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Jim Umpleby

Caterpillar; Chairman and Chief Executive Officer

Andrew Bonfield

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Goldman Sachs; Analyst

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PRESENTATION:

Operator^ Welcome to the Third Quarter 2024 Caterpillar Earnings Conference Call. Please be advised that today's conference is being recorded. I would now like to hand the conference over to your speaker today, Ryan Fiedler. Please go ahead.

Ryan Fiedler^ Thanks, Audra. Good morning, everyone. And welcome to Caterpillar's third-quarter of 2024 earnings call. I'm Ryan Fiedler, Vice President of Investor Relations. Joining me today are Jim Umpleby, Chairman and CEO; Andrew Bonfield, Chief Financial Officer; Kyle Epley, Senior Vice President of the Global Finance Services Division; Alex Kapper, Vice President-Elect of IR; and Rob Rengel, Senior Director of IR. During our call, we'll be discussing the third-quarter earnings release we issued earlier today. You can find our slides, the news release and a webcast recap at investors.caterpillar.com under Events and Presentations. The content of this call is protected by U.S. and international copyright law. Any rebroadcast, retransmission, reproduction or distribution of all or part of this content without Caterpillar's prior written permission is prohibited.

Moving to Slide 2. During our call today we'll make forward-looking statements which are subject to risks and uncertainties. We'll also make assumptions that could cause our actual results to be different than the information we're sharing with you on this call. Please refer to our recent SEC filings and the forward-looking statements reminder in the news release for details on factors that individually or in aggregate could cause our actual results to vary materially from our forecast. A detailed discussion of the many factors that we believe may have a material effect on our business on an ongoing basis is contained in our SEC filings. On today's call we'll also refer to non-GAAP numbers. For a reconciliation of any non-GAAP numbers to the appropriate U.S. GAAP numbers, please see the appendix of the earnings call slides. Now let's turn to Slide 3, and turn the call over to our Chairman and CEO, Jim Umpleby.

Jim Umpleby^ Thanks, Ryan. Good morning, everyone. Thank you for joining us. As we close out the third quarter, I want to thank our global team for another good quarter as our results reflect the benefit of the diversity of our end

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markets. We delivered strong adjusted operating profit margin and adjusted profit per share, which were consistent with our expectations, although our top line was lower than we anticipated. We also generated ME&T free cash flow of \$2.7 billion in the third quarter. Our robust ME&T free cash flow, along with our strong balance sheet, allowed us to deploy over \$9 billion to shareholders through share repurchases and dividends during the first three quarters of the year, including \$1.5 billion this quarter. We continue to remain disciplined in the execution of our strategy for long-term profitable growth.

I'll begin with my perspectives about our performance in the quarter and will provide an update on our full year expectations. I'll then provide some insights about our end markets, followed by an update on our strategy and sustainability journey.

Moving to quarterly results. Sales and revenues were down 4% in the third quarter versus last year, below our expectations due to the impact of lower-than-expected sales to users in Construction Industries and timing of deliveries in Resource Industries and Energy & Transportation. Services increased in the quarter compared to 2023. Adjusted operating profit margin was generally in line with our expectations at 20%. We achieved quarterly adjusted profit per share of \$5.17, in-line with our expectations at the time of the last earnings call. In addition, our backlog increased slightly to \$28.7 billion and remains at a very healthy level.

For the full year, although we updated our expectations since our last earnings call to reflect sales being slightly below our prior estimate, our expected adjusted operating profit margin is unchanged and remains above the top of the range. Also, our expectation for adjusted profit per share is unchanged. We are increasing our expectations for ME&T free cash flow and now anticipate it will be near the top of our target range of \$5 billion to \$10 billion.

Turning to Slide 4. In the third quarter of 2024, sales and revenues declined 4% to \$16.1 billion due to lower sales volume. Compared to the third quarter of 2023, overall sales to users decreased 6%. For machines, which includes Construction Industries and Resource Industries, sales to users declined by 10%, which was below our expectations. Energy & Transportation continued to grow as sales to users increased 5%.

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Sales to users in Construction Industries were down 7% year-over-year. In North America, sales to users were down primarily due to lower rental fleet loading and the absence of a large pipeline deal in the third quarter of 2023. Excluding these two items, sales to users were about flat versus the prior year. Compared to our expectations, sales to users were lower than expected, impacted by rental fleet loading. Our dealers' rental revenue continued to grow in the quarter. Sales to users declined in EAME, primarily due to ongoing weakness in construction activity in Europe. Sales to users in Asia/Pacific declined, while Latin America increased.

In Resource Industries, sales to users declined 18%, generally in-line with our expectations versus a strong third quarter in 2023. Mining, as well as Heavy Construction and Quarry and Aggregates were lower mainly due to softness we've previously discussed for two products: articulated trucks and off-highway trucks.

In Energy & Transportation, sales to users increased by 5%, and we continued to see growth in all applications except Industrial. Power Generation sales to users grew strongly as market conditions remained favorable for both reciprocating engines and Solar turbines and turbine-related services. Oil and Gas sales to users benefited from strong sales of turbines and turbine-related services. For reciprocating engines in Oil and Gas applications, sales to users were higher for gas compression, but lower in well servicing. Transportation sales to users increased, while Industrial declined as we expected.

Our results continue to reflect the benefit of the diversity of our end markets as well as the disciplined execution of our strategy for long-term profitable growth.

Moving to dealer inventory and our backlog. In total, dealer inventory increased by \$400 million versus the second quarter of 2024. For machines, dealer inventory increased by \$100 million, slightly more than we had anticipated.

Looking ahead to the fourth quarter, our current planning assumptions forecast a reduction in machine dealer inventory. And we expect machine dealer inventory to end the year around the same level as year-end 2023. Dealers are independent businesses and make stocking decisions across a wide range of products based on multiple factors across the product portfolio. While machine

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dealer inventory is currently around the top end of the typical range, we remain comfortable with the overall level of dealer inventory. As I mentioned, backlog increased slightly versus the second quarter to \$28.7 billion. Energy & Transportation increased as we continue to see strong demand for Solar turbines in Oil and Gas and Power Generation as well as strong demand for reciprocating engines for Power Generation.

Moving to Slide 5. We generated robust ME&T free cash flow of \$2.7 billion in the third quarter and \$6.4 billion in the first three quarters of 2024. As I mentioned, year-to-date, we deployed more than \$9 billion to shareholders through share repurchases and dividends. We remain proud of our Dividend Aristocrat Status and continue to expect to return substantially all ME&T free cash flow to shareholders over time through dividends and share repurchases.

Now on Slide 6, I'll describe our expectations for our three primary segments moving forward. In Construction Industries, we expect lower sales to users in the fourth quarter but remain positive about the longer-term demand outlook. During our August earnings call we noted a lower level of rental fleet loading in North America, which continued into the third quarter, and we now expect the trend to persist in the fourth quarter. Although we have lowered our expectations for sales to users in the fourth quarter primarily due to lower rental fleet loading, dealer rental revenue continues to grow. In addition, government-related infrastructure projects are expected to remain healthy, supported by funding yet to be spent from the IIJA. In Asia/Pacific, outside of China, we expect soft economic conditions to continue. We anticipate demand in China will remain at a relatively low level for the above 10-ton excavator industry. In EAME, we anticipate that weak economic conditions in Europe will continue, partially offset by continued healthy construction demand in the Middle East. Construction activity in Latin America remains healthy, and we are expecting modest growth to continue. In addition, we expect the ongoing benefit of our services initiatives will positively impact Construction Industries.

Next, I'll discuss Resource Industries. After a strong performance in 2023 in Mining as well as Heavy Construction and Quarry and Aggregates, we continue to anticipate lower machine volume in the fourth quarter of 2024 versus last year. However, the rate of decline for sales to users in the fourth quarter is expected to moderate versus the previous quarters. We expect to see higher

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services revenues including robust rebuild activity. Customer product utilization remains high. The number of parked trucks remains relatively low. The age of the fleet remains elevated, and our autonomous solutions continue to see strong customer acceptance. Customers continue to display capital discipline. However, we continue to believe the energy transition will support increased commodity demand over time, expanding our total addressable market and providing further opportunities for long-term profitable growth.

Moving to Energy & Transportation. For Power Generation, demand is expected to remain strong. And we expect robust growth in the fourth quarter and full year sales for both reciprocating engines and Solar turbines. Overall strength in Power Generation continues to be driven by data center growth related to cloud computing and generative AI. And we expect this trend to continue. In Oil and Gas, in total, we continue to expect a stronger year overall in 2024 versus 2023. For Solar turbines used in Oil and Gas applications, we expect a strong fourth quarter, but sales are expected to be lower than the fourth quarter of 2023 due to the timing of deliveries. The increase in Power Generation at Solar will mostly offset Solar's decline in Oil and Gas. So, we expect Solar's total sales in the fourth quarter to be roughly flat compared to last year. Solar has a strong backlog as well as healthy order and inquiry activity. And we continue to expect full year growth for Solar in Oil and Gas. After a strong 2023, we expect reciprocating engine sales and Oil and Gas to be slightly down this year, primarily due to ongoing softness in well servicing. We still expect gas compression to be up for the full year. However, we expect it to soften in the near term as equipment lead times have normalized. As we had previously mentioned, we can leverage our large engine platforms across a variety of applications. Based on current market conditions in well servicing applications, we are able to serve additional Power Generation demand as we continue to meet Oil and Gas customer needs, while optimizing our overall large engine capacity. Industrial demand [is expected] to remain at a relatively low level compared to 2023 (company clarified after the call). In Transportation, we anticipate full year growth in both rail services and marine applications.

Moving to Slide 7. Now I'll provide an update on our strategy and sustainability journey. In February of 2024, we announced a multi-year capital investment in our large reciprocating engine division to approximately double output capability compared to 2023 for new engines and aftermarket parts. Based on

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increasing expectations of future demand growth, today, we are announcing an additional multi-year investment to further expand our large engine volume output capability to more than 125% compared to 2023. As I mentioned, we leverage these large engines across a variety of applications including data centers, Oil and Gas, large mining trucks and distributed power generation.

Moving on to sustainability. We continue to invest in new products, technologies and services to help our customers achieve their climate-related objectives. In September, we unveiled an innovative solution to help solve one of the most complex aspects of the mining industry's energy transition: energy management. Cat Dynamic Energy Transfer, or DET, is a fully Caterpillar developed system that can transfer energy to both diesel electric and battery electric large mining trucks while they are working around a mine site. It can also charge [a machine's] batteries while operating with increased speed on grade, improving operational efficiency and machine uptime (company clarified after the call). Cat DET is comprised of a series of integrated elements including a power module that converts energy from a mine site's power source, an electrified rail system to transmit the energy and a machine system to transfer the energy to the truck's powertrain. Cat DET will integrate with the Cat MineStar Command for hauling solution, merging autonomy and electrification technologies to provide a holistic site solution. We believe mine sites will benefit from enhanced efficiency with the integration of electrification and automation. When combined, these technologies will help miners achieve production targets, while simultaneously managing energy demands. This example highlights how we leverage our industry-leading technology through an integrated approach across our portfolio to help our customers build a better, more sustainable world.

With that, I'll turn it over to Andrew.

Andrew Bonfield^ Thank you, Jim. And good morning, everyone.

As usual, I'll begin with a high-level summary of the third quarter and then provide more detailed comments including the performance of the segments. I'll then discuss the balance sheet and free cash flow before concluding with comments on our assumptions for the full year and the fourth quarter.

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Beginning on Slide 8. Although sales and revenues were lower than we had expected, our adjusted operating profit margin was 20.0%, generally in line with what we had anticipated. Adjusted profit per share was in line with our expectations, despite adjusted operating profit being impacted by the lower sales and revenues. I will highlight a few of the moving parts in a moment.

As Jim mentioned, our full year margin expectations remain unchanged, and we continue to anticipate the adjusted operating profit margin will be above the top end of the target range, despite the slightly lower outlook for the top line. Our expectations for adjusted profit per share remain unchanged versus our expectations at the time of our last earnings call. Also, we have increased our expectations for ME&T free cash flow for the year, which we now anticipate will be near the top of our \$5 billion to \$10 billion target range.

In the third quarter, sales and revenues of \$16.1 billion decreased by 4% compared to the prior year. The adjusted operating profit margin of 20.0% was 80 basis points lower when compared to the prior year. Profit per share was \$5.06 in the third quarter compared to \$5.45 in the third quarter of last year. Restructuring costs were \$0.11 in the quarter versus \$0.07 in the prior year. Adjusted profit per share was \$5.17 in the quarter compared to \$5.52 last year.

Other income and expense was a \$119 million headwind versus the prior year, mostly driven by an unfavorable currency impact related to ME&T balance sheet translation. We do not forecast the impact of foreign currency translation on our adjusted profit per share, so this acted as a headwind compared to our expectations for the quarter. Excluding discrete items, the provision for income taxes in the third quarter in both 2023 and 2024 reflected a global annual effective tax rate of 22.5%. We recorded a discrete tax benefit, which had an \$0.11 favorable impact within the quarter. We do not anticipate discrete items. Finally, the year-over-year impact from the reduction in the average number of shares outstanding primarily due to share repurchases resulted in a favorable impact on adjusted profit per share of approximately \$0.26 as compared to the third quarter of 2023. This was slightly better than we had expected.

Moving to Slide 9, where I'll discuss our top line results for the third quarter. Sales and revenues decreased by 4% compared to the prior year, primarily impacted by lower sales volume as a result of lower sales to users and impacts

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from changes in dealer inventories. Total sales to users decreased by 6% as a 10% decrease for machines was partially offset by a 5% increase for Energy & Transportation. The impact from changes in total dealer inventories acted as a sales headwind of about \$200 million in the quarter. For machines only, dealer inventory increased by about \$100 million, a smaller increase than the \$400 million increase in the prior year, but slightly above our expectations of being flattish to slightly lower. Services revenues increased versus the prior year as we had anticipated.

Moving to operating profit on Slide 10. Operating profit in the third quarter decreased by 9% to \$3.1 billion. Adjusted operating profit decreased by 8% to \$3.2 billion, mainly due to the impact of lower sales volume, partially offset by favorable price realization and manufacturing costs. Since early 2022, price realization has been strong and has often exceeded our expectations. Over the past several quarters, we have highlighted that price will begin to moderate in the second half of this year. In the third quarter, this moderation began to occur as price realization was lower than previous quarters and generally in line with our expectations. As I mentioned, for the third quarter, the adjusted operating profit margin was 20.0%, which was generally in line with our expectations. By segment, margin in Construction Industries and Resource Industries was slightly below our expectations on lower volume, while Energy & Transportation was about in line. Financial Products had a slightly stronger quarter than we had expected.

On to Slide 11. Construction Industries sales decreased by 9% in the third quarter to \$6.3 billion, slightly below our expectations. The decrease versus the prior year was primarily due to lower sales volume and unfavorable price realization. The decrease in sales volume was mainly driven by lower sales of equipment to end users. Changes in dealer inventories also acted as a slight headwind to sales. By region, Construction Industries sales in North America decreased by 11%, in Latin America sales increased by 19%. Sales in the EAME region decreased by 15%, in Asia/Pacific sales declined by 12%. Third quarter profit for Construction Industries was \$1.5 billion, a 20% decrease versus the prior year. This was mainly due to the profit impact of lower sales volume and unfavorable price realization. The segment's margin of 23.4% was a decrease of 300 basis points versus the prior year.

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Turning to Slide 12. Resource Industries sales decreased by 10% in the third quarter to \$3.0 billion, which was slightly below our expectations. The decline versus the prior year was primarily due to lower sales volume, mainly driven by lower sales of equipment to end users given the challenging comparison to the prior year. Third quarter profit for Resource Industries decreased by 15% versus the prior year to \$619 million. This was mainly due to the profit impact of lower sales volume. The segment's margin of 20.4% was a decrease of 140 basis points versus the prior year.

Now on Slide 13. Energy & Transportation sales increased by 5% in the third quarter to \$7.2 billion, slightly lower than we had expected driven by the timing of deliveries. The increase versus the prior year was primarily due to favorable price realization and higher sales volume including higher intersegment sales. By application, Power Generation sales increased by 26%. Transportation sales were higher by 3%. Oil and Gas sales decreased by 1%, and Industrial sales decreased by 16%. Third quarter profit for Energy & Transportation increased by 21% versus the prior year to \$1.4 billion. The increase was mainly due to favorable price realization. The segment's margin of 19.9% was an increase of 270 basis points versus the prior year.

Moving to Slide 14. Financial Products revenues increased by 6% to about \$1 billion, primarily due to higher average earning assets driven by North America and higher average financing rates across all regions. Segment profit increased by 21% to \$246 million. This was mainly due to a favorable impact from equity securities and a lower provision for credit losses. Our customers' financial health is strong. Past dues remain near historic lows at 1.74% in the quarter, down 22 basis points versus the prior year. Our allowance rate was 0.87%, our lowest on record. Business activity at Cat Financial remains healthy. Our retail new business volume increased by 17% versus the prior year, supported by our financing packages for customers choosing to buy Caterpillar equipment. Though Caterpillar's retail machine sales volume was lower, proportionally more sales are being financed through Cat Financial, which highlights the attractiveness of the financing options we are offering to our customers. We also continue to see healthy demand for used equipment, and inventories remain at low levels. Conversion rates are also strong as customers choose to buy equipment at the end of their lease term.

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Moving on to Slide 15. We generated about \$2.7 billion in ME&T free cash flow in the third quarter and deployed about \$1.5 billion in share repurchases and dividends. Our balance sheet remains strong with an enterprise cash balance of \$5.6 billion. In addition, we hold \$1.8 billion in slightly longer dated liquid marketable securities to improve yields on that cash.

Now on Slide 16, I'll share our high-level assumptions for the full year. For the full year, we have updated our outlook to reflect sales and revenues that are slightly lower than our expectations at the time of our last earnings call driven by lower-than-expected third quarter sales and an update to our expectations for dealer rental fleet loading in Construction Industries. We continue to anticipate services growth in 2024. As I mentioned earlier, our full year expectations for adjusted operating profit margin and adjusted profit per share remain unchanged compared to our last earnings call. We continue to expect adjusted operating profit margin to be above the top end of the target range.

In addition, we are increasing our expectations for ME&T free cash flow for the year, which we now anticipate to be near the top of our \$5 billion to \$10 billion target range. To assist you with your modeling for the full year, we now anticipate CapEx of around \$2 billion and restructuring costs of approximately \$400 million. Our expectation for the global annual effective tax rate, excluding discrete items, remains at 22.5%.

Turning to Slide 17. I'll provide a few comments on the fourth quarter, starting with the top line. We expect slightly lower sales and revenues in the fourth quarter compared to the prior year, impacted by lower machine sales to users versus a strong comparison. On machine dealer inventory, our planning assumptions include the expectation that dealers will reduce their inventories in the fourth quarter, while balancing their need to be prepared for 2025. The magnitude of the decline of machine dealer inventory is expected to be less than the \$1.4 billion decrease we saw in the fourth quarter of 2023.

For perspective, we expect machine dealer inventory to end the year around same level as year-end 2023. Also, the ongoing benefit of our services initiatives is expected to positively impact sales in the fourth quarter.

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By segment in the fourth quarter compared to the prior year, we anticipate a sales decrease in Construction Industries. This is impacted by lower sales to users, which Jim mentioned, along with unfavorable price realization. In Resource Industries, we expect slightly lower sales impacted by lower sales to users versus a strong fourth quarter of 2023. In Energy & Transportation, we anticipate slightly higher sales versus the prior year, supported by Power Generation. Enterprise margin in the fourth quarter is expected to trend lower compared to the third quarter, following the typical seasonable pattern. However, versus the prior year, we expect a modestly higher adjusted operating profit margin, despite lower sales.

We anticipate favorable manufacturing costs and lower SG&A and R&D expenses will more than offset the profit impact of lower sales volume. Lower SG&A and R&D expenses are primarily driven by the benefit of lower short-term incentive compensation versus a higher expense in the prior year quarter. Price realization from machines is expected to trend lower as the pricing environment continues to normalize, though price in Energy & Transportation should act as a partial offset.

Regarding price expectations for machines, it is important to note that discounts to dealers occur through post-sales merchandising programs, which impact our results over time. This includes financing support from Cat Financial, which is an effective way of supporting our customers, and we recover a portion of that support over the life of the deal. Let me explain. Based on the current level of price discounting support, we reserve for the anticipated payments to dealers for these merchandising programs. At times, there is a lag between the timing of [our] invoice [to] the dealer and when the dealer invoices the customer, which impacts the reserve (company clarified after the call). Over the next few quarters, we expect the impact from these merchandising programs to drive a headwind to machine price realization as we continue to adjust the reserve to reflect the current level of price discounting support. By segment in the fourth quarter, in Construction Industries, we anticipate lower margin compared to the prior year, primarily due to unfavorable price realization, partially offset by favorable manufacturing costs.

In Resource Industries, we anticipate lower margin in the fourth quarter compared to the prior year, mainly due to lower volume and prioritization of

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strategic investments around services growth and AACE, which is autonomy, alternative fuels, connectivity and digital, and electrification. Favorable manufacturing costs should act as a partial offset.

In Energy & Transportation, we expect a higher margin versus the prior year, primarily impacted by favorable price realization.

So, turning to Slide 18. Let me summarize. Although sales and revenues were lower than we had expected, adjusted operating profit margin and adjusted profit per share were generally in line with our expectations. We now anticipate our top line for the full year will be slightly below our prior estimate. Our backlog increased slightly and remains at a very healthy level. Our expectations for full year adjusted operating profit margin and adjusted profit per share remain unchanged compared to a quarter ago. We continue to expect adjusted operating profit margin to be above the top end of the target range for the full year based on our expected sales levels. We are now increasing our expectations for ME&T free cash flow, which we anticipate to be near the top of our target range for the full year. Our team executed well in the quarter, and our results continue to reflect the benefit of the diversity of our end markets and the disciplined execution of our strategy for long-term profitable growth. And with that, we'll now take your questions.

Operator^ (Operator Instructions) We'll take our first question from Jerry Revich at Goldman Sachs.

Jerry Revich^ Andrew, I'm wondering if we could just take a step back. Your margin performance this year is really outstanding relative to the long-term targets. And as you see it, is this level of outperformance sustainable? Or should we take the pricing headwinds that we spoke about in the prepared remarks to mean that you folks are evaluating the optimal balance between margins and market share?

Jim Umpleby^ Well Jerry, just as a reminder, our primary measure of profitable growth is increasing absolute OPACC dollars. That's something we're very focused on. Obviously, we're always focused on being competitive in the various markets that we serve. And of course, we serve a diverse group of industries around the world. So, what's happening in one market with one segment can be

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very different than what's happening in another segment just from a competitive perspective. So again, we're focused on remaining competitive. We do provide margin targets, obviously, to give investors and analysts a sense of where we'll be around margins, and we'll continue to do that. So again, we're driving to remain competitive. We're driving to increase absolute OPACC dollars. And you can use our margin target ranges to get a sense of where we expect to be.

Operator^ We'll move next to Tami Zakaria at JPMorgan.

Tami Zakaria^ My question is on the Resource Industries segment. Volumes in that segment have been down for about a year now. And I think you said the rate of decline you expect to get better in the fourth quarter. I'm curious, how are you planning for this segment for 2025? Do you expect demand or sales to stabilize near term or it could get better or maybe stay weak for a few more quarters?

Jim Umpleby^ Well thanks for your question. The full year drop, as we talked about in previous calls, is really primarily due to a couple of products: articulated trucks and off-highway trucks. And we had a strong backlog there that we had to work our way through, and that's created a comparison issue for us in Resource Industries this year. Having said that, obviously we're not going to give guidance around 2025. We'll talk about 2025 in January. But certainly, we continue to be quite bullish on the long-term aspects for mining, just given all the commodities that need to be produced to support the energy transition. Our mining customers use our products to produce those products, things like copper. So, our customers are displaying capital discipline, but we certainly are bullish about the long term. We do expect higher services revenues because the utilization of our products is quite high. The age of the fleet is relatively elevated, and the number of parked trucks is relatively low. So those are all positive things. One of the things that we also see is a lot of inquiry activity and order activity around large mining trucks. So, we're pleased with that. So, that's one of the things that also is the reason for optimism as well.

Operator^ Next, we'll move to Angel Castillo at Morgan Stanley.

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Angel Castillo^ I was wondering if you could expand a little bit more on what you're hearing from your dealers and customers around in terms of Construction Industries, particularly in terms of orders, how is that kind of shaking out for that segment specifically, and then more so qualitatively what you're hearing into 2025 in terms of sentiment and kind of inclinations to buy kind of heading into that year versus the macro that remains a little bit uncertain.

Jim Umpleby^ Well, a couple of things. Firstly, in the quarter, as I mentioned earlier, the primary reasons for the decline [year-over-year] was based on lower rental fleet loading by our dealers (company clarified after the call). And of course, it's important to note that our dealers' rental revenue continues to increase. So, it's really an issue of them having lower loading into their rental fleets. In addition to that, we had a large pipeline deal in the third quarter of last year, which obviously didn't reoccur, and that created a [comparison] issue as well (company clarified after the call). From a positive perspective, we expect government-related infrastructure to remain healthy. If we look at some facts from ARTBA, which is the American Road and Transportation Builders Association, they noted that only 27% of the \$348 billion in total IJA funding has been spent as of August of 2024. About 47% of it has been committed, and only 27% of it's been spent. So that's quite healthy as well.

So, there's a lot of infrastructure activity out there that our dealers are working with their customers to help support. So, we feel good about that as well.

Operator^ We'll go next to Jamie Cook at Truist Securities.

Jamie Cook^ Jim, I think you said during the prepared remarks that you guys are adding incremental large engine capacity relative to your previous announcement.

So, I guess my question is, is there any way you can frame the capital investment? And more importantly, what you think the longer-term revenue opportunity for Caterpillar as you continue to increase capacity here? And then sort of what does that imply for margins for this segment? Again, we're adding a lot of capacity, but the margins are below Resource Industries and Construction Industries. So, should margins be structurally higher as volumes ramp?

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Jim Umpleby^ Thanks for your question, Jamie. And we haven't quantified the amount of capital investment in that capacity increase, but we did talk about the fact that we expect with this incremental investment that we will increase our large engine volume output capability to more than 125% compared to 2023. And of course, those engines are used across a wide variety of applications. And certainly, what's driving the demand today is data centers.

We sell backup generator sets for data centers. But we're also quite excited about the opportunity going forward for what we call distributed generation. Data centers, of course, don't just create an opportunity for us for backup generator sets. But of course, the base load requirements on the grid is going up as well because of data centers, and there's much that has been written about that.

And so just given the fact that there's been relative underinvestment in traditional power plants over the last few years, the fact that more renewables have been added to the grid, which are intermittent in nature, and the fact that now we have data centers increasing base load requirements on the grid, we think that creates an opportunity for us for both our gas turbine generator sets and our reciprocating generator sets in what we call distributed power applications distributed across the grid. And our gas turbines and generator sets can burn a wide variety of fuel, natural gas, biofuels, hydrogen blends. So, we're quite excited about that long-term opportunity that is starting to manifest itself.

And to your question about margins, certainly you saw a nice margin increase [year-over-year] in Energy & Transportation; and just because of mix and because of increased volume and just the fact that business should be higher, again, we have the opportunity to increase margins in Energy & Transportation going forward, but I'm not going to quantify that at this point (company clarified after the call). But certainly, it's an opportunity.

Operator^ We'll take our next question from David Raso at Evercore ISI.

David Raso^ More breadcrumbs for 2025. My question, I guess, two pieces. The comment about the drag, right, the lag of discounting for Construction Industries, it will show itself more as some of those orders get shipped into '25. Can you give us a sense of just where we stand right now? Let's assume no

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further deterioration maybe in Construction Industries pricing. But what we're booking right now at those discounts, what is the most acute period in '25 that, that shows up? Essentially, it's how long are these orders out for? Is this second quarter, third quarter next year that should be the most acute drag from the incremental discounting right now?

And then on the positive side, you kind of just said you didn't want to quantify it. But the investments in Energy & Transportation, the large engines, which I know also go to large mining trucks, but let's think of it as Energy & Transportation in particular right now is there any way to think about regular throughput improvement? Any capacity additions that can show up in '25 to give us a sense of at least your throughput capability '25 versus '24, just some order of magnitude?

Jim Umpleby^ Thanks for your question, David. So, one of the things we talked about when we announced the initial investment to increase our large engine capacity is that would increase over a 4-year period. And so, we haven't laid it out year by year, and again, it's a 4-year increase. So, I'm afraid I'm not going to be able to answer your question to give a sense of additional output for 2025, and I'll let Andrew answer your question about margins.

Andrew Bonfield^ So, on the impact of pricing, this is an accounting [process] that we have. The way it works, David, is the accrual is done [for the anticipated payments to dealers for these merchandising programs and uses] historic [discounting rates] to build up the reserve (company clarified after the call). So potentially, this could impact us for several quarters. As the merchandising programs increase, you then have the amount that's in [dealer's] inventory that you have to effectively [adjust the reserve to reflect the current level of price discounting support] and that's done [every reporting] period (company clarified after the call). So generally, it will be for the next several quarters, but we are starting to see the merchandising programs hit more normal levels now. And obviously that creates a little bit of a headwind on price. We'll probably quantify it a little bit more when we get to 2025 guidance for you in January.

Operator^ Next, we'll go to Michael Feniger at Bank of America.

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Michael Feniger^ I would just love to get a sense on the Oil & Gas side. Obviously retail sales were up a little bit. You talked about the differentiation of what you're seeing in terms of the reciprocating engine side and well services versus maybe gas compression, some of the other areas. Just when we look into 2025, if we see more LNG permitting in the Gulf, is that positive for the Solar business? Do we need a higher natural gas price? Obviously, the oil price has been kind of stuck in a range. So just curious how we're thinking with Oil & Gas being very strong and up in '24. You kind of made some comments on Q4. What do we kind of think about the breadcrumbs for '25 for that business?

Jim Umpleby^ So again, I'll resist giving the guidance for 2025, but I'll just give you some color around the industry. Certainly, we mentioned the fact that well servicing continues to be a bit weak. Gas compression for reciprocating engines for Cat Oil & Gas, we expect to be up for the total year, but a bit of softening in the fourth quarter. On Solar turbines in Oil and Gas, the business is quite strong, a lot of booking activity, a lot of quotation activity, both for gas compression, but also for international projects as well. So again, Solar business is quite robust, and I've described reciprocating engines. It remains to be seen, obviously if LNG exports start again, if that permitting process starts again, I would think certainly medium, long term, that would be a positive for us.

Operator^ We'll move to our next question from Kristen Owen at Oppenheimer & Co.

Kristen Owen^ Jim, I wanted to come back to the Construction Industries competitive dynamics, particularly in North America. You've called out the re-fleeting issue a couple of quarters in a row now but you are at the higher end of the inventory range. Just wondering, can you help us understand how much maybe incremental international competition you're seeing, given the depreciation of the Yen and just continued disappointment in China activity? Just anything you're seeing on a shift in the competitive landscape there?

Jim Umpleby^ Well certainly, we're very focused on remaining competitive, and the competitive situation continually changes. Every year I've been in this job, and before that, the competitive situation always changes. But we are quite confident in our ability to continue to compete. We continue to invest in new technologies, as an example, to allow operators to more effectively operate their

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machines as an example, taking a less experienced operator and through technology, allowing them to operate more like an experienced operator. We continue to invest in our digital capabilities. Our dealers continue to invest in their capabilities as well. So, we're quite confident in our ability to continue to compete and be successful. The competitive situation, there are currency changes that occur. And you're right, the Yen has been relatively weak and that, for a period of time, can create a bit of a tailwind for a competitor, but those things change over time as currencies change. But again, what we're really focused on is providing that long-term value to our customers by continuing to invest in things like technology, our digital capabilities, service capabilities and all the rest.

Andrew Bonfield^ And can I just make a comment on your comment about the higher end of the [dealer] inventory range? One of the things just to remember is dealer inventory is a complex thing. We have [over] 150 dealers around the world. We have three business segments. We have lots of different products. There are some actual product lines where actually dealers holding more inventories would actually be a good thing from a competitive perspective, not necessarily always reducing. So, it's not necessarily about them burning it down.

We obviously work with them through that process where they do need to think about a dealer inventory reduction, and that's what we're anticipating in the fourth quarter. But there are also some business segments where, actually at times, we would like dealers probably to hold a little bit more for competitive reasons as well.

Operator^ We'll go next to Steven Fisher at UBS.

Steven Fisher^ Jim, you mentioned the 4-year process on Power Generation capacity expansion, but the Power Generation growth actually accelerated to about 26% year-over-year from 15% in Q2. So, with being at capacity on some of the bigger projects -- products, can you talk about what drove that acceleration? And to what extent is that maybe a function of shifting some of your Oil & Gas engines into Power Generation? And should we expect some sort of quarter-to-quarter fluctuations in that rate of growth in Power Generation going forward based on comparisons and how you are able to shift capacity around?

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Jim Umpleby^ Just to be clear, when we ship a generator set to an Oil & Gas customer or for an Oil & Gas application, we count that as Oil & Gas, not Power Generation, just to be clear. So, a variety of reasons for the increase. Certainly of course, as I mentioned in my prepared remarks, we do have the ability to reallocate. If the demand for Oil & Gas is not there and we have excess capacity, we can shift those engines from Oil and Gas to Power Generation and back and forth, depending on the needs of our customers. So that's there. Solar - Power Generation, is also increasing, and that also had an impact on it as well. And we've been, of course, working in our reciprocating engine facilities to increase capacity. Yes. The major impact will come later because of the big capital investment we're making. But we're working on increasing throughput and getting more out of our existing facilities as well as the demand goes up.

Operator^ We'll take our next question from Kyle Menges of Citigroup.

Kyle Menges^ I was hoping if you could discuss inventories a little bit more. So, this planned reduction in dealer inventories in 4Q, is that enough to make you guys feel pretty good about machine inventories heading into next year? And then it would also be helpful just to hear your thoughts on used inventories. It sounds like they remain at low levels, but are you seeing used tick up a little bit? And is there any cause for concern that used inventories could become an issue in 2025?

Andrew Bonfield^ So, first of all, let me mention on used. As we say, used inventory levels actually remain at pretty low levels based on history. They had ticked up slightly. Obviously, pricing has become a little bit lower. But pricing still is actually okay from a Cat Financial perspective. So, no concern at this point around used inventory at all from an overall perspective. With regard to dealer inventory, obviously we work closely with our dealers through what we call our S&OP process. That's our sales and operations planning process. We go down by dealer, by product really to understand what their expectations are, what their requirements are, what their ordering needs are. That's part of the way of us helping to manage the factories and production efficiently. At this point in time, we expect that reduction we see to bring [dealer] inventory overall to about flat year-over-year (company clarified after the call). That seems to be the right level based on what we're hearing from dealers at this stage. I don't see any reason at this point in time that there would be a need to reduce them significantly more.

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But obviously that's a discussion process that will go through in 2025. But obviously we are ready and prepared to manage and work and manage production accordingly. As I made the point a moment ago, there are some product lines where actually dealers really could hold more inventory. So, have to be very, very careful about looking at it as holistically. But overall, we're very comfortable with the total level and expectations for the year-end.

Operator^ We'll go next to Chad Dillard at Bernstein.

Chad Dillard^ So I just wanted to revisit the comments about pricing in Construction Industries. So first, just wanted to understand, when do you actually expect the max pricing pressure? And then secondly, if we think about the other side of the ledger, the cost side, you have fuel coming down. It sounds like you're easing on SG&A and R&D costs.

So just trying to think through whether you'll be able to offset some of that pricing pressure with some improved cost.

Andrew Bonfield^ So let me just, first of all, come back to the overall. If you actually look at our overall gross margins for the quarter, gross margins were about flat [year-over-year] despite lower volume (company clarified after the call). So, we have been able to find offsets. Some of that obviously is with a positive price within Energy & Transportation. And some of that is lower manufacturing costs. So, that's part of the benefit of having a broad portfolio of businesses. We are able to manage that appropriately. Obviously, we are looking at commodity input costs and, obviously working from a procurement perspective. I always remind you that there's always a lag. It's never because of the contracting that we do. We often don't necessarily buy at spot prices. We buy contractor prices, which may even be lower than spot. So, all of those things are factors which feed in, takes a little bit of time for that to fall through.

With regard to the pricing pressure, the merchandising programs we put in place will flow through to the P&L within Construction Industries. (Statement removed for clarification purposes). We'll give you a little bit more update on that when we get to January.

Operator^ Next, we'll go to Tim Thein at Raymond James.

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Tim Thein^ Jim, I was hoping you could maybe give some color on the backlog and the orders which were pretty strong in the quarter just in terms of maybe a key driver or two or kind of what's behind that. And I guess, more significantly, I'm just curious if the -- I presume you're going to highlight data centers as part of that. And is there a shift in terms of how you think -- or how we should think about ultimately the delivery -- the timing of those deliveries in that, given the tightness in capacity? I presume some of your bigger data center customers are like -- looking to secure capacity further out. So anyway, just a question around the -- maybe the driver of the orders. And then should we think about any change in terms of the ultimate delivery cadence of those orders?

Jim Umpleby^ So, the backlog increase in Energy & Transportation was quite robust, and that more than offset a decrease in backlog for machines. And of course, it's not surprising that the backlog for machines went down in anticipation of the machine dealer inventory reduction, that we previously talked about, in the fourth quarter. So, the backlog increase in Energy & Transportation is being driven a lot by Power Generation for reciprocating engines, also being driven by robust orders in Solar turbines for both Oil & Gas and [Power Generation] (company clarified after the call). So that's really what's behind it. And so typically, lead times for Solar is 8 to 12 months typically. For reciprocating engines and Power Generation, we're working hard to meet the demands of our customers there, but we do have orders going out 18, 24 months on the outside for Power Generation and reciprocating engines.

Operator^ Next, we'll move to Mig Dobre at Baird.

Mig Dobre^ Just to follow up on Tim's question, is there a way to maybe quantify what percentage of the backlog is deliverable here in the next 12 months? And I'm also curious, given the fact that the lead times are what they are in Power Generation, how are competitive dynamics versus your competitors in that part of the business? Is there somebody else out there maybe with better lead times than you? Can you gain share if you improve your lead times faster than others? Appreciate some thoughts on that.

Jim Umpleby^ Generally, overall, the way we think about it is about 75% of our backlog is expected to be sold within 12 months. That's a general number for a

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total. As I mentioned, some of the large engine orders are out a bit more than that. Certainly, if we can produce more engines, we can sell more engines for Power Generation, reciprocating engines. That's certainly the case. And again, just given the strength that we see in that market, it is obviously why we decided to make an incremental investment and our capability to increase engines and parts. So again, the business is quite strong. It's very, very encouraging.

Operator^ Next, we'll go to Jairam Nathan at Daiwa.

Jairam Nathan^ I just wanted to go over some of the -- your position in China. There's a lot of talk about stimulus, not sure how helpful it would be. But if you could just remind us of your market position there, the freshness of products a little bit.

Jim Umpleby^ So, as we discussed previously for a long period of time, we talked about China being roughly 5% to 10% of our consolidated sales and revenues. It's certainly been less than that the last couple of years and the market itself continues to be quite weak. And so, it is below that 5% again this year. So, it's a relatively small piece of our total enterprise sales [and revenues] (company clarified after the call). Certainly, we have a significant presence in China in terms of facilities, and we've integrated our supply chain suppliers, manufacturing and local leadership as well in dealers. But again, the market is, in fact, quite depressed. And this is a reminder for us that market is primarily excavators above 10-ton. And so, people have asked about the stimulus. It's too early for us to have seen any impact of that, and we have not.

Operator^ And today's final question comes from the line of Rob Wertheimer with Melius Research.

Rob Wertheimer^ So I wanted to follow up, last quarter, you kind of touched on expanding opportunities at Solar turbines and Power Generation. And in today's call you mentioned some of the strong demand you're seeing in the reciprocating engine side and capacity expansion, et cetera. On Vernova's call they had some strong trends in their derivative turbines, which I think are probably still a little bit above your power range. But I wonder if you might just talk about this business and the opportunity you're seeing in the Power Generator segment for Solar. What does that mean? Does it mean behind the

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gated data center? Does it mean data centers? What is the opportunity you're seeing? And then you've expanded capacity in reciprocating engines. Do you have room to grow in turbines? Or would you -- is the opportunity big enough that you're thinking about expanding there, too? Just a general overview.

Jim Umpleby^ So, certainly we are seeing an increase in business for Power Generation and Solar turbines. We're selling trailerized units now and it's being driven by a whole variety of factors. One of the things that we're doing is selling into some rental fleets, where rental fleets are positioning themselves to help satisfy what they believe will be increased electricity demand across the grid and primarily in North America. And sometimes, those units will be rented to utility. Sometimes, those will be rented to a data center, but there's a whole variety of uses for that. So, we are seeing an increase in Power Generation in Solar. Solar is not out of capacity. They certainly have the ability to continue to increase their production. And one of the things you might be aware of is that we are in the process of introducing a newer, larger gas turbine for Solar turbines. It's our largest jet called the Titan 350. And that really will allow us to compete in some areas that we have not been able to compete for in the past because we just didn't have a turbine that was large enough. And so, we're quite excited about that new product. It's early days in terms of just starting to get those shipped, but we are quite encouraged by the amount of customer interest and discussions we're having with our customers about that new product. So again, that's something that's very exciting for us.

Okay. With that, I just want to thank everyone for joining us, and certainly appreciate your questions. I just want to thank our global team for delivering strong adjusted operating profit margin and adjusted profit per share while generating robust ME&T free cash flow. And as we discussed today, our results continue to reflect the benefit of the diversity of our end markets as well as the execution of our strategy for long-term profitable growth. Again, thank you for your time.

Ryan Fiedler^ Thank you Jim, Andrew and everyone who joined us today. A replay of our call will be available online later this morning. We'll also post a transcript to our Investor Relations website as soon as it's available. You'll also find the third quarter results video with our CFO and an SEC filing with our sales to users data. Click on investors.caterpillar.com. Then click on 'Financials' to view

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those materials. If you have any questions, please reach out to Alex, Rob or me. The Investor Relations general phone number is (309) 675-4549. And now we'll turn the call back to Audra to conclude.

Operator^ That does conclude our call. Thank you for joining. You may all disconnect.