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Carrier Global Corp. (CARR)

Goldman Sachs Industrials & Materials Conference

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CORPORATE PARTICIPANTS

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

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Joe Ritchie
Analyst, Goldman Sachs & Co. LLC

MANAGEMENT DISCUSSION SECTION

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC

All right. Looks like we're ready to go with the next afternoon session. Excited to have Carrier here with us today. We've got Chairman and CEO, Dave Gitlin. Sam Pearlstein is also here with us today, Head of Investor Relations.

Dave, I know you have some prepared comments. So, why don't you kick us off?

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

Well, good afternoon, everyone. Joe, thank you so much for having us. Quite briefly, we remain very confident in our ability to outgrow a growing market and to continue to execute despite supply chain and other macro challenges. We proved that last year. We had 15% top line growth last year, 36% adjusted EPS growth last year, and then that continued into the first quarter of this year. You guys saw what we announced couple of weeks ago where sales were up double digits in the first quarter and we expanded our margins by 110 basis points. We remain on track for our full-year guidance of high-single-digit organic sales growth, 75 basis points of margin expansion. And we are absolutely on track to be at least price cost-neutral for this year. Our results year-to-date only give us further confidence in our growth outlook going forward, where we had orders up 10% in the first quarter and our backlog is up 30% versus last year. So, a consistent track record of outperforming proactively addressing the headwinds to deliver market-leading results.

Just a quick reminder, if you look at the slide up here, it's the one side we'll have, but it's a reminder of our key focus areas. It starts with growth. There's a lot that we do control, of course, and that gives us great confidence in outsized growth. The secular trends that we talk about are real. Healthy buildings, we have a pipeline of $850 million of healthy building orders in 1Q. Q1 was up 20% in terms of our orders sequentially. We talk about K-12. Orders were up 50% in the first quarter, the need for healthy indoor environments, whether it's schools or commercial office buildings or retail, is real and we're continuing to see orders for those.

Sustainability, HVAC and cold chain are two of the most critical areas that you can spend on to make a real meaningful impact on climate change. And with air conditioning, it's a self-perpetuating problem, of course,

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because the more air conditioning you have, the more it drives up the Earth temperature, and the more temperature increases that you see in the world, the more demand you have for air conditioning. So the world is undoubtedly getting hotter. The 9 of the hottest years on record have been in the last 10 years. Demand for air conditioning will continue to increase as you see a growing middle-class. There's 3 billion people in the world that live without air conditioning today. So what that means because of this self-perpetuating problem is you need more energy-efficient, low-GWP solutions and we believe that because of our scale, we have more than 4,500 engineers, we have – we spent about this year probably about $550 million on R&D that we can out-innovate to provide the solutions that the planet and our customers need.

Another big theme for Carrier is digital, and we will continue to lean into our two key platforms for our two ecosystems of focus, Abound and Lynx, and we continue to see strong traction on both of those and a major theme for us is continued recurring revenues and aftermarket growth. $4.5 billion of aftermarket growing to $7 billion over the next five years and we continue to see traction in all of our aftermarket initiatives, up high-single digits in the first quarter, you're going to continue to see that increase as the year goes along. And in addition to growth, we continue to drive up margins. We remain on track for $300 million of gross productivity this year. And one area is $100 million of that is G&A. Our G&A is down as an absolute number. Our G&A is down as a percent of sales. Some of you may recall, not talking about SG&A, just G&A, we used to talk about 9%, 9.5% of our sales, this year, close to 7.5% of sales G&A. So, really going aggressively after G&A.

And the last thing I'll mention, Joe, before we get into questions is self-help. We have a very strong balance sheet. We ended Q1 with $3.6 billion in cash plus the free cash flow, of course, that we'll generate this year. So, we're in a strong position to deploy that capital to create shareholder value, whether it's M&A, we will soon be closing on our acquisition of Toshiba's – the HVAC business that Toshiba has, very excited about that acquisition. We'll close that before the end of the third quarter. We've been increasing the dividend this year 25% over last year. And we have $830 million of buyback authorization that we'll complete by the end of this year.

So, Carrier, some of the key themes you'll continue to see quarter after quarter for us, performance culture, execution, growth driven by secular tailwinds, innovation, aftermarket, margin expansion and self-help with a strong balance sheet.

And with that, Joe, we'll get into your questions.

Joe Ritchie

Analyst, Goldman Sachs & Co. LLC

That's great. Yeah. No, thanks. Thanks, Dave. And good slide, Sam.

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QUESTION AND ANSWER SECTION

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC

Q

So, maybe one of the things you didn't mention was China, obviously top of mind for everybody, I know it's about $1.5 billion business for you guys. Just – it's been a couple of weeks since earnings. It's going to be a watch item for everyone. Just – can you provide just an update on how things are progressing there on the ground? I know you mentioned trying to get exclusivity from the Chinese government or exception from the Chinese government. Did that work out, too?

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

A

It did. We've gotten approval to restart. We have four factories in Shanghai, all four are up and running. We don't have 100% of our folks back yet, but they are back. And that's true of the lion's share of our suppliers as well. We have a number of suppliers in the Shanghai area and they're coming back and you're starting to see more of our own people come back and more of our suppliers' folks come back. So, what we sized it up as $100 million timing issue that 2Q into 3Q and that we'll recover by the end of third quarter, perhaps into early for 4Q, we're very confident that that remains the number.

The issue that worries me is not getting our folks back. It's just logistics are still challenging in that Shanghai area, getting parts in and out of our factories. And then of course, the ports are a bit backlogged. So, that's an area that we're focused on. But for us, we're very, very confident. It's a timing issue. I will tell you, Joe, I'm very proud of our team. They will work 24/7 to recover because we try to drive a no excuse culture, which despite whatever happens in the supply chain or things like COVID shutdowns in China, we try not to let that impact us. And the team, I'm very confident, we'll recover quite quickly.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC

Q

That's helpful. And not to focus too much on the near term, but it has been a pretty fluid environment. I'm just curious, is there anything else you want to kind of give us an update on since you reported a couple weeks ago?

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

A

No, we looked at April. Everything consistent with what we've been seeing. Orders were fine, kind of as we looked at it. And the team continues to perform. And it's nice just to get kind of back out on the road. I was in our Collierville, Tennessee, factory yesterday. They're making great progress, really hitting the clip that we need them to perform at every week on a weekly basis. So, output, despite the challenges on supply chain, continues to be where we thought and orders are consistent with what we thought.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC

Q

That's great. I thought it was notable that the comment you made on G&A, right, and the progress you're expecting to make this year, I know you put out a gross productivity target of $300 million. Just help us kind of step through what's embedded in that number, what's driving the kind of acceleration and improvement throughout the rest of the year.

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

The $100 million of that is G&A. And we're being very structured about taking G&A out. We've created this Carrier business services where we have low-cost centers of excellence in places like Monterey for the Americas, Prague for Europe, Hyderabad for parts of Asia-Pacific and Europe, and then we will be adding a fourth one in Shanghai eventually, obviously not the right time to do that. So, we're trying to do it in a very, very structured way that's sustainable. So, very pleased with the progress with G&A with a lot of runway ahead on that.

The biggest thing that's going to move the needle for us is supply chain. If you saw the charts we showed at our Investor Day, our overall cost base of say, $14 billion, 75% supply chain, that's where we really have to continue to make progress and we're being structured on that on how we do dual-sourcing, how we do consolidation with a number of our suppliers. So, that's where I believe we'll see the most traction.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC
Q

That makes sense. You're also investing this year.

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

Yes.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC
Q

There's $100 million in investment. Just elaborate like where is it going, sales force, automation, new products. Just where are you focusing that investment today?

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

Well, we had talked about our investment, it was $300 million over three years, $100 million this year. We had talked about that being sales, G&A – sales, R&D and digital. A lot of our investment in salespeople, we need to let that continue to now mature. So, I don't see a lot of additional investment this year in our sales force. It'll mostly be split between R&D and digital. You think about our R&D, we were spending $400 million in 2019. We continued to increase R&D even through COVID in 2020 and this year, having been at $400 million just in 2019, this year number, it's going to be in that $540 million, $550 million range.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC
Q

And then so just, how do you think about the payback there? And then you mentioned letting that mature. So, beyond 2022, is $100 million like the right placeholder, does that started to come down. How do you think about that?

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

We'll have to see. I mean, we will continue to invest where we see the right payback. We do believe that we are in the midst of an opportunity to really differentiate ourselves on innovation. So, we do like spending in R&D. We're

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very focused on sustainability. We're very, very focused on these digital platforms. So, where we see the right payback, we'll continue to invest.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC

Q

Okay. Price cost, big topic of conversation.

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

A

Yes.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC

Q

I think you guys are expected to kind of basically offset inflation with your pricing actions. I think you were in neutral in the first quarter. Just kind of talk through the dynamics across the businesses because you're running ahead in some, running behind in others, just give us a little bit of flavor for what you expect for the rest of the year.

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

A

I'll tell you that in the first quarter, all three of our segments did better on price than our plan. So, they've all done very well and it gives us confidence for the rest of the year. We came into the year saying that we would have $1 billion of additional price this year and what we had said is that 80% of that was either carryover or became effective on January 1. With the pricing that we've announced in the first quarter, we would get to that $1 billion with no additional pricing announcement. So, we have, very high confidence that we'll get at least to that $1 billion. There's frankly probably upside to that $1 billion. But we also have to keep an eye on inflation. Inflation was a bit higher in the first quarter than we thought. Now, a couple of weeks doesn't make a trend. But we're starting to see a little bit of relief around things like copper and aluminum and steel to some extent. So, we'll watch it.

I think that the good news would be that if we keep price where it is, we don't have any intent to reduce price. So, we will continue to kind of stay out in front of inflation and continue to lean into price and then if we see some relief over time on inflation, that's good news. But we're planning for that to continue to stay at elevated levels. If you look at the segments on price, HVAC was slightly positive, F&S, our Fire & Security business was about neutral, Refrigeration was slightly negative in the first quarter, but they've already taken some aggressive actions that will get them better certainly in 2Q and as the year goes along. So, we've said that we'll be about neutral and we'll see because the pricing has been very encouraging.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC

Q

That's helpful. I want to go back to supply chain for a second, because one of your competitors last week, because of the complexity of their supply chain in North America, particularly, like had a little bit of a shortfall in numbers. And I'm just curious, like as you kind of look at yourself versus let's say joints or controls or a train, can you just maybe kind of parse out like how much of your business is more product versus installation and like just trying to understand, like whether your business is less complex than maybe some others in navigating the supply chain?

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

Well, I don't know, if I may avoid comparing us with some of our peers, because the two words you heard us from our Investor Day are humble and hungry, and we all go through our challenges over time. I can tell you that our supply chain team has been managing this very, very well, and we have been far from flawless. We have our challenges. It's almost every day that there's new supply chain challenges, but we're trying to do a much more structured approach to try to do risk management and get out in front of those problems. So, ships are two-thirds of our problems, come back to chip challenges, whether it's chips that we use to populate our own boards or chips that go into our tier 1 suppliers like motors or compressors or even controls that we buy. So, chips is one of the biggest challenges. We've been meeting with the CEOs of some of our major chip OEMs, there's probably three that we've met with even in the last two weeks. So we're trying to get continuity of supply with our chip OEMs direct rather than through distribution.

We've also been redesigning many of our chips to redesign them around chips that are actually available. So, we will start to redesign and we will procure the chips that we're redesigning towards. We will have 30% of our critical components redesigned, the chips redesigned by the end of the second quarter, 50% by the end of this year. So, it starts to give us more confidence as we get into the second half of this year going into next. But by no means are we out of the woods with supply chain challenges. Most of the supply chain challenges we have, they're not on the installation side for us directly. That's more different partners we may have. For us, it's more around components that we buy. And if we can just start to see some real traction on the chip side, we should see some progress as the second half goes along.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC
Q

Yeah. Super-helpful. So, I'm sure hot topic that you get asked this all the time, the resi HVAC cycle.

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

Yeah.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC
Q

And so, just what's your best guess on how you see that cycle playing out over the next two to three years?

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

What we try to do is talk about what we know and what we don't know. What we do know is that it's 20%, 25% of our sales and we spend an awful lot of time talking about it. And it's a very important part of our business. We love the business. It's high-margin. We've been taking share. We've been performing very well. So, we love that piece of our portfolio. But, I tell you, the amount of oxygen that that topic gets, people think that we are a US residential HVAC business when it is 20%, 25% of our business. If something is 20% and it were to somehow go down 10%, it would affect your total revenues mathematically by 2%. So, that's kind of point number one.

Our aftermarket business, we talked about that being $4.5 billion, aftermarket business, which we've said is going to grow high-single-digit, low-double digits, long term, very well-positioned for great growth in the aftermarket, that's 25% of our business and that's the piece that I want to spend hopefully in the Q&A time talking about, because that's very, very well-positioned for continued growth. Having said that, here's what we see. We have

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never seen the kind of backlogs that we have now. Are some of that backlog pull forward for dealers worried about the supply chain? Surely. I'm sure there's some of that.

But I can tell you there is true demand out there driven by the cycle – driven by the trends that we continue to see. Things like if work-from-home migrates into some kind of hybrid thing, people want higher-end air conditioning in their homes. We continue to see that. When you look at the weather in places like the Northwest where people didn't traditionally buy air conditioning in Seattle, we're starting to see that, people moving South, people buying new homes, continuing to happen. They do the inspection, they say replace the air conditioning. The homebuilders are generally strong right now. So, we're continuing to see that. I know there's anxiety about things like mortgage rates and how that could affect the housing market. We know that we were up 10% two years ago. We were up 20% last year. We were up over 20% in the first quarter. We know we're not going to continue 20% forever and we know we would never say that it can't ever go down. But when we look at it, we see a lot of positivity.

And then in the midst of all this, you see us going to go to a whole new bill of material for 2023, 95% of the BOM, the bill of material changes with the new units coming into 2023, which we've said we're going to price 10% to 15% higher than today's unit. So, you're going to see a complete mix where in the South, where it's state of installation, they'll start to ramp up as we get into July, August to start building up the new 2023 units. Then as you get towards Christmas, the Northern distributors will start buying the products they come in for next year because they'll start distributing those next year. So, you're going to have a mix and you're going to have hopefully a mixing up. And then in 2025, you have the refrigerant change. So, we will see how things play out. But a lot of the underlying factors as we look at them right now remain solid and movement has been where we thought it was going to be and it continued about what we thought in April and we keep a very close eye on inventory levels in the field and those have not gotten away from us, and we expect inventory levels at the end of this year to be in balance. So, we feel solid about where we are today.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC
Q

That was helpful. And I'm going to ask you to call the downturn.

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

No.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC
Q

The...

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

Well, you're presuming a downturn. But anyway, don't get me started, Joe.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC
Q

No, that was good. That was good. Look, I'm actually curious and I know you just talked about the mix up, right, [indiscernible] (00:18:36) products. How does – if we were to go into a downturn, there's a lot of discussion around recession these days...

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

A

Yes.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC

Q

...and like what does the pricing look like in resi HVAC in a downturn? Is it resilient? Do you typically have to get back, like what does it typically look like?

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

A

Our expectation is that we will not get back pricing regardless of what happens with commodities or macroeconomic conditions. We – I will tell you that the team has done a very good job working with our channel appropriately so on pricing. We had much higher realization for pricing in the first quarter than we even had expected. We had said that we were up over 20% in the first quarter, more than half of that from pricing. Pricing was quite sticky in the first quarter. We think that will continue. We said that this year, our volume piece of it would be up low-single digits. Things look like that's continuing to track. So, we'll have to see what happens over time.

We can't predict what's going to happen in the third quarter of next year. But what I can tell you for resi right now is that we're very well-positioned. Our distribution channel is continuing to support us and that relationships across the board have improved the way that's been beneficial both ways. We've been taking share consistently. We're up at least 100 basis points over the last year. So, we will see what the future holds. I know that for some, it presents a cloud, but if it does turn, we can withstand it. But everything we see right now is exactly where we thought it was going to be.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC

Q

By my math, we spent about 20% to 25% of our time talking about this.

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

A

I know. Yes. So, a bit defensive.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC

Q

Yeah. So, I'll ask a question, and then I'm going to open it up to the audience as well.

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

A

Yeah.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC

Q

I'm sure they have questions. The commercial part of the story has been really, really good, right.

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

Yes.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC
Q

And the evolution you've seen in that business and there's lots of different ways we can jump into it. Just talk to us about the health of the applied markets. If you want to throw in some commentary on education stimulus that's finally starting to come through, it seems like with the...

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

Yeah.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC
Q

...50% growth rates you put up this quarter or order rates you put up this quarter. So, maybe just talk to us about the healthy applied.

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

Yes. And thank you for transitioning it for my own health. The – again, we are – we love our resi business, but we are so much worth than that when you look at things like commercial applied, where orders have been really strong, even frankly in the first quarter, orders were strong in China, it slowed a little bit with some of the COVID shutdowns. But other than that one thing over a short period of time, orders were very strong in North America and Europe for commercial applied.

The light commercial business, there is nothing not to like about light commercial right now. We picked up 400 basis points of share in a high-margin business, low inventory levels, orders consistently extremely strong, well beyond what we thought driven by the verticals we talk about like K-12, retail coming back online, pent-up demand. So, light commercial with new product introduction that's helping us take some share as well plus being able to perform and deliver product to our customers. Light commercial, a great, great story, our rooftop units.

Then if you look at the commercial applied, the trends that we talk about are truly real. I mean, we are seeing demand for healthy building orders. I mentioned $850 million backlog. When you look at things like sustainability and we meet with customers, they're looking at now our new digital platform like Abound and they're looking at more innovative solutions around sustainability. So, very positive trends there. And the other two businesses that don't get, I think enough talk about is our controls business, very well-positioned. It's a high-margin business for us that's been growing consistently double digits. Our ALC controls business, great technology, great team performing well, and our aftermarket business is continuing to see very, very strong growth and we're confident that'll continue.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC
Q

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Okay. I'll open to questions from the audience. Anybody have a question? Happy to keep going. So, let's keep going. So, let's just go on the light commercial piece of the business. What – if you had to point to one or two things that's helping you take share in that market, what would you point to?

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

Operations. The fact that we've been able to support our customers and that we've also – we've been able – just it's very similar to our residential business where we've converted some key customers, some key scale customers to Carrier, partly because we had the product available, partly because we've been investing in the product line, some new innovations that drive some energy efficiency. And part of it is just this customer stickiness that has been a big theme for Carrier when we spun, which is that we'd become externally focused, we'd focus on growth, we'd focus on really getting some scale customers and that's worked.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC
Q

Makes sense. And then, you wanted to talk about aftermarket, so I'm going to give you a chance.

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

Yes. Thank you.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC
Q

Right. High-single-digit growth rate, so really great growth rates, stickiness, you're improving your attachment rates. Again, just similar line of questioning, how are you doing it on the aftermarket side of the business, how do you think about the opportunity?

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

The way we think about aftermarket is it's a complete playbook. If you don't do any part of the playbook, it's not going to be successful. So, we look at our supplier arrangements. We look at how we're dealing with the customer relationships in terms of the LTAs. So, how do we provide a tiered offering to them that we drive them to – we have a base agreement, an enhanced solution, then a lease agreement with our customers, which is a full offering, digitally enabled. So now, you're dealing with a top tier, digitally enabled BluEdge offering where they're getting prognostics, they're getting diagnostics, they're getting real-time information on things like sustainability.

If you picture one customer with facilities all around the world in a single pane of glass, they could see how are my emissions for all of my factories. And if one, say, the facilities in India have higher emissions, are there solutions we can provide to get those in check with maybe their facilities elsewhere in the world. So, it's really a holistic agreement that our Head of Aftermarket who did come from aerospace, Ajay Agrawal who knows the playbook there, has applied it with equal effectiveness here with the BUs working together, we've added talent, we've added focus, we've added a playbook, we've added a toolkit for our salespeople, and it's working.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC
Q

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So, when I think about aftermarket, it's interesting, we started having a discussion on the resi side earlier talking about the commercial side now. When I think about it, I normally just think about your applied business. I think about that's where the lot of the opportunity is. But I'm curious like across your portfolio, do you see a lot of opportunity across Fire & Security or whether it's your transport business.

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

A

100%. We often use some of the metrics from our chiller business almost as microcosms of the capabilities that exist across the portfolio where we talk about things like attachment rates with chillers and we talk about our total coverage, 60,000 chillers under coverage going to 70,000 this year on our way to 130,000 chillers covered by some kind of LTA over the next five years. But those same trends exist with transport refrigeration. I mean, remember, we have 1.8 million refrigeration units that are somewhere out there in the world, truck trailer units or container units that are in need of being connected, the same kind of edge device that we'll use to connect our chillers, we will use an edge device to connect our reefer units that are all out there. Once they're connected, you can now provide more value-added solutions to your truck trailer customers, whether it's remote diagnostics, prognostics, geofencing. Now you're starting to get into our Lynx platform where we can say, was the cab of the trailer left open, which would obviously lead to an excursion. So, it applies there. By the way, it applies to our Fire & Security business where it's not only additional parts, but it's also digitally enabled solutions.

So if you think about our Supra business, now, if you go buy a home in the United States, that little locks, we have huge market share of the little locks, but now there's data which can tell you how often did the person come back to look at the home, how long did they stay. That's great information for the agents and the brokers selling the homes. Now, we bought a company BrokerBay that can give you calendarization of their value-add. All of that is lifecycle-type revenue stream. So, the big theme for Carrier is switching from being an equipment provider to a long-term solutions provider and that is really important in any kind of environment but where there are questions about like you were asking before about resi or other things to provide lifecycle solutions is very thematic for us.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC

Q

And I'm interested in terms of the contracts that you sign, are they typically annual contracts like the environment that we're in right now, what kind of price escalators do have or do you sometimes have to wait to, I don't know if you go back and actually re-price, but you have to wait till they roll to price those contracts, just any commentary around that would be helpful?

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

A

We – if in our aftermarket, when we talk about coverage, we're usually looking at three- to five-year type deals and we've been very cognizant of the fact that we cannot lock ourselves into pricing that don't have some form of escalation associated with inflation. So, that's been something that we've had very much aligned across the enterprises that we have to have escalation provisions around inflation.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC

Q

You announced the Toshiba deal recently. It sounded like you were much more bullish around like the resi HVAC opportunity in Europe, the heat pump side. So, maybe provide a little bit of color and what the opportunity is.

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

A

Well we – today, we're I would call us almost a non-influential player in resi heat pump market in Europe. We are number one in commercial heat pumps in Europe. We have great technology, great channel, great positioning, and we continue to grow. We grew a lot in the first quarter and we'll continue to see that to grow. We're very, very focused on residential heat pumps in Europe. Now, with the acquisition of Toshiba, you now have effectively heat pump capability for that European residential market. We have somewhat of a channel with our Riello business that does wall hung boilers for parts of Italy and elsewhere. So, we can use some of that channel to get in with heat pump capability that we can do organically through our own investments. We've announced the heat pump center of excellence for some of the design with the Toshiba technology, and we're also looking at other ways to accelerate growth in that, what's a market that's just going to clearly continue to grow.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC

Q

That's helpful. I'll go back to the audience again to see if there're any questions. None. I'll keep going. Looks like I'll keep going.

Okay. So, we've been talking about M&A.I think you mentioned on the call couple of weeks ago that like you could do north of $1 billion deal. So I'm just curious, like, what's the pipeline look like right now and where're you looking to kind of add to your portfolio?

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

A

We've spent a lot of time building up the pipeline. Like, as I said, when we look at capital deployment, our top priority is growth, whether it's organic or inorganic. We have plenty of firepower. We're increasing the dividend. We've been leaning into buyback especially recently with the stock being where it is. So, we've been doing a lot. You saw the buyback we did in the first quarter and that we'll continue to do buyback as the year goes along. But M&A is a real opportunity for us. And we laid out at our Investor Day our top five themes, but we always want to make sure that we're focused on sustainability, digital, we want things with an aftermarket. So, we're looking globally. We like balance in our portfolio. That's been a big theme for us. Is that so we're not overexposed to any one geographic area, any one vertical, any one business unit. So, we like balance, but clearly sustainability is going to be an area that we focus on.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC

Q

Yeah. And on the portfolio, the addition by subtraction has been certainly a theme that has played out for you guys over the last couple of years, and just solve a bunch of JVs. I'm just curious, like, how are you thinking about potential divesture candidates within the portfolio today.

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

A

Well, we – on the JV side, we did say that we had a number of sub-optimized JVs, which one of our big themes at Carrier has also been focus. We have management going in different directions, so we got to focus on our priorities. And if you have a JV that takes up management time that's not really adding value, we're not going to stay in it. So, we went from 40 minority JVs down to 32. This year it could end around 30, we'll have to see, but we've gotten rid of some of the more obvious ones.

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And then in terms of divestitures, we've said that forever. We will always be very objective and clinical as we look at our portfolio. And we have certain expectations, we have certain growth expectations. We said that we grow our top line 6% to 8%. We get 50 bps of margin expansion a year. We don't want businesses that are consistently in the single-digit ROS range. So, things like our CCR business, we've said that we're going to fix it, because right now it's our drag on our overall ROS. But Tim White and the team, heads down, really doing the right things to raise prices, reduce costs, take out G&A, reduce the number of SKUs that we have as part of our offerings, really improve that business and then we'll take stock. We'll either continue to see margin growth, continue to see EBIT growth or we'll reassess it. But for right now, that's an area that we really have to improve upon because it's one area that pulls down our overall margins.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC
Q

Yeah. Makes sense. You talked about healthy buildings earlier, $850 million, I think it's up 20%. I'm curious, like as you think about the opportunity, how much of what you're seeing is here in the US versus international and how are you thinking about the healthy building opportunity?

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

We're seeing a lot of interest globally. You mentioned K-12. That's – if I just take the United States, there has been and this is something that I don't know if everyone realizes, but there's been $190 billion allocated to K-12. This is a vertical that has been starved of cash for so long, starved of investments where you see teachers buying crayons for the students. Now, they have $190 billion and it's in three tranches, these three ESSER funds that they call. $120 billion of the $190 billion is in ESSER III which they've just started allocating. And that's the most that's going to go towards more systematic structural changes, things like where we play, which is upgrades to the HVAC systems and they are focused on sustainability and healthy, that is a major theme. And it's not only because of avoiding the spread of airborne illnesses like COVID, but 1 in 13 kids in school have asthma and it's been proven that if you have better ventilation, you reduce the buildup of CO2 in the classroom and they test better. So, it helps on so many levels and schools are really aware of that. So, we're seeing nice traction in K-12.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC
Q

Actually curious on that point, like what are you doing to help educate the person or people that are making those decisions to put that – those dollars to work on capital outlays and energy-efficient HVAC as opposed to...

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

Yeah.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC
Q

...the variety of different places they could put it.

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

Well, we've been doing a series of seminars with that community throughout the nation and we have folks like Joe Allen who's really probably the most respected expert in the area from Harvard University supporting us to help us

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educate that community on some of these benefits and we've gotten a lot of interest from those. And then, of course, our sales folks with feet on the street are really doing a nice job of making sure they educate our customers.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC

Q

So, remember when the stimulus measures first got announced, there was a view that maybe it would start in 2021, you'd really start to get significant funds in 2022, and then a spillover effect into 2023. It sounds to me like we're still way earlier than that in terms of the funds actually getting released and spent. Is that a fair assessment and...

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

A

Yes.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC

Q

...how do you see that playing out over the next few years?

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

A

What I would say is it's migrating from point solutions to more structural solutions. So, I think when some of the schools and others first got funding, they started buying our OptiClean unit, which by the way we innovated in like three weeks and now we've sold over 40,000 of them. So, that is a point solution where you put a unit, say, in the corner of a room like this. Now, what they're looking is for more holistic solutions. And as that ESSER III funding becomes available, you're going to see higher ticket items.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC

Q

Got you.

Joe Ritchie
Analyst, Goldman Sachs & Co. LLC

All right. Well, we're coming up to the end. So, I'm going to turn it back to you. I don't know if there's any closing comments you want to make and leave the rest of the audience with.

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

No. Joe, first of all, thank you. Thanks for having us here today. Look, we are very, very excited about the journey we're on. I think that we've established, as I said, upfront, a performance culture of a team that we face the same challenges that industrial companies are facing all over the world. And though it's far from flawless, the team continues to perform for our customers with no surprises for our shareholders. So, we've created an execution culture. We continue to lean in growth. The secular trends are very, very encouraging, and we're seeing the orders result from that. We have a balanced portfolio. We're taking cost out to drive margin expansion. And as I said upfront, we have these self-help capabilities with the balance sheet that provide a lot of opportunity for our

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customers and our shareholders. So, we're very happy with where we are in the year. We're very optimistic as we look forward through the rest of this year and then beyond.

So, thank you, Joe, for having us.

Joe Ritchie

Analyst, Goldman Sachs & Co. LLC

Dave, thanks for coming.

David L. Gitlin

Chairman & Chief Executive Officer, Carrier Global Corp.

Appreciate it. Thanks.

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