding the raw material situation. Hence, the operating result declined from EUR23m to EUR16m. Consequentially, the margin shrunk to 4.5%. The operating result was under pressure from not fully compensated input cost. The margin is expected to recover in the running Q4. Favorable development of working capital improved free cash flow by EUR5m.

Materials and Trade rose sales by 14% to EUR188m resulting in a strong margin of nearly 10%. This improvement of 70% was supported by the end of the Chinese lockdown restrictions and the return of positive at equity contributions accounting for EUR5m. The main reason for the improvement in cash flow are improved earnings.

Rising consolidation effects can be observed in sales and operating result since the beginning of this year. For the full year 2022, we are expecting this effect to be around EUR500m in the sales consolidation and around EUR90m in the operating result consolidation line. Higher intra-divisional activities and increasing overhead cost for corporate R&D activities and the necessary transformation of our IT landscape will keep the consolidation line effects on this higher level for the next two years, 2023 and 2024.

Slide 12 presents the order intake and order backlog profile for the divisions Weapon and Ammunition, Electronic Solutions and Vehicle Systems.

In the absence of larger tickets, order intake in Q3 was roughly EUR700m. Our current order backlog coverage is 32% higher for the remaining quarter compared to the last year’s level. Therefore, we remain confident to achieve our targets, especially since Q4 usually is known for last minute orders with deliveries in the very same quarter. We are currently expecting an order intake in the last quarter in the range of EUR2.5billion up to EUR3.0billion, which will lead us to an order intake volume of roughly EUR6billion for the full year. In comparison to our last order intake guidance of EUR10billion to EUR12billion, we are now more or less missing the Australian contract with around EUR4billion and some contracts from Germany.

Please turn to page 13.

The positive development of the booked business in our civilian divisions continued in the actual quarter. We reported a growth of 16% to over EUR830m.

Q3 experienced high interest lead by two prominent orders. An American truck producer placed an order of roughly EUR300m for our exhaust gas recirculation valves, and a German OEM signed a nomination letter valued at around EUR260m High Voltage Contactor, confirming our excellent positioning in the market for alternative propulsion products.

Year to date, we have already generated new business of around EUR2.7billion. With just one quarter left, we should overachieve last year's level of EUR3.2billion.

Moving on to page no. 14 where you can see the current development of our Chinese activities.

The recovery from the COVID lockdown in the second quarter resulted in a positive development of our Chinese operations, especially in the JV. Although partial lockdowns have re-appeared in China we have so far not experienced negative impact on our operations. Q3 saw also positive effects from our price escalation discussions with our customers on our results. The EBIT margin for our Chinese activities recovered from 2.5% in Q3 2021 to 6% in Q3 2022.

Please have now a look at page 15 and the current situation for our supply chain challenges.

Energy cost accounts for less than 1% of our total cost worldwide. Our cost situation is well protected. We are hedging our price exposure only in Germany, the most relevant country and have already hedged around 90% of the exposure for 2022.

For the year 2023, we have already hedged around 80% of the electricity cost and roughly 65% of the gas cost. We have also implemented certain measures to prepare for energy shortages. For example, we have alternative supplies of oil in place where possible.

The situation for raw materials has relaxed to a certain extend in terms of pricing. Some plastics and Semiconductors remain tight and prices are challenging. We have taken measures to secure the supply chains. Materials price escalation clauses and hedging instruments for most of our materials are in place. We are frequently discussing price increases of materials, which are not covered by pass through or hedging with our customers, and for the time being we have made good progress. But we typically expect a delay of three up to six months before the situation becomes visible.

On the necessary recruitment process to cope with the expected growth, we still experience great interest in our company. In the first nine months of 2022, we have hired around 1.200 additional full-time equivalents, most of them in the fields of engineering and information technology.

This brings me to my last slide, the presentation of the guidance on page no. 19. Despite the known macroeconomic uncertainties with regard to the economic development in Germany as well as in the international market environment, we confirm our current annual guidance for sales to grow around 15% and operating margin above 11%.

Now, thank you for your attention and I hand back to the operator to start our Q&A session.

0:22:10 Operator

Thank you very much. Ladies and gentlemen, if you would like to ask a question, please press 9 and star on your telephone keypad. In case you wish to withdraw your question, please press 9 and star again. Please press 9 and star to register for a question. And the first question comes from Sebastian Growe from BNP Paribas. The floor is yours.

0:22:50 Sebastian Growe

Yes, hi Mr. Merch. Hi everybody. Two questions. The first one would be around the guidance and more specifically to the defence segment. The guidance obviously implies, by my calculations, defence sales of around 2b in the fourth quarter without consolidation, and that would then mean an increase of around EUR600m over the fourth quarter of ‘21. So could you help us understand what the rough increase year on year by segments might be so that we just get a better understanding around the potential mix tailwinds that you have taken into your guidance. And then related to it, I would also be curious to hear your thoughts around the semi-finished or pre-produced goods, so to what extent simply there is a flush out in inventories that you’ve been converting to sales. If we can start there, please.

0:23:40 Helmut Merch

Yes. So, picking up your second question, you are definitely right. We have built up a lot of inventories, and we expect a lot of them to flow out in Q4 because this was also the initial preparation in the last couple of quarters to prepare ourselves in order to cope with short-time orders we still expect in the fourth quarter. And therefore, there will be a significant outflow or decrease of inventories, but we also have prepared for deliveries in H1 2023. So we will be definitely higher at the end of 2022 in terms of inventories compared to 31st December 2021.

Regarding your calculation, you are definitely right. We expect a growth in absolute terms of roughly EUR600m compared to the topline in Q4, 2021, and we have different growth rates in this calculation. I think the highest growth will come from vehicle systems. Here we have a very strong quarter with at least EUR350m more than in Q4/2021. The electronic solutions will be more-or-less flat, a little bit smaller in terms of sales compared to Q4 2021, and we will see also a strong impact on the Weapon and Ammunition side. We expect also a positive growth in Materials and Trade following the first three-quarters where we saw a double-digit growth rate, and we expect a more-or-less flat situation on Sensors and Actuators compared to Q4 2021.

0:26:02 Sebastian Growe

Okay, interesting. And if I just may pick up one of the earlier comments, the short-term orders, so that would at least then play into favor of Weapon and Ammunition that is then quickly converted into revenue and that's probably mostly ammunition. Is that correctly understood?

0:26:16 Helmut Merch

Not fully, but to a certain extent you are right because ammunition is short-term order intake and delivery. It's the same quarter, but we also … and this we tried to indicate it in Q1 and Q2 especially: We built up inventories, especially also in Vehicle Systems, truck business and also Electronic Solutions. For instance, for the soldier systems. We have not signed order on hand but we are highly committed to the German customer to prepare for delivery at the very last in Q4. So all three defence divisions have some amounts of short-term orders and are ready to deliver this when there will be finally a signature.

0:27:16 Sebastian Growe

Okay, perfect, understood. Then if we can move on to free cash flow, you have obviously the 3 to 5% free cash flow quota as a target over the cycle. To my understanding that was also the target for this year, for fiscal '22. I couldn't find it however in the presentation, so, a, can you confirm if that is still the target for 22?

0:27:36 Helmut Merch

Yes. There was the same question in Q2 call, and we confirmed that the range is still valid for this year, and I expect at least that we reach the lower end of the span that means 3% plus.

0:27:58 Sebastian Growe

Which would mean EUR200m after you had a free cash flow negative of about 700 after the nine-month period. So that-

0:28:06 Helmut Merch

Mr. Growe, that is a real challenge, but we have all things under control, and we also expect some downpayments. So we are pretty confident to reach the lower level of the range.

0:28:22 Sebastian Growe

Okay. Well, that sounds good, and then the very last question is around the 2023 … well, I wouldn't call it straight outlook but obviously you had in the prior slide decks a number of EUR5.5b to EUR6b for defence revenues in '23, and if you had commented on it then I apologies because I couldn't join any earlier. So the question is now, A, same as for free cash flow, is this target still on? And, B, how do you get there? So is it also situation comparable to 2022, so that you're going to pre-produce, you know that these frame contracts are coming through and then it's flushing out in the later part of the year? Or how should we think about it conceptually?

0:28:55 Helmut Merch

Yes. So in the last call, Q2, we also refined a little bit the outlook for 2023. Here the expectation was around 5.5 for defence. I beg for your understanding, the precise guidance will be done in our March presentation, but what I can confirm that we will expect once again a double-digit growth rate in our defence segment. And regarding the situation, how we go for it, yes, it would be not the same but I guess a similar situation because it is highly dependent on the speed of the procurement process, especially in Germany, so there will be also – that is my gut feeling – a back-end loaded situation in 2023 with a bulking in Q3 and Q4.

0:30:15 Sebastian Growe

Okay, perfect. Thank you very much.

0:30:19 Helmut Merch

Welcome.

0:30:21 Operator

Next up is Sven Weier from UBS.

0:30:25 Sven Weier

Yes, hello Mr. Merch.

0:30:29 Helmut Merch

Hello Mr. Weier.

0:30:30 Sven Weier

A couple of questions from my side. The first one is on the Australian contract, which is quite interesting that you keep on repeating the contract and you sound very sure that some decision is going to be made, which obviously contrasts quite a bit with what we see in the press, right, that the project is part of the defence review which is only published in spring, which sounds plausible to me, to be honest. So what other signals do you get than we get?

0:31:05 Helmut Merch

So, A, press is press. Media is media. First statement. Second statement is that Mr. Papperger and myself have visited two weeks ago, Australia, and we have met several people, and out of these intensive discussions we got a positive impression. A, they want to decide on the program. They will decide on the program. There is a high certainty that they will go for the higher number of vehicles, and we overall got a good impression out of the discussions and therefore we still have a strong confidence that our chances, as I already mentioned, are good.

0:31:59 Sven Weier

And so the reporting of the “Schwerer Waffenträger”, which actually could coincide with Land 400 phase III, is a sheer coincidence.

0:32:11 Helmut Merch

It is a sheer coincidence, but I think it's also a good sign.

0:32:20 Sven Weier

Yes. Thank you for that Mr. Merch. The other one request I was wondering on the Fuchs successor and apology if you mentioned that in your pipeline commentary but there was also some news that would be sacrificed at the part of the EUR100b inflation adjustments. I was just wondering – of course I think it was said that the successor is taken out for now, and I think there are two things in there, right, first it assumes there is a successor, and that for now, so there might be also another option like just refurbishing the existing fleet. Could you comment on that?

0:32:57 Helmut Merch

Yes, but this is not enough. The refurbishment is one thing that is an ongoing situation, but there is still the demand of more six by six vehicles. I did not mention it in detail in my presentation, but we have mentioned it in our Q2 presentation. So this program is still valid. There’s only a discussion whether this could be a part of a European procurement program in which several countries would take place, then it could be another vehicle compared to the Fox.

But anyhow, if this could be the case, we would be the producer under license of this vehicle. So this is the one thing. If the decision will not go into the direction of a European common program, then we will end up with the Fox and this is also good for us. So the program is still valid because the demand is high for these kind of vehicles and refurbishment of existing fleet is definitely not enough.

[0:34:16] Sven Weier

Okay, good. Then I had just a question on the full-year outlook for this year, the 15%, which is part of the organic guidance of roughly 15%. I was wondering, you had obviously currency effects to the tune of 2% to 3%. You have M&A, so we have probably 4%, around 4% for the full year to keep in mind. So I do not assume that roughly 15% means 11% plus 4% and we get to 15% in total.

[0:34:50] Helmut Merch

No. Our guidance is looking for the organic growth and around means it could be some basis points below, it could be some basis points above. So around is around.

[0:35:07] Sven Weier

And maybe finally also to follow up on Sebastian's point regarding next year, because I also had a question on that regarding what is likely now? Also you have obviously the backlog bridge. That is very helpful, as ever. I mean, when you say double digit, then it would mean EUR5b and there's still a bit of a gap between EUR5b and EUR5.5b. So should we brace ourselves then for another EUR500m reduction as we had it in Q2?

[0:35:39] Helmut Merch

No, definitely not. But I beg you for understanding, Mr. Weier. We were pushed and all the political decision-makers pushed also us and we made some statements regarding the potential order intake flow. We had to revise it due to political or to bureaucratic procedures. We think there will be a certain relief during the next two quarters or so. We have a lot of international order intake in our pipeline, therefore we will be clearly above EUR5b and that means not EUR5.1b but I do not want to make – and this is not the case we have done so far to make the precise guidance for the top line growth for 2023 now. But we will be significantly above EUR5b.

[0:36:49] Sven Weier

Okay, thanks for the clarification. By the way, I think it was a good decision to put off the order intake guidance that you had.

[0:36:56] Helmut Merch

Yes. It was a – we were driven by our understanding to give the market some flavor, but not having in mind that bureaucratic layers were so – not lazy but soslow, yes? But now I think we have learned but I also tried to give you some flavor for Q4 and therefore I think we are already in line of what we have said.

[0:37:30] Sven Weier

Yes. Well done. Thank you.

[0:37:33] Helmut Merch

Thank you, Mr. Weier.

[0:37:37] Operator

Next up is Christian Cohrs from Warburg Research.

[0:37:41] Christian Cohrs

Yes, good afternoon. Thanks for taking my questions.

[0:37:44] Helmut Merch

Yes, hello.

[0:37:45] Christian Cohrs

Hello, Mr. Merch. Coming maybe to the German defence, the regular defence budget, the *Einzelplan 14* there were news that the budget would mostly be frozen at the level of around EUR50b. If I'm not mistaken, out of the *Einzelplan 14* you expected the frame contract in the fields of ammunition as well as trucks will be financed.

[0:38:18] Helmut Merch

Yes.

[0:38:18] Christian Cohrs

Now with the *Einzelplan 14* not growing but frozen at the level of EUR50b and at the same time energy costs are rising, etc. etc. Do you think that this might have a negative impact on the potential size of the prospective framework contracts? That's question number one.

Number two, then maybe in Italy we have a new government, you are – yes, you have put an eye on Oto Melara. So is there any news, have you picked up discussions with the government?

And lastly, minorities are going to play an increasing role due to soaring earnings in defence. Can you maybe give us some sort of guidance or indication where you will end up at the end?

[0:39:07] Helmut Merch

Yes. Starting with the last question, we have already seen an increase of our minorities and this is driven especially from South Africa. The Company did so far a terrific job after being hurt last year, especially by COVID and some delays in order intake and deliveries. So this is one driver.

The second driver, which has the highest contribution, is our truck joint venture with MAN, RMMV, is doing also an excellent performance, showing excellent performance and these two will be also the driver for the full year. So at the very end we expect – let me have one look into one of my slides. I think there will be a minority volume of around EUR50m or so, at the very end.

[0:40:18] Christian Cohrs

Okay, understood. Thank you for that.

[0:40:21] Helmut Merch

Then the second question regarding Italy. It is an interesting question, but I think Ms. Meloni had a start, I guess, three weeks ago and Mr. Papperger was not the first person to be met by her. Therefore there is no concrete answer to your question. Having in mind that Italy wants to launch an infantry fighting vehicle program, we are ready to go for the Lynx and we are also ready for a local production. Therefore it makes still sense to keep an eye on Oto Melara. But I think I expect not a political situation or meeting before end of Q1 2023. Probably during H1, we have a better situation, better knowledge of what the new Italian government wants to do and wants to decide.

And looking to the first question regarding size of the frame contract, this is for sure an interesting question, but there is a very, very strong need for ammunition. In my presentation I mentioned that there will be or there is actually a discussion for increasing the budget for ammunition, from EUR1b up to EUR1.5b. Therefore it could be that there is still a strong momentum on the ammunition budget or title. I am still confident that the frame contract will get the size, which we have mentioned so far.

Also the need of the modernization of the truck fleet is an important one. As you know, Germany is the logistical hub for the European NATO forces and they have obliged themselves to put speed on this modernization. So for the time being, our present knowledge is that the frame contract in the range minimum EUR500m plus is still intact and valid.

0:43:23 Christian Cohrs

Understood. Thank you very much and see you next week.

0:43:31 Operator

The next question comes from Yan Derocles fromOddo BHF.

0:43:40 Yan Derocles

Yes, good afternoon. Just a couple of questions. The first one is on the consolidation line being negatively affected by the cost of the IT transformation;

can you give us maybe a colour on that and what the magnitude of the transformation planning along we will weigh on the results.

0:44:08 Helmut Merch

Yes, so what is behind the transformation of our IT landscape? For the last 25 years, we have more or less outsourced our IT activities to various providers. Due to security reasons but also due to the need to build up new IT infrastructure in new companies, in new sites in Australia, also in Hungary and also modernization of the IT landscape in UK, we have decided two and a half years ago, that we do not want to extend the agreement with our IT provider, and therefore we decided two and a half years ago to build up our own IT resources. This cycle will cover around five to six years. We will reach the peak of this transformation in 2023 and 2024, and we will spend a significant double digit million Euro into this transformation, and we will end up at the very end with two self-operated IT data centers. And we will also have a completely own team for ERP and SAP systems and so on, and therefore we are building up own people, own infrastructure and this will take, as I mentioned, five to six years with peaking in 2023, in 2024 and then normalizing in 2025.

0:46:10 Yan Derocles

And then another one on a different section – raw materials- because the trend in commodity prices seems driving strongly reverse in recent weeks and if I remember correctly you are hedging a good part of your needs in terms of raw materials so I wanted to know what was the risk in fact until when are you hedged and will you have the means to pass on to your customers the level of prices that you have already hedged or can your customer ask you to take on the potential loss on your raw materials hedging?

0:46:52 Helmut Merch

So basically, we have a couple of instruments and a couple of elements. First, as you know, we have implemented with the OEMs material price escalation clauses. And these cover 60% to 70% of the main raw materials, but these normally have a delay, to see it on the bottom line, of three, four up to maximum six months. This is one instrument, second instrument is what we have not covered by pass through clauses we are going to hedge in a three years rolling forward process. And therefore, the running year is more or less hedged by 70/80%, we leave always a little bit for spot negotiation. Then the second year is normally hedged up to 60% and the third year up to 30% to 40%. So, this is a third thing. Now with the extreme raw material increases, which are partly not hedged or especially energy or gas situation, here we have started very early specific negotiations and discussions with our customers. And also, here we got a positive results. As you know, many OEMs are showing peak margins and therefore they are also willing to share something of the pain we actually perceive in the current situation. And then we have the last the fourth element, there is a small portion of additional cost we have to cope with and this is then going directly to our bottom line or we can compensate it with efficiency programs. So this is the universe of different elements and I think up to now we have coped pretty good with the situation.

0:49:26 Yan Derocles

Let me follow upon your third element negotiation with the customers. Should we expect the same line like something like three to six months before seeing the-

0:49:38 Helmut Merch

Yes.

0:49:39 Yan Derocles

Okay, thank you. And maybe the last question from me and I apologize if you already talked about that. I didn’t see any mention of the Puma lot in your slides. Is there any discussion about this order or the size of the order or something like-

0:50:00 Helmut Merch

Yes. Good question. We try to touch on this item because the actual discussion for the lot 2 is around a decision which vehicle is appropriate: Is it a tracked vehicle or is it a wheeled vehicle? So, this discussion is still ongoing. It could be a Puma, this is a tracked vehicle, or a Boxer. And in both vehicles, we have a significant work share and therefore it doesn't matter what kind of vehicle we finally be decided. But it is very clear, and this is our last information, the Puma lot 2 or the lot 2 in terms of vehicle will definitely come. A decision will slip to H1 2023.

0:51:04 Yan Derocles

Okay, fantastic. Thank you very much.

0:51:07 Helmut Merch

Welcome.

0:51:11 Operator

And next in the line is Michael Raab from Kepler Cheuvreux.

0:51:13 Helmut Merch

Yes.

0:51:17 Michael Raab

Yes, hi. Michael from Kepler Cheuvreux.

0:51:18 Helmut Merch

Hi, Mr. Raab.

0:51:20 Michael Raab

Hi. I'd like to get back to the question of the Puma successor as well. Presuming for a second if it's going to be a wheeled infantry fighting vehicle, how high do you think chances are it's going to be equipped with the same turret as the heavy fire support vehicle like “Schwerer Waffenträger” or alternatively with existing turret of the Puma? Any indication on that, that you are receiving?

0:51:48 Helmut Merch

That is a very good question, Mr. Raab as always, but we have not the final insight, what will be preferred. So I cannot answer this question.

0:51:59 Michael Raab

Okay. Which is fair because I haven’t read anything so you could argue both ways by the way. Do you have any indication for us what that would imply for your value share in the corresponding vehicle? If it was either equipped with your Lance turret or the turret from Wegmann, the existing Puma turret? Would that make any difference?

0:52:24 Helmut Merch

So if we have the compared to the Schwere Waffenträger Boxer plus Lance turret that would be definitely a higher work share for us, and therefore it would be highly beneficial for us.

0:52:42 Michael Raab
Okay, thank you.

0:52:44 Helmut Merch

Welcome.

0:52:46 Michael Raab

See you next week.

0:52:48 Helmut Merch

See you.

0:52:52 Operator

If you have any additional questions, please press 9 and star on your telephone key pad. Mr. Merch, there are no further questions.

0:53:06 Helmut Merch

Yes. Before I close the call, please allow me a few personal words. After more than 40 years at Rheinmetall and a good ten years as group CFO, it is now time for me to say goodbye at the end of this year. It has been always a great pleasure to interact with you and I enjoyed the stimulating discussions and your challenging questions as today. Some of you I will see once again at our capital markets day next week in Vienna. Thank you for your great support in the last ten years and I wish you all the best.