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Westinghouse Air Brake Technologies Corp. (WAB)

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning and welcome to the Wabtec Second Quarter 2020 Earnings Conference Call. All participants will be in a 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 Kristine Kubacki, Vice President of Investor Relations. Please go ahead.

Kristine Kubacki
Vice President-Investor Relations, Westinghouse Air Brake Technologies Corp.

Thank you, operator. Good morning, everyone, and welcome to Wabtec’s second quarter 2020 earnings call. With us today are President and CEO, Rafael Santana; CFO, Pat Dugan; President of Freight Services, Pascal Schweitzer; Senior VP of Finance, John Mastalerz. Today’s slide presentation along with our earnings release and financial disclosures were posted on our website earlier today and can be accessed on our Investor Relations tab on wabteccorp.com.

Some statements we’re making are forward-looking and based on our best view of the world and our business today. For more detailed risks, uncertainties and assumptions relating to our forward-looking statements, please see the disclosures in our earnings release and presentation. We will also discuss non-GAAP financial metrics and encourage you to read our disclosures and reconciliation tables carefully as you consider these metrics.

And now, I will turn over the call to Rafael.

Rafael O. Santana
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

Thanks, Kristine, and good morning, everyone. We appreciate you joining us today and I hope you and your families remain healthy and safe. Before we get started, I’d like to once again thank our employees out in the field, in our factories and those working from remote locations for continuing to keep our facilities safe and operational through this pandemic. I’m very proud of how our teams has responded to the challenging environment, delivered for our customers and supported one another during a time when healthcare, economic and social tensions run high, and you see that reflected in our second quarter results and long-term focus.

Turning to slide 3, we had a strong execution in the second quarter despite a difficult environment. Total sales for the quarter were $1.7 billion driven largely by the international freight market and services but offset by disruptions due to COVID in both the freight and transit end markets. Adjusted operating income was $262 million, resulting in an adjusted margin of 15.1% which was impacted by the drop in sales across freight and transit but somewhat offset by synergies.

Cash flow from operations of $311 million was driven by strong cash conversion and good working capital performance. This allowed us to further strengthen our financial position, pay down debt during the quarter by $300 million and increase our liquidity position by $700 million. Total multi-year backlog was over $21 billion, providing us continued visibility across freight and transit despite market conditions. And finally, we ended the quarter with adjusted EPS of $0.87, demonstrating that we’re taking the steps necessary to control what we can, protect the long-term viability of the company and deliver shareholder value.
With that, let's dive into some actions underway. As you know, we remain committed to our synergy targets, and we're accelerating our efforts here. We have $150 million of net synergies planned for 2020. Year-to-date, we are on plan with over $70 million in net synergies realized and we remain confident that we will deliver on the full run rate of $250 million in synergies ahead of schedule. Of particular note, we continued the aggressive action on structural costs and lowered the SG&A expense by 26% year-over-year. During second quarter, we reduced head count by 5% and were down more than 10% year-over-year. We have also reduced our operational footprint year-over-year and we're actively driving cost reductions through lean initiatives. To-date, we have exited more than 60% of the shared service agreements from GE Transportation merger ahead of schedule.

Looking ahead, the rail transportation market and impacts from the pandemic remain challenged and fluid. While we anticipate market conditions to remain somewhat mixed, as I'll share with you in a moment, we believe volumes largely bottomed in the second quarter and we will see a gradual recovery. With this in mind, and based on our first half results as well as based on the backlog coverage for the rest of the year, we are issuing a new outlook for the 2020 year.

Pending no further lockdowns due to COVID-19 pandemic or resulting negative impacts on our business, we expect revenues in the range of $7.3 billion to $7.6 billion for the year. We will continue to adjust our variable and fixed costs to align with volume realities and we are committed to improving segment margins. We anticipate adjusted EPS to be in the range of $3.50 to $3.80 and cash conversion to be greater than 90% for the full year. This includes roughly $130 million from prior restructuring and transactions cash outflows. Cash conversion within the company's core business is expected to be over 100%.

Turning to slide 4, I'd like to discuss the market conditions and drivers we are seeing across the sector. Pascal Schweitzer, President of Freight Services, will also hit on some of this in a few minutes. In both Freight and Transit, we are experiencing mixed conditions as economic recovery begins and commuter travel resumes, and we're carefully monitoring the ongoing impact of the virus in some regions. In North America, rail volumes had a record decline, down roughly 20% year-over-year in the second quarter. However, we have seen rail volume improve since bottoming in the second quarter. Likewise, locomotive parkings after peaking to a record high in the second quarter have also shown gradual improvement, and we remain positive on the aftermarket sector.

In terms of the North American railcar build, a record one-third of the North American railcar fleet is in storage and builders are taking continued steps to slow down production lines in 2020. Industry forecasts currently indicate that the railcar build for the year will be less than 30,000 cars.

Reflecting on the quarter, I want to share a couple highlights. Internationally, rail volumes were more resilient driven largely by agriculture and mining tailwinds. International locomotive shipments were up versus last year and helped offset North American locomotive and freight car build declines as expected. We continue to see demand for new locomotives in Russia, CIS, Brazil and Australia. Some tenders have pushed to the right due to COVID-19, but we expect this to resolve as economies stabilize.

New growth opportunities for next-gen sustainable solutions also remain strong especially for hybrids and fuel-saving technology. We are doing some really innovative work in reducing fuel consumptions by 5% through our engine overhaul process; Pascal will share more on this in a moment. We're also currently field-testing our Flex Drive Locomotive, the first 100% heavy haul battery-powered locomotive in the world operating in a hybrid concept (00:09:11). So far, we are seeing an opportunity to reduce fuel consumption for our customers by 10% to 30%. We are extending battery technology to passenger transit as well and just closed a significant deal with New York City Transit to drive down their overall carbon footprint. Finally, we continue to see our Digital Electronics
product line provide significant productivity and improved safety for our customers. Sales for the quarter were up 4% versus the prior year.

Transitioning to the Transit sector, the COVID-19 crisis has had a significant impact on ridership and service levels in early second quarter. Since then, particularly in Europe and Asia, ridership trends are showing a slow recovery as economies reopen. This has resulted in some positive activity internationally with new brake, new doors and HVAC contracts in regions like Australia, Canada, India and the UK. Overall, we believe the long-term market drivers for passenger transport remain intact especially as governments look to rail as the cleanest, safest and the most efficient mode to address the world's public transportation challenges. Across the segment, we also continue to drive costs down. We continue to improve project execution and profitability. Lilian and the team are on track to expand margins over time while delivering over 100 basis points of improvement in 2020.

With that, let's flip to slide 5 and I'll turn things over to Pascal.

Pascal Schweitzer
Group President - Freight Global Services Organization, Westinghouse Air Brake Technologies Corp.

Thanks, Rafael. Good morning, everyone. It is good to be with all of you today. I am Pascal Schweitzer and I am the Group President of Wabtec Freight Services. This is a roughly $2.2 billion business with operations in around 40 countries and approximately $12 billion in backlog. Roughly 80% of our revenues are generated through multi-year contracts including long-term service agreements, parts contracts as well as multi-year modernization agreements. So in short, we are with our customers for the long haul helping them pull freight in some of the most important logistics corridors around the world.

As I've shared before, we are executing on a focused strategy to create value for our customers. This includes ensuring that our fleet is performing well and running hard, that we are capturing the aftermarket with a superior product and delivering outcomes for our customers through technology upgrades and new tools, all this while constantly improving our fleet total lifecycle cost. Today, as railroads continue to hunt for productivity and efficiency gains through initiatives like precision scheduled railroading for instance and in the mix challenges brought on by the pandemic, this strategy is more relevant than ever.

The second quarter, as Rafael explained, we saw significant disruption in many of the regions where we operate. Government shutdowns had an impact on our customer operations and freight volumes globally. As a result, a record number of locomotives were parked in North America. However, despite this, we continue to have a leading and increasing share of the total active fleet and our customers continue to increasingly prioritize the dispatch of our locomotives due in large part to the performance and reliability of the fleet.

I would also like to point out that in the second quarter, we did hit record performance for on-time parts delivery. And despite regional disruptions and shutdowns from COVID, each of our more than 100 service locations remained open and fully operational. A huge testament to the team in the field and this is a strong illustration that we do so much more than sell parts. You see that reflected in the resiliency of our second quarter top line.

So while the uncertainty related to the crisis has led some railroads to delay certain investment decisions, the value of our portfolio remains. We have worked with our customers to align scheduled maintenance plans to the new market realities. And as a result, we have leveraged the full power of Wabtec to increase the scope of our work and to unlock new growth in R&D.
Now looking ahead, as railroads enter into recovery and the growing level of freight relying on a smaller number of locomotives, we expect demand for reliability to be even greater. This will translate into more comprehensive work scopes, into more comprehensive fleet strategies, into modernization opportunities.

Currently, we have more than 1,000 modernized locomotives in operation delivering improved reliability, better fuel efficiency and overall economic performance for our customers. As our customers strategically consider their investment plans over the long-term, the value of modernization remains very compelling. The second quarter mods deliveries showed good momentum and we continue to have visibility via our multi-year backlog.

Now on a broader international scale, where economies have started to reopen, we are also seeing encouraging improvement in parkings and operational fleet performance. Just to give you a few examples. In Australia rail activity has shown good momentum throughout the quarter as China resumed business following the COVID lockdown. Kazakhstan, year-to-date car volumes are up compared with 2019. Brazil, we see a strong demand with greater dependency on agriculture products following a record harvest. In India, while there were a significant number of locomotives parked due to the pandemic, this ultimately had little impact to our business as we shifted focus to maintenance. And as of July, all of these locomotives are back in operation. Finally, in North America, as discussed, we do expect carload volumes to continue to gradually improve and parking to progressively recover.

In terms of commercial activity for the quarter, the team closed some significant long-term service agreements with Class Is in North America as well as in Brazil and won a key order for our FDL Advantage product.

Going into this product a little bit more specifically, as Rafael described, we have around 10,000 FDL locomotives running globally. Many of these locomotives are approaching their second or third engine overhauls. So with these next-gen solutions, we are able to reduce the fuel consumptions by up to 5%. That means for a single locomotive burning around 200,000 gallons of fuel a year, around $25,000 in savings per year. This is an exciting first win that is opening up a multi-million-dollar pipeline of opportunity for Wabtec, fully in line with our strategy of technology differentiation for the install base.

Finally, I'll share a few thoughts on cost management. So last year, we have reduced our head count by roughly 10%, ahead of our synergy commitment and in line with market realities. We have undertaken lean initiatives to drive cost out of the business while still being able to deliver for our customers and scale up as markets recover.

So to conclude, while the market remains fluid and carload volumes and parking drove significant headwinds, the Freight Services team had a strong operational quarter, giving us confidence that our broad international portfolio, our $12 billion multi-year backlog and our strong aftermarket reach will position us well into the future.

Looking forward, you will see some fluctuations quarter-to-quarter due to the seasonality of maintenance activity due to our engine overhaul profiles and mod delivery schedules. However, the fundamentals of this business and its ability to recover post-COVID remains strong.

I will now turn things over to Pat to provide more color on the company's overall second quarter performance. Pat?

Patrick David Dugan
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.

Thanks, Pascal. Turning to slide 6, sales for the second quarter were $1.7 billion which reflects a 22% decrease versus the prior year. The decline in year-over-year sales was mainly due to disruption across our Freight and Transit segments caused by the COVID-19 pandemic. [audio gap] (00:18:08) quarter operating income was $159
million and adjusted operating income was $262 million. That's down 32% year-over-year, mainly driven by the lower sales and the disruption in our operations as a result of the pandemic offset somewhat by variable cost actions and the realization of our synergies. For the quarter, adjusted operating income excluded pre-tax expense of $103 million, of which $72 million was for non-cash amortization, $31 million of restructuring and transaction costs. Take a look at the Appendix D to our press release for the reconciliation of these.

When looking at some of the detailed line items, SG&A declined 26% year-over-year to $217 million excluding $13 million of the restructuring and transaction expenses. SG&A expense benefited from structural cost actions across the business as well as the realization of synergies. Engineering expense decreased to $38 million or down 33% from last year. Engineering expense moved down with the lower volume outlook as well as some changes in project timing. And amortization expenses were $72 million. In 2020, we expect non-cash amortization expense to be about $290 million and depreciation expense of about $180 million.

Second quarter, we had GAAP earnings per diluted share of $0.46 and adjusted earnings per diluted share of $0.87. Details that bridge the GAAP earnings per share to adjusted earnings per share of $0.87 can be found attached to our press release. As of June 30, our multi-year backlog was $21.4 billion. Excluding the impact of FX, backlog is flat quarter-over-quarter, a rolling 12-month backlog which is a subset of the multi-year backlog of $5.3 billion. Our backlog continues to give us and provide good visibility across both the Freight and Transit segments.

Now let's take a look at those segments, their results on slide 7. Across the Freight segment, total sales decreased 21% to $1.2 billion in the second quarter. FX negatively impacted sales by about $26 million during the quarter. In terms of product lines, equipment sales were down 37% year-over-year as a result of lower North America locomotive deliveries which, as we have discussed, often can vary quarter-to-quarter due to timing. And that was offset somewhat in the second quarter by higher year-over-year international locomotive deliveries and increased mining sales. In the second half of the year, we expect locomotive deliveries to be slightly higher when compared to the first half of this year. And as you heard Pascal discuss, our Services portfolio continues to show resiliency despite the OE headwinds.

Despite a 18% drop in North America freight volumes for the quarter, Services revenues were down 8% year-over-year as result of lower parts sales due to record locomotive parkings, but that was offset by double-digit growth in mod deliveries. We expect our parts sales to improve with the gradual recovery in freight volumes due to timing of maintenance and overhaul work edging into the fourth quarter.

Digital Electronics sales were up 4% year-over-year on higher sales of distributed power products and signaling projects. Component sales were down 30% year-over-year on lower year-over-year railcar build and declines in key industrial end markets such as oil and gas and power generation. Despite the top line headwinds, evidence of our synergies is coming through as segment-adjusted operating income was $229 million for an adjusted margin of 19%. Finally, the Freight segment backlog was $18 billion, about flat with the prior quarter. I would note again that FX negatively impacted that backlog by about $58 million.

Turning to slide 8. Across our Transit segment, sales decreased 25% year-over-year to $533 million driven largely by disruptions stemming from the COVID-19 virus but were also impacted by FX which reduced sales by an additional $18 million. OE sales were down 32% year-over-year on disruptions caused by the pandemic. During the quarter, our operations and our customers' operations, which are primarily in Europe and Asia, were negatively impacted by government shutdowns. Aftermarket sales, which were down 18% from last year, were impacted by reduced capacity at many transit systems around the globe. However, as economies have opened...
up we have seen a resumption in service, increase in equipment deployed, gradual recovery in ridership in most markets.

Our adjusted segment operating income was $51 million for an adjusted operating margin of 9.6%. Margin performance was impacted by the lower absorption of fixed costs in the first half of the quarter. However, we are continuing to drive improvements in the Transit business and expect Transit margins to increase 100 basis points for the year. Finally, the segment backlog was $3.4 billion, also about flat with last quarter. FX negatively impacted the backlog by $79 million versus the end of the first quarter.

Now let's turn to the balance sheet and the cash flow on slide 9. Cash flow generation during the quarter was strong at $311 million. I would note that we had about $40 million of one-time impacts due to prior year restructuring and transaction charges we had identified on our last earnings call. Our leverage ratio at the end of the second quarter was 2.7 times, about flat with the last quarter. But our total liquidity at the end of the second quarter was $1.9 billion, up solidly from the $1.2 billion at the end of the first quarter, and total net debt is down about $282 million.

Also, in July we took proactive steps to restore a more balanced maturity profile of our debt with a successful five-year $500 million bond offering that retired $500 million in floating rate notes due in September of 2021. In summary, our balance sheet is strong and we are confident in our ability to generate cash flow, giving us the liquidity and flexibility to execute our strategic [audio gap] (00:25:27).

With that, let's move to slide 10, and I'll turn the call back over to Rafael.

Rafael O. Santana  
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

Hey, thanks, Pat. So as you heard throughout the morning, and you see on this page, Wabtec had a solid performance in the second quarter despite a weak and fluid environment; a reminder that in difficult times, strong companies must learn how to adapt, find a better way and lead through change. We could not have imagined a greater stress test for our company and how we would perform in a difficult environment than the one we're seeing today.

Over the last 17 months, we have successfully managed a massive merger that doubled the size of this company, we phased into the global pandemic in an industrial recession in one of the most difficult business cycles ever seen. Yet despite all the odds, we are performing strong and we have delivered a true testament to the team and their commitment to position this company as a stronger and more resilient Wabtec.

Heading to the second half of the year, we fully expect to see continued headwinds especially given the uncertainties of COVID-19. Our leadership team remain confident and committed to manage cost and to drive profitable growth that will help us navigate these challenges. I want to personally thank each and every member of the Wabtec team again for all that they're doing in the face of change. Your efforts are reflected in the results we shared today.

With that, I'll turn the call back to Kristine to begin the Q&A portion of the discussion.

Kristine Kubacki  
Vice President-Investor Relations, Westinghouse Air Brake Technologies Corp.
Thank you, Rafael. We will now move on to questions. Before we do, out of consideration for others on the call, I ask you that you limit yourself to one question and one follow-up question. If you have additional questions, just please rejoin the queue. With that, operator, I think we're ready to take our first question.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] And our first question will come from Justin Long with Stephens. Please go ahead.

Justin Long
Analyst, Stephens, Inc.

Thanks. Good morning and congrats on the quarter.

Rafael O. Santana
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

Good morning, Justin.

Justin Long
Analyst, Stephens, Inc.

So maybe to start with the 2020 guidance. So if I look at the revenue guidance, it implies that sequentially in the second half of the year, revenue should get better relative to the second quarter. As we think about just the mix implications, can you give us some color on how much of that sequential improvement in revenue you anticipate to come from Freight versus Transit? And then anything just on a quarterly basis that you can provide to help us think about the cadence of revenue or earnings in the back half?

Rafael O. Santana
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

Sure. Justin, let me start first with – well, as we look at the backlog coverage for the ranges we've provided, we feel strong about that. I think we also feel strong about the strength in the execution. We've got, I'll say, strong momentum in terms of both synergies and cost actions that we're taking. I think in the second quarter, we certainly saw volumes bottoming for our customers.

We think it was also – when we think from operational disruptions, I think we also, to some extent, have seen the worst. I don't think we're through that. I think we have seen improvement in the trends towards the end of the quarter; I'll point out that with unparkings of locomotives. Ridership levels on the Transit side have improved a bit, but I think the better news there is you've got a large number of trains still operating. So I think we're continuing to see those trends. There is, of course, some volatility as we see and as we look into the recovery. But we're seeing trends up starting at end of the second quarter and we're continuing to see that through this month of July as well.

Pat, I don't know if you want to add any more specifics into that?

Patrick David Dugan
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.

No. I think the one thing I would point out is that when you kind of look at our information as it becomes available, the mix of aftermarket versus OE, the decline is much more significant in the OE side kind of quarter-over-quarter.
and year-over-year. You see that as really being impacted by the disruption in the industry and the market. And so I think to get to your question of where and how is the recovery, I think the recovery is going to be in both segments and I think you're going to see it coming back to more typical mix of businesses as the year goes along.

**Rafael O. Santana**
*President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.*

I think one of the things we'll be watching for is really any push-outs on decisions with regards to new projects, and I think that's something for us to continue to monitor here as we continue to build backlog.

**Justin Long**
*Analyst, Stephens, Inc.*

Okay, great. And then maybe, Pat, on the cadence part of that question for third and fourth quarter. Do you feel like third quarter is maybe a little bit worse and then we kind of build off of that into the end of the year? Any color on that front?

**Patrick David Dugan**
*Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.*

Yeah. Just want to be careful about guidance to quarters and everything, but I think you'll see sort of kind of a steady sequential improvement as we go through the rest of the year.

**Justin Long**
*Analyst, Stephens, Inc.*

Okay, helpful. And as my second question, I wanted to ask about free cash flow. I know you made a comment about the cash conversion percentage this year. But any more specific thoughts around free cash flow in 2020 and how that cash could be allocated between debt paydown and maybe potentially even buybacks? I don't know if that's something you're considering at this point.

**Rafael O. Santana**
*President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.*

Well, couple points. I think we've given clear guidance to cash conversion being above 90%. I think we remain committed to that and I think we have the areas of opportunities here to act if you look into areas like inventory for instance. So we'll continue to have a strong rigor around that and we feel strong about delivering above 90% cash conversion here.

**Patrick David Dugan**
*Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.*

Yeah. And as for the allocation, I think it's obviously one of the most challenging times and we want to make sure that we focus on debt repayment and then get into other uses of capital. I don't think – I think it's too early to really be talking about anything aggressive or – but we want to remain opportunistic, and that's the way we've approached this. We're generating cash, we're meeting our goals. And then we're using it to get our debt in the right kind of ratio range as we've always talked about and be opportunistic for all the other things that we can do.

**Rafael O. Santana**
*President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.*

We remain committed to the framework we presented during the Investor Day, and there is a commitment to continue to pay debt down but we're going to be looking at opportunities here. And especially we can see bolt-on
acquisitions being, I'll call, more available than they were maybe six months ago and we'll make sure to evaluate that against the different options. So we're committed to that framework we presented back at the Investor Day.

Justin Long  
Analyst, Stephens, Inc.

Okay. Great. I really appreciate the time.

Patrick David Dugan  
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.

Thanks.

Operator: The next question comes from Chris Wetherbee with Citi. Please go ahead.

Chris Wetherbee  
Analyst, Citigroup Global Markets, Inc.

Yeah. Hey, thanks and good morning. Maybe if you could – I was curious if you could provide a little bit more color on the outlook for the second half on Freight segment, so looking through equipment and components and kind of giving a sense of how we should be thinking about that revenue rebound relative to what we see in the freight market. Services and Digital obviously held up fairly well. But when you think about those two pieces, do those kind of move linearly with a recovery in volume or how are you guys expecting that to play out in the second half?

Rafael O. Santana  
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

I think I'll purely point out to three things to be really watching. Of course, the impact for both customers and operations was very significant in the second quarter. As we go into the second half, I think, first, really watching closely on the freight side the unparking of locomotives. What I feel is North America or international, I mean, we have seen the impact in the second quarter. And as those unparking occurs, I think we have seen that trend. It's not linear, but I think there are some brighter spots than – one places versus others. Especially internationally, I would say we see some of those brighter spots. We see them across some geographies and driven by, well, either agriculture or specific mining. There's still some markets we're heavily underpenetrated.

So I think we see good dynamics coming from some of these markets. And it's reflected also in the pipeline of what I call opportunities for equipment deals. So if I talk about agriculture in Brazil or mining in Australia, we're also continuing to deliver on our contract in India. You pick a country like Kazakhstan's, volumes – carloads are actually up year-over-year year-to-date and that's also I think a significant opportunity for us.

Chris Wetherbee  
Analyst, Citigroup Global Markets, Inc.

Okay. Okay. That's very helpful. I appreciate that color. And then just a detailed question about the 12-month backlog. I just want to make sure I understand sort of what the progression has been over the last couple of quarters. So that's come down a bit, and I know FX is probably some of it. I'm just kind of curious, have we seen any of the sort of 12-month outlook get pushed out and to the right? I think there was some comments about that maybe in the prepared remarks. Just want to make sure I'm understanding what the 12-month view is, because obviously the long-term is very stable. Just want to make sure how we're seeing that kind of play out over the course of the more immediate term.
I'd say certainly, when I look at second quarter or even first quarter, I mean, I can't say those were necessarily great in terms of while favoring a dynamic of order intake. I think when you compare first quarter against second quarter, and if you to exclude FX, you will see backlog remains flattish quarter-over-quarter. I think as we look out ahead, I mean, we're really in the business of looking for business. We're chasing every piece of opportunity that we can go after. Our strategy here is to grow the business profitably, and I would say we're continuing to act to have a more competitive cost structure than ever before.

I think, yes, we are seeing some decisions moving to the right. And I think – especially if you think about some of the dynamics in the Transit side with, really, despite of the fact that ridership is low, I think we're seeing a number of trains in operation, so operators are really re-evaluating some of these. But we think the long-term fundamentals, whether if I look at Transit or Freight, remain strong and we are seeing a commitment to actually be investing in those modes and this is part of the solution as we look at the world ahead in terms of while driving more efficient, more productive, less emissions. And I think we sit in a good place in terms of the long-term fundamentals for the business.

Okay. Okay. That's helpful. I appreciate the color. Thanks very much.

Chris Wetherbee
Analyst, Citigroup Global Markets, Inc.

Hi. guys. Good morning.

Patrick David Dugan
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.

Good morning.

Rafael O. Santana
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

Good morning.

Allison Poliniak-Cusic
Analyst, Wells Fargo Securities

I just want to delve into Chris' question a little bit more on the Freight aftermarket piece particularly as it relates to North America. I guess just given the focus from the rails in terms of increasing utilization versus bringing equipment back, I would've thought your Freight aftermarket – I think you said it wouldn't recover 1:1, but I would think it would actually recover a little faster as a result of that. Any thoughts there or am I thinking about that wrong?
Well, couple comments there. Number one, I mean, we felt the impact in the second quarter in North America. I mean, and it's brutal, right? I mean, as you look into the numbers you've heard from the Class Is, I mean, we've seen volume reduction pretty close to those numbers that you have heard. If you think of transactional parts, and I think some of the Class Is alluded to like 20% down, yeah, I mean, we did feel that directly. And I think what we've also seen is from the bottoming of the volume which fundamentally happened in the first two months of the quarter, we've seen that improvement come through.

That's also been true not just for North America. We've also seen that in the international markets. And we do expect recovery to happen there faster especially as fleets are unparked. It's all dependent on the pace in which those fleets gets unparked. I think we're seeing a faster rate of recovery on international markets. I think I mentioned here earlier some of the dynamics on agribusiness, mining across some of the geographies that we serve, and we're certainly seeing I'd say a much faster recovery. In fact, some customers are actually up year-over-year in terms of carloads in some of these geographies.

**Allison Poliniak-Cusic**  
*Analyst, Wells Fargo Securities*

> Got it. Got it. And then just want to turn to Transit in terms of the recovery in terms of US versus global. I know global is a much bigger impact for you on Transit. Any differences that you're seeing in those markets in terms of how they're recovering or interest in investing in infrastructure going forward?

**Rafael O. Santana**  
*President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.*

> I think the recovery in terms of, number one, ridership has been a little bit better in Europe if you compare against the US, but reality is it remains well below what I'll call the pre-COVID levels. I think the better side of it is we've seen I think number of trains in service, in operations are very significant despite of the ridership being down, so I think we can also be looking at service despite of maybe a lower decline going into a faster recovery. And I think the other element is I think as far as projects goes, we haven't seen any, again, cancellations or anything with regards to impact [ph] to this year (00:41:20). There could be an element of things pushing to the right in terms of just project delays when customers might want equipment. I think that's one of the elements that we're going to keep monitoring.

**Allison Poliniak-Cusic**  
*Analyst, Wells Fargo Securities*

> Great. Thanks so much. I'll pass it along.

**Operator:** Our next question comes from Courtney Yakavonis with Morgan Stanley. Please go ahead.

**Courtney Yakavonis**  
*Analyst, Morgan Stanley & Co. LLC*

> Hi. Great. Thanks for the question, guys. You talked a little bit about kind of the bottoming in volumes and in ridership in Transit, and I appreciate kind of a lot of questions on the aftermarket. But could you clarify what the exit rate trends that you're seeing, kind of that improvement off of the down 18% in Transit aftermarket? And then similarly in the Freight services side, kind of how you've seen that recovery progress so far kind of as you've gone through the quarter and the exit trends?
Rafael O. Santana  
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

So I think in terms of the exit trends, I mean, again, we saw it going back up some of the demand in both — in terms of orders but in terms of sales versus the first two months of the quarter I think in specific I would say in Transit. I think beyond that, I think we've taken significant actions in the business. Lilian and the team is really committed to continue to take the necessary cost actions. And I look at year-to-date, we're 110 basis points margin improvement versus the first half of last year. I think we've talked to you about being at least 100 basis points improvement year-over-year. So despite of what I'll call a really unprecedented quarter in many ways, we're very much on track to deliver on that promise. So still a lot of work to do. Still subject to a lot of disruptions but we feel like the team is heading the right direction here.

Courtney Yakavonis  
Analyst, Morgan Stanley & Co. LLC

Okay. And then just on the synergy targets. Obviously, you mentioned that you feel confident that you can get over the $150 million net by the end of this year. I think you've talked about some of those synergies being volume-related. So maybe can you just comment on your confidence? Is that because you're seeing that volume improve or are you seeing maybe faster footprint reduction than you were anticipating? And then if you can talk at all about maybe the upside to that $250 million since you've mentioned that you'll achieve that earlier than you had previously anticipated?

Rafael O. Santana  
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

Yeah. We're certainly, I'd say, number one reason for that is we do have a pipeline of synergies that's greater than the one that we've provided. So we're continuing to work on those and they're critical in order to offset any, I'll call, downside that we could experience along the way. So we're not giving necessarily any considerations on volume growth at this point as being able to accelerate that. But I think we've got good momentum there and I think we continue to have opportunity here to provide, I'll call, better news in terms of accelerating synergies as we progress this year and into next year.

Courtney Yakavonis  
Analyst, Morgan Stanley & Co. LLC

Okay. Great. Thank you.

Operator: The next question is from Ken Hoexter with Bank of America Merrill Lynch. Please go ahead.

Ken Hoexter  
Analyst, Bank of America Merrill Lynch

Hey. Good morning. Pat, maybe just continuing on the margin commentary there. What are your thoughts on Freight margins now that you're fully integrated with GE and lapping year-over-year? You're in the upper teens, but maybe just help us think about what happens as asset sales come back online. Should we see a mix change? Do you expect that to move back into the 20s? Should it stay at this level? Maybe just your general thoughts as the mix shifts with the business mix.

Patrick David Dugan  
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.
Sure. I mean, when you kind of look at the impacts, you have freight car builds that are really at very historically low levels, you have North America locos and the impacts of that market on our business. As those volumes come back on, we obviously get really good margins on the freight car build and we get good margins in the locomotive builds on OE and the absorption that comes along with that. So I think that you could see the business and the margins for that Freight segment improve with the higher volume. It certainly makes sense. The other aspect to this will be Digital Electronics and the investment that our customers will make, and the growth in that revenue area will also provide really good margins for the segment.

Ken Hoexter  
Analyst, Bank of America Merrill Lynch  

So it’s not like digital has higher margins because of less asset intensity, so therefore it’s peakish now and with more assets it would be pressured you see as the physical assets come back and improving in that margin just as you get more fixed cost coverage, just to clarify?

Patrick David Dugan  
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.  

Yes, exactly.

Ken Hoexter  
Analyst, Bank of America Merrill Lynch  

Okay.

Patrick David Dugan  
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.  

I think the fixed cost coverage is a big part of it, but I think it’s also – those are good product lines for us and they deliver a lot of value for our customers. And I think that as the overall volumes recover and we get the industry improve, I think that you’ll see the margins get back to more historic and typical levels.

Ken Hoexter  
Analyst, Bank of America Merrill Lynch  

Great. And then for my follow-up, Pascal, obviously Freight did well in holding up in the backlog. Can you talk about the mix of contract services versus equipment in the backlog itself in terms of what was added and maybe your thoughts on domestic versus international as well?

Pascal Schweitzer  
Group President - Freight Global Services Organization, Westinghouse Air Brake Technologies Corp.  

Look – you want to take the...?

Patrick David Dugan  
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.  

So we just want to be a little careful. I don't think we've kind of broken out like each of the component, the product line revenue into its backlog and everything. Obviously, we talk in general about the revenue mix in services as about half of it comes under the MSA agreements which is an element of both kind of labor, service and parts and other activity. You have mods in there and you have parts sales in there. So those are basically the rule of thumb that we've been talking about in terms of how to look at that product line revenue. And I think the orders that have
come in kind of hold with that mix. It's not absolute every quarter, but when you look over a longer period, a year or more, you're going to see your order intake be pretty consistent with that mix of revenue.

Pascal Schweitzer  
Group President-Freight Global Services Organization, Westinghouse Air Brake Technologies Corp.

And maybe to your question about...

Patrick David Dugan  
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.

Yeah. Go ahead, Pascal. Go ahead.

Rafael O. Santana  
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

Go ahead.

Pascal Schweitzer  
Group President-Freight Global Services Organization, Westinghouse Air Brake Technologies Corp.

To finish on your question about North America versus international. I mean, what we see is that in North America we've seen this big impact from parking. Now, if you look at the active fleet today, Wabtec locomotives really represent the majority of the fleet that is running today, so this is an effect that is mitigating this high parking number. And the locomotives that are running are running really hard, so in terms of megawatt hour miles per locomotive, we've really seen a strong increase together with the implementation of precision scheduled reloading. So this is one thing that is accelerating scheduled maintenance that is putting more focus on reliability, and this is good for service.

International, Rafael discussed it. I mean, Australia is strong, Brazil is strong, Kazakhstan, Egypt. Many of our big international markets have remained strong. And in terms of mods, with the great work that our supply chain team has been doing to keep our factories open, we've been able to stick to our delivery schedule and to have a strong quarter as well. So these are really the three building blocks that can explain this performance, I would say.

Rafael O. Santana  
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

I think if you look at the last two years, we've continued to see an increase in terms of the percent of our fleets running when compared to our competitors, whether if I look at North America or global markets. I think that's an ongoing trend.

Ken Hoexter  
Analyst, Bank of America Merrill Lynch

Thanks, guys. Appreciate the time.

Rafael O. Santana  
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

Thank you.

Operator: Our next question comes from Matt Elkott with Cowen. Please go ahead.
Matt Elkott  
**Analyst, Cowen and Company**  

Good morning. Thank you. So back at the Analyst Day, you guys provided a chart showing the installed base distribution for locomotives. And based on the age profile of the Tier 4 locomotives, it would appear that some of them may be rolling off warranty in the next couple of years. First of all, does that make sense? And if so, would that be a positive for aftermarket revenue on those locomotives?

Pascal Schweitzer  
**Group President-Freight Global Services Organization, Westinghouse Air Brake Technologies Corp.**  

Yeah. Yes, that's true. Now keep in mind, I mean, this is a big fleet, right? We are talking about 23,000 assets as we presented. I think we have a favorable age distribution. The average age of this fleet is only 13 years so this is a pretty young fleet that is going to keep running for a number of years. You have some of the older fleets that are running less. You have some fleets that are coming off warranty, especially internationally. And so you have a number of effects coming together, but true. We have some locomotives coming off warranty and these locomotives start generating service revenue.

Matt Elkott  
**Analyst, Cowen and Company**  

And then service revenue is – that doesn't make it into the backlog number, does it, that you published at $12 billion?

Pascal Schweitzer  
**Group President-Freight Global Services Organization, Westinghouse Air Brake Technologies Corp.**

Not necessarily. It depends on the contractual coverage that we have for these units.

Patrick David Dugan  
**Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.**  

Yeah. I mean, you can't – you have MSAs that are out there depending on the customer and the fleet and their own decision. There might be a contract agreement that's in place but you could also have customers be doing some of the maintenance on their own with just our parts or somewhere in the middle. It's really it's not something that you can kind of paint a broad brush over everybody. It can be a little bit different and that's why I always go back to kind of the mix of the service revenue for the product line.

Rafael O. Santana  
**President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.**  

There's about, what, $600 million which is more transactional which is orders you get on the go, so you might not be seeing those in the backlog to your point...

Patrick David Dugan  
**Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.**

Right.

Rafael O. Santana  
**President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.**  

...out of the total $2.2 billion that make up the [ph] bids (00:52:33).
Matt Elkott
Analyst, Cowen and Company

Yes. Got it. That makes sense. And speaking of a question that may be in a gray area and it's somewhat hard to answer, I was just wondering if we can gauge what percentage of your international backlog may be for customers that are government-backed entities, federal government-backed entities versus state-level versus private companies. I know that you probably don't have that specific breakout, but any color would be helpful.

Rafael O. Santana
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

Exactly. We don't really have that breakdown like you described. But, I mean, look, we'll certainly look into that and try to get back to you with at least some color around it.

Patrick David Dugan
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.

Yeah. I would just add, I mean, just as like a rule of thumb or something just to consider. I mean, a lot of our – especially in the Freight side, our contracts are backed with bank guarantees and other financing that's in place. When you get on the Transit side, especially on the OE markets where you have the big backlog, those are typically supported with government funding, and often that funding has been in place for years because the contract was awarded years ago. So that's just kind of a thing to consider.

Rafael O. Santana
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

So that's one side on the equipment. And maybe on the service side, they will very often be sold with a services contract on the top of that because they want to make sure ultimately they maintain the locomotives running, and there's an element of continuing training to the operators. And what we often see is our fleets running especially in those remote locations as we support the customer throughout the life of the locomotives.

Pascal Schweitzer
Group President-Freight Global Services Organization, Westinghouse Air Brake Technologies Corp.

Yeah. Look, I mean, internationally we can pretty often, without the proper service support, end up with a brand-new fleet of locomotives that is stranded after a few years only. We really try to stay close with our customers over the entire life of the locomotive. We have more than 160 service locations all around the world, so having local presence and being able to bring engineering support whether physically or with remote diagnostics is – and keeping parts locally is really important for us internationally.

Rafael O. Santana
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

So we're very interconnected with our customers to the point that in a lot of places we manage the inventory associated with parts coming in and ultimately making sure we guarantee the availability and reliability of those assets. So we feel very much upfront any of those changes.

Matt Elkott
Analyst, Cowen and Company

Great. Very helpful. Thank you very much.
Jerry Revich
Analyst, Goldman Sachs & Co. LLC

Yes. Hi. Good morning, everyone.

Rafael O. Santana
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

Good morning.

Jerry Revich
Analyst, Goldman Sachs & Co. LLC

Rafael, I'm wondering if you could talk about how your MSAs performed in the quarter. Obviously, really strong Services result; sounds like mods helped. But can you talk about the MSA performance in particular? And I believe you get higher revenue opportunities post-PSR adoption. And I'm wondering are you starting to see that hitting the sweet spot, if you will? Can you just expand around those points?

Rafael O. Santana
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

Yeah. So I'll just start with the second quarter. I mean, of course the trends were not great there. I mean, we saw a decline in some of these items. And I think I mentioned about parts. I mean, we also saw pressure on MSA. I mean, units just not running as much as they were. But once again, I think as you start seeing the unparking take place, I think we're seeing those trends as early as of June and continuing to July to move in the right direction, and I think we're seeing a good pattern from this point of view.

But I think the one thing that I want to highlight to you here is we're working with customers to make sure that they've got ultimately I think the most efficient, the most reliable locomotives out there. And this presents to us opportunities to overhaul, to modernize and to ultimately also equip them so they can run a lot of the things you've heard from the Class Is; how do I run longer trains, how do I get to more fuel efficiency for those locomotives? And we've got to make sure that we're competitive as we do that, but things like Distributed Power with LOCOTROL, LXA, Trip Optimizer, these are some of the technologies that will enable that.

And these are, in fact, proven technologies that are aligned very well with PSR and all the efficiency railroads want to drive. And I think, again, very much connected with a lot of the story you hear from Pascal on the Services side and one area that we continue to see opportunity here to grow our installed base and to help customers with a great paybacks.

Jerry Revich
Analyst, Goldman Sachs & Co. LLC

Okay. And then a follow-up on mods. Pat, I think you mentioned in your prepared remarks you had double-digit growth. To hit the type of outperformance that you had in Services versus Freight volumes in the quarter, it would seem mods shipments would have to be up 30% to 40% year-over-year to drive the level of outperformance that we saw for you folks in the quarter. And I'm wondering if you can comment on what's the inquiry level like for adding mods to backlog. Are you able to essentially maintain the mods backlog as we hopefully see improving freight conditions entering 2021?
Patrick David Dugan  
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.

Yeah. So the mods are – they’re in the backlog year-over-year. Essentially, we continue to execute on orders received, and it would’ve been in 2019 and according to the schedule that our customers have worked with us on establishing. So there’s a certain amount of quarter-to-quarter variability that’ll come with those mods orders as we execute. Sometimes, it’s – to look at it and say that it’s going to be linear or have a trend there, you really have to look at a bigger picture, a bigger number of quarters or a year-to-date kind of number. So it just so happens that in the second quarter that backlog is more staggered compared to last year. When you talk about order intake for mods going forward, I mean, I think that there’s a lot of interest in our customers to continue to use this mod approach to leverage especially in their PSR strategy and their fleet strategy.

I don’t know, Pascal, if there’s anything you want to add to that?

Pascal Schweitzer  
Group President-Freight Global Services Organization, Westinghouse Air Brake Technologies Corp.

No. I mean, number one, I think that if you look at the service numbers for the quarter, it was not 100% a mod story, right? As we explained, we had a difficult situation in North America due to parking. However, a big portion of our fleet kept running. Internationally, we saw some strong performance. And then we had a strong mod quarter in terms of deliveries.

Now looking forward for mods, I mean, we believe that this is a big opportunity for the railroads which is fully in line with their strategy as Rafael said around longer trains, more reliable trains, better economic performance. We have analyzed the fleet in a lot of details and we have the opportunity to deliver big outcomes to our customers. So we are talking about 50% increase in haulage ability, reliability improvement by more than 50%, 10% fuel efficiency improvement. The addition of all our suite of digital solutions, Trip Optimizer, LOCOTROL, LXA. And all this, when you combine it together, we believe that this is turning into a very attractive investment proposition for the railroad.

Now for them, in the end it’s a question of capital allocation and they decide. I mean, we work hard to show them the value of our product and we believe that there is a big opportunity to create value for the railroad and for Wabtec at the same time.

Rafael O. Santana  
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

You can and you will see big swings between mods and what I’ll call new locomotive volumes quarter-over-quarter. Just keep in mind the same facilities that are doing the mods are doing the new units. And of course, we tend to profile those to make sure, I mean, we’re driving good productivity at our plants. So there could be some significant changes on quarter-over-quarter numbers.

Pascal Schweitzer  
Group President-Freight Global Services Organization, Westinghouse Air Brake Technologies Corp.

I think the seasonality effect is important, then you have mods, you have service, you have scheduled, you have unscheduled maintenance, you have the overall profile. There is a seasonality impact and then you will see some ups and downs there.
Okay. Appreciate the discussion and congratulations on a strong quarter. Thanks, everyone.

Rafael O. Santana  
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

Thank you.

Patrick David Dugan  
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.

Thank you.

Operator: The next question will be from Steve Barger with KeyBanc Capital Markets. Please go ahead.

Robert Stephen Barger  
Analyst, KeyBanc Capital Markets, Inc.

Hey. Thanks. Good morning.

Rafael O. Santana  
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

Good morning.

Robert Stephen Barger  
Analyst, KeyBanc Capital Markets, Inc.

Just a couple quick ones. For the Digital business increase of 4%, is more of that recurring revenue from existing customers or have you been able to convert new customers looking for efficiency in 2Q?

Rafael O. Santana  
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

Can you repeat that?

Patrick David Dugan  
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.

You broke up a little bit, Steve. Can you say it again?

Robert Stephen Barger  
Analyst, KeyBanc Capital Markets, Inc.

Yeah, sorry. The Digital business increase of 4%, more recurring customers or were you converting new customers?

Rafael O. Santana  
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

I think a lot of it is associated with, I'll call, existing customers. We have the opportunity here to grow our installed base on some products that are still underpenetrated. I think I mentioned here LXA as a product that, I mean, we still have an installed base that's relatively small when I look at the potential of this product, and it's a key product
especially as railroads look at making longer trains. I think there's some elements here of other products like Smart HPT that will also enable customers to get significant fuel savings as they run those longer trains. So more with existing products and existing customers. And I think one of the big opportunities we have is to expand that share growth really into the international markets. I think we've got some earlier adopters in places like Brazil, in places Kazakhstan, but we can still be doing a lot into some other geographies.

Robert Stephen Barger  
Analyst, KeyBanc Capital Markets, Inc.

So that was my next question. The Digital business is much more North America and less penetrated in international?

Rafael O. Santana  
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

Exactly.

Robert Stephen Barger  
Analyst, KeyBanc Capital Markets, Inc.

And just last one, one quick clarification. Slide 8 says you expect to drive margin improvement in Transit through the rest of the year. Does that mean sequential improvement by quarter or is that relative to what you put up last year?

Rafael O. Santana  
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

I think, again, what I said last year was we were going to drive at least 100 basis points margin improvement year-over-year, and we certainly have actions that support more than that. And I think my commentary earlier was if you look at the first half of the year, we're very much on track to do so. And actions will continue. It's less about even, I'll call, the improvement year-over-year but making sure that we continue to drive momentum to, well, give to our entitlement. So I want to see continued momentum there.

Robert Stephen Barger  
Analyst, KeyBanc Capital Markets, Inc.

Understood. Thank you.

Operator: The next question will come from Scott Group with Wolfe Research. Please go ahead.

Scott H. Group  
Analyst, Wolfe Research LLC

Hey, thanks for time, guys. A couple quick ones for you first, Pat. So typically, third quarter just normal seasonality is lower than second quarter. Does that sort of normal seasonality apply this year? And then maybe just bigger picture, when I look at the guidance, sort of a faster improvement in revenue growth off the bottom than earnings growth. Maybe just some thoughts there on sort of the mix or margins as revenue starts recovering. Thank you.

Patrick David Dugan  
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.

Yeah. So the seasonality, we kind of find that to be a little bit challenging and a little bit not typical year-to-year when you would consider all that we've gone through. The easy one to point to is the timing of some of our Freight
Services business; we would see a lot of strength of that in the third quarter. And in my earlier remarks, prepared remarks, I kind of mentioned that we see some of that edging out into the fourth quarter. And I think that that's, from what we can tell with our customers, we think that that's going to have an impact. I think you also look at the – that was always kind of a positive seasonality in Q3. You also had some negative impact of shutdowns and plant slowdowns in the summer months in Q3. We're seeing that being a little bit moderated. So I think that that's the expectation for us in Q3, getting back to normal in next year.

And your point about kind of revenue growth outpacing the earnings growth, I think that that's a little bit related to the sales mix, the timing. We certainly will see some kind of return to normal and some of our engineering costs and SG&A being more consistent with the higher revenues, and I think that'll have an impact on our margins a little bit in the second half of the year.

Scott H. Group
Analyst, Wolfe Research LLC

Okay. Thank you. And just last one. If I go back to the beginning of the year, Pat, you were talking about $900 million of cash from ops. It looks like the net income guidance is down around $200 million from January. So should we assume a similar sort of $200 million decline in cash flow from operations or is there reasons why it can be better than that?

Patrick David Dugan
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.

Well, I think you got to obviously consider the impact of net income and the lower volumes on the cash flow. But the areas of confidence in cash flow and opportunities to do better really starts with the ability to work with our working capital, to reduce our working capital with the lower volumes, turn that in a source of cash, obviously the cost savings initiatives that we put in place. And we continue to execute on some of the tools, the balance sheet tools and the supply chain tools that we replaced from exiting the GE transaction. So all those things I think lead to a lot of confidence in our cash flow generation for the rest of the year.

Scott H. Group
Analyst, Wolfe Research LLC

Okay. Great. Thank you, guys. Appreciate the time.

Rafael O. Santana
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.

Thank you.

Operator: Ladies and gentlemen, this concludes our question-and-answer session. I would like to turn the conference back over to Kristine Kubacki for any closing remarks.

Kristine Kubacki
Vice President-Investor Relations, Westinghouse Air Brake Technologies Corp.

Thank you, everyone, for your participation. I will turn the call over to Rafael for a quick few comments.

Rafael O. Santana
President, Chief Executive Officer & Director, Westinghouse Air Brake Technologies Corp.
Hey, just one of the most disruptive quarters for us ever with really an impact for both customers and operations. Wabtec employees have been absolutely amazing in their response, and I just want to thank them for the hard work and dedication to keep serving our customers and running our company well. Thank you.

Operator: The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.