Company Name: Honeywell
Company Ticker: HON US
Date: 2017-10-20
Event Description: Q3 2017 Earnings Call

Market Cap: 110,730.94
Current PX: 145.35
YTD Change($): +29.50
YTD Change(%): +25.464

Bloomberg Estimates - EPS
Current Quarter: 1.839
Current Year: 7.094
Bloomberg Estimates - Sales
Current Quarter: 10459.231
Current Year: 39980.211

Q3 2017 Earnings Call

Company Participants

- Mark Macaluso
- Darius Adamczyk
- Thomas A. Szlosek

Other Participants

- Deane Dray
- Steven Eric Winoker
- Charles Stephen Tusa
- Gautam Khanna
- John G. Inch
- Nigel Coe
- Jeffrey Todd Sprague
- Andrew Burris Obin
- Andrew Kaplowitz

MANAGEMENT DISCUSSION SECTION

Mark Macaluso

Non-GAAP Financial Measures

This call and webcast, including any non-GAAP reconciliations, are available on our website at www.honeywell.com/investor

Darius Adamczyk

Business Highlights

Sales

- As we previewed last week, Honeywell delivered another terrific quarter with strong organic sales growth and margin expansion leading to high-quality earnings
- Sales were up 5%, exceeding the high-end of the guidance we provided in July
- Our Aerospace aftermarket business grew more than 7%
- Our Intelligrated business, which develops solutions for the warehouse automation market, continued to grow at double-digit pace
- And every business in Performance Materials and Technologies grew considerably, led by 25% organic sales growth in UOP

China and India

- In addition, we saw continued strength in high-growth regions
- Organic sales growth in both China and India was up more than 30% y-over-y, driven by strong catalyst demand in UOP and continued growth from our differentiated offering within Home and Building Technologies and Safety and Productivity Solutions

Restructuring and Other Projects

- We expanded segment margins by 120BPS this quarter, driven by strong operational performance in all businesses, leading to EPS that came in at the high-end of our guidance range at $1.75, up 16% on a basis consistent with our guidance
- During the quarter, we also funded about $120mm of restructuring and other projects
- We remain on track to achieving our full-year FCF guidance
- FCF for the quarter was $1.2B, representing about 90% conversion
- I am encouraged by the progress we've made with regard to working capital, but there is much more we can do
- And all of our businesses are focused on driving improvements to our cash cycle

Outperformance

- Overall, I'm pleased by our organic sales growth momentum and the operational improvement each of our businesses continue to achieve
- As a result of our continued outperformance, last week we raised our full-year EPS guidance to $7.05 to $7.10, up 9% to 10%
- As you will hear shortly, this morning we also raised our full-year sales guidance to reflect the stronger top line performance
- Tom will walk you through those updates in a few minutes

Homes and Transportation Systems

- As most of you may recall, last week announced the spins of Homes and Transportation Systems
- As independent companies, Homes and Transportation Systems will be better positioned to make tailored strategic and capital decisions that will enable long-term value creation
- At the same time, these actions will make Honeywell a more focused, growth-oriented and synergistic company, putting us in a better position to continue to deliver the results you've come to expect from us

Aerospace

- I am pleased this quarter's results and looking forward to a strong finish to 2017
- Let's turn to slide 3 to discuss some of the commercial progress our business has made in Q3
- In Aerospace, we launched the new unmanned aerial vehicle inspection service called Honeywell InView

- The service will help customers in the utility, energy, infrastructure, and oil and gas industries improve critical structure inspections while eliminating safety hazards for employees
- InView combines the proven performance of Intel's Falcon 8+ UAV System and Honeywell's varied and extensive experience across verticals with data-driven software that will help customers log, analyze and eventually predict or prevent outages and structural failures
  - We're excited about this unique combination of cutting-edge aeronautics with software and data

Home and Building Technologies

- In Home and Building Technologies, Kuala Lumpur International Airport, one of Asia's major aviation hubs, selected Honeywell Building Solutions to upgrade its airfield ground lighting control and monitoring system
- The Honeywell system will enhance safety and efficiency while accommodating increasing aircraft traffic
- Honeywell's technology will provide real-time location information on light failures to optimize response and repair, promoting enhanced operations and improved up-time

Process Optimization Advisor

- Performance Materials and Technologies announced that Kuwait Paraxylene Production Company will use Honeywell Connected Plant services to improve performance at its CCR platforming and aromatics complex which produces a precursor to plastic fibers and films
- KPPC will use Honeywell Connected Plant's Process Reliability Advisor for ongoing monitoring, early event detection, and mitigation of performance issues before they become costly
- The company will also use Process Optimization Advisor, which continuously monitors streamlining plant data and applies Honeywell UOP process models to determine the most cost-effective method mode of operations
  - Both services use big data analytics and machine learning to improve plant operation
- We continue to deliver results for customers through our connected plant offerings and I'm pleased with the traction we've been gaining in this area

Safety and Productivity Solutions

- In Safety and Productivity Solutions, you'll recall our efforts to develop mobile computing offerings for Google's Android operating system which is quickly becoming the standard for industrial handheld devices
- I'm pleased to announce that earlier this week, we launched the Mobility Edge Platform
- Mobility Edge allows users to easily upgrade to future Android versions more than any competitive offerings in the market, making it easier for customers to manage device refreshers and quickly deploy apps

Edge Platform

- We've conducted comprehensive voice-of-the-customer research prior to the development of the Mobile (sic) [Mobility] (7:17) Edge Platform and rethought our approach to solving customer pain points that come up during our conversations
- This results in a best-in-class scalable platform that makes deployments quick and easy for our customers
- Clearly, there are a lot of exciting things happening across the portfolio as we head into 2018

Thomas A. Szlosek

Financial Highlights

Organic Sales Growth and Segment Margin

- I'm on slide 4
- As Darius mentioned, we achieved 5% organic sales growth in Q3 which exceeded our guidance of 2% to 4% growth
- We've met or exceeded the high-end of our sales guidance in every quarter of 2017 and each of our businesses is contributing to the momentum
- Segment profit was $1.9B, up 13% excluding the impact from our 2016 divestitures, and segment margin expanded 120BPS from 2016, driven by our continued focus on effective selling and operational execution
  - We also had some favorability from lower OEM incentives in Aerospace which was contemplated in our guidance

EPS and Tax Rate

- EPS was $1.75, in line with our preview on October 10
- Our third quarter tax rate came in at 23.4%, lower than originally anticipated which enabled additional restructuring projects beyond what we had planned
- These projects will improve our cost structure, drive further productivity starting in Q4 and begin to address the residual costs we expect as a result of the announced spins
- Excluding $60mm of this additional restructuring and earnings from our 2016 divestitures and normalized for tax at 26% in both periods, EPS was up 16% y-over-y

Gulf Coast and Puerto Rico

- A number of people have asked about the impact from the extreme weather throughout Q3
- The impact from all of the weather issues was approximately $0.02 of earnings, which we were able to overcome with advanced planning and other mitigation actions
- Each of our businesses was impacted in some way
  - We had to temporarily close six Aerospace sites in the Gulf Coast and Puerto Rico
- Several ADI branches were closed, leading to lost revenues for Home and Building Technologies

Process Solutions

- In Process Solutions, several customers pushed third quarter projects into Q4 and SPS experienced lower demand for safety equipment, especially gas-sensing products due to refinery maintenance pushouts
- We're proud of how our employees and management team responded and delivered despite these challenges and are pleased that all of our employees made it through the events safely

  - We're in the process of assessing any ongoing impacts to our business

FCF

- FCF continues to be strong, growing 18% YTD despite about $200mm more of timing related cash tax payments this quarter, and about $500mm more YTD
- As Darius mentioned, our focus on improving working capital is beginning to deliver results, and we expect this to continue into 2018 and beyond
- FCF conversion in Q3 was about 90%, as Darius mentioned
- Overall, we delivered high quality results, driven by strong operational performance in our businesses

Segment Results

Aerospace

- Let's turn to slide 5 for our segment results
- Starting with Aerospace, sales growth was 2 percentage points, above the high-end of our guidance
- Strength in the Commercial Aftermarket continued this quarter with strong air transport and regional spares and continued demand for retrofits, modifications, and upgrades
- The business in General Aviation Aftermarket was also up, primarily driven by the timing of customer demand
- Overall, aftermarket sales grew 7%

OE Sales

- OE sales for the quarter were up 10%, driven by the impact of lower y-over-y customer incentives, as expected
- On the air transport side, we saw higher demand on key platforms including the A318, A320 and 737, strong growth with certain regional OEMs as well
- Sales and business in General Aviation were better than anticipated, primarily due to the timing of engines and avionics shipments and accelerated new platform demand
  - While we are encouraged by the strong quarter in BGA, the market is not expected to fully recover until late next year or early in 2019

Defense & Space

- Defense & Space sales were down 2% organic with strong U.S. core defense sales more than offset by storm-related impacts, supply base execution and the anticipated continued weakness in the space and commercial helicopter markets
- In Transportation Systems, we saw continued growth in commercial vehicles, particularly for on-highway turbos, driven by increased vehicle sales in the U.S., new launches in Europe and continued enforcement of vehicle weight regulations in China
- Growth in light vehicle gas turbos in China was again strong

Segment Margin Expansion

- Aerospace segment margin expansion of 290BPS for the quarter was driven by lower y-over-y customer incentives as we signaled; Commercial Excellence including the impact of our investments in the sales force; the benefit from ongoing productivity initiatives; and the favorable impact of the 2016 divestiture of the government services business

Home and Building Technologies

- Home and Building Technologies grew 2%, driven by distribution and the Smart Energy business within Products
- The distribution side of the business was up 2%, primarily on the strength in our ADI business
- Backlog in the Honeywell Building Solutions business was up over 20% in the quarter with every region reporting double-digit increases and every line of business up y-over-y
- Within the Products businesses, we continue to execute several large smart meter program rollouts and saw continued strong demand for clean-air and water products in China

Commercial Excellence

- Segment margin for HBT expanded 10BPS, driven by benefits from Commercial Excellence in our ongoing productivity initiatives, partially offset by continued unfavorable mix, both within the Products businesses and between products and distribution
- Performance Materials and Technologies had another outstanding quarter with organic sales up 10% and 170BPS of margin expansion

PMT Business

- There is broad strength across the PMT businesses
- UOP sales were up 25% with every line of business achieving double-digit y-over-y increases, including strong licensing, equipment, catalyst and gas processing volumes
  - There was good growth in mega projects in China, strong catalyst reload volumes in India and Asia Pac and new unit growth in the Middle East
- In HPS, sales were up 5% with significant growth in the short cycle software and services businesses as well as in Thermal Solutions
- Advanced Materials had another quarter of strong growth driven by continued demand for Solstice, low-global-warming products
- Orders and backlog were up high single-digits across the entire PMT portfolio

Margin Expansion

- Margin expansion in PMT came in at the high-end of our guidance range, driven by the volume leverage from PMT's exceptional sales growth, results from our Commercial Excellence efforts, and the divestiture of the former Resins and Chemicals business last year

Safety and Productivity Solutions

- In Safety and Productivity Solutions, organic sales were up 3%
- Intelligrated booked a record amount of orders in Q3 and had another quarter of 20% sales growth, driven by strong demand from large customers
- Workflow solutions recorded double-digit growth this quarter with significant demand coming from existing customers of our Vocollect voice-enabled solutions, as well as large project rollout for a key European customer within our Movilizer software business

Sensing and IOT

- In Sensing and IOT, demand for our sensing controls and new sensor products remains strong with growth in all regions, particularly in high-growth regions like China
- In Productivity Products, we saw double-digit growth within our scanning business, as well as robust demand for printers
- And as Darius mentioned, we're working to address the Android-based gaps in our mobility product line
  - We anticipate that we'll see the impact of our new Android launches next year

Safety

- Finally, Safety grew 1% on an organic basis, driven by demand for our high risk and general safety personal protective equipment offerings
- Again, we were modestly impacted in Safety by the hurricanes in the quarter, mostly in the gas sensing line and fully expect a recovery in Q4

Segment Margin

- SPS segment margins expanded 190BPS excluding the first-year dilutive impacts from M&A, primarily driven by higher volume, continued productivity, and restructuring benefits and partially offset by investments in Commercial Excellence, a great third quarter performance across all the businesses, as Darius mentioned, while overcoming unanticipated impacts from the weather-related disruptions

EPS

- Slide 6 walks our EPS from Q3 2016 to Q3 2017
- Earnings from our divestitures in Q3 were approximately $0.04 per share in 2016
- We exclude those amounts from the 2016 baseline, consistent with our guidance framework
- For comparison purposes, we've also normalized the tax rate for Q3 2016 to the 26% effective tax rate we assumed in our third quarter guidance, the impact of which was $0.05 per share

Segment Profit

- As you can see, the overwhelming majority of our earnings growth is coming from segment profit improvement in the business, with all four segments contributing to the growth, led by Aerospace

- This reflects the impacts from the strong top line in the quarter, as well as our Commercial Excellence efforts and HOS Gold deployment and savings from previously-executed restructuring projects
- Below the line items were $0.02 headwind this quarter, primarily due to the absence of Q3 2016 gain from the sale of our former Aerospace government services business, partially offset by slightly lower restructuring expense y-over-y

Restructuring

- In Q3, we funded nearly $120mm of restructuring, which was partially enabled by a lower than planned tax rate at approximately 23%
- Other items, including noncontrolling interest, share count, and tax were roughly flat y-over-y

Guidance

Aerospace and Commercial OE

- Let’s turn to slide 7 for our expectations on Q4
- In Aerospace, organic sales are expected to be up 1% to 3%
- In Commercial OE, we expect roughly flat sales growth in total, driven by strong air transport deliveries, partially offset by the impact of declining shipments on legacy air transport platforms and slight declines in bizjet OE
- We anticipate modest growth in the business aviation aftermarket on the timing of customer demand for spares and expect the air transport aftermarket to be roughly flat, driven by increased repair and overhaul activities, offset by the timing of spares demand

Defense

- In Defense, we have a healthy backlog and expect continued strength in U.S. core defense, partially offset by ongoing space weakness
- Demand for gas turbos in Europe is expected to drive low to mid single-digit growth in Transportation Systems
- Aerospace margin should expand by 70 to 90BPS this quarter, driven by volume leverage, Commercial Excellence, restructuring benefits and productivity net of inflation

HBT

- In HBT, we anticipate organic sales growth of 2% to 3%
- Within the Products businesses, growth in Smart Energy will continue, albeit at a slower pace as we move past the large smart meter rollouts we executed in the second and third quarters

Security and Fire

- We also anticipate improvement within Security and Fire
- Security was improved each quarter in 2017, and we expect that to continue as a result of new product introductions and Commercial Excellence

- In Distribution, the strong Building Solutions backlog I mentioned earlier, combined with the continued strength in the Global Distribution business, will drive low single-digit growth in Q4
- HBT segment margins are expected to contract 10BPS to 30BPS, driven by continued headwinds from product mix, partially offset by savings from prior restructuring actions and ongoing Commercial Excellence and productivity initiatives

Smart Energy

- As a reminder, Smart Energy was recently moved from HBT to Performance Materials and Technologies, and their results will be included in PMT's results beginning with Q4 earnings
- Before our December outlook call, we expect to file a Form 8-K with the SEC to restate the 2016 and 2017 quarterly segment results to reflect this movement of the Smart Energy business

Performance Materials and Technologies

- In Performance Materials and Technologies, sales are expected to be up 10% to 12% on an organic basis, driven by continued conversion to sales of our strong backlog
- UOP is expected to deliver another quarter of strong growth, driven by natural gas recovery projects in the UOP Russell business in Russia and North America, as well strong initial catalyst load in the Middle East

Advanced Materials

- We expect mid single-digit growth in HPS with significant demand for our Thermal Solutions and Field Instruments
- In Advanced Materials, we expect double-digit growth fueled primarily by our Solstice refrigerants for mobile air conditioning
- PMT segment margins are expected to contract 110BPS to 120BPS, driven by an unfavorable mix of equipment vs. catalyst sales in UOP y-over-y
- In Q4 2016, PMT had catalyst growth of 17%, which fueled expansion of more than 500BPS of margin
- Even so for the full year, we expect PMT will still generate 140BPS of margin expansion – truly, an outstanding year

Safety and Productivity Solutions

- In Safety and Productivity Solutions, sales are expected to be up 5% to 7% on an organic basis
- In the Safety business, we expect robust growth as refinery maintenance resumes following the hurricane-related impacts in Q3 which will drive demand for our entire range of safety products

Retail Business

- We expect that the retail business will return to growth this quarter as we execute the new direct selling strategy in that business, and expect we'll see normal elevated seasonal demand
- Growth in Productivity Products will be driven by another strong quarter at Intelligrated, building on the robust orders and backlog growth throughout 2017 as well as continued strong demand for the Sensing and

Control's business and workflow solutions, including Vocollect and Movilizer

Ongoing Productivity and Repositioning Efforts

- SPS margins are expected to expand by 110BPS to 130BPS, driven primarily by higher volumes and the results from our ongoing productivity and repositioning efforts
- For Honeywell in total, we expect another strong quarter of organic sales growth and 30BPS to 50BPS of margin expansion leading to EPS of $1.79 to $1.84
  - We expect that our fourth quarter effective tax rate will be about 21% with the full year closer to 22%
- We intend to undertake additional restructuring projects as we have the past two quarters, enabled by this expected lower fourth quarter effective tax rate
- The difference between the organic and sales projections you see on this page is primarily due to the stronger U.S. dollar

M&A

- On M&A, we've lapped the impacts of our two big divestitures, the Aerospace government service business and the Resins and Chemicals business as well as the impact of the Intelligrated acquisition
- Our fourth quarter and full year guidance does not contemplate significant cost to prepare our Home and Transportation Systems businesses for the spins we announced last week
  - We're working to define those costs and workstreams and we'll provide more details as we progress

EPS

- Let's move to slide 8
- Last week, we raised the low end of our full year EPS guidance by $0.05 – $7.05 to $7.10 per share, up 9% to 10%
  - This growth excludes the impact of 2016 divestitures, fourth quarter 2016 debt refinancing charges, and the pension mark-to-mark adjustments
- Based on current discount rates and asset return assumptions as of September 30, we do not expect the 2017 pension mark-to-mark adjustment to be significant

Sales

- We're raising our full year sales guidance to a new range of $40.2B to $40.4B, up 3% to 4% organic and up 2% to 3% reported
- This new range reflects stronger sales performance and outlooks in Aerospace and Performance Materials and Technologies
- You can see the revised sales guidance on the right side of the page
- We remain within the initial guidance for the segment margin and have narrowed our estimate to about 19%, which is up 70BPS y-over-y
  - There's no change to our full-year FCF guidance

- The YTD FCF performance has been good and each of our businesses continues to remain focused on improving our working capital execution

Backlog and Organic Sales Growth

- Let me turn to slide 10 for a quick wrap-up
- Q3 marked another strong performance for Honeywell with each of our segments meeting or beating their commitments
- We had outstanding sales performance and robust orders and backlog growth across the businesses that will help fuel continued growth
  - We expect to finish the year strong with fourth quarter organic sales growth between 4% and 6% and EPS of $1.79 to $1.84
- For the year, we raised our sales guidance to a new range of $40.2B to $40.4B and reaffirmed the new EPS guidance range we provided last week, $7.05 to $7.10 per share

Shareholder Value

- We continue to make investments to drive future profitable growth as well as to begin to eliminate the residual costs we expect as a result of the announced spins of the Homes and Transportation Systems businesses
- At Honeywell, we're committed to driving shareholder value
- That means optimizing our portfolio, as we announced last week, but that also means remaining focused on delivering outstanding results on growth, productivity, and cash flow every quarter of every year

QUESTION AND ANSWER SECTION

<Q - Deane Dray>: I'm sorry, I signed on late so you may have covered some of this before. One of the follow-up points I had on the spin announcements, divestiture announcements earlier, was the potential for and the use of the Honeywell brand for the divested businesses. Just it's kind of a cleanup question on that announcement, and I'd start there, please.

<A - Darius Adamczyk>: Sure. Yes. I think as it relates to the Honeywell brand, some of those decisions have not been made in terms of how we're going to – or what we're going to do with the brand for either the Homes or the Transportation Systems business. So, I think that we'll provide more clarity on that as we move forward, but there are a lot of different options that we have and it's going to be part of our work product moving forward and we'll be communicating that as that becomes clearer in Q1 and Q2 of next year.

<Q - Deane Dray>: And how about just a broader question on progress report and goals for the transformation of Honeywell to the software industrial, Darius, that you envision, just in terms of portfolio shaping, the way you're looking at M&A, emphasizing perhaps some software-as-a-service opportunities within the portfolio.

<A - Darius Adamczyk>: Sure. No. Overall, I'm very pleased in terms of how our Connected Enterprises is progressing this year. It's up double-digit which is very much in line with expectations. Margins are up even higher than that. And in terms of acquisitions and landscape there, we continue to look at all segments of the business, including our software plays. We've made one acquisition, actually, in the software area in Q3, which is a pretty exciting cyber technology that – although the business itself is relatively small, we have very, very big growth opportunities for it and it's actually exceeding our expectations.

So, the software acquisitions in general would be more of the bolt-on variety. Those are the kind that we're looking at. But overall, we continue to make progress both on the P&L on Connected Enterprise, continue to make progress on the buildout of our Sentience platform and signing up more partners as we go. So, we continue to be very excited about what we're doing. And the most important part of that is generating the right kind of results.

<Q - Deane Dray>: Got it. And just last question. I know we're going to hear more of this on your outlook call. But broad strokes, the outlook on 2018 in terms of the macro environment, where do you think you're particularly well-positioned, both U.S., outside the U.S.?

<A - Thomas A. Szlosek>: Yes, Deane. This is Tom. Yes, we're in the throes of our planning right now. We'll go through the details as we get into November, December. We're looking at trends continuing in most of our businesses. I mean, you see the strength in Aerospace, a lot of good flight hour activity, the Defense is looking up. And with any luck at some point in the tail end of 2018, we'll get some help from the business jet side, although business jet usage remains strong. So, we expect those trends to continue.

PMT, we really are encouraged, not only by their performance, but by the strength of the orders and backlog and it's been in all lines of business. I mean, not to denigrate last year, but we had great orders last year in the after-market side. We're seeing a lot of front-end orders type business in PMT, particularly in UOP and HPS, which bodes well for building installed base and building that service business. So, really strong trends there.

In SPS, Intelligrated continues to perform very well. We expect that backlog, which is well over 20%, to fuel excellent growth. And we expect the trends in that vertical to continue with e-commerce. And the Safety business continues to do well. We've got the Android products on Productivity and the software businesses in SPS.

So, good trends. You saw our fourth quarter expected growth, and I think we'll see that continue into next year. So, overall, I see some trends, some growth trends continuing.

Deane, as you saw, every quarter of this year, the organic growth rate has improved. And if our guidance holds up into Q4, that should at least be equal to third quarter and hopefully, that continues into next year. So, overall, pretty strong conditions as we had. We're encouraged.

<Q - Steven Eric Winoker>: Darius, could you maybe expand a little bit on your thoughts around PMT and UOP in terms of that refining cycle? It's giving you a lot of – I mean, overall, the tailwinds, top line. I know you've got equipment challenges. But the cyclical vs. structural side of this, what are you kind of expecting given Tom's comment for the length of tailwind in that very important segment?

<A - Darius Adamczyk>: Well, Steve, as Tom pointed out, one of the most important things for that business we always watch is the bookings. It is very much a long cycle. Bookings are – backlog's up. We know for a fact that it's going to be up probably double-digit by the end of this year vs. the end of last year. We continue to be bullish. We're winning a lot of work. We're particularly winning a lot of work in our high-growth regions, which I find to be really important. Because as you think about where PMT needs to be strong and has to be strong is in the development and progress of a lot of the developing regions. And that's exactly where it's winning. So, it's win rate in China, India. Markets such as this give me a great deal of comfort is that it's going to continue to perform. Our backlog position is strong, and we expect another strong quarters of booking in Q4 and go into 2018 with a strong position.

And the good news is we're kind of seeing it across all the segments, whether it's our gas processing business, whether it's the catalyst business, all of those have been particularly strong. And by the way, enjoyed the biggest order ever in Q3 in terms of our catalyst orders. So, overall, things are very much moving in the right direction for all of PMT, but especially UOP.

<Q - Steven Eric Winoker>: Thanks. That's helpful. On SPS, I think you had about – you had a month of Intelligrated in that 3% organic. Let me know if that's about right.

<A - Darius Adamczyk>: That's right, that's correct.

<Q - Steven Eric Winoker>: So, ex-Intelligrated, which you said was up more than 20%, the rest of that business must have been down, I don't know, say low to mid single-digits or something. Maybe give a little color on that. And maybe it is all in the mobility productivity side, but maybe just a better understanding of the organic performance ex-Intelligrated there.

<**A - Darius Adamczyk**>: Yes, it's actually good. And you'll see there's growth in every business. The only business where we didn't see growth was Productivity Products and that's due to some of the challenges we previously communicated around the mobility platform because if we look at the scanning side of the business, it was actually up close to 20%. So, we have one small area which is challenged and the Productivity Products business is challenged. But as we just announced, we've had an exciting new product launch this week. We have more coming in the middle of November and another set of new product launches in the mobility segment coming in the middle of February.

So, we're not where we want to be on mobility and Productivity Products, but I'm very confident that business, as we head into 2018 and Q1 and Q2, is going to start turning that performance around as it launches these new offerings.

But overall, a very strong performance across the board by SPS other than the one issue we knew about and we weren't particularly surprised about the outcome.

<**Q - Steven Eric Winoker**>: Yeah, it's actually one...

<**A - Thomas A. Szlosek**>: Yes, not to mention overcoming the storms and hurricanes in the Safety business in particular. As you know, the oil and gas vertical is a big sector and there was a lot of push-outs of projects and activity that affected particularly the gas monitoring business in Safety. But overall, the trends there are really strong, as Darius said.

<**A - Darius Adamczyk**>: Yes. And just to...

<**Q - Steven Eric Winoker**>: Yes, actually, the numbers are – it's up 1%, though, right? Ex-Intelligrated, Tom? So, it was positive still?

<**A - Thomas A. Szlosek**>: Absolutely, yes.

<**A - Darius Adamczyk**>: Yes.

<**Q - Steven Eric Winoker**>: Yes. Okay.

<**A - Thomas A. Szlosek**>: No, no. Steve, I'm not saying that the numbers ex-Intelligrated were up 1%. I mean, as Darius said, every one of the business was strong. It wasn't just Intelligrated that was contributing more than 2% or 3%.

<**Q - Charles Stephen Tusa**>: Hey, guys. Thanks for having me on the call this morning. It's nice to be able to get on calls and ask questions. Just first question, you guys, you recently raised your dividend by how much?

<**A - Darius Adamczyk**>: 12%.

<**A - Thomas A. Szlosek**>: 12%, Steve.

<**Q - Charles Stephen Tusa**>: And the commitment is to continue to do that and drive that faster than earnings going forward for the next few years?

<**A - Thomas A. Szlosek**>: Well, I think that the...

<**A - Darius Adamczyk**>: Yes, the – go ahead, Tom.

<**A - Thomas A. Szlosek**>: Yes, the commitment that we've made that Darius talked about at his Investor Day, at our Investor Day, was continuing for the five-year plan with the idea of raising a dividend faster than the earnings growth. And we're coming up to the end of that. As we look forward, we'll watch that. But at minimum, we're committing to keep the dividend growth in line with earnings growth. It'll track EPS.

<**A - Darius Adamczyk**>: Yes, and then...

<**Q - Charles Stephen Tusa**>: Yes, and then...

<A - Darius Adamczyk>: Steve, just to answer that...

<Q - Charles Stephen Tusa>: Sorry, go ahead.

<A - Darius Adamczyk>: Yes. So, as we said [ph] – as Dave (39:06) committed for the five-year period which ends in 2018, we're going to grow dividends on a pace that's faster than earnings. We're committed to that. It's consistent with what we said five years ago. So, period after that, what I would say it's going to be equal to or greater than earnings. We're going to provide greater clarity on that in our February Investor Day. But I would expect to be equal to or greater than.

<Q - Charles Stephen Tusa>: Right, and you guys have FCF so we can talk about that. Seasonally, it kind of suggest that your cash should be kind of towards the higher end of the range. Just remind us what the target is for 100%. Is that for 2018 or 2019?

<A - Thomas A. Szlosek>: Yes, Steve. The way I talked about that at the Investor Day and largely sticking to it is that by – at a run rate, 2018, but really in 2019 we expect to be at that 100%.

<Q - Charles Stephen Tusa>: Okay. And then one last question. Math is clearly not a strong suit or prerequisite for being on the sell side. But the math around Safety and Productivity Solutions, I was getting to something a little different like maybe 1%, 1.5% growth in the core business. And with your new android product that's coming in, would you expect that kind of core growth? I mean, not that it really matters because Intelligrated is an organic grower that has tremendous orders so I'm not sure why we're picking that apart in the first place. But would you expect that to get better next year and some of these new products come into the fray in Safety and Productivity?

<A - Darius Adamczyk>: Yes, absolutely. I mean, we expect much improved growth rate in Productivity Products next year as these new products launch and gain traction. I'd probably expect it to accelerate a bit through the quarters because the bulk of our launches are coming in Q4 and Q1. So, obviously, it takes time to generate the orders, but short answer is yes.

And I think we continue to talk about Productivity Products. It's one segment of one business where we had a little bit of a struggle, but across all the other businesses, it's been a really nice story of both top line growth and margin expansion.

<Q - Charles Stephen Tusa>: Yes. I guess people just can't live without adjusting numbers everywhere, so I can understand why we would do that for a segment like that. Congrats on the top tier organic growth and keeping your eye on the ball.

<Q - Gautam Khanna>: I was wondering if you could provide your early perspectives on any competitive implications of UTX, Collins. And have you given any more thought to the whole Boeing avionics initiative and their stated goal of kind of moving into the aftermarket on the Aerospace side? Thank you.

<A - Darius Adamczyk>: Sure. Yes. So, I mean, I think starting with Collins and UTX, obviously, is something that we've analyzed. But the way we look at this is the capability that we currently have both in mechanical systems as well as avionics are on par greater than anything that UTX or Collins would have in creating that merger.

I am particularly excited as it relates to our vision of Connected Aircraft because having both front end and electronics as well as the mechanical systems, really gives you the strength and capability to implement and deliver that vision of a Connected Aircraft. And it's not theoretical for us. It's something that we already have and are delivering and it's growing double-digit, and we're marching through the aircraft to get all of our systems connected. We already have APUs launched to wheels and brakes this quarter and we're going to be marching through. So, I'm not sure that that merger puts us at any kind of a disadvantage vis-à-vis UTX or Collins.

And maybe most importantly, I never viewed the Aerospace segment as one where scale matters. What matters for us is technology differentiation and that's going to be our basis for competition.

In terms of the Boeing avionics and services announcement, clearly we respect what they're doing. There is not a lot of clarity yet in terms of exactly what that means and what they'll be doing. Obviously, Boeing is a highly valued and important customer for us which we're going to continue to work with and support. But we also have our own relationship with the end-users, the airlines and we have a strong vision for growing our services in RMUs and Connected Aircraft as well. So, we're going to be as supportive as we can to Boeing and stay in sync with them and create a win-win for both companies.

<Q - Gautam Khanna>: Thanks. And Darius, maybe just a follow-up on M&A. When you look at the pipeline and some of the portfolio actions you've announced, are there any larger properties that are attractive to you? Or should we expect more on the kind of couple billion or Elster size bites going forward or are there some [ph] big swings in this (44:37)?

<A - Darius Adamczyk>: Yes. There is always things that are attractive, but I would expect more of the bolt-on variety, that's really our sweet spot, and that's where we're looking. And I would say our pipeline is filled more with bolt-on variety type of acquisitions.

But you never know, anything could happen. But I would say I would be more expectant of bolt-ons.

<Q - John G. Inch>: And I'd also like to echo Steve Tusa's commentary. It's nice when companies allow questions. So, I want to start. Was the...

<A - Darius Adamczyk>: We aim to please, John.

<Q - John G. Inch>: Yes. You roll with the punches. I appreciate it. So, what about pricing? Was there any discernible trend on pricing? There's a little bit of still this debate around raw impacts, various companies are calling out. And just curious, I realize you guys have – you're not a huge raws spreads company. But there is a little bit of impact. Are spreads improving? Or how should we think about that?

<A - Darius Adamczyk>: Yes. No. I mean, obviously we're in a bit of an inflationary environment for some the commodities. But one thing I'm very proud of all of our teams and all our businesses, they really stayed on their toes and made the adjustments, understand what the impacts are, and really are capturing the value that our services and products provide for our customers.

So, I think overall, we've probably been more challenged on the cost side this year than we've seen in a while, but I also think we've reacted quickly, made the right adjustments. We have a very active value engineering program as well that produces substantial productivity. And we also understand the value that we bring to our customers and make adjustments as required. So, all in all, we've done a nice job here.

<Q - John G. Inch>: Were spreads a drag in the quarter?

<A - Mark Macaluso>: Say that again, John?

<Q - John G. Inch>: Yes. I just said – sorry. Were spreads a drag in the quarter this year vs. last year? If there's a way to kind of capture that?

<A - Thomas A. Szlosek>: No. I think we're – when you look at the actual pricing, it's what we talked about last quarter. It's holding in there quite nicely, 50BPS to 100BPS depending upon the business and largely recovering to the types of inflation Darius talked about. Like you said, the businesses are laser focused on this, particularly on the material inflation side.

<A - Darius Adamczyk>: Yes. And John, I'd just point to the fact that every one of our businesses expanded margins in Q3 – every single one. And we're on that trend for the whole year as well.

<Q - John G. Inch>: Yes. So, that kind of almost leads to the question of cash, and given all the investments you guys have been putting in, the products and so forth, and the growth that you anticipate, it's clearly, growth is picking up in PMT and Aerospace.

I forget, Darius, if you had mentioned this in kind of the portfolio review call, but what's your sort of line of sight to Honeywell getting to 100% free cash conversion if not higher than that? And where does that kind of rank in your strategic priority list of things you're trying to accomplish?

<A - Darius Adamczyk>: Yes. It's important, and that's exactly what we're aiming is 100%. It's consistent with the message we've been giving. We're marching towards that goal. We did roughly 90% this year. We expect to see improvement next year and then further improvement 2019, and it's a very conscious goal. And I can tell you that we've never had more focus on working capital than we do today. We're seeing some progress being made there, and there's more to go. But it's a very important goal, a goal that both Tom and myself and the rest of the business leaders take very seriously and we're committed to.

<Q - John G. Inch>: Just lastly, the question to capital allocation, you basically said, look, let's think about near term, we'll think about foreseeable future bolt-ons. A lot of the stuff out there is pretty pricing given what's happened in the public markets plus, Darius, I think a lot of the things that you want to aspire toward improving or realizing in your mix, software, industrial, et cetera – and that stuff's got to be pretty pricy, too.

Is the playbook kind of in the intermediate term just we're not going to do a lot of M&A? How do you judge that balance or gauge that balance? Because you don't want to overpay, but you don't want to sit and sort of do nothing if the prices are the prices, right?

<A - Darius Adamczyk>: Yes. No. I think that's fair, and we've been very cautious. We've been very active, by the way, in the M&A area. But the one thing we're known for during Dave's era and it's going to be the same during this one, is we're going to stay disciplined in terms of M&A.

But if you're selective and you're active, which we're going to be both of these things, sometimes you can find the gems at the right price. So we're going to continue trying. We have a robust pipeline, and we're not marching off the field because things look expensive. They do, but we believe that there are opportunities out there where we can participate at an appealing valuation.

Now, having said that, if there's nothing that happens, well obviously, we're going to also be looking at buybacks as another way to distribute cash back to our shareholders. So, it's always a balance. We'd like to have some – have ability to stay balanced. Our preference is for bolt-on M&A, but it's got to be smart and we've got pay the right price. And if we can't get that done then we're, obviously, going to be leaning a little bit heavier on buybacks.

<Q - John G. Inch>: Thank you. And by the way, you guys better hold on to Mark. Good Investor Relations are hard to find.

<A - Mark Macaluso>: I owe you one, John.

<A - Darius Adamczyk>: Yes, I think the check's in the mail, John.

<Q - John G. Inch>: Any check would be welcome, trust me. Thank you.

<A - Darius Adamczyk>: It just feels like there's a lot of passive aggressiveness on the call today.

<Q - John G. Inch>: I can't imagine -

<Q - Nigel Coe>: Yes. So, no passive aggressiveness. Maybe some aggression but nothing passive. The 5% to 7% SPS organic growth, obviously, in Q4, we've kind of been chatterboxing around this as well. So, math is not my strong point, but Intelligrated would be what, 2 points, 2.5 points of tailwind for that number. So, we're looking at maybe a core of 4% to 5% ex-Intelligrated?

<A - Thomas A. Szlosek>: Yes, I think, I'd have to do the math, but each of the businesses at least low to mid single-digits, I mean, putting Productivity Products aside.

<Q - Nigel Coe>: Yes.

<A - Thomas A. Szlosek>: So, for example, the Safety business, Nigel, I mean, where it was low single-digits in Q3, that's going to be good mid single-digits in the fourth. Industrial Safety will be well into the mid to higher single-digits. High-risk business is doing well.

We also will have really strong results expected on the retail business. As you know, we've changed the business model. That's going to be well into the double digits. Productivity, even with the Productivity Products, overall, we'll be high single-digits in Productivity. As Darius said, the scanning business is doing fantastic, workflow is going to be north of 20%, our software and sensing business will be mid to high single-digits.

Intelligrated will be up like we said it would be. But it's everywhere and globally as well. I mean, it's in the U.S., it's Europe, China. So, it's not just a pull from Intelligrated that's doing this nor is it the Productivity Products pulling us down. These are all really good growers to give us that organic growth range we talked about.

<Q - Nigel Coe>: No. That's sounds pretty broad. One of your competitors, Dematic, dropped a surprise warning in their warehouse business, I think it was yesterday or the day before. It seems to imply they're losing some share. I mean, maybe could just touch on how you're seeing maybe the front log in the warehouse business as you go into 2018?

<A - Darius Adamczyk>: Yes, we continue to be very bullish and we had a very strong orders quarter in Q3. We anticipate another one for Q4. And as I said, that business is really well-positioned because it's – what's really growing the fastest is the e-commerce high-throughput type of warehouses and that's exactly the sweet spot of that business. And customers are seeing the value and we're generating the orders. And as you can imagine, it's a very quickly growing playing field in warehouse automation given the expansion in warehouse and distribution and we don't see that pausing. We're bullish on our Q4 and we're bullish on 2018.

<Q - Nigel Coe>: Great. And then just a quick one, sorry.

<A - Thomas A. Szlosek>: No, I was just going to say we did take note of the competitor announcement you talked about. But as Darius said, our third quarter was just fantastic in terms of orders growth in Intelligrated. I mean, strong, strong double-digits. And as we said, we expect that to continue. Backlog is really good, I mean, compared to last year and it's all organic growth. I mean, well over 50% backlog growth. So, it's positioned very well.

<Q - Nigel Coe>: And then just a quick one, Tom, on the [ph] 350BPS (55:13) of margin expansion in Q4. Obviously, the FX hedge we got in place for this year is margin dilutive given the dynamics of stronger revenues from weaker dollar, but no impact to EBIT. So, I'm just wondering would that be about 20BPS or so? That's what my math tells me.

<A - Thomas A. Szlosek>: You mean for Q4?

<Q - Nigel Coe>: For Q4, yes.

<A - Thomas A. Szlosek>: Yes. I mean, the translation – that will be about flat for us, I mean, y-over-y. I don't think that's going to be a big impact overall, FX for Q4.

<Q - Nigel Coe>: Okay. Got it.

<A - Thomas A. Szlosek>: When you consider the hedges, the movement in the rates and everything, it's basically flat.

<Q - Jeffrey Todd Sprague>: Just a quick one for me. You guys covered a lot of ground. I just wanted to get a – hone in a little bit further on this FCF question looking forward. And I'm just wondering, perhaps it's for Tom, but Darius is certainly welcome to chime in. Just what are the big bridge items next year when we think about FCF? I'm assuming CapEx might be down a little bit. I don't know if you expect help on working capital. You've got growth that will mitigate against it, right? So, maybe your turns improve but maybe absolute working capital doesn't, pension, et cetera. Just what are really the big items next year that kind of puts you on the path to the 100% in 2019?

<A - Thomas A. Szlosek>: I mean, when you look at 2017, Jeff, we're looking at about $1B of CapEx, although that could be a little heavy. When you look at that as a reinvestment ratio, expect that to come down in 2020. There will be at least $150mm, $200mm less of CapEx which is a big driver for us. We do have incremental cash tax spending this year that's mostly timing related. We'll have probably by the end of the year incremental $500mm y-over-y. I don't expect that to repeat next year, so that should give us some tailwind.

And then most importantly, operationally, as Darius talked about, is working capital. We're kind of improving our trends, which means kind of treading water this year, not necessarily adding huge amounts to working capital. The turns kind of staying flat. But as you said, a lot of business focus on driving that going forward. We're going to need $200mm, $300mm out of working capital next year to drive towards that 100%. Those are the, I'd say those are the big three things that we're looking at.

<Q - Andrew Burris Obin>: Just a couple of questions. On Aerospace, as we think about the Defense portfolio of programs, as Defense budgets improve, how should we think about your portfolio of programs relative to budget, i.e., do you think you can keep up with the budget? Meaning is there something, is there a big outline in terms of your programs that Honeywell is going to be very different?

<A - Darius Adamczyk>: Yes, I think it's going to be aligned. I mean, we're seeing really good growth, particularly in U.S. Defense budgets where we – I think we have obviously greater clarity and a much greater density, and that segment of the business is doing well. We anticipate to continue to do well and it will be aligned or higher than the growth.

When it comes to international, it's a little bit more hazy, because obviously, we're talking a lot of different countries, a lot of different programs, and we have some programs that are ending, some that are continuing. But overall, it's kind of an up arrow given what we're seeing in geopolitical arena, anticipate slightly greater spending by NATO as a whole. So, in some recovery in [ph] helo (59:58) markets in the future which is, as you know, is in that segment. So, overall, constructive when it comes to Defense.

<Q - Andrew Burris Obin>: Right. So, that should be a nice tailwind to Aerospace. Another question, just talking about China and emerging markets visibility, A, what are you guys seeing on the ground with this [ph] party (1:00:20) Congress? Is everything on track? And the second, how should we think about your China exposure going forward given the portfolio changes that you guys have made now that your China business is really driven by Aero and UOP? Do you sort of disconnect from the underlying China macro to a certain degree going forward? Thank you.

<A - Darius Adamczyk>: No, I mean, China and India as we pointed out this quarter have been up 30%, and that success is not isolated to PMT or Aero. That's for every one of our business segments. And as you can imagine, as COMAC gets going even further, Aero actually – that revenue potential is still way ahead of us, not behind us.

Secondly, UOP, HPS are continuing to win across the board in China and India. Tremendous successes there this year. Buildings and Home, we approach those markets a little bit differently than we do in some of the developed markets. But again, double digit growth in both. So, very well aligned with the organization trends. So, whether that's a big independent Homes business or the remaining is Buildings portfolio are going to do very, very well.

Warehouse Automation, now moving onto SPS, again, early days, but it's a maturing segment and one in which we're going to participate in. And then finally, Industrial Safety, another segment that's evolving and still in kind of the early days. But clearly, worker safety is very much on the forefront of the agenda of both China and India. And the regulatory environment there is changing to much more worker-oriented.

So, across our portfolio, we're excited about our potential in both China and India. Both of those are great markets, we have great management team that have both a local perspective, and the results speak for themselves. I mean, 30% growth in Q3 I think is tremendous.

<Q - Andrew Burris Obin>: It's good to know that...

<A - Thomas A. Szlosek>: I'd just add to that, Andrew, just I think your inference was that we're dependent upon HBT for growth there. But if you look at Q3, I mean, HBT was our slowest grower amongst all of the segments in China. So, really a strong position.

<Q - Andrew Burris Obin>: Right. I think that was the gist of my question exactly. Terrific.

<Q - Andrew Kaplowitz>: Tom, last quarter you stepped up restructuring and talked about $150mm of benefits, and it does seem like you will do a fair amount of restructuring here in the short term. I know you talked about the $150mm of benefits from that last restructuring. But will you have a greater than normal restructuring tailwind as you enter 2018? How do we look at that?

<A - Thomas A. Szlosek>: Yes. I mean, I don't think it's necessarily greater than what we would have had going into this year. In fact, if you remember, Andy, that we did the significant restructuring when we divided ACS up into HBT and SPS. There was a fair amount of delayering that took place that gave us some pretty good tailwinds as we headed into 2017.

So, in 2018, I agree, we've put a lot of capital to work on restructuring, and there is clear momentum coming. But I wouldn't say it's a multiple of the – or the tailwind that we had coming into 2017. And we'll give you more color on that as we get into our earnings outlook in December.

<Q - Andrew Kaplowitz>: Okay. That's helpful. Then, Darius, Aero has been a pretty big positive surprise I think for you really the whole year, so far. How much do you think the surprise has been the early year reorganization vs. just you had a confluence of events last year that were kind of negative that have gotten better here in 2017? And maybe what's been the biggest surprise in the performance here in 2017?

<A - Darius Adamczyk>: Well, yes. I mean, you're right, Andrew, I'm very pleased with how Aero is performing. I think, not that I'm surprised by it, but I am very pleased with what's happened in terms of Commercial Excellence, the business capturing the aftermarket business, the RMUs, the growth in Connected Aircraft. It's invested in that last year in Q4, around 200 people that's generating a lot of new sales and we watch that at a very detailed level.

The business continues to drive productivity so it does what I always want every business to do which is grow the top line as well as get more productive every year. And yes, that certainly – last year was a tough year, more headwinds on the concessions, but the reorganization also helped as we segregated the decision-making. It's now a faster business, it moves faster. So, I'm really pleased with how they're executing and its continued outlook for the future.

Darius Adamczyk

Q3 Highlights

Performance

- I am pleased with our continued performance in Q3, especially with our continued organic sales acceleration, our improved profit conversion, and our y-over-y improvement of FCF
- We remain focused on delivering the sustained financial results you would have come to expect from Honeywell
  - There will be no distractions even as we work to spin the Homes and Transportation Systems businesses
- I look forward to sharing more of Honeywell's successes with you and our plans for 2018 over the coming months.