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EDITED TRANSCRIPT

MOD - Q2 2017 Modine Manufacturing Co Earnings Call

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PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to Modine Manufacturing Company's second-quarter fiscal 2017 conference call. (Operator Instructions). As a reminder, this conference call is being recorded.

I would now like to turn the conference over to your host, Ms. Kathy Powers, Vice President, Treasurer, Investor Relations, and Tax.

Kathy Powers - *Modine Manufacturing Company - VP, Treasurer, IR and Tax*

Thank you. And thank you for joining us today for Modine's second-quarter fiscal 2017 earnings call. With me today are Modine's President and CEO, Tom Burke; and Mick Lucareli, our Vice President, Finance, and Chief Financial Officer. We will be using slides with today's presentation. Those links are available through both the webcast link as well as the PDF file posted on the Investor Relations section of our Company website, modine.com.

Also, should you need to exit the call prior to its conclusion, a replay will be available through our website beginning approximately 2 hours after the call concludes.

On slide 2 is an outline for today's call. Tom and Mick will provide comments on our second-quarter results; an update on our Strengthen, Diversify, and Grow strategic initiative; and review our revenue and earnings guidance for fiscal 2017. At the end of the call, there will be a question-and-answer session.

On slide 3 is our notice regarding forward-looking statements. I want to remind you that this call may contain forward-looking statements as outlined in our earnings release, as well as in our Company's filings with the Securities and Exchange Commission.

With that, it's my pleasure to turn the call over to Tom Burke.

Tom Burke - *Modine Manufacturing Company - President and CEO*

Thank you, Kathy, and good morning, everyone. On today's call I will discuss our second-quarter results and provide an update on our Strengthen, Diversify, and Grow strategic transformation, including the pending acquisition of Luvata HTS announced in early September. After that, Mick will provide a more detailed review of our consolidated financial results and review our revenue and earnings guidance for fiscal 2017. I will then provide a few closing remarks prior to opening the call for questions.

Like many other global industrial companies, we experienced a continuation of weak market conditions last quarter, especially in North and South America. Global off-highway markets continue to post significant year-over-year declines, except in China, where recent infrastructure investments are driving meaningful improvements in construction equipment volumes.

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Commercial vehicle markets are mixed, with Asia and Europe seeing solid growth, while North America continues to be weak. Unfortunately, we're not expecting to see improvements in the North America heavy-duty truck market until the second half of calendar 2017. On the positive side, global automotive markets continue to be strong, particularly in Europe and China.

Building HVAC markets have remained flat from the prior year, with weaker-than-expected preseason stocking sales of heating products in North America.

Overall, our sales in the second quarter were down 4% from the prior year on a constant currency basis. The largest decline was in our Americas segment, driven by two things: market weakness in heavy-duty trucks and in the off-highway market; and slower-than-expected new program launches.

Our adjusted operating income was $3.6 million, down $4.5 million from the prior year. Adjusted loss per share was $0.01 for the quarter, down $0.05 from the prior year.

Let me be clear up front: I am disappointed with the performance of this quarter. In addition to the volume decline, we also experienced temporary operational inefficiencies that I will describe in more detail during my segment review. Despite these challenges, I have high confidence in our ability to deliver a much improved second half, and am pleased that we'll be able to maintain our full-year guidance.

We are addressing these challenges head-on; and, in most circumstances, have already corrected the issues. We're able to improve, even in the face of continued market weakness, due to our focus on delivering the benefits outlined in our Strengthen, Diversify, and Grow strategy. We have achieved significant and sustainable savings to date from this program, and expect this to be evident in our second-half results.

Now I'd like to briefly review the segment results. Turning to page 6, as I mentioned, sales for the Americas segment were lower than expected, and our gross margins were also impacted by temporary operating inefficiencies. This was a very complex quarter for the North America team due mostly to challenging product transfers, multiple program launches, and wind-downs. We are actively addressing these issues, with the majority of these inefficiencies now corrected. This will contribute to a second-half earnings improvement.

Sales decreased 13% year-over-year on a constant currency basis, primarily due to continued weakness in the commercial vehicle and off-highway markets, partially offset by higher sales to automotive customers. Sales to commercial vehicle customers in North America were down 38% from the prior year, and off-highway sales were down 20%. Brazil continues to be in a recession, with declines in the commercial vehicle and automotive markets. Our largest year-over-year decline in Brazil was in our aftermarket business, which was down 26% versus the prior year.

Markets were down slightly, but the largest driver relating to the aftermarket decline was our SAP conversion in Brazil, which necessitated an extended shutdown for cut-over and implementation of a new warehouse management system. Modine Brazil is our last business unit to covert to SAP and we expect aftermarket sales to return to normal volumes for the second half of the year.

Gross margin declined by 370 basis points to 12.6%, due to the drop in sales volume and temporary operating inefficiencies in the quarter. As I mentioned earlier, we had higher manufacturing costs related to the transfer of production from Washington, Iowa, along with higher scrap and labor inefficiencies in both launches and planned reductions in sales. These concerns are now well in hand. In addition, we are ahead of schedule in transferring production from Washington, Iowa, and expect to cease production in the plant this quarter.

SG&A was up $900,000 or 6%, primarily due to a $1.6 million increase in a legal reserve in Brazil for a previously disclosed matter. This was partially offset by savings from our SDG initiatives.

Adjusted operating income in the Americas segment was $1.8 million, down $6.9 million from the prior year. As previously discussed, this is due to lower gross profit resulting from the lower sales volume and operating inefficiencies in the quarter.

Although we are not planning for significant market improvements in the second half of the year, we are already seeing significant improvements in our operating performance based on the actions addressing the issues I described earlier. We expect to see an improvement in volume from

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the product launches and in sales mix, along with continued benefits from the closure of the Washington, Iowa, plant and transfer of production to our expanded facility in Nuevo Laredo, Mexico. I just returned from Nuevo Laredo, and I was very pleased with the progress the team is making in launching our new facility.

Finally, we remain diligent in our cost reduction efforts, and we will continue to benefit from lower compensation-related expense due to headcount reduction.

Please turn to page 7. Sales for our Europe segment was down 3% in the second quarter on a constant currency basis as a result of planned program wind-downs and lower sales to off-highway customers. Our automotive sales were flat during the quarter as market-related volume increases were offset by a $4 million decrease in BMW modules, as this wind-down of production nears completion.

Gross margin improved by 160 basis points from the prior year, despite the decrease in sales. This improvement was due to both favorable sales mix and operating performance.

The positive sales mix was due in part to the planned reduction of the low-margin Origami commercial vehicle radiator program and higher volumes of automotive oil coolers. The performance improvement was largely due to procurement savings and lower expedited freight as compared to the prior year.

I continue to be pleased with the operating performance of the European segment. Adjusted operating income was up $400,000 to $5.5 million, due primarily to the higher gross profit. We're seeing ongoing growth in our automotive engine business, and we see further opportunities in the market as Europe automotive OEs intensify their development of electric vehicles, where Modine is well-positioned with our proven technology for this growing market.

In addition, I am pleased to announce that we were awarded our first business win in Europe with our new global commercial vehicle radiator platform. As I previously mentioned, our focus is on expanding our low-cost country footprint in Hungary in order to offer the best possible products to our commercial vehicle customers at a competitive price. This win, along with other awards in India, China, and North America, validates our commercial vehicle radiator strategy.

Please turn to page 8. Sales for our Asia segment were up 41% compared to the prior year, on a constant currency basis. This improvement was primarily related to higher sales to automotive and off-highway customers in China, and incremental sales related to our new joint venture. We continue to see strong volumes for our automotive products from both market improvements and launch activities, particularly for automotive oil coolers. We are pleased with the growth of our Asia segment, and expect this high growth rate to continue.

In addition, we're finally starting to see improvements in the construction market in China, with substantial increases in the sale of excavators. We have a strong position in this market which has been depressed for several years, and I am encouraged that we are finally seeing market and volume improvement.

The higher sales volume led to a $1.6 million improvement in gross profit, or a 76% increase from the prior year. Gross margin improved by 310 basis points to 14.9%. Operating income for the Asia segment increased $2 million for the second quarter compared to the prior year, primarily due to higher sales volumes and lower SG&A expenses. I'm very pleased with the progress that our Asia team is making across the region in growing our business.

Turning to page 9, sales for our Building HVAC segment were up approximately 1% on a constant currency basis. In North America, there were lower sales of heating products during the preseason stocking season versus the prior year, and a lower sales of ventilation products for the school market, as our Canadian competitors benefited from the weaker Canadian dollar. This was offset by higher sales of both cooling and ventilation products in the UK.

Our team is focused on correcting the decline in gross margin, which fell to 25.8% in the quarter. This decrease was due mainly to product mix, as cooling products in the UK generally have lower margins than North American heating products. UK margins continue to be pressured by the labor

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inefficiencies, which we are actively addressing. Also, we have higher year-over-year depreciation expense related to the replacement assets associated with the Airedale fire.

Similar to the Americas segment, we expect to see significant sales and margin improvement in the second half of the year, particularly since that is when we customarily have stronger heating sales. We have put some additional resources and expertise in this segment, and are focused on making improvements to our UK business. This includes implementing aggressive pricing practices, reducing headcount significantly in both of our UK locations, and implementing across-the-board overhead reduction and spending limits. We expect that these actions will quickly result in improved profitability for this segment starting in the third quarter, with the full effect in the fourth quarter.

Please turn to page 10. Before turning it over to Mick, I'd like to give an update on our Strengthen, Diversify, and Grow objectives, including our pending Luvata HTS acquisition.

As announced on September 6, we have entered into an agreement to acquire Luvata HTS, a leading manufacturer of commercial and industrial coils, coolers, and related products, primarily for the HVAC&R markets. This acquisition brings together all of the key attributes of our Strengthen, Diversify, and Grow strategy, and is a key component in the transformation of our business into a more diversified thermal management company.

After the acquisition is completed, approximately 40% of our revenue will be from sales to industrial end markets, which is directly in line with the goals laid out in conjunction with our SDG framework. Luvata HTS will diversify our customer base, which is currently relatively concentrated in the vehicular segment; and will also reduce our exposure to these cyclical markets. Subject to customary closing conditions, we expect this acquisition and related financing to close by the end of this calendar year.

We are also on target to achieve gross cost reductions of $40 million to $50 million, designed to help move us toward a higher operating margin of 7% to 8%. In fact, we will benefit yet this fiscal year from a large portion of the cost reductions which will support our strong second-half earnings forecast.

As a reminder, our operating margin target is ultimately dependent upon revenue growth, since the metric is net of other economic factors. To date, we have identified or implemented actions that will lead to $40 million of total gross savings on an annual run rate basis.

To achieve these savings, we have focused on SG&A reductions, manufacturing footprint savings, and our global procurement initiative. Our team in North America has accelerated the timetable for the closure of the Washington, Iowa, plant. This production is being transferred to other Modine facilities and the plant will be closed during our third fiscal quarter, as I mentioned earlier.

We're also making changes to our European region, transferring production of certain product lines from our plant in Pontevico, Italy, to one of our two facilities in Hungary. We continue to work on our plant expansions in Hungary and Mexico, and are actively quoting from these cost-competitive facilities.

We have achieved significant savings from our global procurement initiative, and we are still identifying and negotiating additional savings as we work through a wide range of product and commodity value streams. The procurement teams have done an excellent job in driving these savings, even in markets where volumes were down year-over-year.

We announced the Strengthen, Diversify, and Grow strategic framework one year ago, and remain fully confident we'll be able to achieve the objectives outlined in that program within the specified time frame.

With that, I'd like to turn it over to Mick for an overview of our consolidated financial results and review of our fiscal 2017 guidance.

Mick Lucareli - *Modine Manufacturing Company - VP, Finance and CFO*

Thanks, Tom, and good morning. Please turn to slide 12. Our financial results on this page have been adjusted to exclude the non-cash charge of $39 million related to a voluntary pension lump sum payout, which occurred in the second quarter of last year. This payout was done to reduce

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the size, risk, and costs associated with our U.S. pension plans and we succeeded by reducing our pension obligation by over $60 million. Our U.S. GAAP income statement is included in the appendix of this presentation and our earnings release.

Starting with the top-line, our second-quarter sales decreased due to the continued weakness in certain end markets and program wind-downs in Europe. Sales decreased 4% on a constant currency basis, excluding an unfavorable currency exchange impact of $2.6 million. In our Americas segment, we continue to see lower sales in the North American commercial vehicle and off-highway markets. We also saw a temporary decrease in our aftermarket sales in Brazil, but expect these volumes to come back in the second half of the year.

Lower sales in Europe were primarily driven by a decline in off-highway sales and the planned wind-down of certain programs. These declines were partially offset by market growth across our automotive business. We also experienced strong growth in Asia due to higher launch volumes of our automotive engine products, and some recovery in the China construction market.

The gross margin decline of 120 basis points was somewhat higher than we would have normally anticipated, but we believe the dip is temporary in nature. We had a normal fixed cost absorption impact due to the decline in sales volume.

In addition, and as discussed last quarter, we passed along lower material cost to our customers. Last, there was an additional impact from temporary production inefficiencies in several plants, primarily in the Americas and Building HVAC segments.

In the Americas, challenges were primarily due to higher labor costs related to Washington, Iowa product transfer, along with scrap and labor costs related to new program launches.

In Building HVAC, our new leadership team is working to address labor inefficiencies and improve through-put in our two UK facilities. As Tom said, we are taking actions to address these issues, and expect significant improvement in the second half of the year. I am pleased to report the team's hard work on our procurement initiatives is generating savings, and helped to offset the operating challenges.

Moving on to SG&A, we are benefiting from our Strengthen, Diversify, and Grow initiatives, along with a relentless focus on cost control. The reported SG&A of $48.7 million includes two nonrecurring items. First, we increased our legal reserve in Brazil by $1.6 million, based on our current estimate of the cost that will be incurred to resolve this previously disclosed matter. In addition, we incurred professional fees of $3 million related to due diligence and integration costs for our planned acquisition of Luvata Heat Transfer Solutions.

Excluding these items, core SG&A was 4% lower than the prior year. Please note that during the quarter we recorded $2.1 million of restructuring expenses. These costs relate to the equipment transfer and plant consolidation costs in the Americas, and severance expenses in the Americas Building HVAC and Corporate.

Finally, we recorded a gain on an asset sale of $1.2 million as we sold a manufacturing facility in Europe during the quarter. Consistent with past practice, this gain was not included in our adjusted operating income.

Second-quarter adjusted operating income of $3.6 million was down $4.5 million, and our adjusted loss per share of $0.01 was down $0.05 compared to last year. The lower table on slide 12 shows the walk of our adjusted operating income. As usual, we have included a full reconciliation between our reported results and adjusted operating results in the appendix.

This was clearly a difficult quarter, as volume challenges in both the Americans and Building HVAC segments were compounded by the impact of unplanned production inefficiencies in certain plants.

That being said, I was pleased with our cost control, and we continue to see the positive impacts of our SDG initiatives. Similar to the past few years, we do anticipate a stronger second half of the year, and I will go over those details with you in a minute.

Turning to slide 13. Free cash flow in the quarter was $800,000, which is down from $18.5 million last year. This is due to the combination of several items, some of which are timing-related. First, we had lower cash earnings in the quarter. Next, operating working capital requirements were $3

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million higher. There were also other unfavorable changes in other working capital, including compensation and income tax accruals. And finally, capital expenditures were $3 million higher than the prior year, which is primarily timing-related.

Please note that we received $4.3 million of cash proceeds from the sale of a European manufacturing facility, which I mentioned earlier. These proceeds are not included in our free cash flow calculation.

We expect our full-year capital spending will remain in the $60 million range. We continue to forecast another positive year of free cash flow, mainly driven by the stronger second-half earnings. And our balance sheet provides the liquidity necessary to support our growth and diversification initiatives, specifically the announced acquisition of Luvata HTS.

$108 million in net debt was up $14.3 million from prior year-end. We also ended the quarter with $63 million of cash, and a net leverage ratio of one.

Now let's turn to fiscal 2017 full-year guidance on slide 14. First, we are confirming our fiscal 2017 full-year sales and earnings guidance. We expect sales to be down 1% to up 3% from the prior year. Throughout the Americas segment, we expect difficult market conditions to continue. This includes ongoing weakness in the North American off-highway and commercial vehicle markets, along with difficult economic conditions in Brazil. Currently our revenue is trending toward the lower end of our full-year range, but the impact will be largely offset by continued cost reductions and operational improvements.

Therefore, we continue to expect adjusted operating income to be $65 million to $71 million. This equates to an increase of 3% to 12% over the prior year. We will continue to drive margin and SG&A improvements through actions planned as part of our SDG initiative. We expect our adjusted EPS to be between $0.77 and $0.87. With our full-year tax expense to run between $12 million and $14 million.

Following the pattern of last year, we expect a much stronger second half of the year. First, we anticipate incremental sales and earnings as we approach the heating season in our Building HVAC segment. We expect our top-line will benefit from the continued ramp-up of program launches in Asia and improvements in the construction equipment market.

Much of the groundwork has been completed by our SDG initiatives to reduce and control costs. These actions will continue to positively impact our results in the quarters to come. In fact, much of the targeted savings are reflected in our fiscal 2017 results, which is helping to offset the volume challenges.

Last, and very importantly, we are already implementing operational improvements at several plants, and beginning to see the improvements. We anticipate labor efficiencies and overhead improvement in the second half. We have a lot of hard work ahead of us to finish the fiscal year on a strong note. We are also maintaining the focus on cost reduction initiatives to achieve our financial goals.

We are managing these activities while many team members are working diligently on completing the Luvata HTS acquisition by the end of the calendar year. Integration plans are well underway, and we are excited to combine these two great companies into one.

Finally, I want to point out that our current-year earnings outlook does not include any impact from the acquisition. We are planning to provide guidance on the combined Company in connection with our third-quarter communication.

Tom, I'll turn it back to you.

Tom Burke - *Modine Manufacturing Company - President and CEO*

Thanks, Mick. We continue to experience challenging market conditions in certain of our key end-markets. As Mick outlined, we are holding our guidance despite a difficult second quarter, and are confident that our performance will improve significantly in the second half of the year. In addition, our management team remains committed to the objectives we set out one year ago when we announced our Strengthen, Diversify, and Grow strategic framework.

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The acquisition of Luvata HTS is a key component of achieving these objectives, and we are pleased that we are on track to close on this transaction during the third quarter. As we previously reported, we expect this transaction will be accretive immediately, with targeted annual cost savings of approximately $15 million anticipated over a 3- to 4-year time frame.

As we are very deep in the integration planning process, I am confident we will be able to achieve these targets. Of course, we will provide an update after closing, as Mick said, likely in connection with our Q3 release.

We are very excited about the benefits of this acquisition as we continue to deliver on the commitments of our Strengthen, Diversify, and Grow strategy while transforming Modine into a more diversified thermal management company.

And with that, we'll take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). David Leiker, Baird.

Joe Vruwink - *Robert W. Baird & Company, Inc. - Analyst*

This is Joe Vruwink for David. I wanted to start, Tom, with some of the new business wins you discussed on the call. And just a couple of questions. Is it possible, first, to say, since the global product strategy was put into place or since you started thinking about quoting from Mexico, Hungary, the low-cost centers, whether your win rates or the pace of bookings have stepped up meaningfully from historical levels? Just trying to get a sense of whether, over the past year since that strategy was put into place, whether growth rates in the backlog have stepped up.

Tom Burke - *Modine Manufacturing Company - President and CEO*

Great question; and, clearly, yes. Our global products strategy has had a direct impact. Just at a high level, since being at Modine, we are in the best position of really understanding our product portfolio and aligning our cost strategy with that. That includes manufacturing footprint and our procurement strategies. So, yes, we are better positioned than we've ever been before, and that's being reflected in our win rate that we're very confident in. Especially as you look at engine products, where we have what we think a very significant position, that we have confidence that we can grow with a win rate that we have confidence in; and a more improving powertrain cooling win rate on the vehicular side.

So, clearly there's been an improvement. And I expect to see that will drive higher incremental organic growth.

Mick, you want to add anything to that?

Mick Lucareli - *Modine Manufacturing Company - VP, Finance and CFO*

No, Tom.

Joe Vruwink - *Robert W. Baird & Company, Inc. - Analyst*

And then with the lower-cost footprint, are you able to expand what you are bidding on? So, let's say there's a particular customer that typically is very tough on pricing. Modine, certainly this cycle, has walked away from a lot of business in order to bring returns up. Given the cost savings you have achieved, can you essentially go back to some of those programs and customers and now bid on them profitably?

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Tom Burke - *Modine Manufacturing Company - President and CEO*

I feel confidently, yes, that we can. Clearly the market pressures are continuing to increase. But clearly the cost reduction, the scale we put into our plants, the location, the low-cost footprint, the product designs themselves are really being aggressive on evolutionary improvements to take material cost out and improve performance has given us that confidence that we can go back and win against any competitor that's out there.

Joe Vruwink - *Robert W. Baird & Company, Inc. - Analyst*

And then I wanted to shift to the cadence of this fiscal year. Obviously this is a tough quarter for certainly people in my seat to model. It sounds like in your seat, there are things that can launch or not launch that creates some volatility.

So, any help maybe you can provide in thinking about the quarterly cadence going forward of whether this ends up being a very back-end-weighted FQ4 type year? Anything that can help maybe smooth the quarter-to-quarter modeling of your earnings.

Mick Lucareli - *Modine Manufacturing Company - VP, Finance and CFO*

Joe, it's Mick. I'll take that question. Last year, as you recall, we had a very similar situation; I think almost identical. Last year, the first half of the year, I think we were about $22 million of operating income, and nearly double that in the second half of the year. And this year, the first six months are about $22 million of operating income, and looking at a similar ramp rate. When we look at it, to help with the outlook and modeling the run rate of the quarters, we do see it happening similar to last year.

So running from Q2 to Q3, we see volume and sales increasing as we come out of the slow, typically our weakest,, slowest quarter. In Q2 we see some revenue increasing into Q3, and then further increasing in Q4. And then the same with resulting in operating income. We see sequential improvement from Q2 to Q3, and then further improvement from Q3 to Q4. So, not a stair step function, but probably more of a linear look, rising all the way from Q4, with the expectation of Q4 being the highest quarter of the year, similar to last year.

Joe Vruwink - *Robert W. Baird & Company, Inc. - Analyst*

And my last question related to this: it seems like achieving a 7% operating margin, maybe by FQ4, is possible, given where the guidance stands. And that would obviously be the low end of the SDG targeted range, I think it was the end of fiscal 2018.

It seems like end markets haven't helped you all in being able to deliver volume needed to get to that margin level. So the fact that you might be on track anyways seems like maybe the plan is running ahead of schedule, or you've been able maybe to uncover more than you expected. Am I thinking about this right, or forgetting something in the equation?

Tom Burke - *Modine Manufacturing Company - President and CEO*

I'll start, and let Mick add to it. Clearly, as I mentioned, that 7% to 8% sustainable is really depending on some top-line growth, as I mentioned in my comments. To your point, that is dependent. However, our targeted $40 million to $50 million of savings is starting to come into fruition. So we're at the low end of that range now that we feel we'll be hitting a run rate as we get through fiscal 2018. So that's encouraging.

And yes, I'd say as we look at the new organizational structure that's going to be a little bit leaner and meaner, and yet more focused on strategically managing our portfolio globally on the vehicular side, the changes that we're looking at the Building HVAC side, and of course, on top of that, the acquisition opportunity, we feel strong about that.

But clearly, overall in the vehicular segment, we need markets to come our way to really hit that on a sustainable level.

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Mick, you want to add to that?

Mick Lucareli - *Modine Manufacturing Company - VP, Finance and CFO*

Yes. I guess two points. When we get to Q4, I think, yes, we can touch the low end of that range, Joe. And hopefully, at that point, we can be talking about Luvata combined with Modine, which we know is going to help margin Modine up. That business runs a couple hundred [to] basis points higher in margin. So that will be an additional benefit. But without that, we can touch that. And you're right; it's really driven by -- we frankly have taken more cost out and we pushed harder on the cost as the markets have been a challenge.

When we built our goals and we talked the last year about SDG, we really felt that Modine running at a $1.5 billion run rate with the cost savings is a good model to get to that operating margin. So, we do need some support here from the end markets.

I went back and I've looked; you asked about the win rate. The order book -- the win rate is there in the last few years, just from the global off-highway and truck markets, just on unit volumes, I estimate that's at least a $200 million impact to Modine that we've been battling despite the win rate of new programs. We've had a lot of headwinds on, especially the heavy equipment markets partially offsetting those launch volumes.

Joe Vruwink - *Robert W. Baird & Company, Inc. - Analyst*

That's great color. I'll step back in queue. Thank you.

Operator

(Operator Instructions). Mike Shlisky, Seaport Global.

Mike Shlisky - *Seaport Global Securities - Analyst*

Wanted to talk, see if we can talk quickly here about maybe calendar 2017 already. Some of the major customers that you have across off-highway and on-highway have both put out some kind of outlook for 2017. And when you map it out, I wonder if you'll be able to -- if you're thinking maybe you'll be in the same range as you are for fiscal 2017 and your fiscal 2018, if everyone is looking flat to down modestly. Are you thinking roughly in the same band next year, potentially with some organic growth on some new product launches? Is that the way to look at it right now for calendar 2017?

Mick Lucareli - *Modine Manufacturing Company - VP, Finance and CFO*

Yes. Mike, it's Mick. I think it's early for us to comment on that. We're beginning the March year-end, we're beginning our planning season. And then, as usual, what we'll do in our next quarter, the January communication, is we'll provide some outlook to calendar 2017, as we normally do.

I think from what we see, and you're referencing, especially the off-highway, the heavy equipment, construction side, commercial vehicle North America, I think we are expecting flattish type markets in that area.

I think where we see potential growth is clearly continued growth on automotive in Asia; launching a lot of automotive engine products in North America and in Europe; and expecting further growth in Building HVAC. Then we have to model Luvata on top of that.

So, not to punt your question; I think certainly we've had the same concerns with some of the large OE's comments about next year. But we also have to model in some of the growth opportunities we see coming before we can net all that out for you.

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Mike Shlisky - *Seaport Global Securities - Analyst*

Got it. That's excellent color. Thank you. I also wanted to touch on Building HVAC. I was wondering if you could tell us if you have a reason why it was somewhat weak here in the fiscal second-quarter. And whether already in October, now that we're getting closer and closer to the wintertime, are you seeing any improvement there, just over the last couple of weeks, at least?

Tom Burke - *Modine Manufacturing Company - President and CEO*

Well, I think we spoke about this before, Mike. We came off of last winter with people having stock on their shelves at our distributors, so the restocking was lower. And I think there was a fear of building up too much stock going into the season again. So we have anticipated that we should see an improvement with the winter season coming on. This is the quarter to do it. October sales are up, okay, from the prior quarter and prior month.

So, we're hoping that that trend continues on for the rest of this quarter. But the biggest dynamic is just the inventory management at our distributors. And then, of course, the cold snap that generally occurs in this quarter, going forward.

Mike Shlisky - *Seaport Global Securities - Analyst*

All right. I also want to ask about, in the Americas segment, the Brazilian ag industry has got an emissions-related changeover starting on the first of the year. And I was wondering -- and of course, that market also seems to be on the ag side, at least flattening out, if not improving for the rest of this year.

I was wondering if you had any kind of view whether that emissions changeover is helping your business in Brazil this year, and/or if you think it will help you next year if there's some higher needs for cooling technology there.

Tom Burke - *Modine Manufacturing Company - President and CEO*

It is definitely helping now. We are winning just about everything we quote on down in Brazil, as far as being very satisfied with our targeted ag, in construction, in growing commercial vehicle. But clearly the products we brought down there are to support that transition. We're winning the business. Obviously the markets are extremely low, so it's not really turning into the revenue that we'd like to see. But when it comes back, we're gaining market share significantly in Brazil.

Mike Shlisky - *Seaport Global Securities - Analyst*

Okay. And then also I wanted to see if anything has changed for you since you announced it, with respect to the financing terms or interest rate for the Luvata deal. Is everything the same as when you first said it? Or have you or are you seeing anything better on the interest rate side, if you have any debt to raise?

Mick Lucareli - *Modine Manufacturing Company - VP, Finance and CFO*

No. Everything has been proceeding just as planned, Mike; no changes. And we expect to complete all those financing agreements very shortly.

Mike Shlisky - *Seaport Global Securities - Analyst*

Okay. If I can just squeeze in one last one here, back to Building HVAC. Is the outlook for Luvata the same as, or similar to, your current Building HVAC segment? Or do you see that as having a whole different set of factors we should be watching over the next 12 to 18 months?

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Tom Burke - *Modine Manufacturing Company - President and CEO*

I think there are similar factors. But, clearly, they cover a much broader market than our Building HVAC folks, which tend to focus on heating, ventilation, and in air-conditioning; though they supply a lot of refrigeration and everything else that's out there, as far as food storage and industrial applications, as well.

But in those applications that are similar to Building HVAC, the drivers are similar. Clearly the tech drivers are significant, with getting from the field to the market. And a lot of things going on in food storage that's really, we feel, is a great tech driver that they are well positioned for; and other similar type things that right now that we aren't really involved in. So we're looking forward to those key markets that will join that we'll be able to benefit from going forward.

Mike Shlisky - *Seaport Global Securities - Analyst*

Okay. Great, guys. I'm going hop back in the queue. Thank you.

Operator

Thank you. And I'm showing no further questions from our phone lines.

I would now like to turn the conference back over to Kathy Powers for any closing remarks.

Kathy Powers - *Modine Manufacturing Company - VP, Treasurer, IR and Tax*

This concludes today's call. Thank you for joining us this morning, and thanks for your interest in Modine. Good-bye.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This does conclude the program, and you may all disconnect. Everyone have a wonderful day.

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