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Earnings Call

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Stefan Neely

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Presentation

Operator

Thank you all for joining. I'd like to welcome you all to the Mayville Engineering Company Third Quarter 2023 Earnings Call. My name is Brica, and I will be the moderator for today's call. [Operator Instructions] I would now like to pass the conference over to your host, Stefan Neely, to begin. So, Stefan, please go ahead.

Stefan Neely

Thank you, operator. On behalf of our entire team, I'd like to welcome you to our third quarter 2023 results conference call. Leading the call today is MEC's President and CEO, Jag Reddy; and Todd Butz, Chief Financial Officer.

Today's discussion contains forward-looking statements about future business and financial expectations. Actual results may differ significantly from those projected in today's forward-looking statements due to various risks and uncertainties, including the risks described in our periodic reports filed with the Securities and Exchange Commission.

Except as required by law, we undertake no obligation to update our forward-looking statements. Further, this call will include the discussion of certain non-GAAP financial measures. Reconciliation of these measures to the closest GAAP financial measure is included in our quarterly earnings press release, which is available at mecinc.com. Following our prepared remarks, we will open the line for questions.

With that, I would like to turn the call over to Jag.

Jagadeesh A. Reddy
President, CEO & Director

Thank you, Stefan, and welcome to those joining us on the call and webcast. As anticipated, our third quarter results demonstrated significant year-over-year growth in revenues, adjusted EBITDA and free cash flow. These strong results were the product of continued steady end market demand and targeted market share gains, particularly in our commercial vehicle, military and powersports markets.

Early in the third quarter, we closed on the acquisition of Mid-States Aluminum or MSA, which was also a contributor to our revenue and earnings growth in the third quarter. In addition to the cross-selling opportunities afforded by MSA's aluminum fabrication and extrusion capabilities, our core business continues to enjoy a robust sales pipeline entering 2024.

Even as we look forward into a potentially more muted environment for end market growth, we are optimistic about our ability to deliver above market growth through the cycle by expanding our share of wallet with our current customers and improving the utilization of our existing assets.

Importantly, our operational and commercial self-help initiatives are continuing to deliver improved profitability and cash generation through improved cost absorption, value-based pricing and enhanced working capital efficiency.

During the third quarter, we generated a record $16.1 million of free cash flow, representing cash conversion in excess of 80%, a new record for our business. Consistent with our capital allocation priorities, we reduced our outstanding borrowings by more than $17 million in the third quarter, while repurchasing $1 million worth of common equity, leaving $17 million under our existing $25 million authorization as of September 30.

This year alone, we have repurchased $2 million worth of shares under our existing authorization. In September, we hosted our inaugural Investor Day event at our Hazel Park facility outside of Metro Detroit. At the event, we introduced a 3-year road map for MEC, one that leverages the key pillars of our MBX framework to drive long-term value creation for our shareholders.

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At the event, we underscored how we intend to drive organic sales growth, adjusted EBITDA margin and improve free cash flow generation while continuing to develop a leading manufacturing platform of scale within key growth markets such as energy transition. As a team, we are committed to excellence through accountability and introduced new 3-year financial targets at the event, which our entire team is focused on achieving.

By the year-end 2026, we expect to deliver between $105 million and $135 million of annual adjusted EBITDA, along with annual net sales between $750 million and $850 million, adjusted EBITDA margins between 14% to 16% and annual free cash flow generation of $65 million to $75 million. While these are ambitious targets, they are entirely achievable.

Our third quarter results demonstrate early progress towards this plan. We remain focused on delivering ratable, consistent growth into 2024, building upon our track record of execution. While we are very pleased with our third quarter performance, it is important to highlight that these results include continued cost under absorption associated with planned ramp-ups at our Hazel Park and Atkins facilities.

Fixed costs under absorption at Hazel Park alone impacted the third quarter adjusted EBITDA and adjusted EBITDA margin by $1.7 million and 110 basis points, respectively. Excluding the impact of the Hazel Park ramp-up, our normalized adjusted EBITDA was 13.2%.

We continue to expect that Hazel Park will ramp up fully by the end of 2024, contributing $100 million in annual revenues with adjusted EBITDA margins of approximately 15% in 2025. As of September 30, we currently had commitment for all but approximately $25 million of the projected $100 million in annual revenue contribution of that facility.

Turning now to a view of market conditions across our 5 primary end markets. Let's begin with commercial vehicle market, which represents approximately 40% of our trailing 12-month revenues.

During the third quarter, commercial vehicle revenue increased 6.6% on a year-over-year basis driven by strong demand and elevated build rates. Customer demand requirements continue to indicate slowing demand going into the end of the year and into 2024, as the industry navigates regulatory changes as well as a general slowing in economic activity.

Currently, ACT Research forecasts the Class 8 vehicle production to increase 6.6% year-over-year in 2023 to 336,000 units. The current projection indicates that build rates will slow during the fourth quarter and decline by nearly 4% on a year-over-year basis.

For 2024, ACT projections reflect a deeper softening in demand to the middle of the year with current production estimates reflecting an 18.5% decline for the full year 2024. Furthermore, we are currently experiencing volume disruptions associated with the United Auto Workers strike with one of our customers. This has impacted our volumes for their products so far during the fourth quarter, and will continue to do so until an agreement is reached.

Next is the construction and access market, which represented approximately 18% of our trailing 12-month revenues. Construction and access revenue declined 2.3% on a year-over-year basis in the third quarter, given weaker fundamentals within the residential housing market, which continues to be impacted by the elevated interest rate environment. While residential construction trends appear to have troughed and infrastructure and energy market demand remained stable, we still expect to see demand softness year-over-year through the remainder of 2023 and into 2024 with the potential for modest improvement later in 2024.

The powersports market represented approximately 16% of our trailing 12-month revenues and increased by 7.7% on a year-over-year basis in the third quarter. We continue to benefit from market share gains, which include new customer programs, which were partially offset by cooling in consumer discretionary spending.

Given current market conditions, we anticipate customers will seek to bolster demand through rebates and incentives going into the holiday season. As we look forward into 2024, indications are that continued slowing in demand would result in growth deceleration as dealer inventory levels have normalized. Our

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agriculture market represented approximately 10% of trailing 12-month revenues and increased 4.6% on a year-over-year basis during the third quarter. The increase during the quarter was primarily driven by growth in large ag demand, along with the contribution of MSA's ag-related sales, which offset continued overall softness in our legacy small ag market. This trend is in line with our expectations as global food stocks remain tight and crop prices remain elevated.

Given elevated crop prices, we believe producer demand will increase through the end of the year and into 2024 with some deceleration going into the middle of 2024. The demand tailwinds in large ag going into 2024 should mostly offset softness in small ag demand.

Our military market represented approximately 6% of trailing 12-month revenues and increased 70% on a year-over-year basis in the third quarter, driven by new program wins and bill rate increases. Our customers have solid contractual backlogs with the U.S. government, and we continue to see good volumes based on new vehicle introductions and related programs.

However, we foresee volume growth moderating during the fourth quarter and into 2024 due to the expected expiration of some legacy projects. I would also point out that with the completion of MSA acquisition during the quarter, the majority of MSA revenues are represented within our other end market category, which grew by over $12 million year-over-year in the third quarter.

The MSA acquisition closed on July 1. And since then, our teams have been hard at work with integration and cross-selling activities. Overall, the MSA integration is going well and we are on track to have them fully integrated by the end of the year, as expected.

Importantly, as we highlighted at our Investor Day, we see MSA generating over $100 million of sales by 2026 with at least $25 million coming from revenue synergies with legacy MEC customers. As of end of September, we are progressing as expected towards the target, as well as the expected cost synergies that we are targeting through the implementation of our MBX lean manufacturing framework at MSA.

Shifting now to an update on our MBX initiative. During the third quarter, we continued to progress in the implementation of our MBX value creation framework. I am pleased to report that we are on track to achieve the objectives we laid out last fall when we first announced the MBX framework.

As we highlighted at our Investor Day, MBX is rooted in organic commercial growth, improved cost absorption through lean manufacturing practices, value-based pricing and working capital efficiency. These key areas of self-help initiatives will allow us to create sustainable value and deliver above-market growth through the cycle.

Commercially, we are targeting growth in higher value, high-growth adjacent markets, including clean technologies and energy transition in addition to expanding our share of wallet among our current customer base. Achieving this goal is dependent on improved utilization of our equipment through better labor productivity as well as utilizing existing capacity at MSA and Hazel Park. Allow me to share some of the commercial milestones we achieved during the third quarter.

Starting out, we are pleased to report that we have been awarded purchase orders for our first cross-selling win after the acquisition of MSA. Our first award was in the commercial vehicle space, which was the largest market opportunity within our cross-selling targets. We have continued to build momentum in our core activity, and we expect to continue to win awards for the coming quarters.

During the third quarter, we continued the expansion of our customer relationship to supply battery thermal management products to multiple end customers as the EV transition continues to progress. This relationship will continue to expand as our customer grows their electric vehicle battery systems while we also are starting to work on significant outsourcing programs with this customer.

In the quarter, we further expanded a new customer relationship in the powersports market with new program wins on new products. We expect to see continued significant growth with this new customer relationship as we look ahead into 2024.

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We also made progress on securing additional market share within our large ag and construction customer. These new parts were related to next-generation products and continue to build momentum on winning new business with the capacity we have installed in Hazel Park. We have continued to gain additional market share as our commercial vehicle customers plan for their vehicle updates, both on next-generation products and battery electric vehicle platforms.

We expect to continue to grow share over the next 2 years with the amount of change that will occur in this industry. As we highlighted during our Investor Day, our 2026 net sales targets are dependent on capturing incremental customer commitments of $65 million to $125 million, including MSA cross-selling synergies.

Based on our current level of sales activity and recent wins, we remain confident that this is achievable. The other pillar of MBX is commercial excellence, where our focus is to implement strategic and value-based pricing models across our customer programs. Year-to-date, the teams have been working tirelessly to implement a programmatic pricing model.

On the operational excellence front, we have continued our rigorous implementation approach centered around our quarterly President's Kaizen, supplemented by monthly operational and commercial excellence Kaizens.

During the third quarter, we completed 25 Kaizens with a focus on sustainability of cost savings measures identified. Overall, our team has performed over 100 MBX lean events through the end of the third quarter. These savings put us on track to achieve the 40 to 70 basis points of margin improvement reflected in our 2023 guidance, as well as the 100 to 150 basis points of margin improvement we expect to achieve by 2026.

Given the current demand environment, the execution we have achieved with our MBX initiatives and the ongoing ramp-up of new program launches, we continue to expect consistent margin performance and free cash flow conversion to close off the year.

Looking ahead to 2024, we anticipate some modest softening across our end markets given broader expectations for a general slowing in the U.S. economic growth next year. However, we anticipate ongoing operational and commercial growth initiatives will position us to deliver above-market growth.

Our ability to deliver above-market growth into 2024 depends in part on driving improved asset optimization across our system, continued price discipline and sustained cost management, all of which were on pace to deliver. 2024 will be a year of ratable progress for us, one where we expect to begin to fully realize the benefits of MBX initiatives, which are expected to support sustained organic growth, margin expansion and improved working capital efficiency.

As before, we intend to prioritize cash generation towards the aggressive reduction in outstanding borrowings, putting us on pace to achieve a net leverage ratio between 1.5x and 2.0x by the end of 2024. Since the announcement of the MSA acquisition, we have received numerous indications of interest from potential acquisition candidates, many of which fit nicely within our acquisition criteria for lightweight materials and high-growth end market exposure.

While we will continue to build a solid funnel of high-quality acquisition candidates, our chief focus over the near term will be on using net leverage to ensure continued balance sheet optionality through the cycle.

In summary, as I have highlighted today, we delivered on several important strategic growth milestones during the third quarter, all of which play a role in building a leading integrated solutions platform equipped to take share in higher-value, underserved growth markets.

As a team, we remain highly focused on delivering a high say/do ratio, one where a continued focus on program execution is at the center of all we do. Collectively, we remain focused on delivering a superior return on invested capital, whether through organic investments, acquisitions or the repurchase of our own common equity.

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As we look to the coming year, we will continue to hone and refine our approach to capital allocation as we seek to maximize value for all of our shareholders. With that, I will now turn the call over to Todd to review our financial results.

Todd M. Butz
CFO, Secretary & Treasurer

Thank you, Jag. I'll begin my prepared remarks with an overview of our third quarter financial performance, followed by an update on our balance sheet and liquidity.

Total sales for the third quarter increased 16.1% and a year-over-year basis to $158.2 million, driven by a combination of the MSA acquisition and improved organic sales volumes, partially offset by softening demand in our construction and agricultural end markets.

When excluding the MSA acquisition, organic net sales growth was 6.2% on a year-over-year basis. Our manufacturing margin was $19 million in the third quarter as compared to $15.5 million in the same prior year period. The increase was primarily driven by increased organic volumes, MBX initiatives and the acquisition of MSA, offset by unabsorbed fixed costs associated with new project launches and an $891,000 negative impact from the inventory valuation step-up associated with MSA.

Our manufacturing margin rate was 12% for the third quarter of 2023 as compared to 11.3% from the prior year period or an increase of 70 basis points. When excluding the impact of the unabsorbed fixed costs and the inventory adjustment, our manufacturing margin would have been 13.7% or an increase of 240 basis points as compared to the prior year period.

Profit sharing, bonus and deferred compensation expenses increased by $2.2 million to $2.3 million for the third quarter of 2023, which was driven by the lower stock-based compensation expense in the prior year period due to forfeitures of unvested awards.

Other selling, general and administrative expenses were $8.6 million for the third quarter of 2023 as compared to $6.5 million for the same prior year period. The increase was driven by $1 million of legal expenses relating to our former fitness customer, $500,000 of transaction costs associated with the MSA acquisition and increased salaries, wages and benefits.

As we highlighted at our Investor Day in September, we believe that SG&A expenses in the near term will be between 4.5% to 5.5% of net sales as our public company costs increased as we work through meeting SOC compliance requirements. In the longer term, we expect operating leverage will drive our SG&A down to between 4.5% and 5% of net sales by 2026.

Interest expense was $3.9 million for the third quarter of 2023 as compared to $830,000 in the prior year period due to higher interest rates and higher borrowings under our credit facility. The increases in borrowings is due to the acquisition of MSA, which closed on July 1, 2023.

Given our current net leverage, we are subject to a higher spread on our floating rate debt, combined with higher sulfur rates resulted in the elevated interest rate during the quarter. As we continue to pay down our debt, we expect that interest expense will continue to decline, not only due to lower borrowings, but also because of the step-down in our spread as a result of declining net leverage.

Adjusted EBITDA increased to $19.2 million versus $16.1 million for the same prior year period. Adjusted EBITDA margin percent increased by 30 basis points to 12.1% in the current quarter as compared to 11.8% for the same prior year period. The increase in our adjusted EBITDA margin was primarily due to increased organic volumes, MBX initiatives and the MSA acquisition, partially offset by $0.5 million of higher underabsorbed fixed costs at Hazel Park.

Adjusted EBITDA margin progression is evident and demonstrates early advancement towards our 2026 goal of 14% to 16%. Turning now to our statement of cash flows and balance sheet.

Free cash flow during the third quarter of 2023 was $16.1 million as compared to $5.2 million in the prior year period. As Jag mentioned, free cash flow generation for the quarter was the highest in any quarter since the IPO and represented a conversion rate of 84% of adjusted EBITDA. The improvement in free

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cash flow year-over-year was primarily due to the $8.9 million decrease in capital expenditures resulting from the completion of the Hazel Park facility and improved inventory turns as we continue to implement lean inventory management processes.

With the heavy capital investment cycle in 2022 behind us, we are focused on improving working capital, and we were able to generate strong free cash flow results that put us on pace to meet our second half of the year free cash flow goal of $25 million to $35 million and show a significant progress towards our 2026 free cash flow target of $65 million to $75 million.

As of the end of the third quarter of 2023, our net debt, which includes bank debt, financing agreements, finance lease obligations and cash and cash equivalents, was $169.6 million as compared to $74 million at the end of the third quarter of 2022, and resulted in a net leverage ratio of 2.46x as of September 30.

As we have stated previously, it's our intention to use free cash flow generation to reduce our net leverage ratio to between 1.5 and 2x by the end of 2024. And during the third quarter alone, we repaid approximately $17 million of borrowings using available free cash flow.

In light of our third quarter results and the outlook for the rest of the year, we are reiterating our financial guidance for the full year 2023. For the full year 2023, we continue to expect the following: net sales of between $580 million and $610 million, adjusted EBITDA of between $66 million and $71 million, capital expenditures of between $15 million and $20 million. Our current full year 2023 guidance does not include any impact from the ongoing strikes within the CV and auto industries.

Beginning in November, we estimate these strikes could negatively impact net sales by approximately $6 million to $7 million per month and adjusted EBITDA by $1 million to $2 million per month.
With that, operator, that concludes our prepared remarks. Please open the line for questions as we begin our question-and-answer session.

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Question and Answer

Operator

[Operator Instructions] We have the first question from Vlad Bystricky from Citigroup.

Vladimir Benjamin Bystricky
Citigroup Inc., Research Division

So thanks for all the information and the update today. Maybe just since you've given some initial thoughts on '24 here, any color on how we should be thinking about raw material pass-throughs impacting '24 just given where raws are today?

Jagadeesh A. Reddy
President, CEO & Director

Sure. I think a week ago, if Vlad walked into this call, I think on Friday, I would have said, hey, no change. We have stable steel prices, and we're expecting some price stability given that almost in the past year, right, now steel prices have stayed relatively calm.

But as markets have shown in the last few days, as steelmakers continue to curtail supply, we are seeing a bit of a spike in our steel prices. We don't expect that to last through 2024, but we are seeing a bit of a spike in the last -- in a week or so. We're expecting things to stabilize in 2024.

Todd M. Butz
CFO, Secretary & Treasurer

And Vlad, I would just comment that we wouldn't expect it to have the impact that it did in '21 and '22. Certainly, there's been a little bit of an uptick, but the fluctuation isn't as steep as in previously. So again, as we look into '24, we don't see that as a real large impact. But again, it's a pass-through, and we'll disclose it going forward each quarter.

Vladimir Benjamin Bystricky
Citigroup Inc., Research Division

And then just on the quarter and into year-end here. You talked about supply chain constraints still impacting some customers. So can you just talk about sort of how you'd characterize visibility from your OEM customers in the current environment? And if you're seeing changes in their order patterns or any increasing stability that could be helpful to your own manufacturing operations?

Jagadeesh A. Reddy
President, CEO & Director

Sure. I would say that in Q3, we did not see any significant customer supply chain disruption. So for us, it feels like things have calmed down. And we saw relatively normal order flow.

Coming into Q4, we are not expecting any significant changes on that front either. Having said that, probably the last sentence on Todd's -- in Todd's remarks, right, if you caught it, we have, obviously, exposure to some customers who are experiencing some UAW strike disruptions.

I would say that by -- through the end of October, our impact has been minimal. And auto exposure we have now, we can say that in rest of Q4, will be again minimal, given that the strikes have been -- at least looks like they're going to be settled.

Other CV customer that continues to be down because of the UAW strike, we're optimistic that given the conclusion of the other big 3 contract negotiations, that our CV customer could also wrap up their negotiations in the short term. But if that continues on, we expect some impact, as Todd mentioned in his prepared remarks, in Q4.

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Outside of those events, we do not expect any disruptions from any supply chain issues or otherwise going into 2024. We have not seen any indications of softness per se in orders or purchase orders or any of EDI feeds we normally see.

But the conversations have been a little muted from some of our customers, even though the order flows haven't changed, the demand picture hasn't changed. So given the discussions about macroeconomic conditions, high interest rates, consumer demands slowing with all of these, we're walking into 2024 on a cautious mode. As we mentioned, we continue to expect to perform our revenue growth to be above market growth next year, given our market share gains and new program wins and start up of multiple long-term programs in both Hazel Park, Atkins and other locations within the company.

Operator

We now have the next question comes from Mig Dobre of Baird.

Mircea Dobre
Robert W. Baird & Co. Incorporated, Research Division

I want to talk on the last point that you made there, Jag, about '24 and about your specific outgrowth drivers. Is there a way to update us or kind of quantify knowing what you know today in terms of business that you guys have booked or programs, incremental programs that you have booked as to what the revenue benefit in '24 relative to '23 would be from the business that you already kind of have visibility on?

Jagadeesh A. Reddy
President, CEO & Director

Yes, Mig, we were not in a position to provide any guidance on 2024 at this point. Having said that, we remain committed to the 3-year revenue, EBITDA and cash flow targets we laid out recently at our Investor Day.

We continue to expect progress towards the goals even with a perhaps muted 2024 growth picture. So we expect 2024 to be a growth year for MEC. We expect to grow above market next year, both top line and margin expansion and cash flow generation as well. So we're pretty optimistic about 2024, but we're not in a position to provide any particular guidance at this point.

Mircea Dobre
Robert W. Baird & Co. Incorporated, Research Division

Yes. Well -- and I appreciate that. And I wasn't necessarily wanting to pin you down on guidance for '24. It was more trying to understand, it's November, right? So you probably have a pretty decent idea in terms of the incremental programs that you have that you know will start flowing into '24 because your macro commentary is obviously more cautious than it was before. So I think we're all trying to figure out what MEC specifically can do to sort of offset this more difficult macro setup, if you would.

Jagadeesh A. Reddy
President, CEO & Director

Yes. No. Okay. So on Slide 5 in our deck that we put out this morning or last night, you can see that we're projecting most of our end markets to be either down or slightly flat. And we're projecting our powersports market to be up even though the market is going to be down, up significantly given our new program starts that we discussed multiple times in the last couple of quarters on our Investor Day.

Similarly, our commercial vehicles also, even the market may be down 18%, 18.5% is what ACT is projecting. That market is going to be down next year. We're expecting at least to be flat in 2024. Similarly, construction and access, we're 60-40, construction and access. That's how we break out our revenues. We expect access market to be pretty good going into 2024, given the customer comments that we heard in their public comments recently.

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Construction, residential construction obviously is down. But we have other programs that we're on, that gives us confidence that we will at least be -- as a second segment, we will at least be flat next year.

Similarly, ag, residential small ag is down. But large ag and then addition from MSA, ag demand -- sorry, revenues as well will continue to give us at least a flattish picture next year in our ag markets as well. And military is a small segment. We expect to be up, given some new program wins. So overall, that's why it gives us confidence that even though the end markets might be down next year, right, we will perform above our end market averages.

Mircea Dobre
Robert W. Baird & Co. Incorporated, Research Division

And sort of sticking with the Slide 5 and the way the mix -- the revenue mix is going to be evolving between these verticals. Is there any insight to be gained in terms of what that looks like from a margin standpoint? I mean like military, for instance, if it's growing quite a bit. Is that positive for margin or mix or not?

Jagadeesh A. Reddy
President, CEO & Director

It's, I would say, generally speaking, maybe slightly accretive when the mix change for next year, Mig.

Todd M. Butz
CFO, Secretary & Treasurer

And I would just add that generally speaking, our margin performance in each segment is very similar. Maybe within 1 or 2 points, it isn't like we're getting 35% margin in 1 market, 15% in another. So it's very similar across the board.

Mircea Dobre
Robert W. Baird & Co. Incorporated, Research Division

Okay. Understood. And last question, just a clarification around the UAW strike. So your guidance for the fourth quarter, does that assume any drag from the strike, like for instance, in the month of November or not, you're just sort of quantifying it, but it's not factored into the numbers yet?

Todd M. Butz
CFO, Secretary & Treasurer

It has not been factored into the guidance. In a normal course, we would expect to be within our original guidance. Now the strike, which we're optimistic and hopefully, they get settled here in the near term. If that is prolonged, that would most likely result in about $6 million to $7 million per month of lost sales and about $1 million to $2 million of EBITDA impact. Which again, has not been factored into our guidance.

Jagadeesh A. Reddy
President, CEO & Director

And just to reinforce the point that in October, even though most of the month of October, the customer was not taking -- or not running rather their production lines, we were able to offset our October volumes with aftermarket production, et cetera, that helped us continue to run our production lines in the month of October.

So if it gets settled in the next week or so, right, I think we'll be okay. But if it continues to drag on in the second and third weeks of November, then we will expect the impact as outlined by Todd.

Operator

Your next question comes from Ted Jackson of Northland Securities.

Edward Randolph Jackson
Northland Capital Markets, Research Division

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So just a couple of questions. The UAW one you just answered was one of them, but I got 2 more. When you -- first of all, when you talk about growth in 2024 that you're expecting to grow as a business, are you -- I'm a little confused, is that organic? Or is that growth -- are you talking about this growth, MSA, the whole combined thing, vis-a-vis, 2023?

I mean are we talking organic growth kind of ex-MSA acquisition or normalized for it? Is that what you're -- or are you saying -- you're just talking about the raw number?

Jagadeesh A. Reddy
President, CEO & Director

Yes. So it's a really good question, Ted. We're expecting organic growth in addition to the lapping of MSA first half revenues.

Edward Randolph Jackson
Northland Capital Markets, Research Division

I didn't want to assume that, but I did want to assume that. Then just a little more color, if you would, on the commercial vehicle market itself. I know the macro outlook you provided previously was '23, and now we're looking at '24. And I understand the dynamics with regards to the pull forward of demand as a result of all the regulatory changes for emissions.

You also have some new product wins within the commercial market itself. Can you provide some, I guess, some color with regards to what -- where you see that business going for you as you roll through '24? I mean you're saying you think you can keep it flat. I mean, so if I was to just take your commercial vehicle revenue for '23 and as a baseline worst case scenario, given what you know today, you'd see no growth in that. Would that -- is that kind of what you're saying with it?

And if you were to see growth on top of '23, is there something that would happen that would drive that? Is there something in your backlog or kind of your dialogue with customers and stuff that would make that a growth business for you? I mean it's your biggest vertical, so a little more maybe discussion around it might be worthwhile.

Jagadeesh A. Reddy
President, CEO & Director

Yes, that's a good question as well, Ted. As we said, or ACT said, the commercial vehicle volumes will be down 18.5% in 2024. That's our current expectations. Given our new program wins, including new tank production volume that's going to come online in Q1 of next year and the outsourcing win we talked about. And then other program wins, we expect to be flat in our commercial vehicle revenues next year. That's our current expectation.

Edward Randolph Jackson
Northland Capital Markets, Research Division

And then remind me, I mean, I've seen this before, but a long time ago. It's not like this is the first time that we've had this kind of scenario within commercial vehicles where regulations change and you get a lot of forward buying. It happens every time that this kind of -- every time the rates change. How long does it usually take for the market to kind of go back to normalized? I mean is it like a phenomenon then all else being equal, let's ignore the macro, the economy and whatever, and that we get through '24 and then we get back to kind of like a base market growth rate. How much for -- how much demand gets pulled forward when the government makes those changes typically?

Jagadeesh A. Reddy
President, CEO & Director

Yes. I would say that typically, it's about a year when the markets sort of go down and then curve back to normal levels. We're expecting, obviously, right, 2024 to be the down year. Even looking at quarter-by-quarter, we expect the softness to sort of hit mid-year and second half to be a little lower than first half of next year. And then 2025, the volumes are expected to come back up to normalized levels. So I don't

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think we have a number from ACT yet. But our expectation is going to be somewhere north of 300,000 in 2025.

Actually, I do have a number from ACT. The numbers are in 2025 are expected to be around 316,000 units. 2022 was 316,000. 2023 is the 336,000, and 2024 is the 274,000, right? So you can see that dip. So there was a pull-in 2023, pulled back in 2024 and then back to a normalized level of 316,000 in 2025.

Operator

[Operator Instructions] We now have Tim Moore of EF Hutton.

Timothy M. Moore
EF Hutton, Research Division

Thanks for the Investor Day goals and those incredible bridges for your road map for EBITDA margin expansion and free cash flow. I just had a hypothetical question to start out here. Regarding the Auto Worker strikes, and if something like this occurs next year for a different end market or even a large customer disruption, then maybe there's a mild recession in the spring or something, how much flexibility do you have to maybe shift some of the capacity or installed work to other end markets to backfill that in and cut overtime costs? Because I think you might have said on Investor Day about 20% overtime mix, but maybe you could flex it to 10%?

Jagadeesh A. Reddy
President, CEO & Director

Yes. Great question, Tim. Yes, we were averaging approximately 20%-ish of overtime in many of our plants. Our long-term goal, our target is to be around 15% or so flex time or overtime rather, right? So immediately, we can shut off overtime. And also, we have the flexibility to freeze hiring.

We still have about 100 job openings across the company as we speak today, and we can quickly freeze some of those hiring plans. But also, we have the flexibility to switch our operations from producing from one end market to another end market, given that majority of our plants, in fact, outside of 2 plants or a majority of our plant, 18-plus plants, we can make parts for any end market. So that gives us the flexibility to quickly switch our customer focus or end market utilization of those assets. So those are the levers we have.

And we -- no one expects any black swan events or anything like that in the near term, at least we don't know. But if something like that happens, we have the ability to quickly switch gears and shift our focus.

Timothy M. Moore
EF Hutton, Research Division

Great, Jag. That's good contingency planning. And nice to hear, a lot of companies actually can't do that, but --or as easily. What about Jag, now that you mentioned your Kaizen, and spend time on all your plants to implement MBX, how would you kind of quantify maybe what inning your value base and strategic pricing is? Is it mostly implemented for contract pricing, fresh start in January? Or do you feel like you won't really fully achieve that maybe till next summer?

Jagadeesh A. Reddy
President, CEO & Director

So a couple of things, we're just getting started on our MBX implementation and our Kaizens are ongoing every quarter, every month in every plant, right? So it, that's a journey. So now we're done with that. So I'm excited. In a couple of weeks, we'll have our -- in a few weeks, we'll have our Q4 President's Kaizen. We're going to do somewhere between 4 and 6 Kaizens across the company in Q4. So pretty exciting events coming up for us.

In terms of pricing, Tim, we implemented through our commercial excellence activities and TPI Kaizens a programmatic approach to value-based pricing. What that means is, we have a new framework on how we think about pricing. It's everything including cost to serve, right? Customers payment terms to

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complexity of their products and manufacturing processes. Two, not ease of doing business with some of our customers. Some need heavy handholding. Some are very easy to do business with, right? So there's a lot of criteria that we have used to develop this matrix, a complex matrix and a model that we're going to use to price, all future work, right?

So that doesn't include all the existing work. For the existing business that we currently have, we're continuing to do our quarterly account reviews and looking at almost SKU by SKU and then say what our profitability is and what should our profitability be for each of these accounts and each of these bodies of work that we currently perform for our customers. That's a long-term process, as you can imagine.

So eventually, everything will lap over the next couple of years. But all the new business that we're beginning to coat in the second half of this year are based on the new pricing framework going forward.

Timothy M. Moore
EF Hutton, Research Division

Great, Jag. That's helpful to hear. The rolling basis plus for the existing in the future being implemented already. At Investor Day, I believe you might have stated that there's about $115 million of new sales opportunities, I guess, signed or won the last 18 months, maybe averaging about $20 million per quarter.

Everyone is familiar with your battery thermal management win, and it sounds like there might be another customer there for Hazel Park. But if you kind of look at your wins and maybe that $20 million a quarter the last few quarters, would you say that a lot of that's in EV-related charging? Or is it more also beyond that battery thermal management into wind, solar, energy grid infrastructure. What are the kind of recent conversations you've been having in potential customers for emerging technologies revenues?

Jagadeesh A. Reddy
President, CEO & Director

Yes, it's a good question as well, Tim. We continue to focus on energy transition as a secular theme within the company. And then we're continuing to look for opportunities where we can go win additional business, whether it's in charging infrastructure, whether it's solar or other renewables.

But I can say so far, majority of the wins have been in battery electric vehicle management applications, whether it is through that one customer we talked about or through our existing customers in CV and powersports and others where they're electrifying their platform. So majority of the wins have been in BEVs, whereas we continue to pursue opportunities in both charging infrastructure and also solar and other renewables.

Timothy M. Moore
EF Hutton, Research Division

Great. So one last question, and this is more so maybe for Todd. So if this year has $5 million to $7 million maybe of underabsorbed costs, turning on EBITDA from the Hazel Park ramp-up, is it fair to assume that next year might be only $1 million to $2 million with none in the second half as you kind of reach that $100 million sales run rate in the fourth quarter possibly next year as utilization plans?

Todd M. Butz
CFO, Secretary & Treasurer

As Jag mentioned earlier, we will not -- at a point yet to provide specific guidance on '24. But certainly, a lot of the projects that we have won really don't watch to mid even in the back half of next year. So there will continue to be a drag in the first half, I would say.

But as you really -- we exit the year, we're confident we're going to exit at that $100 million run rate. And at that point, I wouldn't expect to see any sort of negative impact on that facility. But at this point, again, we're not in a position to really give more specific guidance as to the cadence of that. But I think your comments are fair.

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Generally speaking, I do expect it to be better next year from an underabsorbed position. But at what point, is still we have to go through the details.

Timothy M. Moore
EF Hutton, Research Division

Do you think, Todd, just given maybe the macro slowdown, that you won't move as much stuff over to Hazel Park from some of your other facilities in the first half of the year besides the contract wins, but just existing business you might move?

Todd M. Butz
CFO, Secretary & Treasurer

No, I wouldn't characterize it in that frame. A lot of the new business won again that was specifically quoted and estimated to be at Hazel Park doesn't really launch until midyear and even to the back half. And some of those volumes really don't hit their maturity until even the beginning of 2025. The work that we slated internally to move is still on pace. It's moving in the right cadence. And so we wouldn't make any changes on that front.

Operator

We now have Larry De Maria, William Blair.

Lawrence Tighe De Maria
William Blair & Company L.L.C., Research Division

A few questions. First, maybe you've addressed this, I don't think so, but $5 million to $7 million underabsorbed overhead costs, that's up from, I think, $3 million to $5 million previously. What is driving that delta?

Todd M. Butz
CFO, Secretary & Treasurer

Yes, it did change lately. Certainly, there's been some timing changes from a customer launch perspective. A few of them we thought were going to start sooner rather than later. And so some of that's moved a little further into 2024.

And we have a couple of large ones that are really set to launch in the back half of '24. But even some of the smaller ones, unfortunately, the timing from the customer has in the line, and that's why we've seen a little more drag on the P&L here in the coming quarter or two.

Lawrence Tighe De Maria
William Blair & Company L.L.C., Research Division

So does that present any kind of risk next year that we see continued push-out, especially if the macro is soft? Or how good do we feel about executing on, a, the run rate, and b, remind us what the full year number should be, that we should be modeling?

Todd M. Butz
CFO, Secretary & Treasurer

We feel very good, yes. I mean I think some of the things are just timing of some of it is outsourcing and some of it's moving from other suppliers. It's just the timing of how they're managing their supply chain. It's really been an impetus. And then some design things. Certainly, when they move product, they'd like to improve it and make other changes. I think a lot of that is behind us.

So I feel confident that the launches now, as we see them, will come to fruition. We have said at the Investor Day that next year's sales, we think, are between $50 million and $60 million. And for the full year -- and really, that's going to be more back half loaded. Again, we think we're going to -- we do believe we're going to exit 2024, we do think that fourth quarter, with a run rate of $100 million annually.

Lawrence Tighe De Maria

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William Blair & Company L.L.C., Research Division

Great. So believe me this, Jag talked about growing in '24, right, and getting that -- the big negative, obviously, is CV down 18%, but you can get that to flat. I believe you said flat CV revenue with the outsourcing, new tank production, other wins, et cetera. So you can offset the negative with CV.

But then so are we taking CV flat, from high level, next year CV is flat and then we're layering on the $50 million to $60 million Hazel Park on top of that? Or just help us tie these numbers together so we can -- I know you don't have guidance, but there's a lot of numbers and a lot of deltas, and we want to make sure things aren't overlapping.

Jagadeesh A. Reddy
President, CEO & Director

Yes. The $50 million to $60 million is in that number, Larry. That's not on top. The only thing I would say on top is really the lapping of the first half revenues of MSA.

Lawrence Tighe De Maria
William Blair & Company L.L.C., Research Division

Okay. So CV and as this Hazel Park, the $50 million to $60 million Hazel Park that we're using to offset the CV, some portion of that is non-CV also, right? So how much of the $50 million to $60 million is offsetting the CV declines? And how much of the $50 million to $60 million is non-CV?

Jagadeesh A. Reddy
President, CEO & Director

We're not providing that level of detail at this point in the cycle, Larry. But we're happy to talk about our 2024 guidance ,when it is appropriate.

Lawrence Tighe De Maria
William Blair & Company L.L.C., Research Division

Okay. Yes. It's just obviously -- I think we're mixing some apples and oranges and we're all trying to get to it some kind of a fair number. But we're committing to growth in '24, including MSA, including Hazel Park. CV is down 18%, maybe according to 1 forecast, but it's offset by Hazel Park and some other things. But either way, we're committing to some growth next year, assuming obviously that macro doesn't blow up.

Jagadeesh A. Reddy
President, CEO & Director

Larry, let me clarify. We're expecting to grow overall MEC revenues next year outside of MSA addition.

Lawrence Tighe De Maria
William Blair & Company L.L.C., Research Division

Outside of MSA what? Sorry.

Jagadeesh A. Reddy
President, CEO & Director

Yes, outside of MSA lapping, right, the happier MSA revenues coming into next year. In addition to that, we expect to grow MEC revenues overall.

Lawrence Tighe De Maria
William Blair & Company L.L.C., Research Division

Okay. Fair enough. And then we'll start with less clarification. The $6 million to $7 million and $1 million to $2 million EBITDA from the potential UAW issue. Is that number specific to the one customer? Or that was a gross number prior to all these things through getting sorted out?

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Jagadeesh A. Reddy
President, CEO & Director

It's specific to one customer. Because in October -- and just to clarify, right? In October, we were able to manage most of our challenges with overall UAW strike. As you know, we have some exposure to auto in MSA. And rest of today solves the one CV customer. So October, I think we're able to manage quite well. In November and December, it's just specific to one customer in the CV sector.

Operator

As we have no further questions, I'd like to hand it back to Jag Reddy, President and CEO, for any closing remarks. We do have a further question. We have a follow-up from Ted Jackson.

Edward Randolph Jackson
Northland Capital Markets, Research Division

I just jumped in at the last minute with a couple of nitpicky questions for Todd because he's my favorite person to pick on. So one thing just on SG&A, Todd. The quarter, the number was higher than was in my model. Not a big deal. You got MSA, and there's clearly a lot of things, moving parts inside the business.

What would be, on the other SG&A expense line, how should I think about that for the fourth quarter? Just simply kind of a reset, if you would, as I kind of think through the model. I mean do you -- is there some onetime stuff in there that we would see it go down? Or is that 86 kind of the new baseline and we should be building off of that?

Todd M. Butz
CFO, Secretary & Treasurer

Keep in mind, the 86 includes $1 million of legal fees related to our former fitness customer, and that continues to evolve. So I expect that to continue into the fourth quarter. And then $0.5 million of transaction costs, which I don't expect to continue, right? That's kind of behind us. We incurred those costs in Q3.

But I do expect to have ongoing legal fees, unfortunately, in the near term until there's an ultimate resolution on our claims. So we've said 4.5% to 5.5% in the near term. Next year, as we've talked about, we do have the SOC compliance requirements now that we'll no longer be considered an emerging growth company. I feel like we're in a great position to do that. But certainly, unfortunately, I'd rather -- audit fees and other related things go up. And from there, we'll continue to delever. Delever, I would say, as our sales continue to grow.

So in the fourth quarter, I would say similar without the transaction cost of the $0.5 million.

Edward Randolph Jackson
Northland Capital Markets, Research Division

And then on my second question on the nitpick for you is on amortization of intangibles. I mean will you have an updated table for amortization in your Q, I assume? Because clearly, with MSA and everything and now that's in your balance sheet, that's all going to change. But in the interim, can you give me some kind of color with what you think amortization of intangibles would be in the fourth quarter and then maybe in the aggregate for 2024?

Todd M. Butz
CFO, Secretary & Treasurer

We're not at a point really to score that. You will see in our Q, which certainly will be filed here in the short term. You'll see the step-up. There's footnotes related directly to the acquisition. And I would just take that number and then continue it, right, and use that by quarter into next year.

I don't see -- most of those items that we are amortizing are 5% to 7% in some cases, a little longer to live. So it will be the same, very consistent for the near future.

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Edward Randolph Jackson
Northland Capital Markets, Research Division

And will you file your Q at the end of today? Or when do you plan to put that in?

Todd M. Butz
CFO, Secretary & Treasurer

The expectation is that we'll file it by the end of the day today.

Jagadeesh A. Reddy
President, CEO & Director

Once again, thank you for joining our call. We appreciate your continued support of MEC, and we look forward to updating you on our progress next quarter. Should you have any questions, please contact Noel Ryan or Stefan Neely at Vallum, our Investor Relations Council. This concludes our call today. You may now disconnect.

Operator
Thank you. I can confirm today's conference call has now just -- has concluded. You may now disconnect your line.

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