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Q4 2019 Valmet Oyj Earnings Call

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PRESENTATION

Pekka Rouhiainen ***Valmet Oyj - Director of IR***

All right, ladies and gentlemen, welcome to Valmet's Q4 2019 Result Publication, Webcast. My name is Pekka Rouhiainen, And I'm the Head of Investor Relations here at Valmet; and with me today are President and CEO, Pasi Laine; as well as CFO, Kari Saarinen.

We will today discuss our financial year

2019 results as well as the Q4 results and also go to the new financial targets that were published earlier today as well. And after the presentations, you will have the chance to ask questions here at Keilasatama, over the phone lines. But without further ado, Pasi, please go ahead.

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

Okay. Thank you, Pekka. So our title today is orders received increased to EUR 4 billion and comparable EBITA to EUR 360 million in 2019. So my agenda and Kari's agenda today is that, first, I'll go through the numbers in brief, 2019 numbers, then couple words about the development of business lines. Then Kari goes through the financial development, then I'll come back to continue with dividend proposal, guide and short-term market outlook and the financial targets.

So first, 2019 in brief. So our orders received in stable business increased EUR 1.875 million. So EUR 1,875 billion. And now I'll come back to that later on. Our orders received remained at previous year's level in capital business and totaled EUR 2,168 billion.

Net sales increased to EUR 3,547 billion. Our order backlog increased to EUR 3.3 billion, and comparable EBITA increased EUR 360 million, which corresponds 8.9%, and gearing in the end of the year was 9%.

So all in all, I think all the Valmeteers can be proud of the achievements what we have had during the year. I know that it has taken a lot of work from our teams to achieve these numbers. And of course, we all are happy now that results are, like I usually say, reasonably good. Valmet in 2019, the number. So like I said, orders were almost EUR 4 billion, EUR 14 million missing from EUR 4 billion, but close to EUR 4 billion in any case. Net sales, little bit over EUR 3.5 billion, comparable EBITA, like I said, EUR 316 million. And comparable EBITA margin, 8.9%. Backlog being EUR 3.3 billion, and we employed about 13,600 people. If we look by the business lines. Last year, of course, capital businesses were very strong. This time, Pulp and Energy was the biggest business unit -- from the bigger business unit from the capital business units, and Paper was the second, but Paper was also big.

The Services correspond to 37 points of order intake and Automation to 9% of the order intake. Geographically, Europe continued to gain -- to be strong, 42%, and like we have been saying, as an average, it has been 40% of our order intake. North America was strong, 22%, and South America was strong 17%. And Asia Pacific had good development as well, ended up on 12%, and China, 7%, and that's the lowest order intake in China for many years, better not to say for how many, but for many years.

And I'll come maybe back to that with couple of sentences later on.

Then if we look how Valmet has been developing in last 6 years. So our orders received in 2013 was little bit over EUR 2 billion, and one has to remember that it was the bottom of all the years. So early years '12 and '13 -- were '12 and '11 were better. And since then, we have been growing the acquisition, the orders received by organic growth and by acquisition, and now we ended up to EUR 4 billion. And of course, that's nice development.

Net sales has been growing nicely as well and now ended up at about EUR 3.5 billion. Comparable EBITA has improved year-after-year. Now we started from about EUR 50 million, and now we ended up with EUR 316 million. Every year, we have an improvement in our EBITA euros. And what we are happy also with is that, our comparable EBITA margin has improved every year as well. And now we ended up at 8.9%. So nice development in all these crafts.

Orders received EUR 4 billion, like I said, and the 12 months cumulative curve shows also that it has stayed now about at EUR 4 billion level for 2 quarters. If we look to changes in the areas, that's maybe an interesting one. So here, we see that North America orders grew from EUR 730 million to EUR 880 million. Services was challenging in North America. If I remember correctly, it was declining in euros. And then -- but our capital business was strong, especially in Paper in North America. So North America was good capital market for us last year.

South America grew from EUR 480 million to EUR 670 million. So almost EUR 200 million, and that's of course, due to 2 big projects in Paper and big order in Pulp as well. And Services was developing favorably in South America.

Europe, strong, again, almost EUR 1.7 billion. And then China, went down from EUR 520 million to EUR 267 million. And the reason was the capital markets and Service had challenges as well.

So last year, in capital markets was challenging in China. But like we have been earlier saying, we actually believe that the capital market will be active again in 2020. So we don't see currently problem in Chinese capital market, it's more question of the timing of the orders than the market itself.

And Asia Pacific, Services was developing favorably and both -- and also capital businesses.

This is graph, I like quite a lot. So our stable business has grown to EUR 1,875 billion in order intake. And when we started, our order intake was roughly EUR 1 billion, and now we are almost EUR 1.9 billion. And that's of course, coming from organic growth and acquisitions. And we have set long-term targets to grow our stable business. And up to now, we have been able to do that, both organically and with acquisitions. And of course, this change of about EUR 800 million, EUR 900 million in order intake has changed also Valmet considered up. So that's nice development that we have been able to deliver in 6 years.

Backlog ended up about EUR 3.3 billion. And we say now that about 70% of the backlog is expected to be realized as net sales during 2020. Last year, we had a little bit smaller backlog, if I read correctly, EUR 2,829 billion. And then we said that 75% of that would have been recognized as a revenue in 2019. So which means that if I calculate now correctly, about EUR 200 million big backlog expected net sales realization from the backlog than beginning of last year.

We say now that about 25% of the backlog is coming from the stable business, rest is coming from the capital business, but good and solid backlog.

Then business lines. So Services grew and order intake was EUR 1,459 billion. Organically, our services grew 2%, and the rest came from the acquisitions. So EUR 117 million came from acquisitions. The rest, 2% came from organic growth. And of course, quarter 4 was strong in order intake, and it was 9% higher than a year ago. But I would like to talk more that, that organically, we were able to talk -- to grow it by 2%, which taking into account the market circumstances is a satisfactory result, not a good one, but satisfactory result.

Net sales grew also to almost EUR 1.4 billion. Then if we look by business lines, and these business lines are now calculated, so that the acquired businesses are in those business units where the numbers in 2020 will be reported.

So then it -- this graph is shown that about 1/3 of the orders received is coming from performance parts, 27% from mill improvement, 17% from rolls, 11% from energy and environment and fabrics is corresponding 13%. Geographically, Europe continues to be the biggest area, North America now after the acquisition is almost 30%, and no big changes in the other areas in relation to the total picture.

Then if we look at automation, the automation orders ended up at EUR 416 million. So nice growth compared to last year. Net sales grew as well, almost to EUR 393 million. And all in all, development in automation continued favorably. So we were able to grow the order intake. We brought new products to the markets and cooperation between automation and the rest of Valmet improved. So positive development again in automation in 2019.

About 72% of the order intake came from Pulp and Paper, and 28% from Energy and Process, which is close to average numbers as well, maybe Energy and Process in a normal years is couple percentages higher than last year. And here in geographical area, we see that Europe is still the dominant place, where we have an automation. And then North America, which means then, of course, that we still have a lot of work to grow our Automation business in South America, Asia Pacific and China as well. So of course, if you compare with the total chart for Valmet, this is too much Europe dominated and North American dominated business still. So we still have work to do with Automation.

Pulp and Energy, orders received increased to EUR 1,125 billion, and that's of course not a nice number. And net sales increased to EUR 919 million. This year, Pulp was strong than Energy, and that's what we can see in the next graph that 68% of the orders came from Pulp and 32% came from Energy.

Inside Energy, we have also included our marine scrubber business like they always have been. And last year, the order intake was, it was on the earlier page, but if I remember correctly, EUR 127 million, and that's included in the Energy numbers.

Geographically, South America was strong due to the big order we received into summer time from Brazil, Europe was strong and Asia Pacific improved, China reasonably good, and then North America market was not very active for us last year.

Then if we go to Paper, orders -- order intake exceeded EUR 1 billion, again -- EUR 1.43 billion, and you all remember that last year, exactly a year ago, we said that order intake in paper will not be EUR 1 billion in 2019. So we were saying that the market will slow down in 2019. But we have been successful with winning pick orders in board and paper side, and that has resulted to the very good order intake, which is -- was again over EUR 1 billion. So this was a positive development due to the market activity, but also due to the increased market share, against our main competitor.

Then if you look by business units, we can see that 20% of orders came from tissue. And the tissue was was not as active market than it has been the last 3 years. I think in 3 years, this is the lowest number, what we see in order intake. And that's what we will see later on when we come back to our market outlook that -- the market activity in tissue hasn't been that high in 2019. But like you see from here, board has been very active. So 74% of the orders came from board and paper, corresponding to 6%. So very active packaging machine market last year. Geographically, it's very interesting that only 3% of the orders came from China. This is something none of us remember.

At some years, it was even, so in before the financial crisis, that 80% of the orders came from China. And now it was only 3%. And Europe was strong. North America, you see that big part of our orders came from North America. And that's, of course, positive news to us that North American customers have continued with pre-builds and also by buying new machines for North American markets. That's positive.

And then big news in 2019 was the project we got from Klabin to build big board machine in Brazil, which we announced in -- was it in second quarter or third quarter. And because of that big order, and because of some tissue orders, 20% of order intake came from now from Latin America, South America, and that has been our target to increase -- strategic target to increase our market position in -- or improve our market position in South America and after several years of hard work, we have been successful with. So I'm very happy with that development. So that was the overview. And now Kari goes through the financial development.

Kari Juhani Saarinen ***Valmet Oyj - CFO***

All right. Thanks, Pasi. So good afternoon on my behalf as well. So first, I would like to thank all the Valmeteers who're been working extremely hard now to deliver an excellent closing of the year. And with the world-class quality that is second to none. And then looking at quarter 4 in brief. So stable business orders, they increased 17% during the quarter to EUR 507 million. Our full year increase was 11% for stable business. Stable business, meaning our Services and Automation. Quarter's capital business orders. So Pulp and Energy and Paper business lines, those were EUR 590 million. This is 14% less than what we did year ago.

Full year was plus 4% at capital. Quarter's net sales, they increased EUR 1.1 billion. Stable business increased 10% and capital by 14%. Sales mix for the quarter, that was 47% stable, 53% capital. Last year, we were at 48% stable and 52% in capital. Our order backlog, EUR 3.3 billion, that's 18% higher than year ago. Quarter 4 sales, they were higher than quarter 4 orders by EUR 100 million. So that means that the order backlog actually then reduced about EUR 100 million compared to the end of quarter 3.

Then looking at the key figures here. And looking at the quarter in a bit more detail. So quarter 4 orders much more over EUR 1 billion, same as year ago. Paper business line that increased by 28%. Services increased at the quarter by 21%. Automation was flat, and Pulp and Energy reduced. Services orders received without acquisition, increased by 9% in quarter 4. Out of areas, North American and EMEA increased. Order backlog, 3.3%. So 70% of the backlog will be invoiced during this year. Quarter 4 net sales, EUR 1.1 billion, increased in all business lines, except Paper business line, Pulp and Energy, increase there was 36%. Automation 13% and Services by 10%. Services -- our Paper business line was minus 5%. Services net sales organic. So that was flat for the quarter.

Our comparable EBITA for the quarter, that was EUR 180 million. That's 5% more than year ago. EBITA percent that was 10.7%. So this is the second high -- highest ever with Valmet, but that's actually 0.8% -- points lower than what we did quarter 4 last year, which was the highest ever. Quarter's EBIT, EUR 110 million this is EUR 8 million higher than last year, and quarter's EPS, that was EUR 0.54, that's 10% above last year. And quarter's cash flow, EUR 182 million, that's 35% higher than last year and actually highest quarter's cash flow ever. And then some words on the full year. So full year orders increased by 7% to EUR 4 billion. All business lines, except Paper business line increased, Pulp and Energy, 13%, Services was 11%, and Automation, 9%, Paper was minus 3%. This was now for Paper business line, the third year in a row, where the orders were higher than EUR 1 billion. And Service business orders without acquisitions, 2% increase above previous year. And about areas. So all areas increased except China, where the orders were pretty much half of the previous year, as Pasi already mentioned.

Full year net sales, they also increased 7% to over EUR 3.5 billion. Services increased 13%, our Automation by 12% and Pulp and Energy by 7%. So Paper business line was flat for the year. Services net sales without acquisitions, that was plus 3% last year. Net sales increased in South America and North America, and they were flat at EMEA and decreased in Asia Pacific and China for the year. And then comparable EBITA for the year, that was EUR 360 million or 8.9%. Last year, we did EUR 257 million or 7.7%. So this -- so profitability-wise, this was the best year for Valmet.

Full year earnings per share, EUR 1.35, 33% increase there. Return on capital employed, 23%, and cash flow was EUR 295 million. Gearing, that was minus 9%, good development after the acquisitions that we did during first half of the year. And then looking at gross profit and also SG&A. So quarter's gross profit that was 24%. Last year, we did 25%. The sales split was 47% stable, 53% capital. So I said last year, 48/52. Gross profit percent was lower than last year quarter 4, due to some sales mix effects that we had in Services and also Pulp and Energy business lines. Quarter's absolute SG&A sales increased from last year. SG&As were the same as last year, 15% of net sales. Over 60% of the quarter's SG&A increase actually came from the acquisitions. So we had a very active quarter. And also full year with a lot ongoing. So ERP project, industrial, internet field services and also then R&D costs, they increased by 7% and R&D costs were 2% of net sales. Comparable EBITA, so our rolling 12 months comparable EBITA has now been within 8% to 10% during the 4 consecutive quarters. Quarter's absolute EBITA, that was the highest ever. And quarter's EBITA percent was the second highest ever. Cash flow. So we actually started with cash flow the year with low figures, but then the second half was strong over EUR 300 million second half, quarter 4 and also full year. Those were the highest ever, quarter and also highest full year. Quarter's CapEx is EUR 22 million, full year was EUR 79 million.

Our net working capital, that was around EUR 50 million higher than year ago. A bit less than half of the net working capital increase that is coming out from the acquired businesses. And the rest is coming out of the high business volumes, what we are having now. So the receivables and inventories are a bit higher due to the higher business volumes.

And even though the -- there's some increase in net working capital. So the level was minus 11% of rolling 12 months orders received, which actually is good level. Net debt and gearing. So gearing was minus 9% in the end of the quarter, and net debt was minus EUR 90 million. Impact of IFRS 16, that was EUR 61 million additional debt in the end of the year. Year-ago, our gearing was minus 23%, our net debt was minus EUR 290 million.

During the year, we did 2 acquisitions worth of EUR 160 million. And also paid dividends almost EUR 100 million, EUR 97 million. Those impacting gearing and net debt as well.

And equity to asset ratio, 41%. And then return of capital employed. So comparable return of capital employed that was 23% at the end of the year, year ago, we were at 20%. Our 80% of capital employed is -- was equity. And we have now been over 15% with the capital employed for 2 years, and over 20% for 1 year. So back to you, Pasi.

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

Thank you, Kari. The next one is dividend proposal. So the Board of Director -- first of all, the policies. So the policy is saying that, we should pay at least 50% of the net profit as dividend. And today, our Board of Directors have made a proposal to the Annual General Meeting that we would be paying EUR 0.80 per share. And here, you see how Valmet's dividend per share has been developed from EUR 0.15 last year, it was EUR 0.65, and now we propose EUR 0.15 increase, which would then mean EUR 0.80 a share. And this is, of course, proposal and will be then decided finally in each year.

Then guidance and short-term market outlook. So this year, we state that Valmet's estimates that net sales in 2020 will increase in comparison with 2019. And comparable EBITA in 2020 will increase in comparison with 2019. So both net sales is estimated to be increased, and EBITA is estimated to be increased in 2020.

Short-term market outlook. So we are saying the same than we have been saying now, for a year. So it starts to be a little bit boring. But Services, we still state good. And the reasons are roughly the same. So organically, we're able to grow 2%. And then last year, it was the record year. So it means that, actually, our loading in our Services organization all over the world is good. And like you saw in the recovery of the order intake in latter part of the year, we see -- we see good activity. It's difficult to compare about last year's activity level. But but we see good activity also in Services in the sales front line. And then, of course, one has to remind of 2 things, which are not -- it's difficult to assess the impact.

And one is the coronavirus in China. And we haven't tried to estimate that, if it has an impact and what kind of impact it would have. If it had an impact, then the direct impact would be in China. And you saw that the China Services order intake last year was EUR 120 million. So that's where we would have a direct impact. If the coronavirus situation continues active for a little bit longer time. And then, of course, a small negative situation is now in Finland, where there is a threat -- there is a strike for Pulp and Paper customers. And then, of course, the mills, which are not running, they don't need consumables.

But we hope that these both things are, at least, strike is a very short-term issue and coronavirus is not too long-lasting issue, and that's why we state for coming 6 months, like we say, for the outlook that we see that Services development is still good in 2020 in the first half of the year, long explanation.

Automation order intake has been growing. Market is active. We have all the reasons to continue with the outlook of good. Pulp order intake has been good, like you saw from the numbers, and we have also announced one big order, which will be booked. So market activity continues to be good. In Energy, we still continue to say satisfactory. So year ago, marine was about EUR 190 million -- in '19 it was EUR 127 million. So we estimate that it will continue, maybe not at the level like 2019, but it will still be good a market for us. And then boiler market continues at the level, where it has been, last couple of years.

In Paper and Board, we still say that the market continues to be good for us. Of course, we have good workload, but we still have also active sales cases where -- and that's the reason why we still continue to say good. And this year, we'll continue to have satisfactory. And the market activity in the end of the year improved compared to beginning of the year. But still, like I was saying earlier, order intake was 20% of the pay per order intake, meaning a little bit over EUR 200 billion, and it's the lowest level we have had for many years now. So that's the reason why we continue to keep the tissue outlook as a satisfactory level.

Then financial targets. So many of you analysts have been asking about our financial targets. And now we have new financial targets. So for the growth, we continue to say the same as earlier. So net sales for stable business to grow over 2x the market growth. So the same as early. Net sales for capital business to exceed market growth. So this means that we should increase market share. Our comparable EBITA, we increased the target from 8% to 10% to 10% to 12%. Return on capital employed before taxes, we increased it to 20% -- over 20%, and the earlier one was from 15% to 20%, and dividend policy continues to be the same, dividend payout, at least 50% of the net profit.

Now, what are the tools by which we will improve the profitability. We continue to have the same margin than earlier years as well. But we have our past continuous improvement topics, how to improve our sales efficiency and try to improve the market share, how to improve the technology competitiveness, bring new products to the markets, increase the cost competitiveness of all products, improve our internal processes, like project management or procurement or quality and implement new ERP system, and of course, by training our personnel.

So we are saying that with the same tools, we try to improve the profitability further. Earlier times as well, we have been saying that, after we did the restructuring, '12 and '13, there is no miracle in improving the profitability. The profitability has to come from improving all parts of the operations in the company.

And we still continue that there's room for improvement, even if we have come long way in improving our profitability.

And then, of course, from management perspective, it would have been very difficult to stand here and explain to you that now we are happy with our profitability. If we hadn't changed the profitability target, then I would be saying to all of you that, now I'm happy, not what would I have been saying to my teams that, okay, now it's enough, don't improve anymore, and I think that would have been very difficult management task for all of us in our management team, and that's why management team was very much in favor that we set new targets to ourselves and Board approved them today. And we are -- of course, we understand that it's a challenging target again. But if you don't have challenging targets, then what's the option. Good. So now there will be, I'm sure lively questions and answers.

QUESTIONS AND ANSWERS

Pekka Rouhiainen ***Valmet Oyj - Director of IR***

Okay. Thank you, Pasi and Kari. Now it's time to take questions. We wait till the gentleman to get behind the table. But we start the questions here at Keilasatama. If you're willing to ask a question, please indicate and I will bring you the microphone. Seems to be no questions here. So we'll take next questions over the phone. So operator, I hand over to you.

Operator

(Operator Instructions)

Your first question comes from the line of Johan Eliason.

Johan Eliason ***Kepler Cheuvreux, Research Division - Analyst***

This is Johan Eliason with Kepler Cheuvreux. Congratulations to a good quarter, Pasi and Kari and the team. And some question, you mentioned market share gains in Paper equipment. Can you give some background to why that is? And then secondly, you didn't talk about market share gains in Pulp. What's the situation there? Are you leaving the low-margin business to a competitor? Or how is the strategy, if you could start with those 2?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

In paper, we have now long track record of improving our market share. And of course, I can't go too much in all the details. But I think, we made our restructuring quick in '12 and '13. And thereafter, we have a stable situation in our organization. And they have been focusing on improving our -- improving the competitiveness of our offering. They have been successful in it. We have very good management in our Paper business group. And we have very good R&D facilities in our Paper business line. And those are pilot facilities, what we have are appreciated by customers. And maybe those are the main reasons why we have been successful. Then in Pulp, our Austrian friends have been gaining more orders in Pulp than we and partly, it's because of the risk-taking and partly because of the cost competitiveness.

So it might be that in a couple of projects, they have been more cost competitive, and have been able to take some orders more than we. Then if we look from the other perspective, we have very high workload now in Brazil, for example, after taking very big Paper machine order and also a very big order for Pulp side. So one has to also think about the organization before entering too aggressively in all the competition. But of course, long term, I don't like the situation, but it will take couple of years to improve the market share in Pulp.

Johan Eliason ***Kepler Cheuvreux, Research Division - Analyst***

And what will that entail? Will you expand your organization, for example, like into Uruguay, or those end markets where you're not active? Or is it more product offering?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

Uruguay is one country. So nobody has executed capability just for Uruguay. But it's making sure that we have very good references, and we have good results from our projects, and we continue to develop our technologies. Those are the tools by which we should increase market share, but I'm not ready to have a very aggressive price fight.

Johan Eliason ***Kepler Cheuvreux, Research Division - Analyst***

Good. Then on your new financial targets. I think this is now the first time you have a target that is higher than your most of the peers. Is there -- I mean, apart from you having acquired Automation, and now last year, some Service business. Is there a structural change in your end markets, now with your policy primarily both of your important end markets, that is basically allowing the market to achieve higher margins going forward? Or is it something very company-specific, your ERP investment, et cetera, et cetera.

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

I think it's -- market is of course, now active, but it hasn't been all the time active now over the last years when Valmet has been improving its profitability. So of course, now 2019, we had good market. But -- and I think it's -- why we are increasing the target, it's more related to the wish that -- and goal to develop the company further.

So none of us in management team was saying, when we discussed and we discussed over this topic over half a year. None of us were saying that, okay, now we are ready, and now we can be happy with the performance, now we should not continue to improve.

So it's a sign that we all believe that there is still room for improvement in our operations. And then it's better to set tough targets and strive towards them.

Johan Eliason ***Kepler Cheuvreux, Research Division - Analyst***

Excellent. Then just 2 minor questions. So Services in Q4 now, suddenly, with strong organic growth, again, after the -- I think it was 2 quarters with slightly low organic growth, which you blamed on sort of rebuilds. Is Q4 was the recovery of the rebuild suddenly coming through? Or what happened basically?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

Our mill improvement projects. So mill improvement project didn't come that much back. So mainly the improvement came from -- so Energy part of the business. And then I wouldn't look too much on one quarter -- when -- where we had nice organic growth, I would more say that it was one-year, with 2% of growth.

And then that's how the market is that sometimes you have a little bit worse quarters and better quarters, and we all the time saying that you should look a little bit longer trends than only one quarter. I don't know Kari, if you Kari agree with that.

Kari Juhani Saarinen ***Valmet Oyj - CFO***

Yes, right. And if we look at the business lines, within our services. So actually 2 increased, 2 were flat and 1 reduced. So it was also kind of...

Johan Eliason ***Kepler Cheuvreux, Research Division - Analyst***

And then just on your guidance, short-term outlook, Pulp still good. You mentioned this order that you took in this quarter. Is the pipeline decent also after the order you announced for this quarter? Or how does it look like?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

There are -- there is still one big project, which has been announced, and thereafter, it will be market, where from -- one where from, we have to take smaller orders. But then small orders can be -- can generate also reasonably order intake, as a total. And then usually, it's a little bit smaller ones are also less challenging in many respects. So that's why we keep our outlook as good.

Operator

We will now take our next question. This comes from the line of Manu Rimpelä.

Manu M. Rimpelä ***Nordea Markets, Research Division - Head of Equity Research of Finland & Senior Analyst***

My first question would be on the EBIT targets you announced. And you already answered quite a few questions around that. But my question would be on the competitor companies are benchmarking beyond ANDRITZ when you look at this margin target. So obviously, I mean, in this industry, we don't know any company being able to do more than 10% margin. So have you kind of -- where have you benchmarked yourself beyond this industry?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

We have benchmarked of course, ourselves against Nordic Engineering Companies. And if you take that comparison, then our profitability is not at the level where it should be. If you think about what's our importance to our customers and what's our market position. And then, of course, we have benchmarked internally, not do we still see potential for improvement. And then like I said couple of times already that there is wish to improve as well. Kari, do you want to highlight some other topics?

Kari Juhani Saarinen ***Valmet Oyj - CFO***

Clearly, Emmanuel (sic) [Manu]. I guess that we also need to look at our global market share. So without of the installed base, we have 40% market share in capital, and also with services, we are getting close to 20% now with the acquisitions. So we have all the -- there's a lot of good ingredients here as well.

Manu M. Rimpelä ***Nordea Markets, Research Division - Head of Equity Research of Finland & Senior Analyst***

Okay. I mean, are you sure? And we hope you succeed. And I guess, the reason I'm asking is, if you compare it to other companies who do big projects in the size that you do. So we really see them targeting above 10% EBITA margins, and that's why I would be just curious to kind of learn more about how you think around the bridge? Are you planning to open that up to investors at what point?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

Capital Market Days (sic) [Capital Markets Day] and don't have too high expectations.

Manu M. Rimpelä ***Nordea Markets, Research Division - Head of Equity Research of Finland & Senior Analyst***

Okay. Second question would be on the internal measures you mentioned. So I mean, I don't think you have any kind of formal cost savings program anymore, but we have announced some production changes from Finland versus the Poland, the Sweden to Poland. And could you just talk about that kind of what do you see on this efficiency front, that you can do more or cost up front? What type of plans do you have in mind for the next 12 to 24 months?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

First of all, the thing what you mentioned is something which is now under discussion. So there is no decision yet. And then we would be from Tampere to Portugal If you think -- of course, we all the time have to think, that how to optimize our product -- our production footprint. That might give some opportunities. We don't have currently any pragmatic plans for that. So I think currently, most of our units are actually very heavily loaded. So the main focus is actually to make sure that our deliveries are on time and with good quality. And now it's not that much possibility in actually to think about about big changes in that respect. And there is not that much need either. Like you remember, in '12 and '13, we made huge changes. And luckily, the changes we made were correct ones. So that our capacity cost is now more acceptable than it was before the big restructure.

Do you want Kari to...

Kari Juhani Saarinen ***Valmet Oyj - CFO***

Well, I think, not really -- nothing really to add. Pasi, said already there, that we continue with the -- must means that we are having and we have still. We are not ready there either.

Manu M. Rimpelä ***Nordea Markets, Research Division - Head of Equity Research of Finland & Senior Analyst***

Okay. And then in terms of the outlook, I mean, I guess, the Paper business, you've been talking about the EUR 1 billion coming down for the last 2 years, at least, but it hasn't come down yet, if there's order intake and maybe it's going to happen this year? And then also, the Pulp cycle seems to be kind of one big project left you mentioned. And So if you're running now at very high utilization rate without the potential to cut cost further, then are you looking in '21 at the risk of sales starting to decline, and maybe '22 as well? So how do you kind of match that up with the potential to then improve margins?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

So like we have been saying, Pulp and Energy, we have quite low capacity cost against the net sales. And now of course, when the net sales is even increasing then -- and the capacity cost will go down. So then when the market goes down compared to this year and previous year, the net sales will go down, but still we have so much outsourced work that it -- we don't -- we will not have that much challenges actually to have full utilization in our organization. And then typically, in that kind of situation, the market is formed from a smaller project, where the profitability is little bit better than in big projects. So we have taken that into account when setting our financial targets that we should target to improve the profitability, not meaning only that when we have tailwind.

Manu M. Rimpelä ***Nordea Markets, Research Division - Head of Equity Research of Finland & Senior Analyst***

So it's fair to say that you can reach those targets without top line growth?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

We have said to the earlier ones as well, that it can't be seen as a target, which we achieved only when we have tailwind.

Operator

We'll now take our next question. This comes from the line of Tomi Railo.

Tomi Markus Railo ***DNB Markets, Research Division - Analyst***

And also congratulations on my behalf. Starting with the profit drivers in 2019, if you could just open up a little bit, what was the main delta, in a way, divisionally, was it Service? Was it M&A? Was it Automation or maybe Paper side? What was the big change in terms of profit and profitability improvement in 2019?

Kari Juhani Saarinen ***Valmet Oyj - CFO***

Yes. Thanks, Tomi. And of course, one important thing was that our stable business grew, and we did 2 successful acquisitions. So that was one thing there. And then also, organically, we had growth at Services and Automation as well. Our project execution, specifically at Pulp and Energy business lines. So that was improving a lot. And then Paper projects sold. So the good execution what we have had already a few years. So that continued very strong. So we had a lot of good things here. And then if we look at our cost development. So headcount increased, SG&A is a bit less than 5%, and the -- like, organic SG&A growth was not that high. So we had a lot of good ingredients here.

Tomi Markus Railo ***DNB Markets, Research Division - Analyst***

And for 2020, would you say that the same trends should continue? Or is there something particular? And maybe also here in connection to the element of increased target setting? Is there familiar elements? Or is there something new, you would highlight?

Kari Juhani Saarinen ***Valmet Oyj - CFO***

Well, I think that the one important thing is that if we look at our backlog, so EUR 3.3 billion compared to last year's EUR 2.8 billion. So we have EUR 500 million more in the backlog. And that -- so that gives us a sound foundation. And then if we look at what's inside in the backlog. So we've said already some time that the quality of the backlog, we are quite happy with that.

Tomi Markus Railo ***DNB Markets, Research Division - Analyst***

And maybe coming also back to the Pulp. Are you still possibly in talks with UPM, Uruguay? Or do you think that's all gone to ANDRITZ?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

I can't comment on anything on that.

Tomi Markus Railo ***DNB Markets, Research Division - Analyst***

But this is the one you are talking about over, if there's something also in addition to your biomill would expect in a long while?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

I think there's one public project here in Finland.

Tomi Markus Railo ***DNB Markets, Research Division - Analyst***

So it could be still plus -- one plus one?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

No.

Tomi Markus Railo ***DNB Markets, Research Division - Analyst***

I know that particular project. But...

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

No, I'm not commenting. I think if I have understood correctly, my friend from Austria has announced something for the Uruguay project already.

Tomi Markus Railo ***DNB Markets, Research Division - Analyst***

Yes. And I'm just trying to figure out, if your folks have ended? Or are you still involved (inaudible) something...

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

No. I'm not commenting of any discussions. But if you read carefully on this announcement, then the answer is there.

Operator

And your next question comes from the line of (inaudible).

Unidentified Analyst

I guess, it's just maybe a little bit more big picture around Pulp and Energy and Paper outlook beyond 2020. Because you've been talking about too large or there's maybe order in 2020, we've already seen one order been awarded. So is this business going to go back to, let's say, something like EUR 700 million? And how do you see it beyond 2020? Is there any risk that we go back to EUR 700 million levels? And we have liked to -- in 2013 and there was tension and all those kind of problems?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

So do you want to take...

Kari Juhani Saarinen ***Valmet Oyj - CFO***

Well, I would just refer to our like short-term market outlook, where we are seeing that Pulp as well as Paper are good. And so -- and that's the pipeline for the coming 2 quarters. And so we are seeing that, that's good. But really not really like commenting on the level. So that is something what we are not commenting really.

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

And then you can also take yourself, look at the Page 15 in the presentation, where we have the Pulp and NHC order intake and net sales. And history has been that we have sometimes good activity, then short while, not that good activity. And then as a result, actually, the net sales comes out from the machine as quite even. And then -- but the minimum, it has been somewhere at EUR 800 million. And then we have been saying, that our capacity cost in that business is such that, we should be able to achieve our targeted profitability levels, even if the net sales drops to that level.

Operator

And your next question comes from the line of Antti Sutelin.

Antti Suttelin ***Danske Bank Markets Equity Research - Head of Research of Finland***

First, a big picture question. If I look you and ANDRITZ, I compare 2019 versus 2014, you both have increased sales with about EUR 1 billion, which is quite a lot. So the question is, how far can this growth continue? Are we starting to approach the top of let's call this cycle. Or how do you see around this topic?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

Of course, I don't know ANDRITZ numbers. But I think they have made also a big acquisition, Xerium, which might be EUR 500 million. So that's of course, explaining part of the growth. And we have the same. So if you calculate the acquisitions, we have done automation order intakes was EUR 416 million, and then what did we say from the acquired businesses, 100 and...

Kari Juhani Saarinen ***Valmet Oyj - CFO***

Around EUR 130 million.

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

EUR 130 million. So it starts to be EUR 550 million. So out of your EUR 1.550 billion is coming from the acquired businesses, then you take Services, which started from EUR 1 billion, and then you calculate 6% growth for that 4% -- 5% growth as an average, then you get some growth of that. And then like we have been all the time, capital market is cyclical. So currently, of course, Paper is high, Pulp is high. So when you make your analyzers think about stable business separately. Because that's not cyclical Paper. Is that high level Pulp, is that the high level, and we have been saying that they will not stay at so high level, but don't worry, we have flexibility in our organization.

Antti Suttelin ***Danske Bank Markets Equity Research - Head of Research of Finland***

Yes. Okay. And then in terms of the new financial targets, the margin target in particular. Could you say what are the most important improvement actions that you still can do? Is it -- I don't know, sourcing, project execution, what is it? Your -- you are now at 9, and you want that to be 10 to 12, what can you do practically?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

Practically, we can continue with the same what we have been trying to do up to now. So push the sales price is up, if it's possible, then continue to take cost away from the products by R&D. That's always effective, then bring new products to the market. So that's always effective. And then the rest comes from the improved operations, and we still have work to do in all these topics. And then not -- of course, every year, we are successful in everything. So as we said every year targets for all these topics. And then we believe that when we execute well, then we can continue to profit improvement also from the level where we are now. So no miracles just could execution.

Antti Suttelin ***Danske Bank Markets Equity Research - Head of Research of Finland***

Okay. And then finally, what was behind the 9% organic order intake growth in Services?

Kari Juhani Saarinen ***Valmet Oyj - CFO***

Well, the Services -- the Services orders increased at in -- and also at performance parts. And we had a quite strong push in the end of the year. And maybe also something that came out from quarter 3 now to quarter 4 as well. So as Pasi was saying earlier...

Antti Suttelin ***Danske Bank Markets Equity Research - Head of Research of Finland***

So basically...

Kari Juhani Saarinen ***Valmet Oyj - CFO***

It's more important to look at the full year, we actually, we had 2% organic growth.

Antti Suttelin ***Danske Bank Markets Equity Research - Head of Research of Finland***

So basically, no big one-off in Q4?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

Not untypical. Some bigger ones, but not untypical.

Operator

And your next question comes from the line of Tom Skogman.

Tomas Skogman ***Carnegie Investment Bank AB, Research Division - Head of Research of Finland***

This is Tom Skogman from Carnegie. Can you disclose how large were your quality costs out of sales in 2019?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

We haven't disclosed it now. But if I remember correctly to somewhat...

Kari Juhani Saarinen ***Valmet Oyj - CFO***

EUR 75 million.

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

Little bit over 2%.

Tomas Skogman ***Carnegie Investment Bank AB, Research Division - Head of Research of Finland***

Okay. And then, I wonder whether the 2019 margin improvement or EBITA improvement came more from equipment or Service and Automation? Where did you see a bigger improvement in 2019?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

All in all, so I think Kari was little bit answering already that we have good project execution in Pulp. So of course, part of the improvement came from there. But then earlier on, we have been saying that if Valmet wants to improve -- total Valmet wants to improve the profitability by 1 point, then all the businesses have to improve. Because otherwise, it means actually that the other part has to improve by 2%.

So if we say that we are now happy with capital profitability and we target 1%, then it means that Services and Automation have to improve by 2% and vice versa. So of course, we strive for profit improvements in all the business lines.

Tomas Skogman ***Carnegie Investment Bank AB, Research Division - Head of Research of Finland***

And that happened in 2019? Or...

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

Over the years, that has happened, partly as -- in some businesses, partly as EBITA percentage improvement. But over the years, we have been improving profitability of all the businesses.

Tomas Skogman ***Carnegie Investment Bank AB, Research Division - Head of Research of Finland***

Okay. And then I wonder about this new ERP system. Where are you in the installation? And when will you start to increase amortizations? And when will you start to see benefits from the investment?

Kari Juhani Saarinen ***Valmet Oyj - CFO***

Yes, Tom. So we are in the middle of the project now. And we are doing good speed, good speed and good work there. And we are already booking some amortization out of the releases that we have done. But still, it's generating more cost than actually -- and benefit. So it's not -- we are not yet at the stage that we would be just harvesting the benefits. And I would think that it would still like take 2 years, once we are getting to that point. So first, we need to have installations done. And then still organization needs to learn things well.

Tomas Skogman ***Carnegie Investment Bank AB, Research Division - Head of Research of Finland***

And how large are the operating cost at your book as operating expenses in 2019 -- 2020?

Kari Juhani Saarinen ***Valmet Oyj - CFO***

No. There are some costs, but I wouldn't like to go to details. We've said earlier that, that the total project costs something between EUR 80 million to EUR 90 million. And we are pretty much in that range still.

Tomas Skogman ***Carnegie Investment Bank AB, Research Division - Head of Research of Finland***

But how much of that is booked as operating expenses? And how much do you put into the kind of the balance sheet?

Kari Juhani Saarinen ***Valmet Oyj - CFO***

Pretty much 50-50.

Tomas Skogman ***Carnegie Investment Bank AB, Research Division - Head of Research of Finland***

Okay. And then finally, about acquisition opportunities. Your balance sheet is developing very, very nicely, and you choose not to pay out all your earnings. So -- and you were very successful with Service acquisitions in 2019. So of course, without going into more details, but I mean, what is happening in -- I guess, you have a -- identified a lot of companies. And just help us to understand, can we kind of at least hope that there will be more Service acquisitions? Or how is it progressing?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

No. For the ones which materialized, 2019, we worked, I think, for the other one, 3 years. So of course, we discuss with companies, and we analyze targets, but it's impossible to estimate if something will positively develop in a year, for example, it's impossible.

But of course, we continue to work on the topic. And like I said, our track record is now that we have spent in acquisitions over EUR 500 million, and we generate from that over EUR 550 million net sales.

So of course, we continue to focus on that. But when something happens, it's impossible to tell.

Tomas Skogman ***Carnegie Investment Bank AB, Research Division - Head of Research of Finland***

Okay. And then perhaps, finally, just -- so we don't kind of overestimate the margin improvement in the years ahead. I mean, it's been a pretty stable improvement since 2015. Do you want us to be really cautious with the improvements in the next 2, 3 years, given your new targets? Or is it a good assumption to see that the improvement we've seen in the last 5 years can continue at the same speed?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

I think, it was easier to answer earlier because we had history of improving it by 0.5% a year.

Tomas Skogman ***Carnegie Investment Bank AB, Research Division - Head of Research of Finland***

Yes. And that's reasonable?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

I don't know whether it's reasonable, but that used to be the track record between some years.

So the time precise with my statement between '15 and '18. So on average it used to be 0.5%, then. It's tough job to improve. So the higher the profit comes, the tougher it is to improve. So it will pay tough from now on.

Operator

And the next question comes from the line of Antti Kansanen.

Antti Kansanen ***SEB, Research Division - Analyst***

It's Antti from SEB. Could you talk a little bit about the outlook for board machine orders for 2020? Because you were pretty cautious year ago, and then you had a very good hit ratio on the large order segment. So what's out there in terms of these very large orders for next 12 months? And how do you see the outlook in APAC and China, in particular, in the let's say, a normal sized machines?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

So, I think -- no, how to open it up. First of all, we of course, say the outlook only for coming 6 months. And now we are saying that the outlook is still good for Paper and Board, and it's coming from the good workload, that we have now in our organization and workshops.

And then we have sales cases that also are active, and that's why we keep our outlook as good for coming 6 months. Then I would say, little bit the same, what we said a year ago, that don't expect that this EUR 1 billion level will continue the fourth year.

Antti Kansanen ***SEB, Research Division - Analyst***

Okay. And then maybe a question for Kari, regarding the SG&A cost development in 2019. I mean, majority of it is from M&A, but do you kind of -- are you incurring a lot of extra costs related to the high tendering activity on the Metro Pulp project side. So how should we think about, if we exclude the M&A impacts. The SG&A going into 2020? Are there some tailwinds as well? Or it's just a normal inflation at the ERP project impacts still ongoing?

Kari Juhani Saarinen ***Valmet Oyj - CFO***

Yes, Antti. So that's correct that we had because of the business activity. So there was some additional sales costs now and during 2019 and by then, but I think that overall, things don't lease up because we are having now some salary increases coming this year. This year, most likely. And so we just need to be prudent here. And -- but I wouldn't see any major releases on the cost pressure here either.

Antti Kansanen ***SEB, Research Division - Analyst***

Okay. What's a reasonable assumption for annual inflation-based on the labor increases?

Kari Juhani Saarinen ***Valmet Oyj - CFO***

More than 2.

Antti Kansanen ***SEB, Research Division - Analyst***

Or just a normal -- okay. Then maybe third question on the growth in Services and the outlook on the mill improvement cases. I mean, what's really the delta here? And how should we think about that market in 2020, kind of what kind of projects would you see growing? Or is there still a decline in some activities? You mentioned that it didn't really move that much in Q4. So what's the outlook over there?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

No. It's difficult to give an outlook for PU level. So we gave the outlook for Services. And then of course, in every year, or, let's say, in a normal year, not all the PUs will grow. So like last year was Kari saying that 2 were growing, two were flat and one was decreasing. So that's a normal year. Then it's too early to guess that which of the PUs would be growing and which not. Of course, we target for themall to grow.

Antti Kansanen ***SEB, Research Division - Analyst***

Okay, fair enough. And then the 2 acquisitions that you made, I guess, there are some cross-selling opportunities over there as well. So have you seen any gains from that? Or is that something that we should expect more into 2020 and '21, as you have had those -- are in the books for almost a year?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

Of course, already now, we have been -- we have cross-selling is not that much. So we in one acquisition, we are utilizing our own old network to sell the products. And then, with other acquisitions, we made very big or not very big, but moves now how to integrate it, and where we created an organization, which will strengthen us in stock prep area. And then we created stronger unit to serve our Pulp customers in North America. And there we of course, expect that not only cross-selling, we see with the increase, but the total sales on those areas will increase.

Antti Kansanen ***SEB, Research Division - Analyst***

Okay. And then maybe last question is that you earlier showed a kind of gains that you have -- and you had targets for procurement savings. And now considering that you have higher profitability targets. One might assume that you're expecting your gross margins to improve as well.

So have you kind of seen pricing gains, in terms of that your customers are now more willing to accept higher prices and this procurement saving gains that you are making are not flowing through to the customers, in terms of price discounts? Or how has this developed in the past year or 2?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

Our customers continue to be very price conscious. So they put a lot of pressure on us. So which means then that the big part of the procurement savings are going to our customers. And we'll continue. So we have tough customers.

Antti Kansanen ***SEB, Research Division - Analyst***

So in terms of reaching higher profitability, the sales mix would be the primary driver for higher gross margins? Or should we...

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

No. I was referring already that of course, we have pushed sales prices up for all the products, then we have to develop our product offering, and then make sure that the execution goes well. So those all will be seen in gross profit line.

Operator

And your next question comes from the line of Sven Weier.

Sven Weier ***UBS Investment Bank, Research Division - Executive Director and Analyst***

2 questions from my side, please. The first one is on the Pulp project pipeline. Obviously, we're all aware that it's quite a busy last 12 months on big ticket awards. And you already said that conscious of your high workload. On the other hand you -- we're obviously aware that a lot of this is outsourced, as you said. And I guess it's the same for ANDRITZ. So I mean, I'm aware that you're very disciplined about

your resource and have it very much under control. But how do you make sure that the supply chain is delivering? Because I guess, in some situations, you're using probably the same sub-suppliers as ANDRITZ?

So that would be the first question.

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

Of course, we have to be very careful. And we are using same sub-suppliers and different sub-suppliers. And then of course, the core of everything lies in our own organization like lead engineers. And their engineers who are making very critical engineering decisions and also procurement of the critical items. I said our own manufacturing still. So we have to be careful that we are not overloading our own organization. And then the next topic is the sub-suppliers. And there, it will be tough in coming year to 2 years in managing it.

Sven Weier ***UBS Investment Bank, Research Division - Executive Director and Analyst***

So yes, that's probably the thing that we have to monitor most closely, right? Because I guess you learned from the lessons of the past and ANDRITZ, but the question is, have the suppliers really learned the lessons. The other question I just had on scrubbers. If I remember correctly, you said you expect your marine business to be a little bit down on 2019, but still a good activity overall. I mean, I realize that Q4 was a bit on the low side with order intakes. So would we expect at least kind of a sequential improvement because if I listen to IFRS and Wartsila, they do now see a bit of a pickup in the market because the spreads have gone up. And obviously, the owners are making good money on the equipment. Do you see that reanimation of the market as well? Or what do you sense at the moment?

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

ANDRITZ knows that -- sorry, Wartsila knows the market a lot better than we. But our assumption is that we will have activity, but not as good as this year.

Sorry, last year.

Sven Weier ***UBS Investment Bank, Research Division - Executive Director and Analyst***

But I read it from your results that at least your deliveries and the margins on these things have been going as expected. So you are pretty happy with the business overall.

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

It's good business for us.

Operator

And your last question comes from the line of Johan Eliason.

Johan Eliason ***Kepler Cheuvreux, Research Division - Analyst***

Yes, sorry, for taking your time again. I was just curious a sense a bit of an optimism around China and Board orders, and wanted to know if that could still keep your Board orders above EUR 1 billion this year? But I think you already answered that we shouldn't expect the fourth year with Board orders or Paper orders above EUR 1 billion. So I think, I already have the answer, and congratulations again.

Operator

No further questions over the phone line, sir, you may continue.

Pekka Rouhiainen ***Valmet Oyj - Director of IR***

Okay. Thank you. Are there some questions here at Keilasatama, somebody willing to have something. If not, we will then start to conclude this event. Thank you, everybody, for the active participation, and the Q1 results will be published on the 23rd of April and then the Capital Markets Day for 2020 will also be -- now this year will be the year for the Capital Markets Day, and it's going to take place on September 23. So please save the date on your calendars. But thank you, everybody. And have a nice rest of the day.

Pasi Kalevi Laine ***Valmet Oyj - President & CEO***

Thank you.

Kari Juhani Saarinen ***Valmet Oyj - CFO***

Thank you.