17-Mar-2022

Carrier Global Corp. (CARR)

J.P. Morgan Industrials Conference

Copyright © 2001-2022 FactSet CallStreet, LLC

CORPORATE PARTICIPANTS

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.

Sam Pearlstein
Vice President-Investor Relations, Carrier Global Corp.

OTHER PARTICIPANTS

C. Stephen Tusa
Analyst, JPMorgan Securities LLC

MANAGEMENT DISCUSSION SECTION

C. Stephen Tusa
Analyst, JPMorgan Securities LLC

Everybody, please sit down. Just kidding. So we're great and we're very happy to have up next here, which now starts kind of the HVAC part of the day because we have a train coming in right after this, but we're very happy to have Carrier, Investor Relations Head, Sam Pearlstein, and Chairman and CEO, Dave Gitlin. Dave is going to make a couple introductory comments here. And then we'll roll it into Q&A. Dave?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.

Thank you, Steve. Thanks so much for having us. It's great to be here in person. Just a few slides. A lot of you saw this from our Investor Day a few weeks ago. So I'll go through it quickly so we can get into the Q&A, but just a reminder of some of our key themes.

It starts with why Carrier? We talked about secular trends that are going to drive continued – sustained growth, secular trends like sustainability, indoor air quality. Actually, as I was coming up, the White House and EPA just issued an announcement that they're going to be launching a clean air and buildings challenge. This is coming from the highest levels of government pushing healthy indoor air environments, cold chain, middle class. What these secular trends do is drive increased spend on the ecosystems that we're focused on, buildings and cold chain. And then what we're going to do is drive innovation and digital differentiation to get more than our fair share of that incremental TAM that comes from these secular trends with a key focus on aftermarket growth. We have a strong balance sheet to play offense, and then it results in a financial algorithm of long-term profitable growth with strong cash conversion.

We talked a lot at our Investor Day about differentiation, and it starts with the fact that Carrier starts from a position of strength. We have a channel, a brand – many brands and installed base technology differentiation that really puts us in a great position to go and take more than our fair share of that incremental TAM. And then we have the right investments, the team, the playbook, digital offerings. Especially, you'll hear a lot from us on

Copyright © 2001-2022 FactSet CallStreet, LLC

Abound, it's our digital platform that we use for buildings, Lynx for cold chain to really drive differentiation through digital differentiation in those key two ecosystems to get more than our fair share of that incremental TAM.

And the big theme for Carrier is that we've made a very conscious shift from being an equipment company to a solutions company. And that's why you see on the next slide our big focus on aftermarket growth. Today, we only have 25% of our own aftermarket. That's a crime. That is our aftermarket, and we are going to go after our aftermarket with a vengeance. And you see it growing from $4.5 billion to $7 billion over these next five years, high single digit to the low double digit. It comes with higher margins. We said that our aftermarket margins are 10% higher than the Carrier overall margins. And we're going to use digital differentiation. We're going to use the playbook that is tried and proven in multiple industries, connected devices, driving attachment rate, driving additional coverage, using tiered offerings, working the right arrangements with our suppliers to make sure that we get more than our fair share of the TAM and make sure that we are driving the aftermarket growth that we would expect of ourselves.

We talked a lot about ESG and we use ESG to play offense and to drive it as a growth vector for us. I was reading in the journal yesterday or the day before that in Europe, they import 90% of their gas. 45% of that comes from Russia, and they've launched an initiative to cut their reliance on Russian gas by two-thirds this year. Part of it is through more energy efficiency in buildings. What does that mean for us? That means heat pumps. That means more energy-efficient solutions for HVAC offerings and buildings. It means electric reefer units replacing diesel units for truck trailer. We are the first ones to market with a fully electric truck trailer unit in Europe. It's in 10 different countries and we plan to grow that significantly.

We talked a lot about operational excellence. Taking cost out is in our DNA. We know how to do it. We have a proven track record on this, and we really broke it into two categories. We said that we would be at least price/cost neutral, pushing for price/cost positive this year. And we said that we would drive $1 billion of price increases this year to offset the inflationary headwinds and then we also control the controllables. We said 2% to 3% forever, driving 2% to 3% out of our cost base each year. Now to get 2% to 3% of your total cost base, you have to drive something like 5% or north of 5% of gross productivity in your factories and in your supply chain, and the result is 50 bps of margin expansion a year.

We've made great strides on our balance sheet. As many of when we spun from United Technologies less than two years ago, we had $10 billion of net debt. As we sit here today, we have less than $4 billion. So we have more cash than we need to run the business, which puts us in great position to play offense. You see our priorities on the left, investing in growth, organic and both inorganic. We're building out our pipeline to go play offense on M&A and you see our priorities along the right. A couple other points is that we said we'd do $1.6 billion of buyback this year. Through the end of the first quarter, that number will be something like $750 million. So we have been buying back our shares. We increased our dividend 25% this year. We said that we would pay down $750 million of debt this year.

You may have seen an announcement a couple of days ago from us that we were paying down $1.15 billion. What that is, is we're paying down $1.15 billion, but we're going to issue another $400 million of yen denominated debt as part of our Toshiba acquisition, so the net remains the same. No new news. We're paying down $750 million of debt this year. And the result is an algorithm that we're very pleased with and that we have very high confidence in, 6% to 8% organic sales, top line growth. We talked about 50 bps of margin expansion per year. Last year, we had 80 bps. This year, we've said 75 bps. We think over the long term, we're – it's in that 50 bps range. Double-digit EPS and cash flow equal to net income.

Copyright © 2001-2022 FactSet CallStreet, LLC

And before we get into the Q&A with Mr. Tusa here, just two other comments. One is on the quarter, we had talked about $0.45 of EPS. January and February were a bit better than we had thought they were going to be. But March is always a very important month for us, so we're not spiking the ball, but things were trending a bit better than we had projected coming into the year. The second comment and Steve, maybe you were going to ask this, but I'll perhaps preempt it a bit. But on Russia and the Ukraine, we have no sales or employees in the Ukraine. In Russia, we have 35 employees. It's a very immaterial part of our sales. It's about 0.5% of our sales. We have no tier 1 suppliers there, but of course, our focus right now is supporting our people there, but also the entire situation, of course, is heart wrenching on multiple levels. And we, I think, like so many around the world stand in solidarity with the people of Ukraine, but it is an immaterial part of our business.

So with that, Steve, we'll get into the Q&A.

QUESTION AND ANSWER SECTION

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Great. Thanks, Dave. Just winding back a little bit into the quarter comments. Any parts of the business – I think you – I think Patrick had mentioned residential was doing a little bit better than expected. Maybe some color around what's going better here in the first quarter so far?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

It's probably resi, light commercial.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Okay.

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Resi continues to be strong kind of across the board there and light commercial is just a very encouraging situation between the verticals that we focus on there with K-12 and data centers and so on. Orders are very strong. Our backlog is very strong. Movement from our distributors to our dealers remains very strong. Inventory levels are in check, so light commercial continues to be encouraging.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

I mean, light commercial is, obviously, like blowout numbers in the like last year, I think the second half last year. A very strong – kind of a little bit more magnitude [indiscernible] (00:08:36) magnitude on those so far trending into the first quarter? Is light...

[indiscernible] (00:08:41)

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Copyright © 2001-2022 FactSet CallStreet, LLC

Yeah, because I mean, light commercial was up, I think like 20% plus. So what – on both those, any sense of magnitude of how strong they are in the first quarter so far?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

But what we've said for the year is that light commercial would be up double digits, and we said for the year that resi would be up high single digits, so most of which coming ae from price. And both of those, the volume has been strong just through first two months.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Okay. So obviously stronger than that then for the first couple months?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Yeah, it's been encouraging.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Yeah, okay. You also mentioned in – Patrick mentioned that you guys put through another price increase in March, I think 8% or 9%, across 9%. What's the point in price when you're getting 9% across? Just where was this, was it across all the businesses? Maybe a little more detail on that price increase.

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Well, we're now, I think, on our fifth price increase in resi over the last [indiscernible] (00:09:34) cuts across Fire and Security, which is pushing price. Refrigeration is being – is pushing price, of course. And the 9% was applicable basically for North America HVAC. So it cut across resi, light commercial in North America and the commercial applied business.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Got it. So that is not necessarily the full – that's not going to give you the full $200 million extra?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

No.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Should we should expect another one of these coming in June?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Well, I think all business units are having to drive incremental to hit that incremental 20% and we have to keep an eye on inflation. We continue – it's a very fluid environment, of course. So we continue to watch all of the

Copyright © 2001-2022 FactSet CallStreet, LLC

indicators around inflation. And you expect more price increases out of the other business units, and we'll have to keep an eye on whether further increases are coming.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC

Q

So let's talk about the inflation side. You said $1 billion, I mean, seems like a huge number. Steel was actually trending down. It's moved back up. Maybe it's going to go back down again, I'm not sure. Is there a possibility that that $1 billion is conservatives if steel resumes its kind of downward trajectory or is just the timing of how that all phases in, that's more – that would be more of kind of a 2023 story as opposed to a 2022 story? Maybe just frame the $1 billion and how you're thinking about the variability in that for the year.

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.

A

What I would have told you two months ago is the $1 billion was – we purposely made it a bit on the conservative side. As I sit here today, I don't look at it as conservative. I would describe it as probably a point number. And we were trying to – what we did is we took – the rates that we saw in the 4Q for inflation, that were a bit higher than what we projected coming into the fourth quarter. And we assumed that the inflationary headwinds that we saw in 4Q continue throughout the rest of the year. And we were sort of hoping that, like you said, steel in North America might come down, that could give us a bit of tailwind. And right now, as we look at it, we think those estimates are really right in the middle of the fairway.

We are blocked on around 70%, 80% of copper and aluminum. We have different approaches we take on steel, especially in North America. We have to watch steel in Europe. It's not a huge percent of our steel buy, but it's a percent that we have to watch because of everything going on in Russia and the Ukraine. We watch logistics costs, that's still kind of messy with things going on in China. So the cost of logistics for freight coming from Shanghai to, say, LA is still at elevated levels. So we think it's appropriately calibrated, but we don't think it's conservative.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC

Q

What's your freight as a percentage of cost or sales?

Sam Pearlstein
Vice President-Investor Relations, Carrier Global Corp.

A

We've not shared that.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC

Q

And then labor...

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.

A

[indiscernible] (00:12:26)

C. Stephen Tusa
Analyst, JPMorgan Securities LLC

Q

Copyright © 2001-2022 FactSet CallStreet, LLC

And then labor? [indiscernible] (00:12:29)

Sam Pearlstein A
Vice President-Investor Relations, Carrier Global Corp.

No, no.

C. Stephen Tusa Q
Analyst, JPMorgan Securities LLC

And then labor, you guys talked about that at all?

Sam Pearlstein A
Vice President-Investor Relations, Carrier Global Corp.

I don't think we've given a specific number on that.

C. Stephen Tusa Q
Analyst, JPMorgan Securities LLC

Okay. But I guess these rates of inflation that you're seeing, just in general, is it kind of like a high single-digit type of rate across these cost components?

David L. Gitlin A
Chairman & Chief Executive Officer, Carrier Global Corp.

Well, if you think about $1 billion of inflation on a $20 billion business, you're dealing with 5% or so.

C. Stephen Tusa Q
Analyst, JPMorgan Securities LLC

Yeah.

David L. Gitlin A
Chairman & Chief Executive Officer, Carrier Global Corp.

But our – the good news is that we have shown effectiveness on the price side and multiple price increases, which is not fun for our customers, not fun for us. But it is something that we have to do and we'll continue to do. And we have shown a lot of effectiveness on controlling the controllable. So we said that we'd have $300 million of gross productivity, $100 million of G&A. That's not just a thought. Those are real actions behind it. There's specific targets by function, by area that we have to go dry. We're doing it in a strategic way with low cost COEs. We're driving supply chain, which is tricky in this environment, but we're still working Carrier Alliance and then productivity in our factories, which is encouraging now because COVID-related absences across the world have gotten to pretty close to zero. I mean, we do not have – we have some absenteeism in a couple of our North American factories unrelated to COVID, but – just the general environment. But outside of those couple of factories, absenteeism at very low levels, virtually none related to COVID, which enables us to drive better productivity.

C. Stephen Tusa Q
Analyst, JPMorgan Securities LLC

And then on the kind of purchased component costs, I would assume those are pretty locked for the year. Like you have these long-term contracts and they may be giving you surcharges here and there. But like that stuff, it

Copyright © 2001-2022 FactSet CallStreet, LLC

doesn't – if steel goes down, it's not like Emerson is going to cut its prices on compressors for you until the next round. Is that a fair assumption on the purchased component side?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

We have a mix of suppliers, some under LTA, some that are more on a spot buy. I think where we – we have some level of protections where – even with our blocking positions, where it gets tough, as if you have to buy either electronic components from brokerage market or you have to buy copper or aluminum in the spot market because your volume projections and your volume ends up being higher than what you thought it was going to be.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Right.

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

But we – right now, I will tell you that we watch it like everyone else, but we feel calibrated on our price/cost balance.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Right. But I mean, the – I guess I'm asking like the potential for some relief in the back half of the year on this. The $1 billion of cost is a visible number. That's not a – there's not a significant hedge in that.

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

No. We have – I think we have some detail behind the $1 billion of cost and we have a fair amount of detail behind $1 billion of price and we have a lot of actions behind the $300 million of productivity.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Right. On somewhat related, supply chain, you mentioned having to pay a little bit more to get some electronic components. What are the one or two components that are bugging you these days and relative to maybe a couple months ago, would you say the situation is better, worse, the same when it comes to availability?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

I would say, it's – if it's better, it's marginally better. It's about the same. It's a challenging environment. I would tell you that to a person, super proud of our team because I think that we're managing it as well, if not better than others. But electronic components remain challenging. We're optimistic that the strategic deals we've done directly with the OEMs will help us as we get into the back half. More capacity we're expecting to come online next year. That should provide some relief as we go into next year. But electronic components remain challenging not only for us and the boards that we populate at our facility down in Mexico, but it remains challenging for our Tier 1 suppliers. So we do – we go to great lengths to support our Tier 1 suppliers on the electronic components they need. So generally, we have issues that pop up almost every day, every week. We're managing them and I think the number of issues is getting smaller.

Copyright © 2001-2022 FactSet CallStreet, LLC

C. Stephen Tusa
Analyst, JPMorgan Securities LLC

Q

Got it. Just sticking with the bottom line cost side, this productivity number that you guys put out there, pretty positive. Does that depend on volume or is that something that even in kind of a flat volume environment, there are things you can do to bring – to drive that cost out of the system?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.

A

No, I – I think there is elements of that number that are independent of volume. We're going to drive G&A out of the system independent of volume. Productivity, obviously, you always get a – as you get more load in the factories, that does help you with your absorption. So that is a bit sometimes volume dependent, but supply chain, we got to keep driving. So there's an element that will get independent of volume.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC

Q

Okay. Just jumping into the businesses, you mentioned – you talked a bit about resi, you talked about like commercial. In the large kind of applied market here globally and in the US, what are you seeing on orders so far in the quarter here and how do you see that playing out for the year?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.

A

I would tell you so far, so good. Orders have been strong really across the regions. North American's probably the strongest – not probably, is the strongest in terms of orders. But Europe have been fine with what's going on in Russia and Ukraine, we watch it. Europe is about – it was a higher percentage of our business before we sold Chubb. Now, it's about 25% of our business. But across the board, Europe's been buying especially on the applied side. And frankly, China's been strong. So, we're pleased with orders. You look at some of the leading indicators, like the architectural billing index. You know, Steve, better than anyone that it's been above 50 for about a year now, which is a good six-month leading indicator of commercial construction activity. So I would tell you commercial applied, it's like the rest of our business, order's strong, backlog's strong. Our challenge is just from a supply chain perspective, supporting our customers.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC

Q

And then within kind of the US market for commercial, you can throw light commercial in here as well, what are the verticals? Any change in the leaders or laggards when it's come to the various verticals?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.

A

No, pretty consistent. Data center is very strong. K-12, a lot of pent-up spending and demand there. So we're very encouraged by K-12 commercial buildings starting to come back online. Retail coming back online. So the verticals warehouse has been very strong for us. And frankly, you saw last year we picked up 350 basis points of share in light commercial. Part of it was because I think operationally we could perform. Part of it is that we've gone in a very effective way after some of the bigger national accounts, either on retail or warehousing, and that's served us well.

Copyright © 2001-2022 FactSet CallStreet, LLC

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Got it. So retail and warehousing, you had particular success in taking share. Anything on...

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Data center K-12.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Data centers too?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Yeah.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Feel like everybody is going after the data center market. But you guys feel like [indiscernible] (00:19:33) the market and data centers too...

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

We do.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

on light commercial? Okay. On the services front, maybe just walk through how your strategy – everybody's talking about attachment rates.

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Yeah.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Defined in different ways.

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Yes.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Copyright © 2001-2022 FactSet CallStreet, LLC

Why are you guys best positioned versus – on the commercial HVAC side versus a JCI or a Trane who are going to tout their capability as well?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.

A

Well, what I will tell you is that when we talk about our $4.5 billion and having 25% of our own aftermarket, that's our own aftermarket. So we don't typically compete with some of our OEM peers to get the incremental 75% of that aftermarket that we're going after. I will tell you that having come, Steve, from aerospace a few years ago, there is a playbook to driving aftermarket. And if you miss one piece of the playbook, it doesn't work. So how you deal with your suppliers, how you deal with your customers, how you have tiered offerings, digitally enabled differentiation, connected devices, so you're getting data off of your chillers, so you can use prognostics and diagnostics to drive solutions. There is a whole playbook that Ajay Agrawal working with the BUs that's driving and driving it effectively. So we've said aftermarket double-digits growth this year coming off double-digits last year, attachment rate going. We were at like 19% two years ago. We all define it differently. We all look at it – we don't look at a time material. We have a pretty strict definition for it.

But we – for our 330,000 chillers, we've gone from 19% to 38% and that's going to grow 5% to 10%. So we feel good about attachment rates increasing. We said coverage, total number of chillers growing at least 10,000 units a year, and we're using digital differentiation to drive that customer stickiness and drive them to our elite offerings. So we're very, very encouraged by the aftermarket growth, which is a major, major theme for Carrier. I mean, that is a fundamental theme, which is driving higher margin recurring revenues to dampen any cycles that may happen in any of the businesses.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC

Q

And so what are the mechanics of that? Obviously, that's not maybe all of the new equipment that gets put in any given year, has that connectivity. But 300,000 units sitting out there, what is the mechanical process with which or electronic process with which you go in and enable it to be able to service it effectively at a reasonable margin for you guys and kind of change that business model? Just talk about how that proposal and then execution on that works?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.

A

There's a difference between units coming off the line and what's in the field. Units coming off the line, controller connected coming out of the gates.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC

Q

Yes.

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.

A

The 300,000 that are out on the field, you basically take an edge device, it might look like your smartphone and you attach it to the chiller. Depending on the nature of the chiller it's an hour or two of installation, you now have a connected device. There's other ways to connect devices as well. You may be able to connect a building through other means that then connect the chiller. So not every single chiller needs its own edge device on it. You can put a bound in the system and now you have connected devices. So there's different mechanisms to connect a

Copyright © 2001-2022 FactSet CallStreet, LLC

device. It's inexpensive. It's very – it's an easy installation, even if you do provide an edge device. But then it unleashes data. It creates a connectivity with your end customer and it drives that and...

[indiscernible] (00:23:07)

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

And are they paying for that device? And then you guys – or is that you guys saying, hey, we want to put this in because now we have this contract and we want to...

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Either way. I mean, it depends on the nature of the agreement. We would be fine absorbing that cost for the right LTA. In some cases, they pay for it upfront. It's all about getting the right long-term agreement.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

And then at that stage of the game, how long are you targeting these long term agreements to be? And then what percentage of the installed cost of the machine or the cost of the machine do you get over the life of that contract if you will?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

The cost of installing the devices is not – it's not a huge material piece of the overall revenue that we're...

[indiscernible] (00:23:50)

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Oh, sorry, I meant the cost of the machine, the total machine.

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Oh, yeah. So usually we get 5x to 10x aftermarket revenues from the initial OEM sales. So where you get, the bulk of your revenue stream will be in those aftermarkets. And for the higher end equipment, it can be up to 10x the revenues versus your upfront sale. Typically, say, three to five-year agreements, but once we get an agreement, we have about 90% renewal rates. So the key is, get in, get the equipment connected, get a long-term agreement and then support your customer effectively and usually you'll get a renewal.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Right. And how many of these actual long term – because I know that it's a little bit of a different definition we're working with, maybe today versus three or four years ago. How many of these normal type of contracts would you say you have booked at this stage? Is it in line with the connected?

Copyright © 2001-2022 FactSet CallStreet, LLC

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Yeah. What I will tell you is that if we have 330,000 chillers, we have about 60,000 that are under some form of LTA.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Some form. Okay, got it.

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

And we said we're going to increase that 10,000 a year.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Okay. Got it. So that's kind of the standard that is living with you for four years?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Yeah.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

10% attrition and – that you're going to get – okay. For 25 years?

[indiscernible] (00:25:03)

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Yeah.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

These things sit there for 25...

[indiscernible] (00:25:05)

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Yeah.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Okay. All right. That's a business model, I'm sure you know reasonably well from the aerospace days.

Copyright © 2001-2022 FactSet CallStreet, LLC

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

And it drives me crazy that it's not higher. I mean, I think that the reality is that we now put a phenomenal team in place and there's not a lot of issues that get us much oxygen internally as this one. So this is something that we're going to drive and drive pretty tenaciously.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Why – I have my own views. But why do you think it isn't as high? I mean, obviously, in elevators, it's a way of life and it's a business model. But in commercial HVAC, it's been absolutely the opposite for years, I guess up until maybe 5 to 10 years ago. But why do you think it's so different?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

There's probably a host of reasons, Steve, but what I would tell you is the number one thing right now is just focus. I mean it has to become a part of your business model and focus, and it applies not only to our chillers but it applies – we have 1.8 million reefer units that are out there, transport refrigeration units that are out there that like a tiny percentage are under some form of long-term agreement. That's going to change and that has to change.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Right. On geographically, Europe has come up a lot on the heat pump side. Maybe just clarify, how the resi heat pump opportunity over there, which I think has made a lot of – there's been a lot of news in the last couple weeks around that versus the commercial side because I think they're very different, we're getting a lot of questions about. But maybe how Toshiba helps you on the resi side or what – the difference between the two for the European heat pump opportunity.

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

The European, the resi side is actually a bigger market and we have very little share there. So there is a couple of things that we're doing.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

But that's not different or none of the – to be clear, none of the US OEM? It's not like you're...

[indiscernible] (00:26:59)

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

...fighting against...

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Yeah.

Copyright © 2001-2022 FactSet CallStreet, LLC

C. Stephen Tusa Q
Analyst, JPMorgan Securities LLC

...the US guys and you have a low share. It's more of a geographic kind of global thing.

David L. Gitlin A
Chairman & Chief Executive Officer, Carrier Global Corp.

Yeah.

[indiscernible] (00:27:05)

Sam Pearlstein A
Vice President-Investor Relations, Carrier Global Corp.

It's a Europe thing because in North America, a significant number of our splits are also heat pumps in the residential market.

C. Stephen Tusa Q
Analyst, JPMorgan Securities LLC

Yes. Yeah.

David L. Gitlin A
Chairman & Chief Executive Officer, Carrier Global Corp.

Like 30% in the US and North America. But in Europe, it's a lot of white space, I think, for all of us. So if you look at the resi side, we have a traditional boiler burner company Riello in Italy that has an installed channel with a great potential to really leverage that channel and now we have the technology to really go attack the heat pump space. So we'll leverage Riello. We'll leverage the Toshiba acquisition because that is a sustainability play. Their condensing units going to help us significantly as we go after that residential heat pump market in Europe and then we look at different relationships that we can build with others. But you look at the European market, you have a whole – you have a tremendous opportunity but you have effectively a channel play where the hot water and the heating will come typically from the plumbing section, the air conditioning typically comes from an electrical contractor. How that plays itself out, potentially three for one and providing solutions across those different categories is a real opportunity for us. And we're going to go after...

C. Stephen Tusa Q
Analyst, JPMorgan Securities LLC

Right. And to be clear, that's a kind of a [indiscernible] (00:28:21) market versus a deducted market here in the US, because I think another thing people don't quite understand, very different perspective.

David L. Gitlin A
Chairman & Chief Executive Officer, Carrier Global Corp.

Yes.

C. Stephen Tusa Q
Analyst, JPMorgan Securities LLC

So then on the commercial side, how is it different on the commercial side because that has seemed like an opportunity that's been in front of you guys for the last couple of years. Everybody's generally seeing demand – pretty solid demand there.

Copyright © 2001-2022 FactSet CallStreet, LLC

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Yeah. And we're doing well and we have great technology. So that is more of a traditional technology channel for us. We are very well positioned. We are very confident in our technical offering because we believe and I'm sure that our peers that are going to come in after us would say something similar, but we feel that we have leading edge coefficient of performance technology. So as you transition from traditional chiller boiler to just a heat pump kind of technology that we've been deploying, we think that we have really world-class coefficient of performance, input/output differentiation that is going to withstand the competitive landscape.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

And is that reported through your commercial applied segment or would that be part of kind of global light commercial...

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Commercial applied.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Commercial applied. Yeah. Okay. Any questions out there for Dave? Moving on to resi, just taking a bit of a step back higher level, I think most of the OEMs are kind of punting on, making a [ph] cycle call at this stage of the game and just (00:29:51) take mid-single digits. You had actually a bit more to say than Nelson did. When I asked the question you said, it's still – useful life is still 15 years.

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Yeah.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Maybe just discuss what you guys have...

[indiscernible] (00:30:06)

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Right. You said it was 17 years because it got repaired after 15 years? So...

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Well, I think Chris and I were consistent, but the – well, what I would tell you is that we get this – Steve, we get this question a lot, including from you. And there are a lot of people trying to figure out – doing mathematical models to figure out exactly what's going to happen with the residential cycle and that was happening last year. There were a lot of skeptics that – because two years ago, we had 10% resi growth, they were saying, yes, this

Copyright © 2001-2022 FactSet CallStreet, LLC

year I'm a little bit worried. What happened last year, we grew resi 20%, Carrier was up 15%. We grew our EPS 36% and cash flow was at a 114% of net income.

We said this year resi is going to be up high single digits, of course, the bulk of it from price. But all of the fundamental indicators that we've seen driving the growth that we've seen over the last couple of years, they're still there. There's still – residential, the new construction piece, we had said this year it'd be flattish, maybe there's some upside to that, and you saw what [indiscernible] (00:31:08) said last night and this morning. So some of the indicators – their issue is and our issue is supporting our customers for the homebuilder side. Our – people spending more time at home and maybe that has – that does have an impact on the cycle. It's harder, that impacts the cycle people in the northwest buying air conditioning, didn't use to them. You have more people buying new homes. They do an inspection, it says replace your air conditioning, so maybe that accelerates some of the cycle. And then you have the [indiscernible] (00:31:36) change in 2023, the refrigerant change in 2025. So, there's just a lot of factors that are fundamentally encouraging that don't seem to end this quarter or next quarter.

Movement's generally strong; field inventories are not out of whack; orders – even though the comparison may be a bit down, one quarter or another quarter, but orders remain generally robust. And then keep in mind that it's just over 20% of our total business, so it gets a lot of oxygen, but we talked about driving aftermarket consistently. We talked about F&S being up mid-to-high single digits, refrigeration being up mid to high. We're taking share in applied. Light commercial is very strong. So we get – it's sort of answering the [indiscernible] (00:32:18) what does resi look like in the second quarter of 2026. We don't know. But what I can tell you is a lot of the underlying factors are encouraging.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC

Q

Are you seeing – obviously, with resi outperforming, your orders are growing so far in resi, your data – is there a – are you seeing a quarter here where the comp is going to be so tough that orders will be down?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.

A

Oh yeah. I think they – like I think that as we sit here today, our orders are probably down 5% or so for this part of the quarter versus last year. It doesn't concern us because the orders have been so strong, if you look at our backlog, our backlog is – it is well beyond anything that we've ever seen. So we have very, very strong backlog. What we really watch – and so we're not as much watching the order rates. Orders are very high maybe versus last year, which was exceptionally high. Could the first quarter be down a couple of percent? Sure. But what we're really watching is movement, inventory levels supporting our customers, supporting the right – making sure the right distributors around the country have the right inventory they need to support their dealers. So we put in place a new playbook to make sure that our distributors have what they need when they need it. We are not flawless. I mean we are behind where we need to be operationally, but I can tell you we're going to tremendous lengths to support them and we have a tremendous backlog right now.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC

Q

How are you approaching strategically the 2023 efficiency reg and the 2025 refrigeration regulation? Are you guys kind of taking those one at a time or are you – you don't kind of like a Big Bang approach to the new platforms?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.

A

Copyright © 2001-2022 FactSet CallStreet, LLC

No, one at a time. What I can tell you though is that we – the way we design [indiscernible] (00:33:59) changes for 2023 was with 2025 in mind. So we don't want to implement the 2025 changes prematurely because they do drive a bit of additional cost. As you think about an [indiscernible] (00:34:10) refrigerant and some other things you're going to add to that system to support the 454B refrigerant for 2025. But we've done all the 2023 changes knowing that we're going to add those to it.

And what we're trying to do with 2023 is drive differentiation. It's such – when you're changing 95% of your bill of material which is very unusual versus other industries, we want to drive costs out of the system. We're going from copper to aluminum in many parts of it that we haven't done in the past. We're driving differentiated controls, heat exchanger. So we really wanted to make it a differentiated offering and we've allotted for the 2025 changes in this design.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC

Q

And from the 2022 product to the 2025 product, should we think about the big step-up in the cost, 10% to 15% for the 2023 changeover and then for 2025, it's a little less than that or is it another 10% to 15% kind of step-up?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.

A

We haven't sized the second step but your sizing of the first step is about right.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC

Q

Okay, yeah. That makes sense. Any questions for Dave out there, here we go.

Q

Dave, can you talk a little bit more about how you're going to take that share in aftermarket, because obviously the relationships that already your customers are buying from, so what does it take either organically or inorganically to make those inroads?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.

A

Yeah. When we look at taking a lot of that additional share, what we're doing is driving direct relationship with the customer to have digitally differentiated offerings that really provide them additional value added solutions. So when we go to a building owner and we provide more – we know the product, of course, because we designed it. We – actually, when you now connect the device, we have algorithms to use, things like prognostic and diagnostics and other things that provide some level of differentiation. It may be that in certain parts of the world, we subcontract some of the work, which is fine. We may have different partners in the system that we say you can do the local [ph] wrench (00:36:20) turning or some of the onsite servicing, which can be fine as long as we have the ultimate agreement with the end customer. Does that answer it?

Q

Yeah.

Copyright © 2001-2022 FactSet CallStreet, LLC

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Thank you.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

And I guess what also people don't quite understand is how fragmented the market actually is. So like how many of the 300,000 is being serviced by somebody? How much of that 300,000 is just guys in trucks as opposed to the larger competitors that you'd see that would be better resourced?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Yeah, most of it.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Most of it.

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Yeah.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Yeah. That's another thing that people kind of tend to forget. It's not like JCI came in and took 30% of your...

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

No.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

...of your installed base.

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Not at all. That's why it gives us such confidence that it's there. And back to your question, Steve, why not earlier? Can't really give a phenomenal answer, other than that the opportunity is in front of us and we're going to go after it.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Right. I'm not sure any – I mean, Trane, I think, was one of the first, but that wasn't even until like eight or nine years ago. So it was like a full couple of cycles.

Copyright © 2001-2022 FactSet CallStreet, LLC

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Yeah.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

People didn't really – they left it to the...

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

It's a great opportunity.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

...to the little guys.

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Yeah.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

One last one here just on transport refrigeration. You said very [ph] clearly, at the (00:37:36) Investor Day, you guys took market share. Where and how I mean – I've always viewed this as a very good market for both you guys and I don't see a ton of share shift every year. Where and how did you guys – why did you guys, why were you able to take market share in 2021 and how do you measure that? Is it into certain product line or...?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Well, what I can tell you...

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Where did you see it?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

Well, first of all, container was a great market and container was great for us.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

Yeah.

Copyright © 2001-2022 FactSet CallStreet, LLC

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

When you look at the truck trailer business in North America and Europe, I think again similar to resi, we were able to support our customers generally well, not flawlessly. We had our issues, but I think like everyone in industrial – industrials globally. But I can tell you that I think we benefited operationally and then I think we've done a lot with our customers to provide some level of differentiation. We've introduced new APUs. We've introduced new products with dual controls in different parts of the trailer.

So I think that it's the same playbook we're using in other parts of the business. Investing in R&D – you know, Steve, our R&D went from $400 million two years ago, last year was – in 2019, it was $400 million. Last year, it was $500 million. This year it's probably $40 million or so north of that. So we continue to invest in R&D to drive differentiation and we continue to invest in salespeople and boots on the ground and we continue to invest in digital solutions.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

And how big is the aftermarket and digital and what's the opportunity there on the transport side?

Sam Pearlstein
Vice President-Investor Relations, Carrier Global Corp.
A

Transport still relatively low in terms of the aftermarket. So there is a big opportunity to penetrate that. Right now, it's really mostly parts is our aftermarket there.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

And then lastly, at what point do you make a decision around the commercial refrigeration side? You're – I think you're hell bent on getting margins there. But if it doesn't work out for whatever reason, is that something that you could look to pivot away from at some point in the next 12 months or so?

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

It's something that we'll keep a keen eye on. Our focus right now is heads down, improve the margins. It's not as much focused on growth that we -we have to really improve how we run that business. We will do that and then we'll take stock over time. And if that trajectory is going to continue, then we'll stay at it. If we think it's worth more to someone else, then we'll deal with it.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC
Q

And then just one last one, which I wanted to ask before, but I forgot to ask. Your call on 2023 resi? [ph] My call (00:40:08). Volumes and kind of revenue, I mean...

David L. Gitlin
Chairman & Chief Executive Officer, Carrier Global Corp.
A

We'll get into that later. Yeah, yeah.

Copyright © 2001-2022 FactSet CallStreet, LLC

C. Stephen Tusa

Analyst, JPMorgan Securities LLC

Q

All right. Future.

C. Stephen Tusa

Analyst, JPMorgan Securities LLC

Yeah. Okay, thanks.

David L. Gitlin

Chairman & Chief Executive Officer, Carrier Global Corp.

Thank you, Steve. Appreciate it, guys.

Disclaimer
The information herein is based on sources we believe to be reliable but is not guaranteed by us and does not purport to be a complete or error-free statement or summary of the available data. As such, we do not warrant, endorse or guarantee the completeness, accuracy, integrity, or timeliness of the information. You must evaluate, and bear all risks associated with, the use of any information provided hereunder, including any reliance on the accuracy, completeness, safety or usefulness of such information. This information is not intended to be used as the primary basis of investment decisions. It should not be construed as advice designed to meet the particular investment needs of any investor. This report is published solely for information purposes, and is not to be construed as financial or other advice or as an offer to sell or the solicitation of an offer to buy any security in any state where such an offer or solicitation would be illegal. Any information expressed herein on this date is subject to change without notice. Any opinions or assertions contained in this information do not represent the opinions or beliefs of FactSet CallStreet, LLC. FactSet CallStreet, LLC, or one or more of its employees, including the writer of this report, may have a position in any of the securities discussed herein.

THE INFORMATION PROVIDED TO YOU HEREUNDER IS PROVIDED "AS IS," AND TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, FactSet CallStreet, LLC AND ITS LICENSORS, BUSINESS ASSOCIATES AND SUPPLIERS DISCLAIM ALL WARRANTIES WITH RESPECT TO THE SAME, EXPRESS, IMPLIED AND STATUTORY, INCLUDING WITHOUT LIMITATION ANY IMPLIED WARRANTIES OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE, ACCURACY, COMPLETENESS, AND NON-INFRINGEMENT. TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, NEITHER FACTSET CALLSTREET, LLC NOR ITS OFFICERS, MEMBERS, DIRECTORS, PARTNERS, AFFILIATES, BUSINESS ASSOCIATES, LICENSORS OR SUPPLIERS WILL BE LIABLE FOR ANY INDIRECT, INCIDENTAL, SPECIAL, CONSEQUENTIAL OR PUNITIVE DAMAGES, INCLUDING WITHOUT LIMITATION DAMAGES FOR LOST PROFITS OR REVENUES, GOODWILL, WORK STOPPAGE, SECURITY BREACHES, VIRUSES, COMPUTER FAILURE OR MALFUNCTION, USE, DATA OR OTHER INTANGIBLE LOSSES OR COMMERCIAL DAMAGES, EVEN IF ANY OF SUCH PARTIES IS ADVISED OF THE POSSIBILITY OF SUCH LOSSES, ARISING UNDER OR IN CONNECTION WITH THE INFORMATION PROVIDED HEREIN OR ANY OTHER SUBJECT MATTER HEREOF.

The contents and appearance of this report are Copyrighted FactSet CallStreet, LLC 2022 CallStreet and FactSet CallStreet, LLC are trademarks and service marks of FactSet CallStreet, LLC. All other trademarks mentioned are trademarks of their respective companies. All rights reserved.