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Carrier Global Corp. (CARR)

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MANAGEMENT DISCUSSION SECTION

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Good morning. My name is Brendan Luecke, and I'm the multi-industrials analyst at Bernstein. I'm joined today by David Gitlin, CEO and Chairman of Carrier. David has led Carrier since 2019, through the firm's separation from UTC and an ongoing portfolio transformation. It's a very exciting time for Carrier. Thank you so much for joining us this year.

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

Thank you.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

I believe you got some opening comments.

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

I do. Thanks, Brendan. Well, thank you, Brendan. Thanks to Bernstein for having us. A few quick updates before we get into the Q&A. We have three priorities right now at Carrier: best-in-class execution on the core business, successfully closing and integrating with Viessmann Climate Solutions, and successfully completing the business exits of Fire & Security and Commercial Refrigeration.

On the core business, the team continues to execute well. Aftermarket sales were up in the high teens in the first quarter. We expect a pickup in price/cost benefits starting in Q2 and target another year of strong productivity, which helps funds growth and – helps fund growth investments. In addition, the integration of Toshiba TCC acquisition is going very well with cost synergies and financial performance running ahead of expectations.

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In terms of Viessmann, I just returned from two days in Germany, and I could not be more excited about this combination, which is undoubtedly revolutionary. The more we see, the more we like. We know – we knew from all of our research studying the company over a period of time, and we've studied the market, that Viessmann was the best-positioned company in the fastest-growing market globally in our space.

What we witnessed over the past couple of days was the deeply impressive people and culture, 11,000 team members with the encouragement to dream and think big. And with the support of Max Viessmann and Thomas Heim and their leadership, to give them the empowerment and the space to execute very big ideas. It's the only company globally with end-to-end home energy management solutions, and they are superbly positioned for extended best-in-class growth.

And then in terms of our business exits, we have received a significant number of inbounds for these premier assets, which gives us great confidence in the multiples. We've been very clear that our priorities for these business exits are: number one, a clean exit; two is maximize net proceeds; and three is speed. We expect to be in the market with Commercial Refrigeration, Security, and parts of our Fire business in the late summer of 2023.

Commercial Refrigeration is a fairly straightforward sale process. As we shared with you before, the business we're selling generates about $1.1 billion in sales with high single-digit adjusted EBITDA margins. We expect the 2023 adjusted EBITDA margin exit rate to be higher, given the cost reduction actions that we're taking in that business.

The businesses that we plan to exit with Fire & Security represent about $3.1 billion in sales from last year with high teens EBITDA margins. The most likely scenario is that we sell security separate from Fire. Fire consists mainly of three business areas: Commercial, Industrial, and Residential. We expect to market at least part of the Fire business in the late summer, along with Security and our Commercial Refrigeration business at about the same time, but obviously separate from one another; and then sell or spin the remainder of Fire soon thereafter.

Given the margins growth, technology, and unique positioning of these segments, we are not surprised with the significant level of inbounds that we have received. We have dedicated teams working to complete the internal prep work in the next couple months so we can initiate our formal process with prospective buyers.

And last word on KFI, following KFI's recent decision, this is Kidde-Fenwal, Inc.'s recent decision to file for Chapter 11. We have now deconsolidated KFI. This means our Q2 results will see a couple hundred million dollar write-off of our investment in KFI, including the $130 million or so of cash held at KFI. Any write-downs will be excluded from adjusted earnings. KFI would have represented about $200 million in sales and about $0.03 to $0.04 of adjusted EPS in 2023.

And while we have all hands on deck to complete the purchase in combination with Viessmann and the business exit, we have more than 99% of our 53,000 team members' heads down focused on executing for our customers for 2023 and beyond.

And with that, Brendan, let's get into the Q&A.

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QUESTION AND ANSWER SECTION

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Fantastic. Thank you so much. For our audience members, we are taking questions via Pigeonhole. I'll try to weave them into the discussion as we go. So, feel free and enter them, and we'll try to [ph] discuss (00:04:53) as well.

So, thanks again for joining us this year, Dave. Very excited. I usually like to take a long look, and we start with a quick look-back. So, it's been an eventful few years for Carrier. I guess why don't we start with pandemic?

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

A

Yeah.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Get that out of the way. It's almost over. But we are still working through some of the economic aftereffects. I thought Carrier handled it quite gracefully, even when public, during a time of remarkable uncertainty. Looking back, what are your key learnings from the pandemic and how does it inform your thinking about the business going forward?

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

A

Well, I was so proud of how our team handled it. If you put it in perspective, we spun in April of 2020. So, when we stood on the New York Stock Exchange in February of 2020, at that point, we thought COVID was sort of isolated to China. And then you fast forward to April of 2020, we spun with $11 billion of debt, $1 billion of cash, so $10 billion of net debt. And our first quarter as a public company, our sales were down 25%. So – and we had a leverage ratio that was a bit higher than 3.5.

And what happened was, I think, very profound and really game-changing for us as a team and as a company where I think we went from a team of leaders to a leadership team doing daily calls seven days a week and really focused on our customers, our people, and making sure that we could deliver on the commitments that we had made for the Street. And what ended up happening is that the business turned out to be better than we thought it was going to be in 2020. We really leaned into things like cost reduction, and we surpassed the expectations we had set, we called Carrier 700. We started with Carrier 600, $600 million of cost reduction over a few years. We changed it to Carrier 700. We exceeded that.

We said that we were going to change our focus from – our aftermarket have been growing 1% to 3% a year. We said we want that to grow double digits forever, and we've been growing double digits every year since. We said that we wanted to invest in growth and be best-in-class in growth. And we said that we wanted to reduce – improve our balance sheet and overall be very focused on our capital allocation.

And if you fast-forward, we went from $10 billion in net debt when we spun to $5 billion in net debt. Our leverage ratio went from higher than 3.5 to under 2. And we've shown as a team that we can execute no matter what gets

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thrown our way. It started with [ph] coal (00:07:23), but it went to supply chain. And that's what gives us great confidence as we kind of fast-forward to today.

Yes. After we closed on the combination with Viessmann, our leverage ratio goes back to that 3.5 range. But we've said it would get back to that 2 range within a couple years. And given that we were able to do that through some of the most challenging times in many people's history, I have confidence that we'll be able to achieve that as well.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Well, it must be great to be coming out of the crucible.

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

A

Yes.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Now, a lot has happened since. So, coming out of the spin, you moved very quickly to transform the portfolio. I'd love to understand that thought process. Why did you take it where you did? How did you come to the decision? How did you think about pacing it?

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

A

Well, if you look at the last couple of years of our strategy reviews with our board, we found that focus really matters. And we spent a lot of time thinking about secular trends and our North Star and our focus as a company. And we have concluded that our North Star will be to be the world leader in intelligent climate and energy solutions when we meet with customers.

And by the way, when we talk about scale customers, we're now in the CEO office. We might have in the past been in charge meeting with the head of facilities for the Southeast region of the United States. We're now at a CEO level looking at digital platforms, their entire footprint. And what matters to them most is energy efficiency, whether it's a move to lower GWP refrigerants, more energy-efficient equipment, a shift from fossil fuel to electric heating.

What we know is the most compelling secular trend is this continuous shift towards more climate friendly solutions. And we know that many of our customers have made commitments around ESG and other net zero commitments that they need help to achieve, and that's exactly what we do as a company. So we said, look, that's our North Star.

The first piece of it is that we have gained a very good position globally in really every key market. One of the key gaps we had was variable refrigerant flow technology in Asia; and we purchased Toshiba's business, which probably has the best-in-class technology in that area. And we completed that acquisition a year or so ago. And then that left one critical market, which is the most attractive market because of the energy transition that's happening in Europe, is the residential heating space in Europe. So, we went and we met with virtually every single company because we knew that the market is above 4x the size of the commercial market. We're very well-

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positioned, of course, in the commercial space in Europe. We're number one in heat pumps in Europe for the commercial side. But we basically have no presence on the residential side.

And after meeting with virtually everyone, it was clear from our consultant studies that we had done, our own studies, talking to everyone in the industry that we had to get into the market given the growth rates that every company is seeing over there. And we wanted to combine with beachfront property, the real premier company in all of Europe, and that's Viessmann. Viessmann Climate Solutions, virtually no matter who you talk to, always comes up on top in terms of having the best channel direct to installers that have the best product portfolio, the best technology end-to-end solutions.

So we said, look, from a portfolio perspective, we now have focus. We know that we want to combine. We were very fortunate to be able to come to a combination with Viessmann, which will close towards the end of this year. And then we said that as good as these businesses are, stationary refrigeration business primarily in Europe and our Fire & Security business; Fire & Security, very high gross margins, great businesses, great brands, great product positioning; we felt that we as a company would benefit from focus. We will take those proceeds, we'll pay down debt, we'll do a buyback at least to offset the $2.6 billion that we're issuing as part of the purchase price, and then we'll continue to focus on our core.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC
Q

You've been busy.

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

I'll tell you, it's been exciting busy, though. I think what we're doing as a company, many companies are – they kind of evolved their portfolios.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC
Q

Yeah.

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

I believe this is truly revolutionary. And I think that when all is said and done, there won't be any company like us in the world.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC
Q

Yeah.

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

We will be the – I'm sorry.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC
Q

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No, please, please.

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

No. We'll be the only company – if you look at where the puck is going with home energy management solutions, we will be the only company, us and Viessmann Climate Solutions, that has the capability to connect the dots between solar PV, battery, heat pumps, and a unifying digital tool that interfaces with utilities that provides true home energy management solutions.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC
Q

Yeah. That was my next question, actually.

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

Yeah.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC
Q

I was taken aback when I saw the breadth of your residential energy solutions offer via Viessmann. I mean, you're going to be literally bumping up against folks like Tesla and Enphase. I never thought I'd see Carrier there. As the sandbox moved, are you playing in a different space? Where do you see the boundaries there?

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

Yeah. If you think about the future, everyone is going to get home from work. They're going to be plugging in their electric vehicles. They're going to be turning on their air conditioning or heating, both of which will be electric, whether it's – a heat pump obviously does both cooling and heating. They're going to be starting to turn on some of their appliances in the home. God bless you. And you're going to be putting max demand on the grid between, say, 6:00 and 10:00 PM.

So, as you think about how to provide true energy efficiency savings and the transition, the energy that's happening globally from fossil fuel to electric in the home, in buildings, the same transition that's happening in automotive, you're no longer going to be differentiating yourself by saying that I have a better heat pump than my peers. You're going to be differentiating yourself based on solutions, the solutions to our commercial customers and our homeowner customers.

And to provide real solutions, you need to be able to connect the dots, not only between the comprehensive offerings, but also as you start thinking about interfacing with the utility. So, 100% the competitive landscape is changing, and we can either stand by and watch it change before our eyes or we can lead in that transition, and we chose to lead.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC
Q

So, do you feel that this solutions approach fundamentally advantages you versus other, say, residential HVAC players?

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

100%. And, look, I got to see it. I just – as I mentioned, I spent the last couple of days in Allendorf, Germany with Max Viessmann and Thomas Heim and the team. And a number of Viessmann – they call them family members, but team members, colleagues, were showing me their app, their One Base app, where they've now implemented solar PV and batteries and heat pump with this unifying digital capability on their smartphone. And they could watch. They – capacity, both their backup battery system, their main battery system. They could look at whether they were returning energy back to the grid. They could look at the utilization.

One of the guys that were showing me was upset that whomever was home was running the dishwasher. And I was like, well, maybe they want clean dishes. But they can monitor all of this real time and that is going to be the future.

So, Viessmann way out in front and leading on being able to provide this end-to-end solution. And now if you look at our brands, our channel, our capability to bring some of those end-to-end solutions, whether it's to North America, United States, or Canada or to Saudi or to India or to China, I think that we'll be very uniquely positioned to scale those solutions globally.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC
Q

So, how quickly do you think that journey happens? And what type of what type of difference do you see across geographies?

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

Well, it's happening real time in Europe. Viessmann is the first to be able to provide those solutions in Europe. And some of the technology lends itself because in Europe, you're also dealing with sanitary hot water as well because in Europe you're dealing with air to water systems.

So, they're really connecting the dots between not only that, solar PV, battery, heat pump, the digital overlay and sanitary hot water, but they're doing it in Germany and in various parts of Europe. And they – not only are they only for their battery system, they buy the cell, but they're actually – they're completely assembling the entire battery system in a very, very cost competitive, but also effective way where they come up with these modular concepts where you can customize the capacity needs for the different homes.

Then as you think about expanding these end-to-end-to-end solutions, there's people that do solar PV and battery. There's people that do heat pump and battery. There's no one that does all of the systems today with the combined digital overlay, and I think there's some channel complexities you have to work through. There are some ecosystem complexities as you think about interfacing perhaps with utilities on a neighborhood basis. But I think it's coming over these next couple of years, and we want to be out and front-leading the way there.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC
Q

Is there a dependence on a particular structure for the utility market? And Europe tends to be more vertically integrated. The US is in various phases of unbundling and deregulation, depending on where you sit. Does that help or hurt you?

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

I think it's a reality. I think that whoever's coming up with these end-to-end solutions, there will be an interplay with the utilities spread throughout the United States. And I think we'll be very well-positioned to come up with the right win-win arrangements with the utilities.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC
Q

Very good. So, I love to talk about heat pump specifically.

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

Yes.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC
Q

I think of heat pumps as somewhat of a substitute for HVAC. Does the growth baked into this deal in your mind? Does that depend on replacing HVAC systems before end of life or are these all net new sales?

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

Well, if you think about what's happening in Europe, there are 17 countries in Europe that have either announced or implemented bans on fossil fuel heating. So, if you think about a typical home today, it either has a coal-powered, oil-powered, or gas-powered wall-hung boiler on your wall, either in your utility room or your bathroom. Those are being banned and replaced with heat pumps.

So, why do you have de facto significant hyper-growth for as far as the eye can see? It's because you sell a heat pump for 3 to 4x what you sell a boiler for. So, as you see regulation – and regulations may move around. There's regulation in Germany now. There's a debate – it's not a debate on whether it will get implemented, banning fossil boilers, it's just a question of when. And that's okay. It's okay whether it gets implemented in January of next year or January of the following year. It really – what you look at is the long-term trend around this transition from boilers to heat pumps and you mix up by 3 to 4x. So, that de facto will happen throughout Europe, and that's what's driving this sort of unprecedented, sustainable, predictable hyper-growth throughout Europe.

And if you think about Europe, it has, say, 200 million homes. Today, about 8.5 million homes have heat pumps. So, call that 4%. So, when you think about sustained growth, we have said that the number of heat pumps sold in Europe is going to go from about 1 million heat pumps last year to about 10 million in 2030. So, that 20% CAGR or so between now and 2030, that would get you in 2030 to about 40 million homes having heat pumps. But that means only 40 million out of 200 million. Now you're talking about 20%. So, what's going to be a de facto transition from fossil fuel to electric heating, even if you get to 20%, you still have hyper-growth for as far as the eye can see. And that's why it's such a unique marketplace, very difficult to break into.

And I cannot tell you, leaving Germany last night, how energized I was that this is – you can study a company. You can see how great their channel and technology and positioning. They're in Germany and Italy and France and Poland. They're in great countries. They have a phenomenal moat because of this unique relationship, direct-to-installer relationship. But to really be able to see people in action in a culture that not only facilitates

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entrepreneurialism, but encourages it and empowers it and creates space for them to go think big and then implement it, this is a phenomenal company unlike anything I've ever seen.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Excellent.

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

A

Yeah.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

So, you mentioned the 3 to 4x uplift. What does the services side look like?

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

A

Well, services for Viessmann is a little over 10%. We've said that about 40% of their business is the combination of heat pumps and the related accessories they have. They have a bit that's the boiler piece, which the boiler should decline 5%. Heat pump is growing 20%. They have batteries. Batteries, probably growing in the 20% range. Solar PV, growing in the 10% range. And then services is I think around 12% of their business, and that's growing double digits as well. And it's partly because they have this direct-to-installer intimacy and it's partly because they have ViCare and other digital tools that enable them to not only be on one system that interfaces directly with their 75,000, 80,000 installers, but also interface with their homeowners. So, they can not only do remote diagnostics, but they can also come up with subscription [ph] price (00:20:44) deals with their homeowners and start to use algorithms to anticipate failures before they happen.

So, what we've said at Carrier is that we were going to grow from $4.5 billion to $7 billion in aftermarket sales. If you look at the aftermarket sales that we lose with Fire & Security and Commercial Refrigeration, it's about the same number that we add with Viessmann. Viessmann's aftermarket is probably growing slightly higher than the aftermarket sales of what we're divesting. So, we still stand by that $4.5 billion to $7 billion over a five-year period, perhaps a bit of upside there.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Okay. Fantastic. And when I look at the growth outlook, I mean, it's impressive numbers, of course. How dependent are you on policy support? Lots of countries in Europe, and I do recall Europe has backpedaled on energy policy.

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

A

Yeah.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

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Biofuels come to mind. What's your [ph] sensitivity (00:21:37) to that? What happens to the growth outlook if the policy support does waver a little bit?

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

A

Look, policies in every country will move one way or another, and we saw some of that in Italy. The level of subsidies changed a bit in Italy. But if you look at the gravitational force over any period of time, certainly in Europe, where there's shift to electrification, that shift will undoubtedly happen. And if you think about, even from a national security perspective, it's more existential in Europe than it's ever been before, of course, with the war in Ukraine.

So, you look at the overarching legislation that's been passed in Europe, it started with the Paris Agreement, went to European Green Deal, Fit for 55. There's so many overlaying legislation where it's implemented at a government level. But at a EU level, after the invasion of Ukraine, they did REPowerEU. And it's all about a 50%, 55% reduction in greenhouse gas emissions between now and 2030. And you can't get there without a massive shift to electrification in the homes, because 40% of carbon emissions come from buildings including homes. So, if you're ever going to move the needle on a shift away from fossil fuels, homes, buildings need to be a part of the solution. And that's why these – the regulation supported by subsidies absolutely will happen. It may change on one country one year or another, but that gravitational pull will continue.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Excellent. And I've got a couple audience inbounds here on Viessmann specifically. So, first off, just give us a little color. Why did Viessmann sell? It's a great story. I mean, the outlook for this firm looks outstanding. What attracted them to Carrier?

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

A

Well, look, obviously, I'd be hesitant to speak for Max and the family, but I believe from our very first [ph] interview (00:23:33), which was over a year ago in Allendorf, Germany, the very first conversation we had was about value creation, and value creation for our people, for our customers, for the planet. And we always had the underlying premise that one plus one had to be greater than four. And if you look at the opportunity, the once-in-a-century opportunity, to put these two global firms together to create a true global climate champion, this is a once-in-a-century combination. And I think it was really about impact. It was impact that it puts the 11,000 team members of Viessmann on a different platform where it can create opportunities for them to create value on a global scale.

If you think about you wanting to impact climate change, and I know that that's very personal for Max Viessmann and the family, even some of their VC investments, a lot of what they spend, a lot of their energy and focus on, it's things that impact the planet. And climate change doesn't respect national boundaries, country boundaries. So, to have an impact on a global scale on the planet and truly create change the entire competitive landscape globally where we will be out competing any company in the world, whether it's Asia, Europe, United States or anywhere to create a portfolio that has the technology, has the channels, has the brands on such a global stage, it really creates a unique combination.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

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Excellent. And then building on that, as we think about the global scale combined firms, could you speak a little bit to the product overlap? And then probably more importantly, distribution or channel overlap between Carrier and Viessmann, where you see the potential for upside.

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

A

What I would say is, it's incredibly complementary. They have what I think everyone would admit is, by far, the best channel in Europe. They have – there are some that have a four-step distribution where they go through distribution, to a wholesaler, to an installer, to a homeowner. Others have three-step where they go wholesaler, installer, home. Viessmann is the only company at any form of scale that goes direct to installers into the home.

So, we see an opportunity from a revenue synergy where if they do have some of their installers that do carry – they typically [ph] will have (00:25:47) 80% Viessmann and 20% maybe in some cases somebody else. Ideally, that 20% can be either a Toshiba, which, of course, we own, or a Carrier brand as a second tier offering. So, that could be an opportunity for that channel.

And, of course, we have – you think about the United States, I think we have clearly the most extensive dealer channel here, relations with over 100,000 dealer network here. So, can we bring the Viessmann brand and some of the technology in a meaningful way to the United States? Can we bring it too in a more meaningful way to places like China or India or Saudi Arabia? I think we have very complementary channels and very complementary brands.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Excellent. Thank you.

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

A

Yeah.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

And then one more on the portfolio. I know it's always hard to say we're done.

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

A

Yes.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

But should we be expecting any more big moves in the mid-term? Are there other pieces that you think might be helpful to round out Carrier's offer?

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

A

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Well, I think we're very focused with what we have right now. I mentioned right upfront the three priorities we have is that our expectation is, we'll close on Viessmann around the end of this year. We have an integration team based in Frankfurt, working closely with Thomas Heim and his team to really make sure that we integrate effectively and we give them the space to go execute on what's right in front of them right now, which is tremendous hyper-growth for as far as the eye can see.

We have a small group that's working around the clock on the business separations. Hopefully that will happen sooner rather than later. That's why I kind of went out of my way to say that as we get towards the end of the summer, we should be out in the market with Commercial Refrigeration, with Security. If you think about the three Fires, perhaps one or two of the Fires, we'll see how that plays out. Maybe all the Fire. We're going to have to see how it all plays out.

And then we have to then execute. And that's why we have our – my leadership team and I heads down laser-focused on execution. We've said that over the next couple of years from a capital allocation perspective, we're very clear. As we close on Viessmann, leverage ratio, 3.5 or so, get it below 2 within a couple years. And then after that, we'll see. But right now, we have charted a game plan from a portfolio perspective. And I think we're as excited as we've ever been about making sure we execute on that over the next couple years.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Very good. And then pivoting to divestments, nice segue there. Are there no dis-synergies from peeling out Fire & Security?

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

A

I mean, perhaps there's some lost value in not having that broader offering in the building systems. It's honestly at the margin. We had a hypothesis that we've been working hard on is the value of cross-selling between HVAC and Security, HVAC and Fire, or all three combined. And the reality that we've experienced is that when we think about new building construction, the people making the decision and the timing of those decision, whether it's new construction or modernizations, they're often – those decisions are typically being made by different people at different points in the cycle. So, to the extent there may be some slight technical advantage between having an HVAC system interconnect with a security system, it's far outweighed by the loss of focus. And what we're finding is that the revenue synergy was marginal at best.

So, now we have the opportunity as a company to really think through how we structure ourselves. We don't think of ourselves as becoming HVAC-R. We will be 85% HVAC, 15% R, Transport Refrigeration. But we think about ourselves as an intelligent climate energy and solutions company. But then we need to rethink how we even think about our corporate functions, how we think about operations. So, you will see a significant decrease of overall corporate structure. So, obviously, we want to – as we sell Fire & Security and Commercial Refrigeration, we want to real time reduce corporate overhead. So, when we sell them, they no longer have the corporate allocations that we currently give to them and rethink how we work with our new structure to really minimize a lot of the corporate overhead that exists today.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Interesting. We have busy summer for corp dev teams across the peers, that I'm sure.

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

A

Yes. They will be.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

So, I'll turn to Kidde-Fenwal specifically. The bankruptcy strategy here is notable, and there's a bit of a parallel perhaps there of technologies, 3M. Should investors be reading anything across to how that plays out? And do you see any risk to the divestment process associated with these liabilities?

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

A

No. I think that when you look at KFI – and by the way, just to be clear, the name has Kidde-Fenwal, Inc. but it has no relation to our Kidde business. They happen to share the Kidde name. But when you think about our residential business of Kidde that sells smoke detectors, carbon monoxide detectors for homes and extinguishers, that has nothing to do with the KFI business.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Got it.

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

A

And, look, that company KFI over a decade ago for about a handful of years owned this company called National Foam. That business, KFI, was never integrated into Carrier, a complete stand-alone business. So, KFI made a – we had made it clear to KFI, which is a complete stand-alone business, and to the extent that there's any liability associated with AFFF – it's 100%, we believe, within KFI. And we had said that to the extent there's any liability, we're no longer going to support you.

So, KFI established its own board and came to an independent decision that they were going to put themselves into Chapter 11. And now they will go through a process of the board will sell KFI. They have retained an investment bank. And what I would expect to happen – not my call, it's now a deconsolidated business, completely separate from Carrier in Chapter 11 with no relation to Carrier – it will probably sell itself. And then I would suspect they would use the proceeds from the sale to pay the plaintiff's attorneys as part of a settlement. But that will play itself out between KFI and the creditors, but it's no longer a part of Carrier. And that business is completely separate. It always has been, always will be, and stand-alone in Chapter 11.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Got it. Thank you.

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

A

Yeah.

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Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

So, if we look at the divestments, you've already spoke a little bit to the timing. Any comment on the nature – so spin, outright sale, maybe something more creative like an RMT. How are you thinking about the opportunities there?

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

A

I think the lion's share is you're looking at sale. So Commercial Refrigeration sale, Security sale, and then we'll see about Fire. Like, Fire can cut a few different ways. You could imagine a sale of all of Fire. You could imagine a sale of three Fires: Commercial, Industrial, and Residential. Or you could imagine a sale of two Fires – I'll make it up – but Commercial and Industrial, and a spin of Residential.

So, where the optionality and the TBD is really around, I would say, part of Fire, and we'll have to play that out as we get in towards the end of the summer.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Okay. Excellent. And I have one more here, [indiscernible] (00:33:16). So, with recent acquisitions, do you anticipate any changes to your distribution strategy in the US, specifically the Watsco relationship?

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

A

No. We've been partners with Watsco for obviously many years. And I think that we've both taken steps to improve the relationship for both of us. And, look, I think that Viessmann has really established a phenomenal channel in Europe. We have a lot of optionality around how we think about brands and how we go to market in places around the world, including the United States. But I don't see any major shift in the Watsco relationship.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Okay. Fantastic.

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

A

Yeah.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

So, Viessmann, clearly, the secular play. We like talk cyclical a little bit. North American Residential or HVAC, down this quarter. As you look across the channel and homebuilders, how close do you think we are in the bottom of the cycle here?

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

A

It's hard to say. I would say that we feel very calibrated on 2023 for Residential. We said for 2023 that the year would basically be flat on a sales basis, high single-digit volume decline, which is about probably the case for 2Q

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with flattish sales, as you know, you look at mix and price offsetting the volume decline. And I think that's the case probably for 2Q and probably about the case for the full year. So, we'll see what happens on the new construction side, which is about 20% of the business. We said that was down – well, for the year, be down about 20%.

I think hopefully that turns out to be a bit on the conservative side, but we'll see how that plays out. I think we're calibrated on where we are with inventory and the channel movements, tracking about where we thought. So, I would say pricing sticking, we came in and we announced another price increase in January, became effective in March of 6%. So, the price realization has been quite positive.

So, we feel calibrated on overall Resi. Parts have been – we've been pushing hard on the parts side, and that's been positive. Light Commercial is turning out to be – continues to be extremely positive. So, I think about that P&L that's under Justin Keppy, our Residential Light Commercial business in North America, and I think he's always kind of managing his P&L to the extent there's – that we're always watching Resi. He can offset any challenges we see there with Light Commercial and parts.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Got it. And then looking to Commercial, we saw growth building backlogs. So, all good. But in the US, we do see signs of strain across end markets, the office market, in particular. As you look across your end markets in this business, are you seeing signs of weakness? And do you expect any moderation to growth rates in H2?

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

A

Well, I'll tell you, I'm really proud of that growing in the commercial team where they've shown a phenomenal agility to shift where – to where the strength is. So, in the United States, real estate is less than 10% of our Commercial Applied business. And that's something that with the banks and other things, you do have to watch. But then you look on the flip side and you look at something like data centers with AI and a lot of trends we're seeing there, which is in the low double-digit percentage of our Commercial Applied business. And we're seeing great strength there. We're seeing – complementary to that is the CHIPS Act and some of the investment in new industrial construction happening in places like the United States. So, we've been the beneficiary of that.

Higher ed has been strong. K-through-12 has been strong. Retail, there's pockets of strengths, pockets of not so much. Warehouse, down a bit. So, I think what we've shown is a propensity to really pivot to where the growth is. And we're very pleased with the growth we're seeing, as I mentioned, around data centers, which, again, is about in the low double-digit percent of our overall Commercial Applied business.

So, I'll give you one other example, Brendan. As you take China, for example, China, there was a slowing that we obviously saw in multifamily, residential, and some of the real estate. And we used to just, a few years ago, be 70% real estate, 30% industrial and infrastructure. And we had strategy sessions. We looked at our channel. We looked at our salespeople. And we said, we're going to invert that, 70/30 the other way, I&I versus real estate. And to the team's credit, they did it. That's exactly what we've done over the last three years. So, you're seeing really strong growth in China in electric vehicle production, some of the industrial pieces.

So, there's a lot of green activity in China with modernizations. And that's where we have our salespeople, and that's why we saw orders quite well in China in April.

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Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Good to be in the right place at the right time.

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

A

Yeah. We have to be purposeful about it, and the team has been very purposeful about it.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Yeah. Excellent. So, price has been an interesting lever this cycle for a lot of players. In Carrier's guide, I think your $500 million on the year, that was pretty moderate. Are you taking more or less price in different areas of the businesses you look across?

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

A

I would say the price that we're getting, $500 million this year. We've gotten $2 billion over the last two years. So, I think the team has shown more agility and aggressiveness on price than we've shown in our company's history.

So, I do think that we've gotten price. Price has been sticky. And I think one of the encouraging things about our industry is that there's no intention, thought process around decreasing price. So, we came into the year. We said that we need further price. We did 6%. In just North America, we did 6% Resi, 8% Light Commercial, 10% Commercial Applied. And the price is sticking, and we expect it to continue to stick.

Now, we won't continue at the same pace we've had. We did seven price increases in Residential in, I think, something like 18 months. I think we'll get back to a more typical cadence of price increases. But the pricing realization has been quite strong.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Excellent. So, turning to services, the part that helps us through the cycle. So, it's a big focus for Carrier over the past couple of years. At the last Investor Day, you mentioned, I think, it was $4.5 billion to $7 billion for 2026. That was the God-given aftermarket, if I recall correctly, that falls off your installed base. What kind of attach rates does that pencil out to? And how have they been trending over time?

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

A

Well, if you think about when we spun our attachment rate, now that refers to Commercial Applied equipment. When we sell it, it comes off warranty that we get a long-term agreement. We've essentially doubled the attachment rate. We were at 20%. We're now at 40% in just a few years. And we're going to increase that at least 5% a year.

If you look at the total number of chillers under some kind of long-term agreement out of our 330,000, we have about 70,000. We're increasing that 10,000 a year. So, it's effectively all hands on deck with Ajay Agrawal working with the business units to apply a proven playbook around consistently improving aftermarket in that high single-digit to low double-digit. We drive ourselves to much more than that internally every single year.

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So, we have an internal target for ourselves to do very well this year, certainly into the double digits. We grew in the high teens in the first quarter. But it goes through our relationships with our channel partners, our suppliers, a tier playbook, digital tools like Abound and Lynx, and how we think about digital tools around prognostic and diagnostics. It's an end-to-end playbook that we know for a fact works. And now we just have to apply the playbook, and we're seeing great traction.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Excellent.

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

A

And it comes with higher margin, higher stickiness on the revenues that helps you through any cycles, and it's just going to be the way of life at Carrier for the future. It's – every year, you're going to hear us talking consistently always about aftermarket growth just as part of our DNA, whether it's how we design the product, how we negotiate contracts with either customers or suppliers, or just how we think about our entire business strategy.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

And how much runway do you see there on growth and margin for services specifically? Is it a 2026 story or should we look beyond?

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

A

Oh, beyond. This is a way of life. We put 2026 out there as a five-year marker. That's $7 billion. And as I mentioned, the revenue we lose with F&S and CCR, we pick up with Viessmann. So, it sort of is awash with higher growth rate out of Viessmann. So, we'll get to the $7 billion in 2026, but that's just the beginning.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Is there a world where you play offense here and service third-party equipment?

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

A

That's not our focus because there's so much of our own equipment that we don't service right now, that if you think about servicing 70,000 out of 330,000, now, on a lot of that other stuff that is not under an LTA with us, we obviously provide parts and have a fair amount of sales with the other parts of it. But we have so much runway just to make sure that we provide long-term agreements around our own equipment.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Excellent. And then you mentioned Abound. I just love to hear a quick update on digital. So, Abound, Lynx, BluEdge, how are things going there?

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

Phenomenal. I mean, credit to Bobby George, the digital team and the BUs. Abound didn't exist a couple years ago. Abound is our digital platform that we use for commercial buildings. But I'll tell you, we worked with a tech company. We started with 100 buildings with a tech company. And we increased that to 200 buildings. We have more than 1 billion square feet under a contract with Abound.

But Abound is the enabler. And the whole concept is, we go to a scale customer and we say we're going to put a digital tool which is very inexpensive to install. It's wireless, so you don't need to affect any of the wiring in the building. And on a single pane of glass where you may have 10,000 buildings around the world, you can see your real time carbon emissions of any single building globally. And then you can not only see it, but then you can use AI and other tools to take corrective action. And you may replace a rooftop unit for your facilities in India, or you may just do an adjustment to your control system.

So, today, we use AI for all of the Home Depots in North America where we do all of the temperature control remotely, and we have an arrangement with them where Home Depot and – well, they benefit from better energy efficiency savings for all of their facilities in North America, and we benefit from the upside.

So, the same end-to-end energy management solutions we talked about for homes, we're doing it real time, Abound is the enabler, and I'm thrilled with the traction we're getting there.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC
Q

That's fantastic. And you're able to [indiscernible] (00:43:43) third-party equipment as well or is it just Carrier key?

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

Yes. And that was the whole key, was we had to make it agnostic so it could interface with anyone's BMS because we love our Automated Logic controls business. We have nice share. We have been increasing share, a great product line. But we needed to interface with anyone's building management system. So, it's completely cloud-based, agnostic, open source, so we can work with anyone's BMS.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC
Q

Very good.

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

Yeah.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC
Q

So, turning briefly to financials. I believe at last year's Investor Day, you had a long-term growth target around 6% to 8%. This year at the deal, we saw pro forma is mid-teens looking backwards...

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

A

Yes.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

...absent the divestments, plus Viessmann. And then we're looking at LSD to MSD for 2023. As you look past this to sort of that 6% to 8%, assuming it's still out there, what are the things that have to fall into place for us to get back to that high single-digit range?

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

A

Well, look, we said that the financial algorithm, around 6% to 8%. We feel better about the 8%, the high end of that range with the business exits and the addition of Viessmann because I thought for sure I was going to get the question that Viessmann have been growing mid-teens, and you said they're going to grow double digits, which people somehow interpret as 10%.

Going forward, why would their growth rate go down when you have all these market forces around the transition to heat pumps, which is 3 to 4x, boilers, you have solar PV, you have batteries, you have all this digital enablement. Boilers, only declining 5% with all this other stuff growing 20%. And there's really no fundamental reason why the growth would ever so. I think that hopefully we've been conservative in our estimates. But you're adding something that in a world of a lot of economic uncertainty, we are now adding the premier asset in the premier market, which has not only been realizing great growth, there's no reason that it would slow.

And I will tell you, to the credit of Max Viessmann and his team, they always say they under-promise and over-deliver. And since I've been getting to know him, that has been true, what he told us about the fourth quarter last year, their first quarter of this year, April of this year. That is a business that continues to under-promise and over-deliver. So, we're very optimistic there, and we're very optimistic in that sustained 8% type growth.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

It's good to be in the secular camp.

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

A

Yes.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

One more on the financials really briefly. We had a 50 bps [ph] OMX (00:46:11) cadence out there last year. Is that still the right way to think about your margins long term? And outside of deal synergies, has anything material really changed here?

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

A

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No. I mean, look, we've grown 150 bps over the last couple years. This year, we would be growing 50 bps if it weren't for 50 bps of headwind through the integration of TCC, which we'll be having a little bit of upfront integration cost and cost to go achieve the synergies, which, by the way, we said was going to be $100 million and we'll certainly be well north of that. So, we feel good about 50 bps a year. And even if you think about HVAC margins, the HVAC margins this year, the headwind from TCC is 130 bps or so. So – from just TCC.

So, we feel very, very good about the margin expansion story, especially as we get back of driving true productivity because not only did we get a couple billion of price over the last couple years, we had a significant amount, almost – just under that same kind of amount of inflationary headwinds. So, you talk about God-given rights – or I guess I do and get in trouble for it. But one of them is to get that inflation back. Like, that is – we pay our people a lot of money to go back and drive true productivity, productivity in the factories, material management. Logistics seems very favorable this year. Raw materials were down a bit. So, as we drive true through productivity, we said $300 million. We're obviously internally driving to more than that.

We said we're going to get price, but get back – we called it Carrier 700 upfront. It was kind of a three-year target. But now we talk in terms of percentages because the portfolio is moving around. But we expect operational productivity in the 5% range a year. So, we drive ourselves very aggressively, and we feel there's an enormous opportunity as we get back to basics operationally to drive very significant productivity.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC
Q

Excellent. And I have one more audience question, and then we'll give you the podium back here.

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

Yeah.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC
Q

So, looking at the Viessmann outlook, and we're talking about 40 million homes for heat pumps, what choke points do you see there? Could be distributors, people, components, raw materials, anything material that stop us from ramping that aggressively?

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

I would say the biggest constraint is the number of certified installers.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC
Q

Okay.

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

We feel good about the capacity between the investments that Viessmann has made, the capability, the capacity we have. Remember, with Toshiba's business, Toshiba had a brand-new facility built in China. A brand-new facility, the size of five football fields, built in Poland. That's fairly empty. We can use some of that. There's

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investments that collectively between Viessmann, ourselves we're making in Germany. The German workforce, I got to see it firsthand yesterday, is phenomenal that the amount of technology they have in the factory is simply phenomenal. We just got to see it firsthand in Allendorf. So, the capacity will be there. I think the issue is going to be – the constraint is the number of certified installers.

Now, the beauty of Viessmann is, they have their own channels. So, they're training the installers themselves. This year, I think they're going to train something like 100,000 installers. So, that is an enormous competitive advantage. And it can take three years in Germany to become fully certified to do heat pump installations. So, they have a whole approach they use to not only certify – fully certify trained installers in Germany and throughout Europe and their channels, but also supplement them with people that can do many of the tasks short of the full certification. So, that's something that they and we collectively will continue to lean into the investments.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Q

Very good. Well, we've got a few minutes left in the clock here. What messages would you like to leave people with today? And what are you the most excited about looking forward?

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

A

Well, this is just a new Carrier. This is a Carrier that we positioned ourselves squarely in the middle of this secular trend around sustainability. And if you think about all the money that's going to be spent on intelligent climate energy solutions, as we look at this broad trend of energy transition over these coming decades, and you think about the fact that 40% of carbon emissions come from buildings, there's no question that a significant amount of the resources spent in our space is going to go to more energy efficiency and sustainability.

And with the portfolio changes we're making, I think we're positioning ourselves as the premier climate champion in our space. So, I could not be more proud of our team, and I am so excited about the opportunities that lie ahead for Carrier.

Brendan Luecke
Analyst, Sanford C. Bernstein & Co. LLC

Outstanding. Well, thank you so much.

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

Yeah. Thank you. Thanks, Brendan. Appreciate it.

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