

# **Cummins Inc. (CMI) Q1 2024 Earnings Call Transcript**

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**Body**

Cummins Inc. (CMI)

Q1 2024 Earnings Conference Call

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Company Participants

Chris Clulow - Vice President, Investor Relations

Jennifer Rumsey - Chair & Chief Executive Officer

Mark Smith - Chief Financial Officer

Conference Call Participants

Steve Volkmann - Jefferies

Jerry Revich - Goldman Sachs

Nicole DeBlase - Deutsche Bank

David Raso - Evercore ISI

Angel Castillo - Morgan Stanley

Tami Zakaria - JPMorgan

Rob Wertheimer - Melius Research

Noah Kaye - Oppenheimer

Jamie Cook - Truist Securities

Jeff Kauffman - Vertical Research

Presentation

Operator

Greetings and welcome to Q1 2024 Cummins Inc. Earnings Conference Call. At this time, all participants are in a listen-only mode. A brief question-and-answer session will follow the formal presentation. [Operator Instructions] Please note, this conference is being recorded.

I will now turn the conference over to Chris Clulow, Vice President of Investor Relations. Thank you, Chris. You may begin.

Chris Clulow

Thanks very much. Good morning, everyone, and welcome to our teleconference today to discuss Cummins' results for the first quarter of 2024. Participating with me today are Jennifer Rumsey, our Chair and Chief Executive Officer; and Mark Smith, our Chief Financial Officer. We will all be available to answer questions at the end of the teleconference.

Before we start, please note that some of the information that you will hear or be given today will consist of forward-looking statements within the meaning of the Securities and Exchange Act of 1934.

Such statements express our forecasts, expectations, hopes, beliefs and intentions on strategies regarding the future. Our actual future results could differ materially from those projected in such forward-looking statements because of a number of risks and uncertainties.

More information regarding such risks and uncertainties is available in the forward-looking disclosure statement in the slide deck and our filings with the Securities and Exchange Commission, particularly the Risk Factors section of our most recently filed annual report on Form 10-K and any subsequently filed quarterly reports on Form 10-Q.

During the course of this call, we will be discussing certain non-GAAP financial measures and we will refer you to our website for the reconciliation of those measures to GAAP financial measures.

Our press release with a copy of the financial statements and a copy of today's webcast presentation are available on our website within the Investor Relations section at cummins.com.

With that out of the way, I'll turn you over to our Chair and CEO, Jennifer Rumsey, to kick us off.

Jennifer Rumsey

Thank you, Chris and good morning everyone. I'll start with a summary of our first quarter financial results, and then I will discuss our sales and end market trends by region. I will finish with a discussion of our outlook for 2024. Mark will then take you through more details of both our first quarter financial performance and our forecast for this year.

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Before getting into the details on our performance, I want to take a moment to highlight a few major events from the first quarter. In March, Cummins successfully completed the separation of our Filtration business, Atmus Filtration Technologies. Cummins will continue its focus on advancing innovative power solutions, while Atmus is now well-positioned to pursue its own plans for profitable growth.

We are proud of our employees' hard work and all who were involved to ensure successful separation, and we are excited to see what the future holds for both Cummins and Atmus. The final step in the separation of Atmus resulted in a tax-free exchange of shares, which reduced common shares outstanding by 5.6 million.

In addition, we reintroduced our fuel-agnostic platforms with the name that captures the innovation that powers us forward, Cummins HELM platform. With higher efficiency, lower emissions and multiple fuels, the Cummins HELM platforms give our customers control of how they navigate their own journeys as part of the energy transition.

As the next product in the Cummins HELM 15-liter platform, we announced we will launch the next-generation diesel X15 in North America for the heavy duty on-highway market, which will be compliant with the U.S. EPA and CARB 2027 aligned regulations at launch.

Lastly, in April, Cummins Power Generation introduced four new generator sets to the award-winning CentumTM Series, powered by Cummins QSK50 and QSK78 engines. These new models have been engineered specifically for the most critical applications such as data centers, health care facilities and wastewater treatment plant. I was excited to attend the launch event with our customers and hear about the growing demand for these critical applications and high interest in our genset products, which build on decades of experience meeting our customers' needs and deliver a step change improvement in power density, assured reliability, sustainability and low emissions.

Now, I will comment on the overall company performance for the first quarter of 2024 and cover some of our key markets. Demand for our products remained strong across many of our key markets and regions. Revenues for the first quarter were $8.4 billion, a decrease of 1% compared to the first quarter of 2023. EBITDA was $2.6 billion or 30.6% compared to $1.4 billion or 16.1% a year ago.

First quarter 2024 results include a gain net of transaction costs and other expenses of $1.3 billion related to the Atmus divestiture and $29 million of restructuring expenses as we continue to work to simplify our operating structure and improve the efficiency of our business for the long term. This compares to the first quarter 2023 results, which included $18 million of costs related to the separation of the Atmus business.

Excluding the onetime gain and the costs related to the separation of Atmus as well as the restructuring expenses, EBITDA percentage decreased by 80 basis points as improved pricing partially offset lower volumes and higher research and development expenses as we continue to invest in the products and technologies that will create advantages in the future.

Gross margin dollars improved compared to the first quarter of 2023 as the benefits of pricing more than offset the impact of lower volumes and supply chain cost increases. Our first quarter revenues in North America were flat with 2023. Industry production of heavy-duty trucks in the first quarter was 73,000 units down 5% from 2023 levels, while our heavy-duty unit sales were 26,000 down 7% from 2023.

Industry production of medium duty trucks was 41,000 units in the first quarter of 2024, an increase of 8%, while our unit sales were 36,000, up 22% from 2023. We shipped 38,000 engines to Stellantis for use in their RAM pickups in the first quarter of 2024, down 2% from the 2023 levels. Revenues for North America power generation increased by 21%, driven by continued strong data center and mission-critical power demand.\

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Our international revenues decreased by 1% in the first quarter of 2024 compared to a year ago. First quarter revenues in China, including joint ventures, were $1.6 billion, a decrease of 5% as weaker domestic volumes were partially offset with the accelerating data center demand.

Industry demand for medium and heavy duty trucks in China was 305,000 units, an increase of 14% from last year. However, shifts in the market share during the first quarter led to a decline in our volumes year-over-year. The light duty market in China was up 2% from 2023 levels at 486,000 units, while our units sold, including joint ventures, were 37,000, an increase of 3%. Industry demand for excavators in the first quarter was 50,000 units, a decrease of 13% from 2023 levels. The decrease in the market size is due to weak property investment, high equipment population, and slowing export demand.

Our units sold were 9,000 units, an increase of 10% as a result of the QSM15 penetration and export growth.

Sales of power generation equipment in China decreased 7% in the first quarter as accelerating data center demand was offset by softening in other markets. First quarter revenues in India, including joint ventures, were $758 million, an increase of 1% from the first quarter a year ago.

Industry truck production decreased by 7%, while our shipments decreased by 5% as the market slowed ahead of elections in April. Power Generation revenues increased by 37% in the first quarter as economic activity remains strong.

Now, let me provide an outlook for 2024, including some comments on individual regions and end markets. Our full year guidance now excludes Atmus from the March 18 separation date onwards and also include -- excludes the first quarter gain related to the divestiture. The guidance provided previously included Atmus for the full year as it preceded the transaction announcement.

We are happy to share that our expectations for 2024 have improved from our initial guidance issued in February. Our forecast for total company revenue in 2024 remains the same at down 2% to 5%, which implies higher base business revenues of approximately $1.3 billion compared to our prior guidance as Atmus is now excluded from future quarters.

We are increasing our forecast for heavy-duty trucks in North America to 255,000 to 275,000 units in 2024 compared to our prior guide of 245,000 to 265,000 units, though we do still expect softening in the second half of the year.

In North America, medium-duty truck market, we maintain our prior guidance of 140,000 to 150,000 units, down 5% to flat from 2023, consistent with our prior guidance, our engine shipments for pickup trucks in North America are expected to be 135,000 to 145,000 in 2024, down 5% to 10% from 2023 as we prepare to launch our model year 2025 in the fourth quarter.

In China, we project total revenue, including joint ventures, to increase 3% in 2024, consistent with our prior guidance. We project a range of down 5% to up 10% in heavy- and medium-duty truck demand and expect a range of down 5% to up 5% in demand in the light-duty truck market.

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We expect replacement demand to be in the range -- to be the biggest driver, but the effect may be weakened by a sluggish economy and potentially slower export demand. The short-term shifts in the market share that I noted earlier are expected to normalize as we progress through the remainder of the year.

In India, we project total revenue, including joint ventures, to increase 9% in 2024, primarily driven by strong power generation and on-highway demand, consistent with our prior guidance. We expect industry demand for trucks to be flat to up 5% for the year.

For global construction, we project down 10% to flat year-over-year, up from our previous guidance of down 5% to 15%. We continue to expect weak property investment and slowing export demand in China. We project our major global high horsepower markets to remain strong in 2024.

We are raising our guidance for global power generation markets to be up 10% to 15% compared to our prior guidance of about 5% to 10%, driven by continued increases in the data center and mission-critical markets.

Sales of mining engines are expected to be down 5% to up 5%, consistent with our prior guidance. While a smaller market for us, we continue to anticipate demand for oil and gas engines to decrease by 40% to 50% in 2024, primarily driven by decreased demand in North America.

For aftermarket, we've maintained our guidance of down 5% to up 5% for 2024, as we are through the inventory management efforts and de-stocking that happened throughout the industry in the second half of 2023.

In Accelera, we expect full year sales to be $450 million to $500 million compared to $354 million in 2023, consistent with our prior guidance. We are ramping up electrolyzer manufacturing capacity and capability to deliver orders to our customers as well as expect continued growth in electrified components.

In summary, coming off a strong first quarter, we are maintaining our sales growth outlook for the year of down 2% to 5% as stronger demand in our base business has offset the removal of Atmus for future quarters from our guidance. We have also revised our forecast for EBITDA to be in the range of 14.5% to 15.5% compared to our previous guidance of 14.4% to 15.4%, reflecting stronger North America heavy-duty truck and power generation markets, which more than offsets the loss of profitability of Atmus.

In addition, we are taking steps to reduce cost, optimize our business and position Cummins for continued success in 2024. We are in a strong position to keep investing in the future, bringing new technologies to customers and returning cash to our investors.

During the quarter, we returned $239 million to shareholders in the form of dividends, consistent with our long-term plan to return approximately 50% of operating cash flow to shareholders. In addition, we reduced the overall Cummins share count by $5.6 million as we completed the Atmus share exchange, which will be more fully reflected in the average share count in the second quarter and beyond.

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I am impressed and grateful for the commitment of our employees and leaders around the world for delivering for our customers and generating strong financial performance at the same time. Our results further enhance Cummins' ability to keep investing in the future growth, bringing sustainable solutions that will protect our planet for future generations and returning cash to our shareholders.

I look forward to discussing our long-term strategy further in our upcoming Analyst Day on May 16. And now let me turn it over to Mark.

Mark Smith

Thank you, Jen, and good morning, everyone. We delivered solid first quarter revenue and profitability and generated positive operating cash flow. Given the strength of first quarter results and our improved outlook, we've raised our full year expectations for 2024 after adjusting for the separation of Atmus.

First quarter revenues were $8.4 billion, down 1% from a year ago. The separation of Atmus in mid-March resulted in a year-over-year sales decline of around 1% to our -- to Cummins consolidated sales. Our underlying revenues increased in North America and Latin America and were offset by weaker demand in China and Europe.

EBITDA was $2.6 billion or 30.6% of sales for the quarter. We completed the tax-free full separation of Atmus in March, which resulted in a onetime gain on the divestiture of $1.3 billion, net of transaction costs and other expenses. First quarter results also included $29 million of restructuring expenses. This compares to first quarter of 2023, which included $18 million of costs related to the separation of Atmus.

To provide clarity on operational performance and allow comparison to prior year, I am excluding the one-time gain and the costs related to the separation of Atmus as well as the restructuring expenses in my following comments.

Financial results of Atmus through March 18 are included in our first quarter consolidated sales and EBITDA. EBITDA was $1.3 billion or 15.5% of sales for the quarter compared to $1.4 billion or 16.3% of sales a year ago. The lower EBITDA percentage was driven by investment in new products and capabilities and lower sales volumes.

Now let's look into more detailed by line item. Gross margin for the quarter was $2.1 billion or 24.5% of sales compared to $2 billion or 24% even last year. The improved margins were primarily driven by favorable pricing and operational improvements, especially in the Power Systems business. Selling, administrative and research expenses increased by $72 million, driven by higher research costs as we continue to bring to market new products and capabilities to support future profitable growth, particularly the development of the HELM product line within the Engine business.

Joint venture income of $123 million increased $4 million from the prior year, primarily due to increased earnings in the Power Systems segment. Other income was $21 million, a decrease of $50 million from a year ago. The decrease in other income is driven by the relative negative impact of foreign currency revaluation and lower gains on investments related to company-owned life insurance compared to a year ago. Interest expense was $89 million, an increase of $2 million from the prior year, driven by higher outstanding, long-term borrowings related to the bond issuance we completed in February.

The all-in effective tax rate in the first quarter was 8.7%, mainly due to the tax-free gain on the separation of Atmus. All in, net earnings for the quarter were $2 billion or $14.03 per diluted share, which includes the net gain related to the separation of Atmus of $1.3 billion or $9.08 per diluted share and restructuring expenses of $29 million or $0.15 per share.

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Just to reinforce what Jen said, full impact of the lower share count from the Atmus separation will be seen in future quarters since the diluted share counts counted on a weighted average basis. All-in operating cash flow was an inflow of $276 million compared to an inflow of $495 million in the first quarter last year.

Now let me comment on segment performance and our guidance for 2024. As a reminder, prior guidance for 2024 assume that the operations of Atmus would be included in our consolidated results for the full year. Components segment revenue was $3.3 billion, a decrease of 6%, while EBITDA, excluding costs related to the separation of Atmus, increased from 14.6% of sales to 14.8% driven primarily by improved performance within Cummins Meritor.

For Components, we've updated the guidance for the segment following the separation of Atmus and expect 2024 revenues to decrease 9% to 14% and EBITDA margins in the range of 13.5% to 14.5%. Our latest guidance reflects an increase in both revenues and EBITDA margins after adjusting for the separation of Atmus.

For the Engine segment, first quarter revenues were $2.9 billion, a decrease of 2% from a year ago. EBITDA was 14.1%, a decrease from 15.3% a year ago as the benefit of pricing offset by lower volumes and higher research costs.

2024, we now project revenues for the Engine business to be down 5% to flat, an improvement of 2% at the midpoint from our prior year projections, reflecting a revised outlook in the North American truck markets and stronger-than-expected demand from our construction customers. 2024 EBITDA is projected to be in the range of 12.7% to 13.7%, an increase of 20 basis points at the midpoint due to higher volumes.

In the Distribution segment, revenues increased 5% from a year ago to $2.5 billion. EBITDA decreased as a percent of sales to 11.6% compared to 13.9% of sales a year ago as aftermarket sales, particularly to industrial customers declined from the record levels that we experienced a year ago.

We expect 2024 distribution revenues to be flat to up 5% and EBITDA margins to be in the range of 11.5% to 12.5%, an increase from the prior guide of 3% for revenues and a modest improvement to margins for the full year.

Power Systems segment revenues were $1.4 billion, an increase of 3% and EBITDA increased from 16.3% to 17.1% of sales driven by higher volumes, particularly in the power generation markets, improved pricing and operating improvements, all of which contributed to a strong trend of improving performance in that segment.

2024, we now expect Power Systems revenues to be flat to 5%, up 3% at the midpoint and EBITDA has also increased to be approximately 16% to 17%, up 80 basis points from our previous guide.

Accelera revenues increased 9% to $93 million, driven by increased electrolyzer installations. Our EBITDA loss was $101 million compared to an EBITDA loss of $94 million a year ago as we continue to invest in the products and capabilities to support future growth.

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In 2024, our guidance is unchanged. We expect revenues to be in the range of $450 million to $500 million and net losses to be in the range of $400 million to $433 million consistent with our prior guide.

As Jen mentioned, given the strong performance in the first quarter and the outlook in our key regions, end markets, we are adjusting the full year company guidance, and we project company revenue -- consolidated company revenues to be down 2% to 5%, consistent with the prior year guidance despite the separation of ass.

Company EBITDA margins are now projected to be approximately 14.5% to 15.5%, up 10 basis points from prior guidance, all of which excludes the net gain related to the separation of Atmus and the restructuring expenses.

Our effective tax rate is expected to be 24%, excluding the tax-free gain related to Atmus and other discrete items. Capital investments will be in the range of $1.2 billion to $1.3 billion, unchanged from our outlook three months ago as we continue to make critical investments in new products, capacity expansion to support future growth.

In summary, we delivered solid sales, profitability, and positive cash flow in the first quarter. We do still expect moderation in some of our key markets in the second half of 2024, but we have raised our expectations of our own performance relative to our prior guide.

We took some steps to reduce costs in the fourth quarter of 2023 and continue to identify ways to streamline our business going forward leaving us well positioned to navigate any economic cyclicality and continue investing and delivering strong financial performance.

Our priorities in 2024 for capital allocation are unchanged. We will reinvest for growth, plan to raise the dividend, and reduce debt. Thank you for your interest today, and I look forward to seeing some of you in person in New York at our upcoming Analyst Day.

Now, let me turn it over to Chris.

Chris Clulow

Thank you, Mark. Out of consideration to others on the call, I would ask that you limit yourself to one question and a related follow-up. If you have an additional question, please rejoin the queue. Operator, we're ready for our first question.

Question-and-Answer Session

Operator

Thank you. We will now be conducting a question-and-answer session. [Operator Instructions] Thank you. Our first question comes from the line of Steve Volkmann with Jefferies. Please proceed with your question.

Steve Volkmann

Great. Good morning guys. Thank you for taking the question. I think I'd like to start off with Power Gen, if we could. That business seems to be going well. So sort of two things I'm curious to hear about exactly kind of what you think your position is in the data center market. How much of your business is data centers?

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And then how are you thinking about increasing capacity over the next, whatever, few quarters or years, however, that's going to play out? What should we be thinking about in terms of capacity additions and your ability to kind of grow that business over time?

Jennifer Rumsey

Great. Thanks, Steve. And as you heard in the guidance, we're projecting the Power Gen business to be up 10% to 15% for the year, and data center, mission-critical is really the driver of that. And we've had a very strong demand from data center customers, have had historically a strong position in that market, and that market is obviously growing. We're sold out on our 95-liter through 2025 right now.

And I mentioned the launch of the new CentumTM product, which uses our 50 and 78-liter engine. So, that's providing additional solution to those customers. And then, of course, we're continuing to look at capacity of the 95-liter and how we plan to support what we think will be continuing strong and growing market.

Steve Volkmann

So, sorry, do you have any concrete plans to increase capacity of 95 yet? Or is that still in process?

Jennifer Rumsey

Yes, we do have concrete plans to increase the capacity that we have in place today for the 95-liter.

Steve Volkmann

Okay, great. Thank you.

Operator

Thank you. Our next question comes from the line of Jerry Revich with Goldman Sachs. Please proceed with your question.

Jerry Revich

Hi. Good morning, everyone.

Mark Smith

Hi, Jerry.

Jerry Revich

I wonder if I just ask the cadence of earnings over the course of this year, nice to see an upwards revision to both top line and margins. Mark, can you just talk about where the quarter came in versus your expectations because obviously, the quarter was light versus where the consensus was set up, and I'm just wondering how the quarter developed versus your internal plan. And what's the cadence of the acceleration that you folks are seeing to raise the guidance higher?

Mark Smith

Yeah. I think to be fair to everyone involved to all of you on that side of the fence and all of us, there's a lot of moving parts with the separation of Atmus. So from my perspective, in total, we came in, in line with our expectations and when you adjust for the mid-quarter separation of Atmus, I think we're by and large in line.

I would say, as someone pointed out, the distribution business margins a little bit lower, certainly lower than last year. We see those at the bottom end of the range in Q1 and improving from here, largely driven by what we've seen as a pullback on parts sales, particularly in the industrial off-highway applications. So that's the one area. It's not new. It's been there for a couple of months, two quarters. But otherwise, I'd say we feel good about the gross margin improvement year-over-year. As you can see from our announcements and our comments, we're continuing to look at ways to streamline our organization, make us more efficient where we can.

So overall, in line, Jerry, but expecting distribution in particular to pick up in its margins going forward. We've always expected -- probably we were expecting this a little bit last year, to be fair, and it didn't materialize. But we are expecting heavy-duty truck production to decline in the third quarter, in particular, and you've probably heard that from other industry participants.

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I think the engine business and components will feel some of that in Q3, probably Q4 power systems and distribution shouldn't see any significant volatility in revenues. And really, the momentum is to the up on power systems going forward and into next year, clearly, in distribution. As you know, it's more than half parts and service and quite predictable and reliable. We just had a little bit of a mix shift with the lower parts, but we think that's temporary.

Jerry Revich

Super. And can I just ask from a bigger picture standpoint, so new regulations 2027 will have embedded warranties essentially. What does that mean for your parts market share, is that an opportunity when that field population increases for you folks to have higher engine parts market share because of that warranty dynamic on the new regulations, how significant is that opportunity?

Jennifer Rumsey

Yeah. I mean, as you noted, there's a requirement starting with the EPA 2027 regulations for longer emissions warranty for heavy-duty of 10 years or 450,000 miles, most of that application is going to mile out. So it's essentially what our five-year extended warranty that some customers are already purchasing.

And then that will mean that everybody will need that warranty that will be embedded into pricing on those engine systems and then, of course, we'll drive customers to genuine part throughout that period, which will provide some further benefit to us.

Operator

Thank you. Our next question comes from the line of Nicole DeBlase with Deutsche Bank. Please proceed with your question.

Nicole DeBlase

Yes. Thanks fore the question. Good morning guys. I'm going to ask mine together because they're related. So and they're both around power systems. So I think in the guidance, you guys are embedding full year margins below 1Q levels. I think it's a lumpy business, but if I look back historically, it's more common that the second half is higher. And then similar question on growth, the comps used slightly in the second half, but your full year growth guidance is for an outcome less than the growth you saw in the first quarter. So if you could address both of those items. Thank you.

Mark Smith

We do tend to see some seasonality on revenue in the fourth quarter, a little bit in the second half. But I think the point of your question is essentially right, Nicole, there's positive momentum there. We've been raising the guidance as the performance is improving. There is some modest variation depending on how the parts flow in that business.

But overall, our messages, we're confident in the business and the improvements that we have Jen, Bush [ph] and her team have really worked hard on over the last 18 months. And if we get more revenue, we're confident we'll turn that in higher earnings. But there's nothing dramatically structurally different. Going forward, we expect improvement over time.

Nicole DeBlase

I'll pass it on.

Mark Smith

Thank you.

Operator

Thank you. Our next question comes from the line of David Raso with Evercore ISI. Please proceed with your question.

David Raso

Thank you. May 16, the meeting, can you just give us some expectations around the meeting? I think particularly around the margins. I think people are just trying to figure out the operating leverage in the company in the last couple of years, maybe not quite the margins people were expecting. Even the guide today, it was nice to see the power gen margin increase. But overall, the relative increase in earnings relative to the increase implicit in the sales guide. Still not that tremendous. So I'm just curious if you can sort of tee up a little bit what should we expect May 16. I'm trying not trying to steal the thunder of the meeting but just to level set..?

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Jennifer Rumsey

Yes. Well, obviously, I won't tell you what we're going to tell you specifically, but certainly, you can expect us to talk about overall strategy for the company where we think we're at against some of the 2030 goals that we shared in our last Analyst Day and certainly talking about revenue and margin expectations and what the drivers for that will be within that. So I think you'll hear more about that for sure, David, at our Analyst Day.

David Raso

Okay. And one quick one. The JV income in the first quarter was up year-over-year, but you're still guiding the year down. And I'm just trying to make sure we know why is it down? Is it China not continuing some of the improvement? Is there other parts of the royalty income? I know it's a pretty lumpy line item within the JV income. If you can help us with that would be great. Thank you.

Mark Smith

Yes. I think you're exactly right, David. There's really two moving parts of the operating performance, which generally tends to move in line or better than the market rate. And then we get very lumpy tech fees from the joint venture back to Cummins consolidated results as new products are launched and last year was a particularly strong period of new product launch, to be certain development milestones. So the tech fees are going to be down, particularly in the engine business primarily and that's offsetting any assumptions around the market growth.

I will say it's -- there was some truck OEM build increases in the Q1, but that was more on expectations or hopes about going forward, we're still waiting for clearer signs of momentum as China, as you know, is the biggest driver of the earnings there. But it's really lower tech fees, which were a big at last year -- a little bit in components, mostly in the Engine business.

Chris Clulow

One quick add there, David. And we also have built in our plan the launch of the battery joint venture later on this year post approval. So, that will have some losses as well as that comes back online in the second half.

Mark Smith

Which is embedded in Accelera.

Jennifer Rumsey

Yes, we're expecting that. We have final regulatory approval for that battery JV. So, we're expecting that's going to start flowing in Q2.

Operator

Thank you. Our next question comes from the line of Angel Castillo with Morgan Stanley. Please proceed with your question.

Angel Castillo

Thanks. Good morning everyone. Just back to the Power Generation segment. I think you raised your guidance to 10% to 15% versus a 5% to 10% previously. Can you just talk about the price versus volume mix makeup of that versus prior expectations? Is this a matter of getting better production than you kind of anticipated? Or is pricing growing and just kind of what are you seeing from that perspective?

Jennifer Rumsey

Yes. So, there's a couple of dynamics to keep in mind in that market. So, first of all, as I articulated, the order board is pretty long. And so some of the work to improve price/cost in response to inflation and performance of the business takes some time to play out. So, we're starting to see stronger pricing leverage come into that that market.

And then we're continuing to, of course, drive improvements in the Power Systems business and efficiency in manufacturing and supply chain. And I noted the launch of the new products that we've also designed to be able to sell at some higher margins. So, there are some favorable dynamics that have been happening in the power gen market compared to historically where we would have been in margin performance.

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Angel Castillo

That's very helpful. Thank you. And along the lines of new products, just you talked about your X15 diesel engine that's coming out for kind of ahead of the emissions regulations. Can you give us a little bit more as to what you kind of expect in terms of guardrails around pricing and margin potential improvement?

I know you typically run emission cycles when you get kind of the opportunity to reset and recover some of that margin. So, as we think about maybe not necessarily specifically to any given year, but those projects -- or those products and kind of the implications to your price and margins as those get rolled out?

Jennifer Rumsey

Yes. So, certainly, like in past emissions regulations, our goal is to deliver incremental value to the customer, to have margin improvement associated with that. You will see with the 27 EPA regulations, we already talked about the emissions warranty dynamic. You will also see added content, in particular, after-treatment system to meet those regulations has notable additional content.

And then you will also have the warranty dynamic that we always have as we launch new products where we began at least to launch to accrue at a higher rate from a warranty perspective until the product is out in the market, and we've demonstrated warranty. So, those are the moving parts that you'll see. We have not yet shared specific numbers on what we expect around exact pricing for those products.

Operator

Thank you. Our next question comes from the line of Tami Zakaria with JPMorgan. Please proceed with your question.

Tami Zakaria

Hey, good morning. Thank you so much. So I wanted to understand the margin guide a little better. It seems like excluding Atmus, which probably -- which was a headwind separating that out is becoming a headwind, but you raised the full year guide by about 10 basis points, expecting better margins in Engines and Power Systems. So just to get a sense of what's really driving this improved margin expectation? Is it higher volumes? Or is it more cost savings? Or is it more price cost? So any color there would be helpful.

Mark Smith

Good question. You're right that the Atmus separation is a little bit dilutive to margins. So yeah, good that you picked up on that. It's really volume and a little bit of cost reduction activity. Those are the two primary drivers.

Tami Zakaria

Okay, great. Thank you.

Mark Smith

Thank you.

Operator

Thank you. Our next question comes from the line of Rob Wertheimer with Melius research. Please proceed with your question.

Rob Wertheimer

Hey, good morning everybody. My question is going to be around your competitive positioning in the 2027 EPA from what you can see today. There's a bunch of questions we get on whether there's a prebuy on what the cost increase would be and maybe the warranty should be stripped out of that, I'm not sure.

And there may also be more subtle things that you guys would understand better than most of us around how the standards can be met, whether having an additional nat gas where you guys do pretty well can offset other emissions and so forth. So that's the general question. Price increase, whether share gain and whether there's any subtleties around your mix in your early preparedness that will help you in 2027 transition? Thanks.

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Jennifer Rumsey

Yeah. Great. Thanks for the question. And we are investing, as we've talked about in the new HELM engine platforms. And we're in a unique position because of our scale to continue to invest in what will be market-leading engine solutions to meet those future regulations. And so we expect that, that will provide some advantage for us as we go into those regulations.

There will be a dynamic we think that's going to play out in the 2025 and 2026 time period as end customers anticipate a major regulation change and what that will mean to them. And so we expect that's going to drive some things beyond the normal cycle in the US truck market.

And then as we go into 2017, there'll be some period of uptake, but we think we're well-positioned. Obviously, our position in medium duty has continued to strengthen, and we'll have a next-generation 15-liter natural gas that will go into the market later this year that is of high interest to some of our customers that have sustainability ambitions and see this as the best way, most cost-effective and reliable way to meet those ambitions and then we'll have a new high-efficiency 15-liter platform and 10-liter platform as well. So we're excited about our position with those products and really focused on the execution of development and launching them into the market.

Rob Wertheimer

Okay. Thank you.

Operator

Thank you. Our next question comes from the line of Noah Kaye with Oppenheimer. Please proceed with your question.

Noah Kaye

Thanks. Just sticking with the EPA 2027 for a minute here. If the final rules continue to provide nice crediting of hydrogen trucks. And just given your offerings in this space, wondering if you started to see more of a pickup for hydrogen fuel cell or whether most of the Accelera inbounds at this point are primarily bet?

Jennifer Rumsey

Yeah So if you look beyond even the 2027 into the EPA announced the Phase 3 greenhouse gas regulation, which is going to really start to shape the industry as we get into 2030 and beyond, no major surprises for us with that regulation, but it is really an unprecedented level of ambition and assumptions around zero emissions vehicle penetration. And so the industry and the government is going to have to work really closely together for that to be successful.

So to your question, one of the things -- there are a few things that we're pleased about in the regulation. One is it actually recognizes hydrogen engines as a zero-emission solution. So we believe that that will create a space for hydrogen fueled engine that hydrogen fuel cells still are a good solution over time, but the adoption rate on that is likely to be -- take some time, I would say.

And then the EPA also did commit to work to streamline hybrid powertrain certification. So hybrid engines, we think, may be an attractive solution because the infrastructure availability is going to be a challenge. So that's another thing that we're looking at closely.

So there's still some engine-based solutions. Yes, we're seeing an uptick today in more of the battery electric powertrain as I noted, and of course, electrolyzers, fuel cells are still a pretty low level.

Noah Kaye

Yeah, makes sense. And then you mentioned that you got regulatory approval for the JV. So just can you lay out for us the game plan on how spending for the gigafactory should proceed over the next couple of years? And what you may be doing at this point in terms of lining up supply and demand for the factory, at least your…?

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Jennifer Rumsey

Yeah. I mean the partners have been working together ahead of getting the final regulatory approval we announced that we selected a site earlier this year. So we'll be -- we're getting a site ready in Mississippi, just outside of Memphis, Tennessee and really starting the work to prepare for supply chain and building the plant.

Now that we have regulatory approval, we believe we'll be able to close and finalize the entity in this quarter. And then we'll have phased investment as we build the plant and work towards start of production in 2027.

And then we're, of course, sharing this investment of a 21-gigawatt hour plant across the partners and have this design that will allow us to phase in new lines and scale up the plant and production rates based on how we see the industry developing, and we're still feeling really good about how we're positioned in the market together with LFP cell that will be designed specifically for the commercial vehicle market and have the ability to leverage some of the incentive money that's available here to help enable adoption in our commercial vehicle market.

Noah Kaye

Great color. Thanks so much.

Operator

Thank you. Our next question comes from the line of Jamie Cook with Truist Securities. Please proceed with your question.

Jamie Cook

Hi, good morning. So -- sorry, I'm managing through like seven calls. I hope this hasn't been asked. But Mark, the question is to you, I guess, understanding you have your Analyst Day coming up this month. I'm just looking at Cummins and thinking, okay, perhaps there's a cost story there, you have market share gains that should be helping you may be less spend on Accelera.

I'm just wondering, as you think about margins over the medium term, do you think there's an opportunity to structurally improve incremental margins? Or as you think about sort of the next couple of years, it is more so taking these actions to hit Cummins' historic targeted incremental margins?

And then my second question would be, and if this is addressed, I apologize. Can you just talk to the visibility you have across like in terms of backlog across your portfolio, in particular, for the engine side and the Power Systems side? Thank you.

Mark Smith

So, I heard you we will explicitly address incremental margins in May. You will not miss that for all who are asking very appropriate center of mind or top of mind for us clearly. So, you will hear that very, very shortly, I guess.

Jennifer Rumsey

Yes. And Jamie, good to have you back. We're, of course, working and you're seeing the improvement in the Meritor business as we do the integration and Accelera as we ramp up. Revenue, we'll talk more about that.

In terms of color on the market, we're seeing continued solid demand in the heavy-duty market because of the high backlogs that have been built up, still a lot of strength in the vocational market. Truckload has been down for some time. And so we are still anticipating and hearing from our OEM customers that second half will have some weakening, and that's baked into our revised guidance, which is down, but not as far down as previous guidance.

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Power Gen, I noted earlier, we've sold out the 95-liter through 2025. We're looking at capacity there and how we can take that up as well as with the new CentumTM launch, being able to sell some of our other engines into that market as well.

So, pretty -- really strong feeling very good about Power Gen, feeling good about medium-duty and vocational on-highway. It's really the -- it's the truckload fleet customers in the heavy-duty market. That's the one that we're watching closely and still anticipating that it's going to soften before we enter the next uptick in their cycle.

Mark Smith

Yes. And then what you heard maybe earlier was some industry consensus building about 2025 and 2026 ahead of 2027. So, our baseline assumption today is that this is not as sharp or as steep as normal cyclical downturn. That's an assumption, not a fact, but that's what we've baked into our outlook for this year. China is the one where we're still -- we're waiting for more momentum probably.

Operator

Thank you. Our next question comes from the line of Jeff Kauffman with Vertical Research. Please proceed with your question.

Jeff Kauffman

Thank you very much and thanks for squeezing me in. I was just curious your thoughts. It's apparent that the downturn, I think a lot of us feared in 2024 on the heavy-duty engine side isn't going to be as bad as originally feared. I know ACT Research has taken up their forecast.

You did mention some weakness beginning in 3Q, but are we taking from what would have been otherwise prebuy in 2026 if we have a better 2024? Or do you think the two are unrelated?

Jennifer Rumsey

I'm not sure that they're related. I mean, we're really watching what's going on with production rates with backlog with some of the spot rate dynamics in the market. And if you look at some of the freight carriers out there, they've been challenged now for the last 18 months. And so that's what's driving our outlook, but fair. I mean we -- because of the -- it's really the supply chain dynamic that has made this cycle so different and even unpredictable. It certainly held up better and longer than we had forecast, and we are still expecting to see some softening in the second half.

Jeff Kauffman

Okay. Well, congratulations, and that's my one. Thank you.

Chris Clulow

Thanks, Jeff.

Operator

Our last question comes from the line of Chad Dillard with Bernstein Research. Please proceed with your question.

Unidentified Analyst

Hi. Good morning. This is Federico filling in for Chad. I would like to double click on the R&D intensity and how to think about this on the medium-term basis?

Chris Clulow

Sorry, can you repeat that? I don't think we got the first part.

Unidentified Analyst

Sorry. We would like to double-click on the R&D intensity and how to think about this on a medium term basis.

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Jennifer Rumsey

Yes. So we are -- as you know, we've taken up our R&D investments. We noted that in our comments because we're making investments, in particular in these new fuel-agnostic engine platform. So we're at an elevated level of R&D for those new platform investments. And those products are beginning to launch and really will launch through the 2026 and 2027 time period. And then, of course, we're at a period of investment in the Accelera business as we work to launch new products and ramp up revenue there as well.

Unidentified Analyst

Thank you.

Chris Clulow

Thanks.

Operator

Thank you. I'd like to turn the floor back over to Chris Clulow for closing comments.

Chris Clulow

Thanks, everybody, for your participation today. That concludes our teleconference. Really appreciate the interest. And as always, the Investor Relations team will be available for questions after the call. Have a good day.

Jennifer Rumsey

Look forward to seeing many of you in person in a couple of weeks.

Operator

This concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation.

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