

# **Emerson Electric Co. (EMR) Q3 2024 Earnings Call Transcript**

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**Body**

Emerson Electric Co. (EMR)

Q3 2024 Earnings Conference Call

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Company Participants

Colleen Mettler - Vice President, Investor Relations

Lal Karsanbhai - President & Chief Executive Officer

Mike Baughman - Chief Financial Officer

Ram Krishnan - Chief Operating Officer

Conference Call Participants

Jeff Sprague - Vertical Research

Nigel Coe - Wolfe Research

Scott Davis - Melius Research

Deane Dray - RBC Capital

Steve Tusa - JPMorgan

Andy Kaplowitz - Citigroup

Julian Mitchell - Barclays

Brett Linzey - Mizuho

Christopher Glynn - Oppenheimer

Nicole Deblase - Deutsche Bank

Presentation

Operator

Good day, and welcome to the Emerson Third Quarter 2024 Earnings Conference Call. All participants will be in listen-only mode. [Operator Instructions] After today's presentation, there will be an opportunity to ask questions. [Operator Instructions] Please note this event is being recorded.

I would now like to turn the conference over to Ms. Colleen Mettler, Vice President of Investor Relations at. Ms. Mettler, the floor is yours, ma'am.

Colleen Mettler

Good morning, and thank you for joining us for Emerson's third quarter 2024 earnings conference call. This morning, I am joined by; President and Chief Executive Officer, Lal Karsanbhai; Chief Financial Officer, Mike Baughman; and Chief Operating Officer, Ram Krishnan.

As always I encourage everyone to follow along with the slide presentation, which is available on our website. Please join me on Slide 2. This presentation may include forward-looking statements, which contain a degree of business risk and uncertainty. Please take time to read the safe harbor statement and note on non-GAAP measures. All financial metric in this presentation are on a continuing operations basis.

On June 6, we announced a definitive agreement to sell our remaining interest in the Copeland joint venture. We have included additional information and the accounting treatment of these transactions in the appendix of the presentation.

I will now pass the call over to Emerson's President and CEO, Lal Karsanbhai, for his opening remarks.

Lal Karsanbhai

Thank you, Colleen. Good morning. Please turn to Slide 3. I'd like to thank the 65,000 Emerson employees around the world for delivering another solid set of results. Your commitment to our vision and passion for our purpose comes to life every day. I am moved by our customer focus and the deep care you have for each other, and I am proud and honored to work alongside each of you. Thank you to the Board of Directors for your support of the management team and to our shareholders for your trust in us.

Since I became CEO in 2021, we have talked openly about the transformation of Emerson driven around the three pillars of culture, portfolio and execution. We have moved rapidly to improve across all three. And before we discuss the quarterly financial results, I want to highlight the results of our latest employee survey to show our employees are with us on this journey as our culture continues to evolve.

Our latest company-wide engagement survey, inclusive of Test & Measurement had a participation rate of 89%, up 1.4 points from our 2023 survey. We had an engagement score of 79%, a 1-point improvement and only 1 point from world-class levels of 80%. While this is an evergreen journey, and we still have work to do, I am excited about the tangible steps we have taken to create a more inclusive and engaged organization.

Now let's jump into the operating results. Q3 was another solid quarter for Emerson. Orders in the quarter returned to growth and were up 3% year-over-year, driven by strong project activity in our Process and Hybrid businesses, especially across life sciences, energy and power. Notably, we won several large life science projects in North America and Europe focused on expanding production capabilities for advanced medicines.

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The Middle East and Latin America saw exceptional demand, and we were awarded several large projects in each. As we expected, Process and Hybrid markets remained steady at mid-single-digit growth as we continue to see investments, particularly in LNG, life sciences, energy and sustainability.

While capital project investments continue to progress, MRO orders were slightly softer than expected in the quarter. Discrete Automation orders were softer than expected, down low single digits both year-over-year and sequentially as factory automation end markets remained weak. The green shoots we were beginning to see through April and May took a step back in June, and we are now expecting a slower recovery, though we expect Discrete Automation orders to be flat to slightly positive in Q4 on a low base of comparison.

Excluded from underlying, Test & Measurement orders remained soft, down 11%. Additionally, for total Emerson, we saw a weaker demand environment in China across most of our business segments. We now expect low single-digit underlying order growth for the second half and for the full year.

Emerson delivered strong operating results with margin leverage, adjusted earnings per share and free cash flow all exceeding expectations. Sales came in at the low end of our guide, and I'll provide additional color on the next slide.

Due to weaker orders, Test & Measurement sales also came in slightly below expectations. However, profitability met expectations as we are seeing the impact of our synergy realization. Transportation and semiconductor markets remain weak, while aerospace and defense performed well, and we saw continued government spending and research.

The European market was softer than expected amid lingering EV demand concerns, and China remains sluggish across most Test & Measurement segments. Due to this, we are looking into second half of 2025 for recovery in this business.

With softer orders, we are adjusting our full year sales to be $1.45 billion to $1.5 billion, but the accelerated synergy actions we have taken will help protect profitability and position the business well for a return to growth.

We continue to be excited about the value creation potential of our differentiated portfolio. Emerson's strong performance through the first 9 months and resolute focus driven by our Emerson management system gives us the confidence to execute on our 2024 plan.

We expect underlying sales of approximately 6% and are increasing the midpoint of our adjusted EPS guide to $5.45 to $5.50 and we are raising our free cash flow guidance to approximately $2.8 billion. We look forward to a strong finish to 2024 and are energized to deliver continued value creation for our shareholders.

Please turn to Slide 4. Underlying sales growth was 3%. Life sciences and power markets continue to perform well, both up double digit as we executed key projects across North America and Europe. Europe is seeing continued strength in energy, power and sustainability markets as well as our MRO business, particularly in Western Europe.

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In the Americas, broad-based healthy growth across Latin America was slightly offset by slower MRO in North America. Robust performance in the Middle East, driven by strong project activity was offset by broad-based weakness in Asia.

Continuing the exceptional gross margin performance from last quarter, gross margins were 52.8% in Q3, a 230 basis point improvement from the prior year. Our gross profit percentage year-to-date is 50.6%, even with the acquisition and integration costs incurred in Q1. This gives us confidence in our expectation that this portfolio will deliver greater than 50% gross margins as we look forward.

Operating leverage was 67%, significantly stronger than expected due to better performance from AspenTech, project mix and realization of more cost reductions than expected from actions taken throughout the year.

Adjusted earnings per share exceeded expectations at $1.43, above the top end of our guide and up 11% from 2023. Emerson generated robust free cash flow of $975 million, up 27% year-over-year and with a free cash flow margin of 22.3% for the quarter. Mike will walk through additional details on our results in a few slides. We are pleased to deliver another strong quarter and are excited to continue demonstrating the value creation potential of our transformed portfolio.

Please turn to Slide 5. We continue to see strong capital project investments with our strategic project funnel now at $11 billion, up approximately $200 million from Q2. The funnel growth demonstrates the strong sustained capital cycle aligned to our growth programs. As the increase predominantly came from projects supporting energy transition, life sciences, sustainability and decarbonization.

In the third quarter, Emerson was awarded approximately $350 million of project content, consistent with prior quarters. We had wins in large traditional energy projects as well as additional awards from offshore vessels in Brazil, as mentioned last quarter. Our growth programs also performed well in the quarter, accounting for a little under half of the awards, and I want to highlight a few key wins.

Emerson was selected to automate Nemaska Lithium Whabouchi Mine at the Bécancour lithium conversion facility projects in Quebec, Canada. Based on our proven ability to provide a differentiated solution, including a common control platform across sites. This mine is one of the largest high-purity lithium deposits in North America.

Fueled by hydroelectric power, the Bécancour facility will convert to spodumene concentrate to lithium hydroxide. This is the first such conversion in Canada and Nemaska Lithium projects will play an important role in the North America battery value chain. Emerson will provide much of our leading technology to automate both facilities, including DeltaV control systems and software, reliability solutions, valves and instruments. This example highlights the breadth of the Emerson portfolio and demonstrates how we are well suited to serve this emerging market.

Next, I'd like to highlight Emerson was selected to support one of the largest renewable energy park projects in India, spearheaded by one of India's largest and most prominent renewable energy companies. Emerson will provide our Ovation Green SCADA solution, including pitch control and park power management for the wind turbines. Emerson was chosen for our scalable automation software and technologies that enhance wind turbine performance as well as our comprehensive local support capabilities, including engineering, fuel support and production.

Finally, Emerson was chosen to automate a key green hydrogen project in Uzbekistan, which will use a 52-megawatt onshore wind farm to produce 3,000 tons of green hydrogen annually, which will be used to manufacture 500,000 tons of ammonia fertilizer.

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ACWA Power, a first mover on green hydrogen and part of the NEOM Green Hydrogen project will operate the plant and H-TEC [ph] will design and construct the facility. Emerson was selected for our advanced technologies and domain expertise and will provide several technologies from our hydrogen portfolio, including instruments, control valves and our Ovation Green control system.

Turning to Slide 6. We remain focused on driving our strategic priorities, including accelerating innovation for profitable growth and enhancing our position as a global leader in automation. One of our breakthrough innovation priorities is software-defined automation. Our industry-leading Ovation Automation platform just launched a software-defined AI-ready platform for the power and water industries.

The Ovation Automation Platform 4.0 builds upon our boundless automation vision to bring a unifying data fabric across the organizations to optimize operations from device to enterprise. Ovation 4.0 brings customer-focused innovation, such as secure generative AI models to offer prescriptive operations and maintenance guidance together in a robust solutions portfolio. It also offers integration with our Ovation Green software to improve holistic awareness across traditional and renewable power generation and storage to aid customers who have an increasingly complex mix of generating assets.

Customer-focused innovation is a hallmark of Emerson, and I wanted to highlight one of the key methods we have for formal engagements. Our Ovation business recently held their 37th Users Conference in Pittsburgh, Pennsylvania, with 70% of U.S. power utilities participating in a multi-day event focused on the power and water industries. This conference featured interactive technology exhibits, customer case studies and collaborative industry sessions focused on emerging technical and business topics. Ovation Users Group creates a world-class engagement as users provide direct input for potential product enhancements, which helps inform our strategic product development plans.

We also took a key step forward in our transformation and simplification journey in Q3 as we announced a definitive agreement to sell our remaining interest in the Copeland joint venture. Private equity funds managed by Blackstone will purchase the equity stake, while Copeland repurchased the sellers note. The transaction involving the Copeland note receivable closed on August 2, with pretax cash proceeds of $1.9 billion, which will be used to pay down debt. We expect the equity portion to close by the end of August.

With that, I'll now turn the call over to Mike Baughman to walk through our financial results in more detail.

Mike Baughman

Thanks, Lal, and good morning, everyone. Please turn to Slide 7 to discuss our third quarter financial results. Underlying sales growth was 3%, led by our Process and Hybrid businesses and partially offset by continued softness in discrete. Price contributed 2 points of growth. Underlying growth was similar across regions, with Europe up 4%, the Americas, up 3% and Asia and the Middle East, up 2%.

Intelligent Devices grew 2%, while software and control grew 7%. AspenTech sales were stronger than expected, growing at 7%. Discrete Automation was down mid-single digits, lower than expected due to a slower pace of recovery amidst continued market weakness.

Test and Measurement, which is not included in the underlying metric contributed $355 million to our net sales, slightly below expectations for the quarter. As expected, backlog decreased slightly from Q2 and exited Q3 at $7.4 billion.

Adjusted segment EBITDA margin improved 20 basis points to 27.1% due to strong gross margin performance, favorable price cost and the benefit of cost reductions. This quarter's adjusted segment EBITDA margin of 27.1% is a record high compared to 26.9% last year in Q3, which was the previous record high. Test and Measurement adjusted segment EBITDA margin was 21.4%, sequentially flat on slightly lower volume as we continue to see the benefit of our synergy actions.

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Operating leverage, excluding Test and Measurement was 67%, exceeding expectations. This outperformance was driven by a higher portion of software revenue and fewer lower margin project shipments than expected, offset by negative geographic mix.

Strong quarters from AspenTech and Control Systems and Software benefited leverage. Discrete Automation had sequential margin improvement from cost actions we took as we saw market conditions continue to decline. The operating leverage from our measurement and analytical business was dilutive in the quarter, primarily due to geographic mix and slower MRO. Adjusted earnings per share grew 11% to $1.43, and I will discuss that in more depth on the next chart.

Finally, free cash flow was $975 million, up 27% versus the prior year and above expectations. This was driven by earnings and improvements in working capital, especially in inventory and receivables. Free cash flow margin in the quarter was 22.3%, inclusive of $40 million of cash outflow for acquisition-related costs, integration activities and elevated capital expenditures. To date, we have incurred $210 million of the anticipated $250 million headwind we discussed last November.

Please turn to Slide 8. Our adjusted earnings per share increased $0.14 from the prior year. Strong performance from operations, especially in our software and control businesses contributed $0.16. Corporate was a $0.02 drag due to a higher income tax rate caused by an earnings mix skewed toward higher rate jurisdictions.

AspenTech contributed an incremental $0.03 versus the prior year, higher than expected due to outperformance in GACV and higher revenue. Test and Measurement contributed $0.09, slightly below expectations driven by lower volume. We also had a $0.01 headwind to expectations in Q3 as we stopped accruing interest income from the Copeland note receivable when we reached a definitive agreement to sell it on June 6.

Please turn to the next slide for details on our updated guidance for 2024. Fiscal year 2024 underlying sales are now expected to grow approximately 6%, in line with the midpoint of our May guidance, which is supported by our process and hybrid businesses, which continue to perform well amid a delayed discrete recovery and a weaker China.

Reported net sales growth is expected to be approximately 15%, with Test and Measurement contributing approximately 9.5 points of growth, offset by a 0.5 point drag from FX. We are increasing our operating leverage expectations to the mid- to high 40s, driven by the strong leverage performance through the first 9 months and strong leverage expected in Q4.

We are raising the midpoint of adjusted EPS guidance and expect $5.45 to $5.50. Test and Measurement is now expected to contribute $0.42 to $0.44. Test and Measurement is a business with very strong leverage, so the impact of our synergy actions are helping maintain profitability despite a weaker volume environment than initially planned.

For the full year, we expect Test and Measurement's adjusted segment EBITDA margin to be approximately 23%, a couple of points above the prior year benefiting from the synergy realization. With AspenTech's strong results in Q3, we are bringing their expected EPS contribution back up to $0.32 to $0.34.

We are also raising our free cash flow expectations for the year to approximately $2.8 billion, driven by the working capital improvements and Q3's performance. Dividend and tax rate expectations are unchanged, and we now expect approximately $300 million of share repurchase. We have been focused on debt pay down, particularly with short-term interest rates staying higher for longer, and we retired €500 million of term debt that came due in Q3.

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Our performance through the first 9 months has exceeded expectations, and we are excited to continue delivering strong results. Our transformed portfolio has meaningfully improved with higher profitability driven by gross profit margins above 50% and higher organic growth driven by secular trends, and our Emerson management system is driving operational excellence.

With that, I'll turn the call over to the Q&A portion of our call.

Question-and-Answer Session

Operator

Thank you, sir. We will now begin the question-and-answer session. [Operator Instructions] And the first question we have will come from Jeff Sprague with Vertical Research. Please go ahead.

Jeff Sprague

Hey, thank you. Good morning, everyone. Two questions, one big picture and one smaller picture, I guess. First off, kind of the big picture stuff. Lal, this idea of kind of software-defined automation and what you're doing with Ovation. I think this is also sort of instrumental to better collaborating, integrating whatever you want to say, between DeltaV and Aspen's offerings.

Maybe you could kind of address that, if I'm correct in that assumption and where you're at and sort of kind of propagating that change in technology posture across rest of the portfolio.

Lal Karsanbhai

Yeah. Good morning, Jeff, good to hear from you. No, you're absolutely right. As we laid out that vision, it certainly is designed to accomplish a couple of factors. The first being to liberate the data that exists in silos across operations in broad industry. And the second then is to actually use the analytics power to drive productivity, efficiency, higher levels of safety and efficiency with analytic packages inclusive of much of what AspenTech can bring to the table to optimize facilities and production.

So that vision certainly exists. We are on the path to bring compute out of centralized siloed data approaches into the edge, which is the first step with products that have already released in the marketplace with DeltaV, and we'll continue to move forward to deliver on the vision. But this step with Ovation was very critical as well because, as you know, that serves the power and water industries exclusively and to be able to bring that capability into those markets was critical.

Jeff Sprague

Great. And then kind of more near term, and I may have missed it. I was on 5 or 10 minutes late. But kind of the shorter-cycle elements of the portfolio, just your view on when discrete bottoms when NI bottoms, you brought down the order outlook a little bit for the year, which is probably tied to those end markets. But maybe just what you see as we start to look into 2025 and the eventual bottoming and turning in those end markets?

Lal Karsanbhai

Yes. No, certainly. So the discrete cycle recovery has been slower than expected. We certainly believe that we can get to close to positive orders in the last quarter of the year here on discrete, but that will be, of course, based on some very weak comparisons. But that will start us on the path to recovery into 2025.

Test and Measurement, a little slower. We're watching our customers very carefully there, speaking, engaging with them. We're watching our peers in the marketplace as well and their performance. And we foresee sales turning positive there in the second half of 2025 with orders turning positive in the first half of 2025.

And then lastly, Jeff, I'll just add that offsetting a lot of that is what continues to be a strong capital cycle formation cycle here with process and hybrid markets and also momentum in what we see at AspenTech. And so those offset a little bit of how we're thinking. Certainly, I believe that as we think about 2025 and start to guide that we will be probably towards the lower end of that range that we've given on our through-the-cycle expectations, but well within that.

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Jeff Sprague

Great. Thank you.

Operator

And next, we have Nigel Coe with Wolfe Research.

Nigel Coe

Thanks. Good morning, everyone. Thanks for the question. Just want to pick up on the last question from Jeff there. The $1.45 billion to $1.5 billion range for Test and Measurement in 4Q is obviously quite wide. I think just given the expectation that we don't get to revenue growth until the second half of the year, it seems that we're tracking towards the lower end of that range. Just wanted to make sure that was correct.

Lal Karsanbhai

We guided because we still have confidence that we can hit within that guide, Nigel, I certainly don't -- wouldn't write it up to the low end of the range at this point. This is the best guide that we feel we can commit to as a management team. Obviously, at some point in the midpoint is how you can think about it.

Nigel Coe

Okay. Great. And just to kind of zooming out a sort of a general comment on the environment out there. Obviously, we've seen deterioration in sort of general industrial markets, it feels like some projects are again delayed with some of the uncertainty, maybe higher rates. Just give an overview in terms of what you're seeing out there from customers, maybe a bit more of an end market overview.

And just wondering, obviously, the funnel remains very vibrant, increased slightly Q-over-Q. But what about this funnel to order kind of conversion process? Are you starting to see longer decision-making?

Lal Karsanbhai

Yes. Thanks, Nigel. Yes, I'll comment. Of course, the funnel did grow, as you noted. We booked approximately an equal amount that we've been booking historically on a quarterly basis, $350 million in value. The mix changes a little bit depending on end market timing, and we shared that with you as well in the deck.

So I continue to look at this the funnel and the capital formation cycle in a positive manner. I haven't seen degradation of projects or projects being eliminated. I haven't seen any slowdown in the expansion of the journey -- the sustainability projects or the LNG, particularly as it relates to the Middle East and Africa. So I'm still very optimistic there.

Now what we do -- we are watching very carefully is that projects that have been booked, the pace at which our customers are willing to accept product whether there are delays that are being implemented around inspections and other areas, we're watching that very carefully, and we have experienced some of that in the quarter, which obviously contributed to our lower sales 3% versus the low end of our guide versus the expectation. But that -- there's some of that going on, which obviously we're watching very carefully.

Mike Baughman

I would just add to that, Nigel, some of that read through in the leverage this quarter. We talked in the comments about some projects that did get pushed out, which was a little addition by subtraction because those projects are generally lower margin. So it was part of the 67% in the quarter.

Lal Karsanbhai

That's a very good point. And of course, lastly, Nigel, to the question. Our process and hybrid orders are still up mid-single digits, and that's important to recognize.

Nigel Coe

That's great. Thanks, Lal.

Lal Karsanbhai

Thank you, sir.

Operator

And next, we have Scott Davis with Melius Research.

Scott Davis

Hey, good morning, everybody. And congrats on navigating through the choppiness here. I kind of curious, I mean you're going to have a fair amount of cash on hand. Once you get this Copeland thing done, seem kind of in a good spot from a leverage. Do you feel like you -- I mean, I guess my question really is, what do you plan to do on the proceeds, but I guess more explicitly is, do you feel like you have the capacity to do M&A? Or are we still digesting NATI [ph] this point and want to focus on that?

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Lal Karsanbhai

Yes. No, certainly, I feel great about the balance sheet and what we have to do in terms of maintaining our investment grade. And I think that's very important. We are working very hard to integrate National Instruments and feel really good about the progress that, that team continues to make. It's a set of markets that we like that will drive differentiation and through the cycle growth for our company. And I think that's -- that we feel very good.

Now having said all that, we will have the capacity, if we wish to put that balance sheet to work. And that's something that, Scott, as you know, will continue to evaluate the time and what the right move would be in terms of the majority position that we own in AspenTech.

Scott Davis

Okay. Fair enough. And then I wanted to follow up on Jeff's question on Ovation because I think it's -- you put it on a slide, and it's not a product line. I think historically, you guys have talked about it a lot, but it is a pretty powerful installed base that you have. I mean how big a deal is this 4.0 upgrade? And is there a way for us to think about like what percentage of your installed base you would expect to upgrade? Or is there some sort of kind of way to tangibly think about the impact of this iteration?

And is iteration even the right word to use? Is it a step change, a meaningful step change where you kind of hit that tipping point where people -- like you said 70% of the people came to your event, where people just generally hit the bid on that more so than maybe they did in the past. Any color there would be helpful?

Lal Karsanbhai

Yes. From an Ovation perspective, we've continued to have significant releases in the capabilities of that technology over time. And this is certainly a significant one, which incorporates a lot of technology from Aspen and fundamentally from an optimization perspective, from an analytics perspective, from -- in terms of copilots provides capability that we've not had innovation before.

And I think it is significant given the fact that the investment in the power generation infrastructure in this country and globally is at a tipping point. And just given the boom in AI and data centers, and we talked about it in the last earnings call, we expect the power generation investments as well as transmission and distribution and renewable to be a very, very important growth vector for us. Innovation 4.0 certainly positions us very well in that capacity. And frankly, on greenfield, our modernizations are lifetime extensions of power plants, but also the opportunity to go in and upgrade existing systems with the new capabilities that we have in 4.0. So that's really what we're very excited about.

Mike Baughman

And I think the step change here to your question, Scott, lands on the use of the AI models, which will enable planning purposes around maintenance, taking down assets for turnaround activity. It will give a higher probability that you're actually going to work on the maintenance records and elements that are -- that most needed in the plant. And I think that's incrementally new and different in the marketplace.

And then lastly, Scott, we're highlighting this innovation, but innovation is a core pathway as we've talked in the past, of how we drive differentiated growth at Emerson. Accelerated innovation across our businesses is critical. And we've seen that. You see that as we report R&D spend as a percent of sales, then we have stepped that up, and this is an element in one of the results of that.

Scott Davis

Okay. Appreciate the color. Thank you, guys.

Mike Baughman

Thank you, Scott.

Operator

And next, we have Deane Dray of RBC Capital.

Deane Dray

Thank you. Good morning, everyone.

Lal Karsanbhai

Good morning, Deane.

Deane Dray

I'd like to go back to Page 5 and ask whether you're seeing much demand or overlap with the mega projects. I guess the latest count is 440 projects over $1 billion. If -- how much does this funnel overlay to those? And what kind of visibility do you have?

Lal Karsanbhai

So in terms of -- I'm not quite sure the reference you made, Deane, can you clarify the mega projects you referenced?

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Deane Dray

Yes. This has been a big focus across the industrials for the past year, looking at North America, non-res construction projects over $1 billion, and it encompasses everything from software to batteries. But it's just -- it's a way for us to look at all these secular drivers and how are they translating actually into projects. So it's become this benchmark indicator that we're using now. And so that's the reason I'm asking. You're looking at this funnel, it's a global funnel, I get it, but within -- for North America, how much overlap do you have with these so-called mega projects or maybe you have that information.

Lal Karsanbhai

Yes, we'll go back and map that, but what I will tell you is in terms of LNG, in terms of energy, in terms of life sciences and frankly, also semiconductors and EVs, we have our own map of all the project activity in North America. We'll go back and map it with what you're referencing, but I will tell you that we are certainly participating and every one of those projects are in our funnel with very, very good win rates. And -- but it's an action we'll take away and work with Colleen and get that map. But our participation in North America on those large projects remains very solid. And we had a very good level of project activity in North America, particularly in life sciences and power in the control systems business even in the current quarter.

Colleen Mettler

Yes. And as a reminder, that funnel represents our automation content versus what the entirety of a project is out there in the universe. So that's also to keep in mind.

Deane Dray

Of course. All right. So we'll be looking forward to that. And then second question is a bit of a follow-up from Scott on the balance sheet and the cash. Just can you talk to the decrease in buybacks? I know you said that your use of capital was buying back the Copeland note, but all cash is fungible and just directionally to be pulling away from buybacks. Just maybe -- I know it's early to talk about '25, but just where do buybacks fit in your priorities?

Mike Baughman

Deane, it's Mike. Yes, buybacks are definitely still in the priority along with the dividend and returning capital to shareholders generally. We will exit the year with the commercial paper paid off and 3.5 - $3.5-plus billion [ph] of cash on the balance sheet. But our capital allocation will remain the same. We will continue to focus on funding our organic growth initiatives, we'll be continue to be committed to the dividend and bolt-on M&A that improves the portfolio. And then, of course, there'll be share buybacks. So yes, we will continue with share buyback. We'll be in the market this quarter at, we think, roughly $125 million, which gets us back to that roughly $500 million a year pace.

Deane Dray

Thank you.

Operator

Next, we have Steve Tusa of JPMorgan.

Steve Tusa

Good morning.

Lal Karsanbhai

Good morning.

Steve Tusa

Could you just talk about like the seasonality of your underlying cash flow putting Aspen aside Typically, I think you have a pretty strong 4Q historically. And you're raising it this year. I guess, how do we think about cash in the fourth quarter and then into next year?

Mike Baughman

Yes. So we took the guide up to 2.8 and -- which would imply about $800 million coming through in the fourth quarter, which I think is reasonably consistent seeing a fourth quarter increase. So this third quarter was particularly good. And remember, that has Test and Measurement in there, which they had a great quarter and peeled [ph] about $50 million off the balance sheet, which did skew the numbers this year. So we feel good about the 2.8 for the year and looking at the 800, it looks pretty in line with some of the prior years.

Steve Tusa

And then just looking out to next year, anything in the bridge that's more mechanical that you know of today, whether it's merit increases, bonus payments or anything that's kind of outside the normal operating leverage dynamics that we should be aware of?

Mike Baughman

I can't think of anything in the kind of run the business. But at corporate, I would say we are looking at a headwind and a tailwind that will largely offset and be a slight headwind. And we will have an increase in pension expense, all things equal, just given the way the deferral accounting works. And then we'll have a lower interest expense because of the Copeland proceeds that come in. Lower interest expense overall with more cash yes. So that should net to a pretty small headwind at corporate.

Steve Tusa

Okay. And then one last quick one for you guys. What are the plans for Aspen? Are you guys planning to move on that this year?

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Lal Karsanbhai

Not in this fiscal, as I said, we'll continue to evaluate Steve as we go through time here.

Steve Tusa

Sorry, sorry, I'm already on the 25. I meant fiscal '25. That's I'm already thinking about next year. Sorry about that...

Lal Karsanbhai

And forward-looking...

Mike Baughman

No comment there.

Steve Tusa

Okay, thanks.

Operator

Next, we have Andy Kaplowitz of Citigroup.

Andy Kaplowitz

Hey, good morning, everyone.

Lal Karsanbhai

Good morning, Andy.

Andy Kaplowitz

Well, operating leverage for Emerson has continued to be impressive. And obviously, you raised your guidance for this year to mid-40s, which is higher than the algorithm you gave us at your last Investor Day. We know price maybe is fading a bit as a help, maybe supply chain wins are less likely to help in FY '25. I think you just answered Steve's question about sort of other puts and takes, but can you sustain incrementals in the 40s in '25 from what you see today?

Mike Baughman

Yes. Thanks for the question. We believe we can. We have a significantly higher margin portfolio today with a 1,000 basis point move over the transformation of Emerson to plus 50% GP portfolio. And I think our expectation certainly is that next year will be very similar to the leverage rate of this year.

Andy Kaplowitz

Great. And then, Lal, you mentioned you have decent visibility towards, I think, the low end of your 4% to 7% due to cycle revenue growth as an initial read into FY '25. I guess what do you need to see to achieve that kind of growth for instance?

Lal Karsanbhai

Yes, go ahead, Ram.

Ram Krishnan

Yes. So I mean, obviously, what we're seeing right now is based on the order rates that the second half of this year will generate and that points to the low end of the 4% to 7%. Now what has to change, obviously, at the areas we're really focused on is pace of discrete recovery, the amplitude of the recovery and then China. And now the North American KOB3 or the pace of business is something we're watching. We're not really concerned. Our process hybrid business continues to have order rates of mid-single digits. The capital cycle still remains strong.

So that we feel very good about. It's really the pace and amplitude of discrete recovery in China is going to dictate how we guide into next year as we come off that low single-digit order growth we've seen in the second half of 2024.

Andy Kaplowitz

Lal, you've seeing China stable at low levels? Or is it getting worse? What's China...

Lal Karsanbhai

I'd suggest stable, Andy, at this point.

Andy Kaplowitz

Excellent. Thank you.

Operator

Next, we have Julian Mitchell of Barclays.

Julian Mitchell

Hi, good morning. I think...

Lal Karsanbhai

Good morning, Julian.

Julian Mitchell

Good morning, Lal. Maybe where I wanted to start was just around the different end market verticals because I suppose the lowered orders guide and the slight miss on sales in Q3. Was that solely tied to discrete automation? Because I suppose listening to an automation peer half an hour ago, they do talk about weaker energy transition CapEx, weaker chemicals and mining spend and Aspen last night referred to some weakness in those types of process verticals as well. So just trying to understand that element of sort of process versus discrete the outlook there?

Lal Karsanbhai

Yes. No, I'll answer and let Ram add some color as well from his perspective. Certainly, we continue to see strong capital formation cycle here, particularly as it relates to energy, energy transition, power generation, life sciences, metals and mining. And that is relatively broad from Western Europe through the United States and into Middle East and Latin America. And I -- so I haven't -- I don't have a whole lot of concern today around those markets.

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We -- I highlighted a few specific wins, but there are others in that $350 million bucket that we won. So mid-single-digit order growth in process and hybrid in the quarter, low single digit for the company impacted by the discrete automation business in the discrete orders, which remains negative to the quarter. Ram?

Ram Krishnan

Yes, you said it. I mean I think the cap for us, energy, power, life sciences is driving a majority of our capital project wins as well as the momentum in our process hybrid business. Certainly, we are not a big player in hybrid markets like food and beverage, which could be the dynamic you're referencing in terms of some slowdown. But our life sciences business continues to be very good. Our metals and mining business continues to be very good. So no slowdown, we're not seeing any kind of slowdown in that area.

But the area we're watching very carefully, as I referenced, is the pace of discrete recovery, particularly markets like semiconductors and EVs which impact NI, but also our markets like automotive, which impact our broader discrete automation business.

Now the one segment of Test and Measurement, where we've seen good momentum is aerospace and defense, driven by government spending. It's 25% of their overall mix. So that certainly come out strong, and that's driven growth in North America, but we are yet to see sustained recoveries in semis and EVs, which are markets we're watching closely.

Julian Mitchell

Thanks very much. And then just my follow-up, somewhat related. But if I look at your backlog, I think that was $7.4 billion at the end of June, so sort of down a little bit sequentially and down a little bit from where it was in December as well. When you think about that backlog, it's moving around entry-year [ph] on seasonal factors as much as anything else. Do you still feel confident about sort of decent backlog growth as you enter fiscal '25?

Mike Baughman

Yes. Yes, we do. That backlog reduction for us, frankly, about $100 million, it was all in Test and Measurement. Our backlog in the base Emerson business held effectively flat. Now we typically see a backlog reduction in Q4, but it will be up year-over-year, and we feel pretty good about backlog levels as we enter 2025.

Lal Karsanbhai

And I would add to the earlier comment about the capital formation, Interestingly, in the quarter, the control systems business actually had a book-to-bill above 1 record order...

Mike Baughman

Record levels. And for the full year, we expect Emerson at right around 1...

Lal Karsanbhai

Book-to-bill.

Mike Baughman

Yes.

Julian Mitchell

That's great. Thank you.

Operator

And next, we have Brett Linzey of Mizuho.

Brett Linzey

Hi. Good morning. Thank you. Just wanted to come back to the discrete comments around pace and the amplitude of the recovery. As that business comes back, should we think about the operating leverage above the 45% framework given some of the cost containment and some of the actions you've taken there?

Mike Baughman

Yes. I would say for our discrete automation business, it will be right around in the 40s. Certainly, the other business that's exposed to the discrete end markets, Test and Measurement, given that 75-plus percent GPs will be much higher.

Brett Linzey

Okay. Got it. And then just on power generation. So you've talked about some of the momentum there in that business. I think the grid results at Aspen look pretty encouraging. Any update on the strategic funnel and how that tracked through the quarter and some of the activity you're working on there?

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Mike Baughman

Yes. I mean I think our -- so Aspen clearly referenced the capital formation in grid modernization, which is fundamentally transmission and distribution investments. So our exposure to the T&D side is through OSI at Aspen. On the power generation side, which is the Aviation business, that project funnel continues to build both in North America, Europe, but also we're having a very, very strong year in China interestingly.

So overall, the generation capacity that is being invested in across the globe continues to be robust and the innovation that we're driving with the likes of Ovation 4.0 as well as our Ovation Green that is positioned for renewable investments. The activity there is very robust. Lal referenced that one project in India with a very strategic investment that's happening in India and the renewable space is just an example of the types of activities we're involved in with the Ovation platform.

Brett Linzey

Okay, great. Appreciate the color.

Operator

Next, we have Christopher Glynn of Oppenheimer.

Christopher Glynn

Thanks. Good morning. I had a question on the MRO. Curious if -- how that performed specifically in the quarter, sorry if I didn't catch it. But wondering if there's an impact of some customer inventory rebalancing, if you're seeing any of that from maybe accelerated lot sizes in prior years? Or if end markets are mainly what you're seeing on the MRO side?

Lal Karsanbhai

Yes. This is Lal. I -- certainly, in totality, MRO didn't really change a whole lot. It remains at 64% of the revenue in the quarter, which is relatively consistent with where we've been and well within our expectation for the year. Having said that, there were a few ebbs and flows, as I discussed on the call, European MRO was very strong in the quarter. North America MRO was softer in the quarter. We haven't seen anything there that is alarming in any way. We're not a heavy inventory-driven company from a distribution or customer level perspective. Our equipment is generally bought and put into operation shortly thereafter. And so consequently, and nothing alarming on the MRO side. But again, strength in Europe, weakness in North America or softness in North America characterized the quarter for MRO.

Mike Baughman

Yes. And just to build on that a little bit. The North American softness, you'll recall in prior quarters, we had talked about how, particularly in the measurement and analytical business, there was some strength, and we saw a little bit of that reverse in the quarter. But as Lal said, nothing concerning.

Christopher Glynn

Got it. Thank you.

Operator

Next, we have Nicole Deblase of Deutsche Bank.

Nicole Deblase

Yeah, thanks. Good morning, guys.

Colleen Mettler

Morning.

Nicole Deblase

Maybe just starting with the T&M business. It sounds like the synergy progress is going a bit better than planned. Are you guys actually raising the synergy guidance there? Or is it more about timing, like coming through faster than expected? And maybe any updated thoughts on synergies in fiscal '24?

Lal Karsanbhai

Good morning. No, look, we raised the guide a few quarters ago. We continue to execute across that pace. So no change to the synergy guide, but we are maintaining the pace certainly to be able to deliver these results.

Nicole Deblase

Okay. Got it. Thanks, Lal. And then if I could ask a bit of a detail -- a little bit more detailed question. The discrete automation comps do get a lot easier in the fourth quarter. Is it possible that organic revenue could turn positive? Or do you think that that's more of a 1.25 [ph] event at this point?

Lal Karsanbhai

Go ahead, Ram.

Ram Krishnan

Yes, it's a 1.25. I think orders turned positive in Q4. At this point, we're planning on a first half 25% recovery in sales for the discrete automation business.

Nicole Deblase

Thank you. I'll pass it on.

Lal Karsanbhai

Thank you.

Operator

Well, this concludes our question-and-answer session and today's event. I would like to thank the management team for their time today, and thank you all for attending today's presentation. At this time, you may disconnect your lines. Thank you, and have a great day, everyone.

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