

Alfa Laval
Investor Call Q4/FY 2024
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Transcript

Speakers:

Tom Erixon

Frederik Ekstrom

Tom Erixon

Good morning, and welcome to Alfa Laval's fourth quarter earnings call and also for the full year, so Frederik and I, we will give you a run down on the year and the quarter. As always, let me start with a couple of introductory overview comments from the year. Growth continues strong in the fourth quarter and the full year of '24, ahead of expectations with favourable market conditions in most applications. It was especially good momentum in the short cycle business in the food and water and in service overall.

Now, we enter 2025 with a solid 52 billion SEK order book and good momentum on the short cycle side. The full year '24 margin was at 16.6%, ahead of last year and also slightly above our expectations when we entered the year. Q4 was seasonally a bit weaker but also affected by some one-off charges. The operational cash flow was solid in Q4, with 4 billion SEK and the new record level of 12 billion SEK for the full year '24. And so consequently, our balance sheet is strong at the moment and supportive of various options going forward.

Let me then go to the key figures. Organic growth was strong in Q4 at 8% organically with good conditions in many markets and more positive business climate in the second half of the year compared to the first half. Invoicing also grew at 8% but somewhat below expectations. The order book is solid and there are no extraordinary delays in project invoicing, rather perhaps the precision in our invoicing forecast was a little bit off.

The Q4 margin at 16% was somewhat affected by one-offs related to restructuring costs in a couple of different areas and certain project risk exposures. Operationally it was a stable quarter, with a reasonably stable invoicing mix.

Moving to the energy division, we entered '24 in a weak HEVAC and heat pump market and anticipated a volume maybe in the order of magnitude of 2 billion to 3 billion SEK for the full year. At the end the drop was compensated fully with growth in other end markets and Q4 was back on a healthy growth of 7%. Notably, clean energy applications grew with 40% compared to last year, although from somewhat small level the global concerns regarding the pace of the energy transition is perhaps a little bit overdramatised and we are now looking at a clean tech business in the energy division for around 10% of the total order intake.

Also data centres application grew, especially in the second half of the year, and compensated partly for the continued weak heat pump market. The data centre demand is

expected to remain firm in the first half of '25, while the heat pump market recovery is mainly anticipated into the second half of the year. Both invoicing and margins were stable in the quarter despite the underutilisation of several production units. The profit protection programme has yielded a better result than expected for the fully year '24 and for Q4.

Then moving into the food and water division. The division entered '24 with a strong order book after an exceptional year for Desmet, with several large order bookings in '23. As expected, Desmet returned to normalised order intake level in '24 and most of the drop was compensated for by other end market sin the food and water division. The recovery in the short cycle business continued, both for equipment and service, and Q4 ended very strong in this area including in China.

The margin for '24 was on the expected level but with the Q4 affected by some restructuring costs and some project risk exposures. In most end markets the sentiment is positive moving into '25. The project pipeline, including for biofuels, has strengthened somewhat compared to last year and in the year after the election year it's also expected to recover into 2025, an important end market for the food and water division.

No to the marine division. After strong ship contracting market and a solid order intake in 2023, we were a bit uncertain regarding the order intake for '24 at the beginning of the year. Instead, it became another record year with orders of 30 billion SEK and we finished the year with a 40% order intake growth in Q4, it was a very strong year indeed. The order book is now well loaded for both 2025 and '26 and continued good market conditions are expected as we move into the first quarter of '25.

After two years of strong tanker contracting the expected slowdown in order intake not what it was will likely affect the divisional order intake from Q2 and onwards in the cargo pumping business specifically. For all other applications business conditions will likely remain positive into all of 2025. The margin was positive and stable in Q4, as expected, and somewhat affected by one-offs in the quarter.

Then onto service, again it was a very strong service quarter with a 13% organic growth pace. The full year reached a growth of 8% supported by good momentum in all three divisions. So, then moving onto... Sorry. So finally, then let me say on the service... Sorry, at the large market...

Okay, I recap on this, so we're back to the service. Throughout the period of strong growth in capital sales the

service growth has been following the same growth patterns as capital sales. So service continues to account for approximately 30% of the group invoicing providing a healthy mix. We will continue our strategic focus and operational investment into our service organisation with a positive outlook into '25.

Then finally, to top ten markets. China is now by far our biggest market, driven not least by the marine sector. However, all three divisions have returned to growth in China during 2024. India had, as I mentioned, a weak '24, but markets are expected to recover in '25 supported by a reinvestment in the production capacity locally.

South East Asia was okay but affected in comparative numbers for '23 on a couple of large orders, otherwise the region is positive. The US is obviously a bit uncertain for '25 but in general the momentum was positive until the end of 2024. We do not expect major effects from possible tariffs on the Alfa Laval specifically, however, tariffs may have some effect as the hyperinflation on large capex projects did a couple of years ago with resulting projects delay in the pipeline. It remains to be seen if that materialises.

So with those words let me hand over to Frederik for some further comments.

Frederik Ekstrom

All right, Tom, before we do that I think we want to mention something about the acquisition that we have also announced this morning.

Tom Erixon

Yes, indeed, very good. And so, as we said for a long period of time our belief on the energy transition is that the toolbox is required and especially in the marine you've seen the toolbox of what we call in the exploration market with a number of new initiatives, we have now complemented that with a small acquisition related to anti-fouling of hulls. It's the same principle as for OceanGlide, we are looking to reduce the friction in the water and create energy savings and fuel savings for the ship owners. It is in a startup mode, so when we have commercial installations we will look to rapidly expand it in the coming years. For 2025, however, do not anticipate any particular impact on neither invoicing nor margins or results. So that's where we are with it, we are very excited about it, the toolbox is getting completed.

Frederik Ekstrom

Thank you, Tom. And now a quick update on the quarter four financials and also some comments on the full year 2024. Quarter four exceeded expectations, adding some 18.5 billion to the 75 billion of order intake for the year. Beyond the high contracting levels in marine it is noteworthy that this development of such a normalisation of elevated

project orders in Desmet for all your chemical and biofuel projects booked in 2023. And it also compensates for the continued low level activity in HVAC, notably heat pumps.

Currency has a negative impact on the whole year, mainly driven by the movement of US dollar to euro. However, we have a strong organic growth of 7%, which brings the total growth of the year to 5.4%. A final note is that the underlying strength of the base business, including service, in terms of total order intake is to be noted.

The total order book after a strong quarter four amounts to 52 billion, with a corresponding book to bill of one. The majority of the backlog is phased for invoicing in 2025 and our current view is that it is well-aligned with current market prices. Marine represents some 27 billion of this order book with a heavy marine pumping systems content for delivery in 2025. The order book for energy is at 10.6 billion and food and water at 14.9 billion, which also provides a good fundamental revenue base for 2025.

This all-time high order book compensates for the inherent volatility or lumpiness of orders in relation to revenue and results throughout the year. Sales for 2024 ended on a record level of 67 billion, of which 18.3 billion were recognised in quarter four. Organic growth in the quarter was 2%, with an additional 0.6 added by currency. On a whole year basis the revenue grew organically with 63% and currency had a negative impact of 1.1%.

The service mix proportion of revenue remains on or above the same level of last year, which is 28% of the total, or some 21 billion revenue of 67 billion for the year. From a product perspective, our extensive heat exchanger range stood for 42% of the revenues. With a record high order book our revenues should remain solid throughout the year, despite possible order intake volatility and mix change.

Quarter four gross profit margin was 34.4% compared to 31.6% in quarter four of 2023, adding some 163 million to the result coming from the good factory results and purchasing price variances, the balance coming from volume. R&D increased with 4.8% in the quarter compared to last year and some 12% in S&A, where the majority of the increase is related to added resources.

Operating income increased with 8.7% despite some one-off charges in the quarter. The tax rate of 27.1% in the quarter was unusually high as a consequence of tax audits where the additional tax burden has been recognised but the non-corresponding adjustment is not in other tax jurisdictions. EPS of 4.96 in the quarter represents an

increase of 31.5%.

Let me also give you a quick summary of the whole year. Gross profit margin at 34.6 compared to a 32.8%, which again is boosted by good factory results and positive purchasing price variances. S&A is up with 11.5% but remains close to the historic 15% in relation to revenue. R&D is up some 6% and remains stable around 2.5% of revenues, a welcome increase as we continue to innovate.

Operating income increases were 12.7% yielding an adjusted EBITDA margin of 16.6%. Tax rate at 25.6% is just within our guidance range and brings the EPS to 17.88 kroners, in increase of 17%. A strong result for 2024 underpinning the fundamental profitability of our business and a strong signal to continue to invest in growth initiatives and our strategy.

The quarter four adjusted EBITDA margin bridge confirms the positive development with the majority of the improved margin coming from increased revenues, purchasing price variances, which more than offset year end provisions and restructuring cost that we take as part of operating activities. For those wondering how that distributes itself it's 40% in food and water, 40% in marine, and 20% in the energy division.

However, we also did fall short on invoicing in the last quarter with a revenue contribution that defers then into quarter one. For the full year the revenue growth and the increased gross profit offset the cost increases to yield an improving margin of 16.6%.

Quarter four cash flow from operating activities yielded 4 billion, which after another high quarter of capex at 1.1 billion, resulted in a 3 billion free cash flow. Concluding another quarter of strong cash flow conversion and strengthening our balance sheet. On a whole year basis, cash flow from operating activities increased with 32% to 12 billion. Record level capex at 3.3 billion resulted in a free cash flow level of 8.8 billion, an increase of 31%.

Our debt provision has been proactively reduced with 3 billion, and a dividend of 3.1 billion for our shareholders composed the bulk of the cash flow influencing financing activities. With a final cash flow of 2.1 billion for the 12 month period we conclude 2024 with a strengthened financial position. The positive development of operating working capital and increased EBITDA has also yielded a high level of return on capital employed at 23.2%, compared to an already good 21% in 2023.

Debt has been proactively reduced with 3 billion to bring in the current ratio of debt to EBITDA to 0.8. Net debt after cash and cash equivalents including currency deposits is 2.4 billion, or 0.19 of EBITDA. Lease liabilities increased with 400 million to 3 billion, which yields a net debt including lease liabilities of 0.43. The recommendation to the annual meeting is a dividend of 850 per share, which would equal a dividend of 3.5 billion to be distributed in quarter two of 2025. Our current cash and debt position and its maturity profile allows us for a strong acquisition position in 2025.

Now to some final guidance remarks. Capex guidance remains high with a guided interval of 2.5 to 2 billion. Currency impact based on current FX levels should be accretive in the year, with 265 million. PPA, amortisation of 450 million, and a final tax range of 24% to 26%. And as previously mentioned, an increase of 13% on the proposed dividend for 2024 at 850. With that I hand over to Tom for some closing remarks.

Tom Erixon

Thank you, Frederik. And then finally our outlook statement and this time it's unusually straightforward. We are expecting demand to remain on approximately the same level sequentially as in Q4 and that holds true for all three divisions. So essentially unchanged market conditions expected in all three areas moving into the year end Q1. So with that thank you and we're ready for questions.

Operator

Ladies and gentlemen, we'll now begin the question and answer session. Anyone who wishes to ask a question may press the star and one on your telephone keypad. You will hear a tone to confirm that you have entered the queue. If you wish to remove yourself from the question queue you may press star and two. Questioners on the phone are requested to disable loudspeaker mode when asking questions. Anyone who has a question may press star and one at this time. And the first question comes from the line of Max Yates from Morgan Stanley, please go ahead.

Max Yates

Thank you, good morning. Just my first question is just around your data centre business. Could you just give us a feel for in order terms how fast that business is growing currently? And maybe just, I think there's been some discussion in the market about how much of your exposure is liquid versus air cooling, I was wondering I think you've talked previously about data centres as about 10% of the energy business but could you give us a feel for how much of that is liquid cooling versus air cooling? Thank you.

Tom Erixon

Good question, Tom. In terms of how fast it's growing I hesitate to answer that, I think because we will see. We had

a good momentum on the data centre side in second half, as I indicated, I think we are not a large system supplier, so I think the order intake for us has been a bit later than in some other areas where you've seen the data centre growth in the order book in other sector-related systems. So we feel the momentum for us will carry into certainly the first half and possibly for the full year.

So on the order of magnitude of about a 2 billion SEK business in 2024 if the pace holds the full year it should possibly then grow somewhat compared to last year. I think we feel we are in a reasonable position, we are in some long-term contracts in this area so I think we have a good product solution, we have a good technology base and a good market position to hold our share going forward.

I'm not exactly sure how the split is between... We may come back to you on that, rather than guessing. But what is clear is that the water cooling side is growing in the portals. So for going forward we think this will become increasingly important as part of the mix.

Max Yates

Okay. And just a quick follow up on your pumping systems business. It looks like you've done something in the region of 15 billion of orders in that business, I realise it's unpredictable but at least from where you stand today how are you thinking about the evolution of that business based on everything you see and speak to with your customers and think about for the capacity that you have? How do we think orders there evolve? And what would you say are the major offsets where you look of big buckets of growing business that can help offset that headwind, whatever it may be, 3 billion, 4 billion, 5 billion? Thank you.

Tom Erixon

I lost you, are you referring to the... Your sound went out but were you asking about possible volumes on the marine side?

Max Yates

Yes, I was asking about if we think about as we sit today pumping systems is roughly 15 billion, what is your best assumption for what we may lose in orders from pumping systems? And what would be, in the same way you had some offsets for Desmet in 2024, what would be the major offsets that you would be looking for in terms of building blocks to maybe offset whatever that pumping systems loss may be, whether it's 3 billion, 4 billion, 5 billion of orders year over year?

Tom Erixon

Yes, it's a very relevant question and we certainly are a bit analytical in trying to figure out what the bridge looks between '24 and '25. Let me start by saying I actually thought when we started last year that we would end up with

a smaller order book going into '25 than we had going into '24 because we knew Desmet was coming down, we knew heat pumps were coming down and we did not see the strength of the marine market would hold for the full year. At least it wasn't a strong assumption that it would.

So the fact that we came out with such a strong growth is, a year later, well beyond what we expected at the time. Now, we have a sort of a similar situation coming into this year. And I think our best... So if you think about the from [? 00:23:08] business historically being moving around, maybe the 5 billion up to 6 billion markets and ongoing invoicing obviously the 15 billion, which is more or less the correct number, is not anticipated to repeat itself. There is no way that we can over the cycle move up to 15 billion invoicing per year, it's not going to happen. And the order books in the yards will not allow it and our capacity will not allow it.

So I think what we have achieved with the 15 billion this year and good order intake '23 is we've provided a good and stable platform for invoicing and the invoicing growth over in '25 and '26. So we are not, when it comes to the marine division and the development on invoicing and margins, we are not so concerned about what the order intake number will be in 2025.

Now, if we return to where the predictions are in the market and how we feel about it, cargo pumping will go down after Q1 and we believe that offshore will be somewhat better. And service will be somewhat better. So I think we are looking at order gap that is somewhat higher than you're anticipating, if we get to double digit that would be a very good result but I'm not so sure we will.

So we have a gap to fill, the way we look at it is that it was important for us to come in on the better momentum and higher level on the short cyclical business, there for once. That's sort of what's going to decide how '25 turns out, the project order book largely is pretty much in place. So the pace of short cycle business will determine where we end up invoicing profit-wise in 2025. And we got to a position which was as good as we could hope for, finishing off Q4 strong.

In terms of closing gaps, we believe that the biofuel market, the project market in that area will be stronger this year, so we think that Desmet but possibly also our project businesses in Alfa Laval will compensate somewhat for that. So there is partly something that will fill the gap there. We believe that we will in the second half have a return in a recovery mode on the heat pump market which will also

close part of the gap on that.

So I think those are the two structural ones but otherwise, I would say that if we look at 14 business units in different product segments most of them are looking at the normalised positive growth into 2025. So we are not too concerned on the business cycle or the general market sentiment across the board, we think broadly speaking the portfolio is developing okay.

And if you want a third closing the gap thing I think the question of where we will go on what we call the exploration bucket, or the energy transition bucket with new technologies. And we obviously have been growing well in 2024, the pipeline on some of the energies and switching projects look somewhat stronger now than it was a year ago. So also on that side we may see some structural things that is helping us closing the gap on the order intake levels specifically. Long answer, sorry, I hope you...

Max Yates

No, that's great colour, thank you, Tom.

Operator

Next question comes from the line of Daniela Costa from Goldman Sachs, please go ahead.

Daniela Costa

Good morning Tom and Frederik, this is Mehan working with Daniela from Goldman. So two questions from me, first can you talk about your expectations for marine pricing going into 2025? And a second question if you can share more details on the restructuring you did for food and water marine business and in particular anything that didn't get booked under the adjustment items and are you planning to do any further restructuring in the rest of 2025? Thank you.

Tom Erixon

I think the pricing for '25 is already a done deal, the calls have been accepted, the orders are booked, so we are where we are. But we feel good about the mix and we feel good about our market shares and we feel good about the gross margin level in the book. So when we look into margins and the invoicing for next year marine is not the question mark for us, it's more or less, I will not say it's a done deal but largely speaking the conditions are set for 2025 on that note.

On the restructuring side, we feel we don't want to confuse ourselves and the market with ongoing restructuring programmes and so we are just taking some of these ongoing restructuring activities as part of our operating costs, as Frederik said. And had we had any major restructuring above and beyond that we may have dealt with the question otherwise, but on the 200 million SEK level we felt it was the right to just charge it in the businesses and

take responsibility for our ongoing operational improvements.

It refers partly to some changes in our R&D department, in parts of the organisation where we have stopped certain projects and we're on a structural overcapacity situation. We are on the marine side continuing to building our presses in China, so we are transferring part of our resource base and structures not only manufacturing but also in engineering onto Qingdao. And that is also leading to some restructuring charges.

So there is a host of these things that were spread out and we just thought we'd charge it in Q4, we don't have anticipated any major restructuring effects in 2025. We're going to have to, of course, we have an underutilisation on the heat pump side, we are expecting it to come back in Q2 so all in all we feel we are okay but I would say if there was any uncertainty it is related to that.

Daniela Costa

Got it, thank you.

Operator

The next question comes from the line of Sebastian Kuenne from RBC Capital Markets, please go ahead.

Sebastian Kuenne

Yes, good morning, thank you for taking my questions. First, on marine, it looks like the revenue recognition in Q4 was a little bit softer than what people expected. Is this maybe also reason of shipyard bottlenecks and if so, what's your view on the shipyard capacity buildout for 2025? That's my first question.

And secondly, on food and water, taking out the restructuring charge it looks like that the margin was slightly up year on year but still below expectations. Is this also driven a little bit by the Desmet mix effect or do you see a kind of margin pressure also within the product lines? Thank you very much.

Tom Erixon

Yes, on the revenue recognition, I'd hesitate to... We sit with a big product portfolio, a lot of percentage of completions, and we don't have specific detailed systems to clarify exactly how much of the order book will go out in a given year and a given quarter. So we have to do some qualified estimates as where do we think those dates are.

And so, I think it's more a question of us being able to nail a precise number as the one that should be there and then. So I don't think it's just a deviation in terms of what should be expected, I think it's a deviation maybe that is just reflecting a certain uncertainty as to exactly where will we end up on the invoicing. What is important for us is that we know that we have a firm order book, there's no major

delays, either structural delays or cancellation or worries about the integrity of it. We feel good about the order book and I think we are just a bit humbled that we may have not been perfectly being able to guiding you guys as to where should the expectations be.

So for Q4, I don't see that in marine but to your question, the load on the shipyards and the load on us is significant going into 2025. We are especially when it comes to commissioning taking extraordinary measures in order to recruit and build, primarily in China, a team that can manage the whole commissioning of a huge product pipeline and big demand. And for some yards that are not that experienced in working with part of our product range the support to get this to work is going to be big on our side.

So we have not failed to deliver on time in the marine industry, we don't intend to be there in 2025, but we are putting a lot of our worries, the challenge we're trying to solve is just to be able to complete all of this. We're not so worried about the order book or that sort of stuff. So we see where it goes but we have a lot of pressure on us for '25 and I think we've taken the measures that we can in order to safeguard it so I think we are in a good spot but it's going to be a challenge for our organisation, that's for sure.

On the food and water, yes, it's a bit of a mix thing we have a project business also in food systems that wasn't quite up to the margin level that we were looking at. But otherwise in the product groups, the transactional business and the service business we have no margin deterioration. We were, as you know, in the beginning of the year in a bit of a low utilisation on the transactional side, it started to recover during 2023. But we're now on a good level in the pace, so I think on the realisation level, on pricing and gross margin level we're going to be okay in the various product groups for food and water.

So I think it's mix changes and possibly the question of where we're going to end up on the final margins on the product business that's going to set the level for 2025.

Operator

The next question comes from the line of Klas Bergelind from Citi, please go ahead.

Klas Bergelind

Thank you, hi Tom and Frederik, Klas from Citi. My first question is on energy, on the heat pump side and also like industry and tech. I was under the impression that the heat pump business started to grow a bit here after the third quarter, was this some sort of de-stocking at year end that drove this and you're commenting that the recovery will happen in the second half. I think you said before that we

could see a relatively normal level, of course below the previous peak, but by the second quarter. I wonder if you feel that the recovery is a little bit slower now?

And then on like industry tech, unless the data centre business slowed, the drop in service must have been quite big as data centre is about like half the industry and tech. if you could shed some light on what you see of the total segment into the first quarter? Thank you.

Tom Erixon

I think for the total segment we are okay, we are not have any special concerns on that. So it was okay for us in '24. I think outlook for us is okay. So no big worries on that. I agree with you that the question on how will the recovery in the heat pump market look has been a bit uncertain and I was probably one who would expect that the de-stocking things to show in a somewhat quicker volume recovery than we've seen so far.

But I think the lag and the caution on behalf of the OEMs when they put their production plans and consequently their orders has been a bit mor cautious than we expected so far. If you ask if there are signs of recovery, yes, for sure. Are there some orders now that started to come in, covering for Q1, Q2 yes there are, but they are not meaningfully changing the pace ad utilisation for us in Q1. So we will see a little bit whether the de-stocking effects takes out some of the system a bit quicker now in Q1 but we are just prepared that we're going to have to manage the first half on a conservative volume scenario.

Klas Bergelind

Okay. Final quick one on marine between product tankers and the other segment, you're now talking about orders on the cargo pumping side still being healthy until the first quarter and then to start to normalise. If you could comment would you think orders ex-tankers will accelerate from current levels or you still remain stable? I think, Tom, you said that orders ex-tankers in marine should be healthy but I was just wondering whether this lagged effect, which is typically longer outside tankers, will see orders accelerating or just being stable? Thank you.

Tom Erixon

Yes, no it's correct, that's how we judge it. We are looking at the '24 full year contracting volume across all ship classes at a level we haven't seen for many years. The count now stand at 2,300 something, I think it will go up a little bit in the next couple of weeks as we are updating the '24 numbers. And for many of those, especially on the product tanker side, the orders are in very early for cargo pumping and they are not as fast in the cycle for most of other product groups.

And in the contracting volume for '24 there's a lot of ships

that are for deliver in '26 and '27 and so there's no need to post those orders with us yet. So we believe that the momentum and the conditions are reasonably favourable for essentially all of the other product groups in the marine division into 2025.

Now, with the volumes we're talking about in cargo pumping that my not compensate the whole thing but it should at least balance out a little bit in terms of order intake volume in '25 compared to '24.

Klas Bergelind

Perfect, thank you.

Operator

Next question comes from the line of James Moore from Redburn Atlantic, please go ahead

James Moore

Yes, morning everybody and thanks for the time. I've got some questions on the pumping systems, if I could. Just going back to the order comment of 15 billion or 14.5 billion of orders in pumping systems, could you give us a flavour for what the mix was between the cargo marine business and the offshore business?

I think you commented a few years back when orders made were 5 billion that it was 50/50 but I presume that they might, I don't know 11 million marine, 4 billion offshore? Could you help us just understand a little bit how the mix has changed and what it is now? That's the first question, if I could.

Tom Erixon

Yes, do you have the exact number in your head, Frederik?

Frederik Ekstrom

Not the exact number but I believe it's 70/30.

Tom Erixon

Something I was going to say, So I think we are somewhat shy of double digit on the marine cargo pumping, there is also a service aspect in the total order mix. So subtracting service and then splitting it on capital sales between the two it's probably taking us to a high single digit order intake on the marine side.

And our guidance for '25 is that while we believe the volumes on the marine side will not repeat in this area we see a stronger offshore market. And we also have a stronger product offering there, so that's going to make up for part of the expected volume drop on the marine side.

James Moore

Okay, that's very helpful. And just in temrs of the revenue in pumping, I think you talked in the past about having quite a healthy backlog that stretches into 2026 but would it be possible to give a rough flavour of the revenue of pumping systems these days? And what sort of sales growth you would expect in '25 on the invoicing side?

Tom Erixon

We are not guiding too much specifically in... I understand

your question and we both understand that it has some importance in how you run the calculations but let me just say that we feel we are in a healthy growth phase on the invoicing side for '25 compared to '24 on the marine side, on the cargo pumping for sure. Whether that growth will continue into '26 or whether we will stabilise on that level that's a question for next year's full year report. But we feel quite comfortable about the invoicing growth.

And I was indicating before what's going to determine the invoicing for the year is can the shipyards keep the time plans, the delivery schedules. And so they are a little bit of uncertainty how much it will grow but we will see a healthy growth in this area.

James Moore

And just finally, sort of continuing down the &L, really, on the margin for pumping systems will it be fair to say that we will still expect that to progress quite well because the marine side returning back to a very healthy phase?

Tom Erixon

We have on the order book what we consider to be a normalised margin in 2025 compared to where we've been historically. So the mix change will have some positive impact moving into the 2025, that's our expectation.

James Moore

That's really helpful, thanks so much.

Operator

The next question comes from the line of Andreas Koski from BNP Paribas Exane, please go ahead.

Andreas Koski

Thank you very much and good morning. I just also had a couple of questions about the backlog. If I look at the Q4 backlog for delivery next year that is 60% higher than the backlog you had for delivery in 2023 and it's 22% higher compared to a year ago. It also sounds like we should expect in for out orders to increase in 2025 compared to 2024 based on your comments about the short cycle momentum. So I just want to ask, do you have capacity for these sales levels and what kind of operating leverage should we expect from significantly sale level in '25 compared to '24?

Tom Erixon

Well as Frederik guided you on we certainly have invested appropriately over the last few years in our by far biggest capex programme we ever had in this company. And we are starting to come to an end of, let's say, the capacity expansion and footprint adjustments to get things done. I reviewed a little bit of the, I call myself a real estate manager when we did the capital markets day but we went through a little bit what we have been doing in detail. So we feel good about that and so in terms of capacity our main concern is that we are underutilised in the Brest area due to the heat

pump situation and that is a challenge we are trying to deal with.

But other than that we are fine, we have one larger project most likely ahead of us and that is that we need to set up our pumping system business on the service side, on the offshore side and on the marine side and scale that into what is a different activity level than we've been at historically. And so that is the one outstanding project internally under discussion of any major importance in terms of capex.

And so I'm not too concerned about being able to deliver the one other area that I touched on earlier is the fact that the commissioning of the marine installations will be important and we expect that we need to support the yards more and better in this situation than we have historically. So it's a lot of work on that side. But manufacturing-wise we feel we are okay.

Andrea Koski

Okay, but I was a bit surprised to see that your backlog for delivery later than next year is actually down slightly compared to a year ago. So maybe you've already touched a bit on this but is there a meaningful risk that you overestimated how large part of your backlog will be delivered in 2025? Because otherwise, it doesn't look like you're in a better backlog platform for 2026 than you were for 2025 a year ago.

Frederik Ekstrom

No, and of course the backlog we updated continually the phasing of the backlog and some of it is dependent on how our customers take deliveries, when the shipyards are able to take delivery and when our large project customers are able to take delivery. So there is of course an element of the backlog that will change or alter itself from a maturity point of view based on that.

Based on what we know today we make the judgement that 13.1 billion of the 52 billion is into 2026. That may change over the year but that's our best assessment now and the consequence that that has on an in for out business, yes, I mean if you look at it and you look at the transactional business it does provide strong base for revenue growth in 2025.

What it means also is of course that the replenishment of that order book into 2026 is something that needs to happen during 2025. And of course, Tom has gone to quite some detail in the three divisions to give you a picture of what we believe that replenishment rate is going to be.

Andreas Koski

Understood. And could I just ask lastly on your outlook, if I look historically, sequential Q1 orders have not been down

a single time since 2017, at least. And on average, Q1 orders have been 8% higher than the Q4 order intake. So I just want to understand that we should expect sort of normal seasonality in this quarter and that your guidance of relatively unchanged demand is on a seasonally adjusted basis? Thank you.

Tom Erixon

Well, we haven't adjusted it, I think our guidance is that we expect the numbers to come out pretty much flat sequentially. That is a base assumption and, yes.

Andreas Koski

Yes, understood.

Tom Erixon

I cannot recommend you to put a number in in your own forecast but we feel unchanged is the most likely scenario.

Andreas Koski

Understood, thank you very much.

Operator

The next question comes from the line of John Kim from Deutsche Bank, please go ahead.

John Kim

Hi, good morning. I'm wondering if we could go back to the restructuring charges. Should we expect more or is this kind of a fairly large adjustment in how you're thinking about running these businesses? And if you could just give us a bit of colour on the H2 recovery in heat pumps, what gives you confidence on that? Is there any legislation we should look for?

Tom Erixon

Do you want take this?

Frederik Ekstrom

Well, when it comes to the restructuring charges, as we've said now a couple of times, it is very much to adapt the existing business to the changing market or where we see that there's need to make new initiatives. And we have chosen to take those as an operational cost.

Now, it is true that they accumulated very much into quarter four and that's something that we have taken upon us to make sure that when we have these initiatives and when we have higher provision that was for whatever reasons that may be that we take them more spread out during the year. That is one thing we take away from that.

As regards to larger restructuring programmes in 2025 we have none such identified, we have a running business and if there's need to adjust businesses based on changing geopolitical factors or supply chain movements then we will do so in the course of business. But we have no single larger restructuring programme planned for 2025.

Tom Erixon

You're come from that business, so.

Frederik Ekstrom

Well, I mean to add some colour to the heat pump I think we

did see volumes starting to come back in the later half of 2024 and that's from a very low level. Having said that, it is new orders and it is somewhat indicative of a de-stocking now complete. Now we need to see the fundamental demand, of course, increase and there are many governments moving into subsidies, there are many governments moving into programmes where the decarbonisation of heating continues, or rather the do-fossilisation of heating in the form of gas heating.

But of course the rate of that substitution and the magnitude of those programmes is altered, it is smaller than it was before. So even as we return into what we would say is a normalised heat pump volume into quarter three, quarter four of this year it certainly won't be back at the historic high levels that we saw towards the beginning of 2023 and certainly... Sorry, the end of 2023 and the beginning of 2024. Having said that we expect a healthy business in heat pumps to continue going forward.

John Kim

Okay, helpful, thank you.

Operator

The next question comes from the line of Sven Weier from UBS, please go ahead.

Sven Weier

Good morning, thanks for taking my questions. I'll start with marine services, please. I was just wondering what your best guess would be, how much of the marine service revenues are tied into freight rates and trading activities of your clients? And how much do you think it's really more kind of structural, decarbonisation related, refurbishments? And any best guess on this one and then I'll follow up with another one, thank you.

Tom Erixon

Yes, as you know we have been through a very strong growth period in our service business, not only in marine but also in the other areas and we've been up at double digit, we were again super high in Q4 at double digit growth. So well above what we would consider normalised service growth. And initially after the pandemic we were asking ourselves and we debated also we were transparent with you, we couldn't see a pent up demand situation per se, but we were wondering ourselves whether actually there were elements of accelerated growth over a shorter period of time and then we would plateau and normalise.

So we've been extremely aware of how are the actually underlying trends going. Now with the pandemic years behind us and the growth continuing I think fundamentally we feel the structural growth driver in our service business, in marine and other areas, is related to a broader product range with new products, especially in the marine side that

is being matured for device programmes, including ballast water applications and scrubber applications and a host of other things that we didn't do five, ten years ago in terms of service.

And that's also true in the other divisions as well, the install base after years of strong capital equipment is better. And secondly we are having a higher market share and we serve today a bigger part of our installed base than we did five, ten years ago. And the work we're doing in the service organisation is very important and continues to drive our share of servicing our own products in a better way.

So I think those two factors are common for all three divisions and they are certainly relevant for the marine business as well. Then comes the question of the global merchant fleet and I think there is right now a cyclical aspect related to the fact that essentially, the scrapping of older ships is coming down to zero or very close. And it ought to be higher but under current prevailing economics and freight rates essentially all of the old ships are continuing to move on the oceans. And consequently that does drive a bit of accelerated demand in the marine sector specifically.

Now, I would counterbalance that with the fact that at this point in time we have about 1,000 of those old ships in the shadow fleet for Russia, and those are no touch for us, obviously. And so some of the ships that would have gone to scrapping has actually gone into a non-serviceable fleet for us.

And so I think should we get into an increasing scrapping situation I don't think the negative effect will be as present as you perhaps would have expected otherwise if all was operating under our service contracts and all old ships would be taken care of by us, that's not the case. And so I hope we will see the scrapping of the shadow fleets, it is not a healthy situation for anybody, it has no material impact for us but... So freight rates coming down, some ships going out of service, may have some impact in the future but structurally we feel quite healthy about where we're on the marine side.

Sven Weier

Yes, thanks for this, Tom. And then just two quick ones on product tankers. The first one being you said the orders will flow from Q2, I was just wondering, you had a 1 billion slowing between Q3 and Q4, so was that not product tankers? And the other question I had was the product tankers share obviously being 50% of orders, what was it on sales and do you think the 50% of sales will then be in '25 already? Thanks.

Tom Erixon Oh, that's a bit too detailed for our appetite, right?

Frederik Ekstrom Yes.

Tom Erixon But it's true, the tanker contracting was super high in the idle of the year. And just so you're aware of the numbers if we look on historic average on product tankers over a long period of time we look at a couple of hundreds, I think last year we were at 540 or something like that, two, three times normal averages. And it peaked in the middle of the year.

So yes, I think a fair share of the delta between Q3, Q4 was related to that and our indication is that we will be a reasonably stable into Q1 on the current level and then next quarter we will update you on that. But our anticipation is we will see a weaker market.

One thing we could add there on the revenue side is that the revenue development won't be equal to the order intake development that we saw last year, it will be much more linear over the next 18 months.

Sven Weier So it's still taking until next year before you have the full impact?

Tom Erixon We are probably not peaking in volumes first half this year, no.

Sven Weier And you think product tanker orders will be stable for you in Q1 and then it goes down further in Q2? Is that the guidance, right?

Tom Erixon Correct.

Sven Weier Thank you, guys, thank you.

Tom Erixon Thanks.

Operator We have a last question coming from the line of Max Yates from Morgan Stanley, please go ahead.

Max Yates Hi, I just wanted to come back on the cerebral topic of inflation and I guess we had that period coming out of COVID where you had some challenges in the marine business from fixed price contracts. So, look, you made a comment on tariffs but broadly if we get a return to inflation how are those contracts set up differently today versus where they were three, four years ago? Because we're in a similar position where we've got a very big backlog in marine that's going to be delivered over a number of years, so if we do start to see inflation coming back how are those contracts different to where we were there, four years ago?

Tom Erixon I think the answer is somewhat different and somewhat not. The normalised level of closing those contracts is that they

are fixed and if we look historically the main driver of difference is material prices. And of course, on the group level we're looking at our material purchasing contracts going forward and Frederik is responsible with his tea for the hedging processes. So we do hedge.

And when we look at today's inflationary risks we have a much more healthy raw material market, both on stainless and on common steels. So what drives our gross margin in the marine portfolio is mainly a cost bill of materials question. And that's what we are monitoring very close.

Then there are in some areas opportunities to renegotiate and so we have a fairly clear picture of where it sits. In terms of tariffs, we are getting obviously with some exception, fairly strong presence in China for our manufacturing and contract executions part. Not for the cargo pumping specifically but certainly for the rest of the product range. So we source a lot in China, we engineer and install and build a lot in China. So from generally speaking in the division the tariffs is not anticipated to have a major contract.

If we would get some sort of exposure here on cargo pumping I think we might need to get back to a situation where China would impose heavy tariffs on that order book. I'm not exactly sure what the answer to that question is.

And your question is, I think is a general we are overlooking our various exposures in terms of tariffs analysis various geographies, we are not alone by the initial analysis by any means and we see where the whole thing goes. But we still have some homework to do in terms of calculating whether we have unforeseen risks exposure on it. But at the moment we feel pretty good about the whole thing. But let's see. I don't know if you have a further comment?

Frederik Ekstrom

No, as everybody else we're also moving quickly to understand the flows that could be affected by tariffs and what the magnitude and how we mitigate for the effect of those tariffs, should they happen and where they happen and to which countries they happen.

Tom Erixon

So we might give you a clarification on it but at this point we are good we think.

Max Yates

Excellent, okay, thank you very much.

Tom Erixon

All right. And with that I think we're done, thanks for your attention. If we don't speak before we'll see you t the Q1 report and have a good day, thanks.

Frederik Ekstrom

Thank you.

