



Transcription

Metso-Outotec Q1 2022 / Interim report

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21 April 2022



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PRESENTATION

Juha Rouhiainen

Good morning. Good afternoon, everybody. This is Juha from Metso Outotec's investor relations, and I want to welcome you all to this conference call where we discuss our first quarter 22 results which were published earlier this morning. The results will be presented by our President and CEO, Pekka Vauramo; and CFO, Eeva Sipilä, after which we will take your questions.

Please note the forward-looking statements that are in the beginning of the presentation slide deck, and also a reminder that we try to wrap up this call in 60 minutes, because after that, we are going to have our Annual General Meeting. But with these words, I'll hand over to Pekka. Please go ahead.

Pekka Vauramo

Thanks, Juha, and welcome to this First Quarter Results call for Metso Outotec. We are happy to report that we had a very strong quarter. The first quarter, market activity continued strong, and we delivered a solid sales growth as was expected out of our strong order backlog at the end of last year. Our profitability improved thanks to growth, but also many other actions relating to execution, getting a bit firmer grip on supply chain and related things in some of our businesses and that is visible both in growth and in the profitability.

We also made good progress in sustainability. We launched new products under the Planet Positive label and continue to grow also Planet Positive sales as we will see later on. The good performance during the quarter was though, very sadly, shadowed by Russia's attack against Ukraine in February 24th. And quite a lot of our activity since that has gone into managing the situation with, first of all, safety of our people, people in all related countries in Ukraine, also in Belarus and Russia. And after that, really managing the business under the sanctions export controls and many other difficulties such as banking and logistics.

But I will come back to those ones later on. On a Group level, we still grew our orders faster than our sales, slightly faster than our sales growth of 26%. Out of our orders, we have to say that orders were what we really like. We like the smaller orders rather than huge, big project orders. We've said it said it before and this is a typical quarter when we booked lots of smaller orders and nothing really extraordinary large and we like it in that way. It's less risky, and by all means, and that's what we aim to and would like to have on every very quarter. We, of course, like the big orders as well but they should be seen as the glazing on the cake rather than our bread-and-butter business.

Results grew consequentially by 37%. Adjusted EBITDA being 157%, representing a margin of 13.5, which is 1.1% more than the year before. And operating profit consequentially grew and earnings per share and also positive development. Cash flow was reduced from the year before, and this is a reflection of the fact that our volumes are growing. We are tying more working capital into our supply chain and into our inventories. Markets are active and markets are expecting us as a supplier to be ready for delivering and supporting customers in aftermarket side as well as new equipment and that tends to drive the inventories up and it's a quite normal development. But yet, a positive cash flow during the quarter.



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When looking at the segment aggregates, orders continue to grow, and markets are in good shape mostly in North America. And also, China is showing signs of waking up and returning, which is naturally positive after the slowdown in construction activity over there. Europe was as well strong. Some uncertainty towards the end of the quarter we started to see because of the war in Europe. But that was mainly a European issue and not even across Europe. But some softness we saw there, and maybe that is a sign of uncertainty then affecting the business.

Sales growth, also strong sales growth from the year before coming out of really backlog, and what was also good to see was that the services continued to grow and now being at 34% in our aggregates business. Margin-wise when we look at, we returned to sort of levels where we were before during the first quarters, the first three quarters of last year, we had certain one-time items in the fourth quarter of last year and we saw a drop in margin level then, but we are now back in those 14%+ levels where we were most of last year as well.

Yes, supply chain is still an issue in aggregates, but we were able to deliver quite many of the orders and confirm also quite many of those orders that we were not able to confirm during the last quarter of 2021. So, somewhat positive development there, but tightness continues and I'm sure that we will see new shortages and new issues during the coming months.

In the minerals, good order growth here. Really typically we had in this quarter the smaller orders as mentioned already before from all markets basically. And equipment orders grew by 44%, service orders by 23%. And we can see that margins also turned upwards. Good execution of order backlog sales growing to 731 million. Equipment growth, 50%. Services grew only 6%, even though we have had a good strong order intake in services. But the order growth was still modest in this quarter. Services share did drop because of the equipment growing so rapidly to 58%, but yet we were able to show improvement in margin, and margin being 14.7% during the quarter. And the impact really coming from growth, and then also synergies that we kept on reporting up until the end of last year.

The metal side, good order growth, and here the same picture as in the minerals: not really single major orders during the quarter but many smaller ones and especially several pellet plant orders as you might recall in our press releases during the first quarter. Good execution continued there of the order backlog. Sales exceeding 100 million and services disappointingly dropping. But this is clearly a sort of a strong equipment delivery growth issue in our metals segment.

Adjusted EBITDA, really clear improvement from a year ago. Margin-wise slight drop from end of last year where we had some positive one-time items as we reported at that moment, some one-time items that we could have possibly also reported earlier in the year, which would make the last year look a little bit more even than what it is. But we are well on track with the turnaround, where we set an initial target to reach 10% in all of our businesses and some of the businesses are there within metals and some have still more work to do.

In Russia, all altogether the process that we have gone through during this first quarter and even after the end of the first quarter, we naturally started from the immediate emergency actions that we needed to take with regards to our personnel in Ukraine. We evacuated those people who were able to leave the country. They are now settling in neighbouring countries, and we've offered them jobs and they are being employed by us mostly in Czech Republic at this moment. We had a very small organisation in Ukraine and the remaining individuals are still there working and trying to do and conduct the business, if possible, in those conditions.



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Our backlog altogether to Russian customers was at the end of the quarter 479 million. And out of that, 315 was scheduled or planned for delivery in 22. That's for the second, third and fourth quarter altogether. So, we were able to ship something during the beginning of the year, but we announced in early March that we ceased temporarily all deliveries and we are not accepting any new orders. We are not making any new proposals either to Russian customers. But we do have many contracts with Russian customers and with these contracts, we have now established a process where we wind down the contracts in a controlled way so that we consider really the viewpoints of our stakeholders, including our customers, including our personnel, including our owners as well. So, we are managing those contracts with the idea of winding them down during the coming months.

We know that sanctions are a sort of moving target. We do get a new round of sanctions every three to five days from different regimes and we are naturally following very closely those, and we don't compromise anything with regards to those. There are also export controls that we have started to see, export controls that are relevant for our business as well, and we can expect this situation to become even tighter depending on how the situation develops in Ukraine. Also, banking, availability of banking and logistics is an issue that requires quite a lot of management right now.

And at this moment, I'll hand it over to our CFO, Eeva Sipilä, for the financials. Indeed, and I'll return then at the end.

Eeva Sipilä

Thank you, Pekka, and good morning, good afternoon, everyone, on my behalf. And starting with the income statement. Our CEO already commented on sales and adjusted EBITDA. I would just repeat, we are pleased with the start of the year with a 13.5% adjusted EBITDA margin and 12% EBIT margin. The environment was not exactly providing a tailwind to us. Our sales mix was more equipment than services driven. We had the omicron variant affecting, especially in the early part of the quarter more generally and then moving to effect heavily China in March. So, the supply chain situation was tight, but then we have worked hard on pricing and protecting our margins with the various types of activities. The reality, of course, is that this work is not over. We are chasing a moving train [ph 00:14:18].

Our net financial expenses at -20 million were high for the quarter, but they do include a one-off cost of €11 million which resulted from the termination of the Russian rouble hedging. Our effective tax rate for the quarter was 27%. And in the graph on the right, you see our EPS development 11 cents in the quarter. And the ongoing divestments reported under Discontinued Operations proceeded during the quarter and we hope to be able to close both of them during the second quarter.

Moving then to the balance sheet. So, total assets are up around 300 million from the beginning of the year. The growth in assets comes mainly from working capital items as can be expected when we are seeing such strong sales growth. The amount of operative assets, inventories and receivables related to our Russian customers totalled approximately €100 million of this end of March balance sheet. And the value of these assets will be determined in the coming months and depends on how the conflict and sanctions evolve and to what degree we are able to wind down our business in a controlled way.

The graph on the right tells the most important story on our balance sheet. Our net debt has continued to decrease during the first quarter of the year, and as earlier discussed, this gives us the possibility to move forward on our growth strategy.



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And we did announce a small acquisition last week, well in line with our strategy to continue strengthening our presence in our core markets of aggregates and minerals.

Moving to cash flow. We generated €74 million of cash in the first quarter from operating activities before financial items and taxes. This is down on last year's comparison period. This direction is as such as expected as we have moved into stronger sales growth, which typically ties capital. Also taking into account all supply chain challenges that unfortunately don't look to improve but rather can be expected to become worse due to the war in Europe and the COVID lockdowns in China. Inventories can be expected to grow in the coming months as well.

I will conclude with a slide on our strengthened financial position. Our net debt is down to €443 million at the end of March. And this despite the fact that we made an additional €50 million repayment on a bank term loan during the quarter. This strength in our financial position naturally helps to address any potential cash outflow risks relating to the winding down of our Russian business without affecting our ability to grow the company both organically and inorganically.

A few explanatory words, still perhaps related to cash, on what is hopefully a comprehensive information on our Russian exposure in our interim report. We mentioned in the update separately the contingent liabilities related to advance payment guarantees, something that is off balance sheet but does contain a cash risk. The amount of €269 million we disclosed is a gross number for guarantees related to deliveries to Russian customers, and this would indicate the maximum cash outflow risk.

Naturally, various projects have evolved since their start, a lot, and cash has been used mainly for procurement and deliveries have been made until the start of the war. So, depending on the outcome of the winding down discussions in the coming months, rather than the gross, the relevant number is then what remains the fair value of these original guarantees at the end of the day to either party. This, like the other Russia-related risks, we will know more about in the coming months. The uncertainty today is big, and it comes from so many moving elements that we felt it most prudent to be transparent on the exposure and then we will obviously be able to report on the actual outcome later on.

Further highlights on our financial position include that our sustainability-linked funding arrangement with Nordic Investment Bank signed in Q4 is still undrawn and expected to be drawn during the second quarter. Also to note that our liquid funds will be used in the second quarter for the first of two payments of the dividend, assuming the Board's proposal gets approved in the AGM later today.

And with that, I will hand it back to our President and CEO. Pekka, please.

Pekka Vauramo

Thanks, Eeva. A couple of slides about our strategy, sustainability, and then finally the outlook for the next six months. We announced in January that our metals segment will go through a strategic review. And as a part of that process, we moved hydrometallurgy, one of the business lines previously in Metals, to our Minerals segment. And this was because hydrometallurgy is very much synergistic and then there are future opportunities with regards to battery metals and recycling of batteries with that technology and we wanted to retain that one closely with the minerals business area.



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Hydrometallurgy plays also an important role in our Planet Positive offering. It is technology that will reduce need for combination [? 00:20:40] in metals processing and especially with the very low-grade ore bodies, it will be a sort of more common technology applied into the future. And therefore, we feel that it must be part of our portfolio going forward in any case. The remaining metals business is really going through under strategic review. We have three business lines there. We have smelting metals and chemicals processing and ferrous and heat transfer businesses. And these are all going still through the turnaround programme and there is some work left in that one and we are really preparing now ourselves for the final phase of the review. We don't have a timetable for that one, but we will complete it within this year clearly.

And just recently, as already mentioned by Eeva, we acquired an aggregate company called Tesab Engineering in Northern Ireland. In April, we signed the agreement, and we expect that one to close in May. It's mobile processing plant equipment for aggregates and that complements nicely our coverage and forms a good a platform to put more Metso-branded crushers into marketplace to be serviced later on than by us and our dealers.

In sustainability, we made good progress. We have here a sort of rolling 12-months sales of Planet Positive products. We stand now at 636, and at the end of last year we had a rolling 12 month – so, full calendar year – 21 sales, that was 593. So, clear growth within one quarter of Planet Positive sales. We've launched several interesting products and technologies. We launched our digital twin during the quarter. That is a tool where customers can optimise the entire process, optimise in a way that it really looks forward what will happen in the process and therefore eliminating waste, improving recovery of the process, and thus contributing to Planet Positive targets what we have.

We have taken many actions in our plants and own operations to reduce energy consumption and therefore reduce the emissions. We also launched some of the new Lokotrack range of electric crushers or mobile crushing plants. And that is very much a direction and a trend that we see our customers taking in order to eliminate the emissions in job sites and quarries. So, many good positive developments in sustainability. And we continue these efforts as we move on in implementation of our strategy.

And the market outlook, we sort of repeat our outlook. Market activity is expected to remain at the current strong level. This is despite the situation in Russia. We see very much that the rest of the world will compensate. We are already starting to see increased activity that is very much supported by higher metal prices. And if continued on a higher level, we will see the activities even intensify in other parts of the world and supporting clearly, especially our minerals business going forward.

But those are the words from the first quarter. And now to the Q&A. Thanks.



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Q&A

Operator

Thank you. And if you do wish to ask a question, please press 01 on your telephone keypad. Our first question comes from the line of Klas Bergelind from Citi. Please go ahead.

Klas Bergelind

Thank you. Hi, Pekka and Eeva. Klas at Citi. A couple of questions, please. The first on the Russia impact. There is 215 million – 215 – out of the backlog that you can unwind at the moment that is not sanctioned, and then in terms of orders, you're saying that you could compensate for the lost orders elsewhere, which is a really reassuring message. How quickly can you unwind the 215? Just to understand the quarterly phasing.

And, Pekka, can you talk about the order pipeline outside Russia? Arguably, a tighter supply/demand backdrop right now, but interested in the near-term development, whether this order level also can continue into the second quarter or if it's more back-end loaded in the year? Thank you.

Eeva Sipilä

Thanks, Klas. If you start with the sales, so you're right, that as of today on sanctioned parties is a bit more than 200 million. Basically, sort of the sanctions, the latest round is such that there are export control restrictions coming into place early July. So, I'm not sort of personally expecting a huge amount to be possible since the time is so restricted. Of course, they don't apply to everything, but it just kind of shows the challenge ahead, and probably there will be several rounds if the war continues. So, it's something that one needs to be a bit cautious about. But we'll see what we can agree on in the winding down process with our customers. Then maybe, Pekka, you take the order pipeline question.

Pekka Vauramo

The order pipeline for the rest of the world really looks promising. So in that regard, we are not concerned about the void that the fact that Russia we will not book any orders now, and looks like we will be able to compensate that one. The order book built up very nicely throughout the quarter. We had all months during the quarter were strong order booking months, so they were not front loaded, not back loaded specifically, those orders. So very evenly coming, which is typical for this kind of smaller orders, while the bigger single orders were absent during the quarter.

Klas Bergelind

Okay, good. My second one is on the margin in minerals. The last quarter, I think you had a 15 million – one, five – net negative that you couldn't compensate for in terms of price cost. And that seems to be considerably smaller now, which is a job well done. Can I ask you about the surcharges and how they're now kicking in on the energy side? Are you effectively



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saying that we can draw a line in the sand in terms of energy inflation? Or can this be an incremental risk for you into the second quarter?

Pekka Vauramo

Yeah, I think it's more a line on the water than sand. We can draw, because nobody knows what the energy price will be going forward. But we have naturally sharpened our way of doing our costing and especially the advanced costing of items. And mostly this has been an issue in our consumables business, which is part of our aftermarket. And then we have three items that have been very volatile and where we have seen really sharp price increases. That is energy, that is logistics, and that is also raw materials. And all these items are now major items in our consumables. And therefore, we see the impact over there. And out of our consumables, most go to the Mineral segment.

Klas Bergelind

Yeah. Okay. Thank you. My very final one, quick one, is: into the second quarter outside mining and outside Russia. I'm thinking about aggregate, strong growth in North America; China also seems to do well on the back of those super quarries. European growth, however, is slowing. And I'm just trying to think, is that an Eastern European comment, Pekka? Or is it widespread European construction uncertainty?

Pekka Vauramo

Yeah, it's – how would I say it – it's a somewhat mixed view in Europe. We saw really strong ordering by end customers who place orders directly with us. But our dealers were somewhat reserved in placing orders. That was very much the view in Europe. So therefore, I'm not overly concerned about the European situation since the end customer demand is there. But I can, on the other hand, understand if dealers are cautious in a situation and they maybe might pause for a while before replenishing the stock that they have of new equipment.

Klas Bergelind

Okay. Thank you.

Operator

And the next question comes from the line of Max Yates from Credit Suisse. Please go ahead.

Max Yates

Thank you. Just my first question was around the lockdowns in China, and just wanted to understand sort of for your business, how much or what the specific pressure points from that may be. Is there any sort of sense you can give us of



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what your sort of major component purchasing is out of China, where that may have an impact and kind of how we might think about the size or the direct impact for your business? Just any additional colour, because obviously that was something that happened later on in the quarter, so probably isn't yet showing up in your numbers.

Pekka Vauramo

No, we had shut down in our foundry in China. Shut down one week. That was during the quarter, wasn't it? Yes, it was during the quarter. What has happened since that is that the logistics out of Shanghai is very much congested. It's very slow and therefore congested. We are using other ports currently and we are supplying consumables out of this foundry to North America, for example, out of there.

We do have some other components, but less and less nowadays from China, components that we need to build equipment in our assembly plants. But mostly what we do in China in our own plants are for Chinese market nowadays, and the sort of international logistics is not really a major issue for us. But certainly, there are goods that we are expecting. There are goods that our suppliers are sourcing from China. And let's say the full picture hasn't really been formed yet for us.

Max Yates

Do you think if we'd seen sort of the first few weeks of April revenues, do you think the impact from what is happening in China is big enough to see the impact in total revenues for April? I'm just trying to understand if externally, we would really see an impact from this or it's sufficiently small that it can be managed across the group.

Pekka Vauramo

At this moment, it looks like that it's manageable.

Max Yates

Okay, perfect. And just my second question is on the winding down and Russia. So, if we're talking about 100 million of revenues that won't be delivered potentially some of the 215 as it's wound down, I just wanted to understand whether you think this is likely to have a disproportionate impact on margins from any cost under absorption, any of the factories which may be more dedicated to these orders specifically? Or would it be right to think that the drop-through to profit from the lost sales would be more in line with what we would typically associate with the business? Any sort of disproportionate profit impact we should potentially think about.

Eeva Sipilä

I don't think, Max, there's anything special. I mean, really the bulk of what we're talking about, is equipment deliveries from the metals and minerals businesses. And as we've said, the aftermarket portion has been relatively low in that market, so



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really, and obviously any that has stopped. So, anything is really around now winding down these ongoing projects. But of course, the hassle on a daily basis is quite enormous. In a way, I would guarantee there's some hassle costs there just on the amount of time my team is spending on this. But I wouldn't say that it's relevant from your point of view. The big question is really how to wind down in a controlled way, as fast as possible.

Max Yates

Okay. Thank you. And maybe just one very quick clarification. I think you mentioned on the - Can I just confirm, you said on the portfolio review of the assets within metals that are now discontinued that you expect to - I think you said - conclude that in Q2 potentially with a sale. Can I just clarify exactly what you said on that?

Eeva Sipilä

Okay. Sorry. No, Max, I was referring to the metal recycling business that we announced actually late in December. And that, we have said originally during the first half, and now it looks to go - Obviously, it didn't happen in Q1, so we'll aim to close that during the second quarter. And then the other asset that's reported under Discontinued Operations is a small waste to energy business that was already in that group in the Outotec times. So those were the ones I was referring to. And then the metal segment, per se, continues as a segment. It's still under strategic review process.

Max Yates

Understood. Clear. Thank you very much.

Operator

And the next question comes from the line of Aurelio Calderon from Morgan Stanley. Please go ahead.

Aurelio Calderon

Hi, Pekka, Eeva. Thanks for taking my questions. I've got two, if I may. The first one is on the aftermarket growth that you saw in minerals. Obviously very good order growth, 23%, but the sales growth seems to be more sluggish. What do you think is holding you back? Is it just availability of supplies or is it just because there have been some orders placed for, let's say, longer term than immediately? What's driving that divergence between orders and sales in minerals?

Pekka Vauramo

Yeah, it's very much so. It's our [? 00:36:58] to order service activity modifications, upgrades, because of the supply chain issue, delivery times are very long at this moment. We have been booking for several quarters strongly orders in that area and we are moving towards executing that backlog and getting to deliveries. But the supply chain is low at this moment,



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that's affecting. Customers are also somewhat hesitant during these very high metal prices to start the shutdown activities they just would like to run the operation and produce concentrates and cash flow in the first place.

Aurelio Calderon

Okay, great. Thanks. And the second one is around the metals margin. Obviously, quite a nice increase there. I wonder how sustainable do you think is that? And if you can comment maybe on the legacy projects that you have from the Outotec side, the [? 00:37:58] smelter project and those projects of that similar size? What do you still have in the backlog to deliver and how sustainable do you think margins are in metals from here?

Pekka Vauramo

Yeah, when we look at it operationally, metals, we are confident that the margin levels are holding. Naturally, we have issues with regards to Russian deliveries. They are both in metals and minerals but if not looking at those, I have confidence in margin levels where we are in our metals at this moment. And the order backlog-wise, other than Russia, of course, we are also confident that the margins are holding well.

Then the legacy projects, nothing really new to report on those ones. The ramp-up is progressing very close to the plan in Saudi, the smelter, and like we've said, that it's going to be end of second quarter when we can expect some further news out of it, or early third quarter. But the plant is up and running. It's producing. The quality is good what it's producing. We are ramping up the power level and the capacity as we speak according to a pre-set timetable. And that's where we go. And then the UK energy projects, that's another set of plants and projects where we have issues. The work continues over there. The plants are running, modifications have been made and we are verifying currently the outcome of that and really nothing new to report as such of them either.

Aurelio Calderon

That's great. Thank you very much.

Operator

And the next question comes from the line of Nick Housden from RBC. Please go ahead.

Nick Housden

Hi. Thank you for taking my questions. My first one, a slightly broader question, that if we look back to the 2020 CMD, you said you were looking for around a 15% group EBITDA margin and toward 20% in minerals. And I believe those numbers were over the cycle. I'm just wondering, how do you see the progression towards those targets?



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Pekka Vauramo

They are still our targets. We will not move those targets. If we look at 2020, 2021 and also going forward from now, earlier I've answered to this question that we would like to see a bit more stable environment around us to deliver a firm set of results in a more stable environment. We haven't quite had that luxury, first because of the pandemic and now because of the situation in Ukraine. But we are working towards that one. We have our growth plans. We have set higher targets internally for our business lines and businesses.

What we have there, we do have our M&A pipeline where we have identified product areas that we would like to strengthen through acquisitions. And these product areas are such where the aftermarket content is high, higher than the average aftermarket content. And these are product areas where we don't have antitrust issues. So those are the priority areas for us to look into going forward. And then, of course, the 140 million cost savings that we delivered during the integration, and there is still the annual impact that's coming in and out of that combination, we are starting to get closer to 15. But of course, the Russian situation will mean something in this development again. But we retain the target.

Nick Housden

That's helpful. Thanks. And my second question: One of the themes in the past year or two amongst mining equipment companies is that mines around the world, especially things like copper running at very high capacities to take advantage of the high price environment, and as a result of this, miners have been putting off equipment maintenance work or equipment replacement just to avoid interrupting that high-profit production. Are you still seeing that dynamic? Are we getting close to the point where equipment needs to be replaced or refurbished, otherwise it risks breaking down?

Pekka Vauramo

We are seeing some of that activity. It is coming back. And then additionally, the activity that we see in some parts of the world is that our customers are going through the old suspended operations, mines and mills to see whether they could restart them. And really to get additional production from them. And we have several of this this type of enquiry, it is currently what will support our service business.

Nick Housden

Great. Thank you very much.

Operator

And the next question comes from the line of Vlad Sergievskiy from Bank of America. Please go ahead.



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Vlad Sergievskiy

Yes, thanks very much for taking my questions. If I can start on some clarifications on Russia. Firstly, thanks for disclosing the backlog for execution there. Would you be also able to provide a range of book and [? 00:44:03] revenues, perhaps including services which you hope to get in Russia, in Ukraine, before basically this situation developed? And also, would you be able to disclose maybe the range of order intake contribution from Russia and Ukraine in the first quarter of 2020? So, that's the first question.

Eeva Sipilä

Yeah. On the first one, we wouldn't comment on what we saw as a pipeline. Obviously, a third of the market in Russia was an active mining market and there was an expectation of orders to come that clearly now will not materialise, at least not for Western suppliers. And, obviously, there was no [? 00:44:52] on that. It was an expectation on a pipeline. Then to your other question on the order intake. Some marginal orders were booked in January/February before the start of the war. But obviously nothing since. You could say that very much the order intake is thanks to the rest of the world, and everything else is really marginal.

Vlad Sergievskiy

Thanks very much. That's helpful. And if I can move on to cash flow. Obviously building working capital, which you flagged, which was expected, do you think you are largely through this working capital building phase for the year, or the rest of the year could see some incremental build here? And on the impact on the cash flow from this winding down of Russian activity, would you be able to provide perhaps a range of potential cash flow impacts? Are there any scenarios where actually cash flow impact could be positive from those wind downs?

Eeva Sipilä

Yeah. On the cash flow, if we think, there is obviously a seasonality in our aggregates business and where we ramp up volumes and inventory in the first half more than in the second half. So that would be in line with your expectation that we've seen a bigger build up now. I am a bit hesitant and cautious to comment because of course the situation now with shipping is due to the Shanghai shutdowns, it is very new.

And we remember very well from early 2020 when COVID first started in China, how difficult it was and how long consequences it had. It's very early to say if this will be an issue, as Pekka mentioned, maybe our exports out of China is not a huge amount, but obviously we need vessels all over the world. So how this will impact, I think is somewhat difficult to estimate. I do expect there to be a difficulty to buy because of availability. You have to buy in a batch or then you have to buy something a bit in advance while you wait for something that's late.

So, this type of inefficiency always builds up on inventory. It is quite impossible in today's environment to run a just in time efficient and lean operation, unfortunately. So, I'm more on the cautious side, that we haven't seen the bulk, but obviously there is that underlying seasonality in our business that should of course be visible this year as well.



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Vlad Sergievskiy

That's great. And if you can comment on potential impact on the Russian unwinding on the cash flow. Is there a scenario when this impact could be even positive?

Eeva Sipilä

Well, I think there is an impact where it's certainly sort of neutral. And of course, we're working towards that target. We wanted to kind of flag the risk but obviously we're working for a better conclusion. I wouldn't necessarily, at this point, flag for a positive outcome, more I would say that neutral would be the best case. But, as I mentioned, there's just so many moving parts and this thing move only daily: it moves several times during the day. So very difficult to say at this point. We'll obviously communicate to the markets when we know more during the course of the coming months.

Vlad Sergievskiy

Very helpful, Eeva. Thanks very much.

Operator

The next question comes from the line of Antti Kansanen from SEB. Please go ahead.

Antti Kansanen

Hi, Pekka and Eeva. Thanks for taking my questions. Firstly, coming back to the mineral services side and comparing the order growth and sales growth, and you provided already some colour, but is pricing a significant moving part here? I mean, you mentioned that you're being perhaps more aggressive in hiking the prices and one would assume that this is more impacting the orders at this point of time and not sales. So, could you comment on that a little bit?

Pekka Vauramo

Yeah, we have naturally taken in all our businesses' actions to mitigate the impact of inflation, which in some areas has been more dramatic than in others, and there is clearly that impact visible in our volume growth in all of our businesses. But other than that, I would not like to comment more on pricing.

Antti Kansanen

Okay. And then secondly, if you look at the energy cost and inflation over a longer time period, is it something that you are more looking into your production footprint regarding your foundries in Europe or considering alternative options in, let's say, longer than just Q2 or just 22?



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Pekka Vauramo

We have started the process of looking into what our footprint should be and naturally avoiding extreme energy cost prices. That's one target. The second target that we do have is source of energy. Sustainability is important for us. It's important for everyone. And therefore, we pay attention to availability of green energy: wind power, foundry technology, where we can use electricity rather than fossil fuels to power it and things like that. So, yes, we are looking for a longer-term solution rather than just fixing one quarter.

Antti Kansanen

Okay. And then maybe a couple of questions on the equipment side on metals and minerals. So first, just a clarification. How much of Russia sales did you kind of book on January, February this year on those two divisions?

Eeva Sipilä

We decided not to disclose that number. There were some [? 00:51:35], but we're focussing now in the communication, really on the outlook and hence sort of the forward-looking numbers.

Antti Kansanen

Okay. I'm just thinking that if you then look at the backlog that you have, excluding Russia and going into Q2 and onwards, can we expect increasing sales contribution on the equipment side, given that the Russia is not there really from Q2 onwards? And how should we think about timing of the backlog that you have ex Russia?

Eeva Sipilä

Yeah, since that backlog is equipment heavy, so what I think will happen is that we will see a mix, sort of change, that we actually will have a more aftermarket business in minerals coming through in the second half of the year than perhaps earlier planned. In metals, the share of aftermarket is not that big, that it's not necessarily a material movement. But that is one conclusion you can make certainly for the second half.

Antti Kansanen

Okay. And then lastly on the restated numbers, the division of numbers and obviously you moved a couple of hundreds of millions in sales last year from metals to minerals, but the profitability impact was really quite minor. So, how would you comment on the profitability of the hydrometallurgy business if there are some Group overheads that kind of mix the comparison when we look at the restated and reported numbers, or is there something else that explains the low profitability that that business seems to have?



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Eeva Sipilä

No, nothing really. It was not a good performance year for that business. That is very obvious from the numbers. But there are no allocations or anything like that. There were, I would say, legacy issues in that business and we're confident that can be dealt with and the performance already this year will be better.

Antti Kansanen

Do you see the underlying performance or the potential of that business being more aligned with the equipment business in minerals more broadly?

Eeva Sipilä

Yes, we see that business has potential. And as Pekka mentioned, it's a very good fit. From a strategic point of view also in sustainability and battery metals area. Obviously, it requires that we are able to improve the performance of that. But, yes, we're confident that it can and will happen.

Antti Kansanen

Okay. And then very lastly from me. I'm sorry about labouring the point on the cash flow impacts of the Russia winddown. So, do I understand correctly that the reasonable range that we should think about, best guess is neutral and then the gross advance payment is the worst-case scenario, that in cash flow terms could impact you? And the reality is somewhere in between that.

Eeva Sipilä

Yeah, hopefully not in between in the sense that, as I said, the gross exposure is obviously max and max/max. But, yes, that I think is a good working range and obviously we do our best to get to a decent outcome for, as I said, all stakeholders.

Antti Kansanen

All right. Thanks so much.

Operator

The next question comes from the line of Panu Laitinmäki from Danske Bank. Please go ahead.



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Panu Laitinmäki

Yes, thank you. I have two questions. So, firstly, on the gross margins, it was down one percentage point year on year. How do you expect this to develop going forward? You said that you were better able to mitigate the cost inflation. So, is the gross margin trend improving. And then the second question is on the cost synergies. Would you have a rough number? How much was the EBIT impact in Q1 and what should we expect for the coming quarters? Thanks.

Eeva Sipilä

The gross margin, it's mainly a result of the mix. We had a rather significant change in the sales mix with service services versus equipment. And basically, in Q1 now we were at 47% share for services, which is quite a few percentage points down from last year. And in that sense, this is an equipment cycle, a point of a cycle where equipment is heavy and should be growing fast. Then again, my answer to the previous question – was it from Antti? – on the mix, and obviously the fact that we will have less equipment deliveries because of Russia in the mix then, then obviously that affects the numbers into the opposite direction.

On the cost synergies, no, I have to admit, I don't have the number in my head, but basically what you should be looking at is we had 140 million at the year, and was the run rate on the total. And basically, a quarter of that every quarter is kind of how you then come to the annual full rate then. But obviously if you want to be very precise, you can look at where we were at the end of Q3 and Q4 and kind of look at the delta. That's the other way. But way I think that 140 divided by four is a rather good proxy. But bearing in mind that there is of course, in Q1/21, there was already some benefits there in that number.

Panu Laitinmäki

All right. Thank you.

Operator

And the next question comes from the line of Joel Spungin from Berenberg. Please go ahead.

Joel Spungin

Hi. Good afternoon. I've just got a couple, actually. Maybe I can just start - you talked a lot about, with regards to Russia, with regards to winding down outstanding contracts there. But actually, I'm just kind of curious to understand what exactly does winding down a contract entail? What is the process that you need to go through?



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Eeva Sipilä

Well, it can be many things. Obviously, we need to come to an agreement with the customer, how do we depart? We cannot continue business and they obviously have needs that they will need to fulfil with other partners, and depending very much on the content of the agreement and very many details: where we are, what is the realistic outcome in a way to go our different ways.

Joel Spungin

Okay. And then again, coming back to the question of the 269 million. So, if I've understood this correctly, it is contingent. So, had you actually received this cash, is it actually on your balance sheet?

Eeva Sipilä

It's contingent. But of course, in normal circumstances, it was cash that was expected to cover commitments that we have made in order to proceed with the projects. So, it is of high interest to us, in a way, that it is fairly distributed between the parties at the end of the winding down.

Joel Spungin

Right. So is the point here that you may still have to execute some or all of these contracts or in some way, and therefore, there could still be cash outflows related to that. Is that what it amounts to?

Eeva Sipilä

Yeah, in a way that's true. And then obviously, if we do not execute, it may be the best outcome that the customer uses that money with some other partner to move forward and move their project forward. So, the whole variety, as things were interrupted, unfortunately, very abruptly by the situation, obviously means that it's quite a puzzle to pull together.

Joel Spungin

Yeah. Okay. Understood. Thank you very much for that.

Operator

And we have just one final question from the line of William Mackie from Kepler Cheuvreux. Please go ahead.



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William Mackie

Good morning. A couple of questions, please. Firstly, with respect to the demand outlook in the minerals business, I wonder specifically, would you share your thoughts on the prospects in South America? I mean, the whole market seems disrupted by political turmoil for over 12 months. It's quite acute at the moment, which must cause hesitation to invest.

So, what do you think the prospects are running into late this second half this year and next year in South America? The second question, we haven't really revisited many of your discussions around supply chain, supply chain tensions and logistics. It sounds like you've made great progress in Q1, but do you still see a number of pressure points across the aggregates or minerals business which could lead to some challenges going into Q2, Q3?

And the last question is around pricing. I hear your reluctance to disclose too much, but can you say whether you're able to net price up, i.e. when you look across your business lines, are you successfully fully mitigating the inflationary pressures you're seeing from energy, materials, logistics and other parts of the bomb? Are you happy with that or are you seeing some of these project margins or gross margins having to be partly compromised? Thank you very much.

Pekka Vauramo

All right, good. Starting from South America. Yes, we've we followed the politics there, naturally, and it's not speeding up the investments in south of South America. And then we see also some adverse development in other parts of the world, including Russia. And for us, this means that copper price will continue to be on a high level, and this level is expected to continue, and that will further encourage operating mines to boost their production, will encourage our customers to reopen closed mines and the mills.

And we see this maybe tightness on greenfield leading into more opportunities in upgrades and modernisations and start-ups of old mills, which very often end up in our service business. We also at the same time, if there's something that we cannot deliver to Russia, we will be able to either use those supplies elsewhere if they are suitable, or then release the supply chain for faster delivery. So, we see also opportunities coming out of this development.

Eeva Sipilä

Then on your question on supply chain tension, William. I was referring to that really that it is kind of chasing a moving train in a way. So certainly, the challenge is really on the volatility and availability and in knowing what will be out of availability, so to say, next week. So, we are cautious and expecting very tough months and a tough year from that point of view. And because these, as I said, the supply chain was tight because of COVID and kind of never got to its feet almost, and now it's been kicked again on its knees. So, it is a really difficult situation, even if obviously we have the benefit that we have very strong demand. But obviously, we would want to serve our customers better.

And then your final question on pricing. So, obviously, our aim is to fully mitigate the inflation is such in many of the areas where we work that it is not feasible to squeeze it in the margin. It has so to be compensated. The challenge is really the timing in a way. That's when things move as quickly as we've seen also in this quarter, to get it timely enough and having



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so much proactiveness in being ahead of the curve. So, that is an area where we're more struggling. But I think we'll leave it with that and head into our AGM, I believe.

William Mackie

Thank you very much.

Operator

And as there are no further questions, I'll hand it back to the speakers.

Juha Rouhiainen

All right. Thank you, everybody, for taking part, listening and asking questions. We wrap up this call. Now we go straight to our AGM and we're looking forward to meeting and see you next time. Thank you. Goodbye.