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Schneider Electric SE (SU.FR)

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MANAGEMENT DISCUSSION SECTION

Amit Bhalla
Senior Vice President & Head-Investor Relations, Schneider Electric SE

Well, good morning. Thank you, everyone, for being here for our Q4 Revenues and Full-Year 2018 Results. Appreciate you being here. It's a full room, and we're also live webcast. So, welcome to everyone online as well. Of course, we have Chairman and CEO, Jean-Pascal Tricoire, to take us through the business performance for 2018; and Deputy CEO and CFO, Emmanuel Babeau, on the financial presentation part, followed by a question-and-answer session.

So, with the usual caveats on disclaimers on slide number 2, I think we can get started. Over to you, Jean-Pascal.

Jean-Pascal Tricoire
Chairman & Chief Executive Officer, Schneider Electric SE

Okay. Thank you, Amit. So, I'm going to go straight to slide 5 to go through the business highlights. Like to remember or remind you, sorry, that we've positioned Schneider, over time, in one unique mission which is to supply digital solutions to our customers, energy and automation digital solutions for efficiency and sustainability. And we've done it by building two very strong business, €20 billion in Energy Management, €6 billion in Industrial Automation that serves two major transitions of the fourth industrial revolution namely the energy transition and Industry 4.0. And we do it to bring very tangible benefits to our customers in terms of efficiency, productivity, safety, reliability and sustainability. And we do it by focusing very strictly on four markets: buildings, data centers, industry and infrastructure.

And I will repeat many times today, in a very balanced manner, where our commercial application, say, building and data centers are making roughly 50% of our business; and our heavy duty applications, industry and infrastructure are making also 50% of the business. We're going to review 2018 today and speak about the future, 2019. We're going to try also to go beyond 2019 into the next three years. And what we want to tell you here is that we've been and we want to be very consistent in the future in the way we keep growing and making more profitable the business.

So, going on the next slide, which is a picture at the end of 2018 of our business, €26 billion; plus 7% of growth, again, Energy Management, €20 billion; Industrial Automation, €6 billion, both of the business growing between 7% to 8% in organic growth and both of them improving their profitability by 60 bps to 70 bps, and the total of the company delivering 15.1% of operating results at the top of the guidance we had given at the end of 2016 and repeated at the beginning of the year, plus 50 bps of operating result.

If I go into the detail of 2018, I would say, it's been characterized as a strong year in terms of growth, in terms of profit momentum. It's a year where we've reaffirmed a strong focus on our shareholders. If we start by growth, again, 6.6% of organic growth. Our growth of products is really in line with that. Remind you that Schneider is the strongest company of products going to partners in the world, and we keep expanding our network of partners everywhere in the world, name them contractors, OEM, integrators, we are the leading franchise in providing blocks of technologies that our customers are integrating together to provide solutions everywhere in the world.

But in the past years, we've triggered new sources of growth. The first one is services. So, services this year growing 9%, so growing strong. And it's just the beginning. I would like to say today, services represent 12-plus percent of our turnover, physical services, which we call field services, and digital services. And we see still plenty of potential for the business to grow as, in many cases, only 10% of the installed base is served, as we speak.

Second axis of accelerated growth is digital, and especially everything we do around EcoStruxure and software, so software growing above double digit, EcoStruxure growing easily above group average. And last point I want to mention that our system business is growing lower – at a lower pace. But here, our target is to increase the profitability, and again, in 2018, we saw another 70 bps of operating margin improvement on our system business. With such a growth that starts from strong and leading position, we clearly gained market share in 2018.

Going to second part of the year, which is profit momentum, very happy to and proud to declare more than 10% adjusted EBITA growth in percentage going 50 bps again at the top of the guidance we had given. If you take a little bit more depth of review of what we are doing here, it's a steady and continuous increase of our profit, 210 bps organically over the past three years, which results into a historically high net income, an increase of 9%; and EPS, an increase also of 9%. And we're going to explain later that this is just middle point of our ambition. And we want, in the next three years, to bring the level of profitability of Schneider to the next level and are targeting an improvement of 200 bps as we go forward in the next coming three years.

Then, you know that the story of Schneider has been done of 10 years of building the portfolio, which were 2003 to 2013. Since 2013, we've been consolidating our capability and our portfolio. And we have been very focused on shareholder return, to give back to the shareholders what the company does during the building of – the time of building the portfolio. And 2018 is another strong year of shareholder focus. Strong cash flow generation, 90% conversion. Actually, a bit below that what we were expecting at the beginning of the year, but the cash flow has been disrupted by some of tension on supply chain during 2018, such a strong growth had impacted especially in H1. But the operational cash flow is growing by 13%, which is a great sign for the future.

Very disciplined on successful M&A. First steps of AVEVA which is occurring today, great first steps. Another company in software, IGE+XAO, in electrical design is delivering strong results; and ASCO in the field of Secure Power, in the field of microgrid is great adding to our portfolio.

Then we accelerated our buyback programs in H2 and realized €1 billion that we're supposed to finish mid-2019 in 2018 and we are committing to another buyback program for the next three years of €1.5 billion to €2 billion. And we're going to be proposing a dividend to the AGM of €2.35, an increase of 7%, so a progressively increasing dividend as per the commitment we took a few years ago. And while we still do acquisition and while we are very impacted by the Forex, we deliver another improvement of the ROCE at 11.8%, an increase of 40 bps before Forex.

So now, I would like to review with you what are the foundation of such performance. The first one, and this is clearly a very strong point of Schneider, it's our global presence and the balance of our geographical presence around the world. Now, it's been the case for some time, but number one comes Asia-Pac, which is delivering, which is first, our largest region. You know that it's a matter of debate at the time in my country of origin, but this is our largest business and that doesn't include the non-consolidated Delixi, for instance. So, the reality is even better and higher.

And Asia-Pac is delivering 10% of growth in 2018 growth in 2018 with China almost at 15% of growth, so a very strong contribution of Asia-Pac. Second very good news, our second zone, North America, growing fast and strong at 8%; West Europe, back to growth, which is good news, at 3% of growth; and the rest of the world, namely Latin America, Africa, Middle East and Eastern Europe, growing 5%, which is also a strong support for [ph] our dynamism (00:10:25).

Second point also to underline is that you have a bit of an unbalance between H1 and H2. During the past years, we rebalanced our portfolio to more mid- and late-cycle business, expanding our technologies into the field of industry and infrastructure. And you see that today we have a balanced portfolio between early and mid and late.

Third point, the growth of our accelerated growth engines, services and software, which have been expanded inorganically and organically. I already spoke about them. And you see that this is now more than 16% of our business. And finally, we kept working on the flexibility of the structure of our P&L with 70% of our cost being variable and being shouldered upstream on our suppliers – partner suppliers; and downstream on our partners integrators. So, a lot of what Schneider does is to be working with network of partners, upstream and downstream, to remain very flexible.

What has paid a lot to deliver such a growth also is our focus on very key segments of Schneider, double-digit growth in Buildings; Data Centers, high double digit, very strong presence there. Consumer Packaged Goods is also a strong point of ours. Oil & Gas, a rebound of oil and gas, we see it in our portfolio in Energy Management, in Automation. Wastewater is also a strong place of ours. Mining, Metals and Minerals was also high-single digits and Machine Solution mid-single digit. So, all of those focus have been delivering and, of course, here the platform of integration is EcoStruxure that allow our customer to bring into one solution, Energy Management for energy efficiency, Industrial Automation for process efficiency, into one complete solution, digital solution of efficiency and sustainability.

The next one beyond segment focus has been what we do in digital. So, a big progress in 2018 in digital, and we've spoken a lot about that in the past. So, what we do at the level two and level three of EcoStruxure, which to speak in English is a control level and the software level of EcoStruxure, has been growing clearly above group average. The number of assets connected to our own cloud – [ph] listed (00:13:14) on our cloud, for the sake of our customers, is now reaching 2 million assets, growing by 35% – 34%.

And what is also very interesting is to see that more and more of our interaction with our customers is purely digital. It's no touch. It's customers connecting with us directly through the digital space, e-commerce growing by more than 20%. More and more the customer support being generated digitally, digital customer satisfaction score growing and progressing to reach or to equate the one of our physical satisfaction. We are not yet there. But what you see here is that the number of connected customers has been multiplied by three since 2015 and it's exponentially increasing.

The next one has been launch of numerous new products. Schneider is, by and large, a product company. We sell products, I call them bricks of technologies, that our customers integrate into local solution. And a great strength of our company is to be by far the company that works the most with local partners around the world, and this is why we have to be so multi-local, because the products have to be adapted to the local partners. We have to be very [ph] capillary (00:14:39) on the field to serve those partners.

We have to produce locally to be very fast to deliver, but we've had a flurry of new products launched in 2018. And actually, you're going to see most of the effect of those new products in 2019, multiple recognitions in terms of innovation and the multiplication also of what we call our Innovation Summit, the place is where we gather our customers around the world. One was taking place in Paris this year during the Marathon, 20,000 customers that were gathered into 14 world events, and 10,000 more people into the reduced formula of it, which is the Innovation Days.

We've been, also in 2018, keeping on working on our difference respect to our competition. Why is Schneider different? Because, well, first, we want what we do to be very meaningful, our commitment to sustainable development, commitment to the way we do business on our strict adherence to the principles of the Global Compact and our mission in the world which is to deliver cheap and green energy to everywhere in the world, and help everybody in the world to save resources in their processes, in their life, in their work so that, on one side, we bring more while using less of the resources of the world.

Second point is our total commitment to inclusiveness and to local empowerment of our teams, which means that our model of operation, which is what we call a multi-hub, which mean that, for instance, I'm based in Hong Kong and our teams are based within the operational teams, is targeting to be the most inclusive, the most diverse and the most empowered company in our field. And when I look at the growth we generate in multiple geographies, well, 2018 is a marker of the success of this organizational strategy.

Finally, another year of strong commitment and sustainable development, which we measure in every part of the group through the Schneider Sustainability Impact, we are over-perform, over-delivering in respect to our initial target in this field, which means we're going to increase the initial targets we had. And that drives me into the second part of my presentation, which is more focused on the business performance.

So, I'd like to start first by Energy Management. So, Energy Management, a €19.5 billion business, growing in a compounded manner by 7%. The reality of the business we deliver here is a complete integration of Medium Voltage, Low Voltage and Secure Power. And you see that according to the target segments we have here; residential, small buildings, large buildings, data centers, industries and infrastructure, the mix of those technologies vary, but in most of the cases, we deliver this as a complete integrated solution.

What we have here as priorities is to focus on segment, on accelerating targeted segments. I spoke about that earlier, but that's also valid for Automation. Maximize cross-selling and further penetrate in terms of digital connection of Energy Management. Energy Management has a great potential of connectivity. When I look at our two business, Industrial Automation and Energy Management, Energy Management is vastly unconnected. While the needs to be connected, the needs to do predictive maintenance, the needs to put installations and the monitoring is as high as what we do on the process side.

So if I go into detail of the technology that we have in Energy Management, a great year in 2018. So, the first point I want to mention is a superb growth in Low Voltage. Low Voltage is a very profitable business where we have a strong leadership position. We grow close to 10%. So when you think at the mass of volume that this business represents and that we grow much faster than our competition that means we keep increasing our advantage in a very visible manner respect to our competition.

Second point I want to mention, you know that we had rebuilt our leadership in Medium Voltage, which is absolutely necessary in the Energy Management chain in industry, infrastructure, large buildings and data centers. It's your entry door into the system. And we had rebuilt it with acquisition that we are mostly motivated by the acquisition of technologies. But the problem we had is that some of those business that we had acquired were not profitable enough respect to what we want to have in Energy Management. So, we've been constantly working on the improvement of profitability of Medium Voltage and we scored another year at 130 bps, it's actually 400 bps of improvement over 3 years and which makes that now this activity is solidly anchored above 10% of profitability, more convergence in terms of profitability with the rest of Energy Management. And we can now make sure that we declare or report the reality of what we do, which is 90% of Medium Voltage and Low Voltage packages.

And finally, a great year also for Secure Power where the problem has never been profitability, but it was more growth and the growth was more tame in the past few years due to the changes of architectures in some parts of the business. But what we've seen now is a rebalance of architectures and especially a very strong development of Secure Power in Edge Computing and in securing all the IoT installations, which are happening outside of the IT business. And therefore, you see that this is driving – Secure Power is now going in 2018 by 5% of growth. And this is also the spearhead of a much higher growth in the field of data center, actually it's high-double digit growth in this space. So, what we do in Secure Power there is driving strong growth of Low Voltage, particularly in the data center space.

So, what we're going to do at the end of this year is to put in execution what we had preannounced mid-2016 telling you that – and which I repeat that we had isolated in our report in Medium Voltage and Secure Power, because 10 years before we had done acquisition and we wanted everybody to have a clear picture of what was happening in those verticals. But now, 10 years after, we have brought those business at the right level of profitability and we want to report our business as we do the business.

And when we do the business, we don't report, we don't sell Medium Voltage on one side, Low Voltage on the other side, and Secure Power on the other side. We sell to our customers full powertrains by end markets and by segments. So, that's what we're going to transition to in terms of reporting. And we're going to stay, as always, transparent with you on answering your questions.

But we're going to be speaking now about Energy Management and when you look at it reported by geography, our biggest geography there is North America. The second one is Asia-Pac. That's not inclusive of Delixi, so they would be probably at par with the re-inclusion of Delixi. Then West Europe and then Rest of the World. And what we want to do is to keep working on the synergies that we have between those three parts of technologies and make sure that we deliver a full EcoStruxure Power for our customers whatever the segment and whatever the application.

So now, I'm going to move on our second business, which is Industrial Automation, which is more than €6 billion business, growing once again in 2018 by 8%. Strong profitability delivery, 18% plus 70 bps of improvement. Actually, a great H2 also in this space. I'm going to be very cautious about what I say because the whole team of Industrial Automation is in the room, okay, because they were meeting in Paris and they were kind enough to come and control what I'm going to say on their business.

So, one of the things I want to underline here is that we are a full liner. We have organized ourselves and built the portfolios at Schneider is about to deliver on the whole spectrum of Industrial Automation. From machines to discrete automation, to process automation and, of course, with a capability to build a very strong presence in hybrid automation, which is developing actually very fast in the middle of discrete and containers.

Very proud also by the constitution, the building in 2018 of AVEVA. And without talking about them because they are talking about themselves as we speak today, it's been an absolute success. I mean, think about it. It's only nine months after the creation of the company, strong growth, strong delivery and plenty of synergies between the two parts of our software business and the rest of Schneider. So, a great adventure and a great development as we keep going.

So, Industrial Automation, we are very solid here. We keep developing EcoStruxure Machine, EcoStruxure Plant, strong links with the software. And clearly, what you have to understand is that the reason why we, from the beginning – I think from the inception, from 15 years ago when I was personally appointed CEO of our company, I told you that in industrial and infrastructure applications, the combination of energy and automation was absolutely key to our customers to manage our full equation of efficiency. And automation brings a cockpit of digitization for every system we deliver in industry and infrastructure.

And we verify it every day. As you see, the sales and the split of sale that we do in the main segments that we have in this sector. We always say this is the place, industry and infrastructure, where the balance of automation and energy is the most equal or is the most realized.

So, that's a global frame. Now, the real stuff, I would like to hand over the mic to Emmanuel.

Emmanuel Babeau

Deputy Chief Executive Officer in charge of Finance and Legal Affairs, Schneider Electric SE

Thank you, Jean-Pascal. Good morning, everybody. Great to be with you to talk about our 2018 performance. And I suggest that we dive into our numbers starting with H2, because we've been commenting H1, of course, in detail already, and I would like to have a focus on what we did in H2, of course, starting with our sales.

So, our sales for H2 amounted to €13.4 billion, it's plus 6.6% in published term. If you look at the organic growth for H2, it's plus 6.2%. And I would like to start talking about the Forex impact, which is still negative, around €200 million negative in H2. But, of course, the impact is much lower than the one we experienced in H1. And now, when we are looking towards 2019, we see even, based on the current parity, the Forex impact turning positive. We expect, based on today's parity, a positive impact on the top line that could be between €200 million and €300 million. And we see on the margin a Forex impact that would be close to neutral.

Scope, no surprise, I guess. That's, of course, the acquisition of ASCO and AVEVA, which is nicely contributing to the growth during the second half. And then, looking at the performance by region, a few interesting evolution and trajectory. The first, certainly, remarkable thing has been the performance of North America, growing plus 8%. H1 was already good. H2 is a further acceleration in North America. If we look at the U.S., we've been really growing across the businesses and the technology. And that's a confirmation that we are today having a very good run in North America and business is developing in a very nice manner. Good development as well in Western Europe. Western Europe is growing 4% in H2. It was actually growing 5% in Q4. And we've been growing in most of our geographies in Western Europe in the second half and notably in Q4, which is good news.

Asia-Pacific, I mean, still a star performer, of course, plus 8%. China is again growing in H2 double digit. And if you just look at Q4, China is still growing at 8% despite the fact that the comps are becoming much more challenging and we start to face very dynamic growth in the comps. Outside China, great performance as well in India, in Southeast Asia, so the whole region has showed a lot of dynamism. And then, Rest of the World, plus 4%. I mean, the region has been growing through the year around 5%. Here, it's a bit more of a mixed bag. I think we flagged the fact that Russia was a more difficult market. And it still is and notably for the Medium Voltage technology.

We have faced some tougher Q4 situation in the Gulf. First of all, as you know, we are exiting Iran and that it's taking its toll on the growth of the region. But globally, Saudi Arabia, the Turkish country, of course, Turkey being difficult, that has been more of a drag on the growth of the region. Africa was good and the good news that we see South America accelerating as well and having a much better second part of the year.

Now, if we look at the performance by business. What is very interesting is that it's quite homogeneous actually and we've been nicely growing across businesses and technology. Look, Energy Management 6.5%; Industrial Automation, 5.2%, facing higher comps in the second part of 2017. And when you look at the three technology within Energy Management, here again quite a nice consistency in the growth between 5% and 8% Low Voltage, still flying at the highest altitude, but good to see Medium Voltage at 5% and Secure Power at 6%.

Now, let's look at the margin evolution, which again is good everywhere and especially maybe starting with Industrial Automation, 120 basis point of organic improvement. It's not as good at the published level because of a very strong negative Forex impact in the second part of the year. But Industrial Automation has been very good in increasing price and also at improving the tension on the supply chain and decreasing the tension on inflation and cost of supply.

When you look at total Energy Management, at plus 50 basis point, but of course here the great performance is Medium Voltage, plus 130 basis points; and here, the Forex has been positive quite nicely in H2. So, that's why the published performance is actually 190 basis points. Medium Voltage at 13.4% in H2, and some of you may remember that we've been quite consistent in saying our objective is to have Medium Voltage above 10% in difficult time, and when things will get better, we think it's possible to put Medium Voltage much closer to 15%. It's not the end of the journey, but clearly we've been doing some very good inroad in that respect in 2018.

Low Voltage, 10 bps organic. So, of course, the biggest organic growth on margin is not going to come from Low Voltage, which is already at a very high level. Here, the mix has not been helping the evolution of the margin because it's a lot of growth in Low Voltage put in system and in equipment. So, not at the same kind of profitability that a pure product sales. We've been also investing quite a lot, let's be clear, with the star performer being that we want to ensure that we keep here leading, and that has been in digital, in innovation, a lot of investment, and that has been impacting as well the evolution of the profitability.

Last but not least, because I think it's particularly interesting, is the evolution of the margin on Secure Power, plus 60 bps, nice growth after several quarters of tension. And plus 60 bps here reflects, first of all, the good work that

I think the technology has been doing on cost management, but also the fact that we've seen growth nicely resuming in distributed Secure Power, so notably the small UPSs that are going through the IT channel, and this is a business which is coming at a nice margin, so that's helping when they see the growth accelerating.

So now, looking at the various blocks building the growth of our adjusted EBITA for H2, which amounted to €2.1 billion, the first one, of course, and most important is volume. Everything starts with top-line growth, so that's paramount. Second element, which I think is interesting and not coming as a surprise, is the fact that mix has been turning negative in H2. We are progressing through the cycle. We see, as I said, more solution, more system, more equipment that is generating more negative mix impact. But of course, that is providing nice growth at the level of the top line. Net price, frankly for me, that's the big and great achievement of H2. That mean that now globally on price we have been turning positive in the all H2.

And of course, it's even better if you look just at the transactional part, because here you are seeing the net price impact, which is a mix of price on transactional and the full raw material inflation impact on the entire business, including the solution. So, there is a kind of unbalance on what we are comparing. But if you just focus here on transactional, the price increase in the second half is twice the raw material inflation. So until now, we were saying we want to match one with the other. Actually, we double up in price increase, the raw material inflation in the second half. We think it just show that we are putting our act together and we are moving on price. Last element, which is a nice contribution as well, China has been turning positive in term of price increase in H2, and we have not seen that for quite a while.

Then the productivity, €180 million positive, it's a bit better than in H1. We start to, I would say, absorb the tension on the supply chain, but let's not be mistaken. There is still a lot of inflation in our procurement. So, there is still some pressure on the productivity. And altogether, of course, in 2018, we are not at the level of 2017 on the productivity. Tariff started to kick in and is playing here and, of course, is going to bring more negative impact in 2019. So, we are still expecting nice productivity in 2019 in the future, but we don't expect to be back to the 2017 number, which was quite exceptional, north of €400 million of productivity for the full year.

COGS evolution with inflation and R&D, here you have two elements delivering this negative impact. The first one, of course, is inflation on our wages and it's impacting the cost of goods. And the second one is that we keep growing our investment on innovation, on R&D, and that is also representing a negative impact. So, we are not generating our profit, the margin improvement, the growth to the detriment of building the future of innovation. We are doing both actually.

Then, the SFC growth, we keep investing. Same comment. It's slightly lower in terms of growth. We keep the differential of progression between the top line and the SFC evolution. But we absolutely acknowledge that we keep investing on digital, on services, on marketing for the future of the company. Then you have the traditional other elements that are difficult to classify, and then scope and Forex which are more or less offsetting each other.

One element which we look with a lot of attention, that's the level of gross margin. Gross margin level is absolutely instrumental and defining for the future of the company, because that's where we're going to bring our capacity to invest in our innovation, of course, in our priorities. And that's what's going to bring ultimately the margin improvement. And look at the evolution of the gross margin from 2015 to 2018, it's a net 200 basis point of improvement from 37% to 39%. And it is a combination of organic improvement and inorganic improvement, because, indeed, we've been pruning the portfolio with businesses with lower margin. We've been making acquisition. AVEVA is one of them with business with higher margin. But also, we've been working on price, on productivity and on improving organically our gross margin with the mix pushing product, pushing services, pushing software. So, that's a nice evolution. And it is, of course, our intention to carry on in that direction.

All right. So now, let's move to the full P&L for the group for 2018. So, revenue reaching €25.7 billion; organic, plus 6.6%; reported, plus 3.9%. Gross profit north of €10 billion, plus 5.7% in published, plus 6.7% in organic. I talked about the growth margin, so I don't come back on it. SFC growing plus 5.5%, but be careful, that is integrating, of course, the AVEVA contribution, which is accelerating the FC growth. Organic, it's 4.6%. So, we have 2 points of difference between the top line and the SFC. And it is, of course, our intention to keep having this nice differential and to have the SFC on sales ratio decreasing in the future. It has been contributing a 50 bps margin improvement for the full year.

That gives an adjusted EBITA of €3.874 billion. It's a plus 6.1%, plus 10.3% organic. Remember, at the beginning of the year, we were rather around 7%. So, we've been clearly beating our initial expectation. The margin is at 15.1%. So, now we moved, I would say, decisively in the high end of the lower part of the 13% to 17%, I would say, guidance or bracket where we see our margin and we have here today a clear ambition to see that we want to head toward the 17%.

And as I said, all that is not done to the detriment of innovation or – and to our future. The R&D on sales ratio is growing. So without growing in our R&D, we would have been actually improving by a further 20 bps our margin.

Consistently, Jean-Pascal, you said it, I think that's a very important word for us, we want to be very, very consistent in what we do, consistent, of course, on the top-line growth. We said it. We are a GDP-plus company. We can grow between 3% and 6% organically through the economic cycle. If you look at the last three years, we're at 3%, actually north of 3% without taking the selectivity impact on Medium Voltage. We want to grow very nicely the top line and, at the same time, we want to grow the margin. And look at the margin expansion, 70 bps on average and quite dynamic over the last three years.

And what is interesting to note is that we managed to grow the margin in year even in – like in 2016 where sales were going down, like in year where sales are more dynamic. So, we are also able to grow the margin when we are not growing the top line. And all that translating into a CAGR of our adjusted EBITA organic growth of 8% over the last three years, quite clearly a nice dynamism for our profits.

Let's move to the bottom of our P&L, other income and expenses, negative €103 million. The vast majority of that is coming from our cost of doing M&A, acquisition, working on disposal, cost of integration. And then, you have a much smaller part which is coming from some impairment on asset, and notably something that we flagged on R&D that was capitalized coming from the Schneider Software business and the merger of AVEVA made this R&D irrelevant. So, that was impaired.

Restructuring cost, we mentioned that we were targeting to be between €150 million and €200 million for 2018. We finished within that bracket. It is clear that as we keep shaping Schneider to be a dynamic high-performing company for the future, we'll keep investing on restructuring. And for 2019, we think we're going to stay around this level of about €200 million of restructuring.

Amortization, depreciation of intangible, here this is just the natural impact coming from the acquisition. So, AVEVA and ASCO have some intangible and we are amortizing these intangibles so that's the growth here. That give an EBIT of €3.4 billion, it's plus 6%. Then the financial cost, very nice news. We are decreasing, as you can see, very nicely the cost from the debt and that translates into a €57 million reduction of the charge of financial cost. Income tax, we keep delivering a low effective tax rate for the group, 22.5%, that was 21.1% last year. We are still working in this range of 22% to 24% of effective tax rate for the group.

Discontinued operations, these are the Solar business and you have a mix here of some capital gains that we made on selling the mobile inverter business and still the loss of the year on Solar, plus a few depreciation of asset. We are focusing the Solar business for the future on the commercial and industrial building.

Equity investment and minority, let's not get confused by the fact that it's turning negative. That's actually good news, because it's turning negative because of the very nice profitability of AVEVA and we own 60%, so 40% of the net profit is given back to this line, to the minority shareholder. The other big element on that line is a profit that we make with Delixi. And this profit has been reaching €50 million of net income and it's a 20%-plus increase for the year. So, Delixi keeps growing very well. That gives a net income of €2.334 billion. It's a plus 9%. Adjusted net income, without the non-recurring element, is €2.560 billion, plus 8%. And adjusted earnings per share is €4.62, plus 8%, actually because of the buyback here, it's rounding, but this is growing faster than, of course, the adjusted net income.

On the cash flow, so yes, the free cash flow is slightly down at €2.1 billion. We had flagged the fact that we were expecting the working capital to be negative because of the growth. Actually, it's probably more negative than what we thought at the beginning of the year because of the tension on the supply chain, the risk of shortages and making sure that we build some inventory of cautiousness, I would say. So, it's almost €300 million negative coming just by increasing inventory. That's something that's going to be reversed and certainly we have a possibility to be back to a much more favorable contributions from working capital, both on trade and non-trade.

And the good news here is that, for me, we've been making a step progress here on the operating cash flow, net of CapEx, north of €2.6 billion, growing 13%. It just show that before the working capital impact, which is a one-off, we are growing very significantly our capacity to generate cash in the future. So, that bodes very well for the coming years.

Dividend, €1.3 billion; acquisition, you know them, of course, mainly AVEVA. The net capital increase here is, of course, the buyback. And FX and other, it's first and foremost the impact of the Forex on our U.S. dollar debt and also some contribution to pension. We finished the year with a net debt at €5.1 billion, and we retain, as you can see, first, a very strong conversion rate of our net profit into free cash flow, 90%. But we are still, if you look at the last four years, nicely north of 100%. And the net-debt-to-adjusted-EBITDA ratio remain extremely strong. We keep navigating at between 1 time and 1.1 time, so a very, very strong balance sheet.

We keep improving the quality of our business, first, organically, when it comes to Medium Voltage that, of course, a key technology that we own and we wanted, as you all know very well, to improve its contribution, its profitability, its quality. That's what we've been doing with the 400 basis point organic improvement over the last three years. And we do that, of course, as well inorganically, pruning the portfolio for businesses which are not synergistic, lower performer, and who is very often a lower profitability. And what we are signaling here is that very clearly, we are going to further accelerate on that.

We have the ambition to put €1.5 billion to €2 billion of revenue under review. That compared to €0.5 already announced in Medium Voltage. Here, €1.5 billion to €2 billion are across businesses and across technology, to be very clear. And the plan here is to partner or maybe to dispose some of this business, but certainly to make sure that we are focusing further on the best part of our business, the core part and the synergistic part with the highest future and profitability.

M&A, of course, we receive very often a lot of question on the M&A part. I think we can be very pleased with the M&A that we announced recently, ASCO going very nicely. AVEVA, we don't need to comment, AVEVA has been issuing a press release. The company is still growing very, very nicely. And IGE+XAO, it's smaller, but I can tell you it's a very nice start and it bodes very well for the future. So, we are very pleased with the acquisition that we have been doing.

And we've been very consistent, once again, on returning cash to shareholder and maximizing the return. Look, since 2014, 80% of the cash flow that we've been generating has been returned to shareholder through dividend and share buyback. We finished the share buyback, the €1 billion, in advance and ahead of schedule. We are announcing a new share buyback, €1.5 billion to €2 billion over the next three years, so 2019 to 2021 period.

On M&A, nothing has changed on our policy. It's a disciplined approach. We don't need to do M&A. If we do M&A, like the few acquisition I mentioned, it would be on the core, to further improve the quality of the business. And the acquisition are going to be focused on bolt-on. What I think is very interesting and show the quality of the performance is that despite the ASCO and AVEVA acquisition that, of course, has been increasing the capital employed, we managed, before Forex, to improve the return on capital employed in 2018 by 40 bps, which show that we are both able to keep making some bolt-on investment for the future and, at the same time, improving the return on capital employed.

In the very same order of ID, we of course want to keep growing nicely the dividend, and we're going to propose to our shareholder a dividend of €2.35. It's a growth of 7% reflecting the performance of the year. And if you look back to the last five years, the CAGR, the average growth rate of the dividend, has been north of 5%. So, we've been very consistent in growing the dividend year-after-year, in line with the performance.

That's it for the finance presentation. Jean-Pascal, back to you for outlook.

Jean-Pascal Tricoire

Chairman & Chief Executive Officer, Schneider Electric SE

Thank you, Emmanuel. So, I'd like to try to take two horizons as we look to the future. The first one is [indiscernible] (49:49) which we do traditionally at Schneider, not everybody does it. While we expect the following trends, the first thing is that China is clearly facing a very high base of comparison after such a fantastic 2018. We see a softening OEM demand in China and that's coming from the uncertainties arising from the trade war. Every kind of industrial decision is more uncertain. But at the same time, we still see a lot of dynamism in markets of construction, infrastructure, on other parts of industry, and the industries we're looking for more efficiency, reducing the carbon impact, reducing the pollution, getting better on automating.

So, that's for China. North America, we still see a continuing favorable environment. We've got an exceptional presence in North America between technology, construction, industry. All of this is delivering on full cylinders and on all cylinders, and Q4 was good. Large countries in Asia Pac, we are positive that we'll continue good momentum. On West Europe, we'll keep growing at a more moderate pace, but the Rest of the World economies are contrasted, but there are some good news, I think the price of oil is better than what it used to be in the past as well as the price of resources.

So, all in all, when we put all of that together, and benefiting from that balance of exposure in terms of geographies and in terms of segments, we target in 2019 an EBITA growth in absolute value between 4% and 7%, very well in line with what we had declared three years ago in 2016. This would be achieved with a combination of a growth between 3% to 5% and an adjusted EBITA margin between 20 bps to 50 bps in terms of organic improvement.

And we think, because of the base of comparison on a certain number of other elements that it would be more pronounced in the second part of the year. We're going to – some elements also to integrate is that there are some day impacts as we speak about Q1, especially in China, but we're going to every time correct the impact of that so that you have a clear vision of what is happening.

Now, if I take a little bit more distance, I try to project ourselves in the next coming three years. Look, I'm quite optimist and the reason is the first thing that the world is coming to our direction. You see a clear acceleration of electricity everywhere. So, the world is becoming more electric. IT is one of the major drivers. It's where we have a very strong position.

Mobility is moving to electric, if you can say that of mobility, but it's clearly going electric and it's just the start of it. And then when you see, the world is also getting electric in the field of temperature control, in buildings, in residential. You don't always see that in old Europe, which tends to be more conventional and conservative, but in the Rest of the World between HVAC heat pump, the only way to decarbonize energy is to get electric and you save a lot of infrastructure, because you can use your plug and your electricity. So, you see a very strong push of electricity. More – big correlation between electricity and the total consumption of energy. So one, the world is more electric. No need to tell you that the world is getting much more digital, right? And we see exponential acceleration and there, again, we are well positioned.

On third point, the world is getting more decentralized. Remember, the good old times of the energy chain, where people were on the upstream and then there was transmission, distribution, and management of energy efficiency will position the all of Schneider on distribution and energy efficiency, and decentralized generation. And this is where the world is coming full speed.

The second point is that somewhere our environment is distracted, because we have many people in our environment which are restructuring, splitting, selling and things, and we have the right perimeter. Well, of course, we're going to trim our portfolio to the magnitude of €1.5 billion to €2 billion, but this is something we can do by small blocks. We're already on the way to do. We are not speaking about major restructuring. We have the right organization. We believe in empowerment of our country organization that speak the language, that develop the right policies that are adapted to the local characteristics of the market, and in a world which is still very global, but where the nationalism are expressing stronger claims. The fact that we are country-based at Schneider is a great asset for our future.

So, Schneider is a stable company with a stable portfolio, with a stable organization, and we are just focused on our customers, on our operational efficiency. So based on that, when we look at the future, we confirm our objective to be growing from 3% to 6%, [ph] in organic (00:55:11), as we go through a cycle. And we really want to go – I think 10 years ago, I told you that the potential of Schneider is to be from – to have an operating result between 13% to 17%. It's time to go to the upper side of the bracket.

So, we ambition to add 200 bps of profitability by working on organic growth, as we say, benefiting from the fact that we are positioned, that the organizations are well oiled and they know how to cross-sell and bring solutions together; working on the portfolio optimization, €1.5 billion to €2 billion, that we mentioned; working on the simplification of organization, on building energy and management as one is a great asset for that, because we're going to take some silos out from what we had created in the past; and working on our continued productivity on the basis of our unique and integrated supply chain.

So, this is where we want to go. And if I want to summarize, what we tell you is that – and this has been very consistent for the past 15 years – is we are committed to offer our customers digital solutions for efficiency and sustainability. At the time, those two are very strong on the agenda of our customers. Our strategy is to have more products, more services, more software, and better systems. We are benefiting from a very balanced exposure in terms of geography, in terms of end markets and in terms of positioning the cycle. We've based our growth on the energy transition and Industry 4.0, which are the two major transition of the fourth industrial revolution, and we integrate those two into one, into packages of efficiency.

We're going to work on our portfolio optimization. We want to increase our margin by 200 bps. And we keep focusing on giving back to our shareholders. They have followed us for 10 years of construction of portfolio. And in the past five years, six years, we have restituted or we are focusing on giving back to our shareholders who've been the loyal partners of the building of the new Schneider.

So, that's where we are. And that concludes the conference. I just want to mention that on 26 of June, we'll organize a Capital Markets Day in Paris and you're all welcome to participate. Amit.

Amit Bhalla

Senior Vice President & Head-Investor Relations, Schneider Electric SE

All right. Thank you very much. I think we move to Q&A. We'll try to make sure we take as many questions, all the questions. Of course, we start from the room here for the folks who are in the room. We keep it to one question for analyst and then we come back. So, maybe we start with Gaël.

QUESTION AND ANSWER SECTION

Gaël De Bray

Analyst, Deutsche Bank AG (France)

Q

Thank you. Good morning, everybody. So, the question I have relate to the margin ambition you have, the plus 200 bps. This would, obviously, take the margin to 17%, which is roughly 100 bps above and probably the highest margin ever achieved by the company in the past, and I think that was in 2007, so quite a long time ago. So, what gives you confidence now that you will deliver a better margin improvement, let's say, than in the past? And what will be the real drivers behind? If you could, well, break it down between productivity, organic growth, the effect of portfolio optimization, and all that sort of things, that'd be great. And – well, in relation to that, but more near term for 2019, do you take into consideration a positive effect from IFRS 16?

Jean-Pascal Tricoire

Chairman & Chief Executive Officer, Schneider Electric SE

A

All right. I think I just went through – Gaël, I just went through somewhat an explanation of how we would do it, right. And I don't intend to break it position by position. But if you look at – you are referring to 2007, where we're just a product company and a very different size at that time. In the meantime, we wanted to build the portfolios that was much more on digitalization, making sure which today everything we do in the environment of IoT, connected products, edge controls, digital services is now 45% of our business. So, we've reached now a different size.

During the past 10 years, it was a learning curve and it was a building curve where we had to build not only digital capabilities, we had to build EcoStruxure that was in V1 launched in 2008, but which has been developing in the past 10 years. When you go into digital in the field of industry and building, and what we do, you have to build solution capabilities and that was a tough learning, right.

And we learnt and we took the bruise of learning that, but now we feel very confident that we found the right monetization model. EcoStruxure is built to a larger extent, we are keeping on working on it. We are investing every year more on digital. But this is based on the strong momentum. We've developed new business, like services, which there again you have to learn and you have to invest. But if you look at why we are now in a good position to achieve the ambition that we had declared from the inception of the plan is because we have the foundation and it's done. We have the momentum and it's proven again in 2018. We're going to work partly on it through the portfolio, refocusing on the places that are the most value accretive and the most strategic for us and keeping on rolling out or scaling up as initiatives that we have now well started. I mean, it's not like designing new things like we were doing five or six years ago. We are truly learning, but it's now scaling up things that are well-proven.

On working on efficiency, I mean building the portfolio was – every time you divest, that you acquire, [ph] I'm saying, (01:01:35) is very disruptive. And I see many of our competitors doing that at the moment. We are now in a position where we [ph] said in 2013 (01:01:42) we have the portfolio, now integrate and we are now in a position to have that strategic position, which is integrated and stable that we can really deploy our strategy with a lot of serenity and with a lot of focus.

Emmanuel Babeau
Deputy Chief Executive Officer in charge of Finance and Legal Affairs, Schneider Electric SE
A

Okay. Just to complement what Jean-Pascal has been saying, we're very clear on the fact that we're going to use all levers to generate this 200 basis point improvement. Now, I guess, the question is how do you split that between what can be organic and inorganic. And the only thing I can share with you is that I expect organic to be a majority contributor to the improvement, acknowledging that certainly when we look at the €1.5 billion to €2 billion of sales that we're going to put under review, there exit of the Schneider perimeter should have an accretive value on the margin. But the majority of the 200 basis point will come from organic improvement.

Regarding your question on IFRS 15, no, for us on the P&L, IFRS 15 is about neutral. So, no impact, whether positive or negative, coming from that in the guidance.

Amit Bhalla
Senior Vice President & Head-Investor Relations, Schneider Electric SE
A

Andreas?

Andreas Willi
Analyst, JPMorgan Securities Plc
Q

Thank you. Andreas Willi from JPMorgan. I've a question on Secure Power, data center where you've shown basically that Secure Power reaccelerated a bit in 2018. If we look at the comments from some IT companies that sell the servers or also from some of the Internet giants, they expect a weaker 2019 compared to some of the very high growth they had in 2018 in spending. Maybe you could just give a little bit more information what you expect there also for the Secure Power division? Can it maintain the positive growth if we see in the – maybe the large data center space a bit of a slowdown in 2019? And what are the things that could help on the other side in terms of growth?

Jean-Pascal Tricoire
Chairman & Chief Executive Officer, Schneider Electric SE

A

Yeah. That's, of course, a very good question. Look, we started the year with a good backlog on that space. But what I want to emphasize is that it's not only about large data centers, it's – we do a lot in distributed IT. And what we've seen after a period which was a lot about cloudification of the IT that the more people go on the cloud, the more they have now to reinvest on the Edge to get the right latency and to get the right storage of data on computing on spot. And you see that not only in the pure IT sector, but you see that in manufacturing. The more we do IoT, the more you need the decentralized data centers. And the more you do retail, for instance, the more you need locally or local data center to secure the process in case there is an interruption of communication.

So, what we've seen in 2018 is a redevelopment somewhere of the Edge Computing, which has been a great news, because it is a sweet spot of what we do in Secure Power. So, we see, as we go into 2019, a balance of those two, decentralized or what we call distributed IT. We see more Secure Power going into each and every of our application, including industrial application. When you set up more automation in machines and plants, you need to secure the power for that very sensitive and mission-critical application. And we see still a large development of big data storage with massive plans of deployment that we are addressing. We have to address issues of mix, so we're going to give you visibility on the impact of those larger projects on the mix of what we do.

Amit Bhalla
Senior Vice President & Head-Investor Relations, Schneider Electric SE

A

Alasdair?

Alasdair Leslie
Analyst, Société Générale SA (UK)

Q

Thank you. Good morning. And I was wondering if you just could elaborate a little bit more on pricing turning positive in China. That's quite a change as you noted. I was just wondering how sustainable that really was, in terms of – is it just a high point in terms of the cycle or are you seeing a change in competitive dynamics there?

And then, more broadly on pricing, Emmanuel, I think you said at the Q3 stage, obviously, pricing was a priority, but you were thinking more from a strategic perspective as well, perhaps, not just kind of a reactionary price. And so, I was wondering is there an opportunity now to kind of price up through 2019 to get more of a kind of benefit for some of the values you're delivering to the customers in areas like software and digitalization? Thank you.

Jean-Pascal Tricoire
Chairman & Chief Executive Officer, Schneider Electric SE

A

Okay. So, speaking about what we do in Asia, I mean, our Asia is not only China, to start with. But if we look at China, of course, we are starting with a high base of comparison where – at the end of 2018. But I mean, we've kept investing in new business in China. The first thing is that China, as everybody knows, is a very large country. So, we keep on – the base of the strong infrastructure we have there, on the very local capacity of servicing the whole country, we keep expanding our geographical position. And it's – like, China is many countries, if you will. I mean, each province has the size of something that could be qualified as a country, in many places. And even if we've been there for the past 30 years and we have a pretty deep penetration of market, there are still plenty of towns that would qualify as large towns in Europe or in anywhere in the world where there is still a lot of potential to tackle.

The more local we get, the more R&D we do locally, the more we develop local products which are well-adapted to those more local places in China. So, that's one of the first vehicles for us to keep growing and development in China.

Second point, China is becoming a normal country where people are asking for services. This is something we have barely scratched. In the past, we are too busy building China that we had forgotten serve in China or service in China. So, that's another one which is important.

And the third one is digitization. It's not called the same name as before, but all of China is working on more efficiency to de-pollute the cities, to make factories more competitive, and we see there again very sustained movement of equipment, of investment and collaboration. So, we recognize that there will be probably some weakening or some doubts in some part of industrial investment due to the tariffs and present discussions, you never know what would be open to factor in China in the future. But globally, there are plenty of things, which are local. One tend to forget that it's also a very big domestic market with huge needs. The other thing is that when you think about it, if the trade war is going in the wrong direction, then it will drive China to localize more technology, therefore, to build more capabilities by themselves.

On one side, either they keep exporting or they keep building for – or they start building seriously for vertical integration in China. And on both sides, we are ready to react and ready to support.

Emmanuel Babeau
Deputy Chief Executive Officer in charge of Finance and Legal Affairs, Schneider Electric SE

A

I'll take the one on pricing. And I could not agree more. I think that, of course, for making our case clear, we took about price increase versus cost. But at the end of the days, price is a more strategic dimension of the business that reflect the added value that you deliver to the customers, the differentiation and whether – because you're coming with something specific, the consumer and the final customer accept to pay a certain price for it.

Everything we do and I think we're very clear is investing, is being innovative ahead of the pack in terms of what we propose to our customer starting with, of course, a unique digital capacity. And you're absolutely right, that should enable us to further increase our pricing power in the future, because we want to deliver something that other cannot deliver or not at the same level.

So, there is always a kind of dimension of anyway I have to cover my cost, but that's just the beginning of the reflection on price and then we have to go beyond that and make sure that we price for the value added that we bring to the customer.

Now, for 2019, we're going to have some carryover impact of the work we've been doing in H2 that has started, as you have seen, to deliver in H2. But of course, there will be some nice impact in 2019. And certainly, not the end of the journey on pricing, as we continue to do on digital services, on software, on EcoStruxure that is coming super differentiated, more added value for the customer and we have to price for that.

Amit Bhalla
Senior Vice President & Head-Investor Relations, Schneider Electric SE

A

Alex?

Alexander Virgo
Analyst, Bank of America Merrill Lynch

Q

Thanks. Alex Virgo, Bank of America. Wondered if you could just talk a little bit about the growth acceleration in North America that you called out. [ph] That was (01:11:17) surprising is how much of that's data center related or maybe just talk broadly about the dynamics that have driven that and how that carries on into 2019? Thank you.

Jean-Pascal Tricoire
Chairman & Chief Executive Officer, Schneider Electric SE

A

No, it's broad-based. Data centers are an important part of it, but they are not the only one. So, we've seen things happening in construction, residential and non-residential construction, lot happening in energy efficiency, by the way, making building grids and infrastructure grid. We have, when we speak about the U.S., very specific case of strong development of micro grids, as the grid is not that resilient as you have multiplication of climate disasters or climate disorders, then customers want to secure their installation. It can be a municipality. It can be a more critical application. So, it's really a place where we are developing with a pretty – well, pretty fast those kind of new capability. And of course, when you do that, it goes coupled with digitization because you have to well coordinate the part of demand and the part of supply.

It's also around industrial software, on automation, because – well, a large part of the base of AVEVA and the base of what we do in Automation, remember, the legendary names of Foxboro and Triconex are based outside of the U.S. where we have a very strong position. It's a sector of energy, which by the way is doing well also in the U.S. And it's the technology of all, where we have a strong position there. And plus, there has been some – there used to be some strong competitor there, which has been bought by others, and that's creating the right space for us to develop and take more share of the market. So, the U.S. has been a continuous progression during the year and is good.

Amit Bhalla
Senior Vice President & Head-Investor Relations, Schneider Electric SE

A

All right. I think maybe we move to the webcast. I'm sure there's some questions there. So, let's take the first one.

Operator: Our first question comes from Ben Uglow from Morgan Stanley. Please go ahead.

Ben Uglow
Analyst, Morgan Stanley & Co. International Plc

Q

Good morning, everyone. Thank you for taking my question. Jean-Pascal and Emmanuel, really I wanted just to think about how you were thinking about the growth guidance, the 3% to 5%. The reason being, obviously, that's a nice number and it's maybe an ambitious number, who knows? But when we look at some of the macro data, it seems to be pointing downward. And so, if I think about GDP numbers coming out of Europe, if I look at industrial production data even in the last few days, they're all going the other way. So, I guess, what I want to know is in terms of how you think about it, do you do you just feel that this is a soft patch? Do you think that you have enough internal momentum that you can still deliver 3% to 5% even if external factors are going against you? How are you thinking in broad terms about the economic trends in 2019?

Emmanuel Babeau
Deputy Chief Executive Officer in charge of Finance and Legal Affairs, Schneider Electric SE

A

Well, Ben, of course, we have been taking what we think are reasonable assumption on the global economic environment. And we'll see whether they prove to be right or wrong in the future. But our ambition for growth guidance is not just built on the economic environment. We are coming and we are entering 2019 with a very nice backlog that we have been building. So, we know that some of this backlog is going to be flushed in 2019. We have highlighted it, ambition on increasing price. So, that's also a contributor to the top-line growth. We have the ambition, we're not going to surprise you, to gain market share. So, that's also contributing to the growth. So, that mean that beyond the economic environment, again, on which we think we have taken, at that stage, the best possible view and reasonable view, you have some driver that would, I would say, are self-helped or coming from what we've been doing until now and that explain the guidance that we've been giving.

Jean-Pascal Tricoire
Chairman & Chief Executive Officer, Schneider Electric SE

A

And you spoke about Europe but it's our [ph] served (01:15:49) zone today.

Ben Uglow
Analyst, Morgan Stanley & Co. International Plc

Q

And just generally, you're not seeing that weakness, obviously, in your business, right?

Emmanuel Babeau
Deputy Chief Executive Officer in charge of Finance and Legal Affairs, Schneider Electric SE

A

Well, look at our Q4. I mean, Europe especially had its best quarter for the full 2018. So, that's clearly not something that we've seen in 2018 and certainly not at the end of the year. Now, what's going to be the full 2019? Again, I think we've been taking assumption in line with the most recent available information. We'll see what the final outcome of that is for Europe, but as Jean-Pascal said, Europe is one zone among others.

Ben Uglow
Analyst, Morgan Stanley & Co. International Plc

Q

Very helpful. Thank you.

Jean-Pascal Tricoire
Chairman & Chief Executive Officer, Schneider Electric SE

A

And we'll keep pushing on services, on digital, on the enlargement of our coverage of partners. It's all about us delivering or scaling up or deploying our strategy.

Ben Uglow
Analyst, Morgan Stanley & Co. International Plc

Q

That's very helpful. Thank you.

Amit Bhalla
Senior Vice President & Head-Investor Relations, Schneider Electric SE

A

Thank you, Ben. Next question, please.

Operator: Thank you. [Operator Instructions] Our next question comes from James Moore from Redburn. Please go ahead.

James Moore
Analyst, Redburn (Europe) Ltd.

Q

Yes. Good morning, everyone. Thanks for taking my questions. They're on price and inflation. So, obviously, a very impressive acceleration in gross pricing in the second half to a point of gross pricing and the positive net. Could you help us a little bit with what the momentum will be into the first half or the full year of 2019? Do you think you can maintain that degree of gross pricing into the first half of 2019? Can you talk a little bit about the raw material and also wage inflation and what your net pricing ambition is for the year?

Emmanuel Babeau
Deputy Chief Executive Officer in charge of Finance and Legal Affairs, Schneider Electric SE

A

Yes, James, I can try. I think we've been talking a lot about price. Obviously, as we said, it's a big priority to increase price, not just to offset cost, but just to reflect the value that we deliver to the customer. As I said, I expect a positive carryover coming from the action taken in 2018 in 2019. I won't elaborate more on that one. We certainly expect to have more price action in 2019 to reflect the global environment where inflation has not disappeared, but even more so, as we said, the fact that we keep increasing the value proposition for our customers.

So, I'm not going to be more specific. I would expect price to perform well and deliver nice contribution to the top line through the year. I'm not going to phase that between H1 and H2. For the raw material impact, I think that H1 is still going to be, probably, let's say, neutral plus in term of cost, I think, I still expect a little bit of raw material inflation in H1 based on the current copper price, for instance, which has been accelerating a little bit.

Now, we'll see in H2 – I think, at that stage, I want to be cautious on what's going to be potentially the impact in H2. We could have a bit more positive raw material inflation contribution in H2, but that remains to be confirmed. So, I'm going to stay, at that stage, more cautious. But having said that, of course, after a €200 million negative impact on raw material inflation in 2018, we don't expect to have such a negative amount in 2019 and we remain ambitious on price. So, the net differential should be, altogether, better in 2019. But I guess, you had come by yourself at this natural conclusion.

James Moore
Analyst, Redburn (Europe) Ltd.

Q

And if I could just follow up to the earlier question on the portfolio, the €2 billion. Are you able to quantify the margin? Obviously, less than the group, but is it 12% or 5%?

Emmanuel Babeau
Deputy Chief Executive Officer in charge of Finance and Legal Affairs, Schneider Electric SE

A

No, I'm not because...

Jean-Pascal Tricoire
Chairman & Chief Executive Officer, Schneider Electric SE

A

Yes, we are, but we are not communicating on it, James.

Emmanuel Babeau
Deputy Chief Executive Officer in charge of Finance and Legal Affairs, Schneider Electric SE

A

And I mean, the fact that we are giving a bracket mean that we are still, of course, working on the perimeter. And the only thing we can say is, yes, of course, it's going to be, on average, accretive for the group. And what I also said, and I'm happy to repeat, is that, nevertheless, the majority of the 200 basis point improvement will come from organic. And therefore, that mean that this work that we're going to do on the portfolio will bring less than 50% of the global improvement of the margin that we are ambitioning.

James Moore
Analyst, Redburn (Europe) Ltd.

Q

Yes, I heard that. Thank you very much.

Emmanuel Babeau
Deputy Chief Executive Officer in charge of Finance and Legal Affairs, Schneider Electric SE

A

Thank you.

Amit Bhalla
Senior Vice President & Head-Investor Relations, Schneider Electric SE

A

Thank you, James. Let's take one more from the – one or two more, obviously. Yeah. Next question, please?

Operator: Our next question comes from Simon Toennessen from Berenberg. Please go ahead.

Simon Toennessen
Analyst, Joh. Berenberg, Gossler & Co. KG (United Kingdom)

Q

Yeah. Good morning, everyone. I've got a more of a big-picture question on your growth performance, which, over the past six quarters or so, has clearly been above where some of your peers are and you clearly seems to have gained share. I face a lot of investors who always ask how sustainable that is going forward. Obviously, you've given guidance today. But I've got more of a question related to the Capital Markets Day, I think, back in 2016, which you did in Paris, I believe, where you talked a lot about cross-selling and cost sharing and the likes, and I think neutralizing front office across your divisions on the country level, et cetera.

So, if you look at your growth profile the past six quarters or so and if you dissect kind of where the growth has been coming from, except obviously the underlying market growth, could you share a bit more light into how this cross-selling initiatives amongst your portfolio has really driven this? Obviously, EcoStruxure plays a crucial role in this, too. But from the outside, it's sometimes difficult to grasp how cross-selling internally actually works. And I think people understand how your divisions are related to one another, how you're selling Low Voltage also into data centers, et cetera. But if you can share a bit more light how this actually has been succeeding internally and whether you think there's more potential to drive this going forward or whether you've got this pretty much set up today. Thank you.

Jean-Pascal Tricoire
Chairman & Chief Executive Officer, Schneider Electric SE

A

Well, it's fundamental for Schneider. I mean, the whole strategy that we have is to have an integrated portfolio, which is addressing the whole equation of efficiency with the ultimate goal of sustainability. And for that, it's always about energy efficiency coupled with process efficiency. And I've said it many, many times that you can't disconnect the two. I mean, if you want to tackle the energy equation, you've got to tackle the process. And if you want to deal with the process, you need to get the right energy to service it. So, the two are getting very intertwined. And the more energy decentralize, the more this is getting connected together. If I try to summarize, I would say, first point, we never sell by product, zero. We always sell by customer. And therefore, the customer is looking for a simple life, for a speedy reaction. And the more you can come with something, which is bundled and put together, the better they are, because nobody has time to lose in the world of today.

And it's true when you buy, but it's also true when you service an installation. For anybody installing anything in a remote place, you want to have solid partner that will help you when things are happening. So, our cross-selling is happening in two manners. It's happening at the level of our channel and integrators, like we come with a complete catalogue, which is plug-and-play and which is proven to be plug-and-play. And this is where one person can sell more and more of the offer. That's one kind of cross-selling.

The second cross-selling is when you come in front of a segment and application, which is now more and more integrated around EcoStruxure, EcoStruxure being the digital part of it, where you – it was very difficult before to integrate that whole equation of efficiency, and EcoStruxure makes it really on the shelf, plug-and-play, easy to implement, and easy to put together. The biggest examples, we have that, I would take one example that jumps to my mind, the Zohr, which is one of the oil-and-gas field in Mediterranean, where the customer cut the time to first gas by half, 5 to 2.5 years, and you can imagine how much money it is by coming with an integrated solution of energy and automation.

So, those are the two cross-sellings that we've put together, the one by channel and integrator, which means that you can really leverage your sales force on a much larger scale on the larger revenue and that's applicable to everything. And the other one is the capacity to deal with integrated solution. And another example, which is obvious, is data center. The reason why we develop very fast and gained very strong position in data center is our unique capability to put together the whole powertrain from the grid to the server with whole system of monitoring, which is now hosted on the cloud and gives to our customers the complete capacity of supervision. So, those are the two things I would mention.

The third point, frankly, is that I've never thought or I've never seen that the world would be completely global. I think the world is multi-local. And today, you have the resurgence of national characteristics, which we always saw as part of our strategy. And the fact that we had very strong local presence in all aspects; R&D, sales, delivery, execution centers, makes that we can stick to the local characteristics of the market. The fact that the leaders are spread out on the field makes that we can make very fast decision, including on cross-selling. And that's a tremendous asset as we go into a more complicated world that we see developing today.

Simon Toennessen
Analyst, Joh. Berenberg, Gossler & Co. KG (United Kingdom)

Q

Thanks very much.

Amit Bhalla
Senior Vice President & Head-Investor Relations, Schneider Electric SE

A

Thanks, Simon. Next question, please? Yeah.

Operator: Our next question comes from Wasi Rizvi from RBC Capital Markets. Please go ahead.

Wasi Rizvi
Analyst, RBC Capital Markets

Q

Yeah. Hi. Good morning. Thanks for taking my questions. Just a few left for me, if I could. Just firstly, could you help us think about the shape of growth through the year? I know you don't explicitly guide on this, but you've talked about China having a high base of comparison, particularly at the start of the year. And you also mentioned something about days effect. So, I was wondering if you could expand on. And then, my second question was just a follow-up to the earlier question really, understanding new structure. And are any actual organizational changes required for the new organizational structure or is it simply a change in the way the numbers are reported and actually everything continues as it always has been?

Jean-Pascal Tricoire
Chairman & Chief Executive Officer, Schneider Electric SE

A

I'm going to take the second one. Of course, one of the reasons also is that we have simplified our organization from the point of view; first, organization is simple. P&L are integrated at the level of the regions, the level of, we call them, the operations, so integrating Schneider solution by zones. But we have now two big business, Energy Management and Industrial Automation, which are able to put together even more synergies in there. And then, those two divisions are organizing a case by case project by project to make sure that we integrate Energy and Automation together.

So yes, there has been one further integration that means today Secure Power, Medium Voltage and Low Voltage are part of one large organization of Energy Management.

Emmanuel Babeau
Deputy Chief Executive Officer in charge of Finance and Legal Affairs, Schneider Electric SE

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On trying to help you with the phasing. I think we flagged in the presentation that you have about 1% negative impact coming from working days both I think in Q1 and for the full H1. So, that's going to impact Q1 and H1. And that will be fully compensated in H2. So, for the year, I don't think we expect a net impact. Actually, there's going to be a drag in H1 and that's going to be a booster in H2 for the growth. True, we have particularly high comps in the China growth last year for a number of reason that makes the H1 more demeaning in term of comp for China. So, that will have an impact on the growth for China, H1 versus H2, that's for sure.

And globally, what we are signaling is that in the ambition for the margin improvement, it is possible that H2 will be a bigger contributor to the margin improvement, because of the working day impact that I've been flagging, because of the phasing of some investment that could be more skewed toward H1 than H2, and also because of work that we are doing on the supply chain and recovering from all the tension will probably still be ongoing in H1. And therefore, H2 could be more positive in that respect for all those reason. We see today that possible phasing for our performance between H1 and H2. I hope it's helpful.

Amit Bhalla
Senior Vice President & Head-Investor Relations, Schneider Electric SE

A

All right.

Wasi Rizvi
Analyst, RBC Capital Markets

Q

Thanks. That helps.

Amit Bhalla
Senior Vice President & Head-Investor Relations, Schneider Electric SE

A

I think we're coming towards the close. I just want to give one opportunity further in the room, if there are any more questions even if it's a repeat question? Okay. Gaël, go for it.

Gaël De Bray
Analyst, Deutsche Bank AG (France)

Q

Yes. How are you thinking about the corporate costs, the central functions cost that have actually increased now gradually for the past few years and at 2.8% of sales that seems to be a pretty big number to me? And it seems to be going in the opposite direction of what some of your peers have been talking about recently in terms of reallocating more of the support function expenses directly into the business units.

Jean-Pascal Tricoire
Chairman & Chief Executive Officer, Schneider Electric SE

A

That's a very good question and I thank you for asking it because it allow us to clarify the thing. I don't want to have fake reallocation of costs. So, there are two things which are growing in our corporate costs. It's our common IT and digital platform. And it's a strength of Schneider. I don't believe that EcoStruxure can spread into each vertical, because our customers want a complete integration of the tool – all of that integration. And this, we could, of course, do like others. I mean, we could push that into the business, but that would be a fake kind of things. We are really developing common – for the common platform of EcoStruxure.

On the second one, our Innovation Summit, which are common marketing investment where the all of Schneider is coming together to present our solutions for full machine, full segment. And this one, we don't split it artificially. So that's it. For the rest, frankly, I've been long time in this industry, we can certainly do better, but I think we're pretty lean now in terms of – that probably looks out on our face because sometimes we are pretty tired. But I don't think we are a big corporate organization at all, at all. And the fact that we have put the corporate inside our normal operations makes that we are kept under tight control of our [ph] leanness (01:31:49) by our operations, right?

Emmanuel Babeau
Deputy Chief Executive Officer in charge of Finance and Legal Affairs, Schneider Electric SE

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So, clearly, corporate cost is an [ph] unproper (01:31:53) qualification. These are much more digital, transversal cost that we decide not to allocate. And that's a place where we are investing for the future, but for the benefit of our two businesses, to be clear.

Amit Bhalla
Senior Vice President & Head-Investor Relations, Schneider Electric SE

All right. Just to check if there's any other question online. No? So, I guess, with that, I just want to thank everyone for the time today. Of course, we are getting into the road show conference schedule, which is there. So, we look forward to seeing you shortly.

The IR team, of course, is available for calls, meetings, starting immediately after this meeting. So, thank you very much.

Emmanuel Babeau
Deputy Chief Executive Officer in charge of Finance and Legal Affairs, Schneider Electric SE

Thank you.

Jean-Pascal Tricoire
Chairman & Chief Executive Officer, Schneider Electric SE

Thank you.