

# **AB Volvo (publ) (VLVLY) Q2 2024 Earnings Call Transcript**

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**Body**

AB Volvo (publ) (VLVLY)

Q2 2024 Earnings Conference Call

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Company Participants

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Martin Lundstedt - Chief Executive Officer

Mats Backman - Chief Financial Officer

Conference Call Participants

Hampus Engellau - Handelsbanken

Olof Cederholm - ABG Sundal Collier

Klas Bergelind - Citibank

Miguel Borrega - Paribas BNP

Agnieszka Vilela - Nordea Markets

Virginia Montorsi - Bank of America

José Asumendi - JPMorgan

Daniela Costa - Goldman Sachs

Nicolai Kempf - Deutsche Bank

Björn Enarson - Danske Bank

Erik Golrang - SEB

Presentation

Johan Bartler

Welcome to the Volvo Group Second Quarter Report. Today, we'll do, as always, we'll listen to the presentation from our CEO and CFO, Martin and Mats; and then, follow up with our Q&A session.

So with that, I hand over to you, Martin.

Martin Lundstedt

Thank you, Johan, and also welcome from my side. So as we conclude now, the second quarter of 2024, I would like to start by thanking all colleagues, business partners and, of course, customers for a continuous very good cooperation during this quarter as well in very challenging conditions, a lot of moving parameters, the close and trustful relations are more important than ever. So thanks for that.

And also when it comes to the business side, as expected and following the trend we have seen for a while now, demand continued to normalize across many of Volvo Group's major markets during the second quarter. But still despite lower sales, we did see -- or volumes, I should say, we did see sales coming in on the same level as last year, also with strong operating income and strong operating margin, also posted a number of records when it comes to return on capital employed and earnings per share.

Operationally, as a company, we are continuing to focus on being extremely close to our customers. Of course, the service operation also to continue to execute on price and commercial realization, flexibility in our industrial system and continuous tight cost control but we are also manoeuvring from a position of strength. In times when transformation in different shapes and forms are more important than ever, we are continuing to pursue also a very strong agenda, a strong investment and activity agenda when it comes to research and development, launches of new products and services, not at least also during this quarter as well as digitalization as some examples. And that is, of course, to execute here and now but also to make sure that we are competitive for the future.

So if we summarize a number of the highlights for quarter one, starting then with sales on par with last year at SEK140 billion. Adjusted operating income of SEK19.4 billion with a margin of almost 14% at 13.9%. Operating cash flow was SEK9.1 billion in quarter two which brought also the financial position in our industrial operation to a level of SEK59.3 billion, almost on par with last year. We also -- as I said, posted 2 records, a return on capital employed exceeded 40% for industrial operations increased to 41.3% and also when it comes to earnings per share, that rose to 7.65. So all in all, we summarize another strong result. And again, I would like to thank everyone involved for the achievements.

Then when we go to volumes on the back of the normalized demand, our truck deliveries softened by 8% to 58,900 vehicles and we are continuing to adapt our operations to the normalized demands in steps and you will hear us talk more about that today, both me and Mats here.

Also, Construction Equipment deliveries continued to normalize and softened 10% with Europe and North America down while China showed signs of bottoming out now after rather major corrections over the last quarters and years here. So for both trucks and DCE, it was a good job done, continue to work with the flexibility tools that we have in the group and to gradually and firm just to the different demands in different regions.

Electrification, underlying electric demand is slowing down currently. And the switch over to zero emission transport is still driven by early adopters. In quarter one; booked orders were down 16%, compared to last year. But we regard this as mid or short-term temporary mainly related to uncertainty in the general economy, interest rates incentives but also when it comes to energy prices and infrastructure availability and those components must continue to come together in order to really ramp up here.

Deliveries on the other hand, increased with 52% but the broad adoption at scale will happen when enabling conditions are coming in place in a broader sense. We now have equipment available when it comes to the machines, when it comes to the trucks, when it comes to the buses but customers are still a bit hesitant before they know how exactly, for example, TCO will play out in relation to current powertrains in relation to the future powertrains but also and maybe more and more important also infrastructure availability, both availability of different charging stations but also when it comes to grid capacity and energy availability.

But with that said, we are first out in our core markets and pushing the envelope here. 7 out of 10 trucks in Europe are coming from the Volvo Group still from Volvo Group but we are building a lot of knowledge. We are building a lot of relations with our customers. But we will continue also to be clear for society in the ecosystem as a whole that this is a coordinated effort to make it happen. And even if there is a short-term hesitation, we all know both from a business perspective but also from a societal perspective that we need to deliver on these targets in order to be truly sustainable moving forward.

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Coming to the sales figures and then starting with equipment sales on the back of continuing price carryover. From 2023 vehicle sales remained at high level in quarter two. Group vehicle sales, excluding currency, was down with 2%. Truck sales growing with 2% despite the lower volumes. Construction Equipment, down 19% primarily due to lower volumes in Europe and North America. Volvo Buses, higher deliveries at higher value, gave a vehicle growth of 22% and Penta had lower sales of minus 7% and especially in the Marine segment.

We continue also our focus to grow services and had a 5% growth year-over-year for the second quarter, adjusted for currency. Rolling 12 months, service sales exceeded SEK130 billion. All business areas are growing during the quarter, mainly driven by improved commercial conditions. Efforts to increase service contract penetration and other services are also paying off step by step. Specifically in this quarter, the solid service growth for buses was mainly driven by more coach activities. And VFS service growth was supported by the higher interest rates and the continued good penetration.

When it comes to group news, Volvo Group and Daimler Truck, we share this ambition to lead now the transformation and implementation of software-defined heavy-duty commercial vehicles which will enhance customer efficiency, customer experience and also enable a more swift and solid transition into sustainable solutions. And building from that Volvo and Daimler announced during the quarter the intention to form a joint venture for software or software-defined vehicle platform, of course, still subject to necessary approvals from authorities.

And just after the end of the second quarter on July 2, the divestment of Arquus to John Cockerill of Belgium was completed. And this was another step of pruning the Volvo Group's business portfolio and at the same time, giving Arquus and the colleagues of Arquus a good home for their future development. And we thank all of them for a great job done within the Volvo Group.

When it comes to truck news, we are also in order to complete our road map for fossil-free solutions when it comes to powertrains, developing hydrogen powered combustion engine trucks. As can be seen in this picture, you see a part of the execution and not the details with injectors, etcetera. But on road test with trucks with using hydrogen from combustion will start in 2026 and we intend them to have a commercial launch at the end of this decade.

And to further support this development, the joint venture together with the Westport Fuel Systems and Volvo Group is now operational. Also Renault Trucks is moving ahead decarbonizes its intrafactory logistics first stage involves the electrification of transport between their Bourg en Bresse and Lyon facilities. And in the quarter, the strategic alliance with Isuzu Motors took another important step when Volvo and Isuzu agreed to leverage Volvo technology also into Isuzu branded not only from Isuzu UD branded products in the coming years.

When it comes to market forecast, starting in North America, we are reiterating our forecast from last quarter for this year, 290,000 units and that is a correction of approximately 12% in relation to '23. For Europe, we are also reiterating the correction but we are making a small adjustment upwards to 290,000 from 280,000 that we had as a forecast in last -- in quarter one and that means that we see a correction of around 15% in relation to quarter -- to 2023. Brazil, slightly upwards, another correction with upwards with 5% up to 100,000 total market. India unchanged but we are also correcting China downwards with another 50,000 units down to 750,000.

When it comes to book-to-bill, globally and this is medium and heavy-duty trucks since that is more, I mean, the complete value chain that we are sitting on. Book-to-bill improved to 87% as the European manufacturing system was further and swiftly adjusted during the second quarter. Book-to-bill 12 months rolling was 84%. And the total heavy-duty order intake for the quarter improved with 11% year-over-year. And in Europe, book-to-bill for medium and heavy-duty was 87% as same as the global figure.

In North America, we have mainly delivered out from the big order backlog that we have had. So book-to-bill was weak even though the orders were improving year-over-year with 12%, mainly then related to Mack. We did see a continued good momentum in South America with a book-to-bill 142% and Asia was in good balance in the quarter.

Then when it comes to truck market shares and we can start in Europe. Volvo and Renault are on a combined level of the total market of 26% and at 72% on battery electric vehicles. And in North America, the 2 brands, Mack and Volvo have rebounded and had a combined market share of 17.6% for the first months. Good performance in Brazil, a market share of almost 23% and the same goes for Australia with a combined market share for Volvo and Mack of 26%.

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Then moving into construction equipment, a lot of big news also here during the quarter, showing that we are, of course, forward-leaning when it comes to the introduction of new products and services. As a matter of fact, Volvo CE unveiled during what they call the Volvo days, well attended with customers and media in soon the biggest product to renewal launch ever during this well attended event.

And what you can see on the slide here is also the 12-ton wheel loader, fully electric. And you can also below see a full lineup of a lot of different news. For example, among the news, a complete range of excavators between 14 and 50 tons were launched. And also, we are continuing to invest in VCE for the preparation of different type of powertrains in [indiscernible], for example, investments are ongoing to host.

Market forecast-wise, slight adjustments. I mean, we -- the continuous normalization and correction in our main markets are more or less on expected levels as we already communicated in quarter one but we are making 2 corrections. We are taking down Europe to minus 20% in relation to '23 as a midpoint and that is a correction down with 5 percentage points. And the same goes for Latin America or South America, where we are now expecting flat market in relation to 2023. And also there, it's a correction down with 5 percentage points for in relation to quarter one forecast.

For book-to-bill orders and deliveries, the overall book-to-bill of VCE was 89% in quarter one and 87% 12-month rolling. In Europe, we had a book-to-bill of 65% and we have been adjusting pretty heavy downwards there now. Dealer inventories need further reduction and hence, we have reduced production accordingly and work with flexibility tools to balance with the order intake.

And in North America, book-to-bill is 75% as the market is also softening but from high levels, dealer inventories are somewhat elevated, both in Europe and in Latin America and we are having a very close watch on that, obviously. But we are also showing with the flexibility of the tools that we can manage that in a good way. In South America, book-to-bill was down to 73% but it should see also on the back of a very strong first quarter. If you look at the 12 months rolling, it is in good balance 96% and that goes also for Asia, Africa and Oceania that were on basically 100%.

Volvo Buses, a strong quarter, strong structural improvements. If we start with the news, buses continued to introduce new smart safety systems which support the drivers and bring also more safety features for other surrounding people, not at least vulnerable road users, so a very important element for passenger transport. And the restructuring program and the introduction of new and partly -- modified and partly new business model in Europe is progressing well and supports a structurally improved profitability for Volvo Buses moving forward.

Book-to-bill was 84% in the quarter and 93% 12 months rolling. Here, it should be said that the order book is really full and Volvo Buses for the time being selective in placing orders since the order book is full for the year.

Penta then, on the news side, a lot of interesting development. Maybe some of you did see the field just before the press release -- press conference started here. We have developed a fully electrified rural factor, of course, an application with high potential in partnership with the Belgian company Mall and the first unit is now operational in the DFT's terminals in Ghent, good feedback there.

In addition and also related to applications where electrification is well suited has retrofitted also a conventional crew vessel on the marine side with fully electric propulsion system installed with the inboard performance system that's called IPS system. And this is the first ever Volvo Penta IPS powered 100% by batteries and with no onboard diesel generators. And that is a really robust, sustainable and energy-efficient solution. Book-to-bill 76% in the quarter and 84% for 12-month rolling. And also here, we are adapting our capacity as customers and especially in Marine are destocking on the back of softer demand.

Finally, when it comes to business update, VFS, Volvo Financial Services, good portfolio growth across most markets. The increase in the overall portfolio is related both to growth in the retail as well as in the dealer portfolios. Penetration level were good in a competitive marketplace. The 12-month rolling penetration was 28% end of June. And VFS had stable performance and good earnings. The portfolio performance continued to be at an overall good level, although a return to more average business cycle conditions and behaviors are visible.

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So that is the business update, Johan. And I'll leave back to over to you.

Johan Bartler

Thank you, Martin, for the business update. Then we will start to take a look at the financial update from our CFO, Mats.

Mats Backman

Thank you, Johan. Before getting into all the details, maybe a brief summary and a couple of highlights on the second quarter. Overall, we continue to have a strong financial performance. Operating income and margin were on a high level and this is despite the lower volumes we see mainly in Europe.

Operating cash flow in industrial operations was strong and we wanted new records for return on capital employed being above 41% and our earnings per share being at SEK7.65, a quite strong number. While we keep investing in transformation activities, we got a good balance in our performance as well. Price realization mainly driven by price carryovers from 2023, offset the underlying cost inflation and was together with increased productivity key to deliver all-time high gross income margin for the quarter at 28.5%. We expanded our service sales and for the first time, reaching SEK33 billion in the quarter and we continue to address production capacity and cost levels to balance the normalizing demand in Europe.

Our trucks industrial system in Europe is now balanced with the current demand. We also continue to work on our inventory levels. Second quarter showed a slight buildup of inventories but comparing to last year, we had almost SEK4 billion less inventory built up. Focus going forward will be to reduce the overall inventory levels in the second half of the year, with positive impact on the group's cash flow. And in parallel, as Martin mentioned, we continue to invest in our future to execute on the transformation agenda. So all in all, another strong quarter with a high activity level.

Looking into some details then and starting with the net sales. Adjusted for currency movements, net sales were on the same level as second quarter last year. We keep seeing a weakening demand in Europe, with sales down almost 5% FX adjusted. The decrease is driven by lower volumes, mainly in construction equipment but also visible on trucks, however, to a lower extent. South America is showing a strong comeback after the downturn last year, mainly driven by group truck sales. And in Asia, we see some contraction in both trucks and machines.

Moving to the adjusted operating income. The adjusted operating income for the group was SEK19.4 billion with an adjusted operating margin of 13.9%. On gross income, we continue to be successful with price realization, both for vehicles and services which together with a lower freight cost contributed positively to the improvements we saw year-over-year. This was, however, partly offset by lower volumes and negative brand and market mix within Construction Equipment.

The January inflation and salary increases were negatively affecting the operating expenses and we are also investing in the transformation for zero emission vehicles and autonomous vehicles and this is reflected in higher activities and thereby increasing R&D and selling expenses. The net capitalization effect in the quarter was negative with some SEK600 million compared to last year. The full year impact on current year is expected to be about SEK1 billion positive for net capitalization. And that would represent a negative deviation versus last year of about SEK1 billion.

FX a small positive impact of some SEK200 million in the quarter and we expect the effect from the transaction exposure to be neutral for the full year '24. And we don't give any guidance on the full FX effect on earnings.

Moving over to the cash flow. We delivered a consistent and stable cash flow during the second quarter. While inventory went slightly up, the strong earnings were the main contributor to reach SEK9.1 billion in operating cash flow. Thanks to the strong performance and our efficient balance sheet, the return on capital employed improved to 41.3% on a rolling 12-month basis. Net financial position remains solid at SEK59.3 billion being impacted by the positive operating cash flow and by the dividend distribution of SEK36.6 billion in the beginning of the quarter.

Then looking at the different segments and starting with the trucks. The increased FX adjusted net sales for group trucks of 2% on lower volumes were driven by positive price effect and product mix. The higher adjusted operating income and adjusted operating margin was mainly driven by price realization of vehicles as well as service, lower freight cost and a positive product mix. This was achieved despite the lower volumes, especially in Europe and the cost inflation. We also saw increasing investments in the transformation impacting the level of R&D and FX was neutral in the second quarter.

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Moving over to Construction Equipment. FX adjusted net sales decreased 16% due to lower volumes and negative brand and market mix. Adjusted operating income decreased with SEK1.5 billion to SEK3.9 billion. Higher prices on both new vehicles and parts together with lower material costs and R&D expenses were offset by negative mix from more volumes in China and less volumes in North America and Europe. Adjusted operating income margin reached 15.9% and there was no impact on earnings from currencies.

Moving down to buses. FX adjusted net sales increased with 19%, mainly driven by strong price realization and volume. Adjusted operating income increased with SEK335 million to SEK554 million, driven by price, volume and market mix, partly offset by supply disturbances which had a negative impact.

Adjusted operating income margin increased to 8.5%, representing a record level for the second quarter. Currencies had no material impact on the results. And then looking into Volvo Penta, driven by lower volumes, FX adjusted net sales decreased 3% to SEK5.2 billion. Adjusted operating income increased to SEK1 billion due to strong price realization and a positive product mix, slightly offset by the impact of reduced volumes and higher R&D expenses.

Adjusted operating margin came in at 19.5% and there was no material FX impact in the quarter. And then last but not least, looking into financial services. The credit portfolio increased to SEK271 billion with a rolling 12-month return on equity at 13.6%. Return on equity peaked in late 2021 and early 2022 due to the gradual release of the COVID resurge and the strong price realization achieved during the pandemic and is now starting to normalize to the target range of 12% to 15%. Customer financials and payments continue to be good, reflected in relatively low write-offs and credit provisions. Adjusted operating income increased to more than SEK1 billion and FX had a positive effect of SEK77 million in the quarter.

So with that, I'm handing back to Johan.

Johan Bartler

Thank you for that, Mats. So taking a holistic view, I would like to summarize the second quarter. Martin?

Martin Lundstedt

I think most have been said already but maybe to take a step back and talk a little bit about, I mean, all the moving different parameters that we see. We have a correction in the market. We are following that smoothly. We are adjusting accordingly. We are showing that we have flexibility in the system. And often, when we talk about a quarter, we are talking in financial terms about carryovers and I mean, what leverage do you have and utilizing a number of different vocabularies. But reality is that the job needs to be done. And the job has been done in a fantastic way by our colleagues but also by business partners. And we see that in the underlying business here, a strong gross margin, strong flexibility and not sacrificing the quality of the business, while we are continuing to invest for the future for sustainable solutions, safe solutions knowing that infrastructure, transport logistics will continue to increase.

Johan Bartler

Very well. Thank you. So well, very soon start with the Q&A session. But just before that, we will also remind you about the Capital Market Day coming up in November. So please reach out to us in Investor Relations, so we can book you in.

So with that, we move over to the Q&A session. We kindly ask you to try to limit yourself to 1 question. And first out today is Hampus Engellau from Handelsbanken.

Question-and-Answer Session

Q - Hampus Engellau

I would like to -- if you could maybe talk a little bit about this Westport collaboration and hydrogen in combustion engines. How -- in terms of cost for this product, if you would compare it with fuel cell trucks which I presume would be quite expensive. If this is more a price attractive alternative? And if you would compare that to a normal combustion engine trucks? And then if you could just give a comment on when you would reduce run rate in North America or if that has already happened? That's 1.5 questions, sorry.

Martin Lundstedt

Thank you, Hampus, for those questions. And a little bit coming back then to Johan, maybe also to have that as a cliff hanger, I think we will go more into depth regarding your first question in November then when we have the Capital Markets Day. So that is also, I think, giving certain level of attractiveness to attend. But having said that, I should say, generally speaking, you are right. But you need to look into the complete, so to speak, TCU equation and also revenue equation. And that's the reason why we -- all the time in Volvo has been very clear that the future transformation will consist of a number of different technologies running in parallel.

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And when we have talked about the combustion engine technologies, we have always been clear that, that will be a part of this equation, together with fuel cell electric and battery electric. And the reason for that is obviously that depending on application, depending on geography and depending on legal requirements, notably in cities where it's not only about the CO2 reduction but also about particulates and NOx reductions, etcetera. We will need to have that portfolio to comply to cope with it. The smart piece is that we really can utilize, so to speak, the modular setup for trucks but then leverage that also for buses, for construction equipment and also for our business partners as we see now, for example, providing components to Isuzu Group, etcetera. So the question is rather broad because the answer on price points, cost points will depend very much on applications.

The name of the game to reach that is to have a technology that is scalable while still flexible and that you can actually combine that in the industrial system and there we have the right type of formula. But more on those details. But it will be an important component because the Westport joint venture is both about future hydrogen but it's also a very important component already today when it comes to liquefied natural gas but even more important for the mitigation activities liquefied biogas where we have a very competitive and fuel-efficient solution for long haul already today.

Then when it comes to U.S., we have as you have also maybe noticed, seen a good development when it comes to our market shares in quarter two. We have a strong offering and we have been limited by our own industrial capabilities over '23 and into quarter one. But as we have seen for Europe, we will be very clear on demand and swiftly doing so when it's required. But we have not done any bigger changes so far but when that will be required. And that is, of course, the balance with the current demand going forward and how we look into 2025, given also that we know that in '27. We have a new legal requirement coming in. So being very close to that, as we have been doing in Europe is name of the game.

Johan Bartler

Very well. Thank you for that. Then we move over to Jefferies and Michael [ph].

Unidentified Analyst

Just one on customer utilization. You mentioned that it's at good levels. Could you just give us a bit more color there, maybe what you're seeing as the year progresses in Europe or any other details you can provide on how your truck customers operating environment is evolving?

Martin Lundstedt

Thanks, Michael. Yes, we have said and I also said it in some interviews here that still, we feel that utilization level is holding up well. Of course, what we see is certain corrections in certain segments and that is really related to also how does consumption pattern look like and how does industrial pattern looks like for different sectors. But generally speaking, we feel that the utilization level is holding up. There is a certain drop of a couple of percentage points but no drama. Then obviously, how will that play out now a little bit longer will also, of course, relate to the common truck demand but no dramatic changes to what we have seen before. I don't know if you would like to add something on that.

Mats Backman

I think well on.

Johan Bartler

Good. Then we move over to ABG. Please go ahead, Olof Cederholm.

Olof Cederholm

I'd like to talk a little bit about the backlog versus new orders. How should we think about the lead times now in in trucks and construction equipment in particular. Is there any support from backlogs in these businesses when we go into the second half of the year? Or is sort of the Q2 order intake, the basis for volumes in the second half?

Martin Lundstedt

If I start then, as we -- a little bit already said in quarter one, we are starting to see now that we are coming back to more normalized order levels. And -- and that's the reason also what we have been clear or not at least and in Europe that we have been adapting step-by-step starting at the end of last year and then in a number of steps in quarter one and quarter two. In relation to the quarter one report, we said that we should be in balancing during quarter two and we are that also now for Europe. So you can say, normal lead times when it comes to the order backlog with maybe then the exception of Latin America, where we have had a very good order intake and that the order backlog has built up and we are adjusting upwards. And the same goes also for Mack in North America where we still have a prolonged order backlog given the fact that they are positively exposed to segments that are still running very strong and also still some, so to speak, carryover effects on the backlog related to the strike that we had during the fall. But generally, a good balance and now it is, so to speak, the handcraft of adapting to the current demand. And you see that also in the book-to-build on heavy-duty, medium duty that it's coming up and we are getting to that balance. I don't know. Mats?

Mats Backman

Maybe to stress a little bit looking at Europe and the situation in Europe with the normalized lead times that you talked about, so -- and relating that to the capacity and the capacity utilization internally as well. I mean we started the adjustments in Europe already in November and then we have done it gradually throughout the first quarter and becoming in balance than in the second quarter. So we are kind of fully balance when it comes to the capacity and the demand situation which I think is good then. And I think it's also kind of due to the good deliveries we had already in the fourth quarter in Europe, giving us the visibility then to take quick actions and not having this kind of long order stock done. So I think the organization have managed that in a great way.

Johan Bartler

We move over to Citibank and Klas Bergelind.

Klas Bergelind

I have a couple of questions. My first one is on discounting on fleet orders. We're hearing that this is increasing; obviously, we can't see this in the P&L today. But given short lead times now, this could perhaps weigh on pricing here into the second half, maybe even into the third quarter. Would you say, Martin, that the discounting towards fleet are increasing now versus what you saw early in the year?

Martin Lundstedt

I mean, Mats, I think you can complement as well later on but I should not call it discounting because -- I mean, in that regard, it's more about, I mean, how can mix evolve temporarily between different quarters, depending on who are in the market quarter-by-quarter. But in my book and what we see now, it's not the discounting, it's more in that case, so to speak, customer mix effect.

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And that might be a little bit more visible given the fact that the fleets are more recurrent, more planning when it comes to their replacement and their cycles than smaller customers are. But still, we feel that we are well positioned when it comes to the pricing. It's easy to talk about price carryover. But as I said in the summary, the job needs to be done. So if you have, so to speak, orders normalizing means that what we are producing during the fall or orders taken during the spring. And so the job needs to be done and our commercial organization is doing a great job here.

Klas Bergelind

Now exactly, that's my point. But obviously, it's all about pricing now on orders first and second quarter that you will obviously deliver on in the second half. Yes, very, very quick one. This is my half question, I promise to be quick. On the truck margin, JV, the JV in Dongfeng still fell tough in China while your net capitalization, looking at R&D came lower than I thought. But you also had higher inventory that boost the truck margin much. So did you, in any way, run production higher or was busy as the volume effect? I mean, typically, there's summer effect ahead of the shutdowns, etcetera? Or is it just pure volume, trying to understand the inventory effect on EBIT, if any?

Mats Backman

No. I don't -- I mean, you can't really say that we have an inventory buildup that is driving some kind of overabsorption. I wouldn't say so. And I mean, just looking year-over-year, as I mentioned, I mean, we had kind of a less stock built up year-over-year with almost SEK4 billion. So from kind of an inventory point of view, I think it's good -- we have managed it in a good way. And the buildup has been more on the kind of work-in-progress side rather than finished units then. So I wouldn't say that we have any help from kind of stock build up when it comes to the margin, no.

Johan Bartler

And we move over to Paribas BNP and Miguel Borrega.

Miguel Borrega

The first one, just on order intake. Maybe -- can you explain what happened in Renault European light duty with orders down 70% year-on-year. Is that market related or something internally? And then maybe a follow-up to that. Can you help us understand how we should think about the current run rate of orders and deliveries into the second half? I think it's well understood that the European market is slower but do you think there's an element of price to it? In other words, do you think if you cut prices a little bit, would help orders to pick up? Or should we wait it out until the market recovers? That's my first question.

Martin Lundstedt

Thank you, Miguel. I mean, when it comes to light commercial vehicles and the light-duty segment for Norden, it's fully, I should say, related to the fact that we have a model shift together with the Renault assay when it comes to our master model, you can say. And thereby, we are hesitant in order to make sure that we have the right balance with the phase in and the phase out. So it is not market related but it's related to the shift of models basically. And that's the reason also why we, in the bill wanted to be clear that we showed, so to speak, the medium and heavy duty. I think -- from a market perspective right now, a 290,000 market is still a good market. We have had strong markets, obviously, both related to catch-up and also to the cycle in general.

Now that is correcting downwards to somewhat 290,000. I don't think that any type of price support will substantially help that because the market is, as we see it now in rather good balance. So it's about really making sure that we are maintaining a good commercial discipline that we are providing value. We are now also introducing new models as we speak, the Volvo Aero, for example, in Europe that will provide further value. We have done that rather recently for renewables in Europe, etcetera. So we need to continue to work with the value in this market but to try to gain volumes from commercial reductions is not in the cards.

Johan Bartler

I think we move over to Nordea and Agnieszka.

Agnieszka Vilela

Perfect. So I have a question regarding North America. Just looking at what you did in Europe, you did quite a good balancing job when it comes to production adoption to the volumes. What is your planning now for North America trucks given that we see close to record high truck inventories in the market and production so far has been running quite high. So my question is do we need to see a significant production cut in order to balance the market?

Martin Lundstedt

Thank you, Agnieszka. No, as we said, we will, of course, apply the same strategy as we have done in Europe being very close to our dealers, to our customers and look to your point about the inventory levels. I don't think we can answer that generically because it depends very much on the segments we talk about. And when it comes to long haul and regional haul, there have been, so to speak, a correction also in utilization, etcetera. We see that on spot rates. So here, we need to be cautious and make sure that we are following the market then I should say, primarily also for the Volvo brand. For Mack, it is different, as I said, we have an order -- solid order backlog that is more or less covering the full year and partly into next year. Here, we need to continue to execute give back that they are serving markets that are still doing well in terms of infra rebuilding energy markets, etcetera. I don't know if anything more to add.

Mats Backman

No, I mean, just like you say, Martin, it's a little bit of a different story with North America comparing to Europe as we kind of getting into 2024 with some kind of supply chain issues in North America that we didn't had in Europe with the strike late '23 and so forth and also with a very long order book when it comes to Mack but we are, for sure, kind of monitoring it but it's a different dynamic in North America with the new products and when we are aiming for market shares as well and we're aiming for volumes in North America. But we are monitoring it in the same way as we are doing in Europe. We -- but we are still not there, so to speak.

Martin Lundstedt

I have to say whether we are super excited about it also because, I mean, as we speak now, we are just about introduction of the all-new VNL. It's, I mean, a fantastic range of products for Volvo in the hauling segment with a very good reception; so the race is on.

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Agnieszka Vilela

And then just maybe a short follow-up. When do you expect the prebuy orders start to realize ahead of the new legislation 7?

Martin Lundstedt

Difficult to say. Obviously, a little bit also related to the sentiment in the general market because the better the sentiment, I think the more forward-leaning customers would be in planning. So if we will see a little bit of development now on interest rates, etcetera, that might be a little bit earlier in that case because then the market tend to be more forward leaning and want to plan a little bit ahead because they know that it will be a certain hedging situation at one point in time. So, I think the name of the game here is again flexibility. We very close, not overoptimistic but not overcautious but be able to move quickly when you have the right signs.

Johan Bartler

We move to Bank of America, Virginia Montorsi.

Virginia Montorsi

I had a quick one on R&D. Could you help us understand how to think about R&D development for the second half of the year, particularly for trucks and construction equipment. And apologies if I missed it but could you clarify your comments on the R&D impact on the group EBIT bridge [ph] that you made in the presentation.

Mats Backman

I can probably -- it's the net capitalization when it comes to the R&D that you are alluding to then. And we had year-over-year, a negative effect of SEK600 million then from net capitalization. And what we foresee for the full year is a year-over-year effect of SEK1 billion then. So, we will have lower capitalization this year which is kind of hitting the P&L. But in terms of the gross R&D, that's kind of a different story. But we have a negative impact from the net capitalization, yes.

Martin Lundstedt

But I think the good news here and thank you for that question. I think it's an important one. It's of course also that we see that we have a very good underlying quality in the business. And that's the reason why we don't want to have a type of stop-and-go situation for R&D. We have a great pipeline and we want to continue to pursue that. So to Mats' point, situation where we are now. We are, of course, monitoring if something should further, so to speak, be corrected in the marketplace. But given the situation we are now, we are responsible executing here and now and investing for the future. And it is not massively excessive. We are at a 6% R&D level, including this net effect. So I think that is a good way of looking at it.

Johan Bartler

We move over to JPMorgan, José Asumendi.

José Asumendi

Just one question, please. Do you think order intake in Europe on heavy-duty is stabilizing now in the second quarter. We should expect an uptick now as we go into second half of the year? And do you think you have done enough cuts on the blue collar? And hence, you have already stabilized your industrial footprint to the lower levels.

Martin Lundstedt

Yes. Thank you, José. When it comes to Europe, we see ourselves being in balance now during second quarter, including, so to speak, the industrial part, as you allude to blue collars or complete ecosystem there. Of course, we have further flexibility tools if needed. But as we can see it now, we are in balance. So I think that is the short answer, basically. And then, when it comes -- we are, of course, not guiding beyond what we are saying but that is following, of course, the planning that we have over 290,000 market for Europe.

Mats Backman

And maybe to add -- I mean, we have done the capacity kind of adjustments. And I mean that's one we are with demand. But I think it's also important to stress and especially when we're coming from a year that 2023 with kind of abnormal volumes is that I mean now the name of the game is continuous improvement and to work daily with issues, it might not be as exciting as talking about the big adjustments but that is very high kind of priority in the organization as well.

Johan Bartler

We move to Daniela Costa at Goldman Sachs.

Daniela Costa

I have 2 questions, if it is possible. One is regarding margins and what -- how do you view the sustainability of these margins? You've done a lot of changes on the model on buses. So interested on that. And then if I have time, I want to ask one other thing.

Martin Lundstedt

Yes. I mean, very briefly on that, obviously, we had a good quarter when it comes to, I mean, volume improvements and also product mix coach activities. But we also see that buses and the whole organization in and around buses -- they have done a great job. And we see an underlying structural improvement of that, obviously, not at least when it comes to the drag that we have had in Europe with the previous business model and when we are moving into a business model that contains much more flexibility in terms of partnerships and ways of working. So positive development and we have expectations that, that will, of course, continue to structurally improve. I don't know if you would like to...

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Mats Backman

Yes. I mean we are looking at sustainable kind of improvements, of course I mean we have done the restructuring and we are kind of benefiting from that in Europe right now. So the expectation is to be sustainable when it comes to improvements, yes.

Martin Lundstedt

And maybe just to add on that, that is not visible in bus segment is also on the Nova piece that is sitting in group and others Nova Bus of Canada and North America, where we are also pursuing the same type of activity.

Daniela Costa

Got it. And then just given all the discussion at the moment regarding potential U.S. tariffs to anything coming into the U.S. from anywhere else. Can you talk us on your production system in the U.S., are you bringing any components from Euro bond from elsewhere? And how would you deal with this if so?

Martin Lundstedt

Yes. Of course, I mean, we -- we have a global production system, so part -- some components are coming in from outside and that doesn't go only for us but because when it comes to some specific components, it's not just available in that system. But having said that, we have -- and we are continuing to invest even further in our regional value chain when it comes to North America. We are at the time now pursuing the biggest investment program ever for North America in the group. And we have seen a part of that result now with the launch for the all new VNL for Volvo Trucks that contains also further strengthening of the regional value chain.

So -- and on top of that, of course, we have the majority of our production in the United States in itself. That is also further, so to speak, guarantee; so I think we are well positioned. But of course, we are watching that closely.

Johan Bartler

Thank you, Daniela. We move over to Deutsche Bank and Nicolai Kempf. Nicolai, we don't hear you actually.

Nicolai Kempf

I know the European market is quite fragmented. And so sometimes it's a bit more tough to forecast. But what are the key drivers here for your uplift? Is it country mix? Is it segment? Can you just give a bit more color on that?

Martin Lundstedt

I think, of course, it is a buildup of the different type of components that you are alluding to but maybe even more at this point in time that we have had, so to speak, a strong start of '24 when it comes to registrations in Europe. And we don't see with that strong start that the market should be equally weak in order to compensate for that strong start. So that is the main reason for the uplift actually. Then again, of course, it's consisting of the different components that you said. But if you take on a more overall view, that is the main dynamics.

Johan Bartler

Thank you, Nicolai. We move over to Stockholm and Björn Enarson, Danske Bank.

Björn Enarson

I just have a question on the battery investments. I mean, over the years, you have had quite a few announcements and you have some big plans ahead. Where are you on those? And if needed, can you stop some of these plans? Or are all of them live and running, etcetera?

Martin Lundstedt

No. Thank you for that question. Very important, obviously. The whole setup in that sense is, of course, built on a mix of captive, if I may say, or internal investments but also external partnerships in order to keep flexibility. And so that is the continuous work we are doing with our key partners on how do we make sure that we contain the flexibility because we are still convinced that for certain segments, this will take off to a much higher extent than we have seen so far. But flexibility is the name of the game. So for us that we have the mixed model assembly that we have flexible contracts that we have a visibility together and that we also have other downstream opportunities. For example, for batteries is very important with Penta and Volvo Energy, for example.

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Then when it comes to our own investments, we have already from the start, said that we should do this step-by-step and thereby not doing, so to speak, big investments and that goes for the cell production, it goes for the module and pack production. So that will also be mitigated the following, so to speak, the demand buildup but also what we are setting in terms of opportunities together with our partners. So it's a flexibility toolbox also in that area.

Björn Enarson

So is it possible to conclude that, I mean, the potential quite big investments captive then for cell production. Is that an opportunity depending on where the market ends up and also where it's possible to use external partners instead of suppliers?

Martin Lundstedt

Yes. I mean, again, I mean, as we have in other areas already today, historically, for example, on powertrain, we have had a mix of captive and noncaptive. It is the same here. So we will, of course, look at the holistic view. And when it comes to our long-term captive investment, we will not make them to have a negative backpack without feeling sure that, that capacity is needed over time. So here, I think we have an advantage in relation to others that are more pure play, obviously, that we can take a step by step.

Johan Bartler

We'll continue in Stockholm with Erik Golrang.

Erik Golrang

I have a question on your growth ambitions in North America. And clearly, the new VNL and the new plants are big parts of that. You want to drive share plenty of others also want to do that and the concern is then that it happens on the expense of pricing. Could you say something about how the new VNL is priced compared to the outcome version? And also in terms of the impact on sort of near-term order intake from that? Is there a negative impact or a positive impact from the recent launches? What's the dynamic there?

Martin Lundstedt

Thank you, Eric. I mean, Johan speak, of course, we have ambitions. Otherwise, I mean, we should not have invested that amount in North America. I think we are, in that sense, manoeuvring from a good position since we are still relatively small in relation to some others when you look at the market share. And now the introduction of the whole new VNL and also further investments will bring good opportunities. The VNL -- the all new VNL is a considerable uptick when it comes to productivity for the customers and that will be of course, price and commercialized accordingly. So I will not give the exact figure here but it is, so to speak, of course, the value-based pricing based on the extended performance. We have -- we have conducted big activities now during this quarter, not at least since mid-May with both customers and dealers, etcetera and a very good reception. Then I don't know if you would like to comment something in the short run regarding launch but.

Mats Backman

No. And I mean, when it comes to pricing, I mean, this is an opportunity when it comes to more kind of value-based pricing, charging for the kind of the improvements we have in the new models and new features as well. But I think looking at the kind of expectations on that, I mean it will kind of start late 2024. So this is from a kind of a pricing and value pricing point of view, more a question for 2025 when we are fully up and running.

Martin Lundstedt

But I mean we will not aggressively drive market share. We will do that thanks to the fact that we have a very strong offering. And recently, we have been short of market capacity due to the fact that we didn't have the value chain capabilities as others. But we are taking step by step and we'll do that with quality and not with quantity.

Johan Bartler

Very good. And more about that when we meet in North America in November. So conscious of time, thank you for all the good questions. And with that, we thank you for today. And all material is available on our homepage. So, see you next quarter.

Martin Lundstedt

And wish you a great summer.

Johan Bartler

Thank you.

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