

Shyft Group, Inc.

Second Quarter 2023 Earnings Call

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CORPORATE PARTICIPANTS

Randy Wilson - *Vice President Investor Relations & Treasury*

Daryl Adams - *President & Chief Executive Officer*

Jonathan Douyard - *Chief Financial Officer*

PRESENTATION

Operator

Good morning, and welcome to The Shyft Group's Second Quarter 2023 conference call and webcast. All participants will be in a listen-only mode until the question-and-answer session of the conference call. As a reminder, this call is being recorded.

I would now like to introduce Randy Wilson, Vice President, Investor Relations and Treasury of The Shyft Group. Mr. Wilson, you may proceed.

Randy Wilson

Thank you for joining this morning's call. I am joined by Daryl Adams, President and Chief Executive Officer; and Jon Douyard, Chief Financial Officer. Their prepared remarks will be followed by a question-and-answer session. For today's call, we have included our presentation deck that has been filed with the SEC and is also available on our website. Before we begin, please turn to Slide 2 of the presentation for our Safe Harbor Statement.

Today's conference call contains forward-looking statements, which are subject to risks that could cause actual results to be materially different from those expressed or implied. Primary risks that management believes could materially affect our results are identified in our Forms 10-K and 10-Q, filed with the SEC. We will be discussing non-GAAP information and performance measures, which we believe are useful in evaluating the company's operating performance.

During today's call, we will provide a business update before moving on to a more detailed review of the results and our updated 2023 outlook. We will then open the line for Q&A. Please turn to Slide 3, and I'll turn it over to Daryl Adams.

Daryl Adams

Thank you, Randy. Good morning and thank you for joining us to review our second quarter 2023 results. Overall, results in the quarter were in line with our expectations, highlighted by strong performance in Specialty Vehicles and robust cash generation. We made great progress on the execution of our long-term, strategic priorities, delivering on key Blue Arc electric vehicle milestones. And consistent with our prior communications, we remain on track for Blue Arc production in the second half of the year.

While Fleet Vehicles and Services grew modestly in the quarter, we experienced further weakness in end market conditions, as well as operational inefficiencies, that impacted overall performance. Second quarter sales were down 3%, year over year, with strength in both our truck and service body product lines, more than offset by softness in last-mile delivery and motorhome.

Despite the sales decline, we delivered \$16 million of adjusted EBITDA, up 16% versus last year, led by record margin performance in Specialty Vehicles. We made solid progress on reducing working capital, resulting in \$30 million of operating cash flow and ending the quarter in a strong financial position. Turning to our Market Commentary, on Slide 4 -- long-term outlook remains favorable in our key, end markets, including last-mile delivery and infrastructure. And we believe we are well positioned as the industry leader in these areas.

However, throughout the second quarter, we saw accelerated signs of demand weakness, due to broader economic conditions, and evolving market dynamics. I will now provide additional details on what we are seeing within our businesses, starting with fleet vehicles and services. We previously discussed concerns and a level of uncertainty in the last mile delivery market. After speaking with our customers and listening to their public commentary, there are several factors

influence -- influencing immediate buying decisions, including continued, year-over-year declines in parcel package volume, as well as specific customer dynamics regarding fleet strategy.

As a result, -- we have seen customers defer and cancel orders, leading to higher dealer inventory levels and reduced OEM chassis production. We experienced the impact of reduced chassis supply late in the second quarter, and we now expect to see more significant reductions in chassis production levels in the second half of the year. At the same time, we're also hearing from customers that there is an ongoing need for vehicles, which gives us confidence in the long-term prospects for last-mile delivery vehicles.

While orders have been deferred, it is clear that fleet replacement needs, e-commerce growth projections and regulatory requirements to reduce emissions will drive future vehicle purchases. In response to the current environment, we are taking decisive actions within FES, including adjusting operations to efficiently support current volumes while focusing on long-term productivity drivers, driving improved product quality and on-time customer deliveries and refocusing our sales efforts by expanding into new customers and locations.

Moving to specialty vehicles -- our work truck products, including service bodies, a Isuzu contract manufacturing, and police vehicle outfit continue to perform well, supported by increased infrastructure spending and demand for vocational vehicles. We expect these positive trends to continue, and we are focused on executing our strategy to expand our products and geographies to support the growing needs of the market. For example, we recently launched our Royal XP body and opened our Nashville facility, which encompasses both service bodies and police vehicle outfit.

For our motorhome chassis business, the broader RV industry has been challenged by general economic conditions after multiple years of growth. Entering 2023, we expected to see softening demand. However, in the second quarter, we have seen the demand decline accelerate and RV manufacturers have further reduced their production schedules in light of higher dealer inventory. That said, despite declines in the market, we continue to increase our market share in the greater than 400 horsepower diesel segment, and we experienced recent market share highs in the quarter.

Looking forward, industry reports suggest that there will be a market improvement in 2024. However, we remain cautious about this outlook and have adjusted our business accordingly. Overall, we are confident we have positioned the Shyft Group in markets with our long-term secular growth, including last mile delivery, infrastructure and electric vehicles. We have demonstrated the ability to manage challenging market conditions like the ones we are facing today, and we have industry-leading brands, flexible operations, and a talented team that will enable us to win in the future.

Turning to Slide 5 -- I'll provide an update on our Blue Arc EV progress and the key milestones we expect to achieve in the second half of the year to have a successful product launch. As we review our Blue Arc operational plans, we consider these lessons learned from our decades of manufacturing experience and are ensuring that Blue Arc vehicles are built with the quality and value for the best-in-class products in the market. We are currently field testing our vehicle with a key customer, and the initial feedback is positive, which gives us confidence in the vehicle's capability.

We are excited by the vehicles test performance in the hot weather conditions, as well as the feedback that we have received from multiple drivers that they have delivered packages on their

daily routes. In addition, our suppliers are actively working to finalize component testing and provide final certification ahead of start of production. We are nearing completion of the facility construction and are conducting operator training through virtual and slow builds at our Michigan campus. We have completed the standard operating procedures and are on track for the initial production of 50 units for delivery to customers in the fourth quarter.

We are committed to building out a highly qualified Blue Arc dealer network to ensure fleet customers receive the products and services they expect. We have previously talked about a nationwide dealer and service network, made up of a small group of dealers and an established service provider. We remain in the process of finalizing agreements to support this structure, while also establishing banking relationships to ensure dealers can support their floor plan needs.

While arrangements are being finalized, dealers are highly engaged with customers, and there continues to be a high level of interest in our product. We are incredibly excited about Blue Arc's prospects and our team's ability to execute this product launch in the second half of the year. With that, I'll now turn it over to Jon to discuss our second quarter financial results.

Jon Douyard

Thank you, Daryl, and good morning, everyone. Please turn to Slide 7, and I'll provide an overview of our financial results for the second quarter of 2023. Overall, we delivered second quarter results that were in line with our expectations, with solid, year-over-year adjusted EBITDA growth. We continue to see pockets of strength across the company, particularly in our Specialty Vehicles segment. Sales for the second quarter were \$225.1 million, down 3.1% from the year ago quarter.

Net income was \$4.7 million or \$0.13 per share, compared to net income of \$5.3 million or \$0.15 per share in the previous year. Second quarter net income was negatively impacted by approximately \$3 million of expenses related to our CEO transition, as well as actions taken to adjust our cost structure, given the lower volumes. In the second quarter, adjusted EBITDA was \$15.9 million or 7% of sales, up from \$13.7 million or 5.9% of sales in the second quarter of 2022.

These results include EV program spend of \$7.4 million, up slightly from the prior year. Excluding these expenses, adjusted EBITDA was 10.4% of sales, up 140 basis points year-over-year. Adjusted net income improved to \$8.7 million, compared to \$7.5 million in the year ago quarter, while adjusted EPS rose to \$0.25 per share, from \$0.21 per share last year.

I'll now walk you through our second quarter results by operating segment, beginning with Fleet Vehicles and Services on Slide 8. In the quarter, the FVS team delivered solid working capital reduction and meaningful, year-over-year improvements in truck body output, while taking short-term and structural cost actions in a highly dynamic environment.

FVS achieved sales of \$139 million, up 1.5% compared to \$136.9 million a year ago, with sales growth from truck body and aftermarket more than offsetting declines in our last mile delivery products. Truck body sales in the quarter included \$7.5 million of chassis pass-through revenue. Adjusted EBITDA for the quarter was \$12.5 million versus \$14.5 million a year ago. Adjusted EBITDA margin was 9% of sales compared to 10.6% in the second quarter last year.

As we transition to the second half of the year, the FVS team remains focused on adjusting production to support softer, near-term last mile demand, while driving operational improvements to address ongoing margin challenges. Please turn to Slide 9 for the Specialty Vehicle second quarter results. We are pleased with our SD results, as the business delivered strong, year-over-year profitability growth and record margin performance.

The team also achieved a significant milestone with Isuzu, and we have now delivered more than 100,000 N-Series trucks through our partnership over the last 12 years. Overall, second quarter sales were \$87.6 million, an 8.1% decrease from \$95.3 million in the prior year, driven by a motorhome volume decline. Adjusted EBITDA was \$17.4 million or 19.8% of sales, compared to \$12.9 million or 13.5% of sales in the same period last year.

As we close out the SV comments, we would like to recognize the addition of Jacob Farmer to the Shyft Group as President of our Specialty Vehicles segment. Jacob is a proven operations leader with broad industry experience, and we look forward to benefiting from his contributions. Please turn to Slide 10 for our 2023 outlook. Entering the year, we were cautious regarding our outlook, as there was uncertainty across our key markets, driven by broader economic challenges.

As a result, we responsibly monitored and managed our cost structure to align with expected demand, while continuing to deliver for our customers and focusing on generating cash flow. By the end of June, total headcount was down approximately 25% versus the start of the year, and the team able to drive a solid working capital reduction. However, as we progress through the second quarter, our prior concerns surrounding a challenging demand environment materialized and conditions further deteriorated for last mile delivery vehicles and motorhome chassis.

We saw last mile delivery orders canceled and purchases deferred, ultimately leading to lower second half OEM chassis production. All these factors significantly impacted our volume expectations for the year. Given these factors, our updated outlook for the full year 2023, notwithstanding further changes in the operating environment, is as follows -- sales to be in the range of \$850 million to \$950 million, compared to the previous outlook of \$1 to \$1.2 billion; adjusted EBITDA of \$40 million to \$60 million, compared to the previous outlook of \$70 to \$100 million;

Blue Arc production remains on track, and we currently estimate 50 units to be produced and delivered in 2023, as we take a disciplined approach to our initial production; we also expect to drive positive, incremental cash flow in the year, as we continue to drive down working capital. We will continue to responsibly monitor and manage the business in the second half, while protecting our Blue Arc product launch and maintaining a focus on long-term growth.

Please turn to the capital allocation update on Slide 11. Our balance sheet continues to be a strength and differentiator for the company. And despite a challenging environment, we were able to improve our financial position in the quarter. For the second quarter, we generated \$29.7 million in operating cash flow, reflecting significant improvement over the prior year, as we completed and reduced work in process vehicles.

The company's capital structure remains strong, with a net leverage ratio of approximately 0.6 times, and a \$400 million revolver, which provides us strong access to capital. We are funding organic growth opportunities, including the investment in Blue Arc EV and \$6.5 million in capital expenditures. Before turning it back to Daryl, I want to take a minute to reiterate the financial strength of the company. Over time, Shyft has proven to be a successful cash flow generator. In the last 18 months, we have deployed \$125 million of capital, including \$75 million into organic growth investments that will accelerate growth in the coming years, the largest being Blue Arc.

In addition, we have returned nearly \$50 million to shareholders through dividends and share repurchases during that period. We expect to drive additional, second half cash flow and maintain

our financial strength as we close out the year. We are also confident that Blue Arc will generate positive cash flow in the coming years and provide solid returns on our investment. Overall, we have strong liquidity and are confident in our growth story, giving us the financial flexibility to efficiently deploy capital and maximize shareholder value.

With that, I'll turn the call back to Daryl for closing remarks.

Daryl Adams

Thank you, Jon. Please turn to Slide 12. At the Shyft Group, we have created a compelling industrial growth company, and we remain nimble in response to changing market conditions, while maintaining a long-term, strategic focus. With our financial strength, investment in innovation, and focus on secular growth markets, we have positioned any to be a leader and drive shareholder value over the long term.

Before I conclude, I'd like to acknowledge the recent announcement of my transition and personally thank the investment community for their support and interest in the Shyft Group. I look forward to continuing to lead the company until my successor is in place. Thank you. And with that, operator, we are now ready for the Q&A portion of the call.

QUESTION AND ANSWER

Operator

We will now begin the question-and-answer session. To ask a question, you may press * then 1 on your touch tone phone. If you are using a speaker phone, please pick up your handset before pressing the keys. To withdraw from the question queue, please press * then 2. The first question is from Greg Louis of BTIG. Please go ahead.

Greg Louis

Thank you and good morning, everybody. And thanks for taking my questions. I was hoping to dig a little bit more into the updated guidance, just as kind of -- as kind of we look at the updated revenue, the step down in the revenue. And I realize you were talking about that in some of the prepared remarks, but could you talk a little bit about that step down, in terms of, is that primarily deferrals or any -- or were there any cancellations? And just as -- any kind of color around the types of customers and where that kind of -- in which businesses that would kind of being stepped down in?

Jon Douyard

Thank you and good morning, Ray, this is Jon. I mean, I think when you look at it, and we touched on this in some of the prepared remarks, I think we saw both deferrals and cancellations, from an order perspective. I think, if you look at the midpoint -- and we went from about \$1.1 billion down to the \$900 million, so \$200 million -- I would say it's predominantly within the FVS business. There is a portion that is motorhome, just given the overall dynamics there.

But when you look at FVS, we've talked about there being some noise in the system on dealer inventories, historically, that that seems to have materialized, as we discussed. And really, what we're seeing is in response to that chassis production reduce. And so, as we've had sort of an elevated backlog over the last couple of quarters, we've seen some cancellations, given they haven't been able to match that, from a chassis perspective, and so that's really impacted the outlook in the second half of the year.

I think some of the dynamics that Daryl talked about -- he talked about specific customer dynamics -- there are some -- every customer sort of has their own sort of actions at this point, but we're seeing sort of reorganizations, internally. We've talked about cost actions and CapEx restrictions, historically, with these -- or recently with these customers, as well. And so, there's a bit of a pause as the environment settles and package volumes continue to be down.

And we expect that to continue through at least the end of the year, and potentially even into early next year. And so, again, we've taken sort of a cautious view of what that looks like. But the biggest drivers have been in the FVS business.

Greg Louis

Okay. Great. And thank you for that. And then, you also did allude to some of the, I don't know for -- the cost-cutting and kind of the rightsizing of the business and realizing that this has really only been going on for a brief period of time, with some of the commentary from your customers.

But as we stand here in July, are we kind of where we need to be? Or could we see some other moves to kind of protect margins, just to your comment, Jon, about the lack of visibility, maybe all the way out into early next year?

Jon Douyard

Yeah, I mean I think the -- I think, as we entered the year, we did have a cautious view. So it's not like we've taken immediate cost actions, following some of the late quarter news that we've had. We've been sort of managing the cost structure of the business throughout the first half of the year. And so, I think that's beneficial for us.

We'll continue to be flexible, from a manufacturing perspective, as we always have been. Right now, we're looking at different ways to leverage the capacity that we have, and potentially shift some production in products around to ensure that we're meeting customer expectations and getting the appropriate output. And so we'll continue to do those things, as well as to the extent that there are times when there's no volume, we will certainly flex, from an hourly perspective.

But we feel like we've gotten ahead of this. Not to say that we won't continue to look at, monitor and look at this, going forward, but we feel like we were a bit ahead of it.

Greg Louis

Okay. Good to hear. Thanks for taking my questions. Have a good rest of the day.

Jonathan Douyard

Thanks, Greg.

Daryl Adams

Thanks, Greg.

Operator

The next question is from Mike Shlisky of D.A. Davidson. Please go ahead.

Mike Shlisky

Yes, hi. Good morning, and thanks for taking my questions. The weakness that you've been talking about in the e-commerce world, is that a sector-wide thing? Or is it, maybe, just one or possibly two customers that are causing that right now?

Jon Douyard

I missed the first part of your question, but I think the -- as you look at each -- I mean, there's only a handful of large, parcel customers that are out there. I would say there's specific dynamics with each of them. But I think the themes are consistent across -- I mean, the -- certainly elevated dealer inventories. I think, pat -- if you look at any of the parcel companies right now, they're reporting year-over-year package declines, and certainly, specific reorganizations. And those types of things are attributable to one company.

But I think all of that sort of adds up to a point of pause, from a purchase perspective. And that's really what we're seeing, from -- out in the environment. I think Daryl made the comment earlier, in his remarks -- we continue to have positive discussions with our customers, right? They continue to tell us that there's a need for vehicles. It's just balancing sort of CapEx expectations, in the short term, with how they're managing their fleets over the long term.

And so -- we expect those -- from a demand perspective, we expect that to come together at some point, but it's probably pushed out a little bit. And, could there be some activity later in the year? Potentially. But we think that, again, we want to be somewhat cautious here, over the next couple of quarters.

Mike Shlisky

Okay. Thanks for that. Can you comment on the fleet age for some of your larger final mile customers? Are they still going out -- to outside, third-party light van providers to ensure they have just enough trucks to just meet every day demand -- every day delivery demand? Or is that -- has the EV age caught up to prior levels?

Daryl Adams

Yeah. Mike, this is Daryl. I'm not sure we can give you an exact number on fleet age. But -- to your question about the light trucks -- I think we've mentioned on previous calls, we have a parcel delivery company depot right next to our office here, close to our office. They had a lot of those white trucks. And now those white trucks are now gone. So I think, to John's point and my commentary, right, the package volume is going down, post-COVID.

And those vans were needed, because they couldn't get the vehicles. They got their vehicles. Those vans are gone. So it's -- it's a dynamic environment, trying to figure out exactly what's the right formula. The customers are trying to figure that out. And we're right with them and having conversations. So, to the point of -- that's going to keep coming.

The point is the fleet age and the replacement cycle. And what we're making sure is that our FVS division is ready to take on those orders and flex back up once the volume comes, and that's what we're doing right now, right? Any good manufacturing company will take this opportunity and put some different processes in place to make sure, when it comes back, that they're ready to be more efficient at the time. And that's what we're doing.

Mike Shlisky

Okay. Great. Maybe one last one? Does your 2024 outlook for Blue Arc still appear to be in line? And I guess belatedly, does your, kind of -- you had mentioned a certain run rate you hit in 2025, in Blue Arc -- does that also appear to still be in line? And just a little more detail on people who have been testing the vehicles, what they've been saying, etc., would be really appreciated.

Jon Douyard

Yeah, I think. Daryl made the comments in his EV update. I think the feed -- we've been in field testing now. The vehicle has performed very well. The customer feedback, from the broader team, as well as the drivers, has been fantastic. And so we're really pleased with the progress that we've made there, and we'll continue to execute those types of field tests and demos with customers, going forward.

I think, as you look at where we are, from a production standpoint, we are -- our expectation is that we'll have capacity for up to 1,500 as we get into next year, which will continue to ramp, as we get into 2025. And so certainly, we'll see an acceleration of production and deliveries -- delivery expectations, as we move forward.

Mike Shlisky

Okay. I'll leave it there. Thanks for the time, guys.

Daryl Adams

Thanks, Mike.

Jonathan Douyard

Thanks, Mike.

Operator

The next question is from Matt Koranda of ROTH MKM. Please go ahead.

Ben

Hey, guys, it's Ben (inaudible), on for Matt. As it relates to the guidance, we talked about revenue already and how much is coming out of FVS. And maybe just moving over to adjusted EBITDA. You cut about \$35 million at the midpoint, maybe just to speak to how much is coming from FVS and SV? Is it a similar dynamic? And then just put a finer tune to actions that were taken this year to cut cost.

Daryl Adams

Yeah. I think as you look at it, I think it's more heavily weighted towards the FVS business, but primarily related to the volume decline, as we've talked about. When you look at some of the cost actions that we've taken, we talked about 25, roughly a 25% reduction in headcount through the first half of the year, which we'll continue to flex and adjust, as necessary, to manage the second half.

We've also been managing discretionary programs. I think a key for us is to protect the Blue Arc investment, as we are confident in what that will return here in the future. And so we've been able to manage other investments, from -- whether it's in IT, marketing, go through the functions. And so those are the two biggest pieces. And we'll continue to look at other items as we get into the second half of the year, but those are the key actions.

There hasn't necessarily been any facility consolidation or anything like that. I think the one -- the additional thing that we are doing is looking to leverage the facility and footprint capacity that we have by transferring products, which I talked about earlier, as well.

Ben

Got it. Makes sense. So then, I guess, firing off that, how should we think about the cadence of EBITDA margins in the back half of the year, for both FVS and SV. Do SV margins come down a bit from here? Do FVS margins improve at all? Just a little bit more color here would be helpful.

Daryl Adams

Yeah. I mean, I would expect -- as you think about sort of the quarterly profile, I would expect the second half of the year to be relatively balanced. I think when you look at it from a margin perspective, you probably see a step down in SV, off their record highs in the quarter. And I would say FVS is -- continues to operate where they are, with some of the volume pressures that we have in the second half of the year, offset by the productivity actions that we're looking to drive.

Ben

Got it. That's helpful. Maybe just one more for me -- on the backlog, any line of sight into when demand improves? I know you kind of talked about it a little bit dependent on package volumes. But do we expect more cancellations in the next few quarters? Or do you think we've seen the worst of cancellations and deferrals in 2Q?

Jonathon Douyard

I think, from a cancellation perspective, I think we're probably past the -- probably troughed here in the second quarter. I think, when you look at when the demand comes back, I think there's a couple of variables, one being dealer inventory. I think there needs to be some comfort in what longer -- in what package volume does, or we need to see that start to turn, as well, which may happen here in the second half of the year.

I think -- I point back to Daryl's comments that we continue to have good discussions with customers about the need for vehicles. And so, there's a bit of a pause or a timing shift here that's impacting the second half of the year. But the long term -- the outlook continues to be very solid, from our perspective. And so, we will continue to manage the business through the second half, and do that in an efficient manner and be ready to return to production when it comes back.

Ben

Got it. Makes sense. That's all from me, guys. Thanks.

Daryl Adams

Thank you.

Jonathan Douyard

Thank you.

Operator

The next question is from Felix Boeschen of Raymond James. Please go ahead.

Felix Boeschen

Hey, good morning, everybody. Hey, I was wondering if you have a rough number for us, or a rough bogey on what percent of the FVS backlog today is not tied to parcel customers?

Jon Douyard

I would say that it is probably more balanced than what it has been in the last couple of quarters. I don't have a precise number for you. We can certainly look into that. But we have seen sort of a shift, particularly with the growth in the truck body, sort of that mid-mile business shift away from parcel. So I'd say more balanced than what it has been, historically.

Felix Boeschen

Okay. Okay. And then I going to circle to Blue Arc. And I'm kind of wondering two things. But number one, what's sort of the next milestones that investors should be looking out for, whether that's dealer partnerships, hard orders, more testing with customers? Just maybe if you could help us understand those dynamics better.

And then the 50 vehicles in 4Q, I think when you did the EV day, that number was a little bit higher. Can you maybe talk about what's driving that difference?

Daryl Adams

Yeah, sure. It's Daryl. I think the next milestones you're going to see will probably be some dealer agreements and then the service provider agreement. And then, not sure if we'll have a press release when we roll out the first vehicle or not, but then it'll be getting those vehicles off the end of the line after we complete the training of the operators in the virtual install builds.

So, on the -- the number was higher. And I think we talked about it in the past, I don't remember exactly what form. But one of the brake suppliers that we initially went with had -- wasn't going to have a component, so we needed to go to the current brake supplier, mid-testing. It was a little bit longer. They did both winter and summer. The other one was only doing one battery of testing.

So that pushed it out a little bit, and their certification. So they -- once they get done with the brake testing, they need to certify it internally, and that's the process they're in now. So, what we don't want to do is get the vehicles out there without having that -- all the certifications we need to make sure it's a safe vehicle.

So that was the main (inaudible). And there was a little bit of some battery testing that went on, but that's all behind us now. So it's -- we just want to make sure the vehicle is safe and ready to go for the customer, and we're not going to jeopardize any of that.

Felix Boeschen

Okay. So, you don't think it's a demand-driven thing?

Daryl Adams

No.

Felix Boeschen

Okay. I appreciate that. And then, just my last one -- I was just curious if we could, Jon, maybe compare FVS margins today, implied for 2023, versus levels that you all did in 2019 and 2020, on seemingly a similar revenue base?

I understand, overall, in the corporate P&L, there's heightened R&D spend associated with Blue Arc. But can you maybe talk about some of the margin differentials in FVS, and how we should think about, maybe the back half of the year and into '24, in the context of what you guys used to do?

Jon Douyard

Yeah, I mean I think, as I mentioned, I think the second half of the year looks pretty close to what the second quarter looked like, from an FVS standpoint. When you look at -- I mean, we -- certainly, when volumes were up and parcel delivery vehicles were -- units were high, we delivered significantly higher margins than where we are today. I think, as you look at that shift of the business more towards truck body versus parcel, I think there's a bit of a mixed aspect, from that perspective.

But I think it's also important to note out that we -- there are inefficiencies that continue to get, after experience. And I think if you look at it, part of that is just volume related and the absorption of some of the capacity, which I mentioned, we're looking to fill, to offset some of that. But some of the material issues that have plagued us for over a year, as we go back to rework some of those vehicles, it's created more cost inefficiencies and have been a challenge from that perspective, as well.

And so, there's still a couple of points of margin headwinds that we have, from a -- just an operational perspective that we've -- the team is working to get us through as we get into later in the year, and into 2024. And so, I'd expect margin expansion as we move forward. But I think the -- we'll continue to manage it through the second half of the year, with some further volume challenges and the leverage that that creates, or leverage issues that creates, offset by some of the productivity improvements that we expect.

Felix Boesch

Got it. I appreciate the time this morning.

Jonathan Douyard

Thanks, Felix.

Daryl Adams

Thanks, Felix.

Operator

The next question is from Ryan Sigdahl of Craig-Hallum Capital Group. Please go ahead.

Ryan Sigdahl

Good morning. Ryan on for Steve Dyer. Curious on market share -- you guys commented on SUV and the high horsepower chassis. But on FVS, are you guys seeing any dynamics there, where the share shift moving around, given the current dynamics?

Daryl Adams

Hi, Ryan. This is Daryl. No, it's -- FVS is one of the harder ones, because there isn't really any good data. It's all self-reporting. And I think we've mentioned multiple times in the past, right, it depends on year-over-year orders. But on average, it's -- we don't see any deterioration. It's two suppliers, it's us and Morgan. So it would be -- maybe this year, they get a different order from one customer that we had last year. So it does move around.

But overall, not seeing any deterioration. It's a wide market challenge that's going on right now, with parcel delivery volumes going down. And I think you read that in all of the parcel delivery company commentary that I mentioned during my part of the call.

Jon Douyard

And I think I'd just to add to that. Ryan, I think it's -- as you look at the OEM chassis manufacturer reaction of cutting production for the second half of the year, I think that points to it being more of an industry challenge than a specific company or a market share issue.

Ryan Sigdahl

And then just secondly, any price changes, I guess, where your customers are trying to press for price reductions within the backlog or in future negotiations, which is causing them to kind of pause and cause a stalemate here?

Jon Douyard

Nothing I would say that's impacting, moving forward from an ordering perspective. Certainly a more challenging pricing environment than when -- where we sat 12 months ago. But nothing specific to point out, from that perspective.

Ryan Sigdahl

Last one for me. Just remind me, dealer inventory versus direct business, kind of a mix of how much is in each? And then, how long do you think it will take to normalize the dealer channel inventory?

Jon Douyard

Yeah, I would -- I mean, every -- to Daryl's point, our business is a little bit lumpy, from a customer perspective. But it's relatively balanced between direct -- I'll call it direct and dealer, on the SVF side of the business. Sometimes it's tilted one way or the other. We would expect to see some of that clear through as we get into next year. I think we want -- we don't want to get ahead of ourselves and assume that it's just going to turn around here in the second half of the year.

And so we expect it to be a softer environment here, through at least the next three quarters, three or four quarters, maybe even through mid-next year. So we'll continue to monitor that. Again, I'd point back to the conversations we're having with customers, is that they need vehicles. And so at some point, that's going to break, and we'll see an increased demand. I think we're just in a period of pause.

Ryan Sigdahl

Thanks, guys. Appreciate it.

Jonathan Douyard

Thank you.

Daryl Adams

Thanks, Ryan.

Operator

This concludes our question-and-answer session. I would like to turn the conference back over to Randy Wilson for closing remarks.

CONCLUSION

Randy Wilson

Thank you. I'd like to thank all investors for participating in today's conference call. We look forward to hosting investors in September at the RBC Global Industrials Conference in Las Vegas, The Raymond James Vehicle Technology Day held virtually, and the D.A. Davidson 22nd Annual Diversified Industrials and Service Conference in Nashville. We thank you for your interest in the Shyft Group. And with that, operator, please disconnect the call.