Company Name: Honeywell
Company Ticker: HON US
Date: 2018-01-26
Event Description: Q4 2017 Earnings Call

Market Cap: 125,693.14
Current PX: 164.99
YTD Change($): +11.63
YTD Change(%): +7.583

Bloomberg Estimates - EPS
Current Quarter: 1.894
Current Year: 7.977
Bloomberg Estimates - Sales
Current Quarter: 10010.909
Current Year: 42202.316

Q4 2017 Earnings Call

Company Participants

- Mark Macaluso
- Darius Adamczyk
- Thomas A. Szlosek

Other Participants

- Jeffrey Todd Sprague
- John G. Inch
- Charles Stephen Tusa
- Steven Winoker
- Andrew Kaplowitz
- Scott Davis
- Gautam Khanna
- Peter J. Arment
- Andrew Burris Obin

MANAGEMENT DISCUSSION SECTION

Mark Macaluso

Non-GAAP Financial Measures

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

Darius Adamczyk

Business Highlights

Commercial Excellence

- Honeywell delivered an exceptionally strong fourth quarter with EPS of $1.85, enabled by organic sales growth of 6%, which reflects our renewed emphasis on commercial excellence, revitalization of the Velocity Product Development process, and the benefits from growth investments
- In 2017, we expanded our sales force in key regions and businesses and armed all our sales teams in newest digital tools that are helping us win in the marketplace
  - We also revitalized our new product development process to ensure that the products we're selling are delivering value to our customers
- Our order rates continue to grow, and our backlogs are strong as we head into 2018

FCF and Working Capital

- Cash was a highlight as we generated $4.9B of FCF in 2017, above the high end of the guidance range
- In Q4, we achieved 123% conversion, which brought full year conversion to 90% or 109% excluding the impact of pension
- Our efforts to improve working capital discipline are working
- While I'm encouraged by our progress in this area, there's still significant opportunity and each of our business is taking the necessary steps to improve their working capital performance

FY EPS

- Full year EPS were $7.11, up 10% y-over-y
- This growth excludes the impact of separations costs for spin and charges for fourth quarter 2016 debt refinancing, pension mark-to-market and Tax Cuts and Jobs Act
- Our EPS exceeded the guidance we've provided in December, driven by 4% organic growth and 70BPS of margin expansion

Capital Deployment

- We also continued to aggressively deploy capital for share owners in 2017
- We increased our dividend by 12% this year which marked the eighth double-digit increase since 2010
- And we bought back $1.6B of shares in Q4 and $2.9B for the full year
- As a company, our total shareowner return was 35%, far exceeding the S&P 500 CSR of 22%
- Today, we are raising our full year 2018 EPS guidance to $7.75 to $8, which reflects a lower expected tax rate as a result of the Tax Cuts and Jobs Act

Tax Reform

- Tom will walk you through the tax reform detail later in the call
- But I'm pleased to announce today that our 2017 performance, coupled with the anticipated benefits from this legislation, has enabled us to increase our 401(k) employer match for Honeywell employees in the U.S
- This change represents a sustained, long-term commitment to provide enhanced financial security in retirement which we believe is extremely valuable, important to employees
  - Honeywell remains committed to being an employer of choice

Commercial Success

- Let's turn to slide 3 to highlight a few of our recent commercial successes
- In Aerospace, United Airlines selected Honeywell avionics for its new fleet of more than 150 Boeing 737 MAX airplanes
- The flight deck package will include the first-ever installment of Honeywell SmartRunway and SmartLanding on a Boeing 737 MAX and will feature Honeywell's integrated multi-mode receiver and IntuVue weather radar

system, which can enable connected radar part of our Connected Aircraft offering allowing Honeywell to download weather hazard data and provide pilots and dispatchers immediate information through the GoDirect weather app

- Honeywell solutions work in tandem to greatly improve passenger safety and comfort during takeoff, landing, and potentially hazardous weather conditions
  - We are excited about our continued partnership with United Airlines

Home and Building Technologies

- In Home and Building Technologies, Honeywell designed a new contemporary and state-of-the-art Connected Home solution, and we signed a long-term agreement with ADT, a leading provider of security and automation solutions in the United States and Canada to sell it exclusively through ADT's direct and professional dealer network
- This solution includes security, smoke detection, carbon monoxide detection, innovative long-range and battery operated motion viewers and home automation and incorporates both ADT's and Honeywell's user experience
  - We are excited to continue our long-term partnership with ADT, providing their customers the most innovative products for the Connected Home

Performance Materials and Technologies

- In Performance Materials and Technologies, Honeywell Process Solutions leveraged Connected Plant offerings to position Honeywell as a specialized software industrial partner, ultimately winning three strategic projects with Kuwait Oil Company to enhance crude production in the southeast Kuwait fields
- Honeywell will provide software and services to help KOC visualize and optimize the production and operations in the fields and will supply an integrated control and safety system based on our Experion PKS and Safety Manager technology for a gathering station
  - This project enhances the capacity and capability of the existing facility in East Kuwait to manage excess water while keeping crude production at the facility's designated capacity

Safety and Productivity Solutions

- In Safety and Productivity Solutions, we achieved major wins with two global package delivery companies to provide more than 100,000 Android-based handheld computers that will aid in delivery operations
- We are seeing strong adoption of our new Android-based offerings and have significant new launches planned for early this year that will drive growth for the Productivity Products business in H2
- A number of these technologies will be on display at our Annual Investor Conference which will take place on February 28 at Honeywell's headquarters in Morris Plains, New Jersey
- I'm looking forward to talking with you more about our progress then

Thomas A. Szlosek

Financial Highlights

Organic Sales Growth, M&A and Margin Rate

- I'm on slide 4
- As Darius mentioned, we achieved 6% organic sales growth this quarter, capping off a very strong year
- Our growth improved sequentially every quarter from 2017 starting with 2% in Q1
- It's a reflection of the investments we've made in the sales organization, the M&A that we've done, our capacity expansions, and new product development, coupled with an improved economic environment in many of our end markets
  - We generated more than $2B in segment profit in Q4 through our continued focus on effective selling and operational excellence
- We experienced strong volumes, primarily in Aerospace and Safety and Productivity Solutions
- Our margin rate increased by 30BPS to 19.3%, stronger than we previewed in December, primarily due to stronger than anticipated demand in the Air Transport & Regional aftermarket

EPS, Tax Rate and Share Count

- EPS was $0.01 better than our preview in December and includes $0.19 contribution from segment profit
- Our tax planning actions drove a lower-than-planned tax rate for Q4 16.5%
- Now this is before the impact of the Tax Cuts and Jobs Act
- The lower tax rate and lower share count driven by the share repurchase activity Darius mentioned combined for $0.22 benefit, which was more than offset by restructuring and other projects we funded in the quarter, which was $0.30 headwind

Cost Structure

- We funded over $150mm in attractive restructuring project this quarter that will improve our cost structure, drive further productivity, and address the potential residual cost that would otherwise result from the upcoming spin transactions
- On a reported basis, we had a loss per share of $3.18, driven by the impact of the $3.8B TCJA charge
- That reported loss also includes an $87mm pre-tax pension mark-to-market adjustment, primarily related to a lower discount rate and $16mm in pre-tax spin-related separation costs

FCF and Working Capital Initiatives

- Our FCF in Q4 was very strong at $1.8B or 123% conversion
- We're in the early stages of our working capital initiatives, but we're encouraged by the progress so far and more importantly by the opportunities that we intend to pursue in 2018
- Overall, another strong performance with high-quality earnings to cap off a great year

Segment Results

Aerospace

- Let's turn to slide 5 to discuss our segment results for Q4

- Starting with Aerospace, sales were up 5% organically, 2 percentage points above the high end of our sales guidance
- In Commercial OE, we saw improved air transport deliveries on key platforms, including the Airbus A320 and A330 and Boeing 737 and the benefit of lower OEM customer incentives, partially offset by slow demand in business jets, as expected
- Growth in the aftermarket was stronger than anticipated, driven primarily by air transport, repair and overhaul activities and sales of spares in business aviation

Defense

- In defense, we saw continued strength in U.S. core defense driven by spares demand and deliveries on the F-35 and Apache platforms
- In Transportation Systems, we saw a robust event in commercial vehicles across all regions and continued growth in light vehicle gas turbos in China and South Korea
- Aerospace margins were up 270BPS, driven primarily by higher volumes, productivity net of inflation, slightly more modest OEM and customer incentives and commercial excellence
- Aerospace margin performance was well ahead of our expectations

Home and Building Technologies

- In Home and Building Technologies, organic sales growth was 3% for the quarter
- As a reminder, we realigned the Smart Energy business from HBT into PMT in Q4
- So, the HBT results for this quarter and going forward now excludes Smart Energy
- Organic growth in products of 2% was driven primarily by the Commercial Fire business and Environmental & Energy Solutions in Europe
    - There was continued strength in global distribution, particularly in the fire vertical
- Our businesses in China grew high-single digits with strength in all of the HBT businesses
- HBT segment margins contracted 40BPS, driven by lower residential security volumes, investments for growth and a different regional mix

Performance Materials and Technologies

- In Performance Materials and Technologies, sales were up 9% on an organic basis, driven by growth across UOP, Process Solutions and Advanced Materials
- That's the entire PMT portfolio
- In UOP, there was strong demand for our modular equipment, strong initial catalyst loads in the Middle East and significant growth from natural gas project wins at UOP Russell in Russia and in North America

Advanced Materials

- Growth in the short-cycle businesses within HPS continued to be strong with significant demand for Thermal Solutions and Field Instruments

- In Advanced Materials, we again achieved double-digit organic sales growth, fueled primarily by our Solstice low-global-warming refrigerant for mobile air-conditioning
- PMT segment margins contracted 180BPS in the quarter, primarily driven by the unplanned plant outage we flagged in November and a different y-over-y mix of sales in UOP.
- The lower-margin performance is also in part due to integration of Smart Energy, which was not contemplated in our original fourth quarter guidance

Safety and Productivity Solutions

- In Safety and Productivity Solutions, sales were up 12% on an organic basis, exceeding the guidance we provided in October, driven by another strong quarter at Intelligrated, building on the robust orders and backlog growth throughout 2017
- We had a significant increase in retail business sales as our direct selling strategy matured as well as continued strength in China

Mobility Business

- There was also robust growth in the Safety business as refinery maintenance resumed, driving demand for our entire range of Safety Products and continued strong demand for our legacy Sensing and Controls and Workflow Solutions, including solutions provided by Vocollect and Movilizer
- The mobility business remained soft, but we secured several large orders for our new Android-based products, which Darius mentioned
- As a result of strong volumes in SPS, margins expanded 140BPS, also exceeding the high end of our guidance, helped further by the benefits from ongoing productivity efforts and from previously funded repositioning

Orders and Backlog

- I'm now on slide 6
- I'll be very brief on this slide as we've discussed each of these measures previously
- What this slide does is it takes us back to the original 2017 guidance and compares it to the final results
- For all categories, the final outcome met or exceeded the original guidance, so the do matches our say in Honeywell vernacular
- Also, not included on this slide, our long cycle orders and backlog
    - Those results were also impressive, each growing double digit in 2017

U.S Tax Reform

- Let's move to slide 7 to discuss the recent U.S. tax reform and its impact on Honeywell's 2018 financials
- Honeywell has long been a proponent of corporate tax reform that will enable us to compete more effectively on a global basis and to enjoy efficient and unencumbered movement of our capital
- On December 22, as you know, the U.S. Tax Cuts and Jobs Act passed

- The legislation significantly revises the U.S. corporate income tax by lowering corporate income tax rates, implementing the territorial tax system and imposing a repatriation tax on deemed repatriated earnings of foreign subsidiaries
- As a result of legislation, we recorded $3.8B provisional charge in Q4, comprising of three elements
- The first is a mandatory transition tax or deemed repatriation charge on the $20B of previously unremitted earnings of our foreign subsidiaries
  - This non-cash charge was recorded entirely in Q4 2017 but is to be paid over an eight-year period in accordance with the legislation

Non-Cash Charge

- The second element is also a non-cash charge
- It's a deferred tax liability adjustment, favorable in this case, to reflect the impact of the lower U.S. corporate tax rate on our deferred tax balances

Tax Structure

- The third element, also a non-cash charge, is for the implementation of the territorial tax system, including withholding and local taxes associated with the future repatriation of cash back to the U.S
- These taxes will generally be paid as the cash is repatriated
- This portion of the aggregate charge reflects the tax structures we have in place today as is required by the accounting rules and does not anticipate the benefit we would realize from future tax planning
  - It's only been a month since the tax reform passed, and further guidance continues to flow, clarifying the legislation

Tax Legislation

- Our accounting reflects our best estimate using the current information we have available to us, and the amount of the provisional charge may be adjusted over the course of 2018, as things become clearer
- We will update you on the changes, if any, to the amount of the charge to our effective tax rate and to other provisions of the tax legislation, which are material to Honeywell

Cash Proceeds

- At our upcoming Investor Day, we will also update you more completely on the cash repatriation opportunities that we have as well as on our expectations for the use of those repatriation proceeds
- Preliminarily, we expect that at least $7B of the $10B of cash held by our foreign subsidiaries can be repatriated in the next two years and, of course, we'll continue to generate overseas cash, which will add to that pool of potential repatriation
- But there's still this extensive tax analysis and planning to be done to ensure we execute repatriation in the most efficient manner

Dividend and M&A

- This new global mobility of our cash will allow us to continue investing in our businesses in the U.S., to a pay competitive dividend to more aggressively seek out M&A, particularly in the U.S., and to repurchase our own shares
- Our preference is for attractive bolt-on acquisitions in our core markets
- But to the extent M&A opportunities do not materialize, we'll gradually accelerate share repurchases as we did in 2017

Tax Rate

- Looking at 2018 as a result of the reduction in the U.S. corporate tax rate, our effective tax rate is now expected to be between 22% and 23% vs. our normal 25% to 26% historical rate
- Given the uncertainties that still remains around the implementation of tax reform and the extent of the analysis still to be done, we are conservatively assuming a tax rate of 23% in our guide, which increases our 2018 EPS guidance range by $0.20 to a new range of $7.75 to $8 per share, an increase of 9% to 13% from 2017
- So as Darius and I mentioned, we're pleased with the new legislation, particularly the mobility of capital and global competitiveness it provides to Honeywell and to our share owners

Guidance

Backlog, Organic Sales Growth and Tax Rate

- Let's discuss our expectations for Q1 on slide 8
- We exited the year with strong order rates and firming backlogs that we expect will drive a continued acceleration in organic sales growth every quarter in 2018
- Segment margins are expected to expand 30BPS to 60BPS, driven by volume leverage, commercial excellence and productivity net of inflation, leading to EPS of $1.87 to $1.93 or growth of 9% to 13%
  - This is based on an estimated first quarter tax rate between 22% and 23%
- As we previewed in the December outlook call, the guidance for Q1 and full year exclude costs related to Home and Transportation Systems spin-offs and adjustments, if any, to Q4 provision from the tax legislation

Aerospace

- Starting with Aerospace, we expect sales to increase in the low-single digit range organically
- Our air transport OE business will be impacted by fewer deliveries on Boeing 777 and a decrease in production rates at certain regional OEMs, partially offset by increased A350 deliveries

Business Aviation

- On the business aviation side, we expect organic sales to improve as production rates increase across most of our OEM customers, offset by higher OEM customer incentives
- In the aftermarket, we expect to see strong spare sales with airlines across the Americas and Asia Pac and demand in Maintenance Service Plan in business aviation

- For defense, a very similar story to recent quarters with growth buoyed by demand in U.S. defense, partially offset by declines in space

Transportation Systems

- In Transportation Systems, we expect continued light vehicle gas turbo penetration across most region, particularly in China, North America and Europe as well as continued momentum in the commercial vehicle segment

Home and Building Technologies

- In Home and Building Technologies, sales will be slightly up
- We expect continued strength in Global Distribution, the Commercial Fire business, and our businesses in China
  - We see improving order pipelines in our EMEA products businesses offset by weaker volumes in residential security in the U.S

Building Solutions

- In Building Solutions, growth will be modest as the robust high growth region activity is offset by slower activity on large install and service projects in the Americas region
- As we progress with our planning for the spin-offs, we have reorganized Home and Building Technologies to better align with how the segment will operate going forward
- So instead of showing you results from products and distribution, we'll start reporting on results in the two new reorganized business units, Home and Buildings
  - This will be effective when we release first quarter earnings

Performance Materials and Technologies

- Moving to Performance Materials and Technologies, sales are expected to be up low- to mid-single digit on an organic basis, driven by continued conversion of our strong backlog
- Entering 2018, PMT long-cycle backlogs are up 8% from 2017

Process Solutions

- In Process Solutions, we also expect continued demand for our short-cycle software and service offerings and field and instrumentation products
- In UOP, we expect significant catalyst deliveries for new units in China as well as sustain equipment and engineering growth
- Solstice growth and Advanced Materials is expected to continue, although there are tougher y-over-y comparisons in Q1

Safety and Productivity Solutions

- Finally, in Safety and Productivity Solutions, we expect sales in the mid-single digit range organically, driven primarily by large project wins at Intelligrated and strong orders demand exiting the year in Sensing and IoT and workflow solutions, including from Movilizer's cloud service application

- In Safety, we expect growth across the gas vertical in China and all lines of business in the Americas as a result of our new product launches, sales investments, and improved market condition
    - We also expect improvement in the retail business
- On a regional basis, the SPS China business is expected to grow more than 10%, driven by Sensing and IoT, Safety and Productivity products in the region

FY Margin

- Let's turn to Slide 9
- I want to talk about our revised full year guidance
- We've updated our full year margin guidance to reflect our stronger-than-expected performance in 2017
- Full year segment margin is now expected to be between 19.3% and 19.6%
    - This reflects 30BPS to 60BPS expansion, which is consistent with what we said in December
- The segments have been updated accordingly

EPS

- We've also updated our EPS guidance, as Darius mentioned, to reflect a lower anticipated full year effective tax rate between 22% and 23% due to the tax legislation
- Full year EPS is now expected to be $7.75 to $8, up 9% to 13% y-over-y, excluding separation costs, Q4 2017 charge related to the tax reform, and any 2018 adjustments to that charge

Capital Deployment and Share Repurchasing

- Let me wrap up on slide 10
- Fourth quarter was an outstanding finish to 2017
- We achieved strong sales growth, continued margin expansion, double-digit earnings growth and exceptional FCF conversion
- At the same time, we continued our aggressive capital deployment with more than $1.5B in share repurchases in the quarter and $2.9B for the full year
- We also funded more than $350mm in restructuring in 2017, which is helping us to proactively address stranded costs ahead of our two planned spin-offs
    - Those spin-offs remain on track for completion by the end of this year

U.S. Tax Reform

- We're also pleased with the passage of U.S. tax reform, and we've raised our 2018 EPS guidance by $0.20 as a result
- We believe that the tax reform will provide a sustainable, long-term benefit to Honeywell, not a single quick hit

- In that same light, we believe that the benefit that we share with our work associates should also be a sustainable, long-term benefit
- So, we've chosen an ongoing mechanism that will benefit them now and in the years to come throughout their retirement
  - That is an increase of the employer matching contribution in our U.S. 401(k) plans

Backlog

- Our strong order rates and increased backlog heading into 2018 give us confidence in our first quarter guidance
- We're well positioned for continued outperformance in 2018

QUESTION AND ANSWER SECTION

<Q - Jeffrey Todd Sprague>: Hey. Just a couple things, first, I just wonder if you could elaborate a little bit more on Aero margin. It was very strong. Was there any unusual timing and incentives or program closeouts or anything like that? First question.

<A - Darius Adamczyk>: I wouldn't say there's anything unusual. We obviously had a very favorable mix as reflected by the commercial aftermarket, and that was probably a little bit even more favorable than we had anticipated. But I wouldn't say there's any kind of one-time charges other than the impact of a more favorable mix of business than we had originally projected.

<A - Thomas A. Szlosek>: Yes. That's really the punch-line.

<A - Darius Adamczyk>: Yes, you might be thinking about the incentives comment, Jeff, but the 270BPS expansion, most of that was a combination of the volume, mix and productivity that we generated. I think the incentives were probably 0.5 of the 270BPS, so a small piece of it.

<Q - Jeffrey Todd Sprague>: Okay. Great. And then just trying to kind of wrap up just the cash flow outlook overall. Could you just update us on what you're thinking about CapEx as pension income moves around at all here at year-end? And does the outlook here anticipate any additional share repurchase in 2018 at this point?

<A - Darius Adamczyk>: Yes. I mean, starting with CapEx, Jeff, I mean we've been peaking in 2014 to 2016 north of $1.1B or so. That will be down in the $900mm range or less in 2018 and will continue to go down. We've got continued emphasis on our working capital, hoping to get another 0.5 point of working capital turns. The HOS Gold toolset is helping us with that.

On pensions, the plan is at the end of the year was fund it close to 105%. Right now, it's funded probably 110% or more. So, those assets are driving more income if you can believe that. But from a cash perspective, it is a non-event. I mean with the plans fully funded, there are no contributions for the foreseeable future. We think that's in pretty good shape, and we'll continue to drive the conversion. I mean, our cash conversion in 2016 was 86%. We told you we're trying to move towards 100%. We hit 90% in 2017, and we think the prospects are good to drive that further in 2018.

<A - Thomas A. Szlosek>: Yes. And Jeff, it's kind of reflected in the cash guidance for 2018. And I think even if you only take the midpoint of our guidance, I mean it's a fairly healthy increase. And as we discussed at length last year, we're going to continue to make progress on cash generation and cash conversion just like we showed in 2017 where we reached the magical 90% level and that's kind of where we want – it's a starting point.

<Q - Jeffrey Todd Sprague>: Great. And share repurchase? Then I'll give the floor. Thank you.

<A - Darius Adamczyk>: Yes. On share repurchases, Jeff, right now the plan is to do what we normally do, as I said. So, we will be offsetting any dilution that comes up as a result of option exercises and contributions, employee benefit plans. But as I also talked about on the repatriation, there's an opportunity materializing. I mean, the timing needs to be further analyzed. Our priorities overall remain the same and we prefer to prioritize bolt-on acquisitions that can be accretive to our businesses. But like in 2017, when the market was a bit more frothy for us in terms of M&A opportunities, we chose to deploy it towards share repurchase. We did $1.5B in Q4 alone, $2.9B for the full year, and we're able to take the share count down for the year over 2%. So, that's the kind of approach that we'll continue to head into the year with.

<**Q - John G. Inch**>: So, can we start with just the core volumes? So, you gave the update on December 13. Tom, you thought core growth would be 7% to 8%. It's 6%, but your numbers are solid with great cash flow. I guess my question is did something happen at the end of the year like was December an anomaly at the very end to cause the core growth expectations to shift lower kind of by 1.5 points...

<**A - Darius Adamczyk**>: No. I mean, as you can imagine, fourth quarter is a big volume quarter for our businesses. Aerospace, in particular, you have a lot of OEM customers, and we're kind of partnering with them to meet their delivery schedules. Those changed, and sometimes the deliveries pushed out, which was the case for Aerospace. Most of that slight moderation in the growth rate was due to Aerospace OEM. But as you saw the growth in Aero and Honeywell for Q4 organically was still very strong, and we had a better mix in Aerospace aftermarket as I said.

<**Q - John G. Inch**>: Yes, you did. So, Aero was the primary factor then, is that the message?

<**A - Darius Adamczyk**>: A little bit in PMT as well.

<**Q - John G. Inch**>: Okay. All right.

<**A - Darius Adamczyk**>: Lower-margin stuff in PMT. But no trends per se, more binary kinds of things either large transactions in most cases.

<**Q - John G. Inch**>: The shift from Windows to Android, you guys have called out increasing traction right in terms of orders. How does that dynamic work? Like are you still selling the Windows-based products? Do you have to write-down the inventory? What's actually going on here? I'm trying to understand how that prospectively impacts the financials probably in your margins, I'm assuming, in 2018 for that segment.

<**A - Darius Adamczyk**>: Yes. No. I mean, we're still selling both types of products. And as a matter of fact, the majority of the installed base in Productivity Products is still – most of the software were still written in Windows-based code. So, we foresee continuing robust sales on the Windows product offerings. But as we discussed on multiple calls last year, Android is becoming a much more prominent part of our portfolio offering. We've launched some new products in Q4, we launched some Q2. And then we have a pretty big launch coming up here also in Q1.

The great news for us as we highlighted in the announcement is we've already secured some major, major wins with these new offerings that are Android-based. So, it gives me a lot more confidence around the future of the Productivity Products business. But rest assured the Microsoft-based mobility offerings, we're still selling those fairly aggressively, and they still make up more than 50% of our sales.

<**Q - John G. Inch**>: And it's the customer, Darius, right, that incurs, if they want to shift from Windows to Android, it's sort of it's their prerogative. It's not as if Honeywell is somehow on the hook to pay migration costs...

<**A - Darius Adamczyk**>: That's correct.

<**Q - John G. Inch**>: ...or something like that, right?

<**A - Darius Adamczyk**>: Yes, exactly. They have to convert their software from Microsoft-based to Android-based and we're offering our customers a choice. Some of them are making that conversion; others are maintaining their current platforms.

<**Q - John G. Inch**>: Cash was very strong in Q4 despite obviously the business putting up robust growth. How do you manage the 2018 cash in terms of growth and acceleration in the economy and the demands in working capital, but then trying to get working capital out of the system? I guess I understand you want to keep a conservative guide, but do you think there is upside to cash given the backdrop of kind of macro improvement? Or was there a little bit of an anomaly

in Q4 given how strong it was?

<A - Darius Adamczyk>: John, I'm an optimist. I always believe there's upside but I think there's a couple of factors going for us. Number one is working capital has been a point of emphasis we saw. We had our senior leadership meeting kick off early in January and I can tell you that was one of the two major, major highlights that we talked about.

Number two, as Tom talked about the reduction in CapEx, and I think it's important to note we're not constraining CapEx. It's just that we have gone through a fairly substantial investment cycle, and we just see that waning a bit. But if we see great projects, we're going continue to invest. But nevertheless, we anticipate that CapEx number being lower this year and even potentially next year.

And then three is just being – we're looking at all these working capital levers and all the businesses have what I call pretty aggressive targets in terms of working capital. But then also last thing to add is we're still assessing a lot of these moving pieces when it comes to the new tax legislation, particularly as it relates to cash taxes because, as you know, we have kind of eight years to pay back that one-time fee. So, that's offset somewhat by the reductions. So, we still have some work to do in terms of the overall impact for the year and we're going to be working – Tom and his team are going to be working through all those details.

<Q - John G. Inch>: Got it. One last one, as inflation, Darius, comes back into the U.S. economy, how are you thinking about managing the company in terms of say pricing – the trade-off between pricing and cost, that sort of thing?

<A - Darius Adamczyk>: Yes. No. That's a good question because that can be a very dangerous phenomenon. I can tell you that every one of the SBGs and that's something that we already implemented last year is that they're really watching their inflation and the impact on their product costs, and I am very confident in saying that all of our businesses have a very good process to monitor the inflation of products and making sure that they're passing that through to the marketplace.

And frankly, the inflationary environment for raw goods is not new. It's really been in place last year as well, particularly in H2. So, we've been watching that more carefully and put the processes in to make sure that we monitor proactively.

<Q - Charles Stephen Tusa>: So, just to follow-up on John's question on cash flow just to be clear. You raised your net income guidance to reflect the tax rate, but you're basically not raising the cash number because of the uncertainties around this, the cash going out the door on the transition. Is that kind of how we should read the lack of guide on raise on free cash?

<A - Darius Adamczyk>: Well, I mean, our original guide that we gave you in December, Steve, it was under the provisos of the old law. And every year, we anticipate some cash benefit from the tax planning that we do and in fact, in 2017, we did realize some benefits there. So, it's not as if we had just put off the brakes on tax planning and the cash management around tax planning in that original guide.

When you look at 2018, there will be some benefit certainly on the U.S. side from that lower cash tax rate. But it's offset by the payment of the mandatory toll charge. And we need to continue to study the developments in the legislation before we step out and say it's going to be a huge impact. I mean, the guide range that we gave was fairly wide in any case from $5.2B to $5.9B. So, I think we're still comfortable at this early point sticking to that range.

<Q - Charles Stephen Tusa>: Okay. And then...

<A - Thomas A. Szlosek>: And Steve, as you know, we had substantial overseas cash and retained earnings. So, at least for the next eight years, that is going to be a bit of a cash drag because we got to pay for that onetime tax hit.

<Q - Charles Stephen Tusa>: Yes, okay. Just on the EPS guide, a little bit of a higher kind of operating base and you guys clearly beat ops this quarter. I think you tweaked up your margin assumptions, yet you are and I think share count is coming out a little bit lower than we expected exiting the year. You're only raising for the incremental tax benefits.

Is there something else that's kind of below the line, or anything else we have to be aware of? Anything you're concerned about that has slowed down as to why the raise didn't flow a little more through there or just building a little bit more contingency and hedge into the plan?

<A - Thomas A. Szlosek>: So, I think not a lot has changed since December. I mean, we actually expected a more robust fourth quarter as we said earlier from a top line perspective. And so overall, the momentum in each of the businesses is strong, and we expect that to continue, maybe there'll be some upside on the top line. But in terms of large things that we're concerned with that we haven't articulated, there's nothing of that sort here. Most of the assumptions we talked about in December are still intact.

<A - Darius Adamczyk>: Yes, and Steve, just to maybe to add onto it. First of all, as you know, 60% of our business is short-cycle vs. longer cycle, and we're in a new year so I think early on in the year, it's best to be prudent and just really, a little more on the caution side to really see how the business evolves. But having said that, I can tell you that I'm a lot more bullish on the year heading 2017 into 2018 vs. 2016 into 2017.

Now the comps are a little bit tougher, but nevertheless, as I look across the entire business portfolio, I can't think of a single business where I would view as a down arrow vs. 2017. So overall, things look good. But we have to see and see that the business materializes and comes through on the P&L. And I think kind of first quarter, we'll see how things go and after that, we'll be back to discuss it with you and see what adjustments we need to make for the year.

<Q - Charles Stephen Tusa>: Okay. One last one, in your March Investor Meeting, can you just maybe describe not what the targets are going to be, but are you going to give kind of a refreshed longer-term view financially? Just asking about kind of framework and format, how you guys are going to approach that?

<A - Darius Adamczyk>: Yes. I mean, I kind of felt like I did that last year, kind of the low- to mid-single digit 30BPS to 50BPS, that kind of range. I mean I think we'll probably, just to give you a little bit of preview, I think you should expect to see something in that similar range going forward. But yes, I mean, we'll give a refresh on that outlook. I don't know if it's going to be as precise as we're laying out every year because I think once you get out four, five years, I think it's a little bit more unknown. And if we go through a recession or something, you end of kind of not looking so smart. But I think the kind of framework that provided last year's margins should be your expectation for this year.

<Q - Steven Winoker>: Close enough, right? I've been called worst things. So Darius, maybe just talk a little bit about the key messages and the difference for managers [indiscernible] (43:02) leadership meeting that you just had. I know you mentioned cash. But just a little more on sort of how you're kind of trying to steer the ship and give folks priorities as they think about 2018.

<A - Darius Adamczyk>: Sure. Yes. No. Well, first of all, the key message was that I thanked for a really nice 2017. I think we had a very nice year across-the-board, and I think it was a good time to recognize the kind of outstanding efforts that the team contributed. So, that was sort of the first key message.

In terms of priorities for 2018, I'd say two or three-fold. Number one, working capital, I talked about that. We want to drive FCF. We want to drive FCF conversion. I just want to emphasize, too, that this is sort of where a very healthy and well-funded pension plan is actually hurting us from a cash flow conversion perspective and I always emphasize that because that somehow gets forgotten.

The second point is software and software not just in our Connected Enterprise, in our Connected – but really the incorporation of software into anything and everything we do. So, software in a sensor strategy for any and all products that Honeywell launches.

And the third one was much more about innovation, making sure that we leverage the latest and greatest technologies that are available in the marketplace today and making certain that those are reflected in our NPD pipelines and so on.

And then the last one is that we've kind of had a bit of – we have a different behaviors that we're trying to incorporate in the company and reemphasize leveraging and exhibiting those behaviors in everything we do. So, those were some of the key messages from our senior leadership meeting.

<Q - Steven Winoker>: All right. That's helpful. And then secondly, as you think about the kind of follow-on effects of tax reform for your customer base and their decision about how to spend that money and whether or not that kind of works its way back to your own growth rate and your own decisions even. I'm really seeing kind of mixed messages out there from corporate in terms of what they see in their own customer base kind of considering additional spending that's just sort of macro-related vs. maybe tax-related. I'm not sure it matters, but maybe a few thoughts on that potential for acceleration?

<A - Darius Adamczyk>: I think for us, undoubtedly, this is a very constructive outcome. I mean, we were supportive of tax reform. We're very pleased with what ended up happening. I think it's going to be good for U.S. business. For us, we certainly see a much greater level of bullishness on the part of our customers, which should translate to continued investment. And you're right, their CapEx is our revenue, and we do expect some level of investment to accelerate. Now, I think it's a little bit early. I think we sometimes forget that the details of this are still becoming clear – it's only 30 days old – and what the implications are for us.

I mean, for us, we've been bullishly investing in the U.S. already. I mean, if you think about our elevated CapEx that's been in place for the last two to three years, a lot of that investment went into manufacturing jobs, particularly in states like Louisiana and others. In addition, we're aggressively hiring a lot of software engineers, particularly in our Atlanta COE, and we're going to continue to do that. So we have and will continue to invest in the U.S.

Now, longer term as we assess further investments, does this make a U.S. more appealing place to invest? Absolutely. We think that this makes the U.S. a much more appealing place to invest. And as we contemplate further investment, U.S. will be near the top of the list.

<A - Thomas A. Szlosek>: Yes, just to add a little color on that, Steve. When you look at the momentum that we have in the U.S., I mean, overall, we closed the year about 3% organic growth or so in the region, but it was Q4 that was pushing close to double digits. So I think there was some anticipation of what was coming possibly and we'll see how that goes. I mean, so far so good at this early point in January as we look forward. But it's hard to make that direct connection between the benefits from the legislation, including the expensing of CapEx and our order rates. But we are looking for it, for sure.

<Q - Andrew Kaplowitz>: Darius or Tom, we know you have more difficult growth comparisons in Aero moving forward but you did 5% growth in Q4 and you averaged over 4% in H2. We've heard some more positive commentary on business jets that you guys have talked about, a potential turn towards the end of this year and next year. So, how do you look at the business at this point? Is the 1% to 3%, I'm sure there's some conservatism for the usual suspects like Space and maybe TS. But is the overall environment actually still getting better, would you say, in Aerospace?

<A - Darius Adamczyk>: Yes. I think as we discussed, we think the environment is still getting better. But I think what's also important to note is that we're coming off a much stronger year 2017 than a weaker year, which is 2016. So all in all, we're still very bullish. And I'm very excited about our prospects, more excited than going into 2017. But nevertheless, the baseline is a little bit different.

In terms of specific around your question on Aerospace, yes, I think the framework there on the business jets is similar to what we've been saying. We expect some level of acceleration but more likely in H2 2018, not early, particularly some of the new platforms are launching and deliveries taking place. So, I'd I say cautious optimism reflected in the growth rates but probably more later rather than sooner given the year.

<Q - Andrew Kaplowitz>: Appreciate that, Darius. And then you mentioned that you're seeing short-cycle growth in Process Solutions. In December, you suggested you really hadn't seen any evidence of bigger projects coming back, but you guys see the same thing that we do, tax reform and Brent oil prices being very high. Do you have any expectation that larger projects could begin to come back? Are you seeing any signs of them yet as we sit here today?

<A - Darius Adamczyk>: Yes. I mean I think, overall, our pipelines are very strong. I think you have to remember that our PMT backlog is up 10% on a y-over-y basis. And we had a positive orders growth in both UOP and HPS in Q4. But I would tell you also the pipeline and the project pipeline is strong.

And I think what's important in terms of the price of oil is sustainability, is that we don't like to see it as bouncing around. So, to the extent that it stays at this level, just right around, it's a very healthy environment for investment. So, as long as this is sustained, I'd become that much more bullish on our outlook in PMT, particularly UOP and HPS.

<Q - Scott Davis>: I asked this question with a couple of other corps, I haven't really gotten an answer that seems helpful yet, and I'll throw it at you guys. I mean, this new Tax Act thing seems to have somewhat made it simpler to do tax planning globally that maybe creates an opportunity for you guys to unwind some structures that were created in the past that whether it's supply chain related or otherwise. Is there a cost benefit at all from this simplification? I mean, you guys probably have like 700 different corporate entities or something crazy like that, right? So, is there any chance that you can unwind some of that stuff and just [indiscernible] (51:37)

<A - Darius Adamczyk>: That's some inside information now. Yes. No. I think, Scott, it's funny if you could see us in the room, I was actually smiling at Anne Madden because that's actually – I think your point is spot on. I mean, I think its underestimated today is that there is an opportunity to simplify a lot of our legal entities. That is an effort that actually we've already launched. Anne is leading that effort. But I also think that something that's underestimated is the level of complexity in this new tax structure in terms of vs. where we're going vs. where we are today. So, I applaud the new tax code, and we think it's extremely helpful for U.S. business. But it will require us to restructure ourselves and we do believe that new structural longer-term will be simplified, will cost us less, will make it a lot easier to do business. Can I quantify that for you right now? I can't because I mean we literally just started that work a couple of weeks ago. But I do anticipate it will be a source of value for Honeywell and our shareholders.

<Q - Scott Davis>: Okay. Good. That's the only good answer I've gotten so far, so thanks for that. I wanted to ask about business jets in the context of this Tax Act, too, and that you know, there's money coming back and seemingly it doesn't seem like anybody's bought a business jet in a while. I mean, you guys have always had really good forecasters, were known for a long time is being the best source for a business jet forecast. What are your guides saying? And if you commented on this earlier and I missed it, I went out for coffee, sorry. But what are your guys saying as far as the potential impact on guys having a few extra bucks sitting around and buying some planes?

<A - Darius Adamczyk>: Yes. I think probably the right answer is it's a little bit too early to tell because we'd like to see that reflected in kind of the order rates on the part of our business jet customers. But one would have to believe that this should have a positive impact on the overall demand. I think for now, we're kind of sticking to what we said before is that we anticipate some uptick in H2 this year and stronger environment in 2019. But like I said, I think it's just a little bit too early to tell, the real impact. The new tax code is 30 days old and difficult to project at this point the impact it has. But sort of logic would tell you that it should be an up arrow for us.

<A - Thomas A. Szlosek>: Yes, and I think the other thing we have going is the mandates and some of the software aftermarket offerings that we do on the business jet side. So, even though OEM might not be clicking away at double-digits, we certainly are getting new technology investments for existing platforms.

<Q - Gautam Khanna>: Two questions. First is I wanted to ask given tax reform, how does it change, if at all, the profile of the types of acquisitions you're looking at? Does it encourage you to go bigger? Does it do anything to the criteria that you've set out earlier?

<A - Darius Adamczyk>: I don't know if that dramatically changes it. I think given with our -maybe the only thing that's certainly very helpful for us is the ability to bring back some more cash to the U.S., it certainly makes U.S.-based acquisitions a bit easier to execute because now we have that more access to cash. But in terms of focus or – I think our financial metrics are set up such that the hurdles [indiscernible] (55:39) adjustment in the tax rates will be reflected in the financial metrics we look at. So, those would dramatically change the calculus, I'm not sure, other than we'll have more firepower in the U.S., which is important. It's important to have that kind of flexibility.

<A - Thomas A. Szlosek>: Yes, I would add to that though that we've not really been constrained in where we're looking. Our M&A team and the businesses haven't been saying well, let's not look in the U.S. because we don't have cash. We've always been able to accommodate that with our capital structure, and that will continue to be the case even more so now.

<Q - Gautam Khanna>: Okay. I appreciate that. And just one follow-up, Darius, how do you keep the potential – SpinCo is going to focus ahead of the spin? What kind of – just to make sure that everyone keeps their eye on the ball and doesn't get distracted as they move into the new world on their own.

<A - Darius Adamczyk>: Yes. So I mean, I think both through sort of our attention, we view these as our businesses before and after the spin. I mean, I think we want to make sure that these are incredibly successful. We have very focused management teams in both the spins businesses. They're doing a great job in running their businesses, but also getting ready for the spins. I'm very confident that the teams in those businesses are focused on delivering now and after the spins take place. So, I think there's also proper incentives that are aligned to the success before and after the spin as well, which we've taken care of and put in place.

<A - Thomas A. Szlosek>: Hey, Gautam, this is not an effort that's being done in some far-flung part of the company. The team, the SpinCo team, that's executing on the transactions actually reports into Darius and I directly. We do involve the businesses being spun but we want them focused, for the most part, on executing on their operating plans and that's the way we've structured it. The two objectives of the spin team are one, day one readiness for those organizations, and we have a very strong cadence and operating system around that in terms of systems, in terms of people and staffing and doing all the regulatory filings and so forth. So, that's very rigorous.

Secondly, it's stranded costs, and with 20% of the revenues from the RemainCo going with the spin, we need to right-size the company. And so, that SpinCo leadership team also is in the process of managing that cost structure. So, Darius and I get regular weekly visibility to it. We've put on some of the most senior people in Honeywell to do this, and we're encouraged by the progress we're making.

<A - Darius Adamczyk>: Yes. And I think just to add to it, I mean, we have a full-blown what do we call, de-integration team which is staffed by senior leaders whose full-time job is nothing but to focus on making certain that we have a successful spin in place and execute the business in the near-term. So, we have the right level of focus on this.

<Q - Peter J. Arment>: Darius, just a quick one, sticking in the Aerospace, obviously, the United Airlines selection I thought was certainly very favorable for you guys. But just kind of talking about the competitive landscape, we're months into this deal with one of your bigger competitors and certainly the headline reads that it would be more competition for you but at the same time it seems like there's going to be a lot of opportunity. What are your guys hearing in terms of your sense of post this merger that you'll see other opportunities for growth?

<A - Darius Adamczyk>: Yes. I mean, to be honest, Peter, we haven't been really focused on the merger of others. I think what we've really been focused on is executing our strategy. I continue to be extraordinarily excited about our vision for Connected Aircraft. I think it's industry-leading. It's reflected in our rates. It's certainly been a factor in the United win, and we're getting more and more traction every day. And I feel good because we have – if you think about the real estate and the scope on an aircraft, we have the avionics, and we have the mechanical systems and we have an integrated play and integrated offering. I think we have a very compelling vision for the kind of value we can create for aircraft owners, maintainers, passengers, pilots, create a more efficient, more safe experience for everybody. And that's not visionary. That's not a dream. That's something that we're executing, selling and generating revenue today and we feel that's a very unique place to be in, in the Aerospace industry. And frankly, we're the only ones that are executing it. I think probably our biggest opportunity or challenge at the same time is just being able to communicate that clearly and add value to end customers. But as you can tell by some of these wins, we're doing that more and more effectively.

<Q - Peter J. Arment>: Okay. That's helpful color. And just a quick one, Tom, just the sensitivity around for your defense business with the CR impacts, how do we think about that? Is there any near-term impact? Or what's the right way to think?

<A - Darius Adamczyk>: Well, thankfully, we got another reprieve, but it's kind of one of those things, it's more timing than anything else. There's a slight risk that volumes push out depending on shutdowns and so forth, but I don't think we are anticipating any significant adverse impacts from those activities.

<Q - Andrew Burris Obin>: Hey. Just a question, the focus on economy was all in the U.S. but European macro metrics actually looking better than the U.S. right now, so is China. Can you just talk about what you guys are seeing in Europe? And what you guys are seeing in China and other emerging markets? And specifically in China, if you're seeing any signs of deceleration, we've been getting a lot of questions from investors on that.

<A - Darius Adamczyk>: Yes. No. I mean, we're extremely bullish on China. It was an absolutely terrific year for us in China. I mean, I think close to a 30% organic growth rate in China last year. And could it be a slight downtick from that rate? Maybe. But we continued to see double-digit and planning on double-digit growth rate in China for us. So, we're bullish there.

<A - Thomas A. Szlosek>: And that was every...

<A - Darius Adamczyk>: Every business. Every business grew. And I think we really kind of figured out the calculus as to how to be successful in China, acting like a local company. Our whole value chain now is localized. And the great news and the one that I'm really excited about is we made similar progress in India. So, I think we're really firing on all cylinders in China and India.

Back to your Europe question, we're also bullish on Europe. I mean, Europe is continuing to grow. We're seeing growth in Western Europe, not seeing a lot of trouble spots here. So, as we head into this 2018, as I said, I'm continuing to be bullish on a global basis in terms of our prospects for growth. So, overall, strong environment.

<Q - Andrew Burris Obin>: And just a follow-up on your Aero 2018 outlook. You said on the call that none of your businesses are going to be negative but just sort this 1% to 3% growth does imply that perhaps Commercial OE is negative on wide-body deliveries. How should I think about sort of sub-segments within Aero?

<A - Darius Adamczyk>: Well, I think number one is the aftermarket in the services business are going to continue to be strong both through sort of what I call the proactive segment is always that great fix. Sort of we talked about the business jet OE which is – our plan is that acceleration as we get deeper into the year. And on the narrow-bodies, I mean, obviously, this is going to be really aggressive growth for our customers. So, that's sort of a rough framework that we're planning for in 2018.

<Q - Andrew Burris Obin>: So, none of that within your framework, none of the sub-segments are negative into 2018?

<A - Darius Adamczyk>: No. I mean, on the OE side, we'll continue with low-single digit kind of growth all-in is the plan. I mean, that could change quarter-to-quarter, and vary quarter-to-quarter based on customer delivery schedules. But I think we're planning on an overall Commercial OE growth rate in that range.

<Q - Andrew Burris Obin>: So, just similar level of conservatism across your guidance. Thanks.

Darius Adamczyk

Closing Remarks

We've begun 2018 with significant momentum, including strong order rates, a growing backlog and favorable U.S. tax legislation

We are excited by our prospects both in near term and long-term as Honeywell continue to outperform

I'm looking forward to speaking to you next at our Annual Investor Conference Day on February 19 here in Morris Plains.