Raytheon Technologies Corporation (NYSE:RTX) Q4 2021 Earnings Conference Call January 25, 2022 8:30 AM ET

Company Participants

Greg Hayes - Chairman & Chief Executive Officer
Neil Mitchill - Chief Financial Officer
Jennifer Reed - Vice President of Investor Relations

Conference Call Participants

Sheila Kahyaoglu - Jefferies
Robert Stallard - Vertical Research
David Strauss - Barclays
Noah Poponak - Goldman Sachs
Peter Arment - Baird
Ron Epstein - Bank of America
Myles Walton - UBS
Mike Maugeri - Wolfe Research
Kristine Liwag - Morgan Stanley
Robert Spingarn - Melius Research
Cai von Rumohr - Cowen
Seth Seifman - JPMorgan
Matt Akers - Wells Fargo
Doug Harned - Bernstein

Operator

Good day, ladies and gentlemen, and welcome to the Raytheon Technologies Fourth Quarter 2021 Earnings Conference Call. My name is Lisa, and I will be your operator for today. As a reminder, this conference is being recorded for replay purposes.

On the call today are Greg Hayes, Chairman and Chief Executive Officer; Neil Mitchill, Chief Financial Officer; and Jennifer Reed, Vice President of Investor Relations. This call is being carried live on the Internet, and there is a presentation available for download from Raytheon Technologies' website at www.rtx.com.

Please note, except where otherwise noted, the company will speak to results from continuing operations excluding acquisitions, accounting adjustments and net non-recurring and/or significant items often referred to by management as other significant items.

The company also reminds listeners that the earnings and cash flow expectations and any other forward-looking statements provided in the call are subject to risks and uncertainties. RTC's SEC filings, including its Form 8-K, 10-Q and 10-K, provide details on important factors that could cause actual results to differ materially from those anticipated in the forward-looking statements.

Once the call becomes open for questions, we ask that you limit your first round to one question per caller to give everyone the opportunity to participate. [Operator Instructions] You may ask further questions by reinserting yourself into the queue as time permits.

With that, I will turn the call over to Mr. Hayes.

Greg Hayes

All right. Thank you, Lisa, and good morning, everybody. Happy Tuesday. Okay. 2021 was an important year for Raytheon Technologies. As we laid out our strategy at the beginning of last year, and that strategy, of course, is to drive top line growth, margin expansion and robust free cash flows through 2025 and beyond, while at the same time, continuing to invest in our businesses and returning significant capital to shareowners.

Our continued focus on operational excellence and program execution, along with our industry-leading technologies, positions us well to continue to capitalize on the commercial aerospace recovery and to grow our defense franchises.

As you saw from our press release this morning, we delivered another solid quarter with strong full year financial results, with both top and bottom line growth and $5 billion of free cash flow. That's more than double of what we delivered in 2020 on a pro forma basis.

Our performance in 2021 gives us confidence in the long-term fundamentals of our businesses and that we're able to -- and that we're on track to deliver to the 2025 targets that we outlined last May at our investor conference.

Before I turn to the highlights, let me first provide some comments on the current market environment. During the quarter, commercial air traffic remained resilient despite the Omicron variant, with global available seat miles, ASMs, growing about 1% sequentially in Q4. That's reflecting a continued recovery in air traffic despite the typical seasonal trends.

Here, in the U.S., passenger traffic through TSA checkpoints also remained steady at about 1.9 million passengers per day. That's up almost 125% versus the fourth quarter of 2020, a remarkable recovery.

On the defense side, we're pleased to see the President signed the bipartisan Defense Authorization bill into law at $740 billion. That's about $25 billion higher than the original Presidential request.

And given the global threat environment, we continue to see strong demand internationally for our products and services. Our focused aerospace and defense portfolio, along with our $156 billion backlog, gives us confidence in our ability to grow the business in 2022 and beyond.

Okay. Turning to Slide 2, some highlights from the fourth quarter. As I said, we delivered strong financial performance in 2021. Organic sales grew 1%, which is in line with our expectations, while adjusted EPS and free cash flow for the year, were both above our initial expectations. And importantly, we saw margin expansion in all four of our businesses, with strong commercial aftermarket.

Our defense backlog remained robust at over $63 billion, where RIS and RMD both ended the year with book-to-bill slightly above 1.0. In addition to several large awards earlier in the year, we also had several notable awards during the fourth quarter, including over $1.3 billion in classified bookings, plus over $670 million for the Electro-Optical Infrared awards at RIS, as well as $730 million in Standard Missile-2 production awards at RMD.

We also remain focused on operational excellence and program execution to drive structural cost reduction and productivity in our operations. In 2021, we achieved about $760 million in incremental cost synergies from the RTX merger, bringing us over $1 billion since the completion of the merger in April of 2020. That meets our original merger cost synergy target two years ahead of schedule. And there's always, of course, more to come and more to do there.

It's also worth noting that the Rockwell or the Collins Aerospace team achieved over $600 million in total Rockwell-Collins synergies since the acquisition in November of 2018. They're meeting their commitment a year ahead of schedule despite the significant downturn in our commercial aerospace business.

We also continue to fine-tune our portfolio during the year. As you know, we completed the acquisition of SEAKR Engineering and FlightAware, which will expand and enhance our capabilities in key growth areas, and we completed the divestitures of Forcepoint. And in December, we completed the sale of RIS' Global Training and Services business.

On the capital allocation front, we returned $5.3 billion to shareowners in 2021 for a total of $7.4 billion since we closed on the merger, well on track to the $20 billion-plus that we've committed to in the first four years after the merger.

As you saw in December, our Board of Directors also authorized a $6 billion share repurchase program, positioning us to continue returning significant capital to shareowners, including at least $2.5 billion of repurchases that we expect to complete in 2022.

In addition to our strong financial performance during the year, we also achieved several notable strategic and operational milestones that I'd like to highlight. Let me start with Collins Aerospace.

The business completed more than 750 Lean events in 2021. By utilizing our best practices from our core operating system, the team was able to reduce labor content on the F-18 heat exchanger by over 30%, reducing costs and importantly, creating capacity to support increased demand.

At Pratt, the team introduced the GTF Advantage engine, which reduces fuel consumption and CO2 emissions by a total of 17% compared to the prior generation engines. It extends the GTS lead as the most efficient power plant for the A320neo family. The engine will also be compatible with 100% sustainable aviation fuels, supporting the aviation industry's goal to significantly reduce emissions in the coming decades.

At both RIS and RMD, they achieved significant program milestones in the quarter ahead of schedule. Through strong program execution in RIS, the Joint Precision Approach and Landing System program completed delivery on the first LRIP units 60 days ahead of schedule. This achievement has given the Navy the confidence to certify JPALS on the CVN carrier and two amphibious ship classes.

RMD team also successfully completed the initial integration of the SPY-6 radar and the USS Jack Lucas in the quarter. This is the first time power simultaneously applied to the entire radar system, completing a critical milestone for integration of the ship, its combat system and the SPY-6 radar.

So with that, let me turn it over to Neil, and I'll come back at the end for a wrap up in Q&A. Neil?

Neil Mitchill

Thanks, Greg. I'm on Slide 3. I'm pleased with how we finished the year as well as our performance in the quarter where we continue to see solid growth in organic sales, adjusted earnings per share and free cash flow. Sales of $17 billion were in line with our expectations and were up 4% organically versus prior year on an adjusted basis. Our performance was primarily driven by the continued recovery of domestic short-haul international air travel, partially offset by continued supply chain pressures and lower 787 OE volume. It's worth noting that the global training and services divestiture at RIS closed in early December, resulting in a sales headwind of about $100 million versus our prior outlook.

Adjusted earnings per share of $1.08 was ahead of our expectations, primarily driven by commercial aftermarket strength at both Collins and Pratt as well as favorability in our effective tax rate. On a GAAP basis, EPS from continuing operations was $0.46 per share and included $0.62 of acquisition accounting adjustments and net significant and/or non-recurring items.

And finally, free cash flow of $2.2 billion was in line with our expectations and resulted in full year free cash flow of $5 billion, which was $500 million better than our expectations at the beginning of the year, primarily driven by higher net income and lower capex.

With that, let me hand it over to Jennifer to take you through the segment results, and I'll come back and share our thoughts on 2022. Jennifer?

Jennifer Reed

Thanks, Neil. Starting with Collins Aerospace on Slide 4. Sales were $4.9 billion in the quarter, up 13% on both an adjusted and organic basis, driven primarily by the continued recovery in commercial aerospace end markets. By channel, commercial aftermarket sales were up 47%, driven by a 59% increase in parts and repair, a 52% increase in provisioning and a 17% increase in modification and upgrades.

Sequentially, commercial aftermarket sales were up 10%, driven by strength in parts and repair. Commercial OE sales were up 4% with strength in narrow-body, offsetting headwinds from lower 787 deliveries. And military sales were down 3% on another tough compare. Recall, Collins military sales were up 7% organically in the same period last year. The decline in the quarter was driven primarily by lower F-35 volume.

Adjusted operating profit of $469 million was up $380 million from the prior year. Drop-through on higher commercial aftermarket sales, more than offset higher E&D and SG&A expense.

Shifting to Pratt & Whitney on Slide 5. Sales of $5.1 billion were up 14% on an adjusted basis and up 15% on an organic basis, driven primarily by the continued recovery of the commercial aerospace industry. Commercial OE sales were up 32% by higher GTF deliveries within Pratt's large commercial engine business as well as general aviation and biz jet platforms at Pratt Canada. Commercial aftermarket sales were up 28% in the quarter with legacy large commercial engine shop visits up 30% and Pratt Canada shop visits up 37%. Sequentially, commercial aftermarket sales were up 17%.

In the military business, sales were down 6% as expected on another difficult compare. Recall, Pratt's military sales were up 18% in the same period last year. The decrease in the quarter was driven by lower spare sales on legacy programs. Adjusted operating profit of $162 million was up $57 million from the prior year. Drop-through on higher commercial aftermarket sales volume more than offset lower military volume, higher SG&A, E&D and the impact of higher commercial OE volume.

Turning now to Slide 6. RIS sales of $3.9 billion were down 2% versus prior year on an adjusted basis and down 1% on an organic basis, reflecting four fewer workdays in the fourth quarter of 2021 versus the prior year. Adjusted operating profit in the quarter of $400 million was up $30 million versus prior year, primarily driven by higher net program efficiencies.

RIS had $3.4 billion of bookings in the quarter resulting in a book-to-bill of 0.97 and a backlog of $18 billion. In addition to the significant bookings that Greg discussed, RIS also booked $227 million for the next generation Jammer mid-band program in the quarter. RIS book-to-bill for the year was 1.01.

Turning now to Slide 7. RMD sales was $3.9 billion, down 10% on an adjusted basis and down 8% on an organic basis, primarily driven by four fewer workdays in the quarter, as well as lower material receipts and expected declines in several international production contracts. Adjusted operating profit of $486 million was $93 million lower than the prior year, driven by lower net program efficiencies and lower sales volume.

RMD's bookings in the quarter were approximately $3.2 billion, resulting in a book-to-bill of 0.83 and backlog of $29 billion. In addition to the SM2 bookings Greg mentioned, RMD also booked $269 million for Evolved Seasparrow Missile Block 2. RMD's book-to-bill for the year was 1.02. Before moving on, I would also like to comment on the previously disclosed DOJ investigation into cost accounting matters, at legacy Raytheon's Company's former Integrated Defense Systems business or IDS, which is now part of RMD.

As you will see in our upcoming 10-K filing, we have made progress in our internal investigation into the matter. And we now have determined that there is a probable risk of liabilities for damages, interest and penalties. In addition to the amount recorded in the first quarter of 2021 in connection with the finalization of purchase accounting, we recorded an incremental accrual in the amount of $147 million, during the fourth quarter relating to the matter, bringing our total reserve to approximately $290 million. We still do not currently believe the resolution of this matter will result in a material adverse impact to our financial condition, and we will continue to cooperate with the government's investigation.

With that, I'll turn it back to Neil to provide some color on the rest of the year.

Neil Mitchill

Thank you, Jennifer. I'm on Slide 8. Before I get into the specifics of our '22 financial outlook, let me give you some perspective on how we are thinking about the environment as we look ahead. Let me start with the positives. Despite the impact of COVID variance, we expect the commercial aerospace recovery will continue into 2022 with continued growth in commercial aftermarket and narrow-body OE deliveries driven by further strength in domestic traffic and growth in international traffic.

By the end of the year, we are assuming global RPMs recover to about 90% of 2019 levels with domestic travel recovering to be approximately in line with the 2019 levels and international travel recovering to between 75% and 80% of 2019 levels. The reopening of international borders, specifically in the Asia Pacific region and the related wide-body traffic will be a significant factor in the timing and extent of the related aftermarket recovery.

Ultimately, the timing and trajectory of the overall recovery this year isn't likely to be linear and it will depend on our customers' fleet decisions and buying behavior. Looking longer term, we continue to expect commercial traffic to return to 2019 levels by the end of next year.

On the defense side, we expect continued organic growth in 2022 as we deliver on our $63 billion backlog, continued bipartisan support for the fiscal 2022 defense budget, and international demand for our products and technologies.

And across RTX, we remain laser-focused on driving operational excellence to deliver cost reduction and further margin expansion, including $335 million of incremental RTX merger cost synergies during 2022. And this keeps us on track to achieve $1.5 billion in gross cost synergies by Q1 of 2024.

On the challenges side, we anticipate that global supply chain and inflation pressures will continue and that 787 build rates will remain low. With respect to the supply chain, we anticipate that COVID-related labor disruptions will persist through the first half of the year, but will ease through the second half of the year. And as we've discussed, a significant portion of our material spend is under long-term agreements.

That said, we are assuming a level of inflationary pressure across our businesses and our outlook that will be partially offset by productivity improvements. And of course, we're continuing to monitor the US and global tax environment and the current and potentially protracted continuing resolution.

So, with that backdrop, let me tell you how this translates to our financial outlook for the year. Let's turn to Slide 9. At the RTX level, we expect full year 2022 sales of between $68.5 billion and $69.5 billion. This represents organic growth of between 7% and 9% year-over-year. Keep in mind, the sale of RIS' global training and services businesses puts about $1 billion of sales headwind year-over-year as well as the associated profit.

From an earnings perspective, we expect adjusted EPS of $4.60 to $4.80, up 8% to 12% year-over-year. And we expect to generate free cash flow of about $6 billion. That's up about 20% versus 2021. It's important to note that this free cash flow outlook assumes that the legislation requiring R&D capitalization for tax purposes is deferred beyond 2022, which as we've said before, the free cash flow impact of this legislation is approximately $2 billion.

It's also worth noting that if the legislation is not deferred, you would see about a $0.10 EPS benefit as well from the impacts of the R&D capitalization that would have components of our US taxable income. And as Greg mentioned, we expect to buy back at least $2.5 billion of RTX shares over the year, subject to market conditions.

With that, let's move to Slide 10 for the segment outlooks. At Collins, we expect full year sales to be up low double-digits and adjusted operating profit to grow between $650 million and $800 million versus last year. This is primarily driven by higher narrow-body OE deliveries and growth across all three commercial aftermarket channels, supporting both narrow and wide-body aircraft. And military sales at Collins are expected to be up low single-digit for the year.

Turning to Pratt & Whitney, we see full year sales growing low double-digits versus prior year, principally driven by higher OE deliveries in both Pratt's large commercial engine and Pratt Canada businesses, as well as continued growth in legacy large commercial engine and Pratt Canada shop visits.

Military sales at Pratt are expected to be down mid-single-digit, driven by lower F135 production inputs partially offset by higher F135 sustainment volume.

With respect to operating profit, we see Pratt's adjusted operating profit growing between $500 million and $600 million versus last year, primarily on higher aftermarket volume and partially offset by higher large commercial OE engine deliveries and lower military volumes.

Turning to RIS. We expect full year sales to be down slightly versus prior year on a reported basis and to grow low single digit on an organic basis with strength coming from classified programs and production ramps in airborne ISR and EWS. And we expect year-over-year adjusted operating profit at RIS to be flat to up $50 million, driven by higher net program efficiencies and volume. At RMD, we see sales growing low single to mid-single digit, driven by growth across multiple programs and for adjusted operating profit to be up in the range of $150 million to $200 million versus prior year, driven by improved program performance and the volume. It's worth mentioning that we expect both RIS and RMD to again have a book-to-bill greater than 1.0 for the year.

And finally, we expect intercompany sales wins to grow in line with total company sales. I will note that we've included in our outlook some of the below-the-line items and pension in the webcast appendices.

So turning now to Slide 11 for our 2022 adjusted EPS walk. Starting with the segments, we expect the segments to generate about $0.83 of EPS growth at the midpoint of our outlook range. From there, pension will be a headwind, primarily due to lower CAS recovery and higher discount rates. Our tax rate in 2022 is expected to be between 18.5% and 19% versus the 15.5% in 2021, primarily due to one-time tax benefits associated with the prior year optimization of our legal entity and operating structure that we realized in the third quarter that will not repeat. This will result in a $0.19 headwind.

We expect corporate expenses to be a $0.06 headwind year-over-year due to higher investment related RTX synergy projects and digital transformation initiatives that are partially offset by lower LTAM spend. And finally, lower share count, interest and other items are expected to be a $0.07 tailwind. All of this brings us to our outlook range of $4.60 to $4.80 per share.

Now turning to free cash flow on Slide 12. We expect strong operational growth, along with lower restructuring to contribute about $1.5 billion of free cash flow growth in 2022. These will be partially offset by expected pension headwinds and higher cash taxes to get to our free cash flow outlook of about $6 billion. Again, this outlook assumes the legislation requiring RMD capitalization for tax purposes is deferred.

And lastly, before turning it back to Greg, a couple of comments on the first quarter. With respect to sales, we expect sales to be up mid-single digit organically versus prior year, driven by the continued commercial aerospace recovery and partially offset by lower defense sales driven by continuing supply chain pressures and the impact of Omicron.

And again, just to remind you, the prior year included Q1 sales of about $200 million as well as the associated profit for the divested RIS services business. On the adjusted

EPS side, we see low double-digit to mid-teens growth in the quarter versus prior year. And for cash, we expect to see an outflow of about $500 million in the quarter due to typical seasonal factors in the timing of collections.

So with that, let me hand it back to Greg to wrap things up.

Greg Hayes

Okay. Thanks, Neil. We're on Slide 13. So a lot of moving pieces as always. But I would tell you, we actually exited 2021 with really good momentum across the businesses. And we expect to make further progress on our priorities here as we enter into 2022. First and foremost, let me repeat that we're focused on keeping our employees safe, keeping our commercial customers flying and protecting the war fighter while they defend our country and allies and of course, supporting our suppliers.

We're also going to continue to invest in differentiated technology and innovation to maintain our industry-leading positions, which will drive growth over the long term, and of course, to capitalize on our growing end markets.

At the same time, our leadership team is making significant progress to reduce structural costs, drive operational efficiency through our core operating system and to deliver on our synergy commitments.

Finally, we remain disciplined with capital allocation. We have a very strong balance sheet, along with our cash-generating capabilities supports investments in our businesses and our commitment to returning capital to shareowners, including at least $20 billion in the first four years following the merger, as I said earlier.

I'm confident in our ability to deliver both top and bottom line growth and margin expansion across our businesses this year, as we continue to leverage the growth opportunities that are in front of us.

So with that, let's turn it over to Lisa, and we'll take whatever questions you might have. Thank you.

Question-and-Answer Session

Operator

[Operator Instructions] In the interest of time and to allow for broader participation, you’re asked to limit yourself to one question. The first question will come from the line of Sheila Kahyaoglu with Jefferies.

Sheila Kahyaoglu

Hi. Good morning, Greg, Neil, Jennifer. Thank you.

Greg Hayes

Good morning.

Sheila Kahyaoglu

So free cash flow is guided to $6 billion this year, up from $5 billion last year and 20% growth. And you have a pretty consistent cadence of free cash flow growth for your 2025 target of $10 billion despite pension headwind of $1.3 billion. Maybe if you could get into the different buckets and different impacts as we get into that 2025 $10 billion free cash flow number.

Neil Mitchill

Thanks, Sheila. Good morning. It's Neil here. As we think about the walk from where we are today to 2025, as we've said before, the majority of that is going to come from the operating profit growth that we'll see in the segments as we continue to go through the recovery here, probably a little bit north of $7 billion.

If you were to strike 2021 as a starting point, you'll see there's $1.6 billion of pension headwind. And we'll probably have somewhere in the range of $600 million to $700 million of CapEx headwind. And that will be partially offset by a couple of hundred million of corporate and other items. So still see a clear path to the $10 billion of free cash flow, as we get into 2025, and we get through the recovery here. Feeling very good about that.

Operator

Your next question comes from the line of Robert Stallard with Vertical Research.

Robert Stallard

Thanks so much. Good morning.

Greg Hayes

Hi, Rob.

Neil Mitchill

Good morning, Rob.

Robert Stallard

This might be a question for Greg. I was wondering if you could maybe give us some more color on the supply chain situation. Have things got any worse since what you experienced in Q4? And then in relation to that, how are you getting all the supply chain in place for the A320 ramp that's planned for this year? Thank you.

Greg Hayes

Yes, Rob, that's a really good question. And I think RTX, just like many other large companies, has seen its share of supply disruptions, I would say. And it's really -- I would bucket it in two different ways.

One is, in our supply chain, we see some labor shortages with skilled positions. And I can think of probably the most important one right now is in the casting -- castings, where we see a shortage of welders. And so, we're working with our suppliers to make sure that we can get demand or get supply back up to demand.

It's not going to happen here in the first quarter. We see that we're going to have a slow Q1, as Neil said, primarily at Pratt, that will also impact a little bit at Collins. We're also seeing, I think, as we talked about, a slowdown of receipts on the defense side of the business. We saw that in December. That's gotten a little bit worse than what we had seen at the end of the third quarter.

And I would say, again, there's two pieces to that. Obviously, the Omicron variant had a significant impact on our -- not just our workforce, but our suppliers' workforce. But also, again, the labor shortage that we're seeing as well as the need to continue to drive wages up to attract talent.

Just to put it in perspective, we've got about 13,000 product suppliers. We are monitoring the supply chain on a daily basis. There are less than 100, I would say out there that are giving us real concern, but it only takes one to make us miss a shipment. So we're actively trying to manage this. I think we're doing a good job, but we certainly will see some impact here in the first quarter from supply chain.

Operator

Your next question comes from the line of David Strauss with Barclays.

David Strauss

Thanks. Good morning, everyone.

Neil Mitchill

Good morning, David.

David Strauss

Greg, Neil, maybe could you touch on the moving pieces of the implied incremental margins at Collins and Pratt looks like Collins kind of in the mid-30s, Pratt in the mid-20s. I guess, on Collins, what you're assuming for E&D and kind of what's hitting the range that we might have expected? And then on Pratt, the negative engine margin that you're expecting in 2022 relative to 2021? Thanks.

Neil Mitchill

Thank you, David. Let me start with Collins. So you're right on the incrementals. We're expecting incrementals in that mid-30s percent range as we go through the year. Recall, we called out a few onetime items last year that probably helped margins by about 50 basis points. So good strong incrementals there.

Just hitting on a few of the components of our Collins outlook. We do expect that our commercial OE will be up sort of high teens on the sales line. Commercial aftermarket, up around 20% or so, probably a little north of that. And military, up low single digits.

As you think about Pratt, same thing. The incremental is there in the mid-20s, as you expect -- you said. Commercial OE, expected to be up between 20% and 25%. On the aftermarket side, also between 20% and 25%. And as we said, military, down mid-single digits. So again, great growth at Pratt. We do expect to ship probably about 200 more engines.

And as I think about the AEM headwind, it's in the range of $100 million to $150 million. So, we're seeing good absorption as we ramp that volume back up over the course of 2022. And as Greg said, the supply chain issues at Pratt with respect to castings could result in a little bit of lower deliveries here in the first quarter, but we do expect that full year, we will be up a couple of hundred engines.

Operator

Your next question comes from the line of Noah Poponak with Goldman Sachs.

Noah Poponak

Hi. Good morning, everyone.

Neil Mitchill

Good morning, Noah.

Noah Poponak

Could you spend another minute on sort of how you built the aerospace aftermarket forecast for the year and how you expect it to progress through the year? Obviously, when Omicron lets up, there's a huge question mark and there's a wide range of possible outcomes of where travel could be exiting the year versus starting the year. And Neil last year, you kind of framed what you were expecting for the broader ecosystem and then how you layered your own forecast on top of that and the degree of conservatism or lack thereof. So, it'd be helpful to hear that from you again today.

Neil Mitchill

Yes, Noah. Let me give that a shot here. So let me start with the macro outlook here. So we talked about our RPM and ASM assumptions as you get to the end of the year, but a little bit of color on the way we see that coming through the year.

So if you think about -- I'll start with ASM sequentially, sort of low single-digit sequential growth in the first quarter, hitting the mid-30s Q1 to Q2; Mid-teens, Q2 to Q3; and then actually down seasonally in the fourth quarter, mid-single digit, call it. So the crux of our outlook as we think about the year really depends on the wide-body recovery.

Last year, I would say about 75% of our aftermarket improvement and the improvement that we saw in ASMs came from domestic narrow-body. And this year, we're expecting about 80% of the growth to be driven by international long-haul and about 60% of that driven by long-haul routes. So it's going to be a really important factor as we look at the year.

If you think about how that translates to the aftermarket sales assumptions, the compares are getting a little bit more difficult sequentially given where we ended the fourth quarter. I would expect Collins to be in the low to mid-single digits sequentially on the aftermarket growth throughout the course of the year.

Pratt, we'll see down in the mid-single -- mid- to high single range here in the first quarter as we come off a traditionally high fourth quarter, and that goes to mid -- up -- I'll call it, high single digits second quarter and mid-single digits through the rest of the year. So hopefully, that helps give you a little color on what we're seeing. Greg, anything you want to add?

Greg Hayes

Yes. Noah, I think that the most important part just to reinforce what Neil said is really the -- our forecast for the aftermarket really is dependent upon a wide-body recovery. And as you know, that is primarily a Pacific reopening. So you have to see China reopening. We have to see all of the countries in the Pacific Rim start to reopen, which will allow traffic to recover.

Your guess is as good as mine with the China zero COVID policy that they have, whether or not we'll see that here in the second quarter or the third quarter or the fourth quarter. Right now, we're assuming in the second quarter, we start to see it. And we'll hopefully see that kind of progression throughout the year, which will get us back on track to give wide-body back to 2019 levels, hopefully by the end of 2023.

Operator

Your next question comes from the line of Peter Arment with Baird.

Peter Arment

Yes. Good morning, Greg, Neil, Jennifer. Hey, Greg, Maybe just switching over to defense. Could you maybe just give us a little bit of some of the things you're expecting for maybe on the international side, historically, Raytheon’s had a lot of international awards, what your expectations might be for a book-to-bill and if you're seeing any kind of increased input from international countries just given the rising tension? Thanks.

Greg Hayes

Yes, Peter, it's a good question. And I think the answer is, obviously, we are seeing, I would say, opportunities for international sales. We just have to look to last week where we saw the drone attack in the UAE, which attacked some of their facilities. And of course, the tensions in Eastern Europe, the tensions in the South China Sea, all of those things are putting pressure on some of the defense spending over there. So I fully expect we're going to see some benefit from it.

I would say, though, that should there be hostilities, whether it's in the Middle East or whether it's in the Asia Pacific region, you're not going to see an immediate benefit here because what you'll see is a reallocation of inventory that we already have out there with the services. But I fully expect we should see a recovery in the international defense maybe in the book-to-bill, well north of one as we move into 2022 and beyond.

One of the biggest drivers, of course, will be LTAMs. And I think, again, that's probably a 2023 benefit. We'll start to see bookings then for LTAMs, which, of course, is the upgrade of the Patriot Missile Defense system. But that will be, again, a couple of years out.

Neil Mitchill

Greg, maybe if I could just pile on a little bit, too. We do see some international Gem T awards at RMD. And as we look at the $29 billion backlog of RMD and the sales outlook that we put out there, which is low single-digit to mid-single-digit, think 3% to 4% or so year-over-year at RMD. We're confident that we have the backlog to continue to grow as we get through 2022.

Operator

Your next question comes from the line of Ron Epstein with Bank of America.

Ron Epstein

Hey, good morning. So, I guess, a question for both of you. A key part of the story is operational improvement as we walk out over the next couple of years, right? That's going to be a big cash flow driver. And a big part of that is GTF. So, a question we've been fielding from investors and maybe you can give us some perspective on this, how can we feel better about the long-term contracts you've put in place to do maintenance on the GTF family of engines, where it seems like time on weighing and the hot section maybe hasn't has performed like we were hoping it would at first. Meaning, how can we feel good that those contracts are priced right be it that they're kind of long-term in nature?

Greg Hayes

Let me take a shot at it, Ron, then I'll turn it over to the former CFO at Pratt to answer the actual contract question. Maybe just to put it in perspective, to-date, on the GTF program, we have had more than 12 million flight hours on that. In the last 12 months, dispatch reliability has been 99.96%. So, I know that we had a lot of teething problems back in 2016 and 2017, and we talked ad nauseam about all of those teething problems. And obviously, it impacted some of our time on wing, impacted some of those maintenance support contracts.

But given where we are from a reliability standpoint today, those programs will start to generate positive cash flow coming up as the first full shop visits happen in the next year and beyond. And I actually feel pretty good about where we are on those contracts given the robustness of the current engine.

Of course, in 2023, we're going to be delivering the advantage engine, which gives again better fuel burn and we think even more durability, which, again, will only benefit those aftermarket contracts.

Neil Mitchill

Yes. Thanks, Greg, I'll just add that the average age of those airplanes is still under three. There's plenty of time. These are long-term contracts. We've made significant improvements. You mentioned the durability improvements, and we are factoring that in, obviously, as we look at those contracts. And I would tell you that as we perform warranty-type work under these contracts today, we've been reasonably conservative in our outlook and our bookings on that.

So, we are confident that we're able to see the improvement fall through the bottom line as those major overhauls begin. And we're also confident that we're able to demonstrate significant efficiencies and fuel savings that come from that engine, and we're seeing that in the campaign activity that we're engaged in currently with the engine. So, feel well-positioned with the product and the GTF advantage, I think, only gets us in a better place as we go forward.

Ron Epstein

Great. Thank you.

Operator

Your next question comes from the line of Myles Walton with UBS.

Myles Walton

Thanks. Morning. Hey Greg, I was wondering if you could comment on the F-35 engine program progress through the course of 2021. And if you get to a better point towards the end in terms of resolving some of the issues that have been raised over the last 18 months, and importantly, as sort of the NDAA starts building momentum potentially towards opening the door to ATP and GE being second source in the later part of the decade?

Greg Hayes

Okay, Myles, it's a good question. And I would just say a couple of things that -- a couple of points I would make. First of all, we did make good progress on OEM deliveries last year. We were on contract as we exited the year for F1-35 deliveries. And we also made good progress, I would tell you, in the shops in terms of supporting the overhauls. I think we had about 80 overhauls of the power modules last year, which is double what we saw in 2020. That number is going to probably double again this year.

So again, we feel pretty good about the engine where it is today. Obviously, I think everybody that follows the program understands that you're going to need more power on that engine. You're going to need better fuel efficiency in that engine. And there are two different -- there are two choices, I think, in front of the services today. One is to do an upgrade of the current engine. We call that the EEP program, which is an enhanced version of the F1-35 or you could see a whole new engine, which would be the adaptive engine that both GE and Pratt are currently testing.

Of course, those engines are years away. We're talking late in this decade before you would ever see those on the aircraft. Frankly, what we think is, from a risk standpoint, a single-engine fighter, an upgrade of the current engine was probably the most cost effective, lowest risk solution. And again, I think that's something that we're working with the customer on. We think that is a much lower cost than the adaptive engines that we're developing. And the adaptive engines are really targeted for sixth-gen fighter, which again will probably not be fielded until the end of this decade.

So again, we've got options. We're working with the customer. The first and most important thing, of course, is to keep the engines that we've got out there flying. And so we're supporting the folks out in the shops around the world making sure that that happens and also continuing to drive OEM productions as we mature in the program.

Myles Walton

Thanks Greg.

Operator

Your next question comes from the line of Mike Maugeri with Wolfe Research.

Mike Maugeri

Hey, good morning. Thank you. Neil, on your cash flow guide, can you break your bridge between 2021 and 2022 down a bit further? Specifically, I'm curious to understand the $1.4 billion figure for operational growth in CapEx. If you can add some more color around working capital as well? Thank you.

Neil Mitchill

Yeah, sure. So a couple of comments there. The first thing is if you look at our segment profit guide at the midpoint, that's about $1.4 billion. So think about that being the major driver of that piece of our cash flow walk. And you'll see from our guidance about $400 million or so of capital expenditure headwind year-over-year. So the net of that.

That would imply a few hundred million dollars of working capital improvement. I think that remains to be determined as we see the year play out. So that will either turn into higher segment profit. As we get later into the year, if we are able to achieve the higher end of our range, and in particular, given the supply chain issues, we could see a little bit of working capital pressure as we bring inventory in a little bit sooner.

And again, the timing of that profit recognition and the timing of collections will all play out in the fourth quarter. But I would characterize those as the three key elements of that piece of our cash walk.

Mike Maugeri

Thank you.

Neil Mitchill

You're welcome.

Operator

Your next question comes from the line of Kristine Liwag with Morgan Stanley.

Kristine Liwag

Hey, good morning, everyone.

Neil Mitchill

Hey, Kristine.

Greg Hayes

Hey, Kristine.

Kristine Liwag

Greg, Neil, Jennifer, if we continue to see raw material and labor inflation at elevated levels for longer, how should we think about potential impact on margins? How much will you be able to pass-through with your contracts? And how much would the businesses have to absorb?

Greg Hayes

So let me start here. First of all, we have seen inflation, obviously, I think, like everybody else. It has been higher than what we expected, I would say, towards the end of last year. As we think about 2022, we've probably got about $150 million of, I would say, price pressure from unexpected inflation in the supply chain.

Now typically, we entered the year, and we'll see about $200 million or so of pricing pressure that we go out and we work to alleviate. I mean, the whole goal here is to keep input costs flat year-over-year. So we go out, we work cost reduction. This year, we got a little more work to do. That $150 million of inflation impact is baked into the guidance that Neil took you all through before. And it's something we're keeping an eye on.

The labor inflation, obviously, is also a little trouble. We're seeing it in our own shops. The good news is most of that, we can price it on the government side and pass that along to our customers. But again, there will be pressure. And what we have to do, of course, is figure out ways to continue to reduce costs. That's why we've got the core operating system to let us go out and find efficiencies in the factories so that we can get productivity to offset the continued pressure on wages.

But again, our hope here is that we're going to see inflation start to slow down here by the back half of this year. And we'll have to keep an eye on it. And again, I think it's everybody's concern across the country right now when you see 7% inflation, that's a big headline. And we've got to keep after it.

Kristine Liwag

Thank you for the color, guys.

Greg Hayes

Thanks, Kristine.

Operator

Your next question comes from the line of Robert Spingarn with Melius Research.

Robert Spingarn

Greg, last week, Secretary of the Air Force, Frank Kendall, was talking about hypersonic strategy and suggesting that maybe because our targets are different than China is we need to rethink the strategy, boost glide versus air breathing. And I wanted to ask you your thoughts on this and how this might change the dynamic between Lockheed on the Boost Glide side and Raytheon on the cruise missile side?

Greg Hayes

Yes, that's -- that is a great question, and one I think that we're all wrestling with right now. And I would tell you there is – I would say, several different markets here. Obviously, the Boost Glide is an interesting market as we saw the Chinese demonstrate that capability.

We've also -- of course, we've demonstrated our capability to launch a air breathing, which is the hypersonic missile that we did the test on late last year. I think both of those technologies are going to be funded going forward. I think most importantly, however, is what are going to be the defensive systems against hypersonics. And again, I think those are the things that will provide us the biggest opportunity, whether that's going to be directed energy, some anti-hypersonic glide vehicles things that we're working on. There's a lot of money being devoted to this. Unfortunately, most of it, as you can imagine, is classified. We really can't go into what those individual technologies are.

But I would tell you that, any defense would be a layered defense where you'd be using ground-based effectors, you'd be using ship-based effectors as well as potentially directed energy. And we're going to continue to work on that with the Air Force this year. And we'll hopefully have some interesting opportunities as the year unfolds.

Robert Spingarn

Okay. And just a quick one for Neil, if I'm still here. Neil, I was wondering if you could clarify, maybe I didn't catch it. If there's a full year CR, what would the sensitivity be in the guidance?

Neil Mitchill

That's a good question. I didn't put that out there. But couple of pieces here. First, that will expire or set to expire February 18 of this quarter. It will see a lot of impact through the first quarter, if that were to extend through March 31, maybe $50 million to $100 million, $150 million of sales.

If it were to persist through the full year, I would see probably between $500 million and $600 million of sales headwind. So I think that underscores the importance of us getting the continuing resolution behind the country.

But, yes, that's how I would size it up looking at it today. And I would say that would be relatively evenly spread across our businesses, frankly. Each one of them will have some headwind as it relates to a continuing resolution that persists through the year.

Robert Spingarn

Okay. Thanks so much.

Neil Mitchill

You bet.

Operator

Your next question comes from the line of Cai von Rumohr with Cowen.

Cai von Rumohr

Yes. Thanks so much. So there's a fair amount of debate on the profile of recovery in deliveries and production of the 737 and the 787. Could you tell us approximately where your rates are today and the type of profile you're looking for in 2022 and what you've baked into your 2022 guide?

Neil Mitchill

Thanks, Cai. Good morning. Let me give you a couple of thoughts there. I don't want to get ahead of Airbus and Boeing, obviously, but let me start with the 737. Obviously, we ended the year sort of in the high teens per month range.

We are aligned with Boeing in terms of that growing to that rate 31 in the second half of the year. So I'll leave it at that for now, but we do see obviously growth there in the back half of the year and it kind of gradually grows through the first half.

On the 787, as we talked about it last call, we had -- we were shipping very, very little, if any, on the 787. We ended the year in the, call it, low single-digit per month shipset rate. We are anticipating that same type of rate through 2022. Because of inventory that is in the channel, I think a good estimate would be about two per month as you think about the full year for 2022.

Cai von Rumohr

Thank you very much.

Neil Mitchill

You're welcome.

Operator

Your next question comes from the line of Seth Seifman with JPMorgan.

Seth Seifman

Hey. Thanks very much and good morning.

Greg Hayes

Hi, Seth.

Neil Mitchill

Hi, Seth.

Seth Seifman

I guess, Neil, when you spoke, I think, back in November and kind of talked about the outlook for the segments for the year, did that change very much? I'm thinking specifically about the progression of the aftermarket recovery?

Did that change very much as a result of the emergence of Omicron? And, I guess, is there any kind of information or new information kind of underlying a level of confidence that you have about the international travel recovery this year?

Neil Mitchill

Yes. Let me start with the first point. So a couple of things have definitely changed since that early November time frame. And I'd say, the first was the variant Omicron clearly came on quick. We hope that it will go away quickly as well. But I think we've factored some of that thinking into the first quarter. As I look at today's outlook relative to where we were thinking a few months ago, we see a little bit slower recovery in the first quarter than we were thinking, but we do see that getting back to where sort of the line we were projecting from Q2 and beyond. So we'll see how that plays out.

Again, I said last year, a lot of this depends on airlines getting ready for the summer travel season. So, we are expecting to see an uptick in their behavior for provisioning and parts here in March and April, which sort of gets to your second question there in terms of the support underlying -- the reopening of international borders. We have seen reopenings of some international borders in the fourth quarter, and that's encouraging, in particular, Europe.

And as Greg mentioned earlier, the key, I think to us realizing what we've laid out here today is Asia Pacific opening up and the long-haul routes coming back in earnest as we get towards the end of the year here. So we'll have to wait and see. But certainly, sometime in the March and April timeframe is when we would expect to see an uptick that would drive the ranges that we're predicting here for Collins in particular.

Seth Seifman

Great. Thanks Neil.

Neil Mitchill

Welcome.

Operator

Your next question comes from the line of Matt Akers with Wells Fargo.

Matt Akers

Hey good morning, guys. I was wondering if you could just comment on the new Ashville facility. And I guess, specifically, how far are we sort of through the investment there? And how do you think of sort of the ramp-up of production at that facility?

Neil Mitchill

Make great progress there in Asheville. The building is up. And when I was looking at it the other day, actually I have visibility to that via webcam. And it's in great shape, so we're on track. Some of the CapEx favorability that we saw here in 2021 is the deferral of some of that spend into 2022. But I'd say, we're on-track there to stand up that facility and get the production going as we had planned to do. So it's really a good shape.

Matt Akers

Great. Thanks.

Neil Mitchill

Welcome.

Operator

Your next question comes from the line of Doug Harned with Bernstein.

Doug Harned

Good morning. Thank you.

Neil Mitchill

Good morning.

Doug Harned

I'd like to go back to the geared turbofan and the aftermarket outlook. You've been delivering your turbofans now for about six years. And if we go back to the earlier days of the design, one of the big advantages was going to be because of the year, you have fewer stages and in principle, lower maintenance costs. So that -- the thinking was, as I understood it back then, that could lead to higher margins in the aftermarket as you go forward. First, do you still see it that way? And if so, when should we see margins in the aftermarket for the GTF gets to the levels we've seen on the V2500?

Greg Hayes

Doug, that's an interesting question. Obviously, when we originally -- the original design of GTF, there were a couple of different priorities. One, obviously, was fuel burn. That was a 15% benefit over the V2500. We clearly achieved that. What we did not achieve, I would say, in the first few years of delivery was a robust engine.

We had teething problems, as we've talked about, primarily around the combustor and primarily in some of the more difficult environment environments like India. And so of course, that impacted the aftermarket as we brought those engines back sometimes within a year or two of shipping them to update the combustor.

Right now, I would tell you the combustors there are lasting at least 10,000 hours now, which is good news. And we're starting to see that already in these -- in the aftermarket contracts.

As you said though -- as Neil said before, the average age is only about three years on these GTFs. So, we're not seeing the overhaul activity in a significant number yet, but we will in the coming two or three years. And I think you'll start to see margins improve in the aftermarket once we start going through and doing the heavier overhauls.

Will they ever get to the same level of profitability as the V2500? Absolutely. It's just going to -- keep in mind, the V2500 has been out there for 30 years. It's not a brand-new engine. It's a very, very durable engine. And it's just it will take us time to get the number of engines out there to drive the kind of efficiencies in the aftermarket. But we fully expect. It's a great design. It gives the fuel burn, and it does, to your earlier point, have fewer moving parts, right about 1,500 fewer blades than the competing engines and that should and will reduce costs over the long-term.

Doug Harned

Very good. Thank you.

Operator

This does conclude our question-and-answer session. I would now like to turn the call back over to Mr. Greg Hayes for closing remarks.

Greg Hayes

Thank you, Lisa and thanks everybody for listening in today. Again, a lot of moving pieces, but we have high confidence in the outlook that Neil and Jennifer took you guys through. Look forward to hearing from many of you in the coming days and weeks. Jennifer and the team will be, of course, available all day today and tomorrow to take whatever follow-up questions you might have. Have a wonderful day and stay healthy. Thank you.