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Dowlais

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Questions on the webinar from

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H1 24 Overview

Liam Butterworth, Chief Executive Officer

Thank you, and good morning, everybody. Thank you for joining us today for our 2024 interim results. In the first half, our market-leading driveline business, China JV, and Powder Metallurgy, which account for more than 75% of the group's revenues, all outperformed their markets while volatility in BEV production significantly impacted four high-content platforms in our ePowertrain business.

The past six months have been challenging for both our industry and Dowlais as we navigated a volatile market environment, but my management team and I are absolutely laser-focused on everything that we can control. We've navigated volatility before, most recently during COVID and the supply chain and semiconductor crisis, and we'll do it again. We've taken decisive actions to limit the impacts of the volume headwinds on profits and unlock value from our portfolio.

And here are the actions that I want to highlight. Firstly, we've been absolutely relentless in controlling our cost base to limit the impacts of volume decline on operating profit. Secondly, we've initiated a comprehensive program of commercial recoveries with our customers. Along with ongoing restructuring programs and performance initiatives, these actions will positively impact the drop-through margin in the second half of the year.

And finally, today's announcement of a strategic review of Powder Metallurgy and the disposal of our hydrogen operations underscores our commitment to unlocking value from our portfolio and delivering shareholder returns. We completed the disposal of GKN Hydrogen earlier this month, eliminating the expected cash losses associated with the business, which amounted to GBP23 million in 2023.

And we've commenced a comprehensive review of the GKN Powder Metallurgy business, considering a range of options, including a potential sale. Over the last 18 months, Roberto and I have worked closely with the teams who understand the business, established a new leadership team and developed a clear strategic and commercial plans to accelerate the portfolio transition.

I believe now the time is right to move forward with our strategic review I remain confident in the medium term outlook, as we continue to accelerate the transition of our portfolio to powertrain-agnostic products, which I firmly believe will better position us to navigate market volatility and deliver sustainable, profitable growth and cash generation in the medium term.

I'm now going to hand over to Roberto to present the financial results in detail.

Financial results

Roberto Fioroni, Chief Financial Officer

Thank you, Liam, and good morning, everyone. We will go into detail on each of these P&L lines. But in summary, our adjusted revenue declined by 5.1% in the first half, with adjusted operating profit down 9%, driven by lower volume. The adjusted operating margin of 5.9% was 30 basis points lower than prior period as the impact from lower volume was partially offset by rigorous and proactive cost management and pricing recoveries.

We generated GBP10 million of adjusted free cash flow, down from GBP33 million in H1 2023, mainly due to lower earnings, higher interest and restructuring outflows. Adjusted basic earnings per share were 4.9p, down 30% year over year, and the Board has declared an interim dividend of 1.4p per share, in line with the group's dividend policy, reflecting the confidence of the Board in the medium-term outlook.

Let's delve further into group revenue. The decline in revenue in the first half was primarily driven by lower revenues in automotive and foreign exchange headwinds, with Powder Metallurgy revenues remaining broadly flat. Foreign exchange headwind of GBP114 million was largely driven by the British pound strengthening against the US dollar, the Euro, and the Chinese yuan. At current spot rates, we expect the foreign exchange impact on revenue for the full year to be approximately GBP200 million.

Moving on to operating profit. Adjusted operating profit for the period was GBP151 million, including a GBP7 million loss for the hydrogen business. Operating margin declined by 30 basis points year over year at constant currency to 5.9%. As you can see in the chart, this decline was mainly driven by lower volume.

Despite the volume weakness, we took actions to proactively manage our cost base, effectively mitigating the impact on margins and limiting the drop-through from 30% in our financial model to 11%. Inflation was more than offset by procurement efficiencies and recovery from customers. The column labelled performance represents the benefits delivered by continued operational efficiencies, which had a positive contribution of GBP24 million net of labor inflation.

Foreign exchange headwinds were GBP10 million. And at current spot rates, we expect the foreign exchange impact for the full year to be approximately GBP17 million. We remain focused on long-term profitability by rigorously managing pricing, proactively controlling costs and executing our self-help initiatives to deliver improved margins.

Let me now deep dive into the performance of our individual businesses, starting with GKN Automotive. Adjusted revenue declined 6.3% to approximately GBP2 billion. Driveline, with an adjusted revenue decline of 1.4%, outperformed a declining global light vehicle production rate, excluding China, of 2.4% in the half, demonstrating resilience through customer and geographical diversification. Our China business continued to perform well, gaining share with local OEMs as revenues grew 6.6% ahead of the market.

ePowertrain accounted for over 60% of revenue decline in automotive due to volume decline in product mix, given it has significantly higher content per vehicle than the driveline product group.

Adjusted operating profit of GBP122 million declined 13%, leading to adjusted operating margins of 6%, a decline of 50 basis points at constant currency. The continued execution of the team around commercial recoveries and performance initiatives only partially offset the impact of lower volumes on profit as we contained the drop-through margin to an impressive 14%.

Moving to Powder Metallurgy. Powder Metallurgy had a good start to the year and generated adjusted revenue of GBP527 million, a slight increase of 0.2% year on year in constant currency, growing ahead of the market. The slight drop in revenue in the core portfolio due to the ICE decline was offset by growth in EV products and metal-additive manufacturing.

Adjusted operating profit for the period was GBP50 million, resulting in an adjusted operating margin of 9.5%, a 50 basis points improvement from the prior period. This improvement was mainly driven by the successful resolution of one-time operational challenges from the prior period and a favorable regional mix. The business also offset inflationary increases through operational efficiencies, generating a net GBP2 million benefit versus first half of 2023.

Moving to earnings per share. We delivered adjusted basic EPS of 4.9p. Compared to prior period, adjusted EPS was down 30%, largely due to lower earnings and higher finance costs. Adjusted net finance charges of GBP56 million were higher than prior period year -- were higher than prior year as it reflects a full first half impact of the post-demerger capital structure and our effective interest rate on bank borrowing remained stable at 6.5%.

Tax charges were GBP24 million with an effective tax rate of 25%, in line with our medium-term outlook. Statutory basic EPS was a loss of 7.3p. Moving to cash. As a group, we generated GBP10 million of adjusted free cash flow in the first half. This is GBP23 million lower than H1 2023, largely due to lower adjusted EBITDA, higher interest payments and higher restructuring payments, partially offset by lower capital expenditure and higher dividends from equity-accounted investments due to the timing of payments from our China joint venture.

Working capital will reduce in the second half of the year due to seasonality and as we take proactive measures to align our working capital requirements with lower volumes. Interest payments totalling GBP49 million were GBP28 million higher than the previous period due to the annualization of the post-demerger capital structure. Therefore, interest payments for the full year are expected to be in the range of GBP80 million to GBP90 million, in line with previous guidance.

Capital expenditure of GBP103 million was GBP19 million lower than prior year as it was adjusted to align with lower volume and did not include any material capital expenditure on new production facilities associated with our footprint restructuring initiatives.

Restructuring cash flows of GBP51 million related to continued performance improvements were higher than previous period and in 2024 are now expected to be in the range of GBP105 million to GBP115 million, higher than the previously communicated range of GBP90 million to GBP100 million, largely due to further restructuring initiatives resulting from lower volumes.

We ended the half with a leverage ratio of 1.6 times higher than in December 2023 and outside our target range of 1 times to 1.5 times due to lower EBITDA and higher net debt. However, we expect this to be temporary and to be back within our target range in the medium term.

In our last trading update in May, we indicated that we expect a sequential improvement in the second half of the year. However, at the group level, we're now seeing slower-than-expected growth and we no longer anticipate that H2 revenue will be better than H1, primarily due to weakening market conditions.

As a business, we are facing three key headwinds. Firstly, weaker volumes. In May, when we issued our guidance, industry forecast expected a flat global light vehicle production. Since then, S&P has downgraded its forecast twice. Secondly, BEV volatility. Volatility in certain battery electric vehicle platforms is expected to continue impacting our ePowertrain product line in the second half.

And lastly, adverse customer mix. We anticipate that an adverse customer mix will impact performance for the remainder of the year, especially in North America and across our BEV platforms. At the group level, this means that we now expect full year revenues to decline mid-to high single digit.

As we continue to execute actions to limit the impact of lower revenues to operating profit, such as commercial recoveries, restructuring savings and ongoing performance initiatives, we expect constant currency operating margin to be between 6% and 7%. Adjusted free cash flow will be lower than the prior year due to reduced volume and higher restructuring costs. We have also included our usual guidance slide to help you with the modelling.

If you have any questions on this or other modelling matters, please speak to me or Pier. Thank you, and I will now hand it back to Liam.

<u>Business Performance</u>

Liam Butterworth, Chief Executive Officer

Thanks, Roberto. I'll now talk you through more detail about our businesses but first, I wanted to provide a quick update on the overall market. Let me start by briefly discussing global light vehicle market. After a strong growth in 2023, global light vehicle production declined by 0.2% year over year in the first half of 2024. However, most of this growth was driven by China, where- where production grew by 5.1%.

Excluding China, it was down by 2.4%, mostly driven by softness in EMEA and Asia. For the full year of 2024, S&P is now projecting a 2% year-over-year decline or 2.9% decline, excluding China, indicating continued market pressure.

Looking ahead, there are reasons to be optimistic. S&P projects that production will reach approximately 94 million units by 2026, indicates a compound annual growth rate of nearly 3% over the next two years, with strong growth expected in both China and North America. We've seen significant volatility impacting BEVs in both the short and long term.

In the short term, there was a notable slowdown in the ramp-up of EVs in the first half, making it challenging for auto manufacturers to plan and commit to long-term investments. In the first half of the year, battery electric vehicle production increased by 2%, but this growth was entirely driven by

China. BEV production, excluding China, declined by 9%.

Longer term, the adoption of BEVs has consistently been pushed out. And according to the most recent S&P forecast, BEV penetration is now expected to be 34% by 2029 compared to 40% at the beginning of the year. Other industry forecasts put BEV penetration as low as 30% in 2029. So therefore, it now seems likely that the EV transition is going to take much longer and will be much more complex than previously expected, with ICE and hybrid platforms likely to play a much bigger and longer role.

Let's move now to our two market-leading businesses, starting with automotive. To enhance our disclosure and provide more clarity on the different moving parts within our segments, we decided to give more details on the different product lines within the automotive business. Driveline representing almost 60% of revenues is the core of the automotive business and includes side shafts and prop shafts. ePowertrain, which includes all-wheel-drive systems, ePowertrain components and eDrive systems represents almost 26% of our revenue.

And finally, the equity-accounted portion for our long-established JV in China represents about 13% of revenues. Despite market volatility, more than 70% of the automotive business has outperformed the market in the first half of '24. Therefore, demonstrating its resilience to propulsion mix.

In driveline, we are the global market leader with a long history of engineering excellence. We entered the automotive industry in 1950 and invented the automotive constant velocity joint in the 1960s, when front-wheel drive vehicles were first introduced. We have the largest portfolio in the industry with a vast range of joint sizes and types, and the sheer scale of our business allows us to be competitive and produce our products with the same quality and delivery standards all over the world, close to our customers.

We are the number one globally in sideshafts for both ICE and BEVs where we're nearly twice the size of our nearest competitor. We are also number one globally in propshafts, again, significantly ahead of others. We also work with 90% of the global OEMs across the Americas, Europe, and Asia Pacific. So this means our revenue is highly diversified. No single customer represents more than 15% of sales.

And additionally, we're extremely well-distributed across our customers' vehicle platforms, meaning that we are never dependent on the performance of one individual program. We have a clear strategy for both of our product groups in Driveline. The side shaft business is the jewel in our crown. In H1, sideshaft revenue performed in line with the market as its propulsion-agnostic revenue profile demonstrated its resilience despite market volatility.

Our strategy remains to continue to invest and grow. And given our market leadership, scale and relationship with customers, we are extremely well-positioned to grow in line with or slightly ahead of market. As for propshafts, we intend to maximize utilization of existing assets to benefit from the longer and slower decline of ICE platforms. Our strategy is simple. We are well-positioned to maximize cash generation and profitability, given the limited investments in R&D required.

Moving on to ePowertrain. The ePowertrain portfolio is made up of three product groups, all-wheel-drive systems, where we are the market leader in all-wheel-drive systems supplying mainly large pickup trucks and large SUVs in North America and Southeast Asia, where we have the full capability to design, engineer, manufacture, optimize, package and integrate a complete all-wheel-drive system in-house.

ePowertrain components, we are the market leader in advanced torque management products, a technology developed and built on our legacy and expertise in all-wheel drive. Both product groups make our portfolio of propulsion-agnostic as most components within an all-wheel-drive system transition to ePowertrain components as BEV penetration increases.

And the eDrive system, we've been a pioneer in eDrive market for over 20 years, building our expertise in all-wheel drive. We've designed over 2,000 subcomponents and our 600 active patents with 800 engineers across 10 sites.

While our driveline business is well diversified across a broad range of customers, geographies and platforms, the ePowertrain product line is more exposed to platform and customer mix. It has a significantly higher content per vehicle, making it more prone to volatility and exposed to the commercial success of specific vehicle platforms.

In H1, 80% of the overall revenue decline was driven by only four platforms, three of which have been eDrive systems and were impacted by BEV volatility and one of which being an all-wheel-drive system, which was related to the timing of a new ramp-up of the new launch. Excluding these four platforms, the ePowertrain product line declined by 4.7% compared to a market decline of 2.4%.

Like Driveline, we have a clear, focused strategy to maximize value from the ePowertrain product portfolio. All-wheel-drive systems, we will manage our all-wheel-drive portfolio similar to propshafts, maximizing for cash and profitability. Our all-wheel-drive system products are on long-lasting ICE platforms in North America and Southeast Asia, where the ICE decline is forecasted to be much slower than the market, benefiting us in the near to medium term.

ePowertrain components, we will continue to invest and grow our ePowertrain components portfolio. These are high-value products, typically on high-end platforms and our heritage and technological capability position us well to increase market share. I expect the demand for our advanced torque management systems to increase on BEV platforms as customers will increasingly demand better handling of the vehicle to match the driving experience of high-performing ICE platforms.

eDrive systems, as previously stated, we will be even more disciplined with our investments in eDrive systems. We will be very selectively investing in programs that deliver target profit margins, aligning our investment strategy and capital allocation with our ambition to transition to a powertrain-agnostic portfolio.

Moving on to China. Let me remind you of our strong position in the Chinese market. Our automotive JV with HASCO, which celebrated its 35th anniversary last September, continues to be extremely successful. We work with all the leading Chinese OEMs and are profitably growing our market share with many of them across our entire product portfolio.

As in other parts of our business in China, we are rigorous to our commercial strategy, prioritizing profitable growth over volume. Our Chinese JVs margins are already at target levels, reflecting our disciplined approach. Our strong positioning in China is evident in the successful execution of our commercial strategy aimed at growing market share with local OEMs.

Over the last three years, we've made significant progress. For instance, 40% of our H1 2024 China revenue came from local Chinese OEMs, up from 27% in 2021, all without compromising on margin. Our local order book has also continued to improve. In H1, our book-to-bill ratio was 1.5, which is a significant increase from 2022 levels.

While our Chinese plants continue to serve the local market, we are extremely well-positioned to leverage our long-standing relationships and support our Chinese OEM customers as they pursue global expansion plans. We've also made significant commercial progress in the broader GKN automotive sector. The business continued to expand its pipeline, securing contract awards worth GBP2.4 billion in forecast lifetime revenue, translating to a book-to-bill ratio of 1.2.

Notably, 52% of new business wins were related to EV programs, demonstrating our strong alignment with market trends. Our robust order book reflects products, customer and geographical diversity. While current market volatility has impacted this year's performance, the strong order book gives me a high level of confidence and the business is well positioned for the future.

To summarize our GKN automotive business, we are the market leader in driveline, all-wheel-drive and torque management systems. We will continue investing in our core market-leading driveline business while maintaining a disciplined investment approach in ePowertrain in order to maximize profitable growth opportunities and cash generation.

Our strategy and capital allocation is aligned with our ambition to transition to a powertrain-agnostic portfolio, and we remain committed to expanding our margins, and we have a clear line of sight to significantly increasing cash generation in 2026 as all of our restructuring initiatives related to our global footprint optimization come to an end in 2025.

Now let's move on to the Powder Metallurgy business, which comprises of three product lines, sinter metals, powder and additive manufacturing. Again, we are the market leaders in both sinter and powder segments. We leverage our world-class engineering expertise and globally diversified supply chain to supply a broad range of customers with parts that are lighter, stronger and more efficient. Our focus on Powder Metallurgy is centered on accelerating our transition to a more diversified portfolio.

To accelerate this transition, we've implemented a new leadership team and developed a clear commercial strategy, and I'm very pleased with the progress they've already made. The PM portfolio performed well in the first half with revenue growing ahead of market. Our body and chassis and EV portfolio, which includes propulsion-agnostic and EV products grew 3% year on year, more than offsetting the 1% decline in the engine and transmission portfolio comprised of ICE platforms.

Bookings in H1 were also strong with new contracts secured representing a peak annual revenue of GBP77 million, which is a 10% year-on-year increase. Notably, 53% of these new wins were from propulsion-agnostic product groups, confirming that new products are gaining commercial traction and the business' portfolio transition is well on track.

In summary, Powder Metallurgy has had a good start to the year, delivering revenue growth ahead of market and margin expansion. We've continued to make good progress to diversify the portfolio. And with the new leadership and commercial strategy in place, now is the right time to commence a strategic review of the business with the aim to maximize value creation for our shareholders.

So in summary, in a complex market environment, our market-leading driveline business, China JV and Powder Metallurgy, all outperformed their markets, while volatility in BEV production significantly impacted our ePowertrain business leading to a 5.1% revenue decline.

Despite these challenges, myself and the team have taken several decisive actions. Firstly, we've implemented a relentless focus on cost control, limiting the impact on operating profit and our proactive measures mitigated the margin decline to 30 basis points. Secondly, we have a comprehensive program of commercial recovery initiatives with our customers, which, together with the ongoing restructuring programs and performance initiatives, will limit the impact from lower revenues in the second half of the year.

Lastly, we are taking decisive actions to unlock value from our portfolio and today's announcement of a strategic review of Powder Metallurgy and the disposal of the hydrogen operations underscores our absolute commitment to unlocking value from our portfolio and delivering shareholder returns.

Our strategy and relentless focus on execution remain unchanged. We are the global leader in our core driveline side shaft business and have also market-leading position in prop shafts, all-wheel-drive and torque management positioning systems. We will continue to accelerate the transition to a powertrain-agnostic business model, which will better position us to navigate market volatility and deliver sustainable, profitable growth and cash generation in the medium term.

That's all from me. And we now can open the floor to questions. Thank you very much.

Questions and Answers

Vanessa Jeffriess, Jeffries

Just a question first on the order book mix. So in order book, you've given for order, obviously, hybrids have now doubled to 32% from 16%. Last time you disclosed BEV down to 21% from 33%. I'm just wondering how we think about 2026 margin target now with that mix shift?

Roberto Fioroni, Chief Financial Officer

Vanessa. I'm not sure we've given our order book by propulsion type. But I'll answer your question around the margin target. We're still very much committed in auto to double-digit margins. As you heard from Liam, our restructuring programs are on track, and those were meant to deliver -- those are going to deliver 2 percentage points of margin expansion on -- off '23 flat volumes.

So then, as we're not standing still, we're looking to see with, given the market volatility, if there's more that we need to do, but we're still very much committed to taking more within our control, and rely less on volume. But the summary is we're still very much committed to those double-digit target margins in the medium term.

Vanessa Jeffriess, Jeffries

Okay. And then just on Powder Met, obviously, Jean-Marc's been in the role for 6 months now. Are there any early learnings or any kind of thoughts on the strategy transition that you gave compared to last year?

Liam Butterworth, Chief Executive Officer

Vanessa, this is Liam. As I alluded to in my talk is we're very, very happy with Jean-Marc and he brought some excellent talent into the team as well. And a lot of the focus that Jean-Marc is doing is looking at the commercial strategy and the front end of the business in terms of how to accelerate growth. And as we've seen how the business has performed in the first half, a number of new products and new programs that were in the pipeline have really started to take off in the half, and we're very happy with that overall transition.

I was also in China with Jean-Marc about two weeks ago and Roberto looking at our China strategy and how we can also accelerate growth there with a lot of new exciting products really around electric braking systems, electric steering, where Powder Metallurgy technology is extremely relevant in terms of just the complexity of the mechanical systems, where sintering is very, very unique to that kind of application.

So we're extremely excited about the portfolio, the technology and the drive that Jean-Marc and his team are bringing into that business.

Vanessa Jeffriess, Jeffries

And then just because you just mentioned it, on China, obviously, orders are seeing pretty fantastic momentum there. I think a big improvement on last year. Is there anything specifically driving that?

Liam Butterworth, Chief Executive Officer

Roberto and I were over there a few weeks ago, and we have an outstanding relationship with our JV partner HASCO, we've been with them for 35 years.

And it's all about making sure that we're aligned with them in terms of which are the key customers we want to focus on and how are we going to get set up to support them, that's having the right engineering and commercial support close to those customers where they're designing the new platforms, making sure we've got the right cost structure and focus in terms of the portfolio of product that we need for the Chinese OEMs and being very, very focused on in terms of the margin targets and expectations.

And you can see that, that mix of Chinese versus global OEMs has really started to transition in the first half of this year, and we're very, very aligned with our JV partner, how we want that to move going forward and as well as supporting those OEMs as they put capacity outside of China.

Harry Philips, Peel Hunt

It's Harry Philips with Peel Hunt. Three questions, inevitably, I'm afraid. Just in terms of the four particular programs and how they're going to perform ongoing, I mean just trying to do crude math, it looks like the four have suffered a volume drop of about GBP140 million, which obviously is pretty substantial. Just, can you give an idea of how that sort of plays out over the next couple of years in terms of potential recovery? And are those programs centered in particular facilities, so you've got sort of considerable underutilization of particular plants?

The second one is just on the phasing of the restructuring. Obviously, you got the 200 basis points in auto and what have you, but just how -- is there any change as to how that sort of plays out in current volume environment?

And then lastly, just one of the downsides for you guys, and having more time to read the statement, just looking at the cash flow, you're saying the JV sort of outflow is GBP53 million and the joint venture dividend is GBP70 million, both seem quite big numbers and obviously interest in seeing the dividend being bigger than the outflow, so some explanation around that would be very helpful.

Liam Butterworth, Chief Executive Officer

Harry, this is Liam. Let me kick off with the BEV platform challenge. I think in four platforms, three of which are BEV-specific platforms and one is a transition -- it's a brand-new all-wheel-drive portfolio, very high content in North America that's going through -- our OEM customers going through a changeover, that changeover has been much more challenging for that OEM than they forecasted.

But that's now ramping up, and we're seeing the volumes coming through for the second half. On the three BEV platforms, they're primarily impacted by, I would say, the chaos that we're seeing in Europe with regards to the BEV transition and the stop-start nature of subsidies and the changing dynamics that we're seeing across different countries and different OEMs in terms of their overall BEV strategy.

We've seen significant volume drops in the first half of three BEV platforms. We're not foreseeing that those volumes will come back. We're having very robust commercial discussions with the associated customers as a result of those platforms. Those platforms are across a couple of manufacturing facilities.

And as you can imagine, my operational team are taking extreme measures to make sure that we mitigate any impacts or, as much as we can, the impacts associated with the lower volumes on those BEV platforms.

Roberto Fioroni, Chief Financial Officer

So let's talk about the 200 basis points, first of all. Our auto restructuring programs, as I mentioned earlier, are very much on track and on budget. And we said that those 200 basis points we're going to be -- the timeline around those or the phasing would be one-fourth this year, half next year and one-fourth in 2026. We're still very much committed to that.

As I alluded to, answering Vanessa's earlier question, we are also looking to see if there's more we can take into our own control in terms of achieving that double-digit target margin and being less reliant on volumes. And then in regards to the cash flow question, I just want to remind everyone that on the adjusted EBITDA perspective, it includes consolidating China.

I think that's what you're referring to in terms of GBP53 million in the cash flow. So we remove the China EBITDA to get to a, let me call it, cash EBITDA number. That's just an adjustment essentially. And then the GBP70 million dividends that we got from [SDS] takes you back to more equity accounting practices, I would say, but that's the inflow.

And again, the dividend policy in China has always been, at least since I've been in the auto team for over five years, to distribute 100% of retained earnings. There's a bit of withholding tax for us to repatriate that cash. But that equated to GBP70 million, which is last year's essentially earnings being distributed. Now what happened this year, and I think you alluded to that, is we got the full dividend paid in the first half.

Typically, it's split equally 50-50 first half to second half. But that was an agreement with both HASCO and ourselves, so the two JV partners. I got a bit technical, but I hope it answered your question, Harry.

Arya Ghassemieh, Barclays

The first one, I was wondering if you could maybe provide a bit more color on ePowertrain and how you're currently thinking that might develop into H2 and 2025 at this stage. I think you said to one of the earlier questions, you don't foresee the volumes on those four platforms, which impacted you in H1. You don't foresee those volumes recovering into H2, but do you have any new key programs coming online in the second half and '25 to provide additional volume momentum? That's the first question.

And then secondly, could you maybe provide a bit more color on the key drivers for the sequential improvement in EBIT into H2?

Liam Butterworth, Chief Executive Officer

It's Liam. I'll talk about the ePowertrain side of things, and then Roberto can talk about your second question on margins. As we look out for the rest of the year, as I said, we are assuming that those volumes won't come back on those ePowertrain programs. But as we've seen the volatility in the EV transition is something I've never seen before in my entire career in terms of the stop-start that we're seeing with the customer build rates and incentives as OEMs wrestle to put more EVs or not into the market.

We've assumed that it will remain at the current level for the rest of the year. As I look out to next year, we're still in the early stages of looking at our planning for 2025, what I can say is we've got another one new eDrive program that's starting to ramp up at the end of this year.

And also, we've got an all-wheel-drive program that is one of the programs that has been delayed in terms of the start of production this year. That will continue to ramp next year, and we'll be at full volume with that program next year in North America. And we also see a number of our all-wheel-drive platforms continuing to be or extended throughout the period.

So it's a bit early to say what we think next year will look like. But I would say that relatively flat, if not some slight growth in our ePowertrain business next year.

Roberto Fioroni, Chief Financial Officer

And Arya, from a profitability perspective, H1 to H2 sequential, I guess there's one headwind, which is aligned with the industry, which is volume, and then the tailwinds come from commercial recoveries, hydrogen coming out of the numbers and then restructuring savings. Those are the three key categories that drive the improvement in H2, versus H1.

Akshat Kacker, JPMorgan

Two left from me, please. The first one on eDrive systems. Are you still quoting for new orders on systems? And how should we think about specific R&D expenditure on assembly and integration to evolve going forward, please? That's the first one. And the second one, coming back on China. The book-to-bill has clearly improved in the last 18 months. Could you just lay out any key success factors, any products or OEMs that are being very successful in the last few months there?

Liam Butterworth, Chief Executive Officer

I'll take both of those questions, Roberto, you can complement. So let me talk about eDrive systems to start with. So the eDrive system market has significantly evolved, I would say, over the last couple of years. And I think there's two fundamental changes that we've seen. One is, it's clear that the OEMs are doing a significant portion of those systems in-house themselves as they want to vertically integrate and control the cost structure of the BEV platforms.

And the second one is the number of eDrive systems that are coming out on to the market, the competitive intensity makes absolutely no commercial sense for me to allocate and dedicate an engineering resource to pursuing those programs because it's the race to zero in my opinion. So we are being incredibly selective where we will pursue an eDrive program if it meets our financial criteria, which should generate returns and free cash flow for the company.

What does that mean for us going forward as a business? It means that Roberto and I and the auto team are looking very closely at our eDrive engineering resources, how much we're investing, and is that the right amount we need for the future. And that process is underway as we speak. The second piece of your question -- part of your question was around China.

And key success factors is our China business is China for China. One of the things that I did with Roberto over the last couple of years is we pulled -- we removed any expats that were over there, and we've put a Chinese team in working closely with the JV. And as I said, we have a very, very long, very aligned relationship with our JV partner.

And the success is to make sure that we give our Chinese operating team the freedom to operate in the local market with local specifications, local commercial agreements, dealing with the local OEMs and having the right individual relationships and engineering and commercial teams where it's appropriate and just making sure that we make sure that with our JV partner, the boundaries around that relationship remain very, very firm in terms of what we expect.

And as we go over there, I was over there a couple of weeks ago, it's just making sure that the boundary is still in place, and we're happy with how things are progressing. And again, it's been also very focused on five or six local domestic Chinese OEMs that we believe value our technology and will be successful as they start to export out of the Chinese market and grow in international markets. And that's our strategy is to be focused on those five or six OEMs.

Operator

There are no further questions on the webinar. I will now hand over to Pier to moderate written questions submitted via the webcast page.

Pier Falcione, Investor Relations

Yes, I have a few questions. So the first one is from Mark Fielding from RBC. He's asking to talk about the path to the auto 10% margin target and the timeline and what volume recovery from now lower levels are needed together with the 200 basis points of self-help.

Roberto Fioroni, Chief Financial Officer

Mark, I'll tackle this one again. So we had previously said that off prior year revenues in auto, so about GBP4.3 billion, we could get 2 percentage points of margin expansion just by restructuring programs. And the last 1% needed to come from revenue growth, which was -- you can do the math, but we flow volume at 30%, right? That's our targeted operational leverage. That equation hasn't significantly changed.

So we're still very much focused on executing the already announced and ongoing restructuring programs that will drive 200 basis points and then this volume needed. Now what we are looking at and as I hinted, answering a couple of other questions this morning, is how do we bring more of that within our control. And again, nothing has been identified or kicked off just yet, but we are looking at options to take more of that journey within our control.

Pier Falcione, Investor Relations

Next is from William from BNP. For the Powder Metallurgy strategic review, what options are you considering alongside the potential sales? And if you did elect to sell the business, do you have an idea of the size of the offers you would entertain?

Roberto Fioroni, Chief Financial Officer

So I'm not going to discuss valuation or timing. We'll update the audience as relevant. In terms of other strategic options, it's part of the execution of the transition from ICE to BEV. So as -- just to name a few examples, you know that we've been looking in magnets. Is there an opportunity to partner with someone on magnets? We are looking at the whole strategic portfolio.

As Liam said, in the last 18 months or so, we've gotten the opportunity to really get into the details of the business. And most recently, with Jean-Marc and his team, we've developed what we've aligned on what is an exciting strategic plan for the transition. And now we're just going to look at strategic options to execute and accelerate the execution of that plan.

Pier Falcione, Investor Relations

Next one is from PY from Stifel. Interim dividend was flat. How should we think about full year? Would it be maintained flat for the full year as well?

Roberto Fioroni, Chief Financial Officer

PY, you asked me this earlier this morning as well, I think. I'll say for now is the Board approved the interim dividend, as you rightly pointed out, flat 1.4p per share. We will have a discussion with the Board later in the year to see what the full year dividend is. Our capital allocation policy, is 25% to 35% of adjusted net income. That will be a Board discussion later in the year.

Pier Falcione, Investor Relations

Next one is from Michael from Bank of America. Are you comfortable that existing contract structures with OEMs are providing adequate compensation for significant volume mixes? And going forward for new model and platform launches, particularly for BEVs, and thoughts on linking pricing more directly to actual volume levels, i.e., exiting scale approach?

Liam Butterworth, Chief Executive Officer

So we have an extremely strong commercial team in the automotive business as we do in Powder Metallurgy. And that commercial team has shown its ability to perform as we've seen over the last several years in terms of COVID, supply chain disruption and specifically inflation, where we have a very disciplined approach to how we enter into contracts with customers and how we enforce those contracts, whether that be volume-related discussions or commodity related and steel, energy, labor, et cetera.

Nothing has changed in terms of how we contract with our customers, and we will continue to make sure that we've got all the right volume clauses in place, and we are having discussions with customers at the moment regarding the shortfall on volumes on some of those BEV platforms, which are -- we have contractual volumes in the agreements with them.

Elaborating a little bit further about our Chinese business. That commercial rigor and discipline also remains in place with our China team. So we make sure that whenever we enter into a contract with a customer, it's entered into on a fair agreement with -- between ourselves and the customer in terms of what are the volume expectations, what we have capacity for, how much are we investing and what are the commodity indexation clauses that we have in those contracts. That's in place today and will remain in place as we go forward in the future.

Pier Falcione, Investor Relations

Next one is from David Larkam from Edison. Powder Metallurgy sales seems to have slowed later in the half, given the growth reported in the previous update. Is there anything to note? Also, do you have any time scale on the review of the business or the strategic review of the business?

Roberto Fioroni, Chief Financial Officer

David, I would say, just like for the first half result, Powder Met has pretty much performed in line and of course, largely outperformed market and market has slowed in the last two months of the half as well since our trading update. You're right, there was a bit of a slowdown, but it's trended with industry. And in terms of the -- sorry, the second question? In terms of the sale, as I said earlier, I'm not going to comment on the time frame, we'll update the audience as and when relevant.

Pier Falcione, Investor Relations

Okay. Couple of more question. If there were to be cash proceeds from the strategic review of Powder Metallurgy, how would you use those proceeds? And then separately, how do you think about restructuring costs in 2025?

Roberto Fioroni, Chief Financial Officer

Okay. So if and when there should be a sale of Powder Metallurgy, we have a capital allocation policy that is very focused on returning value to the shareholders. There will be a discussion with the Board. And there's a lot of variables that go into that conversation. So more to come as the process continues. And then in regards to restructuring for next year, I don't really want to get into 2025 conversation just yet, considering the volatility and the uncertainty that is in the industry. We'll pick that up later in the year, if you don't mind.

Pier Falcione, Investor Relations

And the last question, for you Roberto. Does the full-year guidance includes the hydrogen business that was sold?

Roberto Fioroni, Chief Financial Officer

Yes. In the step-up required to achieve the full year guidance, if you pick the midpoint, there are really three key actions driving it. One is the commercial recoveries. Second is to continue seeing the restructuring benefits flow through and then there's the hydrogen, we had GBP7 million losses in H1 that are not going to recur in H2.

Pier Falcione, Investor Relations

Okay. That was the last question. Liam, if you have any final closing remarks?

Liam Butterworth, Chief Executive Officer

No, I think we've covered everything on the call today. I just want to thank everybody for taking your time to join us this morning and look forward to seeing many of you in person over the coming weeks. Thank you very much.

Roberto Fioroni, Chief Financial Officer

Thank you all.