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Q2 2019 Modine Manufacturing Co Earnings Call

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CORPORATE PARTICIPANTS

Kathleen T. Powers *Modine Manufacturing Company - VP of IR & Tax and Treasurer*
Michael B. Lucareli *Modine Manufacturing Company - CFO, CAO & VP of Finance*
Thomas A. Burke *Modine Manufacturing Company - President, CEO & Director*

CONFERENCE CALL PARTICIPANTS

Joseph D. Vruwink *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Associate*
Matthew T. Paige *G. Research, LLC - Research Analyst*

PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to Modine Manufacturing Company's Second Quarter Fiscal 2019 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 of Investor Relations and Tax.

Kathleen T. Powers *Modine Manufacturing Company - VP of IR & Tax and Treasurer*

Good morning and thank you for joining our conference call to discuss Modine's second quarter fiscal 2019 results. I am here with 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, which can be accessed either through the webcast link or by accessing the PDF file posted on the Investor Relations section of our website, www.modine.com. This morning, Tom and Mick will present our second quarter results and update our revenue and earnings guidance for fiscal '19. At the end of the call, there will be a question-and-answer session.

On Slide 2 is our notice regarding forward-looking statements. 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.

Thomas A. Burke *Modine Manufacturing Company - President, CEO & Director*

Thank you, Kathy, and good morning, everyone. Our top line momentum continued this quarter, as our global team drove record second quarter sales and overall double-digit top line growth on a constant currency basis. In particular, our CIS segment made a solid contribution with significant increases in both sales and earnings. However, we were not able to convert on sales as planned in our VTS segment in part due to continued cost pressures driven by the direct and indirect impact of tariffs as well as isolated operational inefficiencies we are continuing to work through.

Overall, sales increased 8% or 10% on a constant-currency basis. Each of our segments reported sales growth and all of our major end markets showed positive top line growth. Our first quarter adjusted operating income was $26.5 million, down slightly from the prior year. Mick and I will provide more details on the drivers, but growth in the CIS segment was offset by lack of earnings conversion in the VTS segment, which came in well below our expectations. Although our second quarter earnings were somewhat below our expectations, we are still planning to have a record year with solid sales and earnings growth.

Before moving on to the segment results, I also wanted to mention that our Board of Directors recently approved a 2-year, $50 million share repurchase program. The last time we had an authorization in place was in 2015 prior to the Luvata acquisition. This authorization demonstrates our Board's confidence in the future of our business and in our ability to continue to execute on our strategic initiatives.

Now I would like to briefly review the segment results for the second quarter. Turning to Page 5, sales for the VTS segment increased 8% or 10% on a constant-currency basis to $335 million. This increase was driven primarily by a 24% increase in sales to off-highway customers primarily in North America and in Asia. We also benefited from a 6% increase in sales to automotive customers despite declining sales in Europe.

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Commercial vehicle sales were up 2% with increases in the Americas more than offsetting a decline in Europe. We continue to have a significant sales growth in Asia, where sales were up 26% from the prior year, driven by multiple program launches. In addition, sales in the Americas were up 15%, driven by improvements across all end markets and again, multiple new programs. Europe, sales were down 4%, driven primarily by lower sales of powertrain cooling products to automotive customers in line with the market.

Adjusted operating income for the VTS segment was $16 million, $4 million lower than the prior year. And adjusted operating margin was down 160 basis points to 4.8 -- down to 4.8%. As I mentioned, we were not able to convert on the higher sales volume in this segment due to a number of factors, some of which were within our control and others that were outside of our control.

Like many industrials this quarter, we are still experiencing the year-over-year impact of higher material costs. Although we continue to benefit from the pricing provisions in our contractual material pass-through agreements, this only covers the LME component of the cost. Much of the impact of our cost has been driven by other factors, including fabrication and freight. This resulted in a net impact in the quarter being negative. A big driver of these increased costs were the direct and indirect impact of tariffs that are being imposed on our raw materials. These tariffs are not only increasing the cost of the components that we import, but are also disrupting our domestic supply base. Domestic aluminum and steel suppliers are continuing to leverage their positions related to import tariffs and have raised prices as expected. As we renew our supply contracts, we're receiving significant increases in fabrication costs. In some cases, we're even being asked to find other sources.

In addition to fabrication costs, the Midwest transaction premium has doubled from the prior year and is adding to our increased cost. As you may recall, this premium covers freight and warehousing cost that historically have been relatively stable.

In addition, we're continuing to file for exclusion requests on imported components that are now subject to tariffs. The requests that have been submitted so far are pending without comment. Although there have not been any objections raised, we do not know when or if we will receive an exemption. For those imported components where we do not believe we'll receive an exemption, we are working diligently with our customers to pass along the cost, but this is a complicated and time-consuming process. We are invoicing these costs, but in most cases, the customers are requesting more information and have not paid. We are working through this process and are together evaluating whether there are alternative sources for these materials.

Second, we are still experiencing operating inefficiencies at a few of our VTS plants as a result of the many new program launches. We are disappointed that the inefficiencies have dragged on longer than we expected, and are working to address these issues that are within our control. We have deployed some of our most experienced operational leaders to these sites, and I am pleased by the improvements we have seen over the recent weeks, and I am confident that we will achieve our expected improvements in the second half of the fiscal year.

Please turn to Page 7. Sales for our CIS segment increased 9%, or 10% on a constant-currency basis, to $178 million, primarily due to a 65% increase in sales to data center customers in North America and Europe, partially offset by a 30% decrease in sales to the industrial markets. As I mentioned last quarter, the decline in industrial market sales relates to the lower sales of transformer oil coolers in China, based on the government's recent pullback in the development of high-voltage, direct-current power grid systems. This was expected and was also the cause of the drop in Asia. Sales in the Americas were up 24% and sales in Europe were up 1%. In Europe, higher data center sales were partially offset by the lower industrial sales. Excluding the impact of the data center sales, growth in the Americas is low-single-digits driven by higher commercial HVAC and refrigeration sales.

From a product standpoint, sales increased for coils and coolers, while sales of coatings were flat. Coolers increased by 19%, driven by the sales to data center customers, in line with the ongoing expansion of data center capacity.

This segment reported operating income of $12.9 million, a $3.9 million or 43% improvement over the prior year. The operating income margin was up 170 basis points from the prior year to 7.2%. This improvement was due to the higher sales volume, favorable sales mix and lower SG&A as a percent of sales. Overall, I am very pleased with the performance of the CIS segment. When we completed this acquisition nearly 2 years ago, we knew it was the right move for Modine. Now we're seeing the benefits to our diversification strategy as we continue to serve the growing global opportunities such as data center market where countries are increasingly demanding additional

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capacity.

Turning to Page 9. Sales for our Building HVAC segment increased 4% on a constant-currency basis to $50.7 million. From an end-market perspective, sales to the commercial HVAC customers increased 4% and sales to data center customers increased 3%. From a product standpoint, the increase in sales was primarily driven by a 4% increase in heating products in North America and an 18% increase in aftermarket and service sales primarily in the U.K. Sales in North America were up 3%, driven by higher sales of heating products, partially offset by lower ventilation product sales. Sales in Europe increased 6%, driven by higher data center and aftermarket and service sales. Adjusted operating income increased 3% from the prior year to $6.5 million. This increase was driven by higher sales volume along with a slight decrease in SG&A expense. Adjusted operating income margin was down slightly to 12.8%, compared to 13% last year.

We also continue to see strong order activity in our Building HVAC segment in both North America and in the U.K. We continue to grow our leading market share for gas unit heaters in North America and have seen -- and particularly have seen strong sales in Canada. In the U.K., we have recently had several large data center orders for both our chiller and precision air conditioning lines. We also continuing to focus on the Greenhouse segment where our high-efficiency products are some of the first in the industry to connect to the building management systems allowing for greater energy efficiency.

With that, I'd like to turn it over to Mick for an overview of our consolidated financial results as well as to provide an update on our outlook for the remainder of fiscal 2019.

Michael B. Lucareli: Thanks, Tom. Good morning, and please turn to Slide 10. First, I want to say that we remain on track for another record year of sales and earnings despite some VTS challenges in the quarter. Sales increased $41 million or 8% including a negative FX impact. Revenue improved in all business segments this quarter, with the highest rate of growth in the off-highway and data center markets. Gross profit of $88 million was up 2%, but our margin was down 100 basis points. The Building HVAC margin was in line with our expectations and CIS showed significant improvement.

On the VTS side, we had positive impacts from higher sales volume and ongoing purchasing initiatives. Unfortunately in the quarter, we continued to see higher material costs and we did not realize the anticipated level of operating improvements. Given the material cost challenges, we are tightly managing SG&A. At $63 million, it improved 70 basis points as a percentage of sales, as we continue to leverage our top line growth. The 2% increase in SG&A was due to normal increases in employee compensation and also includes $1.9 million of environmental charges. Adjusted operating income was $26.5 million, down slightly and mainly due to the gross margin decline in VTS.

Please note that in the appendix is included an itemized list of adjustments to operating income and a reconciliation to our U.S. GAAP results. These adjustments totaled $3.7 million and relate to the sale of our small South Africa business, and environmental charges related to previously-owned manufacturing facilities.

I also want to point out that we recorded a benefit in the U.S. GAAP income tax line this quarter of $22.9 million. This included a $10.8 million benefit related to adjustments of the provisional charges related to tax reform. In addition, we were able to record $13.6 million -- well, a $13.6 million benefit for foreign tax credits that will be utilized in the future. Both of these benefits are excluded from the calculation of adjusted earnings per share. After adjusting for tax reform and foreign tax credit benefits, along with certain other items, we had a low effective tax rate of just 5%, our adjusted earnings per share of $0.35, which is down $0.01 from the prior year.

Let's turn to cash flow on Slide 11. Our operating cash flow year-to-date of $37 million benefited from a strong second quarter, which was $41 million. Second quarter free cash flow was $26 million. Year-to-date, our working capital has been running higher due to strong sales across the company offsetting the improved cash earnings. Based on the current trends and outlook, we expect our full year free cash flow to be in line with the prior year. And our leverage ratio is 2.4, which is within our target range of 1.5 to 2.5.

Last, as Tom mentioned, I'm very pleased to report that our Board recently authorized a $50 million share repurchase plan. We will follow our capital allocation strategy and balance repurchases with our priorities of investments that support diversification and growth.

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In addition, we remain committed to continuing to delever our balance sheet and keeping our leverage ratio within the targeted range.

Now let's turn to our fiscal 2019 guidance on Slide 12. We adjusted our outlook based on the most recent quarter and evolving tariff situation. In short, we are holding our revenue and adjusted earnings per share while slightly lowering our adjusted operating income. With regards to revenue, we continue to project sales to be up 3% to 8%. We expect ongoing vehicular market growth driven by global off-highway sales. With regards to CIS and Building HVAC, we expect low-to mid-single-digit market growth, with our sales outpacing the market. In addition, we expect the second half will be better than the first due to operational improvements in VTS, the North American heating season -- seasonality and continued strength in our data center markets.

As Tom and I both covered, the tariff situation is creating multiple cost challenges that our teams are working through on a continuous basis. We now expect our adjusted operating income to be in the range of $130 million to $140 million, about 3% to 4% below our previous range of $135 million to $145 million. Despite the adjustment, we continue to see year-over-year growth of 8% to 17%.

As usual, I want to briefly review some of our key assumptions. First, metals prices have stabilized, yet we anticipate this will be an ongoing headwind until our pass-through agreements adjust. This includes the Midwest transaction premium in the U.S. that is still up over 100%. Second, we expect annual interest expense of approximately $24 million. Third, we are using current foreign exchange rates, which result in a slightly negative impact year-over-year.

And finally, we expected our adjusted tax rate to be approximately 22% to 23% in fiscal '19 versus 12% in fiscal 2018. This is better than our previous expectation due to the recent tax planning and second quarter actions. Given the lower expected tax rate, we anticipate adjusted EPS to be -- remain between $1.50 and $1.65.

And just to wrap up, we are currently seeing operating improvements within our VTS segment and we expect to regain our positive momentum through the remainder of fiscal 2019.

Tom, I'll turn it back to you.

Thomas A. Burke ***Modine Manufacturing Company - President, CEO & Director***

Thanks, Mick. Turn to Slide 13, please. As I mentioned last quarter, we continue to focus our strategy around our core strategic building blocks of Strengthen, Diversify and Grow. And we'd like to provide an update on where we stand today. First off, our focus continues to be on driving growth. We have several areas that we are targeting for improved organic growth across our segments. In our VTS segment, we continue to believe that the electrification of buses and other on-and-off highway specialty vehicles will develop quickly in the market. And we're in an advantaged position to provide thermal management solutions.

In our CIS segment, the growth this year has been led by sales to data center customers and we expect this trend to continue for the upcoming quarters.

In our Building HVAC segment, we will continue on our focus on our end markets, looking for ways to improve productivity and efficiency for our customers.

I previously mentioned the Greenhouse segment, but this can be extended to various forms of indoor industrial growing, where our products and controls can provide climate humidity control required for this growing market segment.

Our growth focus is not only organically focused. Our Strengthen, Diversify and Grow strategy led us to the decision to acquire the CIS business, which has proven to be a great move for Modine. As we look forward, we continue to look for opportunities for bolt-on acquisitions in both our CIS and Building HVAC segments. Our goal is to continue to expand our Industrial portfolio of products to sustain the long-term sales and profitable growth.

As discussed, this has been a challenging quarter with various items impacting our VTS margins. We continue to focus on improving operating margins by rapidly correcting inefficiencies and controlling our costs globally. We believe that actions we have already taken

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will lead to improved operating margins in the second half of the year, but we're also putting a heavy focus on further actions that will improve the overall return of this business segment in the current environment. Following a complete strategic review of our VTS business portfolio, we have a clear focus on where to prioritize our capital and ensure we are driving sustainable returns on investment.

We see clear opportunities in both the commercial vehicle and off-highway markets. With our recently-developed global product platforms for commercial vehicle and off-highway applications, I am very pleased with our recent business wins in both North America and in Asia. Modine just demonstrated at the IAA Show in Hanover, Germany, we have an advantaged position in the rapidly-growing electric bus market. We have the right products, technology and customer relationships to support electrification of these vehicles, along with other on-and-off-highway specialty vehicles.

Within our automotive markets, which makes up approximately 25% of Modine's total sales, we have a strong position with our engine and electric drive-train platforms. However, there are portions of this business that are highly capital-intensive and struggle to meet our financial targets. We have identified approximately $200 million of revenue in this area for strategic review. We are evaluating all options and capital investments for these product lines are being controlled judiciously. I will continue to provide updates as we proceed with our analysis and decisions as we go forward.

And with that, we'd like to take your questions. Thank you.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question is from Matthew Paige with Gabelli. Your line is now open.

Matthew T. Paige ***G. Research, LLC - Research Analyst***

Hey, good morning. Thanks for taking my question. I wanted to ask about the commercial vehicle market. There's been a lot of discussion there about constraints in the supply chain, especially in North America. So I wanted to hear what you were facing in terms of your own utilization. And if you aren't seeing any issues with your factories, is there an opportunity for you to gain share in the longer term?

Thomas A. Burke ***Modine Manufacturing Company - President, CEO & Director***

Well, clearly, there's an opportunity for us to gain share. I'll start with the end of your question and move forward. I mentioned we're really pleased with some recent product platform developments in our global design strategies that we're applying now. And that's resulting in business wins and share gain -- will result in share gain in the future. So that part I can confirm.

As far as the current supply chain constraint, we're not -- obviously, we're having some of the issues that I mentioned with materials because of the indirect effects of the tariffs that are putting some pressure on aluminum producers specifically, okay? And so we're watching that carefully and managing that. We have a cross-functional team between engineering, purchasing and materials that are in our chem lab of making sure that we're looking at every options that we can take to get around what might be a short-term constraint that's resulted from that. But right now, we feel that we're moving down a path and feel that we don't see any direct impact of supply delivery issues to our customers. But again, I'd just like to reiterate, very positive about our product platforms going forward and our position in North America specifically on the commercial vehicle and off-highway markets.

Matthew T. Paige ***G. Research, LLC - Research Analyst***

Great. I appreciate that color. And then just to touch on the last comment you made, what products fit into the electric drive-train product group that you mentioned that was up for strategic review, the $200 million of revenue?

Thomas A. Burke ***Modine Manufacturing Company - President, CEO & Director***

Yes, so that $200 million does not include our electric product portfolio, okay?

Matthew T. Paige ***G. Research, LLC - Research Analyst***

Okay.

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Thomas A. Burke ***Modine Manufacturing Company - President, CEO & Director***

What typically is -- if you break automotive down -- and we've talked about this a couple of times; I'll just slow down. We have -- essentially, in our automotive business, which is about 25% of total sales, we have a very strong automotive engine component business, okay? Those are components that are [mounted in] or integrated into the direct engine application or transmission oil cooling. Could be liquid charge air cooling, liquid condensers. That platform is doing very well and we're very excited about it. It also has -- able to convert into electric vehicle applications with things like chillers and other related components. So that part of the portfolio is very strong in automotive.

The $200 million result is really focused on what we call our powertrain cooling, or typically the things that sit upfront in the car, mostly revolving around air conditioning condenser business, but it's -- there's where we're seeing some challenges on getting returns where they need to be as far as hitting a return on capital requirement. So that's where we're looking at strategic review is that $200 million of what I would call the front end type components that sit on the front end of the automotive vehicle, condenser mostly, but some other powertrain-related components and that's what we're reviewing. The engine side remains a very strong key part of our business portfolio.

Matthew T. Paige ***G. Research, LLC - Research Analyst***

All right, understood. Thanks for the clarification and congrats on a nice quarter.

Operator

Thank you. (Operator Instructions) Our next question comes from Joe Vruwink with William Baird. Your line is now open.

Joseph D. Vruwink ***Robert W. Baird & Co. Incorporated, Research Division - Senior Research Associate***

Still Robert Baird. Hi, everyone. I wanted to start on VTS because -- and the last question kind of got at it -- there were a lot of disruptions in various vehicle markets during the quarter. And I'm surprised by how strong your growth ultimately still was. One region that specifically stands out is Europe, given that the German automakers reduced production by 20% to 25% in the September quarter. So can you maybe walk through in Europe specifically if you look at your performance excluding the commercial vehicle roll-offs, what adjusted organic growth might've been in Europe? And then from a global standpoint, did growth actually end up better than your expectation in the quarter within VTS?

Thomas A. Burke ***Modine Manufacturing Company - President, CEO & Director***

Well, let's start first on Europe, okay? They were down 4% I think year-over-year in auto Europe, if I -- or general sales --

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Michael B. Lucareli ***Modine Manufacturing Company - CFO, CAO & VP of Finance***

In the region.

Thomas A. Burke ***Modine Manufacturing Company - President, CEO & Director***

-- in the region, which of course, that region is about 50% automotive. Our automotive sales weren't down as much. Specifically, the drop in sales in German providers was from the lower-displacement diesel engines, our EGR application specifically, and is going towards -- and a lot of our business is going towards higher displacement diesel engines and also [petrol] engines. So we were I think kind of -- were able to not be as impacted by the impact you talked about as far as German sales being down. So I think from that end, it ended up being a good mix for us with what the market conditions did because of the changes in the test certification requirements that went into September. So from that standpoint, I'm pleased.

Now, I wanted -- the second part of your question was -- I want to make sure I understand what that was, Joe.

Joseph D. Vruwink ***Robert W. Baird & Co. Incorporated, Research Division - Senior Research Associate***

From a global basis, would you actually say VTS exceeded your expectation from a revenue standpoint?

Thomas A. Burke ***Modine Manufacturing Company - President, CEO & Director***

Yes, and clearly, being up 10% for adjusted inflation, it is what I would say [positive] again when we're forecasting it. We have a lot of new model launches that were happening this year. You know about the China launches that, again, I think up this quarter

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20-something-percent year-over-year and that's coming off a 50% quarter last year. Then we have a lot of launches going on in Mexico as well, supporting one of the big three providers on -- specifically on pickup trucks and some other big component launches. So you put that all together and saying that we manage through Europe with the mix that we have at a fairly decent level, you'd have to say that we're pleased with the growth.

We're not pleased with the conversion because we said, okay, in there we've got lots of ins and outs between materials that I'm sure you'll have a question or two on. But we'll rest assured that our operating inefficiencies that are really driven by these multiple program launches in two of our plants, okay, one in China and one in Mexico, are being addressed. I'm very pleased with the direction of the last, say, month on what we're doing. We're getting in front of that now, but again, that kept us from having from what I'd say is a really positive quarter despite the material issue.

Joseph D. Vruwink ***Robert W. Baird & Co. Incorporated, Research Division - Senior Research Associate***

On the profit conversion, so I understand lowering it by $5 million for the year isn't the hope for outcome, but at the same time, in thinking about some of the things that have impacted Modine over recent years, and particularly this Midwest premium, you've undertaken bigger hits to profit in the past. $5 million seems to actually be not that bad, and I'm just wondering does that reflect the improvements you've made from an organizational standpoint, from a procurement standpoint, from a footprint standpoint? Would that $5 million impact a few years ago have been $10 million, $15 million in this type of environment?

Michael B. Lucareli ***Modine Manufacturing Company - CFO, CAO & VP of Finance***

Yes, Joe, it's Mick, and we're nodding; Tom and I are nodding, absolutely. And you touched on a few of them. You know the journey we've been on to create a global procurement group, so just on that side, our global procurement team is already looking at options and negotiating and resourcing for a price increase, as Tom mentioned, we don't anticipate happening until calendar '19.

And then when you look at the total Modine, to me, it completely aligns with the SDG strategy Tom laid out. If you go back to the Modine that was 90% vehicular, you can't get away from material swings and a lot of what we're seeing in the market now. We jump ahead and you saw a 40% increase in earnings in CIS and we've got a very strong backlog in Building HVAC and we expect ongoing data center growth. I think the other big piece of us having good discipline and procurement in operations on vehicular is just now Modine is truly becoming that more diversified industrial. And I see it in all of our metrics.

Thomas A. Burke ***Modine Manufacturing Company - President, CEO & Director***

Joe, let me just add an echo to Mick's points. On a qualitative basis, we are much more focused as a strategic company delivering operational excellence. Procurement is a great example. We've brought in leadership from the outside that has put us at a, what I would say, a best-in-class kind of performance on how we manage our billion-dollar buy, okay? I'm really pleased with what that's driving strategically with our segments lined up the way they are now, and are driving strategic reviews. It's a lot easier in making sure we deploy globally the same strategy that can be applied to all markets.

Michael B. Lucareli ***Modine Manufacturing Company - CFO, CAO & VP of Finance***

Sorry, the one thing I would add, Joe, is that in addition to all the work we're doing in procurement, the tariffs alone are a significant cost increase to Modine. That part is really going to get back to our ability to negotiate and deal with our customer base, where there's no way we can absorb all of the tariff, the LME portion, the transaction premium, you know well, and pass-throughs. But in addition on the vehicular side, probably the biggest challenge every supplier has is the tariffs are increasing cost and that's going to have to be a commercial --

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Thomas A. Burke ***Modine Manufacturing Company - President, CEO & Director***

Yes, and so we -- to quantify that more, we have 5 customers that are about 90% of the challenge we have with the tariffs both indirect and direct. Our teams have done a great job of laying that out, getting it into the piece-price, invoicing it, as I mentioned. The reception from our customers have been varied, but typically, there's more questions they have that they need answered, like what are all the alternatives? Can you find me another source? So we're going through all the motions there we need to go through, but it is going to

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come down to discussions that I personally will engage myself in these discussions because I'm not going to be sitting here taking on -- absorbing issues that, quite frankly, need to be passed through. So I feel very confident that we're taking the right approach and I think we'll see improved results because of it.

Joseph D. Vruwink ***Robert W. Baird & Co. Incorporated, Research Division - Senior Research Associate***

Okay. That's good color. If I can switch over to CIS, where does Luvata stand relative to your plan at the time of the acquisition? It would seem to be running ahead of schedule in terms of profit contribution, but I guess the question is how far ahead of schedule might it be at this point?

Michael B. Lucareli ***Modine Manufacturing Company - CFO, CAO & VP of Finance***

I'll leave -- Joe, I'll leave it with it's ahead of schedule and to be fully transparent, whenever we do acquisitions, you have a range of assumptions and models. And we were lucky enough, when we acquired Luvata, Tom and I felt like we acquired it right, meaning you don't -- we had the discipline not to build everything into the purchase.

We've exceeded the synergies, I'd say, by $3 million to $5 million. And the margins are moving up faster than we have planned -- not everything. There's also challenges across that business. In certain markets, the data center is clearly a tailwind. I think we'd all tell you there's a heavy focus also just on operational improvements, delivery times, backlog, that kind of thing. But overall, I think we couldn't be more happy, both what's in our control and some favorable market dynamics is that we're ahead of plan.

Thomas A. Burke ***Modine Manufacturing Company - President, CEO & Director***

Yes, and let me just kind of qualify that by saying integration of a $600 million carve-out into Modine was a big challenge. We stepped up; we did that right. But that's happened right because of both sides of the equation were working together. I couldn't be happier with the cultural integration of the two businesses and how that's worked out. And the leadership team that was Luvata that's integrated itself is now CIS Modine, has done so very well.

Standard practices that we worked on every day to drive whether it's procurement operational improvements, all those quality systems, have really worked well together, so a very positive thing that gives us encouragement. As I mentioned in my comments, about moving forward with additional bolt-ons or acquisitions to go with that, we feel very confident about it.

Joseph D. Vruwink ***Robert W. Baird & Co. Incorporated, Research Division - Senior Research Associate***

And then maybe my last question still on CIS -- when you look at the order book you put together within the quarter, and I'm thinking on some of these markets like data center can be really volatile quarter-to-quarter, do you have an order book entering FQ3 where you at least feel confidence about maybe sustaining this really high rate of growth?

Michael B. Lucareli ***Modine Manufacturing Company - CFO, CAO & VP of Finance***

So from my side, when you look at forecasts and we talk to the team, Joel (sic), I think if you go by market, Joe, the answer is kind of different. So I would say what we've learned on the data centers is it tends to be cyclical, so we've -- you guys, we've all seen the industry go through a downturn. I think that lasted a year or more. All expectations from multiple sources and our customers is we expect data centers to continue the strength well into calendar '19 and that's good news for us. So we'd probably call that -- it can be lumpy over longer periods of time. We would fully expect at some point that market will go into another year of slowdown, but we're not seeing that.

The rest of that business, of CIS business, is really a very short window, visibility only out maybe 1 or 2 months. So we really rely on trends and what the teams are telling us at that point. But we knew that at the time, if you recall, and we also remind everybody that a large portion of that business is also replacement product. So we look at it as kind of a nice counterbalance to the rest of Modine.

Thomas A. Burke ***Modine Manufacturing Company - President, CEO & Director***

And I would just add, Joe, that the CIS element is what makes us great. On the Building HVAC side, with data center cooling, we're also seeing -- although this past quarter wasn't that dynamic, we're seeing in the order book, strong, strong sales coming in; as a matter of fact, one of our largest orders ever coming in that's now just being placed for data center improvements that'll drive chiller and precision unit -- precision air conditioning unit sales as well. So this is a clear mega-trend we're seeing that we're being -- benefiting from.

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Joseph D. Vruwink ***Robert W. Baird & Co. Incorporated, Research Division - Senior Research Associate***

That's great. I'll leave it there. Congrats on the quarter. Thanks, guys.

Operator

Thank you. And I'm not showing any further questions at this time. I would now like to turn the conference back to Kathy Powers.

Kathleen T. Powers ***Modine Manufacturing Company - VP of IR & Tax and Treasurer***

Thank you, and thanks for joining us this morning. A replay of this call will be available through our website in about 2 hours. We hope you have a great day.

Operator

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

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