GE Aerospace

Edited Transcript

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<<Peter Arment, Senior Aerospace & Defense Analyst, Robert W. Baird & Co.>>

We are delighted to have GE Aerospace with us here today. From GE, we have Rahul Ghai, who is Senior Vice President and Chief Financial Officer. Rahul, thank you again for your continued support for the conference. Really appreciate it. Welcome. Rahul is going to make a couple of opening comments and then we'll get into a little Q&A. So, Rahul, welcome.

<< Rahul Ghai, Senior Vice President and Chief Financial Officer, GE Aerospace>>

Peter, thanks for having us, much appreciated. Pretty big conference, so thank you for allowing us to meet some investors. But it's been a busy fall so just maybe taking it from the top, really good momentum in the business. Obviously, we've got the largest installed base between commercial and defense in the industry with 18,000 engines and continued commercial success building on that installed base just since we released earnings. And in the third quarter here, we got the LEAP-1B order of about 300 engines from Turkish Airlines. And on the defense side, our engine for the NGAP program got down selected for the next phase. So just continued commercial momentum. Operationally very strong, we had 26% services growth year-to-date and 21% engine deliveries increase on a year-over-year basis.

So, good operational momentum as well. And as most of the people in the room probably know, we also announced the CPP transaction just after Labor Day. And the thinking behind that was on the strategic side, we wanted to do two things. One, castings is one of the most mission critical components in our industry and we wanted to build capacity for that commodity, not just for ourselves, but for the industry in general. And that goes for defense, that goes for commercial because that is a critical component that is needed for continued growth of output across our product lines.

The second thing was we've been testing this new airfoil that runs much cooler. And we have about 3,000 test cycles on that new airfoil. And, it's more durable and it will increase the time on wing for both the current generation and our next gen products. And as we think about bringing that technology to market, this acquisition definitely accelerates the time to market for that new technology. So that was the second strategic reason for doing that. And operationally as we think about the transaction, clearly there's value that FLIGHT DECK can bring to how CPP is run today. We've demonstrated that with our own results over the last couple of years, but now even more so with and we can take that to CPP, reduce the scrap, reduce the rework that happens as they produce their both structural and airfoil castings.

And so you put all that together between the strategic and the operational benefits that we drive that leads to a year one accretion on EPS and free cash flow for the GE shareowners and a double digit ROIC as we get into early 2030s. So it, it should be a good financial transaction. And then on our financial performance since we started the year and in the third quarter, our orders were up 50% year-over-year. So really strong momentum on orders including Commercial Services that was up 23%. And Commercial Services is up about 30% on a year-to-date basis. So strong orders momentum across all our product lines. And then that translated

into really strong revenue growth. Our revenue was up high teens, profit of $3 billion, margin expansion of 220 basis points in the quarter, so really strong third quarter results.

And that's largely on the back of our strong Commercial Services performance, our revenue is up like 26% on a year-to-date basis. And that allowed us to raise the full year guidance. For the year, we're going to now grow our profit about $2 billion, grow cash flow $1.5 billion for the year. And that gets us very, very close to our 2028 targets on profit and exceeds the target for '28 that we have provided just last summer.

So much stronger growth rates than we expected in the business, you know, when we gave our '28 guidance in July of 2025. So great, great operational momentum, great commercial momentum, financial results are strong. So we expect that to continue as we get into 2027 and we're expecting Commercial Services to be up low double digits next year, which is higher than our double digit kind of run rate that we had expected. And that low double digit growth is mostly going to be driven by the engines that will be off wing as we exit this year. So that will be more or less in our backlog and the removals that we are expecting in the first half based on the number of cycles that the engines have already flown.

So they need to come off because, you know, they need, it's time for an overhaul. So that should drive continued profit growth as we get into 2027 as well. So that's where we are. With that, I'll let you lead us into questions.

<<Peter Arment, Senior Aerospace & Defense Analyst, Robert W. Baird & Co.>>

Terrific. Great overview, strong momentum in '26. So you talked a little bit about '27. You also mentioned, I think, high single digit, expecting high single digit growth in Defense and Propulsion Technology as well in addition to the low double digit growth. But I guess beyond those comments, you know, what assumptions are most important to you as you kind of build the plan for January? What is, like where is the visibility strongest? Maybe thinking into airline conditions as well, production rates, execution, kind of all those things wrapped up?

<< Rahul Ghai, Senior Vice President and Chief Financial Officer, GE Aerospace>>

Absolutely. So again, just thinking about ‘27 on defense, so maybe we start there. We're expecting high single digit revenue growth for defense. The defense backlog is up 20% this year, 33% orders growth on defense. Defense book-to-bill is like 1.5. So we expect high single digit growth next year with continued margin expansion on the defense side. And as we think about the commercial business, we're expecting on services $3.5 billion to $4 billion of revenue growth, which is the low double digit that I mentioned. And that $3.5 billion to $4 billion is higher than what we started our expectation in 2026. Because we started the year, we were expecting $3.5 billion of services growth, ending is like $5.5 billion. So better momentum during the year than what we expected in the beginning.

But next year, our initial outlook is $3.5 billion to $4 billion. That as I said a minute ago is mostly driven by the backlog that we'll have at the end of this year and the engines that will come off-wing in the first half of next year. You combine that with improvement in workscopes that we're expecting and I'm sure we'll get into that here, Peter, so I won't spend too much time on that and the improved pricing. So you put all that together that gets us to the low double

digit growth rate, which is better than what we, you know, what we are, you know, what we kind of normal run rate is. And the good news there is and that why we feel confident about that growth is because if you look at even with the strong 26% year-to-date services growth that we've had, our spare parts backlog and the backlog that is delinquent is actually up sequentially and up the last couple of quarters.

So that, you know, the backlog continues to grow, which speaks to the strong demand environment that we're in. So that's on services. And on the engine side, we expect engines to grow higher than our services on a percentage basis, but obviously engines or the OE side is a smaller business. So the dollar growth will be lower than services, but the percentage growth will be higher. And then we'll continue to build on our 9X shipments to Boeing as well. And that has an incremental financial impact of about $300 million as we think about 2027 versus 2026.

So you put all that together, Commercial Engines and Services should be, margins should be consistent with 2026, given services growth offset by the 9X impact. Total company expect, we haven't really commented on profit, but we did speak on our earnings call that our margins should be consistent with 2026 at the total company level. But if you take our revenue growth, you take consistent margins, that just means, you know, strong continued momentum on profit growth with continued 100% plus conversion for '27.

<<Peter Arment, Senior Aerospace & Defense Analyst, Robert W. Baird & Co.>>

Yes. So I was going to ask, right about cash conversion, so you led me right there. Just how durable is cash conversion that shop, shop visits and investments kind of continue to grow? How do we think about that?

<< Rahul Ghai, Senior Vice President and Chief Financial Officer, GE Aerospace>>

Yes. So this year, Peter, just to kind of anchor everyone, this year our latest cash guidance is $9.1 billion to $9.4 billion. Last summer, we said $8.5 billion by 2028. So we're exceeding that 2028 target by call it, you know, $600 million to $1 billion in 2026, so couple of years earlier. And that's at 110% conversion. So the conversion has been very strong. A big driver of that has been the continued billing increase and the favorability on contract assets and liabilities. And as we think about 2027, we expect greater than 100% conversion even for 2027. The favorability on contract assets and liabilities will come down, won't be as strong just given the increase in shop visit output.

So that will continue to grow. So that favorability won't be as strong. But our inventory has been building up. Because just given the material availability, we don't get all the material that we want from all our suppliers. So we've got a lot of trapped inventory right now because we've got, you know, 9 out of 10 parts for an engine, we don't have the 10^{th} part, right, to complete a shop visit or an engine. So as material availability gets better our inventory growth should moderate substantially as we get into 2027. So that kind of offsets that. So therefore, we expect greater than 100% conversion for 2027 as well.

And as, you know, as we look beyond that, if we get into the medium term, we still should be in that 100% range even over the next few years.

<<Peter Arment, Senior Aerospace & Defense Analyst, Robert W. Baird & Co.>>

Perfect. Let's talk a little bit about services and orders. You determine -- you know, what determines how quickly some of the kind of strong commercial service orders become revenue? Like, what, what's the driver there?

<< Rahul Ghai, Senior Vice President and Chief Financial Officer, GE Aerospace>>

Yes. So the typical cycle, Peter, is six to nine months. On average, if things are flowing seamlessly across our value chain, you would think six to nine months because this is a shorter cycle business. But given where the material availability has been and even though material availability is getting a lot better, we've had probably 10 consecutive quarters of material increase and last quarter we were up 10% both sequentially and on a year-over-year basis. So material availability is getting better. But even with that, as I said a minute ago, our, both our backlog and our delinquent backlog both have increased on spare parts.

So the cycle is more closer to 12 months if not, maybe even slightly longer than that. So it is lagging behind. But it is converging. So if, you know, I spoke to some of these numbers earlier but our orders growth this year has been 30% year-to-date, revenue growth of 26% year-to-date. So those numbers are converging, but still not, not exactly there. So it keeps getting better, but that is what makes us feel better that, you know, the orders that we received this year, they should convert into revenue in 2027. And thus, the confidence in this continued strong services growth for next year.

<<Peter Arment, Senior Aerospace & Defense Analyst, Robert W. Baird & Co.>>

Got it. Perfect. Let's stick with kind of an aftermarket theme around kind of your worldwide shop visits, you know, maintaining around the 2,400, I think was the number next year that was out there. And that I guess in your opening comments we talked, you mentioned the workscope, you said we'd probably talk about it. So is that kind of the flat workscope that you were kind of referring to and maybe just flush that out a little bit regarding when you think about retirements and supporting of the airframers?

<< Rahul Ghai, Senior Vice President and Chief Financial Officer, GE Aerospace>>

Yes, absolutely. So I think we're talking about CFM56 shop visits at 2,400. I think that's what you're referencing. So overall, listen, if you look at the CFM56, it's a relatively young fleet. Two thirds of the engines have not yet gone through a second shop visit. And if you look at the work that we do, more than 80% of the work that we do is on, you know, first or second shop visit, engines that are less than 20 years old. And most of the retirements that are happening are happening in the 20 year plus range. So the retirements does not really reduce and impact the shop visits directly.

But even if you touch on retirements a little bit, if we, when we started the year, we were expecting the retirements on CFM56 to be between 2% to 3% for the year. Now with 10 months kind of behind us, we think the number is going to land somewhere below 2%. So the retirements continue to kind of lag behind our initial expectations. And as we think about next year, we think that, I mean, we expected 3% to 4% retirements for next year. But given the rate push out of Rate 52 at Boeing into the second half of next year, that probably takes the retirements closer to three than three to four, right, just given that, you know, there won't be as much OE output as there was previously expected.

So that pushes CFM56 retirements closer to 3% range. And we had taken up the number of shop visits for CFM56, as you mentioned, to 2,400 back in the summer. So now and that was obviously built on that 3% to 4% retirement rate. So now as we think about a 3% retirement rate, that probably gives us a little bit of contingency in that number. And, you know, even if other things happen, we should be able to get to 2,400. So I think that's kind of our overall expectation now.

As we think about the workscopes on CFM56, the workscopes are driven by the amount of cycles the engines have already flown. And most of the work that is with the engines that we are seeing right now need a replacement for life limited parts. So there's not a lot of variability in the workscopes that the airlines can manage because those life limited parts do need to change. And they need a new stack of life limited parts. So that is driving the workscopes. The workscopes are largely consistent. There's not only -- there's not been a huge issue in the last few quarters and that's what we expect for 2027 as well that the CFM56 workscopes should be consistent with this year very similar and the growth will just come from incremental price and slightly higher shop visits next year.

<<Peter Arment, Senior Aerospace & Defense Analyst, Robert W. Baird & Co.>>

How sensitive is the CFM56 aftermarket to kind of the fuel prices or things of that nature? So you know, whether and we're obviously planning for a lot more deliveries and used material availability, you know, that's out there as well.

<< Rahul Ghai, Senior Vice President and Chief Financial Officer, GE Aerospace>>

Yes, absolutely. So the, I think in the longer term, of course, there is a linkage between the two. But in the near term, as the work for '27 is more contingent on the cycles that have already have been flown. And if you look at the park, number of parked aircraft, the parked aircraft is still below where it was before the start of the conflict. As I said a minute ago, the retirement rates have not increased. So we've really not seen any change in fleet plans, based on what is happening in the air traffic. So if you look at the work being contingent on the number of cycles being flown, the fleet cycl -- the fleet plans for various airlines just learning from the COVID experience not changing a ton, a lower OE growth rate especially at Boeing for next year.

I think that just gives us confidence the CFM56 is going to be here, you know, strongly in 2027 and beyond. And that does not factor in any of the power demand that is emerging.

<<Peter Arment, Senior Aerospace & Defense Analyst, Robert W. Baird & Co.>>

Right.

<< Rahul Ghai, Senior Vice President and Chief Financial Officer, GE Aerospace>>

Right? Because with, I'm sure, you know, lot of people in the room are aware of a lot of need for our engines to power the new data centers and a lot of, and that has largely been a wide body play. And now with the tightness in the number of engines that are available for data centers and the power needs that the data centers have, there's a lot of push to convert CFM56 engines for the data centers as well. So that gives us another leg of growth and absorbs a lot of retirement that may have otherwise created some used material in the market.

So it reduces the cannibalization of OE sales. So I think given everything that I've just said, I think we expect that shop visits for CFM56 should stay in the 2,400 range for '27 and '28, you know, then gradually starting to come down. But the revenue growth should continue right into 2030 given price increases.

<<Peter Arment, Senior Aerospace & Defense Analyst, Robert W. Baird & Co.>>

Very clear. Thank you. On the, let's talk a little bit about LEAP service margins, you know. How, how should we think about like, you know, what must happen for LEAP service margins kind of reach the broader service margin level as you know, kind of the target in 2028?

<< Rahul Ghai, Senior Vice President and Chief Financial Officer, GE Aerospace>>

Yes. So listen, overall really pleased with how LEAP is doing. Our backlog for LEAP is now more than 17,000 engines. And if you look at Boeing, of course, that's 100% because we are the sole supplier. And at Airbus now our backlog for the undelivered engine, aircraft at Airbus is now at close to 70%. So 70% share on the backlog at Airbus, 100% share at Boeing. So really strong commercial success that I spoke to earlier. So that's on one side. And then if you look at the, on the services profitability that you just asked about, Peter, the, our services business broke even in 2024.

And what we're expecting is by 2028 the LEAP Services margins get to the overall Commercial Services margins. So within a four year time span, you know, there's going to be a huge ramp up in margins, which and, and we are tracking really well to that. So it's not back end loaded. You know, we are on a steady state up curve on our LEAP services margins. And it's coming, I would say, largely from three things. One, the cost. The cost of the shop visit is coming down. It's coming down for two reasons. One, we're expecting about 25% growth in number of shop visits every year on a CAGR between 2024 and 2030. So if you look at that, we have a fixed installed base. We are pumping more volume through it. So basically, it helps us with fixed cost absorption.

The second thing that we're working on is we're developing a lot more repairs for the LEAP parts and the number of repairs growing is like 20% every year. So anytime we don't need a new part and we use a repaired part the cost is like a fraction. So that brings down the cost of the shop visit. The second thing that is happening is that the third party channel is growing. About maybe if you go back a couple of years about 10% of the shop visits were performed by a third party channel partner. This year the number is 15%. And if you look at our services backlog of number of shop visits globally that number is closer to 25%.

So that number will continue to climb up and as external channel grows that comes with higher margins. And the third part of the LEAP margin expansion is going to be on price. If you look at the shop visits that we -- the pricing of shop visits, our pricing of shop visits is up 50% from ‘19 to ‘21 time frame, so kind of the COVID and the launch period to between ‘22 to ‘26. So that, you know, what we're selling the shop visits is like 50% higher. So that begins to show up in 2028 in a very, very small way, but maybe a small contribution, but a lot more beyond that.

So if you look at 2030 LEAP margins that incremental pricing should contribute almost two points of margin expansion for LEAP. So LEAP will get to services, overall services margins

level by 2028 with additional margin expansion beyond that. And then if you look at the profits on a dollar basis, LEAP and CFM56 should contribute kind of similar levels of profit by 2030.

<<Peter Arment, Senior Aerospace & Defense Analyst, Robert W. Baird & Co.>>

Wow.

<< Rahul Ghai, Senior Vice President and Chief Financial Officer, GE Aerospace>>

So, so really, really strong again going from breakeven in 2024 to CFM56 type of profit by 2030. So it's been, it's been a really good story for us.

<<Peter Arment, Senior Aerospace & Defense Analyst, Robert W. Baird & Co.>>

Yes, it's terrific. Maybe staying within services, just talk a little bit about how much runway remains within the widebody services cycle with thinking about GE90 and GEnx, you know, as those kind of fleets mature. How much will workscope continue to contribute to growth? How are you thinking about that?

<< Rahul Ghai, Senior Vice President and Chief Financial Officer, GE Aerospace>>

No, listen, overall widebody franchises is something that's really strong for us. So we power maybe about 55% to 60% of the widebody cycles in the world between GE90, GEnx and CF6, right? Those are three kind of key franchises. And what we are seeing for widebody is our overall services growth for this year is very similar between widebody and narrowbody. So widebody is growing really nicely. And it's coming from I would say kind of, you know, three main things again. One on GEnx, we expect the installed base of NX to double between '24 and '30. So a lot more growth on NX just because the new engine it continues to grow.

And on NX, 50% of the engines have not seen their first shop visit, 90% have not seen their second shop visit. So as they go from like a quick turn to their first shop visit, second shop visit, we're seeing a workscope increase, right. And very similar to LEAP, the pricing for NX shop visits has also been increasing. So I, I quoted a number of 50% growth in the LEAP shop visit price, equal in number for NX is that NX shop is now 30% higher. The price of NX shop visit is 30% higher over the last few years than if you go back to, you know, before 2020.

So that drives kind of the NX growth and then on GE90, a lot more of demand just given it's both for passenger and now increasingly for freight. And we missed the kind of the freight story but if you look at our departures for freight, they are up call it mid-single digits this year, just given the disruption in shipping lanes, a lot more airfreight, which was similar to where we were last year. So a lot of GE90, and we've seen almost no retirements on GE90, just given the increased need for freighters, and the push out on the 777X from Boeing. So if you put all that together, the GE90 installed base is very steady and the growth is largely coming from increase in workscope, because we're seeing a lot more second shop visits for GE90 and that's like, you know, 50%, 60% higher workscope on GE90 second shop visit versus the first shop visit.

And then CF6 is steady as, as it goes, right. So between GEnx install base growth, workscope increased pricing, all that is working in our favor, GE90 workscope expansion is working in

our favor and CF6 is steady. So you put all that together, it's a great franchise and we think, that's a high single digit growth services business with above overall CES service margins. So margins on widebodies are very strong.

<<Peter Arment, Senior Aerospace & Defense Analyst, Robert W. Baird & Co.>>

Yes, good tailwinds there. Let's maybe switch a little bit to 9X. You know, maybe how should investors separate the GE9X kind of timing effect from the underlying equipment economics?

<< Rahul Ghai, Senior Vice President and Chief Financial Officer, GE Aerospace>>

Okay. Yes. So I think what you're trying to get at Peter is, okay, on the financial impact that we're seeing, how much is from engine shipments and how much is the rest?

<<Peter Arment, Senior Aerospace & Defense Analyst, Robert W. Baird & Co.>>

Yes, that's right.

<< Rahul Ghai, Senior Vice President and Chief Financial Officer, GE Aerospace>>

Yes. So if you look at, you know, again, proud to be underwing on 777X, the backlog currently sits at more than 1,300 engines. We've been shipping engines to Boeing starting last year. We shipped more in the first half of this year. So the shipments continue. And if you look at the total financial impact to us, it's losses of about $250 million or so in the first half expecting similar amount in the second half. About $100 million of that $250 in the second half is going to be like R&D, somewhere in that range and the remainder is going to come from engine shipments. And where we're spending the R&D is obviously dust and durability testing, making sure that the engine is as durable as it can be.

The engine has been certified since 2020. So all we're spending money is just making sure that it's, you know, the durability is strong coming out of the gate and that is where the R&D money is going. So that's kind of where we are. So and as I said earlier on, you know, on the year 2027 question, overall, we think the financial impact is go from like $500 million or so this year to with an incremental $300 million of losses for next year.

<<Peter Arment, Senior Aerospace & Defense Analyst, Robert W. Baird & Co.>>

Got it. Let's quickly touch upon CPP. I think that's hard to ignore and not ask you. So, you know, how, how do you think about that? How does that change capacity, technology, some of the returns you're thinking about there?

<< Rahul Ghai, Senior Vice President and Chief Financial Officer, GE Aerospace>>

Yes. I said a couple of things in my opening comments. But again, the strategic rationale here, Peter, is around building incremental capacity for the industry and defense customers. You know, CPP has some of the key components on a lot of the missile programs. And it, you know, the technology at CPP is very, very strong. So CPP provides airfoils for us for our most advanced engines like they provide airfoils for LEAP, they provide airfoils for 9X which is our, our highest technology airfoil. So they have the technological capability, we need to build some

capacity. I think our ownership of that business will drive that build out of capacity because we'll take a longer term view of that business. So that's one.

And then secondly, as I said earlier that we've been testing this new airfoil that runs much cooler. So it's been under development. We have 3,000 cycles of testing on that new airfoil. And owning that asset in house will accelerate the time to market. So that was kind of the second strategic reason. And then you've seen the value that FLIGHT DECK has added to our business with kind of, if you look at a two stack, a two-year stack of services and engine growth, two-year stack is close to 50% growth on services and on engine deliveries and that's all FLIGHT DECK.

I think we can bring the same mindset to CPP and drive their, you know, reduce their scrap, reduce their rework, and drive higher output. So that's kind of the thinking behind doing that. And as I said earlier, for our shareowners that should be an accretive transaction both on an EPS and free cash flow basis in 2028.

<<Peter Arment, Senior Aerospace & Defense Analyst, Robert W. Baird & Co.>>

Terrific. And then let's wrap up with kind of capital deployment.

<< Rahul Ghai, Senior Vice President and Chief Financial Officer, GE Aerospace>>

Yeah.

<<Peter Arment, Senior Aerospace & Defense Analyst, Robert W. Baird & Co.>>

Maybe how does CPP change the balance between organic investment, innovation, anything else, you know, on the shareholder returns, how you're thinking about that?

<< Rahul Ghai, Senior Vice President and Chief Financial Officer, GE Aerospace>>

Yes, it doesn't really change anything, Peter. Luckily, given the strong cash flows we've had, we have, you know, we are an A minus company right now. So a lot of cash on the balance sheet. So we deployed some of the cash towards CPP acquisition. But we still, our dividend is still up 30% this year. We expect dividend to continue to grow because we are still below kind of what we're targeting as percentage of net income. So we expect dividend to continue to grow. And then we are buying about $7 billion of our own shares this year.

And we continue as we think about 2027 and beyond, we still feel that our goalpost at greater than 70% of our free cash flow goes back to shareowners. That does not change with this transaction. So I think we're going to maintain our, our buyback posture, we're going to maintain our dividend posture.

<<Peter Arment, Senior Aerospace & Defense Analyst, Robert W. Baird & Co.>>

Yes. And still be able to invest in things like RISE and things like that.

<< Rahul Ghai, Senior Vice President and Chief Financial Officer, GE Aerospace>>

Absolutely. You know, that organic investment comes first. So we are investing $3 billion in R&D between our own funds and customer funded funds and then about $1 billion in CapEx. And R&D is going towards LEAP, you know, just improving the durability, R&D is going towards 9X as I said earlier. And then for Future of Flight between our commercial RISE, we're working on the open fan, we're working on a compact core, we're working on hybrid electric and then obviously for Sixth Gen defense, our R&D is going towards that and then on, on the Collaborative Combat Aircraft, the CCAs. So that has been our investment for defense. So that does not change either.

<<Peter Arment, Senior Aerospace & Defense Analyst, Robert W. Baird & Co.>>

Terrific. Well, we're out of time, but thank you so much for everyone joining us. Rahul, thank you again for supporting the conference. Thank you again.