Trane Technologies
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Nigel Coe: Okay, good. So for those on the webcast, thanks for joining. We're going to restart the Wolfe Industrials & Transports Conference with Trane Technologies. Very pleased to have President of the Americas, Donny Simmons; and CFO, Chris Kuehn, with us on stage.

So Chris, let me hand over to you for some remarks, and then we'll get into Q&A.

Chris Kuehn: Great. Thanks, Nigel. Glad to be here, already a strong conference. So thanks for having us and good to be back in New York. I'm here with Donny Simmons. As Nigel described, Donny leads our Americas business for Trane Technologies. Do you want to spend a moment, Donny, just on your background?

Donny Simmons: Sure. I've been with the Trane for 24 years, worked in multiple businesses. I'm responsible for all the businesses in the Americas. The majority of my background is in the commercial HVAC space, but also worked in Thermo King as well. Happy to be here and looking forward to answering some questions.

Chris Kuehn: And I'm just the CFO. So I'll sort of answer those questions. But look, we're celebrating our fifth year as Trane Technologies, very excited for what the future holds. But -- let me just set you up for what we've done in the last four years. We've reported revenue growth of 12% CAGR over the last four years. We've had EPS growth in each of those years over 20%. And then what I'd like to describe is high-quality earnings.

We've delivered free cash flow as a percent of net income of an average of 108% over those four years. So very excited about what we've delivered, but even more excited about what we're going to have happening in the future and our growth prospects for the future. We've guided 2025 to 7% to 8% revenue growth and $12.70 to $12.90 EPS. We said on our call a few weeks ago that we expect to be at the high end of that range, and we'll deliver strong free cash flow and also strong investments. So happy to talk about how we started out the year at a very strong first quarter.

And with that, Nigel, I'll turn it over to you.

Nigel Coe: Yes. Thanks, Chris. That's fantastic. Look, Trane, the company has been almost five years. We measure quality on the basis of organic growth, EPS growth, but more importantly, the consistency of that growth, both organic growth and EPS. And on those dimensions, Trane is top of the pack of our coverage. So very high-quality company, great performance, congratulations. Hope, I haven't cursed you by the way. That's not the performance cycle. But Donny, I'm really pleased to kind of double-click on the Americas, because it is the most – the largest and arguably the most important region for Trane. So maybe just kick off with in terms of what would you say right now are your top two or three priorities, top of your mind?

Donny Simmons: Serving our customers, number one, always. And look, we've we had a really dynamic first quarter. We've had a great last four years, five years plus. Our commercial HVAC business continues to be strong. We're seeing broad-based growth. And so we can't really think about that in terms of one particular vertical market. We look at 14 vertical markets and we're seeing growth in the majority of those. And so we really have to stay honed in on.

One big priority for us is innovation. We just had innovation reviews yesterday. We're going to do more tomorrow with all of our businesses. And that flywheel is extremely important for our success, it's part of the reason that we've seen significant growth. I just pick commercial HVAC and think about the applied business growth that we've seen over the last four years at 200% growth, that's significant. That's because of the innovation pipeline that we've got in place. Last year we launched across the portfolio of the company, 190 new products. That takes a significant amount of effort. So that's a number one priority for us.

Ultimately we have to serve our customers. We have to make sure they're taken care of. Certainly we're thinking about supply chain always. We did a lot of work with supply chain resiliency and we're always making sure that we keep that in the front of us in terms of making sure that we're ahead of any challenges that we have. We've got a great business operating system that helps us work through those issues now. We always have issues that come up and we now have a really robust business operating system that helps us work through those issues on an ongoing basis.

Nigel Coe: So, I thought it was actually interesting. You start off with customer, that's the key, [indiscernible] to the customer. Maybe just talking about more recent trends and what you're seeing out there in the markets, I mean, I don't think I've ever seen such divergence in the market right now. There is a lot of different cross currents going on in your various markets, be it residential, commercial, transport.

So, if you think about residential, you saw high teens growth in the first quarter, competitors saw flattish growth. The market certainly wasn't growing in the high teens. So, your guidance embeds a real slowdown in the second quarter, in the back half of the year, maybe just talk about what you see in residential. There has been a big sort of concern if you will, or debate about pre buy of R-410A systems. Maybe just talk about some of the context of that.

Chris Kuehn: Sure. I mean we thought there was a bit of a pre-buy in the end of last year, but what we learned in the first quarter is there really wasn't. And so as product became available we saw our channel really stock up on product. And so we feel like there's maybe a little bit, maybe $75 million, $100 million in our independent wholesale distributor channel. That's a little bit too much. So, we think that will maybe create a little bit of a pocket there in the year. It's hard to look at one quarter. It's hard to compare anybody on one quarter in that business, because the way that we go-to-market, and how product is available and when it's not.

And so, we're pretty confident what we've announced here for the remainder of the year expecting mid-single digits for the total year for residential it's early. The season hasn't hit. So, we'll learn a lot as the second quarter continues, as we get into the third quarter.

Nigel Coe: So, if you're getting 10 points of mix, I think that's the number you talked about on 12 systems. The mid single-digits embeds down mid single-digit volumes. Again, I don't want to get too much in the weeds here, but it does seem like a very conservative view of the world just based on what you just reported.

Chris Kuehn: Think about the transition to the new refrigerant would be more high single-digit price increase just given the sensors and the higher cost. But that's only on, say, 75% of the year on 60%, 70% of the portfolio, not everything changed with the upgrade to 454B. So that componentry probably gets you to 3% to 4% growth in residential, then layer on a normal GDP type growth environment, which adds about another 3 or 4 points. And then back off the pre-buy, which as we started the year with it being from Q3 and Q4 of last year, now it may be kind of got refresh, let's say, in the first quarter, you pulled probably 3 or 4 points of growth off of that, you're right around the mid-single digits, Nigel. So let's see, to Donny's point, the first quarter is an important quarter, but not the most important quarter for residential and we'll give you an update when we get to the end of July.

Nigel Coe: Your math is a lot better than mine, that's for sure. So it's more like 3 to 4 points of net realized price mix as opposed to 10.

Chris Kuehn: I think on the refrigerant transition, yes, think about it as the year is probably 75%-ish, 454B, and then you've got a componentry of the products. It's not the full product set. That's right.

Nigel Coe: Yes. Okay. I don't want to kind of spend too much time on tariffs, but it is top of mind for us, everyone here, you guys as well, I assume. How does the pullback in the China tariffs or the pause, I should say, in the China tariffs? How does that change any additional actions, be they pricing, be they supply chain kind of measures? How does that change the way you're thinking about the world?

Chris Kuehn: Yes. Well, I'll start with the tactical side, and then I love Donny to jump in on kind of the more broader things we've been doing with our supply chain in region for region. We guided $250 million to $275 million impact, unmitigated impact from tariffs based on what we knew as of April 30. And to your point, Nigel, a lot's changed since that period of time. That number – think of that number, it's more Tier 2 and Tier 3 for us, okay? It's more around our suppliers' suppliers and where they're buying with the largest impact of that tariff cost would be from China. So with the latest news of tariffs being paused down to 30%, it would certainly mean that, that dollar amount will be less. We haven't quantified it publicly what the number would be, but it would be less. It doesn't change our approach, though.

And number one, let's mitigate the cost of the tariffs. Let's work with our supply chain. When we think about the growth that we've had and the growth we're anticipating gives us a lot of flexibility with our supply chain to let's migrate more to markets to be more in region for region. So we're continuing to work that each and every day with our operations teams. So let's get the cost down first to mitigate. And then after that, if there's pricing requirements, we'll do that with up to pricing kind of environments. And we can be very surgical, very nimble. But the fact is we've been in region for region for quite some time.

Donny Simmons: Yes. I mean I think that's a really important point. We have stressed that. Just in North America, we've got 25 factories. Only one of those factories is in Mexico. So we produce in region for region. We don't import any product from Asia or Europe into the U.S. as finished goods. We manufacture everything ourselves in region for region. So we're really set up here.

We have 900 suppliers that exist in North America. The majority of those produce in the U.S. Certainly, they bring Tier 2, Tier 3 components from elsewhere. So we've got a bit of a cushion there relative to the impact that the tariff has on us. It gives us a little bit more capability to be a little bit more surgical, a little bit more nimble. We can make sure that, as an example, in the transportation industry, surcharges are very normal. We can put a surcharge in place to make sure that we're covering anything that's very specific and then we can easily pull that back, which is how we're reacting to the changes that took place.

Nigel Coe: Yes. It seems to me like given your largely in-country, for-country manufacturing sourcing for the Americas – sorry, North America, U.S., I should say. It seems like it's a durable competitive advantage given that a lot of your competitors, your key competitors are actually very heavy in Mexico and in some cases, are sourcing from China, et cetera. Do you agree with that? Do you think it gives you a customer-facing durable competitive advantage?

Donny Simmons: I believe it gives us a competitive advantage, but don't forget that even manufacturing in Mexico, manufacturing in Canada, if you qualify through the USMCA, you're not – there's no real advantage there from that standpoint. So that changes, that could change, right, for now.

Nigel Coe: Sure. Yes.

Chris Kuehn: Yes. To Donny's point, 95% of our products sold in the U.S. are manufactured in the U.S. And over the last four years, we've put I think, $1.2 billion of capital into the U.S. for capacity expansion and added close to 4,000 employees in the U.S. So the fact is we keep driving in terms of the growth and making sure we've got the infrastructure to support the growth in the Americas. But let's keep working on the supply chain, resiliency as well as the optionality to really drive it closer and closer to in region for region.

Nigel Coe: So when you benchmark the fact that you – in theory, you've got a higher cost base in the U.S. versus Mexico for some of your competitors. But when you benchmark your product costs versus your competitors, are you offsetting that labor arbitrage with productivity? So when you compare your unit costs, are they a disadvantage, advantage? I mean, where does that stand today?

Donny Simmons: You mean as opposed to competition?

Nigel Coe: As opposed to – versus your competitors, as the commercial...

Donny Simmons: We'll do tear down some products, and we'll look at the makeup of the products and how that would compare. We're always looking for opportunities to improve costs. I don't think that labor is a significant portion of our product cost to begin with. So it's not something that drives us to make a decision in terms of where we manufacture. What really is important is making sure that we have a productive and lean environment, and we've got a business operating system to support that. We add capacity. We don't just stand up four walls of new factories. Chris mentioned that we have invested significantly in our infrastructure. We added significant capacity in La Crosse, Wisconsin. We added significant capacity in Grand Rapids. These were existing facilities that we already have. Much less expensive to that than go say, stand up a new factory in Mexico.

Nigel Coe: Yes. Yes, that's fair. So the most surprising part of 1Q results for me at least was the growth you saw in TK Americas. The markets for truck and trailer down 20% plus this year, I think down low 20s is what you're planning for. Maybe just talk about how you managed to grow in the first quarter? And how that might change over the balance of the year?

Donny Simmons: Sure. Look, I think for one, we had some big customers that had their planned purchasing cycles and they placed the orders, and we were able to deliver those on plan. It doesn't really change our outlook for the year. We absolutely feel that the industry is going to be down 20%, that's off of a 14%, 15% down last year. ACT, which I know you have them coming in, just call it down closer to what our guide was, which we're – we had called in our guide around, call it, the 28,000. They're now down to 28,900. So we're absolutely confident that's kind of where things are headed. We don't see that changing. There's a lot of dynamics there. But at the same time, we feel like we're going to outperform what that market should look like just as we did in the first quarter.

Chris Kuehn: If the market lands where we expected to land this year, it's going to be a 15-year low in the transport market. So we're back to 2010 levels. And it just shows the age of the fleets are just getting older and older. And at some point, right about now, the cost to maintain those older fleets starts getting pretty punitive. So we do think that there's going to be an inflection point. And ACT is really talking about very strong growth in 2026 and 2027, 20% plus…

Donny Simmons: They are calling – now they're calling 30% growth there.

Chris Kuehn: So we'll get through 2025 and keep innovating in the product sets. Donny mentioned the innovation reviews we're doing. Yesterday, it was a bit of a focus on the transport portfolios. So keep investing in the business. We'll be ready when it comes back, and we're getting excited about what 2026 and 2027 can bring.

Nigel Coe: What goes down comes up eventually. What about Applied? I mean, Applied seems to go up and up and up, and never seems to come down.

Donny Simmons: Beautiful thing.

Nigel Coe: I think the data point was in 1Q, your Applied – Americas Applied equipment was up 40%, I think, year-over-year. The rooftop was down, I think, within that. So just would love some perspective on the durability. I'm not saying you're going to grow 40% forever, but the durability of double-digit growth in Applied Systems.

Donny Simmons: Look, we have a very healthy pipeline. We talk a lot about our sales force and the direct sales force that we have and really the way we go to market. I mean you just have to think about it in terms of having a highly educated technical sales force that call on consulting engineers, call on mechanical contractors, call on owners across 14 different verticals, and they can pivot to where the opportunities are. That's very different in the marketplace in terms of how we go-to-market. A lot of that is what's driving that Applied business. It's not all one vertical that's helping drive that Applied business. So we have a flywheel of innovation as well.

We talk about our innovation reviews and I mentioned that we launched 190 products. We've got a tremendous amount of great new products coming out. We've got our digital capability that we have that is absolutely connected to that Applied business and helps create that tether and helps create additional opportunities as well. So look, the future is bright relative to the Applied business overall and really confident with that. And we'll see how that plays out for the remainder of the year. But it's...

Nigel Coe: Any pockets of weakness though within that – within the verticals? I think you talked about 14 verticals. You've called out, I think lodging is maybe a little bit tougher, commercial office maybe...

Donny Simmons: Well, there's parts of commercial office that are soft and there's parts that are really strong, like Class A buildings in New York City is actually pretty strong right now. You think about – you want to have the most attractive space to get clients to come in to the space. And so we're seeing a lot of retrofits in those type areas. And so we see pockets there. Retail is a bit soft right now. You can see that really in the unitary. I mean, that would certainly be an indicator in terms of what's going on in the unitary portfolio.

Life sciences is a bit slow. But look at where the strengths are. We have strength in health care. We have strength in education. Even though we don't have significant strength in K-12 education, it's not. I mean it's still growing. It's actually still a very nice market. So there was a lot of concern that ESSER funding went away that we're going to see this big drop off. Infrastructure is still there. It still needs to be upgraded in the K-12. And so we're still seeing growth in that segment as well.

So there's pockets. But again, we use our sales force, make sure that we find where the opportunities are. They direct themselves. We don't direct them. They direct themselves to where the opportunities are and make sure that we're able to take care of the customer.

Nigel Coe: Donny, just to double click in the K-12 because one of your big competitors did call out that as a watch item. Are you still seeing order growth and backlog expansion within K-12?

Donny Simmons: Yeah. We're seeing a stable environment in K-12 is the way I would talk about it. I mean it's certainly not the growth that we were seeing during the prime of ESSER in the last couple of years really in 2023 and halfway through 2024, but it's a very stable market. And we're seeing – like – just keep in mind that K-12 doesn't only get funded through elements like ESSER. You have municipal bonds that get approved. And we have an energy services business that takes advantage of those municipal bonds and offerings to our customers to make sure that we're able to retrofit their entire school system. So that's a big. It's not reliant on ESSER funding to make that.

Chris Kuehn: I think it allowed those school districts to really just do a further inventory of where their assets are at and what can you get upgraded through ESSER, but the others still remains. So let's leverage back to historical level or ways in which you would fund those projects through municipal bonds, as Donny shared. And we would call out higher ed as a strong vertical for us as well. I mean there's strict competition around students going to colleges. And I know Dave's kind of used this analogy, and I had to go through with my oldest about a year ago. Schools are differentiating themselves. And one way they do that is let's talk about the campus environment, the learning environment, the dormitories and the investments that they made there. And as parents are thinking about, okay, where do those dollars wind up going. You want to make sure you're in a safe space. And that's the way that they're differentiating. We still see a lot of growth within higher ed.

Nigel Coe: Okay. That's great. I'll take one more question, and then we'll throw it up into the – I know there's one or two, but just one more for me. Please be patient. Data centers. I know Dave gets a little bit – I wouldn't say annoyed, but the assumption that it's all data center driven, the growth. But maybe just talk about data center in terms of what you're seeing. And I don't know if you can quantify the size of the data center business for Trane, but that would be helpful as well.

Chris Kuehn: Well, I'll jump in on that one. We have not quantified it externally, but we do talk about the broad-based growth. And we've been talking about broad-based growth for well over a year, not more recently. And the intention is our sales force is encouraged and incented to go out and try to find opportunities in any vertical and working across the 150-plus sales offices we have in the Americas, making sure that they're finding opportunities. There's a lot of laws and regulations that are happening at a state and a city level. And when you've got a sales office in a city that they understand the local laws and New York would be a perfect example of Local Law 97 and more punitive measures that happen in 2030 and 2035, if you don't decarbonize. It's the power of that sales force, knowing what those rules are and let's avoid those taxes, let's avoid those penalties really to move through that. But data center has been a strong vertical. And Donny, I know you've been investing in that for many years.

Donny Simmons: And it continues to be a strong vertical. I'll tell you what has changed a little bit is, first off, the activity is as strong as it's ever been, right? There's more activity. It's just growing and growing. So the pipeline is very healthy. The customer behavior has changed a little bit in that – during the supply chain constraints of 2022, 2023, it was – you were more apt to get orders well in advance, like far in advance of lead times, that's normalized now, which I think is a good thing. So we're not going to see the lumpiness that we once saw in order rates coming from data centers. So it's a little bit more consistent. You have good visibility two, three years out in terms of what the customers are going to do, but the actual purchase order doesn't come in. So they'll make commitments to us in terms of what they're going to give us, but the purchase orders have come in within lead time. So it's very normal. I like that. It makes it much easier to answer questions.

Nigel Coe: Thank you. Thank you. Yes. Just very – three quick questions, if I may. One is that one of your competitors mentioned that they want to concentrate only in verticals that just makes sense like in terms of growth and margins. And so they don't want to spread themselves thin. So like for your strategy, I mean, obviously, you've been always successful in kind of 14 verticals as we mentioned. But do you see that going forward, maybe you have to cut something like just to make sense out of it? Or – just a question.

And then second, in terms of that estimate of the tariff effect, is it already like official numbers that you get from your suppliers? Or is it just your estimates so far?

And third question is in terms of bonus depreciation, do you have any upside there at all or it kind of like not really – it's very minimal?

Chris Kuehn: Well, why don't we start with direct sales force on the first one and just our ability to serve all verticals, I think is a part of the secret sauce of Trane Technologies is the direct sales force we have in commercial HVAC.

Donny Simmons: And I would add there. I don't – I was – as you were asking that question, I was trying to think, are there any verticals that I don't see as attractive for some reason, structural margin within the vertical. There's nothing that sticks out to me. There might be aspects of a vertical you might want in the services business as an example. Facilities management is not really attractive to us, so that's not an area that we would focus on. But it's not a vertical market, right? I mean the actual vertical markets are attractive equally in the commercial space.

Chris Kuehn: On tariffs, it was an estimate but also working with our suppliers on estimating where their source of supply is. So – maybe that's different for Trane Technologies. Our number at $250 million to $275 million estimate we gave on April 30 was really more around Tier 2 and Tier 3 exposure. Others have talked about Tier 1 with copper, aluminum, steel, that's not really a big exposure for us. In the U.S., we buy 100% of our copper and 100% of our steel from within the U.S. Over 90% of our aluminum is purchased from within the U.S. So for us, it's really getting into a deeper level, and that's just our business operating system is to get into that. And then your last question was depreciation, maybe just repeat that, if you could?

Donny Simmons: I mean there might be some tailwinds from that, but I think we just have to see how that plays out. Certainly, if that comes to fruition, we'll have conversations with customers. We do a great job sitting with our customers, making sure that they understand what the benefits that they would have from any type of incentive that's out there, and we would use that in those discussions.

Chris Kuehn: Yes. We think you have strong paybacks already in the three- to five-year range on average. But if there's a faster cash flow payback for the customer, right, that's a great conversation to have.

Nigel Coe: Is there any other questions?

Q&A

Thank you. I was just curious, do you believe you're at peak in any of your 14 commercial end market verticals, at the peak of the cycle?

Donny Simmons: I don't know that I'm just thinking through each one of the verticals that anyone stick out as a peak. I mean there might be some that are more in a trough and at the low end that are going to rebound like retail, as an example. Warehouse saw a really big boom during the COVID. Shortly after COVID, that certainly has come down.

So we'll start to see those come back. But on the flip side of that, I'm not seeing a peak in higher education. There's still a lot of work to take place there. We've talked about data centers. There's no peak in sight there. So no other vertical sticks out to me is that something that I would think at a peak starting to look at retrenchment.

Nigel Coe: Here is the question. Maybe just quickly on the rooftops, which has been trending a little bit weaker. I think do you see a divergent or more [indiscernible] in terms of how that develops? What is your perspective on the rooftop model?

Chris Kuehn: Well, we've said, our unitary for the year from a guidance perspective would macro as fast as applied. Unitary could be flat to slightly down, sure it could be. But maybe to Donny's point, it kind of plays more to certain verticals and other verticals.

Donny Simmons: Yes, it does. It plays more on certain verticals. It's really well correlated with ABI. And ABI has been really kind of low in the last several months. We feel like we're at the low end of that. So we're in that kind of flattish space right now. There's a few factors there. I think you got to remember.

One is we had the Department of Energy regulations that efficiency changes that took place that created some demand early. We had refrigerant change that created some demand. We had supply chain constraints that extended lead times. All that's normalized now. So now we're in a very much of a normal market. And so I think we can now look at the market and expect where it is and anticipate how that recovers on a go-forward basis. As consumer sentiment increases, we're going to see impact there as well. So I think it's – on the unitary side, it's got a really bright future here for us.

Nigel Coe: That's great. And then maybe on capital allocation. I'd say Trane tends to do M&A that you would – I would never forecast. In terms of the companies you're buying, BrainBox AI. The more I look at BrainBox AI, it looks like an even better deal every time I look at it. So...

Donny Simmons: I'd love to talk about BrainBox because….

Nigel Coe: Yes. So – I'd love for you to just double click on BrainBox AI. What that brings to the organization? And what kind of other technologies are you looking to add to the portfolio?

Donny Simmons: So, BrainBox is an artificial intelligence capability that we – that you think about it as being built into our building automation system. It enables customers using both structured and unstructured data to save up to 25% of their energy costs. So, think about gas and electricity, 25% in savings. And we call that Trane Autonomous Controls that's powered by

BrainBox. They have another capability. So that – we are actively selling now, like we have a big pipeline of opportunities there that just add value from a services standpoint.

In addition to that, we have a portfolio called ARIA, which is A-R-I-A. In ARIA, it gives – it's a productivity for technicians. It gives us artificial intelligence to diagnose a system before a technician shows on site. They can say, here are the fault codes, here's the diagnosis of those based on the data that we can pull, here's what you need to look at. So, think about that as really enabling our commercial technicians and also think about that in the future, enabling our residential dealers to be able to diagnose systems and be that much more productive. Super, super exciting.

And then the third element is they have a cloud-based BMS system. And so, think about that in terms of not requiring hardware to connect to all the systems that exist in a building, now you have a cloud-based BMS system, and they've been very successful with that, being able to do all the algorithms and everything in the cloud as opposed to on-prem. And so, there's just – that's a perfect example of buying a technology that complements how we go to market perfectly.

Nigel Coe: Is BrainBox, is that a revenue driver, i.e., spend the TAM for Trane? Or was it more making your field more productive?

Chris Kuehn: I think it's both. Yes, I'd lead with expand the TAM and – it's a perfect example of take a bolt-on acquisition that's got great technology and match it up with, we believe, the unparalleled direct sales force and channel in the Americas. And frankly, there's no reason why it couldn't be brought to Europe or brought to Asia, too, as you think about building management systems, let's start in the Americas, but a great way to go take that business and great partners already, but prior to the acquisition, and now you're partner up with the channel, we're excited about that.

Nigel Coe: Okay. I think we're out of time. So, thank you very much for the conversation. Donny, Chris, that was great. Thank you.

Donny Simmons: Yes. Thanks, Nigel.

Chris Kuehn: Thank you.