Modine Manufacturing
Third Quarter Fiscal 2026 Earnings Call
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<u>Presenters</u>
Kathy Powers, VP, Treasurer and Investor Relations
Neil Brinker, President and Chief Executive Officer
Mick Lucareli, Executive VP & Chief Financial Officer

<u>Q&A Participants</u>
Matt Summerville - D.A. Davidson
David Tarantino - KeyBanc Capital Markets
Noah Kaye - Oppenheimer
Chris Moore - CJS Securities
Neal Burk - UBS
Jeff Van Sinderen - B. Riley Securities
Brian Drab - William Blair
Brian Sponheimer - Gabelli Funds

Operator
Good morning, ladies and gentlemen, and welcome to Modine's Third Quarter Fiscal 2026 Earnings Conference Call. At this time, all participants are in a listen only mode. Later, we will conduct a question-and-answer session, and instructions will follow at that time. If anyone should require assistance during the conference, please press star then zero on your telephone keypad. As a reminder, this conference call is being recorded. I would now like to turn the conference over to your host, Miss Kathy Powers, Vice President, Treasurer, and Investor Relations.

Kathy Powers
Hello and good morning. Welcome to our conference call to discuss Modine's third quarter fiscal 2026 results. I'm joined by Neil Brinker, our President and Chief Executive Officer, and Mick Lucareli, our Executive Vice President and Chief Financial Officer. The slides that we will be using for today's presentation are available on the Investor Relations section of our website, modine.com. On slide three of that deck is our notice regarding forward-looking statements. This call will 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, I will turn the call over to Neil.

Neil Brinker
Thank you, Kathy, and good morning, everyone. Before launching into our quarterly results, I'd like to take a moment to review some of the details from last week's announcement regarding the future of our performance technologies segment. Since launching our transformation at our

first Investor Day, we have made significant progress evolving our portfolio of businesses by investing in high-margin, high-growth businesses while improving our lower-margin businesses and making strategic divestitures. This past summer, we launched a process to divest our remaining automotive business and instead identified an opportunity to accelerate our transformation by spinning off the performance technologies segment and combining it with Gentherm, a leading player in thermal management and pneumatic comfort technologies.

Modine will receive approximately 210 million in cash, and Modine shareholders will receive stock in the new business in a tax-free distribution equaling 40% of the combined ownership. The combined business will provide renewed focus on investment and growth for performance technologies business and create cross-selling opportunities for Gentherm across new attractive markets. This values the performance technologies business at 1 billion or 6.8x the 12-month trailing EBITDA. This recognizes and reflects the hard work we put into improving margins in the business and allows current Modine shareholders to participate in future synergies and the strong earnings conversion we expect from the business once market volumes improve. The transaction presented an exceptional opportunity to find an ideal home for our PT business while maximizing value for our shareholders and further accelerating our transformation. The remaining business will consist of our current climate solutions segment plus corporate support functions. This is a business where we've been focusing on our investments for growth including six acquisitions over the past three years and the significant CapEx for expanding capacity for our data centers product. The transaction will allow us to further concentrate on these high-margin, high-growth businesses, allowing us to become a pure-play, highly focused diversified climate solutions company. This is the right transaction for Modine and for the shareholders at the right time, allowing us to further our vision of always evolving our portfolio of products in pursuit of highly engineered, mission-critical thermal solutions.

Now turning to our quarterly results and the strategic updates. Please turn to slide five. Our end markets in the performance technologies segment continue to be challenged, and volumes remained down this quarter. However, commercial execution and cost recoveries resulted in revenues increasing 1% from the prior year. The segment's adjusted EBITDA margin increased by 400 basis points to 14.8%, reflecting the hard work done over the past year to reduce costs and reallocate resources to the climate solutions segment. Now that we've reached an agreement with Gentherm, the next several quarters will be spent preparing the business to be spun off in anticipation of the combination. We will also be working on getting the necessary regulatory approvals for the transaction, which we expect to close in the fourth quarter of this calendar year. The performance technologies team has worked very hard to improve the business over the past several years and deserves the opportunity to grow. I'm confident that Gentherm will provide a great home for this business and the structure of this transaction will allow Modine shareholders to continue to participate in their success. We are at a major turning point for Modine. We are making unprecedented investments in the future of our company while simultaneously accelerating the transformation of our portfolio by merging our performance technologies segment with Gentherm.

Please turn to slide six. Our climate solutions segment delivered another quarter of outstanding growth with a 51% increase in revenues, including the contributions from acquisitions. Organic revenue growth from the segment was 36%, driven by a 78% increase in data center sales. Our capacity expansion remains on schedule, supporting the sequential margin improvement we saw this quarter. We commissioned four new chiller lines this quarter including the first two lines in Jefferson City, Missouri. We have four lines scheduled to come online in the fourth quarter, the final two lines in Grenada, Mississippi and the first two lines in Dallas. We have also launched initial production in Franklin, Wisconsin, providing additional capacity for the products currently produced in Calgary including air handling units and modular data centers. We are often asked if we are concerned about ending up with too much capacity. And the simple answer is no, not at all. Our current projections fully support the capacity we're putting in place based on known demand with existing customers. In fact, we had record order intake this past quarter, further solidifying our confidence in our strategy and financial projections.

Looking forward, if there's change in the mix of the products that we need to produce, we'll easily be able to pivot to other data center products on the same lines we are building today. A chiller line can be converted to produce modular data centers or large air handling units. This gives us flexibility to manage future demand and meet customer requirements in what continues to be a dynamic environment. We've also received many questions regarding the recent comments on the ability of next-generation chips to operate at higher temperatures and the potential impact to the future of data center cooling. First off, none of this was a surprise to us. We are constantly working with our customers to ensure that we are designing the data center cooling solutions they need today and into the future. Having a higher ambient temperature for water running through the liquid cooling loop is a positive development as it potentially reduces the energy required to run mechanical cooling processes by leveraging a hybrid technology utilizing free cooling options currently available on our chillers. In fact, we recently announced the launch of a new 3-megawatt turbo chilled chiller platform that is specifically designed to provide advanced free cooling heat rejection for high-density next-generation GPU-powered data centers. Power remains a focus for data center operations, so increasing PUE by reducing energy consumption in the cooling process is a major advantage and why we continue to gain market share. It is also important to realize that there are many different approaches to data center cooling, and our goal is to provide a full range of solutions that are customizable at scale.

We see our market opportunities continue to grow as we continue to invest in both capacity and product development to cement our position as a technology leader in the market. We previously shared our target of delivering over 1 billion in data center sales this year, and we remain on track to deliver on that goal. We have also shared that our current capacity expansion will allow us to reach 2 billion in data center sales by fiscal 2028, and I'm happy to report that we remain confident in this target, as well, further supported by our record order intake last quarter. We've recently updated our data center revenue projections and currently expect to deliver 50% to 70% annual growth in data center revenue over the next two years, which would put us comfortably ahead of this target.

Our confidence in this target comes from understanding our customers' long-term strategic road maps. The industry is moving towards long-term supply agreements that lock up supplier capacity in advance. Our team is actively engaged in these discussions, which we expect to lead to multiyear orders. Our recent success and growth stems from our 80/20 focus and market-leading technology. The feedback from our customers is clear. Our products are the most efficient on the market, resulting in substantial savings from lower energy costs. This allows us to be a key partner in developing next generation cooling products, cementing our role as a key strategic supplier. As we scale our production capacity, we are in a prime position to continue capturing market share. I'm very proud of all the hard work put in by the climate solutions teams this year. We've completed three strategic acquisitions and embarked on the largest capacity expansion in the history of the company, all squarely in line with our strategic goal of investing in high-growth, high-margin businesses. With that, I'll turn the call over to Mick.

Mick Lucareli
Thanks, Neil, and good morning, everyone. Please turn to slide seven to begin reviewing the Q3 segment results. Performance technologies revenue increased 1% from the prior year including a 3% decrease in heavy-duty equipment offset by a 6% increase in on-highway product sales. Despite typical Q3 seasonality and end market challenges, adjusted EBITDA improved 38% from the prior year, and the adjusted EBITDA margin increased 400 basis points to 14.8%. The margin increase was driven by significant cost reductions and improved operating efficiencies across labor, overhead, and materials. Pricing was also a benefit in the quarter driven by tariff recovery through surcharges and our normal pass-through mechanisms. In addition, with the reorganization of this business, SG&A expenses were nearly 7 million lower versus the prior year. As we look to Q4, we expect a sequential ramp in revenue, which will be primarily driven by the typical seasonal pattern. We remain focused on costs and operating efficiencies, which will allow us to drive higher operating leverage and margins when market volumes begin to recover.

Please turn to slide eight. Climate solutions delivered another quarter of strong revenue growth increasing sales by 51%. The main growth driver was data centers, which grew 130 million or 78% as we begin to capitalize on our investments and utilize the new capacity. As anticipated, there was a 31% sequential revenue growth for data center products in Q3, and we expect significant incremental volumes in the fourth quarter, as well. HVAC technologies sales increased 35 million or 48%, driven by our recent acquisitions and stronger heating product sales. Heat transfer solutions sales grew 14% or 17 million, mainly due to higher coils and coatings demand. Climate solutions third quarter adjusted EBITDA improved 29% given the strong top line growth. We made good progress this quarter with sequential improvement in the adjusted EBITDA margin to 17.9%, and we continue to expect further margin improvement in Q4. The Q4 margin improvement is expected to be driven by the increasing data center volumes and leveraging our recent capacity investments along with the ongoing integration of the last three acquisitions. Before moving on, I want to reiterate that, as the demand for Modine data center solutions continues to grow, we are again increasing our revenue outlook for the current fiscal year.

Now let's review the total company results. Please turn to slide nine. Third quarter sales increased 31%, driven by revenue growth in climate solutions. Gross profit increased 24%, driven primarily by higher data center sales volume in climate solutions along with the margin improvement in performance technologies. SG&A expenses increased 9% due to increases in climate solutions, which were partially offset by the performance technologies cost savings initiatives. Looking at earnings, I'm pleased to report a 37% improvement in adjusted EBITDA and a 70 basis point margin improvement to 14.9%. With regards to EPS, the adjusted earnings per share increased 29% to $1.19. Please note that this excludes the 116 million noncash settlement loss recorded in connection with the termination of our U.S. pension plan. I'm happy to report that this project was completed, removing a liability from our balance sheet along with the time and expense of the ongoing administration. To summarize our consolidated results, Q3 represents another good quarter of revenue and earnings growth. As we look to Q4, we continue to expect that the adjusted EBITDA margin will sequentially improve and begin to reach more normalized levels as the data center production volumes ramp up. Based on this outlook, we expect to exit the fiscal year at the highest quarterly margin rate and expect further margin improvement next fiscal year.

Now moving on to cash flow metrics. Please turn to slide 10. Free cash flow was negative 17 million in the third quarter. As discussed last quarter, the lower cash flow is primarily due to inventory builds and higher CapEx in climate solutions. However, this represents much needed and temporary investments to prepare for additional sales growth for our data center products. Also, third quarter free cash flow included 24 million of cash payments primarily related to the U.S. pension plan termination and restructuring. Net debt of 517 million was 238 million higher than the prior fiscal year including the three acquisitions completed earlier this year along with the incremental data center investments. Our balance sheet remains quite strong with a leverage ratio of 1.2, and based on our earnings and cash flow outlook, we expect that it will decline further by fiscal year-end. We anticipate generating positive free cash flow in the fourth quarter and are now expecting CapEx to be in the range of 150 million to 180 million for the full fiscal year. From a timing perspective, we anticipate that some of the data center capital investments will now carry over into the next fiscal year. And looking ahead to next year, we anticipate that our free cash flow will rebound, aligning with our long-term goals of improving the free cash flow margin.

Now let's turn to slide 11 for our fiscal '26 outlook. As we enter the fourth quarter, we're happy to announce that we are raising the revenue and earnings outlook. For fiscal '26, we now expect total sales to grow in the range of 20% to 25%. For climate solutions, we're raising our outlook for full year sales to grow 40% to 45%, up from 35% to 40%, with data center sales expected to grow in excess of 70% this year. For performance technologies, we're holding our sales outlook with revenue anticipated to be flat to down 7%. We expect that the end markets will remain depressed over the next quarter. As expected, more favorable foreign exchange rates and material cost recoveries will support sales, but the underlying market volumes are not recovering yet. With regards to our full year earnings, we're raising our fiscal '26 adjusted EBITDA outlook to be in the range of 455 million to 475 million. This reflects the strong performance this quarter and further improvement in Q4. To wrap up, we're encouraged with our Q4 outlook and fully expect to deliver another fiscal year of record sales and earnings. The teams have worked very hard to execute on our strategy using 80/20 as a guide. And the recent announcement to spin off performance technologies is truly historic. We remain confident that these actions are setting the stage for long-term sustainable growth for Modine shareholders. With that, Neil and I will take your questions.

Operator
Thank you. If you have a question at this time, please press the star then one key on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press star then two if you would like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the star keys. Our first question comes from the line of Matt Summerville with D.A. Davidson. You may proceed with your question.

Matt Summerville
Thanks. Morning. So, I want to understand a couple of things. Can you talk about kind of the puts and takes embedded in the margin outlook for both climate and PT in the fourth quarter? On the last conference call, you had sort of led us down a path whereby climate kind of ends the year in Q4 with further sequential margin improvement maybe in a range of 20% to 21%. So, if you can kind of backfill on the margins across the two segments. And then also help us understand what defines kind of the high and low end of the algebra on that 50% to 70% CAGR, because obviously, you extrapolate that out two years. It's a pretty wide range. Is it demand? Is it capacity? So, a little bit of help there, as well. Thank you.

Mick Lucareli
Yeah. Hey, Matt. It's Mick. Good morning. I'll go and then Neil can add on the CAGR comment. So, yeah, as we look at the outlook and for the balance of the year, I want to be clear about that. We are comfortable with the margin improvements in climate solutions after the 120 basis point sequential in Q3. We're still on track for a 200-plus basis point sequential improvement in Q4. So, we still see climate solutions in that 20% to 21% range. On the PT side, we do expect a step down in the EBITDA margin. So, that might be one thing that you're trying to model out. And we -- a couple of things happening there. One is we see this as a Q4 temporary dip. We've got some material pass-through mechanisms that will be catching up. We've had a spike in aluminum, copper, steel. We also have some timing of the tariff recovery and also some Q4 inventory cleanup write-off work that's been tied to our 80/20 PLS activities and some of the plant conversions we did from going from PT plants to data center plants. So, we're comfortable. I should also say we're comfortable with analyst estimates and dollars that have been out there in Q4, and that would imply we're trending above the midpoint of the

range. So, we are trending towards that above the midpoint of the range in dollars. But again, CS fully on track for a Q4 margin improvement, and that's being led by HVAC and data centers. And then a Q4 dip in margin for PT, and we expect PT to rebound in Q1 back to that 14-plus percent type range. So, let me throw it over to Neil, and then you can come back, Matt.

Neil Brinker
No, I think that's covered well, Mick. Any other questions on that, Matt?

Matt Summerville
On that note, if we can get to the kind of data center question on what defines kind of that high low-end range when you extrapolate out 50% to 70% growth off a '26 base of 1.1 billion plus, you get a wide range. Is it capacity? Is it timing? Is it demand? Maybe you can just help out a bit there. That would be great.

Neil Brinker
Yeah. When we think about that in terms of the capacity expansion, we're giving ourselves plenty of space there. As we get to further -- as we get further along in our project launches in the U.S., particularly in Jefferson City and Dallas, I think that we'll have -- we'll be at a tipping point of having the majority of capacity in place and online, and that would give us more confidence to tighten that range.

Matt Summerville
Perfect. And then as a follow-up, can you maybe talk about how we should be thinking organically around the non-data center businesses in climate over the course of calendar '26? Thanks, guys.

Neil Brinker
Yeah. At a high level, we're seeing good business particularly in the HVAC side in our heating product line. We've seen great business in orders in the indoor air quality portion of the group. We've seen, obviously, really good results from the acquisitions, and then we've seen some softness in the HTS business relative to the margins. There's been some pressure on the margins there as we've seen a spike in materials, and we've been able to obviously counter that through commercial activities like pricing, but we -- there's a lag there. So, we've got a little bit of time to catch that up.

Matt Summerville
Got it. I'll get back in queue. Thanks, Neil. Thanks, Mick.

Operator
Thank you. Our next question comes from the line of David Tarantino with KeyBanc Capital Markets. Please proceed with your question.

David Tarantino
Hey. Good morning, everyone. You mentioned record order intake in data center. Could you give us some color around the profile of these orders? How much of the growth is being driven by expanding relationships with customers and/or adding new ones versus your existing customer set? And what do you have embedded here in the longer-term growth profile around expanding these relationships beyond what you currently do?

Neil Brinker
Yeah. So, that's a good question in terms of the profile and the concentration. This expansion is coming with our existing customer base primarily. Certainly, we are actively working with all the hyperscalers but at different degrees and different levels. And there's potential for even greater upside when you think about some of these hyperscalers if we were to win orders at the order rates that we have with the ones that we have the longest relationships with. So, this order intake and the upside that we see is with our strongest relationships with our longest customers, and we're still working through and doing quite well with the other hyperscalers and some of the [inaudible] cloud providers, as well.

David Tarantino
Okay. Great. That's helpful. And then maybe just on free cash flow. The CapEx investments are pretty well documented. But could you talk about the working capital investment side of things related to the ramp and specifically what gives you the confidence that free cash flow begins to return to more normalized levels next year?

Mick Lucareli
Yeah. It's Mick. We've been trending about 19% to 20% working capital to sales. So, I think that's going to hold relatively well. But two things that were happening that will kind of cause us to get back to more normal free cash flow levels was the rate of the ramp that when we did the expansion this year when we announced it beginning of the year, a lot of prebuy. So, we actually have spiked above our normal inventory carrying levels. And then secondly, the amount of CapEx, whether you look at it as onetime spends or percentage of sales also had a spike. So, I think what will happen, David, is we'll trend back down. I don't think it will be a step function. Inventory working capital will trend back towards normal ratios to grow with sales. And same with CapEx. We'll still have some CapEx carrying over into next year and elevated. But as a ratio or driver of capital, we won't have -- this year is probably 200 million. We probably had $400 million that we invested in capital spending and working capital builds.

David Tarantino
Okay. Great. Thanks for the color, guys.

Mick Lucareli
Yes.

Operator
Thank you. Our next question comes from the line of Noah Kaye with Oppenheimer. Please proceed with your question.

Noah Kaye
Hey. Thanks for taking the questions, and good to see folks earlier this week at Expo. It was really helpful to get your commentary just now on the climate solutions margin outlook for 4Q. Basically, this is going to be then if you hit that a couple of quarters in a row where you get roughly, call it, 200 bps, 100 to 200 bps margin expansion sequentially even as you're adding a bunch of new chiller lines, right? So, I guess the question is really how do we extrapolate this and thinking about where margins could be going here? You've talked about kind of mid- to high 20s as a longer-term target. But should we think about that kind of margin progression as continuing into the future quarters as you continue to add more lines but get better absorption?

Mick Lucareli
A couple of things, Noah, that -- I wouldn't extrapolate and we're not implying that we'll have 200 bps sequentially every quarter. I think this was -- and we talked about it in Q2. We had a significant decline and was tied to the amount of fixed costs we added. So, to climb back out, we said we'd expect it to be kind of two quarters to pick up whatever that was, 400, 500 basis points. And then from there, it's going to be more of a normal climb step by step up. We've been clear with climate solutions that the goal next year would be 20% to 23%. We'll provide some guidance in our Q4. And a reminder for the group, when we announced our announcement on performance technologies, we're going to split and have two climate solutions segments. So, we can provide some other color in Q4 for data centers. But I'd say short until we come out with specific guidance by the two climate solutions segments, I think next year being -- taking that midpoint of that range is a fair starting point, and we'll tighten that up and give you some more color in Q4.

Noah Kaye
Very helpful. Neil, it's good to hear you talk about the record orders intake. Obviously, not historically disclosed orders. But can you talk a little bit about just sort of a sense of magnitude of that orders intake and also the composition, how diversified it is among the customer base? What does it imply about kind of your customer mix as we head into next year?

Neil Brinker
Yeah. Thank you. It's roughly 50-50 in terms of the products where 50% of it is with chillers and 50% is with the rest of the products that we have for the full solutions in data center. It's a larger -- more of the majority of the revenue is with our hypers. And what gives us great confidence is these are projects and programs that we've seen that have been in the funnel for a while, and they're starting to come to fruition in terms of purchase orders. So, long-standing relationships, strong relationships with these customers, seeing these things progress through our probability funnel moving from 40% or 50% probability into the 80% to 90% category at a

much heavier and faster rate than we've ever seen. So, those are the things that give us confidence in terms of our customers, who we're serving, as well as the products, knowing that we have the capacity to keep, and it consists with our ramp schedule that we're public about a couple of quarters ago.

Noah Kaye
All right. I'll take the rest of the questions offline. Appreciate it. Thank you.

Operator
Thank you. Our next question comes from the line of Chris Moore with CJS Securities. Please proceed with your question.

Chris Moore
Hey. Good morning, guys. Thanks for the taking a couple or so. Obviously, as you talked about, the 50% to 70% growth in '27, '28 recognizes the market dynamic, the mix of products there might change. I think on the follow-up call on the PT spin-off, you talked about chillers potentially being better than 50% of the mix in '28. Maybe can you just talk a little bit about how the ultimate mix impacts your margins and kind of what the biggest wildcards are?

Mick Lucareli
Yeah. I'll go first, and Neil can add. It's pretty uniform across the data center space. And so -- just take a step back. One thing I think Neil had covered and will help is we -- now that data centers has gotten to the scale, we think it's the right time to carve that out as a segment. But when you peel back the onion in climate solutions, what we've had over the last few quarters, right -- so, total segment is the three acquisitions we brought on and then Neil said on the coils or HTS side, we've had some lag effect on material pass-through. So, kind of putting that off to the side, that's had some impact in the margins that you've all seen. Across the data center then product portfolio, it's a pretty uniform margin profile. Obviously, we really like the service element. So, I don't think it's as much there. I would leave it at -- it's a pretty uniform -- mix is not going to be as big of a driver for us. The other one then the factor, as you know, over the last three to six months was just the amount of fixed costs we brought on with greenfield facilities. So, not to punt on your question, I think the main drivers are in data center capacity utilization and then less about product mix.

Chris Moore
Got it. I appreciate that. And maybe just a follow-up in terms of the capacity ramp. So, is the expectation that, by the end of fiscal '27, you will have the capacity in place to manage the high end, the 70% CAGR for both '27 and '28, '28 specifically. Is there more -- if you're doing that 70%, that implies in that $3 billion range in '28, will you have that capacity in place by the end of '27?

Neil Brinker
We would expect to have the capacity in place by the end of '27. However, they may not be at full utilization yet.

Chris Moore
Got it. Makes sense. I will leave it there. Appreciate it.

Operator
Thank you. Our next question comes from the line of Neal Burk with UBS. Please proceed with your question.

Neal Burk
Hey. Thanks for taking my question. Apologies if I missed this on capacity utilization, but I think your guidance based on my math at least has annual data center revenues kind of exiting the year at 1.6 billion. Is that the correct way to think about the annual number? And what is the kind of capacity utilization that that assumes?

Mick Lucareli
Yeah. A quick -- I'll jump in on that where, Neal, you're going. Yeah, our Q4 has implied a 400 million plus sales quarter. So, yeah, that would be an annualized run rate of 1.6 billion. Neil, do you want to add anything on capacity here?

Neil Brinker
Yeah. Again, capacity is in line with where we want it to be. We're -- it's as expected. We're getting more efficient. You saw it in the margin improvement this quarter, and we're very comfortable in terms of getting back into that 20% range as we continue to add more capacity to data centers.

Neal Burk
All right. Thanks. And one more follow-up, again, on the point of demand. I know you said record orders in the quarter, but maybe just like taking a step back. Like the data center pipeline as you see it, can you talk about how that's trending? And like specifically, do you have more visibility on future orders and revenues than you did, say, 6 to 12 months ago? Thank you.

Neil Brinker
Yeah. And that's an interesting question because I say yes to that every time that's asked every 6 to 12 months because it just gets bigger and bigger, and the visibility gets broader and broader. So, if you go back 3 years ago, we had 8 to 12 months visibility. And you go back a year ago, we had 24 months visibility, 36 months visibility. Now we're looking out as far as five years. And certainly, the top of the order funnel is swelling for sure.

Neal Burk
Thank you.

Operator
Thank you. Our next question comes from the line of Jeff Van Sinderen with B. Riley Securities. Please proceed with your question.

Jeff Van Sinderen
Hi. Good morning, everyone. Just kind of maybe this is a little bit premature, but given that your next fiscal year is upon us and you're ramping production, how do you think we might see the growth cadence of the climate solutions business trend in the next fiscal year? And might we anticipate sequential revenue growth for the next several quarters?

Mick Lucareli
Total climate solutions -- I want to make sure I understood your question. Yeah. Yeah. Well, I think I'd separate them again. I would expect -- again, Neil can jump in -- that at the greater growth in order intake on the data center side, and that's becoming a much bigger piece, right, of the entire climate solutions segment, that we will see sequential growth for quite a while on data centers. I have to go back and study a little bit the HVAC side. We get seasonal patterns with heat. And then you have a coil HTS business that can be heavy replacement and also some of that tied to residential OE customers. So, I think of that as more normal and that we've said that's probably a high single-digit organic grower annually. The last thing I'd say, I don't want to be too repetitive, but it will help when we give you some more color in Q4, and I could split those two dynamics. HVAC is a very different dynamic, HVAC&R versus data center. So, hopefully, that's enough color to give you some direction.

Jeff Van Sinderen
Okay. And I'm sorry, just to clarify, for Q4, are you going to start breaking out in the P&L, the two segments for climate solutions?

Mick Lucareli
So, beginning our Q1 with our new fiscal year, we will have three segments. We'll have a data center segment, a commercial HVAC segment, and obviously, performance technologies until that transaction closes. And we'll report as we have with our other segments revenue and earnings. What we'll just do in our Q4 is we'll provide some guidance for the new year outlook. But to be clear, I won't be able to give you those segment splits until we hit our Q1.

Jeff Van Sinderen
Okay. Fair enough. And then maybe for Neil, as you're talking to your data center customers, what is really top of mind for them at this point in determining their go-forward cooling needs? How are those needs evolving? And then I guess, as a result, how is Modine evolving its products for the future?

Neil Brinker
So, a few things. One is there's a lot of conversations about them now, which is securing capacity. How do we ensure that the strategic suppliers that they've selected are investing in

capacity and investing in production and investing in their own internal supply chains so that they can keep up with the demand as you see the hyperscalers continue to raise their CapEx spend? Almost every quarter, they're raising their CapEx spend. So, what are we doing now to ensure that we're in sync and locked in with their progress as well as their build-out? That's one. The next piece is around our innovation and technology. What are we doing to make sure that we deliver products that help them solve two critical problems. One is the lack of power, so energy consumption, and the other is around water and the amount of water that's used typically in some data centers. So, if we can continue to innovate and evolve with better use in terms of power and water, which are often measured through PUE and WUE, we can continue to improve their metrics and stay innovative in that regard. Those are two critical problems that we're trying to solve for in the industry in addition to keeping up with the breakneck speed of CapEx deployment.

Jeff Van Sinderen
Okay. Thanks for taking my questions.

Operator
Thank you. Our next question comes from the line of Brian Drab with William Blair. Please proceed with your question.

Brian Drab
Okay. Thanks for taking my questions. First, I wanted to ask on the capacity expansion. You have the -- it sounds like 1.6 billion in revenue capacity for sure now as you're going into the fourth quarter. But to get to the 3 billion, how much additional investment is this going to take? Just trying to get this whole framework in place. I think that Mick made some comments on the call last week, but we're getting a lot of questions on this. Like, how do you get to 3 billion? And does it -- how much additional investment beyond the 100 million that you talked about before? And then also, are you just getting there from some higher utilization or increased pricing? Can you frame all of that for us?

Neil Brinker
Yeah. High level, we can get there on the amount of capital that we've been public about in terms of what we needed to spend to get to the 3 billion. But 40 million of that will carry over from this year into the next fiscal year.

Mick Lucareli
Yeah. And we'll have another -- we had about 40 million of capital spending in Q3. So, just in Q4, and this is -- this will be equipment that won't even be producing really much in revenue. We'll have another 40 million to 50 million in Q4, and Neil just mentioned the 40 million plus amount that we'll spend in the new year. So, one other maybe data point, if you take that, almost 100 million left of that spending that Neil talked about that we've laid out that isn't even in these production sales numbers yet that will be supporting future sales growth.

Brian Drab
How many -- can I ask how many chiller lines would you be at as you enter fiscal '28 to execute on the plan?

Neil Brinker
20.

Brian Drab
Got it. And last question is, Neil, I don't know if you want to provide or if there's any update to provide on this, but you had talked late last year about a couple of new potential hyperscaler customers for chillers who had not purchased chillers in the past looking for sample product. And I'm just wondering are you -- how many total hyperscaler customers are you working with? And then can you give a specific update on anything that's developed and potential new customers for chillers specifically?

Neil Brinker
Yeah. Obviously, we're working with all of them at different levels of engagement. And then if you recall from last quarter, I talked about one of the reasons that we had that miss in the margins in data centers was that we had to cut production with a couple of hyperscalers that we hadn't sold chillers to in the past, and they needed some pilot builds for fiscal year '27 and '28. So, pending the results of the field trials, which we would anticipate to be in line with how we typically perform, we'll continue to grow with those other hyperscalers with chillers.

Brian Drab
Do they give you any visibility to when you hear about the field trial results?

Neil Brinker
Yeah. Typically, it will be -- we'll hear about it all the time in terms of we'll get feedback regularly, but a decision won't be made for a couple of quarters.

Brian Drab
Got it. Okay. Thanks for taking my questions.

Operator
Thank you. Our next question comes from the line of Matt Summerville with D.A. Davidson. Please proceed with your question.

Matt Summerville
Thanks. I just have one follow-up here. Neil, Mick, how are you strategically thinking about LTAs long-term agreements? How much of your capacity will you ultimately be willing to have sort of spoken for over what kind of time frame? And I guess, in turn, what price kind of considerations are you thinking about? And would you be able to structure these almost as a take-or-pay arrangement such that you're not absorbing risk?

Mick Lucareli
Yeah. Well, it's not that we couldn't structure -- it's not as if we could structure it in a way that it's completely risk-free. But certainly, it derisks substantially, and it gives you higher confidence and great confidence that the commitment of the customer is there, as well, particularly long term. So, certainly -- I mean, we'd be willing to do LTAs for all of our capacity. Why wouldn't you, right? So, we're -- that's definitely new and certainly a part of this capacity expansion equation that we're seeing with our large OEM customers. So, those conversations are being had. I think you've seen evidence of this happening with other suppliers that these things can happen. And we strategically align ourselves behind our 80s customers that we believe are our best customers, and those would be the ones that we would lean in on in terms of providing more capacity with an LTA.

Matt Summerville
Do you think, Neil -- obviously, it's been tough for you to name -- use specific customer names. If you sort of begin to go down the road where LTAs start getting signed, maybe absent specific customer names, is this something we can expect to be publicly announced and communicated?

Neil Brinker
Yes.

Matt Summerville
Okay. Very good. Thank you, guys.

Neil Brinker
Thank you.

Operator
Thank you. Our next question comes from the line of Brian Sponheimer with Gabelli Funds. Please proceed with your question.

Brian Sponheimer
Hi, everyone. Thanks for having me on again. I'm curious, the heavy focus on data centers and yet within this past fiscal year, you found LB White and Climate by Design. I'm just curious about that pipeline maybe outside of the data center set on climate from an M&A perspective. You're going to end pro forma. You'll be less than 1x levered when this is all said and done with Gentherm.

Neil Brinker
Yeah, you're right. CDI, Absolute Air, and LB White, certainly inside of that HVAC business as we continue to look at ways to diversify around some of these higher-margin businesses that are not typically in data centers. We believe we have what we need in the data center space. Right

now, we continue to cultivate the funnel. We're often in conversations and at different milestones with many potential targets. Probably over the next couple of quarters, it's all hands-on deck on our project with Gentherm but we can still work in the background on the active funnel that we currently have around additional businesses and technologies that we see would continue to help evolve our portfolio inside of the HVAC business for sure.

Brian Sponheimer
Could you give -- I mean, with the understanding Gentherm probably happened fairly quickly, could you give any color as to what that pipeline looked like prior to you engaging with Gentherm?

Mick Lucareli
Yeah. It's Mick, Brian. It's good. It's -- there are some things we paused on when that accelerated. But that HVAC space has a lot of privately owned and fragmented businesses. So, I'd say -- I classify it as there's a funnel of businesses from 50 million to 100 million sweet spot in revenue that we can relaunch discussions with.

Brian Sponheimer
Okay. Great. Congratulations again and look forward to talking to you soon.

Mick Lucareli
Thank you.

Operator
Thank you. I'm showing no further questions at this time. I would now like to turn the conference back to Kathy Powers.

Kathy Powers
Thank you and thanks to all of you for joining us this morning. A replay of this call will be available on our website in a couple of hours. I hope you all have a great day. Thanks.

Operator
Thank you. This concludes today's conference, and you may disconnect your lines at this time. Thank you for your participation.