

# **DEUTZ Aktiengesellschaft (DEUZF) Q2 2024 Earnings Call Transcript**

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**Body**

DEUTZ Aktiengesellschaft (DEUZF)

Q2 2024 Results Conference Call

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Company Participants

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Sebastian Schulte - Chief Executive Officer

Timo Krutoff - Chief Financial Officer

Conference Call Participants

Jorge Gonzalez - Hauck & Aufhäuser Investment Banking

Stefan Augustin - Warburg Research

Presentation

Mark Schneider

Good morning to everyone from Cologne. Please note that this call is being recorded, and a replay will be available on our website at deutz.com later today. Your participation in the call implies your consent. Joining me today are our CEO, Sebastian Schulte; and our CFO, Timo Krutoff. Sebastian starts with operational and strategic milestones of the first half of the year. Timo will then provide a deeper insight into the financial data.

Following this, our CEO will go into more detail on the most important points of our strategy implementation in recent calls. As always, we conclude with a look at the forecast and outlook before we look forward to your questions. Please note that management's comments during this call will include forward-looking statements, which involve risks and uncertainties. For the discussion of risk factors, I encourage you to review the disclaimer contained in our annual report and this presentation.

All documents relating to our first half of 2024 reporting are available on our website. Having said that, I'm handing over to you, Sebastian.

Sebastian Schulte

Thank you very much, Mark. Good morning to all of you dialing in for our H1 results 2024. Indeed, I'd like to start giving an overview on what we achieved operationally. I'd like to mention a few words on how we see the market at the moment. Then obviously, after Timo will have gone through the numbers, we'll give some more details on the milestones of our strategic projects because what's clear that in the last couple of months, we've done quite a lot on the strategic side, on the rebuilding Deutz for a more resilient future.

Let me start with looking back really at the first 6 months, and I think it's always good to have that chance of that opportunity to look back in a particularly challenging year like this one because before going to the numbers, let me emphasize that the dynamic of the market has changed significantly from, let's say, the years '22 and '23, where we were in a situation that despite the various supply chain challenges, demand coming from our customers clearly exceeded the supply. We and also competitors were able to provide. That tide has turned already in the fourth quarter last year. It's a theme since then. But we want to show you that how well we manage this situation, because difficult situations always provide a good opportunity to become better, more resilient in order to benefit even more when the tide is turning again.

New orders, EUR 791 million. If you compare that with the prior year period, that is down 18.1%, are clearly on reason coming from weak orders, particularly from construction, agriculture and also Europe, I'll go to regions and industries in a couple of minutes. We do see, on a positive side, a further growth of our service business and service orders were up 6.5%. So that's the plus side on that. Revenue, EUR 876 million, also down on a prior year comparison, down 12.6%.

However, if you look at revenue, the decline is significantly smaller than the decline in unit sales, which is down almost 19%. Here, same picture as on the new orders, share of service business was up 5.2%. Now our service business represents almost 30% of our overall business. So book-to-bill still are slightly below 1. That means trends not changed yet.

EBIT margin at 5.7%. That's actually quite a good message that on a group level, we clearly show how our business improved resilience against this mentioned tough economic environment. Also, needless to say that the margin is well in line with the guidance we provided throughout the year so far. If we look at our markets, both on a segment perspective as well as on the regional perspective, our core markets still represent really a mixed bag. We are caught in the cycle.

We are well in the situation like our customers, our suppliers, our competitors. We do benefit continuously from the strengths we see from the United States, also due to the fact that we grew that business significantly and successfully over the last years. But one after the other. So first of all, looking at construction were down was speaking on revenues, EUR 1 million were down 26%, EUR 212 million now. Also, agricultural equipment down even 32%.

Material handling on the plus side has been almost up 10%. We'll see that, and you know that. Those who follow us more closely. There's a high correlation between our material handling sector and the United States because our sort of largest material handling customers, JLG, Terex, they are U.S. customers.

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The service business has gone up 6% to EUR 253 million for the first 6 months 2024. Looking where we come from the EUR 253 million multiplied by 2, we are now on a run rate of above EUR 500 million. That is before the Rolls-Royce Power Systems effects come into place after the closing. So here, we are really on good track. Regionally, again, the mixed bag, Europe down 19%, mainly due to the high share of construction ag.

America, on the other hand, still growing slightly, but growing to EUR 240. China and APAC, both on relatively speaking low levels, but China down 20% as I said, from a low baseline already, APAC, excluding China, down 11%. So we see here a similar picture like we see in Europe. So that's clearly summarizing ag and construction is still low, slightly cyclical low and U.S. and material handling continues to grow.

If you look at profitability, look on absolute numbers, and we see it in the top half of the picture, yes, true were down from previous year. We went in the first quarter was EUR 27.7 million. Now we're slightly below that EUR 22.4 million. But if you look at revenue, here you see really the large decline, and we'll see later related from Timo on the numbers, how structurally we are quite already benefiting a lot in order to ensure that on these relatively speaking, low revenues, we are able now to generate a yield like margin above 5%. That's something, quite frankly, which, let's say, 2, 3, 4 years ago would have been impossible on the revenue and cost structure and portfolio of Deutz.

So in the same way, we are not happy only making EUR 50 million, EBITDA after 6 months, that's below our ambition. But on the other hand, given the top line, it is showing very clearly that our performance initiatives, in particular, the expansion of the service business stabilized profitability on a level, again, which shows that we are on the right track. Speaking of performance initiatives, one of the things we put very early focus on this year is material cost and purchasing, because in the last years '22 and '23 where demand exceeded supply where we had some really seller's market all over the value chain. For us, it was very important to fix several pricing issues, we've inherited from the past. We've done that very successfully in '22 and '23.

Now with the types turning to what's more of a buyer's market. That means, obviously, the buyers have certain strengths. on the price side, it means we're defending our -- we are defending our price quite successfully. But on the purchase side, we obviously need to really seize the momentum in order to generate savings and both on a direct as well as on the indirect side on the spend side, we show clearly that we're quite successful here on the way. Let me go through in structure.

In direct expense savings, what we've realized in the first half is already a low double-digit million Euro amount. We put ourselves, we gave ourselves a target by the end of last year based on what we think is possible. The savings target we did lower slightly, but mainly because we looked at a rather a bit more ambitious volume numbers when we entered the new year. But what we see now is that actually, more than 50% of the targeted savings we have realized after 6 months. On top of that, we were faced with a lot of supplier claims for partly actually quite significant price increases.

We were able to fight back the vast majority of that and so we were able to reject more than EUR 30 million worth of claims, and that shows really a pushback ratio of roughly 90%, and that's quite a good result. So the purchasing team has done a tremendous job in this difficult environment. We also obviously don't want to expose individual suppliers or components here, but we did have a few situations where critical suppliers, meaning serving critical components, approached us with really difficult claims, and we were able to fight back the vast majority of that. So that means we're not only stabilizing our supply base, supply chain, our costs, we're also realizing here cost savings, as mentioned before. More successfully even we have been on the indirect side here as well, realized savings in the first 6 months, higher single-digit million Euro more successfully, I said because the spend obviously is significantly lower, indirect compared to direct.

Here, we did the opposite; we increased even our target because with our teams, we identified more potential than we initially thought they would be. So that means we are almost able to compensate here our slight target reduction from the direct [indiscernible]. We are even better on track. After 6 months, we are on track with having already achieved more than 70% of our target. So that's good news, and we'll continue to work on that as well.

One nice example is packaging. Packaging plays an important role for our products, for our parts. So for everything we sell a chip to the customers. We looked here at benchmark producers. We looked at lower-cost country producers.

In the end, we managed to reduce our overall packaging costs by 25%. I mean that's a great achievement, and that helps us significantly in securing and increasing profitability. But it's not only about cost improvements or cost cutting is also about getting our operations more modern, more flexible, leaner and so on. So one of our highlights on the operations side is that we successfully started our new assembly line #6 in April in Cologne. That assembly line #6 replaces an old assembly line, and this assembly line is much more scalable, allows more flexible production.

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We think as we speak here about the assembly line to produce engines power in the displacement range between 4 and 8 liter diesel and also our new hydrogen engines. For those who are more familiar with our production setup, we do have a fairly new assembly line #5 that covers our [indiscernible] engines, highly automization, or highly automized. So a very good setup. now when we have this sort of second state-of-the-art assembly line here in place, which, as I said, is enabling us to produce much more flexibility and particular in the time we're currently living in of fluctuating demand, of fluctuating mix between different engines, this greater flexibility helps us here tremendously. On that assembly line, by the way, we are also going to start to see production of our 7.8 hydrogen engine, the one which we currently apply mainly in power generation products, including the small serial order to be delivered to China.

So that's going to start in September this year. Our prototypes are already built and have been shipped. By the way, we expect the opening ceremony of the first 4 gensets to happen in Beijing in September. So here we are well on track as well. Yes, it cost the money we spend in total, so EUR 15 million on that.

That's a really great achievement. With that assembly line, coupled for the existing assembly line #5, we really have a state-of-the-art engine assembly now here in Cologne. Before handing over to Timo, I want to just provide at least a bit of an update of our strategic moves and the implementation of such. Afterwards, I will go through that in a bit more detail, but we did really achieve a lot of highlights in the last months. So end of June, we acquired or we signed the purchase agreement for the acquisition of Blue Star Power Systems, just a couple of days ago, beginning of August, the closing occurred.

Beginning of July, we also entered into a strategic co-operation with Tafe Motors, the Indian ag company. Also last week, so just a couple of days ago, the closing of the transaction with Rolls-Royce Power Systems for the Daimler truck engines occurred. So we really, in a short period of time, we've taken quite a lot of boxes and I will go through that in a minute. But before doing so, I'll hand over to Timo, who will lead you through the 2024, H1 numbers in a bit more detail.

Timo Krutoff

Thank you very much, Sebastian and also a very good morning here from Cologne from me. Let's jump directly into the first numbers. We're looking here now at new orders and unit sales and revenues. So as Sebastian said it already a little bit, new orders down 18.1%. That leads to a number that is a little bit shy of EUR 800 million for the first half year and fairly much in line with that is also the unit sales of now roughly 74,000 engines produced and sold, and that is down 19%.

So just to give you an idea of what that means for us, if we look at, I would say, normal 2-shift production in our facilities, at least here in Europe, we would be at 80,000 to 85,000 engines at a normal run rate for the 2 shifts. So that's ideal for sure, for us, not the ideal production point. But [indiscernible] Sebastian said that on the example of the new line we have, we are now flexible enough to act accordingly. If we look now at revenues, the revenues is just down 12.6%. We see 2 effects here.

The first one is a negative. If we compare unit sales to revenue, it's the product mix. So we're selling a little more smaller engines compared to bigger engines before. So that would lead to, of course, compared to unit sales, a little less revenue. But on the other side, and that was very important for us now is that the pricing measures from the last year still have an effect for this year, and the other part is that the service business is still growing and therefore, pushing revenues and making us more resilient also a little bit on the revenue side.

The book-to-bill ratio is at 0.9. So a little less than one coming in now in new orders. That means we still have orders on hand of EUR 366 million. So that's something we can still work on and deliver these parts. Then for the second half of this year.

One thing that needs to be clear or should be clear for everyone. This is, of course, without the new acquisition. So if you are looking at the second part of the year, then we'll have the effect of the 2 bigger acquisitions we've just closed. Okay. Next slide, please.

We're looking here at some details on the revenue split. The first is the breakdown by applications. So service I've said that already, but also material handling, if we look into the certain segments is up in total numbers, service 6.5%, material handling 9.2%, while on the other hand, and that's really not surprising if we look at what's happening in the market, construction and agriculture are both down. If we look at specialty agriculture, it's down 32%. But if you look what you hear in the market, we see a lot of numbers with competitors or customers that's down more than 40%.

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So I think we're still holding up a very difficult environment here. Now looking at how is the split between the different application segments, then we can now say service is our biggest segment here, which is now super important. So 29% of our total revenue comes now from the Service segment, followed by material handling with 27% and construction with 24% and I'll ask by not least of the bigger ones, at least agriculture starts to play a minor role compared to the others with only 11% of our total revenue left. Quick look at the markets. Sebastian has already said a little bit about it.

Yes, Americas luckily still up to 1% everyone else is down, EU without Germany is now at 36% of our total share in revenues. Germany is at 19%. So total Europe at 55%. In the Americas, again, and we've seen that over the last years already is gaining an importance for us now having a share of 27%. Asia Pacific, now we're at 14%.

So we also see a slight decrease or a decrease of 14 percentage points at least in this market. Looking at profits, especially EBIT here. Sebastian has said it, and I think it was phrased very well. We're not happy with just EUR 5 million EBIT in the first half of the year. If we think about mid- and long-term targets that we have, we want to be significantly better.

But at the same time, I want to say that a margin of 5.7% is still acceptable in such a difficult environment and shows the resilience of our company. So we are very much in line with the guidance we gave out of 5% to 6.5%. So we are doing at least okay here. This can only be seen if we look at, while sales was down compared to the year before by EUR 125 million. EBIT is down by EUR 20 million.

So we can say contribution margin wise, it's 16% in normal manufacturing environment. You usually see higher contribution margin losses if the sales target goes down, and this is a clear sign that our cost reduction programs work that the flexibility and production work, so where the fixed costs are not so high and of course, better growth and service is helping us with a more stable EBIT. What we're still luckily able to do because we are more resilient is to invest in our future. We're not cutting costs here, at least not dramatically in any of the typical parts here where you see our R&D spending is actually up compared to year before, not significantly up. It's a similar range, but we've now spent almost EUR 50 million in R&D, and this is true for our new segments, but also for our classic segment.

So we're still investing here in the future. If we look at the capital expenditure, I would say it's now on a normal level here. You need to remember if you compare the numbers with last year, that the big acquisitions of the licenses and the IP rights of Daimler Truck was included in the first half of the year. But I'd say $45 million now, including leasing is an okay number. We are still going to look very closely into that in the second half of the year to make sure that we achieve our cash flow targets.

Working capital is up. You probably wouldn't have expected that. If you look at the market development, there is one special thing going on here. We have an external logistics supplier that's handling a lot of our logistics things, and they need to do a very big maintenance in their part, which they haven't done for the last 10 years. So it's not something that happens all the time, but that's why they're shutting down for 3 weeks.

Therefore, we also had to shut down production now in August for 3 weeks since we're still supplying some of our customers, we had to increase the stock levels and did produce a little bit more over the last couple of months. We have sold, but that was planned. So we see an increase here on the working capital of EUR 44 million. That of course, relates directly into the cash flow situation. If we compare here our operating cash flow.

It's down quite a bit. We're still positive. But remember, working capital, EUR 44 million increase compared to at least to the start of the year. So that has a big effect. But of course, the EBIT reduction also plays a part here.

On the free cash flow side, including M&A, we're good, were at EUR 31.2 million positive, of course, here the Torqeedo sale is included. If we then look at the free cash flow before M&A, you see minus EUR 35 million, well, again, it relates to the operating cash flow and the buildup of the inventory and some of the reduction in EBIT. In the net financial position, not much to happen. We can still say that here, we have an equity ratio that is very solid at almost 50% as of June 30. In the different segments, we actually have to say that the classic segment here plays the absolute major role.

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I don't think I need to talk about new orders, unit sales and revenue here because it's almost exactly the same numbers I've already done. But you can see here the split in R&D expenditure that we are still investing, as I said, quite significantly in the classic segment. But also at the same time, in the green segment and first, the green segment has more the character of a start-up where we now need to invest into the future. We're therefore, losing here EUR 17.8 million which on the other side also shows the stability of the classic segment, which still has a fairly big profit contribution to what's going on. Then one last topic from my side.

It's much directly related to the first half of the year, but we did do the capital increase with an accelerated book building in early July from our perspective and for the funds we raised that was a very successful one. We were very happy with the interest of the investors. So a lot of people wanted to buy the part of the approximately EUR 12.6 million in new shares, which we were able to place at the cost point of EUR 5.71. That led to gross proceeds of EUR 72 million. That of course, is very good if we look into the future, what we are still planning to do, but also for the financing of the acquisitions we've just done.

So in total, we can say that we are financially on a very stable position and that our financial firepower is still strong for everything that we want to do and need to do for the transformation of this company. Thank you very much. That's all from me. So for Sebastian on some of the strategic things.

Sebastian Schulte

Thank you, Timo. Yes, let me guide you quickly through the progress of our strategic initiatives. Let me start with the acquisition of Blue Star. We did announced about 6 weeks ago on the rationale and the main focus points of why we did that. Now we actually show that we've done it.

Blue Star, one of the top 10 gen set producers in the North American market, in the active, in the small, medium and lower large power range up to 2 megawatts. So we're talking about 110 employees, revenues this year, above USD 120 million on a full year basis, of course. We signed on June 27th, we closed end of last week. We did agree with the private previous owner [indiscernible] on the terms. But what we can assure you is that valuation has been very much in line with usual parameters on deals like that.

The founder, Doug Fahrforth, has agreed to continue to run the company for us as CEO until at least '26. We are very grateful on that. We're very excited about that because data really shows that he can not only build a company like that, but also develop it into a really, very profitable business with a fantastic reputation with their customers. So I was there for the closing, I spoke to some of the distributors, and they were really all up on not only the performance of the product, but particularly the way Blue Star treating the customers. So that really shows it fits so well to our value proposition at Deutz.

In terms of numbers, seeing that we are at the start, we're close to the 1st of August. So we expect a bit more roughly EUR 50 million top line effect of that and profit margin is certainly well above the Deutz current group level. So that's backing up significantly H2 this year for Deutz. It puts us really, as I said earlier, it makes us broader and more resilient than it is only the starting point for building up the BU energy going forward. Why is it good for us?

I said it before. The energy business, the energy market is very attractive. It shows a very good growth trajectory going forward, less cyclical as well. We'll buy and build this energy business on what we have with Deutz and we're now with Blue Star on top of the existing operations in Morocco, Magideutz. We've got the first 2 building blocks in that, and we expect these to be added in the future.

We do have a right to win here. We know the technology. We know the service, so that's good. Blue Star will be really the relevant strong building block for that. It helps.

It strengthens all our areas of 2 or plus classic, but also green because even though so far, power gens, we're providing on the larger scale power, gensets are still relying on diesel and gas engines. But with our hydrogen technology, our 7.8 hydrogen, where I said earlier, we're going to launch the first 4 gensets in China within a couple of months. So that's really a fantastic proof of concept also for power generation. Let's not forget service business. We are good at that, not only in the U.S. but particular there. We are continuing really to build our service business with genset supports our growth strategy. We gained size and relevance in energy and yes, as you probably hear from the turn of my words, we're super excited about that. Why is it good for us? Profitability, as said, it's more profitable.

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It has a sustainably stronger growth than our core markets. Although this has never been the main focus of that, it represents an opportunity for Deutz engines as well, a distribution channel, but I said that is not the main focus of that. We want to grow here agnostic of the engine product itself. It broadens our portfolio, broadens our business. We've become a solution provider rather than just a very successful Tier 1 engine provider.

I spoke about the hydrogen potential earlier. Last but not least, it really makes us more resilient. The market is less cyclical, and it strengthens with the initial focus on the United States, our geographical diversification is significant. The other big project we announced a few weeks ago was our partnership with Tafe, the Indian ag company. We did sign a long-term cooperation with Tafe.

Tafe will for us produce Deutz branded engines 2027. So not only Deutz-branded engines, but they're pretty much identical with the engines producing today out of Cologne. We're talk here about up to 30,000 machines per year. When I mentioned that number, we speak about a number after ramp-up in 2030. So in 2017, the number is going to be even smaller initially.

I would talk about 2.2 liter, which is up to 75 horsepower, 2.9 liter, which is up 100 horsepower and the focus is that Tafe uses these engines in their own tractors, to upgrade their tractors with a state-of-the-art engine product, but also give us the opportunity to market those state-of-the-art engines produced under a better cost basis in India itself, but also neighboring regions, particularly in Asia-Pacific. Engines were produced in a state-of-the-art manufacturing facility in Alwar, and that's very important for us in terms of resilience. It also gives us the opportunity to expand our supplier base. Supplier base is challenging is a challenging field for all players involved into a combustion engine field. We'll try to source as much as possible for the Indian production in India, not everything, but 75%, 80%, we would target to source over there.

If you get components that right specification, right quality and competitive cost made in India, we may well use them also in our German production assembly lines. So that will benefit not only the market potential, but also our own production facilities and positioning in Germany. Tafe is such a great partner, we're already taking on additional opportunities to expand the cooperation, including also climate friendly solutions. So India is a fast-growing market, and we're very excited to be part of that as well. Again, the benefits, profitability.

I think it's very clear, access to new customers, receiving their license fees for the production to be purchased by Tafe. India is not only a fast-growing market. It's also a market where the combustion engine, even in the lower power ranges will and that's our conviction will be around for probably much longer than what we already expect in Europe, America and other of our core markets. So we can we can market our proven technologies even longer than what we currently see. When it comes to the supplier aspect, it will increase our resilience further and makes us also less dependent on other countries or regions, particularly China.

Then next point. Defense, we spoke quite a lot about defense as a growth opportunity for Deutz. This is something we're at the beginning. First of all, we are already in the market on a small scale. So we do sell our Deutz engines into defense vehicles, but also for power generation.

But we want to expand that much more structured and that's supposed to become a new market for us, a new customer field for us, which is very interesting, very attractive due to the changed geo-political outlook. I think that is clear. We'll also look here into partnering where required to quickly gain scale and to quickly actually get access to existing products and programs. I think it's also clear on all aspects, profitability portfolio and resilience why entering defense takes all those boxes to reduce the cyclicity of the business, but also to provide another long-term sales pipeline for diesel engines and including the after-market. So also here, we are excited about that.

We cannot announce more at this point in time, but there is more to come in the future. Final strategic milestone. We are very happy to have concluded the transaction with Rolls-Royce Power System. Just to recap quickly, most of you are very familiar with that business. We took over an engine portfolio associated with a revenue of EUR 300 million on an annual basis for engine and service.

We talk about Daimler truck medium-duty and heavy-duty engines for the off-highway sector to start with. This EUR 300 million top line business comes along with the EBIT margin above the current Deutz group margin. We did not disclose the purchase price, but it is in a higher double-digit million euro amount revenue for this year because it's only on a pro-rata basis is expected to be above EUR 100 million. Recap again, a couple of years ago, we concluded that transaction with Daimler Truck for MDEG for the medium-duty and the heavy-duty engine to start beyond 2028. With that follow-up transaction with Rolls-Royce Power Systems, we filled that gap between now and 2028, 2029, and we showed that we can actually execute transactions like that.

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Combined, having Blue Star now part of our books as well as the Rolls-Royce business. On a like-for-like basis, we grew Deutz significantly with that 2 closings on the 1st of August. It's more than just the immediate effect on numbers. It's a very strong proof point that we are not only talking about becoming an active part in the consolidation of the internal combustion engine market, but we're actually executing that. So that's why there was some room for celebration when those 2 transactions closed a couple of days ago.

I'm just providing a few sort of pictures. You see here, these are the 3 top customers of that engine portfolio. We've got the South African mining and construction company, Bell which is based out of South Africa, one of their iconic products, the dump truck, and from now on, with the Deutz engine, we've got class fantastic ag company out of Northern Germany with tractors, with forage harvesters, balers and other great products also from now on, some of them equipped with Deutz engines and last, but certainly of the sponsor Finnish forestry equipment company, you see Forrester in action also equipped from now on with the Deutz engine. I think when you look just at the sheer size and robustness of those great products becomes very obvious why a state-of-the-art modern, clean combustion engine is probably here the way to go. The way to stay to power those equipments despite obviously all important focus and activities to make the product or product portfolio greener, but this is really what it's all about when it comes on the strong tough demands of the off-highway markets.

With that in mind, let me conclude with a view on the guidance for this year. We came and we heard it earlier from my previous words but also from Timo's points, we came 2023 from almost 190,000 engines. This year, we now see a maximum of 160,000 engines to be produced and sold. We do confirm the revenue range between EUR 1.9 billion and EUR 2.1 billion. We also do confirm the adjusted EBIT margin range between 5.0% and 6.5%.

We also do confirm our guidance in terms of free cash flow, mid-double-digit million euro amount. it's important really that the closing of the agreement with Rolls-Royce and the acquisition of Blue Star Power Systems, they obviously have a positive impact on revenue and profit now from Q3 or to be more specific from August onwards. So that's great. Obviously, the full impact will only realize in '25 when we get the full year, helping us here. We're growing.

We continue growing the service business. We're working on pricing and cost cutting to really strengthen the resilience in this downturn cycle where we are faced lower unit sales. But this is a description of the moment. Going forward, as soon as we are enjoying a slight recovery on the cyclical market that will help us tremendously. That's also why we're not only confirming the outlook for next year.

This is our mid-term outlook, which we do confirm with a couple of highlights, also in particularly now moving the service business to the next level of around EUR 600 million. We are well on track with that. So we're confirming those previous mid-term targets. Why do I say previous because 25 is not mid-term anymore, but also give us an outlook on the Capital Market Day, which will host here in Cologne and our headquarters at the beginning of October 8, where we will then guide everyone who's joining us in more detail through the strategy, through the building blocks we've added to the company in the last month and also giving us new mid-term and long-term view on the size and profitability of the company. With that in mind, thank you very much, and back to you, Mark.

Mark Schneider

Thank you, Sebastian. Now we are happy to answer your questions.

Question-and-Answer Session

Operator

We will now begin the question-and-answer session. The first question from the phone comes from Jorge Gonzalez with Hagfors Investment Banking.

Jorge Gonzalez

My first question is just a clarification on the cost savings that you mentioned were achieved in the first semester. You said in the low double-digit million euros. Is this correct?

Sebastian Schulte

That's correct.

Jorge Gonzalez

Then the rest of my question because all is one stent question is related to the guidance and also the view for next year. I know it's difficult to tell at this time. But taking into account the order intake that you had in Q2, should we assume that Q3 is going to be at best as Q2 in terms of sales with the units that you have now in the backlog? Or is there any reason for Q3 to be in line or better than Q2, that I'm missing here?

Sebastian Schulte

Yes. If you compare like-for-like, so before the acquisitions, we expect it to be roughly similar on the top line. We obviously have a little bit of a seasonal effect that some of our customers shut down in August. So August itself probably being a bit weaker, but it's always like that, but taking that apart from that, we expect it to be, let's say, similar on a similar level. Then obviously, we will see the positive impact from those acquisitions where, let's just be careful, unit numbers become, less relevant after the acquisitions because, obviously, the Rolls-Royce Power Systems engines, so the previous Rolls-Royce Power Systems we still need to get used to the Deutz engines now.

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They are the larger and thus also more pricey engines. So the average revenue per engine is obviously going to go up significantly. The same applies for the power gensets out of Bluestar, which are no engines, but which are products. So you can see here the unit sizes. We would put less focus on unit sizes going forward, and it makes more sense now to look in revenue.

But to answer your question, August is going to be seasonally weak as I agree. Apart from that, we're probably we're expecting still a bit of a flat development here.

Jorge Gonzalez

I did not really send you the right question because I forgot to mention without the acquisitions. So then for the full year, I mean, well, in my model, even with this run rate that you can get to the EUR 1.9 billion with acquisitions. But I'm wondering, do you have not changed the mid-term targets for next year? Or do you have also not commented much about them in my numbers, I mean, the inconsistencies is also below, it is implying like a rebound of 20%. I don't know if you still think that we can see a pickup of demand in Q4. Is there any green shoots in this regard that make you still optimistic for the last quarter?

Sebastian Schulte

Let's say, we're cautious. We look obviously what our customers and competitors announced and there's a very high level of cautiousness on the pickup of demand. We do see very few customers who actually placed more orders now, but this is really sort of the silver lining so far, not more than that. Actually, I was consciously not talking too much on the '25 targets because it's very difficult to make an assessment. We are very well able to make an assessment on the service business for '25.

We're very well able to make an assessment on the power gen business for '25, but we are reluctant to make an assessment on construction and ag business for '25 because the visibility is just not there. We do not expect it to get worse. That's for sure than this year. But when is the pickup is still a bit unclear, and that's why we're a little reluctant on that. To be perfectly honest, I'm quite glad not having to make a prognosis for '25 yet because there is lots of dynamic just ahead of us.

But that's why we are reluctant on that. Please do not misinterpret that in being pessimistic or not like that. But we just want to say there are certain blocks of our top line where we feel very comfortable, as said service power gen and there are other blocks where we probably need to wait a few more months in order to make a better assessment, that's also why I'm referring again to the Capital Market Day in October, not to promise how much we can say there, but then obviously, the visibility towards '25 is going to be much better than now.

Jorge Gonzalez

So following up on your comment. So then the order intake in Q3, it might be similar to Q2. It could be more or less at the same level with what you are seeing at this point? Or we are still at that point that could worsen a little bit more because tonality...

Sebastian Schulte

We do not see a worsening order intake at the moment if we compare with the past months. So we see this low level to continue for the time being. Again, the acquisitions obviously help us. But my answer was like-for-like.

Jorge Gonzalez

My very last one also on some comments on the mix. The average price for the classic went down slightly year-on-year. But around EUR 300 per engine compared to Q1. So for the rest of the year, in terms of seasonality, we should expect something similar to last year. For instance, something closer to 8,500, 400 something like that or the prices that you are seeing now with the mix that you have now are valid for the rest of the year with what you have in the backlog at this point?

Mark Schneider

Yes, I think it's a very good observation. We do have a change in the product mix. That is also especially true because we are selling more in the U.S. market. In the U.S. market, we have a lot of 2.2, 2.9-litre engines that go into the market that, of course, they're smaller, have a lower average price compared to the big engines, so that does have an effect on the other side. Profitability is not directly linked to the size of the engine. So it doesn't really mean that just because they are smaller, we don't like to sell them as well. That's the one side. If you were asking about the near future now of the next quarters, as Sebastian as just mentioned, we're going to have quite a bit of a change in the product mix because of the comparison and just average engine price in the near future is going to be very difficult.

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Having said that, of course, the service and the gensets will do also play an even bigger role. So I don't think that's the number we can focus on too much in the future. But again, if you're looking back, you're very much correct. It's more smaller engines, especially for the U.S. market.

Operator

The next question from the phone comes from Stefan Augustin with Warburg Research.

Stefan Augustin

Maybe one follow-up here. First, on the development of the business. If you look at agricultural and construction, we clearly go through a de-stocking phase at your customers. If you would have to judge now, what would be your estimate, what the current final demand is actually below the call-off rate or the production rate of your clients. So what would you say is the underlying demand.

I mean the question is actually, when is the backlog the clients worked off and when I pick up starts, but the question is here, do you have a feeling of what would normalize anyway without the broader market finally improving?

Sebastian Schulte

It's difficult to say at the moment, in particular now in the summer breaks. So what we believe the best clarity we get on that is once all the customers return from their summer vacations, summer closures and then what is the rate of order placements there. We do probably now run a monthly process where all our sales force consolidates the signals, the demand from the customers worldwide. We are very interested in what they bring back in the September session of that. Currently, I mean, we have only rather anecdotal knowledge that we see that in some areas, the storage inventories are still there, but going down.

But again, I know that this doesn't satisfy because it's a little wishy-washy, of course, but we really need to see what happens after the summer stoppages, the summer applications are over, particularly in Europe and Southern Europe, in particular, right? U.S. is still, by the way, this is not [ ag ], but this is still very constant. Here we've got better visibility because our main customers are also in our rental companies who have fairly transparent information as part of their capital market disclosures, but the [ ag ] companies is indeed a little bit, I wouldn't call it the black box, but at least the most limited visibility.

Stefan Augustin

Then on your genset deliveries, you said last year, you said you have roughly a signed order for around 100 of these gensets to China. Now we see a delivery of the first 4. Is that how I put the numbers correctly together.

Sebastian Schulte

First 4 is they're not only delivered. I mean, obviously, the engines have been produced already months ago here in Cologne. We have assembled them as a genset also months ago in Ulm at a partner. They've been shipped to China. They're currently already assembled on the demonstration side in Beijing.

We currently expect mid-September, the grand opening ceremony, most likely with high-ranking political representatives joining, I'll also personally be there. So that's very important. That's on the proof of concept, so to speak. There's a huge attention coming on that. We are now working on producing the next sort of 96 on that, which we will then produce, assemble and deliver over the coming months.

Stefan Augustin

These were not yet somewhere in the revenue, right?

Sebastian Schulte

This is something to be seen exactly. We've got the order placed and the first 4 are installed, and we're very excited about that. But look, Stefan, even once the 100 are completed, this is still the beginning of it, right? We're talking about 100 gensets, not about 5,000 or 100,000 or whatever. So this is still like really for this technology, it's a milestone, which I don't think we see anywhere else.

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But in the grand scheme of things, it doesn't move the top line yet significantly, like none of the green products do nowhere at the moment in our field, of course, right?

Stefan Augustin

If I look actually between classic and green. I would say that the performance in green is actually really good in light of the number of lower engines you have to produce. As Timo pointed out, the operational leverage is quite low to the downside. That brings me a bit to green where I see, let's say, the constant amount of EBIT in light of your cost savings ideas, would you envision to be more prudent on the green side and getting the EBIT loss per quarter still lower from the level where we are.

Sebastian Schulte

Yes, absolutely. I mean, I don't want to tease too much, but we're going to go into more detail on the Capital Markets Day on our green strategy. What we've done in the past 2 months is doing a prudent assessment of our electrification portfolio, and we're currently doing the same for our hydrogen portfolio and we'll put a stronger focus on the market. So in other words, we have now shown that we are able to develop a functioning hydrogen combustion engine, so that's great. Does it mean we're developing the next hydrogen combustion engine only then when there is really a market demand and specific orders insight.

If that's not the case, we are very happy to have shown that we can do it. Obviously, half of roughly 50% of the R&D expenses in green, we allocated on the hydrogen combustion engine. So in other words, this is going to be stretched in the future a bit more. Focus is much more. It's on what we need a signal from the market.

On the electrification side, and then I will stop because I don't want to tease too much or anticipate too much what we'll announce on the Capital Market Day. But on the electrification side, we also have our E-DEUTZ portfolio there. Will we invest without market demand and more, most likely only on a very limited basis. But on the other hand, we see also the positive signs, let's say, our green business, which is with the new CEO, Bert van Hasselt, we are doing a fantastic job in hunting new customers, where we're looking here into retrofit opportunities and so on and so forth. So we see the market on small series slowly ramping up, but we need to be more prudent with the R&D expenses, which is generally a valid statement.

Stefan Augustin

The final one is on the extraordinary costs included in Q2. Could you elaborate a little bit how that is actually split? Do we have to expect something in Q3 as well?

Sebastian Schulte

I'm assuming you're referring to the difference between EBIT and EBIT adjusted, correct?

Stefan Augustin

Yes, the EUR 7 million where this is partially for stock options and then there is something for some programs.

Sebastian Schulte

Yes. You mentioned one of the aspects, the deferrals provisions for the LTI. I think that's fairly clear and doesn't probably require additional explanation. The lion's share of the remaining amount really is cost related to transactions, particularly the acquisitions of the Rolls-Royce Power Systems business because we structured that transaction as an asset deal. That's been not always easy to carve out business out of long built organization such as Rolls-Royce and then carve in an equally long built organization.

So it required quite some work on the IT side and thus quite some cost where we used external consultants on as well. Then of course, the typical transaction cost is legal fees and so on. But again, the lion's share to that Rolls-Royce Power Systems business. We had pretty much we were faced with the choice in taking more time and using less external support or getting it done quickly. Then as we have actively decided not to operate or not to entertain huge own resources for something like that.

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We rather work here in a way that if there's a need, we outsource and that keeps us a lean cost structure. Given the fact that for several reasons, we wanted to have that business as quickly as possible in our books, not only for the financial impact, but also in order to allow us to start the marketing of the products with the customers as soon as possible, take uncertainty out of the market. We decided to be front load here a little bit. Yes, that led obviously to cost. Coming back to your other question, we don't expect similar effects in Q3 because the transactions have been closed.

There may be a little bit of cost related to the first month of Q3, of course, but the closing is done, and there's no other large-scale M&A product currently, which leads to this. So yes, this is it and not a continuation expected.

Operator

We have a follow-up question from Mr. Jorge Gonzales.

Jorge Gonzalez

On Blue Energy, I noticed that the expected sales for the year are much better than the ones you presented at the time of acquisition, although you showed a graph now with potential to be above $100 million. But I am wondering, so for next year, should we still assume growth rates of 15%, 20% on top of this EUR 120 million, the $20 million that you are achieving with Blue Star, or we should be more cautious in '25.

Sebastian Schulte

Let's be a bit cautious on that because the company is developing so far better than expected for '24, as you observed fully correctly. We've just taken the ownership 7 calendar days ago. We don't want to intrude too much in order to keep the entrepreneurial spirit. But certainly, one thing we will do is we will get transparency on the planning for next year. Currently, we know that the order backlog of Blue Star is very good.

We know they are sold out from now until March. Obviously, we have interest in expanding the business. We need to now carefully assess what is the capacity of Blue Star for next year? The market is good. The market is good enough to fill up the existing capacity of Blue Star a 1-shift operation.

That's the way they operated so far. Whether next year is already the point in time to increase capacity going to shift, we need to carefully assess. Again, I will ask to be a bit patient until October because then we have certainly a better view on next year. But what we can say is we already received really a lot of interest from the U.S. but also from other countries.

Can you provide us gensets made in America? Now we really check, well, can we? The demand is there, but let's check whether we get the supply up running. But even that, I tell you, even if we are on that level, as you implied, before that sort of [ life style ] better outlook for this year. We're very happy about that because it's profitable business growing quickly.

Jorge Gonzalez

Last follow-up on service. Is there any seasonality for service in Q3 to be considered or the run rate at this point is valid for Q3 and Q4?

Sebastian Schulte

Run rate is fairly valid. It's always give or take, EUR 43 million, EUR 44 million per month. It depends a bit on how many public holidays are in the country. So typically, I mean, the only seasonality is, let's say, Easter is not at the week the month with Easter is typically not great. The months with Christmas is not great.

It's very simple. If the workshops are closed, we're not selling parts, but there's not the sort of typical summer seasonality, at least not as strong right because often, even now our customers use the summer breaks to service their equipment. So I would say this effect, to an extent compensates the fact that other people are on holiday. Here we are like on the service side, I mean, we'll obviously have also the ramping up business with the new products from Rolls-Royce Power Systems that goes a bit delayed to the new equipment sales because it takes for us some time to incorporate the products and the offerings into our workshops. We're also continuously working on other inorganic acquisitions, but it's too early to speak about that.

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But let me tell, we are on track with our service targets for this year as well as for next year.

Operator

Gentlemen, there are no more questions at this time.

Sebastian Schulte

Thank you very much. Then I would close the call. Thank you for your interest and your questions. If you have further questions, please reach out to all for me. With that, have a good day, and I hope to talk to you soon. Thank you.

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