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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to TomTom's Third Quarter 2022 Earnings Conference Call. (Operator Instructions) Please note that today's conference is being recorded.

I would now like to turn the call over to your host for today's conference, Mr. Freek Borst, Investor Relations. You may begin, Freek.

Freek Borst - TomTom N.V. - Investor Relations

Thank you, operator. Good afternoon, everyone, and welcome to our conference call during which we will discuss our operational and financial highlights for the third quarter of 2022. With me today are Harold Goddijn, our CEO, and Taco Titulaer, our CFO. We will start today's call with Harold, who will discuss the key operational developments, followed by a more detailed look at the financial results and outlook from Taco. We will then take your questions. As usual, I would like to point out that Safe Harbor applies.

And with that, Harold, I would like to hand it over to you.

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

Yes. Thank you very much, Freek. And ladies and gentlemen, a very warm welcome and thank you for joining us today. As usual, I will go over the operational highlights of the quarter. It was a good quarter, our third quarter, and we recorded better-than-expected revenue, driven by our Location Technology business. In Automotive, we saw solid new car production hitting the road with our software and our services, while Enterprise benefited from FX tailwinds. Our progress this year is satisfactory, and we expect that we'll be able to outperform our initial guidance.

We were able to secure some key commercial awards, both in Automotive and Enterprise, and I'd like to highlight our new partnership with Hyundai Motor Group. It's an important award that sees TomTom support its entire vehicle lineup in Europe across all brands, with maps and real-time traffic. And over the coming years, millions of vehicles from the group will become equipped with our technology as standard, and that is establishing 100% take rate for the first time we see that in the automotive industry.

Our Maps will enable advanced driver assistance systems to better anticipate the road ahead. And we will provide highly-accurate, verified content for all speed limit types across Europe, and that will help all cars to become compliant with the Intelligent Speed Assistance regulations.

In Enterprise, we significantly matured our Maps APIs portfolio, making it more complete for developers in our key markets. Three APIs were launched for the fleet and logistics segment. In partnership with PTV Group, we are providing the German transport authorities with products to improve safety on German roads. We will provide real-time travel time information and hazard alert services.

During the third quarter, we finalized the realignment of our Maps organization. And our focus on transforming the mapmaking process to a highly-automated platform paves the way towards a new era in mapmaking. And this means that we will be able to deliver a significantly better product that will open up new markets and new use cases. We are able to offer a better map, while becoming more efficient at producing it.

And we expect our maps to improve along 3 axes. We will have better coverage, especially outside Europe and North America. We will add more and richer attributes to our maps, and a more dynamic update mechanism will result in both fresher and more accurate maps. As a result, the addressable market will expand significantly, it will open up more geographies, and we can serve a much broader set of use cases.

We look forward to providing you an update about the implications for our competitive position and our growth at our Capital Markets Day on the 2nd of November.

And with that, I hand over to Taco.

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

Thank you, Harold. I will provide some commentary on the financials and outlook, afterwards, we will proceed to the Q&A. Group revenue was EUR 136 million in the third quarter, an increase of 7% as compared to the same quarter last year. Location Technology revenue, meanwhile, was EUR 108 million, 14% higher than the same quarter last year.

Let me briefly discuss revenue business by business. We reported Automotive IFRS revenue of EUR 62 million, representing a year-on-year increase of 19%. Automotive operational revenues increased by 29% to EUR 75 million. This marks an outperformance compared to the development of car production in Europe and North America, which we consider our core markets. In both Europe and North America, car production growth was roughly 25%. The outperformance we recorded resulted from market share gains. Some of our automotive customers showed a relatively strong recovery in production and some contracts saw a ramp-up during the quarter.

Enterprise revenue increased by 7% year on year to EUR 46 million. We continue to benefit from a stronger U.S. dollar as most Enterprise revenues are U.S. dollar-denominated. Lastly, Consumer reported revenue of EUR 28 million, representing a decrease of 13% year on year.

In the third quarter, our gross margin was 81%, comparable to last year. Both in this quarter as well as the same quarter last year, the gross margin was not affected by material exceptional items. OpEx were EUR 128 million, an increase of EUR 2 million compared with the same quarter last year. Operating expense for the quarter included a EUR 5 million gain from our release of the restructuring provisions we took in Q2, as some of the impacted employees were successfully redeployed. This release is booked in the G&A line. Excluding the impact of the restructuring, depreciation and amortization, operating expenses rose by EUR 10 million year on year. This increase in spending is related to further investment in our application layer and sales and marketing.

Free cash flow was an inflow of EUR 8 million. This is excluding the restructuring costs for the Maps realignment as announced earlier this year. Last year third quarter, we saw an outflow of EUR 14 million. This improvement was the result of a strong year-on-year increase in Automotive operational revenue. Lastly, our net cash position was EUR 330 million at the end of the quarter. This is comparable to last quarter.

Having discussed the results for the quarter, let me move on to the outlook presented on the next slides.

We are pleased with the performance this quarter and have good visibility on outperforming our initial guidance for 2022. We're updating our guidance to reflect this. So, group revenue is expected to be between EUR 505 million and EUR 520 million, with Location Technology revenue now expected to be between EUR 410 million and EUR 425 million. In terms of free cash flow, we expect a cash outflow of around minus 2% of group revenue for 2022. We should note here that our free cash flow guidance excludes the charges related to the restructuring we announced last quarter. Of the EUR 25 million restructuring charge, we paid EUR 6 million this quarter and expect to pay the remainder in Q4 of this year and Q1 of next year.

Then moving to the 2023 guidance. Our reported revenue guidance for next year stays intact. That said, the persistent macroeconomic uncertainties have lowered our expectations for Automotive operational revenue. We now expect this to grow with -- by 15%, which is lower than our expectation at the start of this year. Second, the high inflation is influencing our cost of labor. Both effects combined made us lower our guidance for free cashflow to break-even.

Operator, we would now like to start the Q&A session.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) We have a question coming from the line of Emmanuel Carlier from Kempen.

Emmanuel Carlier - Kempen & Co. N.V., Research Division - Research Analyst

I have three. First of all, on Enterprise. So at constant FX, I calculated that the revenue was down 7%, which is a bit worse than in Q2. So, you kind of say that this is a growth segment, but so far, we don't really see that. And I understand that it's driven by the fact that you are still updating the map, and probably a little bit too early. On the other hand, you also say that you see some price pressure there, so I would like to better understand a bit how long these contracts typically last on average, why you see price pressure, and if this is something that you expect to continue? So that's the first question. And I prefer to take them one by one.

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

Okay. Thank you, Emmanuel. We -- if we do the calculation, we see declines were 2% on constant currency. What you need to take into account is the timing of the billing and -- et cetera, has an effect as well. So, you can't just apply the overall appreciation of the dollar against the euro and multiply that by 80%. It's -- there's a lot more detail that goes in. But it's true that on constant currency, the Enterprise business declined, but that's with 2%. And the second question was on the term. What we see is that the term is on average 3 years, I would say, but you also see 1-year contracts and also 5-year contracts. But most contracts are 3-year terms.

Emmanuel Carlier - Kempen & Co. N.V., Research Division - Research Analyst

But what is the reason you are seeing price pressure, and is this something that you believe could continue?

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

No, that's mostly related to value assessment, so that's a case by case. Sometimes prices go up and sometimes, prices go down.

Emmanuel Carlier - Kempen & Co. N.V., Research Division - Research Analyst

Okay. Then, the second question is on Automotive. So on the operational revenue side, you had 30% growth, but 25% is driven by production. So yes, if we deduct, you have actually 5% sales growth from, let's say, market share gains, increased take rates and also taking into account price pressure. Is this a kind of run rate that you believe is fair for the coming quarters and years? And if not, why?

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

Do you mean the growth percentage or just the run rate?

Emmanuel Carlier - Kempen & Co. N.V., Research Division - Research Analyst

Yes. So, what I mean is that you have a high operational revenue growth this time, but a big part is coming from production, which is a kind of one-off, of course. Once it's back at normal levels, what will drive top line is the take rate, market share gains or losses, and pricing. So, if you calculate the delta, the last 3 elements have something like 5% sales growth. So, the question is, if you believe this is a kind of good run rate for the coming quarters and years?

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

Yes. No, yes. And it's indeed, those are all factors that influence that. We expect that on the longer term, so not per quarter, the longer term, let's say, the average of the last 4 quarters, we will do better than the market. And that will always be a couple of percentage points better, so 3 to 5 percentage points. And then the main drivers here are higher take rates, and the second is, I think, market share gain. So, with the caveat that some quarters can be different because it has to do with the OEMs that we serve and the models, et cetera, from a longer term, we will outperform the market.

Emmanuel Carlier - Kempen & Co. N.V., Research Division - Research Analyst

Okay. Understood. And price pressure, is that something that you still see? Or is this kind of done, you think?

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

Well, I wouldn't call it price pressure. I think prices are very stable. What we see is that adoption rates are going up. And of course, in our price book, if you ask for more product, then you get a better price, than if you only want to have half of your fleet equipped with our product. So, the more volumes, the better the price for the customer, but that's in both our interest.

Emmanuel Carlier - Kempen & Co. N.V., Research Division - Research Analyst

Okay. And then the final question is on the free cash flow guidance for 2023. Is it correct to say that the lower downgrade is driven by the fact that on sales, you expect rather to achieve, let's say, the lower end of your range? And then on top -- yes, mainly OpEx, that is going up higher than expected? Or could gross profit margin also play a role in that?

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

No. The way to look at it, and there are, of course, multiple elements, but the main factor here is what we foresee for Automotive operational growth. When we went into the year, we were even more optimistic than we are -- than we still are. So, we think that our operational revenue can grow with 15% next year. And due to all kinds of effects, that used to be a bit higher at the start of the year. So, a big part of our free cash flow assumption -- or reduction of that is coming from this, and the second is the pressure that we feel on wages. But let's say 60% is coming from a bit less operational growth in Automotive, and the second effect is the wages.

Emmanuel Carlier - Kempen & Co. N.V., Research Division - Research Analyst

Okay. And there is no impact on gross profit margin? Because in Q3, it was also a bit softer versus Q1, Q2 this year.

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

So, for the gross margin, I think that is on a continuous increase, and the main factor there is the mix from -- or the dominance of software. Of course, the effect was more extreme a couple of years ago. But we're trending towards a sustainable gross margin of, let's say, 85% over time. So there's, I think, still room to grow that number.

Operator

The next questions come from the line of Marc Hesselink from ING.

Marc Hesselink - ING Groep N.V., Research Division - Research Analyst

First question. I would actually like to go back to those take rates. Where do you see them today, given, I think, the nice Hyundai contract there with 100% take rates. Also, I think 100% take rate on the electric vehicle models. In general, I think we have seen a mix towards more -- a shift towards the more premium models. So where do you see it across your client board?

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

At 40%, roughly.

Marc Hesselink - ING Groep N.V., Research Division - Research Analyst

And it is a trend that from here, it will continue to grow gradually or what kind of expectations do you have there?

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

Yes. No, yes, for sure, that it will grow. But don't expect that to grow to 50% in the next quarter or so, that takes time.

Marc Hesselink - ING Groep N.V., Research Division - Research Analyst

Okay. Then the second question is actually the Maps realignment. Do you see any commercial impact on that? You see, okay, we can now provide a better product to the clients, that you also have that kind of discussions which are -- with maybe new potential clients to move them to TomTom.

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

Yes, Marc, so we have not launched the products that are resulting from our new mapping platform, so you won't see any revenue and you won't see that this year in real terms. But there is an exciting development in our mapping platform. We will be able to produce significantly more detailed maps. We will have a lot more coverage with our maps, so we can expand our base -- our business. And we can start addressing a market that has not been available to us in the past, and that involves markets where we are traditionally not very strong. So that's everything outside of North America and Europe. All of a sudden, that opens up new possibilities.

And the second way we can expand our addressable market is by addressing use cases that are -- that we currently cannot serve. Due to the high-precision type of attributes, that we're bringing into our new map platform, will allow us to play in consumer applications, display applications, more web-based, mobile phone-based applications, where we currently don't have a big presence.

So, if you look at our current customer base, of course, we're doing well in Automotive. And we have seen a lot of activity this year in the Automotive segment, which is very encouraging -- will lay a foundation under longer-term growth also in the Automotive industry. But on top of that, we can start developing a whole new segment in what we have defined as the Enterprise sector, where we currently don't have a strong position.

And that's all very -- I think that's all very exciting. We're preparing for that. We'll be ready by the end of this year, have everything in place to start selling and licensing those products, and we will start informing the market in Q4 about those developments that are taking place.

Marc Hesselink - ING Groep N.V., Research Division - Research Analyst

Okay. How should I see that sales process? Is that something that the market is very aware that you have that product or is that something that you really have to push and make it visible?

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

Well, it's a bit of both. So at the moment, it's all under wraps, we're in stealth mode. We talked to a handful of selected target customers, but then we will, of course, go broad. We have prepared our sales capabilities in the anticipation of that to happen. And then you will see, yes, revenue coming from that -- from those new activities in '23, be it -- albeit at a modest scale. The sales cycles are typically not that short. It typically takes between 3 and 6 months. And then after that, depending on the use case, a bit of a ramp-up period before you go mainstream and you go high volume. But definitely, in '23, we will start seeing the outline of growth potential for the medium term.

Marc Hesselink - ING Groep N.V., Research Division - Research Analyst

Okay. Clear. Then the final question that I have is actually on visibility on the car production volumes into next year, because I see actually quite a mixed signals. You're also highlighting today that it maybe a little bit lower than you initially thought. But how is that built up? Because some are saying, okay, there's still a lot of pent-up demand from the last 3 years, that still needs to be produced. But on the other hand, there are also people maybe becoming a little bit more anxious. How do you get your info there?

Operator

Ladies and gentlemen, please continue to stay on the line. The conference will resume shortly.

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

Yes. Marc, I think we -- somehow, the line got dropped. This is a -- this has never happened before, apologies for that. I hope you can hear me loud and clear now. Can you confirm?

Marc Hesselink - ING Groep N.V., Research Division - Research Analyst

Yes.

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

Yes? Okay. Yes, the question about what's happening in the volumes on the Automotive side, well, to put things into perspective, the last 2, 3 years have been obviously disappointing in terms of car production, the COVID, chip shortage -- supply. We -- at the beginning of the year, we expected those chip shortages to continue into the beginning of '23. I think that's still the case, but we do have -- but what we have seen is a relative relaxation of supply chain constraints in Q3. So, for the first time, we were kind of -- we were seeing production numbers that were beating our expectations, and we expect that to continue in Q4.

At the same time, we need to be aware of the macroeconomic circumstances. We don't know exactly where we'll land in '23, but it's reasonable to expect that overall car demand will be depressed to a certain level in 2023, because of inflation and customer happiness and whatnot. So, you have two conflicting macroeconomic events at play. Further relaxation of supply chain constraints will lead to higher production numbers. And on the other hand, dampening of demand -- expected, I should say, dampening -- that's how we are planning. We expect some dampening in demand because of macroeconomic conditions. But quite frankly, where it'll exactly end is not that easy to guess.

Marc Hesselink - ING Groep N.V., Research Division - Research Analyst

I understand that. So at this stage, you took a little bit of extra margin, given that uncertainty?

Operator

Ladies and gentlemen, please continue to stay on the line. Your conference will resume shortly. Ladies and gentlemen, please continue to stay connected. The conference will resume shortly. Thank you for your patience. The line is now reconnected. Can you hear us?

Freek Borst - TomTom N.V. - Investor Relations

Yes, we can, indeed. We can resume the call, please.

Operator

Okay. So Marc is still in the question-and-answer session, so you may continue, Marc, with your question.

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

Marc, we are here. Can you hear us?

Operator

Okay, I think he just disconnected from the questions. So we are going to proceed with the next question. The next questions come from the line of Wim Gille.

Wim Gille - ABN AMRO Bank N.V., Research Division - Head of Research & Equity Research Analyst

I've got a few questions. First of all, can you give us a bit more color on the ramp-up of the Hyundai contract, as this is definitely one of those contracts that actually can shift the needle on the top line. So, it would be quite nice to have a bit of feeling on when shipments, et cetera, start to commence and how you look at that going into 2023.

Second question is on the 2023 revenue outlook. Just for my understanding, you reduced expectations there. Is this something that you've done based on revised estimates from the OEMs? Or is this that you've done, let's say, on your own, let's say, account, i.e., is this something that your customers are telling you, or are you building a bit more precaution yourself?

The third question would be on your IVI platform. If there's any new developments there -- new clients that you've onboarded and, or, discussions that you're having with clients on that particular product?

And my last question is on the APIs. I'd like to get a bit of better feeling on how broad the applications are that you are targeting with these new APIs for fleet and logistics? You specifically mentioned ride-hailing and food delivery markets as big markets where there's only a handful of companies that are active in that market. And more specifically, you are quite intimate with the biggest one, more specifically the one that everybody else hates. So, can you give us a bit of feeling how broadly applicable these APIs are, and if you by any means are constrained to Uber or not?

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

Yes. Let me take the first 2 questions, and then I'll hand over to Harold for the IVI and API questions. On the Hyundai, that is in, as you say, in ramp-up. We saw that happening during Q3. I expect that to -- that it will take another 3, 4 quarters to get to full production levels. So, that will take another 3 quarters of a year, I would say.

On the guidance, that is a mix of things. We look at industry data almost on a weekly basis, so that's a bit of a top-down approach. On the bottom-up approach, we have our account teams having a direct dialogue with the OEMs. And based on both, we came to the -- so yes, roughly, we saw 20% increase. Now, we're at the 15% increase for next year. And it's something that we felt we had to do.

Over to you, Harold, on IVI?

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

Yes. So yes, IVI platform, it's quite exciting times, actually, because one of the first cars that's based on our new IVI platform will -- is nearly ready for SOP, start of production. And that is the first proof point out there in the market that it all works. We had, in our marketing communication, told the market that we think we can, by applying this technology, reduce cycle times by at least half and reduce cost of developing those systems by 70% to 80%. And those numbers are confirmed.

Now, we can do postmortem with our launch customer. We have indeed developed this in record time, and total cost to develop these systems are only a fraction of what it typically would cost a larger, more complex -- arguably, also more complex OEM, to develop this. So that is an early proof point that the assumptions for getting in this market are validated. And that means that this platform is especially suitable for lower volume applications. The benefits are real. You need to think about electrical vehicles and start-ups, but also trucks, light commercial vehicles, that can benefit from the implementation of this technology.

On the commercial side, forward-looking, we're busy. There are five situations where we're in discussion to license this platform. We expect at least some of them to be finalized in a positive way over the next, I would say, 6 to 12 months or so.

Your fourth question, Wim, API, better -- if we have better feeling for the applications we can serve with those APIs. So, it is indeed ride-hailing where we have already significant market share through one of the largest ride-hailing companies in the world. We have added other ride-hailing companies to our client portfolio. Delivery is an important segment as well. There is a real opportunity there, but also some gaps in our product offering. We have to be honest there. But we think we can close those over the next -- in the medium term, and open that -- mostly talking about 2-wheeler navigation and last-mile delivery, that kind of stuff. But also encouraging signs of early wins and interest in the technology.

And then a very large segment is logistics in a broader sense, so light commercial vehicles and trucks and fleet management companies. We know that market well. We have run and build up a fleet management company ourselves with Webfleet, so we know the market quite well.

And there, we also see significant traction for our APIs and SDKs. That's a fragmented market, but it's large, typically lower volume, but high added value.

Wim Gille - ABN AMRO Bank N.V., Research Division - Head of Research & Equity Research Analyst

Very good. And then a follow-up question on the IVI platform. You mentioned that you're in commercial discussions, active discussions, with five potential customers. I remember from the past that the expectation was that, first, the, I would say, smaller brands would kind of be looking to adopt this, and let's say that potentially larger brands would only follow after that -- after there is a bit more proof points there. Is that still kind of, let's say, the current dynamics? Or do these five customers also include one or two of the larger OEMs?

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

Well, I think, with those five we are in detailed discussions. There is interest from the larger OEMs, but indeed, they would like to see more proof it is really working and doing what it is supposed to be doing. But that proof is accumulating, and we are in a much better position, a strong position than we had -- than we were, let's say, 12 months ago.

Wim Gille - ABN AMRO Bank N.V., Research Division - Head of Research & Equity Research Analyst

So indeed, the five are kind of still the smaller brands out there, and the larger brands “kijken de kat uit de boom,” how do you say that in English?

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

Yes, “the cat out of the tree,” Willem. I don't know, yes. So that's right. But we have gathered a ton of experience, of course, also connecting to the rest of the hardware and the electronics in the vehicle, how that all works together. It's a good trajectory, and it gives us an opportunity to serve those start-ups and smaller vehicles in a very cost-effective way. That's good both for the OEM and for us. And we hope that we'll build a nice portfolio of growing brands in that space.

I think it's kind of where the market is going to anyway, we see smaller runs. Electric platforms give you more opportunity, flexibility, to do special purpose vehicles. All that needs IVI and software. There's no known way of doing that cost effectively. And I think that our IVI platform is a clear beacon and an example of how you can build in flexibility and efficiency in your development flow, by working with well-thought-out components, to do in a fraction of the time and cost what the larger players need to spend in order to get their IVI products to life.

So, it kind of fits in a market trend of modularity, reusability of software, scale, and shorter times to market. So, in that respect, it's also an important development. I think we are on the money here, in terms of what the market will require over time, and that's not just for the smaller ones. But over time, that will also matter for the larger ones.

Operator

We are going to proceed with the next question. The next questions comes from Miki Sugimoto from Red Wheel.

Miki Sugimoto - RWC Partners Limited - Investment Professional

I want to understand a little bit more about next year's guidance, just some clarification on the change in the -- so the reported revenue outlook remains unchanged, but I understand that your operational revenue is going to go -- you revised it down. And could I ask -- I think you did sort of dwell on that, but is it -- how much is that because of the macro outlook or your specific product outlook? So that's one question.

And then the second part, you said that because the reason why the free cash flow is turning -- you revised down the free cash flow outlook, is the higher wages. So is that because you are spending -- how much is that? Is that because of the pure wage inflation or is it more because you are spending more on R&D because you are -- it's more like your investment as opposed to pure wage inflation?

And then as regards to that, if you are seeing wage inflation, what's your ability to pass it on to your customer -- OEM customers? Or is it because you have a 3-year contract period, as you said, on average, you would have a gap where you have a 3-year existing contract that you cannot pass on your wage inflation cost? So a little bit more color around that would be very helpful.

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

Yes, thank you, Miki. Yes, your first question about being still very optimistic about next year, but a little bit less than compared to the start of the year, that has to do with macroeconomic effects. That's purely the market that we look at and the market data that we receive. So, it's more a bottom-up approach where we see the industry analysts being more cautious over the recent weeks, and we have applied that to our own forecast.

On the wages, yes, wages can go up because of various things. Of course, it is your headcount, or the location, or the mix of roles. I don't think it is so much the increase in headcount, neither is it the distribution in which countries we work at, but it is indeed, predominantly, it's that we are becoming more an R&D company. And that sometimes means that the average cost of our employees is going up. Coupled with the effect that this year's cycle will need a higher increase than what we've seen in the past.

Your last question, on the cash flow. Could you remind me of the question? What was the question?

Miki Sugimoto - RWC Partners Limited - Investment Professional

Yes. So, I just wondered if you -- the reason why your cash flow guidance has gone down next year is a combination of lower operational revenue and higher inflation, you said. So, if you were to say -- would you be able to quantify that, could we break it down to half is due to revenue and half is due to inflation?

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

Yes, roughly 60-40.

Miki Sugimoto - RWC Partners Limited - Investment Professional

60 to revenue and 40 to inflation?

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

Yes.

Miki Sugimoto - RWC Partners Limited - Investment Professional

Sorry -- wage. Okay. That's very helpful. And I just wonder, in terms of your ability to pass that increase in wage on to your customer?

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

Yes, it depends, of course, what kind of contract we have. If it's all set in stone, that's not possible. But yes, the contracts -- there are a lot of contracts that mature on a regular basis, and that opens up the possibility for us to renegotiate, of course. But there is -- it is not -- we tend not to have an automatic correction.

Miki Sugimoto - RWC Partners Limited - Investment Professional

No, so you would have to renegotiate. But would you be able -- for example, like if you have a contract that just started last year and you're in the second year, are you able to go back and renegotiate for the rest of the remainder of the 2 years, or no?

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

It all depends. But contractually, probably not. But it all depends.

Freek Borst - TomTom N.V. - Investor Relations

Ladies and gentlemen, since there are no further questions, I would like to thank you all for joining us this afternoon. Operator, you may now close the call.

Operator

Thank you. This concludes today's presentation. Thank you for participating. You may now disconnect.
