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Carrier Global Corp. (CARR)

Baird Global Industrial Conference

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Analyst, Robert W. Baird & Co., Inc. (Broker)

MANAGEMENT DISCUSSION SECTION

Timothy Wojs

Analyst, Robert W. Baird & Co., Inc. (Broker)

Good morning, everybody. And thanks for joining us. I'm Tim Wojs, and I cover building products here at Baird. And we're delighted to have Carrier Global join us again this year at our Global Industrial Conference. Carrier is a global leader in intelligent climate and energy solutions. They offer heating, cooling, cold chain, and related aftermarket services to homes, buildings, data centers, and transportation markets. And from the company, up on stage with me is Chairman and CEO, Dave Gitlin; and then CFO, Patrick Goris. And then Michael Redner, who's VP of IR, is in the front row here. So we'll start with a few prepared comments from Dave, and then we'll hop into Q&A.

With that, the floor is yours, Dave.

David L. Gitlin

Chairman & Chief Executive Officer, Carrier Global Corp.

Well, thanks, Tim. Good morning, everyone, and thanks, Baird, for having us. The Carrier of today is significantly different than the Carrier at spin. We are better positioned for sustained strong growth than we've been in decades. How? By becoming a pure-play climate and energy solutions company with a focused yet balanced portfolio.

By investing in product differentiation, which you can see across our portfolio, by building an aftermarket playbook that drives consistent recurring revenues and double-digit growth, by adding a new vector of growth and differentiation through systems and digital offerings, and by transforming our commercial HVAC business where our win rate is 3x what it was at spin. We've spent the past 6 years creating a comprehensive ecosystem to outcompete while expanding margins by investing in spec engineers, sales force, field technicians, new and differentiated products complemented by lifecycle, digital, and system solutions.

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We have had significant share and margin gains since spin. Certainly data centers are helping, where our sales will be up 2x versus last year and our orders year-to-date are up 350%. So it's a great source of growth, but this year it is just about, just under 10% of our total sales. So plenty of room for growth. It'll be up about another 50% next year without being overexposed to it. Importantly, we are also winning in non-data center verticals globally with more to come following our capacity investments. All complemented by residential and light commercial end markets recovering in the Americas and Europe.

By the end of next year, commercial HVAC and aftermarket will be nearly half of Carrier, giving us multiple ways to win. Great long-cycle backlog with many verticals of strength and recovering RLC markets. All in, we have built a more resilient company that is not reliant on any one vertical or geography, positioning us for sustainable growth, which is what you should expect from us over the years to come. Now, we recognize that growth needs to come with strong earnings conversion. This year, our in-year pricing actions were a reaction to the in-year tariff and inflationary challenges.

As we prepare and start thinking about next year, we are clear-eyed about the input costs and are getting out in front of these headwinds. We have already announced price increases globally and are also, of course, leaning into productivity through Carrier Excellence, our business operating system, which is deeply embedded in our DNA. We deliver on productivity across the company, including through our factories and supply chain, as well as product re-engineering to deliver lower costs. That playbook is working and we will continue to use it with great focus and effectiveness.

While temporary cost inefficiencies, including expedite and logistics costs associated with the significant volume ramp, have impacted the business this year, we expect these headwinds to fade as we go through 2027. We are taking tough but important structural cost actions, including closing high-cost locations and other restructuring actions. We have a track record of doing great things even when it's hard, and that is exactly what you should expect from us.

With that, Tim, let's get into the Q&A.

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QUESTION AND ANSWER SECTION

Timothy Wojs
Analyst, Robert W. Baird & Co., Inc. (Broker)

Q

Awesome. Thank you, Dave, for that. If you have any questions, you can raise your hand or you can email session1@rwbaird.com. Maybe just to start off, kind of big picture, Dave, I mean, you held an Analyst Day last year that outlined kind of 6% to 8% organic growth over the medium term. Just maybe talk about the puts and takes, how you're tracking to that, and your confidence in kind of attaining those over time.

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

A

We feel good about it. I mean, this year we'll be up around 10%. Next year, that's the kind of zone that we're thinking about, mid to high single-digit type growth. And if you look at it, it always started with the market, and we see very good market conditions on the commercial side and great backlog. We have record backlogs, $8.5 billion, really well positioned on the commercial HVAC side. I mentioned double-digit forever on the aftermarket side. And then if you look at this new frontier for us, systems differentiation, that'll give us another point or two as we go into next year and beyond. So we said 6% to 8%, and that's the kind of zone that we feel good about.

Timothy Wojs
Analyst, Robert W. Baird & Co., Inc. (Broker)

Q

And aftermarket's been a really big focus for you kind of coming out of the spin. Kind of what have you done over the last 3 to 5 years to kind of position that into your kind of double-digit forever type of model?

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

A

Yeah, prior to the spin, we consistently grew at about 1% or 2%. Every year since the spin, we've grown double digits, and we're on track to do it again this year. And it's really a holistic playbook. If you look at just how you get parts from A to B and getting your fill rate up north of 95%, if you look at your service attachment rate, if you look at our complex chillers, we have close to a 90% attachment rate, which means that when the product comes off warranty, do you get a long-term agreement?

We've expanded our focus on modernizations and upgrades, and this year it'll be up 25% or so with a complete playbook that we've deployed globally on how to drive change to a chiller before the end of its life. We've leaned in a little bit on CapEx to drive more rental sales. So the whole playbook around service attachment, parts connectivity – we have 270,000 Lynx subscriptions for our transport business. Lynx didn't exist a few years ago. You look at the number of connected devices, that's just par for the course. It rolls off the line, it's connected, and we have about 120,000 chillers now connected through Abound.

So it's a holistic playbook. And the thing that's out on the horizon, all these chiller sales that we're seeing right now, that's all going to result in very good recurring revenue with the aftermarket down the road.

Timothy Wojs
Analyst, Robert W. Baird & Co., Inc. (Broker)

Q

And what is usually kind of the path to that, especially on like the data center side?

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

A

For data center, I was actually at one of our major data center customers yesterday. We're going to sell them in the first phase about 600 chillers. They have all of our BMS. They have 100% Automated Logic controls. We're talking to them about CDUs and they're really excited about Quantum Leap, so systems offering. But they have an entire – this multi-thousand-acre facility, they have a whole area that they're thinking about for how they think about parts and remanufacturing and maintaining chillers and other equipment on the site. So we're talking to them about various options for long-term agreements.

We have three tiers of long-term agreements. We have a very base one, where some data centers will have already designed for redundancy and they don't need white glove treatment where you're going to repair, that you need onsite support, onsite parts. You need to make sure that any chiller that goes down, you fix it in a matter of minutes, not hours. And some haven't designed for full redundancy and they want what we would call an Elite Blue Edge agreement. So for each data center, they will end up with one of the three, a base, a mid-tier, or a very high end. We usually, we put people on the site during the warranty period, call it a year or so.

Then we have a couple years where it's – there's some level of payments associated with an attached service agreement and then varying degrees of long-term agreements. But that's going to be a great source of revenue. Remember, the chiller will last longer than 7 years, but in many cases, the chips will get replaced after about 7 years. That will trigger a whole new – as you introduce new chips, the thinking around the cooling needs will change. So there's a lot of strategy that we're discussing internally, how we make that 7-year upgrade to the chips, a part of our chilling upgrade strategy.

Timothy Wojs
Analyst, Robert W. Baird & Co., Inc. (Broker)

Q

Okay, okay. Maybe just kind of staying on the data center topic. I mean, obviously, the election kind of moved sentiment a little bit last week. Just any kind of early thoughts or implications, kind of any customer conversations or data points you can talk to?

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

A

I spent the weekend with one of our biggest hyperscaler customers. We had a lot of discussions. Excuse me. I was with a colo customer yesterday. If you look at the next few years, that's pretty locked in. We have firm orders, we've signed LTAs with mandatory minimum agreements. So when we look at our backlog and we look at the kind of commitments that they've now – they're already under construction with, what we're seeing with the election, I would not describe that as a 2027, 2028, 2029 type issue. And so we feel good about the orders we have.

The great thing for us, and there, look, you look at the ultimate underlying demand for more token usage and all that. I think the underlying demand will continue to increase the demand for compute. So long-term, it still feels good. What I will tell you is the great thing for us is that we have great exposure to it. I mentioned 350% increase in our orders year-to-date. We've been growing 2x every year. We went from $500 million to $1 billion to $2 billion this year. We'll be around $3 billion next year, so that'll be up another 50%. So for us it's great, but we're not one of these companies where it's 70% of our sales.

So this year, just under 10%. It'll become a more meaningful number next year, north of 10%, but it's not 70%. So when I think about the Carrier portfolio, we went through, I would say a couple years where those that really

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wanted to be all in on North American commercial HVAC and that you wanted to buy someone where it was like a huge part of what they did, there were a couple clear folks that people would lean into. If you wanted a pure-play resi guy, there was probably a guy that you might focus on. We're in a phase now where we love our resi business. There's a lot going on. I'm sure you're going to ask about it. It's the topic du jour, but it's 20% of our sales.

So we have a pure-play HVAC, our climate and energy solutions company. It's a great growing space. Our backlog's at record highs. But we're not overexposed. We're not overexposed to resi. We're not overexposed to European resi or commercial or commercial. So we have focus but balance, and I think that's going to serve us really well in these years to come.

Timothy Wojs
Analyst, Robert W. Baird & Co., Inc. (Broker)

Q

Yeah, I mean, I guess you do have more of kind of a global kind of diversified portfolio. I mean, what are kind of the pros and cons of being, so global and in so many different kinds of regions?

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

A

I think one of the big advantages that we have with the portfolio we've established with folks like Viessmann and Toshiba is we have 5,000 engineers. So as we start thinking about different technologies around the world, if we want to do variable speed side or vertical discharge, we have rotary compressors with the Toshiba acquisition. We have phenomenal inverter technology. We have – as we start thinking about domestic hot water in the United States, you have all of the technology that Viessmann brings to bear as they've combined hot water with heating in the same technology envelope.

So what's great about having what we have is we can scale the technology through product differentiation. We have systems differentiation, we have digital capabilities, and we're not overexposed to any one geography or vertical. So we think that over the last couple of years, if you're in a pure play, one geography, one vertical, and that vertical and that geography is great, you're going to ride that wave and it's going feel pretty good for a while. When there starts to be any kind of question marks about a single vertical or single, it's nice to have balance and not be overexposed to one geography and one vertical. And that's what we have is balance but focus.

Timothy Wojs
Analyst, Robert W. Baird & Co., Inc. (Broker)

Q

Okay, okay. Maybe just, kind of going into the business a little bit, just kind of North American resi, kind of where do you think replacement volumes are this year and how does that kind of compare to normal?

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

A

We said that the total market typically is at about 9 million units. We went through a stretch there, 2020 to 2024, where it was a bit north of that. And then, we were in the 7.5 range. We came into this year thinking it'd be around 6.5 million units, and it's going to be somewhere between 7.5 and 8. So it's been more resilient than we expected. We had said coming into this year our resi business would be down high single digits. We'll be up around 10% this year. So the underlying market conditions have been better.

And the question is why, when you have high interest rates and there's some anxiety around the consumer? It's because at the end of the day, it's a replacement business. It's 75%, 80% of our business is replacement, 20%,

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25% is new construction. And at the end of the day, units fail. You can't limp along forever with a motor or compressor change. So it's a replacement business and we're seeing that. And then I think as we start to hopefully down the road get the benefit of – we'll see what happens with rates, we'll see existing home sales have been suppressed, as those start to come back. I mean, the market's doing better with these macro headwinds. As those macros start to give us a little bit of relief, it should start to improve as well.

Timothy Wojs
Analyst, Robert W. Baird & Co., Inc. (Broker)

Q

Okay. And I mean, obviously the kind of repair part of the market kind of picked up last year, but you also had a lot of complexity around the refrigerant change and things like that. So where do you kind of think you are from like a fix replace standpoint? And is that – was that a cyclical dynamic, or do you think that that's some sort of secular change?

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

A

I think that was – I think what happened last year was you had this sudden macro headwinds that created a bit of a dynamic where folks did opt for repair. I do think that because existing home sales seem to have been suppressed for a bit, I think people are just back to the new normal where it's a replacement business. So we have not seen the dynamic. I just spent a lot of time with AJ, the Watsco CEO, and his leadership team. And also, we were with our independents a couple weeks ago. What I will tell you coming out of those discussions is that the replacement dynamic is what it's traditionally been.

We get a lot of questions and it comes in all different ways. If you listen to our earnings call, has something changed with the resi market? So I ask, I mean, these are people that are deeply steeped in the business. So I ask the question, I go to an investor meeting, I get 70% of the questions on 20% of our business. And is, has something changed in resi? And I will tell you to a person, the answer is no. It's a phenomenal business. There is a handful of companies that fundamentally define the business. We are proud to be the market leaders in this business.

If you look at what's happened over the last handful of years, we went through a stretch where we had the semiconductor problems where people were charging $5 to $10 for a $0.01 component. So we had a sudden influx. We did raise some prices. Then we had the A2L transition. And we all – the new product versus the 410A was higher priced, and we all raised some prices.

Now we have inflation and tariffs, so there's price increases, and we'll get price increases this year as we always do. I do think that the difference about this year was that usually we have a pretty good envelope of where the input costs are going to be. We can say copper will be somewhere here, and steel, aluminum, and we can kind of look at logistics costs and we're usually, and this year I will tell you the – what happened in April with the tariffs on the 232 tariffs, that was kind of unexpected and a significant number. And it was exacerbated by some of the stuff with raw materials and fuel.

And it happened all at the same time when the consumer was under some level of pressure. So what I will tell you when I talk to people that have been in the business for a very long time, I'm talking about people that used to work at Carrier, they've been in the industry for 40 years. The fundamentals are the same. The channel dynamics are the same. We have great channel partners. We have a great route to market. We're introducing new products. We're introducing system products. We're introducing a digital ecosystem that we call Comfort360. We're going to get pricing. We've already announced price increases for next year. It's going to be effective December 15th. We

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announced an 8% price increase for our resi business. So the fundamentals are the same. We'll continue to drive differentiation and channel stickiness, and we'll continue to drive price.

Timothy Wojs
Analyst, Robert W. Baird & Co., Inc. (Broker)

Q

So on the pricing topic, because there's a few questions here from the audience on it, just so really kind of the pricing not kind of real, being realized in the year was kind of more of the suddenness and the severity of the cost increases relative to something that's kind of changed in an underlying basis. Because then you kind of layer in like, maybe some increased competition from foreign players and things like that. So maybe just kind of unpack that a little bit.

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

A

I'll take this and then turn everything else you ask to Patrick, because you're probably going to get into harder questions. I think, yes, there is a trend to – are we seeing more ductless? Yes, we – and that's a good thing. We love our ductless business. We have a crossover unit that's effectively a hybrid unit that if your outdoor unit is a side discharge and it connects to a traditional air-to-air internal system. That hybrid system plays really well for us. We have great channel, great branding, and great margins on our crossover and on our side discharge business.

We have a great partnership with Midea, which will continue, and we have great technology in our portfolio that plays perfectly for that part of the market. So we're very happy with how we're positioned on that side discharge space. Are there competitors that are in the market in that space? Yes, but if you look at most of them, they're almost all partnered with one of the US players. So we feel very positive about that space.

Timothy Wojs
Analyst, Robert W. Baird & Co., Inc. (Broker)

Q

Okay, okay. And then maybe just to kind of the last resi question, I've got is just, you're seeing your customer base kind of get bigger. You're seeing kind of new people get into kind of HVAC distribution. How are you guys positioned for that? What are the positives and negatives?

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

A

It's very good. Look, I would tell you that our relationship with Watsco has never been better. We spent a lot of time with AJ and his team, and it's very collaborative. Not only the Carrier Enterprise piece, but the other parts where – excuse me – that we use Watsco. We have a recurring cadence of how we look at KPIs, how we kind of find win-wins for each other. So the Watsco piece is very, very positive.

The non-Watsco piece, yes, we've seen the Home Depot subsidiary come in and buy a couple of our distributors out in the Midwest, in the Colorado area, and in the Southeast in the Georgia area. Those are phenomenal distributors and we're very happy with The Home Depot. They're a great partner. They're a great customer. So that opens up new avenues for us as we think about things like parts. So there, we have Ferguson and some, we have The Home Depot, we have our traditional independents, and of course, we have Watsco and our partnership there. So we feel very – we think that distribution, of course, our 100,000 dealers is a competitive differentiator.

Timothy Wojs
Analyst, Robert W. Baird & Co., Inc. (Broker)

Q

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Okay.

Patrick P. Goris
Executive Vice President, Chief Financial & Strategy Officer, Carrier Global Corp.
A

I would also say that every time a transaction like this happens, it opens a window for us to enhance our agreements, our contractual agreements. So actually it's an opportunity from that point of view as well.

Timothy Wojs
Analyst, Robert W. Baird & Co., Inc. (Broker)
Q

Okay, okay, great. Maybe just on the data center business, just can you speak to just your confidence about getting to the $2 billion number this year? I know there's just a lot of, it is kind of a big ramp in the back half of the year. So just maybe talk about that and if you're on track there.

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

Yeah, I said, Pat, but I'll do this. We feel very good about it. Yeah, I mean, look, it implies a $1 billion in the fourth quarter. We have a complete, dedicated, integrated product management team that's cross-functional. It's a very, very collaborative, focused team that we have high, high confidence in achieving what we've had. It has not been easy. Some of the input cost challenges we've had has been the result of expediting parts from A to B, might be fans, it might be some other things.

So we feel good about achieving the number. What's happened this year is that we made commitments to especially hyperscalers, but some colos as well, where we had some new 2-megawatt, 3-megawatt air-cooled chillers. The designs were still being completed while we were releasing the bill of material to our supply chain. What happens once you have a stable design, which we now have? So the 2-megawatt, 3-megawatt totally, we've passed all of our first-of-a-kind testing. They've been witnessed. The design is stable. The BOM is stable. The bill of material is stable. It's out in the supply chain.

Once you do that, then your expedite fees and some of the issues, the startup issues that you have, some of the takt time issues that you have in your factory, those are very normal for your first builds. Those are now behind us. So what happens now is now you start your dual and multi-sourcing. The new factory we're building in Texas, we've created, I was there yesterday.

We have space for a whole series of insourcing some of the key subassemblies, not exclusively, but we will have ourselves as an alternate source to our suppliers, some of the key subassemblies. So now what you do is you have a stable design, you improve takt in your factory, you have dual and, in some cases, multi-sourcing, all of that expediting starts to subside. And that's what we'll see as we go into next year.

Timothy Wojs
Analyst, Robert W. Baird & Co., Inc. (Broker)
Q

Okay, great. Patrick, as we kind of think about kind of 2027, if there's any kind of swing factors that you can kind of talk about kind of big picture. And I know you guys kind of committed to double-digit EPS growth, but just kind of any big picture things that we should think about there?

Patrick P. Goris
Executive Vice President, Chief Financial & Strategy Officer, Carrier Global Corp.
A

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Yeah, so the big swing factors obviously are going to be the levels of organic growth. Dave mentioned earlier he's very comfortable with the 6% to 8%, but if you look at our visibility there, our backlog for data centers at this point for next year is already over $2 billion. And Dave mentioned that we're comfortable that our data center sales next year will be about $3 billion, maybe a little bit more.

So from a backlog point of view, it looks really good there. $1 billion of data centers is already 4 points of organic growth for the total company. Add aftermarket, we would target, of course, another year of double-digit growth. Dave mentioned we've done that 5 years in a row. But that adds another point or two. So that alone, with no contribution from any of the other businesses, gets us to about 6% organic growth. So growth factor looks good from a sales perspective, driven by data centers and aftermarket. And then of course, with potential from the other shorter cycle businesses.

The other swing factor clearly is going to be what's happening with price, cost and productivity. And that is the element we talked a lot about this year. This year, we're having a headwind of $800 million in incremental input costs. We're driving price and productivity to offset as much as possible of that. We know at this point that our headwind next year from input costs will be $500 million, a little bit more than that. And so that's why we have announced additional price increases. That's why we're driving additional productivity. And so a big swing factor for next year clearly will be price cost and then productivity, what the net impact is of that.

Timothy Wojs
Analyst, Robert W. Baird & Co., Inc. (Broker)

Q

Okay.

Patrick P. Goris
Executive Vice President, Chief Financial & Strategy Officer, Carrier Global Corp.

A

And so that's our focus now. The good thing is, we know it now. In 2026, this year around Easter weekend, we woke up and three days later we had a $300 million plus headwind surprise because of tariffs. So we have better visibility now unless there are additional surprises.

Timothy Wojs
Analyst, Robert W. Baird & Co., Inc. (Broker)

Q

Okay. Okay. And then as you kind of think about kind of the margin mix in Americas and things like that, I mean, it does seem like that kind of dynamic will kind of phase in through the year. I mean, it seems like even if Americas margins have some pressure next year, just that's your highest margin business, your fastest growth business. So at an enterprise level, you do get some mixed benefits from that in aggregate, right?

Patrick P. Goris
Executive Vice President, Chief Financial & Strategy Officer, Carrier Global Corp.

A

Yeah, you're not going to hear us say now that Americas margins next year will compress. So we're not there. But clearly, the fastest growing region next year is expected to be the Americas. And as long as the Americas grows faster, and actually the commercial HVAC business in the Americas is a good business, we can see total company margins increase. So it doesn't mean that if Americas margins would decline, which we're not saying, that the total company margins wouldn't go up.

Timothy Wojs
Analyst, Robert W. Baird & Co., Inc. (Broker)

Q

Yeah.

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Patrick P. Goris
Executive Vice President, Chief Financial & Strategy Officer, Carrier Global Corp.

A

You also heard us say that there is a lot of focus, not just in the Americas, but also in Europe, on margin expansion, as there is for the two other segments as well.

Timothy Wojs
Analyst, Robert W. Baird & Co., Inc. (Broker)

Q

And then maybe just on that, I mean, obviously Europe, I mean, it seems like just what we've seen with heat pumps and what we've seen with energy prices like that, and you've got a new leader there, like that business does seem to be turning. So could you just talk about how optimistic you might be on the European business?

Patrick P. Goris
Executive Vice President, Chief Financial & Strategy Officer, Carrier Global Corp.

A

Well, the total environment is certainly better than it has been at any point in the last 2 or 3 years, which is really good. On the commercial side, we've seen after five or so quarters of modest order intake and not great sales performance, we've seen that turnaround. So we see significant order intake helped by data centers, and we see Commercial HVAC now returning to growth. On the residential side, as you mentioned, electrification is there. Our biggest market in Germany is picking up from multi-decade low heating units. And on top of that, we're seeing a big uptake in air conditioning. And so it looks well for growth in Europe in general. And I think we would be surprised if there wouldn't be revenue growth in Europe next year.

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

A

And to add to what Patrick said is it was good to see last quarter at double-digit margins and you're going to see us continue Thomas and the team continue to take the right actions on the cost side. We've done a lot with more to come on the cost side. So you should see margins continue to expand in Europe. And as Patrick said last quarter, we saw heat pumps up nearly 35%. Air conditioning sales up nearly 35%. There were 16,000 Germans that died this past summer in the heat wave. So the air conditioning opportunity in Europe is really having its moment. What's happening there is just not okay from a health and safety perspective. And if you look at the fact that we have Viessmann branded, Toshiba branded, Carrier branded, and the channel we have, we have the very unique channel because we're direct-to-installer. We're kind of having the moment. We, of course, wish we had this moment 3 years ago, but it's good that it's happening now.

Timothy Wojs
Analyst, Robert W. Baird & Co., Inc. (Broker)

Great. We're out of time, so please join me in thanking the Carrier team for being here today.

Patrick P. Goris
Executive Vice President, Chief Financial & Strategy Officer, Carrier Global Corp.

Thank you for having us.

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