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Westinghouse Air Brake Technologies Corp. (WAB)

Q2 2026 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day and welcome to the Wabtec Second Quarter 2026 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 Kyra Yates, Vice President of Investor Relations. Please go ahead.

Kyra Yates

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

Thank you, operator. Good morning, everyone, and welcome to Wabtec's second quarter 2026 earnings call. With us today are Chairman and CEO, Rafael Santana; CFO, John Olin; and Senior Vice President of Finance, John Mastalerz. Today's slide presentation, along with our earnings release and financial disclosures, were posted to our website earlier today and can be accessed on the Investor Relations tab.

Some statements we are making are forward-looking and based on our best view of the world in 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.

I will now turn the call over to Rafael.

Rafael O. Santana

Chairman & Chief Executive Officer, Westinghouse Air Brake Technologies Corp.

Thanks, Kyra, and good morning, everyone. We are proud of the progress we have made in the first half of the year, which is strengthening our position as a leading industrial technology company. It reflects the strength of the leadership position we continue to build across our portfolio, and the continued focus of the Wabtec team to deliver for our stakeholders.

With that, let's move to slide 4. I'll start with an update on our business, my perspectives on the quarter and progress against our long-term value creation framework. And then John will cover the financials.

We delivered a strong first half of the year, which exceeded our expectations despite tariff headwinds, unfavorable business mix, and challenging prior year comparisons. Through disciplined execution across the organization, we achieved robust growth, expanded margins, and delivered double-digit earnings per share growth.

Looking ahead to the second half, I remain encouraged by the healthy pipeline and continued demand for our core products and services, the profitable growth of our 12-month and multi-year backlogs, and our focus on driving productivity and efficiency. This momentum is evident in our second quarter operational execution and our overall financial results.

Having said that, sales were $3.2 billion, which was up 17.5% and adjusted EPS was up 22% from the year ago quarter. Total cash flow from operations for the quarter was $441 million. Backlog remains a key strength. 12-month backlog was up 11% from the prior year, while the multi-year backlog exceeded $30 billion, up 42%. Our financial position remains strong. We continue to execute against our capital allocation framework and expect to continue to compound long-term value for our shareholders.

Shifting our focus to slide 5. Let's talk about our 2026 end market expectations in more detail. While key metrics across our freight markets remain mixed, we continue to be encouraged by the overall strength and resilience of our business. We are seeing solid momentum in our international markets and the pipeline of opportunities across geographies remains strong.

In North America, cargo traffic was up 4% in the quarter. As a result of this growth, Wabtec's and the industry's active locomotive fleet was up compared to last year's second quarter. Internationally, carloads growth during the quarter was mixed, but the long-term carload growth trends continued to be robust. Significant investments to expand and upgrade infrastructure are driving our international orders pipeline.

Looking at the North American railcar build, the industry forecast for new railcar is slightly up compared to prior quarter, and is now projected to be approximately 25,000 cars for 2026, which is still down 21% from 2025.

Finally, turning to the transit sector, we continue to see positive underlying indicators for growth. Ridership continues to increase in key markets such as Europe and India, and we continue to see strong backlogs at car builders, supported by robust levels of public investment for fleet expansion and renewals.

Now, let's turn to slide 6 and highlight several recent business wins. During the quarter, we secured $1 billion order from an Australian customer, spanning across locomotives, services, components, and digital solutions. This award highlights the breadth of Wabtec's capabilities and demonstrates how our integrated offering are creating value throughout the product lifecycle. We also signed a $184 million order for Positive Train Control with Vale, strengthening our long standing partnership and marking an important step forward in advancing rail safety, efficiency, and automation across Brazil's rail network. In Transit, we were awarded a $55 million platform door order for the Grand Paris Express project. Moving to mining, our APAC team secured a $52 million order to supply drive systems for 240-ton mining trucks.

Overall, these successes continue to demonstrate our leadership in the markets we serve, the strength of our pipeline, and the commitment of the Wabtec team to deliver meaningful results for our customers and stakeholders.

With that, I'll turn it over to John to review the quarter, segment results, and our overall financial performance. John?

John A. Olin

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

Thanks, Rafael, and hello, everyone. Turning to slide 7, I'll review our results in more detail. Our second quarter results came in better than expected, driven by stronger revenue growth and increased operating margin expansion. As we discussed in our last call, we expected the quarter's revenue growth to be similar to first quarter's results.

Second quarter revenue growth came in stronger than the first quarter, driven by a combination of a couple things. First, we had favorable timing of shipments, and second, we experienced incremental flow business revenue. We also expected our margin expansion to be similar to the first quarter. In actuality, our operating margin expansion also came in favorable to Q1's results. This was driven by better-than-expected product mix and our continued focus on productivity and efficiency with programs such as Integration 3.0.

Having said that, sales for the second quarter were $3.18 billion, which reflects a 17.5% increase versus the prior year, with strong contributions from both the Freight and Transit segments. Excluding the impact of currency, Q2 sales were up 16.6%. For the quarter, GAAP operating income was $600 million, which was up 27.1% versus the prior year. The increase was predominantly driven by higher sales, improved gross margin and lapping prior year's transaction costs resulting from our recent acquisitions. Adjusted operating margin for Q2 was 21.9%, up 0.8 percentage points versus the prior year. This improvement was achieved despite tariff-related headwinds, unfavorable mix and tough year-over-year comps.

GAAP earnings per diluted share was $2.33, which was up 18.9% versus the year ago quarter. During the quarter, we had net pre-tax charges of $6 million for purchase accounting charges and transaction costs associated with our recent acquisitions. In the quarter, adjusted earnings per diluted share was $2.76, up 21.6% versus the prior year. Overall, the quarter reflects the strength of our execution, the resilience of our business and solid momentum as we move through the year.

For the second half, we expect year-over-year revenue growth to temper as we lap the inclusion of inspection technologies in the prior year period. We also expect the majority of our margin expansion for the year to occur in the back half of the year. Our second half margins are expected to benefit from, first, tempering year-over-year tariff impacts as we begin to lap 2025 tariff increases; next, increasing productivity momentum from our Integration 3.0 and portfolio optimization initiatives; and finally, lapping more moderate prior year margin growth.

When we look at the cadence of growth between the third and the fourth quarters, we expect revenue growth to be slightly higher in the third quarter versus the fourth. And on the margin side, we anticipate the opposite dynamic. We expect a meaningful acceleration in margin growth in the fourth quarter with third quarter's performance generally consistent with the margin growth rates delivered in the first half of the year.

Now turning to slide 8. Let's review our product lines performance in more detail. Second quarter consolidated sales were up 17.5%. Equipment sales were up 35% from last year's second quarter. This was driven by higher locomotive deliveries and increased mining sales. Our Services group drove strong core Services sales growth in the quarter, which was offset by lower modernization deliveries as we expected. Looking ahead, we expect modernization deliveries to grow in the second half of the year, returning Services to growth in the back half. That said, we continue to expect full year Services revenue to be down due to the lower number of modernization deliveries that were shipped in the first half when we compare that to the prior year. Consequently, as modernization deliveries ramp up in the second half, we would expect Equipment revenue growth to remain positive, but at a very moderate pace versus the 43% growth achieved in the first half.

Components sales were down 0.7% versus last year due to the industry's decline in the North America railcar build, and due to lower revenue from our portfolio optimization efforts, partially offset by increased industrial product sales. Digital Intelligence sales were up 88.5% from last year. This was driven by contributions from the Inspection Technologies and Frauscher acquisitions.

In our Transit segment, sales were up 18.9%, driven by the Dellner acquisition and growth across our products and services businesses. Foreign currency exchange had a favorable impact on sales in the quarter of 1.3 percentage points.

Moving to slide 9. GAAP gross margin was 36.5%, which was up 1.8 percentage points from the second quarter last year. Adjusted gross margin was up 1.9 percentage points during the quarter. GAAP operating margin was 18.9%, which was up 1.5 percentage points versus last year. Adjusted operating margin improved 0.8 percentage points to 21.9%. Operating margin was positively impacted by cost recovery from contractual price escalation, increased productivity and integration savings, partially offset by rising manufacturing costs, higher year-over-year tariffs and unfavorable mix. Adjusted and GAAP SG&A expenses were higher year-over-year due largely to the SG&A expense associated with our acquisitions. Engineering expense was $70 million, $20 million higher than Q2 last year, primarily due to acquisitions.

We continue to invest in engineering resources in current business opportunities, but more importantly, we are investing in our future as a leading industrial technology company focused on improving our customers fuel efficiency, labor productivity, capacity utilization, and safety.

Now let's take a look at segment results on slide 10, starting with the Freight segment. As I already discussed, Freight segment sales were up a strong 16.9%. GAAP segment operating income was $504 million, driving an operating margin of 22.5%, up 0.9 percentage points versus last year. Adjusted operating income for the Freight segment was $579 million, up 20.6% versus the prior year. Adjusted operating margin in the Freight segment was 25.8%, up 0.8 percentage points from the prior year. The increase was driven by higher gross margin of 1.7 percentage points, partially offset by an increase of 0.9 percentage points in our operating expense, expressed as a percentage of revenue. The key driver of this is due to the mix of higher gross margin businesses as a result of our acquisitions of Inspection Technologies and Frauscher, and our continuous focus on productivity and efficiency. Finally, the Freight segment's 12 month backlog was $6.64 billion. Our 12-month backlog was up 10.2%, while the multi-year backlog of $25.33 billion was up 47.8%.

Turning to slide 11, Transit segment sales were up 18.9% at $936 million. When adjusting for foreign currency, Transit sales were up 17.7%. GAAP operating income was $146 million, which reflected the quarter's robust revenue growth and operating margin expansion. These strong results were partially offset by $20 million of purchase accounting charges and non-cash amortization expenses, which were primarily associated with the acquisition of Dellner in the first quarter. Adjusted segment operating income was $166 million. Adjusted operating income as a percent of revenue was 17.7%, up 2.5 percentage points from prior year, with the underlying momentum of the business and the Dellner acquisition serving as key contributors to this quarter's margin expansion. Finally, Transit segment 12-month backlog for the quarter was $2.5 billion, and our 12-month backlog was up 14.5%, while the multiyear backlog was up 19.4%.

Now let's turn to our financial position on slide 12. Our second quarter cash flow generation was $441 million, resulting in a cash conversion of 82%. Our balance sheet and financial position continue to be very strong as evidenced by, first, our liquidity position, which ended the quarter over $2 billion; and our net debt leverage ratio, which ended the quarter at 2.2 times. Our leverage ratio remained in our stated range of 2 to 2.5 times, even after funding the purchase of Dellner during the first quarter for approximately $1 billion and repurchasing $457 million of our shares in the first half.

We continue to allocate capital in a disciplined way to maximize returns with an expectation of compounding our earnings for our shareholders. During the quarter, we repurchased $215 million of our shares and paid $53 million in dividends.

With that, I'd like to turn the call over to Rafael to talk about our 2026 financial guidance.

Rafael O. Santana

Chairman & Chief Executive Officer, Westinghouse Air Brake Technologies Corp.

Thanks, John. Now let's turn to slide 13 to discuss our 2026 outlook and guidance. Overall, the team delivered a strong second quarter with operational results ahead of our expectations. Importantly, we continue to see underlying demand for our products and solutions across the business. That demand is reflected in a strong pipeline and both our 12-month and multiyear backlogs provide clear visibility into profitable growth ahead. With that backdrop, we are increasing our full year guidance. We now expect 2026 revenue of approximately $12.5 billion at the midpoint, up 11.5% from last year, which is an increase of 1 percentage point versus our prior guidance. We also now expect adjusted EPS to be in the range of $10.60 to $10.90, up 20% at the midpoint.

Now let's wrap up on slide 14. As you heard today, our team continues to execute against our value creation framework and our five-year outlook. The strength of our performance is driven by our resilient installed base, world-class team, innovative technologies and our customer-focused approach. We are also encouraged by the integration and early performance of our recent acquisitions, which are strengthening our portfolios and expanding our total available markets for future growth.

Overall, I believe Wabtec is uniquely positioned as a leading industrial technology company with a strong foundation, a talented global team and significant opportunities ahead. We are well-positioned to deliver profitable growth and continue to compound shareholder value over time.

With that, I want to thank you for your time this morning. And I'll now turn the call over to Kyra to begin the Q&A portion of our discussion. Kyra?

Kyra Yates

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

Thank you, Rafael. We will now move on to questions. But before we do, and out of consideration for others on the call, I ask that you limit yourself to one question and one follow-up question. If you have additional questions, please rejoin the queue.

Operator, we are now ready for our first question.

QUESTION AND ANSWER SECTION

Operator: Our first question comes from Ken Hoexter with Bank of America. Please go ahead.

Ken Hoexter
Analyst, BofA Securities, Inc.

Q

Hey, great. Good morning and congrats on raising the outlook. Rafael or John, maybe you noted kind of the mixed carload outlook on a global basis. Some wins on international, Australia in particular. Maybe thoughts on sustaining the 12-month backlog at that nearly one-time book-to-bill, is there – are you seeing – maybe Rafael just give an update on kind of what you're seeing out in the market in terms of keeping that progress going on, on the orders?

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

A

Okay. Ken, in terms of demand and backlog conversion, I mean, we are seeing improved demand in the year, and we are converting a strong pipeline into multi-year backlog and higher margins. You certainly see that globally. You saw the strong win we had in Australia in the second quarter. We continue to have opportunities of size, and you're going to see a couple of those coming to the second half of the year, so strong from that perspective.

On the execution front, I'd say we're continuing to drive better execution. And that's really coming with improved margins, and that's driven by productivity gains and the progress on simplification, Integration 3.0, despite the headwinds we still face with inflationary pressures, still managing through tariffs and chip shortages with the impact to electronics.

I think the other item to highlight is the acquisitions, which continue to perform very well, early days. So, overall, it's been stronger year with our teams delivering ahead of plan in support of the long-term guidance.

John, you might want to comment more on the specifics of the quarter.

John A. Olin
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.

A

Yeah. When we look at the second quarter, Ken, revenue was ahead of expectations as well as earnings. When we look at revenue, revenue was driven by a couple of things. Number one, on more of a sustainable basis, we saw our flow businesses accelerate, and that is on the Freight side. And as you pointed out, Ken, partially driven by the improvement in carloads, which has driven to higher year-over-year locomotives and operations during the quarter, and then we also saw some strength in the aftermarket in our Transit business.

The other piece of our revenue in the second quarter was some timing on shipments. We did see some pull forward from the back half into the second quarter. And also, as we talked about in the first quarter, we had a lower organic growth. We saw some push-outs of that. So they landed in the second quarter as well. But, overall, very strong revenue growth at 17.5% with organic growth up 8.5%.

When you kind of shift to the earnings side of it – and I'm sorry, going back to the revenue for that and the piece that is really more sustainable on the flow business, we've looked at that, we've forecasted it forward, and that growth to continue in the third and the fourth quarters at largely the same rate. And that has resulted in us raising our overall revenue guidance by $110 million or a full percentage point on the year. So, now we're sitting at a midpoint of 11.5%.

On the other side is the earnings. We did see earnings come in a bit more than what we had expected and a fair amount of that was driven by two things. Number one is on the flow revenue, it comes at typically a higher margin and we saw that reflected in favorable mix in that aspect. But overall, mix was still unfavorable, but less unfavorable than what we had anticipated. And then the other area is the integration and productivity came in stronger, making really good progress on Integration 3.0. And with that, we did the same thing and extended that goodness over the back half and with that, raised our midpoint of our guidance by $0.30 up to the $10.75.

Ken Hoexter
Analyst, BofA Securities, Inc.

Q

Hey, John, if I can just get a follow-up there, you mentioned the 3.0. Can you talk about how much cost savings were realized? And it sounds like, I don't know, maybe the message you're trying to give for margins into the third quarter from second quarter based on the run up you gave us?

John A. Olin
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.

A

Yeah. So, Ken, as you know, in the first quarter, we raised our guidance by $15 million on Integration 3.0. And we saw the momentum and the timing of these projects at that time, and we've seen that convert certainly in the second quarter. And we would expect from our original thoughts on the year that Integration 3.0 is going to drop more goodness on the year. And again, that is as part of that increase in the EPS guidance of $0.30.

Ken Hoexter
Analyst, BofA Securities, Inc.

Q

Thanks, John.

Operator: Our next question comes from Scott Group with Wolfe Research. Please go ahead.

Scott H. Group
Analyst, Wolfe Research LLC

Q

Hey, thanks. Good morning. So, if I look the 12-month backlog's up 11%. The total backlog's up 42% year-over-year. I think that's the biggest spread we've ever seen between the two. I guess, I'm trying to understand like what's the timing for that multi-year backlog to start converting to revenue? And ultimately, I guess what I'm trying to figure out is like, we had high single-digit organic growth in Q2, is that sustainable?

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

A

Well, two things. I'll start with just total backlog. And this is very strong coverage, Scott, to your point, and that's how we run the business, to make sure that we have that coverage. It's probably the strongest coverage we've had. It's a multi-year backlog that cover really a multitude of years. So, that's very good and really strengthens our position to deliver on the long-term guidance we provide.

In terms of the 12-month backlog, I think that number really supports the mid-single-digit growth from 5% to 6% that we've described for the year. And I think you got to extract from that some of the nuances associated with especially the acquisitions we've done.

John, I don't know if you want to add to that.

John A. Olin
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp. A

Yeah. Scott, you had mentioned organic growth in the second quarter. When you look at our overall growth of 17.5%, the easy way to look at this is half of it, about 8.5% is driven by the year-over-year impact of acquisitions. And the other half of it, about 8.5% is driven by organic growth. And that's certainly an acceleration from what we saw on the first quarter. If you remember, our first quarter organic growth was up 2.3% based on timing of shipments as well as the write-down of a digital project.

So I think the best way to look at organic growth is to look at it on the first half basis that takes care of some of the timing nuances there for which we're up 5.5%. And we feel good about that. When you look at the 12-month backlog as an indicator of that, if you take out the acquisitions and currencies and more normalize that, we are in that range of mid-single digits. And we see that continuing on in the back half of the year, given the strength that we're seeing in particular of our flow business.

Scott H. Group
Analyst, Wolfe Research LLC Q

Okay. That's helpful. And then just one follow-up for you, John. I think your comment about like the pace of margin suggests Q4 we see some really strong year-over-year margin improvement. I know it's early, but like is that a good way to think about what 2027 could look like that exit rate?

John A. Olin
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp. A

I would say looking at the half, Scott, is more indicative of that. So let's talk about why we're expecting what we're expecting, right? We're expecting the probably a significant majority of our margin growth to be in the fourth quarter. We expect growth in the third quarter, but that's going to be in the range of around 0.5 point that we saw on the first half of the year.

So why is the fourth quarter going to be up so much? And I think, first, we start with what happened a year ago in the fourth quarter. If you remember, Scott, we had one heck of a cash flow in the quarter. And actually, cash conversion was just shy of 300%. And as I think you also know is our comp plans and our focus on cash is throughout the organization, but it is embedded in both our short-term and long-term comp plans. And that drove a higher expense than we had anticipated. The second area in last year was the fact that our Transit business was level loading some production and move forward some benefit through production and moving production forward in the second and the third quarter. And consequently, we had a pretty weak margin in Transit in the fourth quarter, and that was driven by the manufacturing inefficiencies as we rebalance that. So we're lapping those two things that aren't going to repeat again this year.

The other piece of it, again, goes back to tariffs, right? Our tariff expense is going to be pretty even between quarters this year and certainly in the back half. However, the comparable is very different. In the third quarter last year, we had very little expense. We just started to see some, but it was nominal at best. The fourth quarter, though, we saw a large rise in our expense for tariffs as things came off the balance sheet, right, from when we incurred the tariff. And so the headwind in the fourth quarter is going to drop quite significantly between what we saw in the first three quarters. And between the confluence of those three things, we expect our fourth quarter to be up more than we would typically expect in a quarter with regards to margin growth.

Scott H. Group
Analyst, Wolfe Research LLC

Q

Super helpful. Thank you guys.

John A. Olin
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.

A

Thank you.

Operator: Our next question comes from Angel Castillo with Morgan Stanley. Please go ahead.

Angel O. Castillo
Analyst, Morgan Stanley & Co. LLC

Q

Hi. Good morning and thanks for taking my questions. Just maybe I wanted to start on Components. I was hoping we could kind of unpack that a little bit more. I guess you still have railcars down even though the outlook has improved a little bit. But just, the 1% decline is quite notable and you've talked about some of the pieces around flow, and you also mentioned, I guess, industrials business. So could you just help quantify, I guess, how much has the flow business improved? How much is maybe the railcars OE side down?

And then on the industrials part of the business, we would love to just hear a little bit more about, how that's progressing, what changes you're seeing there. In particular, I guess, the data center part of your Components business. Just curious, one, what you're seeing in terms of demand there? And then just more broadly from data centers, how is your strategy kind of changing or evolving based on the demand you're seeing? I know there's a lot in there, but all kind of related to Components.

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

A

[ph] Always is, (00:32:20) Angel. Angel, I'll start, and I'll let John dive into a little bit of the details. As we described them and we saw North America freight volumes strengthening, with that we saw really more of a demand for our full product [ph] re-did on parts (00:32:35), some fleets being unpart as part of that. And we've seen that continued strength on the Transit backlog.

When you talk specifically about the Components business, I think despite of the lower freight car build, I think our teams have continued to adjust, number one, the operations to align with that volume. I think they've driven significant cost discipline and margin improvement for the business, and we are continuing to see strong demand in the industrial applications. And some of that is particularly visible in the heat exchangers, which go into some of the demand for power generation, which is a positive in that regard.

John?

John A. Olin
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.

A

Yeah. Specifically, Angel, the Components was down 7/10 of a percentage point. And, actually, if you go back over the last six quarters, we've really seen pretty much the same thing is we're bouncing around that flat. Certainly, the team has been absorbing a significant down stroke with regards to railcar business, which is about 60% of overall revenue. And the other piece of it that we're finding this year, seeing this year as the exit of some non-strategic business and revenue in there.

So they're fighting, as Rafael had mentioned, from a cost standpoint, certainly from a market share, and they're offsetting a fair amount of what they can, but also getting a little bit of help on the industrial side. And we're not seeing a big shift in what we've seen in the industrial side for the last six or so quarters. It is up on a small basis, it's up pretty good, again, benefiting from some of the data center stuff. But it's a small base, but it is enough to largely offset what we're seeing that and the work of the team to offset what we're seeing with railcars being down. Now, we're hoping that that turns in 2027 and that's what the early forecasts are, but we've still got a couple more quarters that we expect railcars to be down in the 20% range.

Angel O. Castillo
Analyst, Morgan Stanley & Co. LLC Q

Got it. That's very helpful. And maybe just as a follow-up, I guess, could we maybe unpack the data center portion of power generation, maybe separate from what you might be seeing in heat exchangers and how that's progressing versus maybe any potential equipment demand. And how your earlier strategy, if it's changing at all, how you're viewing that market, the attractiveness to potentially look to target that a little bit more readily. I guess, just how are you thinking about that or what are you seeing?

Rafael O. Santana
Chairman & Chief Executive Officer, Westinghouse Air Brake Technologies Corp. A

Angel, I mean, as you mentioned, I'll start with the positive, heat exchangers. It is a positive for us. You're seeing that as, I'll call it, a significant offset to some of the pressures we've got on the freight car side of the house.

In terms of the engine side, when you look at engines in specific, I mean, our engines are really built for some of the most demanding applications in the world. They're exceptional for reliability and fuel efficiency. With that being said, when we think about data centers, a large part of that is connected to backup power only applications. We charge engines are generally not the most competitive solution for that application. We're continuing to look into selective opportunities for power generation applications, especially where we have more restriction around emission standards. But this is very much a niche segment of the market, and at this stage, we have had really only very, very nominal sales in the space.

Angel O. Castillo
Analyst, Morgan Stanley & Co. LLC Q

Very helpful. Thank you.

Operator: Our next question comes from Bascome Majors with Stephens. Please go ahead.

Bascome Majors
Analyst, Stephens Q

Good morning and thanks for taking my questions. I wanted to revisit the EVO Advantage modification program. I know you guys reported quite a bit of orders earlier this year in that space. Can you just give us an update on how the product is resonating with the Class 1 rails in North America? Where you are on the ramp up of actual delivery to where you think you'll be a run rate into next year? And how the pipeline compares to the backlog? And just a big picture of how you expect that to evolve as this product continues [ph] to route (00:36:59) in the marketplace? Thank you.

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

A

Thank you. Hey, first, I think we have seen continued progress in terms of the EVO Advantage program. We've announced that in the first quarter. We've gotten our first order in North America in the second quarter. So, that's consistent with what we expected. We see that as an opportunity to really continue momentum with regards to refreshing our installed base around the world, but especially in North America, providing what I call more value for our customers with fuel efficiency and really driving, I think, greater and better value outcomes for our customers. So, we continue to expand on the value that we can bring to our customers on fuel efficiency and continue to stay ahead and widen, really the competitive advantage versus our competition, so positive from that perspective.

Bascome Majors
Analyst, Stephens

Q

And you said first order in 2Q. So, just to be clear, the $1.3 billion in orders you received later last year, that was not for the EVO Advantage. The order conversion for this product is still mostly ahead.

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

A

Exactly. That's correct.

Bascome Majors
Analyst, Stephens

Q

All right. All right. Thank you.

Operator: Our next question comes from Rob Wertheimer with Melius Research. Please go ahead.

Rob Wertheimer
Analyst, Melius Research LLC

Q

Thanks. Rafael, you just touched on some of the fuel savings, but just given the global uncertainty around diesel, could you remind us of the, kind of, the fuel economy savings on mods and new, and then just how do your customers react to that? Do we have to see elevated prices for a year and then they think about doing more mods? Do they park older locos and run newer ones? Is there any impact from your business from diesel spiking now?

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

A

So, let me start at a high level. The short answer is we're much more efficient on moving goods through rail than by road. And I mean, that's favorable to the overall business as we see it. And I think that drives up positive dynamics. When we look at it specifically in North America, I think some of the comments I'll make is, I mean, you're seeing some of that movement of freight going into rail. I think that has translated into, I'll call, more visibly in our flow businesses, especially in Freight where we've seen that with specialty parts. With that, we have not seen yet any, I'll call, shift on demand for mods or new units on that. It's remained consistent with the demand as we have described before. But fuel prices up, it's a positive for the overall business.

Rob Wertheimer Q
Analyst, Melius Research LLC

Perfect. And then just in your last question, you touched on EVO orders. Are people still doing work on mods on older FDLs as well? I mean – or are they kind of waiting for EVO to be exciting? And I'll stop there. Thanks.

Rafael O. Santana A
Chairman & Chief Executive Officer, Westinghouse Air Brake Technologies Corp.

Yes, they are. I think, this is two-fold. And keep in mind, it's not just a function of North America. It's a function of international as well. This programs drive, I'll call, an average 5% plus advantage point on the fuel side, so very significant returns for our customers, but it's very customer dependent. You've got to look at the application. You've got to look at how they run their fleets. But this is a program that's going to advance our ability to continue to modernize the fleets, and that's how we think about it. It's continue to drive replacement, continue to drive modernization in that context. Early days on EVO mods but it's good to see the first order here in the second quarter.

Rob Wertheimer Q
Analyst, Melius Research LLC

Thank you.

Operator: Our next question comes from Ben Mohr with Citigroup. Please go ahead.

Ben Mohr Q
Analyst, Citigroup Global Markets, Inc.

Hi. Good morning, Rafael, John, Kyra. Thanks for taking my questions, and congrats on the quarter and the raise. I just wanted to continue on Ken's and Scott's questions there on revenue-related backlog. Midpoint of your revenue guide raise of up 1%, can you help us parse out how much of that is related to the rail volume strength in North America rails in 2Q that helped generate non-backlog revenue. You got your 2Q organic revenue up 8.5%. Sounds like you're guiding to second half organic revenue being roughly closer to mid-single digits. How much are you embedding continued rail volume strength to generate non-backlog revenue in the second half? Is it assuming the up 4% carloads, is it still there or is it more bringing that down to flattish and anything above could be upside?

John A. Olin A
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.

Yeah. So, going back to when we look at the revenue raise of the $110 million is largely driven by the flow business. And, Ben, as we've talked about 30% of our businesses flow, 70% is backed up by long-term agreements. And so, that's really just executing against the orders that we have. So where we're seeing the growth is, it's coming strictly from that. And as mentioned, it's coming from two places, one, is on the Freight side, and that is driven by that increase that we saw on the first half. Overall, carloads were up about just shy of 3% on the half, 4% on the second quarter. So what we've done is we've looked at that and held what we're seeing in the second quarter throughout the back half. And looking at the revenue that's behind us, driven by the flow business in the second quarter and adding on what we believe is a similar run rate in the second half, and that's delivering the $110 million of additional benefit.

Ben Mohr Q
Analyst, Citigroup Global Markets, Inc.

I appreciate that. Thank you for that color. That's very helpful. And then maybe looking further ahead, can I just ask – and congrats on this $1 billion Australia order. Seems like it's across Equipment and Services and other segments as well. Has that entered into your 2Q backlog? And then as related to that, are you still looking ahead in one- to two-year negotiations with some of those regions? I'll quickly list them out, Australia, East Asia, Uzbekistan, Mongolia, Pakistan, Brazil, parts of Africa. Are you still excited about potential orders from these in upcoming quarters where you're still on one- to two-year negotiations?

Rafael O. Santana A

Chairman & Chief Executive Officer, Westinghouse Air Brake Technologies Corp.

Very much. And that's why I mentioned really continued strength in the pipeline of opportunities. I feel like we've been talking about Australia for more than a couple of quarters. It has materialized and we continue to progress. Those international deals can take a bit longer than you would normally see. We feel very strong about more than a couple significant deals happening here in the second half of the year, and they're exactly tied to what you described there, and they're meaningful in that context. So, pipeline remains strong. And I think it's providing us stronger and stronger coverage as we look at the years ahead for Wabtec.

Ben Mohr Q

Analyst, Citigroup Global Markets, Inc.

Fantastic. Thanks for the time and insights as always.

Rafael O. Santana A

Chairman & Chief Executive Officer, Westinghouse Air Brake Technologies Corp.

Thank you.

Operator: Our next question comes from Steve Barger with KeyBanc Capital Markets. Please go ahead.

Christian Zyla Q

Analyst, KeyBanc Capital Markets, Inc.

Hello. Good morning. This is Christian Zyla on for Steve Barger.

Rafael O. Santana A

Chairman & Chief Executive Officer, Westinghouse Air Brake Technologies Corp.

Good morning.

Christian Zyla Q

Analyst, KeyBanc Capital Markets, Inc.

Can you just give us a sense of the current breakdown of the backlog for Freight? Is it primarily Equipment and Services in there or does it look more like the product mix for Freight? And then I guess just following up, which category are you seeing the most growth in the backlog?

John A. Olin A

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

Christian, the backlog would be made up of more of the Equipment side. They've got long lead times, and not so much on the flow stuff. That doesn't fall into the 12-month or the multi-year backlog because it's more of a turn product. And again, about 70% of our revenue falls into that backlog category, either 12-month or the multiyear. But it is predominantly on the longer lead-time equipment.

Christian Zyla
Analyst, KeyBanc Capital Markets, Inc.
Q

Got it. That makes sense. Thank you. And then just second question, kind of switching gears on the international opportunities and the regions you talked about. Are you guys starting to see a deeper penetration for the digital offering in international or is it still mainly core equipment, mods, service, etcetera?

Rafael O. Santana
Chairman & Chief Executive Officer, Westinghouse Air Brake Technologies Corp.
A

No, we are and I think that's a very exciting part of what we're saying is this – if you think about the technology and the strong momentum in digital innovation and automation, you asked specifically internationally, I mean, this is – we're seeing meaningful advancements. You saw our win on PTC 2.0, that's becoming more of a vital, element of how you run the railroad internationally. You combine that with Zero-to-Zero, this really brings great advantages to our customers. So, significant advantages there. We're continuing to also advance versus competition. I think we mentioned about EVO Advantage. We're continuing to advance on hybrid battery program. So, a lot of those things are really driving, I think, significant opportunities for us to continue to win internationally.

Christian Zyla
Analyst, KeyBanc Capital Markets, Inc.
Q

Great. Thank you.

Operator: Our next question comes from Harrison Bauer with SIG. Please go ahead.

Harrison Bauer
Analyst, Susquehanna Financial Group LLLP
Q

Great. Thank you for taking my questions. As you've implemented some of your tariff mitigation actions, have any of those changes proven structurally beneficial enough that they're likely to remain permanent regardless of how tariff policy evolves, specifically regarding sourcing, localization, supply diversification, stickiness of pricing processes? Thank you.

John A. Olin
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.
A

Thanks, Harrison. I would say that some are, and some are waiting to be implemented once we see some of the shifting of tariff rates in order to become more concrete, right, so some of these moves on the supply side. So, Harrison, we talk about a four-point plan to minimize these. One of those is working with the supply chain. So, yes, where we can, we've moved products from higher tariff areas to lower tariff in the United States. And a lot of these require a fair amount of investment to move. So there's still opportunity ahead of us once we get some stability in the overall rates before we start to change things around. But yes, some have proved to be good moves and that would stay that way if rates change again.

Harrison Bauer
Analyst, Susquehanna Financial Group LLLP
Q

Okay, great. Thank you. And maybe just to follow-up on some of the discussion regarding your mix. Within your long-term margin framework and I know you don't separately disclose the Freight component of margin growth, but can you help us understand what the relative contributions are from operational improvements, mix and synergies from some of your recently acquired businesses, and maybe just the natural maturation of your installed base toward a higher margin, aftermarket and digital revenue, and how each of those contributes to steady Freight margin expansion over time? Thanks.

John A. Olin
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.

A

So, Harrison, number one, in terms of strictly mix, over the long term, we would expect there to be a mix headwind as we grow our mods and locos at a faster rate than the average. And, Harrison, what I would like to say is there's two kinds of mix in this world, there's good mix and bad mix. And what we have here is a case of really good mix, right? Because putting these out even at a lower margin than the average, allows for us to garner service revenue off those for the next 20 to 30 years, and the components and certainly the modernizations that come from that.

When we look at, overall, the margin growth that we expect in our long-term plans, we've talked about 350-plus basis points of margin growth. I think the way to think about that, Harrison, is about two-thirds of it is going to come from the hard work that we do on managing the company's productivity and driving the company's productivity, right. And those are things such as everyday productivity and lean. We got a lot of opportunity to continue to propagate lean throughout the organization. Then there's the integration programs, which are more structural changes that are driving significant margin expansion. And then we got portfolio optimization as getting rid of some of the things that aren't going to take us to the future that we aspire to. So, that's how we see a fair amount of that 350 basis points going forward.

The rest of it is on adding more value, which is recovering the costs in the inflationary aspects that we have. Most of our contracts, 60% of our revenue have long-term contracts, and they have predominantly price escalators. And so that, along with the innovation that we're investing in and the selectivity that we're displaying certainly on the Transit side, would drive the extra third of that margin expansion over our time horizon.

Harrison Bauer
Analyst, Susquehanna Financial Group LLLP

Q

Thanks.

Operator: Our next question comes from Jerry Revich with Wells Fargo. Please go ahead.

Jerry Revich
Analyst, Wells Fargo Securities LLC

Q

Yes. Hi. Good morning, everybody. Nice quarter. Rafael, I want to ask on Service. As we've seen these really good freight volumes this year, has your Service business picked up steam or are you looking for the pure Service part to accelerate?

And then back on the mods part of the conversation, we've got obviously a product line transition here or life cycle transition here. Are we thinking about mods being down again 2027 versus 2026, given that FDL to EVO transition, can you just calibrate us on that lifecycle? Thanks.

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

A

Yeah. Jerry, I mean, I think we've been quite clear in terms of the benefit we've seen from the flow business, which is tied to this volume growth in North America and unparting of locomotives, so that's a positive. It's kind of early to comment on 2027 at this point. But what I'll tell you is we look at the balance of the year. The things we're watching are like if you think about upside where it could come from, it could come from customers continue to unpart units and sustaining that unpart fleet. So, I think that's something to watch. It could also come from as we continue to advance Integration 3.0 and simplification, if the productivity that we get from these initiatives materialize faster.

Now, we've got to take into consideration the risk side, which we continue to be mindful of. Well, I guess inflation pressures, especially on the container side, we mentioned chip shortages with electronics. And we're closely watching here the North American railcar built in this context and managed through tariff-related changes. But execution remains always a key variable to watch, but it's been a positive, so far.

Jerry Revich
Analyst, Wells Fargo Securities LLC

Q

Okay. Super. And then can I ask on Transit, really nice margin performance. Can you just talk about out of the legacy business excluding the acquisition? Where are we in terms of the proportion of backlog that's at your target margin levels? And is it fair to think about the margins in backlog as higher than what's flowing through margins through sales this year?

John A. Olin
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.

A

I'll start. When we think about Transit, I mean, it's great progress. Our teams are continuing to drive a lot of the actions around productivity and simplifying the operating footprint. I think we see here a clear path towards the [ph] high-teen (00:54:18) margin performance that we've described before. Mix was a positive for the quarter. And I think the other positive point here is the acquisitions, the Dellner acquisition, still early days, but it's going very well. In fact, when we think about the acquisitions overall, I mean, they're on track to deliver on the synergies. And when we think about the overall dynamics, it's positive there, ahead of plan.

Jerry Revich
Analyst, Wells Fargo Securities LLC

Q

Okay. Thanks.

Operator: Our next question comes from Tami Zakaria with JPMorgan. Please go ahead.

Tami Zakaria
Analyst, JPMorgan Securities LLC

Q

Hey, good morning and congrats on very impressive results. I wanted to double click on a prior question on freight traffic because in North America, freight traffic accelerated quite notably in the quarter. What are some of the factors you believe drove that? Was it driven by any specific industry? Or was it broad-based? And do you believe this is sustainable going forward because it's probably great news for your flow business then. So any color would be helpful.

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

A

Tami, I think we've certainly seen movements into rail. And I think there's a combination of factors there which tied to the dynamics on the truck market, fuel prices being up, some still driver shortages there. And I think some of those dynamics are connected with better service in rail and I think are kind of driving some positive results so far.

Now that's certainly very visible on the second quarter. As I mentioned, I think we'll continue to watch that. And that's where, I'd say, upside could come from. It's customers continue to unpart units and continue to sustain that level of unpart units in that context. But that's something that you need more than a couple of quarters, and that has not yet translated into any shift in terms of demand for mods or new units in North America. The demand there continues, but to be very consistent with how we've described before.

Tami Zakaria
Analyst, JPMorgan Securities LLC

Q

Understood. Thank you. That's all I had for today.

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

A

Thank you.

John A. Olin
Executive Vice President & Chief Financial Officer, Westinghouse Air Brake Technologies Corp.

A

Thank you.

Operator: This concludes our question-and-answer session. I would like to turn the call back over to Kyra Yates for any closing remarks.

Kyra Yates
Vice President-Investor Relations, Westinghouse Air Brake Technologies Corp.

Thank you, Bailey, and thank you, everyone, for your participation today. We look forward to speaking with you again next quarter.

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