Company Name: Honeywell
Company Ticker: HON US
Date: 2019-02-01
Event Description: Q4 2018 Earnings Call

Market Cap: 109,703.32
Current PX: 148.19
YTD Change($): +16.07
YTD Change(%): +12.163

Bloomberg Estimates - EPS
Current Quarter: 1.826
Current Year: 7.937
Bloomberg Estimates - Sales
Current Quarter: 8820.167
Current Year: 36910.800

Q4 2018 Earnings Call

Company Participants

- Mark Macaluso
- Darius Adamczyk
- Greg Lewis

Other Participants

- Peter J. Arment
- Sheila Kahyaoglu
- John G. Inch
- Gautam Khanna
- Julian Mitchell
- Charles Stephen Tusa
- Jeffrey Todd Sprague
- Scott Reed Davis
- Andrew Burris Obin
- Joseph Ritchie
- Christopher Glynn

MANAGEMENT DISCUSSION SECTION

Mark Macaluso

Non-GAAP Financial Measures

Adjusted EPS and FCF

- This call and webcast, including any non-GAAP reconciliations, are available on our website at www.Honeywell.com/investor
- For this call, references to adjusted EPS, adjusted FCF and FCF conversion and effective tax rate exclude the impact from separation costs related to the two spin-offs of our Homes and Transportation Systems businesses as well as pension mark-to-market adjustments and U.S. tax legislation, except where otherwise noted in 2018
- With regards to 2019, references to adjusted FCF guidance and associated conversion on this call exclude impacts from separation cost payments related to the spin-off

Darius Adamczyk

Business Highlights

Performance

- Let's begin on slide 2

- We're extremely pleased with our results in 2018
- We made progress both from a portfolio and financial perspective, continued smart investments in our businesses and our people and took steps to position the company for next 20 years
- This quarter, we successfully completed our second spin-off of the year, Resideo Technologies, launching our New York Stock Exchange in October
- We also continued to advance our software strategy while growing our core businesses in attractive end-markets
- And most importantly, consistent with what we've done all year, Honeywell delivered on its commitments to our shareowners

Adjusted EPS, Organic Sales and Margin

- We met or exceeded our financial commitments on all metrics, delivering adjusted EPS of $1.91 in Q4, driven by 6% organic sales growth and 80BPS of segment margin expansion
- We continued to see strength in our long-cycle businesses, most notably in commercial aerospace, defense and warehouse automation, where our Intelligrated business is a global leader
- Furthermore, we're aggressively planning and mitigating the impacts of the tariffs' dispute in all of our businesses, as evidenced by the strong margin expansion we generated this quarter
- Based on what we know of today, we do not expect any material impact to our results in 2019 related to tariffs

FCF and CapEx

- For the full year, we achieved 100% FCF conversion and 105% conversion in Q4
- We generated over $6B of FCF for the year, excluding spin cost payments up 22%, even after spending nearly 20% of the company in Q4
  - This was principally driven by profitable growth, higher net income and continued efforts to free up working capital, all the while funding smart growth investments through $800mm of CapEx
- Our FCF, as a percent of sales, is the highest it's been in at least 15 years and we expect it will continue to grow from here
- Importantly, our U.S. pension is funded at over 105% and we do not expect any cash contributions in near term
- The financial health of this company heading into 2019 is as strong as it's ever been and we still have ample resources to deploy

Capital Deployment

- Lastly, we continued a steady cadence of capital deployment for an additional $1.7B of Honeywell share repurchases in the quarter, bringing the full-year total to approximately $4B
- As a result, I now expect the fully diluted share count to be down at least 3% in 2019 based on our plan to reduce share count by at least 1% from 2018, as we continue to return cash to our shareowners through $2.3B in dividend, following another double-digit dividend increase in 2018
  - This was a particularly good year for Honeywell

- We have a simpler, more focused portfolio after the spins and continue to execute on our initiatives as we look to the future
- We see strength across several end-markets and have significant balance sheet capacity to deploy
- And while we are not planning for a recession in 2019, we are taking steps now to ensure we build on our commitments in an uncertain economic environment

Organic Growth and Portfolio Optimization

- Let's turn to slide 3 to review some of the progress from last year
- As I mentioned, we took significant steps through 2018 to transform the business
- One of my key priorities from the outset was to accelerate organic growth
- As you've seen by our results, we're making good progress on this front
- We are encouraged by the fact that nearly 60% of the portfolio grew just 5% or more organically for the full year of 2018 with several businesses growing above 10%
- With the spin-offs complete, we now operate a more focused portfolio on a smaller number of attractive end-markets
- Portfolio optimization is central and will continue to be part of Honeywell's operating system

Dividends and Share Repurchases

- We plan to continue effectively deploying capital by funding high-return CapEx and returning capital to shareholders through dividends and share repurchases
- We have had nine consecutive double-digit dividend increases since 2010 and still have a strong and flexible balance sheet with the ability to deploy over $14B of cash to M&A, CapEx, dividends and share repurchases
- A combination of strong sales growth, favorable end-market exposure and significant balance sheet capacity positions us well as we head into 2019

Key Transformation Initiatives

- We are now on slide 4
- As I mentioned, continuous transformation is part of Honeywell's operating system
- On this slide, we highlight three key transformation initiatives to establish Honeywell as a premier technology company for the future

HCE

- Earlier this year, we established Honeywell Connected Enterprise, or HCE, which is a strengthened and centralized organization that will serve as the software innovation engine for all of Honeywell
- HCE operates through its speed and agility of a start-up, working closely with our businesses and our customers across the entire portfolio to build the world's best software solutions rapidly and efficiently on a single platform
- Our transformation to a premier technology company require us to look beyond just spin-offs

- Our Chief Supply Chain Officer, Torsten Pilz, is leading Honeywell's efforts to improve our supply chain and optimize our global footprint

Margin Expansion and Operational Efficiency

- We see a lot of opportunity here to drive margin expansion and operational efficiency and you'll hear much more about this from Torsten at our Annual Investor Conference in May
- We are making similar enhancements on our capabilities internally with Honeywell's digital initiative
  - This requires people, process, data and technology elements to come together, which will allow for more effective and efficient decision-making throughout Honeywell
  - This effort includes a continuation of our progress through centralized ERP systems

ERP Applications

- Thus far, we have eliminated 35 unique systems in 2018, going from 106 to 71 and we are on path to just 10 ERP applications by the end of 2020
- The result will be consistent processes and centralized data governance of a common IT foundation
- As you can see, we have achieved a lot this year and continue to redefine the limits on what Honeywell can achieve to be the best positioned multi-industrial company for the future

Key Priorities

- Let's turn to slide 5 to briefly review progress against our key priorities
- I laid out my key priorities for the company in 2017
- Since then, we've continued to foster a culture within Honeywell of doing what we say or as we call it the say/do ratio

Organic Sales Growth and FCF

- As you stack the results against our long-term commitments, you can see we are clearly making progress and, in some instances, achieving milestones sooner than we thought such as with our organic sales growth and FCF conversion
- We are accomplishing these objectives while making smart investments for future through CapEx, restructuring and research and development

Investments

- Our software businesses grew in the mid-teens range last year on a path to the 20% long-term compound annual growth rate we anticipate
- We have taken steps to unify and strengthen our software strategy through the Honeywell Connected Enterprise and continue to invest in software development, sales and marketing capabilities and build-out of the Sentience platform

- In 2018, Honeywell Ventures made five investments, including in Soft Robotics, a developer of automation solutions and soft robotic gripping systems that can grasp and manipulate items with same dexterity of the human hand, and in ioTium, a managed secure network infrastructure platform for an Industrial Internet of Things that primarily serves building technologies and industrial customers

Bolt-on Acquisitions

- We also completed two bolt-on acquisitions totaling roughly $500mm
- Ortloff Engineers is a privately held licensor and industry leading developer of specialized technologies that drive high returns in natural gas processing and sulfur recovery
- This complements our existing UOP offering, which allows us to better meet customer needs for high recovery, non-gas liquid extraction plants globally
- Transnorm, now part of Safety and Productivity Solutions, is a global leader in high-performance conveyor solutions that are used in diverse end-markets such as parcel delivery, e-commerce fulfillment and airports
- The acquisition strengthens Honeywell's warehouse automation portfolio and positions the company to support the growing European e-commerce market while broadening Honeywell's Connected Distribution Center and aftermarket offerings

Greg Lewis

Financial Highlights

Organic Sales, Segment Profit and Margin

- Let me begin on slide 6
- As Darius mentioned, we finished 2018 very strong in every financial metric
- Organic sales growth for Q4 was 6%
- We have been at or above 5% every quarter this year
- This reflects our continued commitment to customer excellence, new product development as well as our realization of benefits from the investments we've made in our sales organization and new product development process
- We generated approximately $2B of segment profit in Q4, driven principally by higher sales volumes with segment margin expansion of 80BPS
- The impact from the spin-offs of lower-margin businesses, net of acquisitions, contributed 30BPS, while the core business generated 50BPS expansion

Pricing, Productivity and Adjusted EPS

- Pricing and productivity was strong, which enabled us to effectively mitigate the impact of material and labor inflation
- We also saw continued benefits from previously funded restructuring
- Adjusted EPS was $1.91, up 12% vs. prior year excluding the spins, which exceeded the high-end of our guidance range by $0.01

- The adjusted EPS figure excludes both the impact of an approximate $435mm favorable adjustment to Q4 2017 tax charge and $104mm in spin-related separation costs

Separation Cost, Share Buybacks and Working Capital

- At the outlook call in 2018, we estimated a separation cost for the two transactions would be in the range of $800mm to $1.2B
- I'm very pleased to report that the total separation cost for both spins came in lower than this estimate at $730mm, which demonstrates our ability to effectively execute complex transactions both ahead of schedule and below budget
- We also recorded $300mm in repositioning charges in the quarter to fund future productivity and stranded cost reductions
- Share buybacks totaled $4B in 2018 and drove $0.06 benefit from lower share count in the quarter
- You can find a bridge to Q4 adjusted EPS in the appendix of this presentation
- Finally, working capital improved 0.6 turns y-over-y
- Our businesses are all focused on improving working capital and we continue to see progress on our initiatives with room to free up more cash for capital deployment

Segment Results

Aerospace Business

- Now, turn to slide 7 and review our segment results
- Our Aerospace business continued to perform extremely well in a robust demand environment, capping off a strong year of near double-digit organic sales growth
- In Q4, we generated 17% organic growth in defense and space with double-digit growth in both the U.S. and international businesses, led by global demand for sensors and guidance systems, original equipment shipment volumes and higher spares volumes on U.S. Department of Defense programs
- We also saw growth in our space business, driven by new satellite program wins and commercial helicopters, driven by repair and overhaul demand

Commercial OE and Aftermarket Growth

- In commercial OE, sales were up 8% organically with increased HTS engine demand for Gulfstream and Textron Longitude platforms and higher aviation shipset volumes driven primarily by the certification of the Gulfstream G600
- Aftermarket growth was strong in all businesses, including defense, driven by increased demand for avionics upgrades, both software and hardware, navigation products and safety mandates
- Our Connected Aircraft offerings continued to gain traction, driven by GoDirect Cabin tail capture and robust JetWave demand

Honeywell Building Technologies

Organic Sales Growth and Projects Backlog

- Turning to Honeywell Building Technologies, organic sales growth was 1%, driven by continued demand for commercial fire products in North America, Europe and our high-growth regions
- Building Solutions' projects growth was also strong, particularly for international airports
- The HPS projects backlog is up 15%, setting up a strong 2019 as we continue to expand in critical infrastructure markets like airports, cities and stadiums
    - These gains were offset by declines in our China air and water business and temporary supply chain challenges within our Building Management Systems business

New Product Introductions

- We expect the air and water business to recover in 2019, driven by new product introductions for the mid-segment and stronger demand as inventory net levels normalize after a challenging 2018
- In December, the supply chain issues within Building Management Systems began to stabilize and we expect continued improvement in H1 2019
- HBT also benefited from one month of single-digit organic sales growth from the former Homes business, driven by strength in both products and ADI Global Distribution
- As a reminder, the results for HBT exclude Homes and Distribution after October

Performance Materials and Technologies

- In Performance Materials and Technologies, sales were flat on an organic basis
- Sales in UOP were up 2%, driven by ongoing strength in licensing and engineering sales, but were offset by an expected decline in gas processing, which was driven by an extremely strong fourth quarter in 2017

Process Solutions' Sales

- Process Solutions' sales were up 1% organically, driven primarily by a strong demand in our software, maintenance and migration services and field devices
- This was offset by declines in large project activity and in smart energy and thermal solutions both shorter-cycle businesses due to supply chain challenges
- Notably, we continue to see solid trends within the automation businesses of Process Solutions with total orders up double digits and short-cycle backlog up over 30%, suggesting that oil price volatility in Q4 may have temporarily delayed customer investment decisions

Advanced Materials' Sales

- Advanced Materials' sales were down 3% on an organic basis as continued strong demand and adoption of our Solstice line of low global warming refrigerants, which was up 5%, was offset by declines in specialty products, particularly in our electronic materials business, which is in the semiconductor space as you know and tough comps associated to Q4 2017
- PMT segment margins expanded 200BPS in Q4 as expected, driven by the timing of catalyst shipments within UOP, commercial excellence and the benefits from previously funded repositioning

Safety and Productivity Solutions Business

Organic Growth

- Now, turning to the Safety and Productivity Solutions business, that continued to perform at a high level with organic sales up 15%, driven by broad-based strength across all lines of business
- Double-digit organic growth in Intelligrated continued as orders for major systems and robust backlog conversion fueled by e-commerce drove strong results
- We also saw double-digit growth in our sensing business and continued strength in our productivity products business, driven by demand for Android-based mobility offerings and handheld printing devices
- In total, organic growth in our Productivity Solutions segment business was up 23%

Safety

- Moving to Safety, the Safety business sales grew 5% organically, led by ongoing demand for gas products and strong growth in retail footwear associated with the holiday season
- Finally, we continue to see strength in our businesses across high-growth regions

China, India and Middle East

- In China, SPS grew double digits with robust growth across industrial safety, productivity products and SIoT.
- Excluding the ongoing softness in air and water, HBT also grew double digits in China
- For all of Honeywell, China was up 9% organically for the full year
- In India, our capabilities and strength provided exceptional growth in Q4, greater than 25% over prior year
  - This was driven by our Building and Process Solutions businesses
- We continue to see positive macroeconomic trends in the Middle East with supported growth across all businesses with three segments growing double digits organically compared to the prior quarter

2019 Outlook

Now, with 2018 in the rearview mirror, let's move to slide 8 and discuss our 2019 outlook

We have a reliable playbook at Honeywell and it's not changing for 2019

Our focus on smart growth investments, breakthrough initiatives and new product development, coupled with productivity rigor and the benefits of funded repositioning, has positioned us well for continued outperformance

Organic Sales Growth and Segment Margin Expansion

- For 2019, we anticipate an organic sales growth range of 2% to 5%, the low-end of which reflects the possibility of some economic slowing, but not a recession in 2019
- Segment margin expansion is expected to be 110BPS to 140BPS or 30BPS to 60BPS excluding the impact of the spin-offs
  - This will drive EPS growth of 6% to 10%, excluding dilution from the spins in 2018

Adjusted FCF, Orders and Backlog

- We expect to generate adjusted FCF conversion near 100%, consistent with 2018, driven by high-quality income growth and continued working capital improvements across the portfolio
- We're confident of our businesses in the year ahead, supported by positive long-cycle orders and backlog trends exiting 2018
- We have put forth a strong plan with multiple cost levers to pull in the event the recent volatility and the macro-environment persists

Tariffs

- As Darius mentioned in his opening, we don't expect a significant impact in 2019 related to tariffs
- We have worked very hard to mitigate that across the year for 2019, including addressing the potential impact of the still unannounced List 4, which contemplates 25% tariff on all remaining items imported from China
- We will continue to monitor this throughout the year and react accordingly as we did in 2018
- Some other items to take note of related to our 2019 plan, we are on-track to slightly ahead of our plan to eliminate all stranded costs in 2019 related to the spin-offs with a little over half the cost removed to-date
    - We see the impact of these costs primarily in the net corporate cost line and in the segment margin in Honeywell Building Technologies

Pension Income and Share Repurchase

- Also, based on the planned reduction in pension income, driven by discount rates and assumed asset returns as well as lower repositioning and other charges, driven by the spin indemnity, our total net below-the-line charges are expected to be approximately $80mm in 2019
- We will see continued benefits from planned and executed share repurchases
- Our 2019 plan assumes a weighted average share count reduction of about 3% year-on-year or 730mm shares
    - This is based on the 2% share count reduction we executed from 2018 repurchases and at least 1% additional reduction in 2019

Organic Growth and Revenues

- You will find additional details on our 2019 planned inputs in the appendix
- Based on what we can see today, we expect to be at the upper-end of our sales guidance range for organic growth
- However, given the many uncertainties in the macro signals, we are planning cautiously in 2019 overall as it's difficult to predict short-cycle revenues, particularly in H2 and remember that is still approximately 60% of our business

End-Markets

- Let's turn to page 9
- We provided initial assessment of our end-markets and anticipated organic growth rates in each for 2019

- The green arrows are an indication that we expect market conditions to improve, while the gray flat arrows indicate that we expect market conditions to remain relatively similar to last year

Aerospace

- Starting with Aerospace, we expect organic sales to be up strong mid-single digits for the year
- We continue to see a robust demand environment in both commercial aerospace and defense
- In air transport, we expect continued growth in narrow-body production rates
- We forecast new business jet deliveries to increase 8% to 10% in 2019, supported by several new aircraft models entering into service, a decline in young used aircraft inventories and stable used jet prices
- Our long-term strategy of securing good positions on the right platforms and building our installed base will serve us well in 2019, particularly with new business jet platforms where we are well positioned from an OE standpoint
- Mid-single-digit flight hours growth will continue to drive aftermarket demand and we expect further tailwind from the ADS-B compliance mandate deadline, along with increased demand for connected aircraft solutions across all products
- The industry dynamics in defense will be positive in the U.S. and internationally, driven by budget growth, but we are planning conservatively for 2019, given the tough y-over-y comparisons following 2018's banner year, where we grew 15% organically in the business
  - With the favorable margin rate uplift from the former Transportation Systems' spin, you should expect segment margins of approximately 24% for the Aero business going forward

HBT

- Now, on to HBT, as a reminder, following the spin of our Homes portfolio, HBT's primary exposure is to non-residential construction
- Here, we anticipate low single-digit organic sales growth after a challenging 2018, driven by better execution in our operations, better selling strategies and sales coverage and new product introductions
- We expect commercial fire will continue to be strong with the expansion of sales coverage and share gain and commercial security to improve with the expansion of our channel partner network
  - The declines we experienced in our China-based air and water business should subside through a combination of stronger market demand and new product introductions for the mid-segment and mass mid-segment

Building Management Solutions

- Globally, we see building management solutions' growth in both hardware and software, driven by high-growth regions' expansion and our investments in software
- Honeywell Building Solutions growth will be driven by government investments in smart cities, social infrastructure and airport modernization and capacity enhancement, particularly in high-growth regions
- We also expect continued adoption of connected building solutions on a global basis
- You should expect to see margins in the range of about 20.5% in HBT after the spin-off of Homes

PMT

- For PMT, sales are expected to be up low single digits-plus on an organic basis
- In oil and gas, petrochemical market growth should remain steady at about 4%, driven by demand for packaging and plastics
- However, given the volatility in oil prices in H2 2018, investments in global megaprojects slowed and we see the oil price volatility potentially putting some pressure on upstream spending plans in 2019
- Nevertheless, we anticipate similar market dynamics overall to 2018
- And the basis for our plan is that oil prices remain in the low to mid-60s per barrel

Refining Market

- The refining market should continue to be strong as global demand for cleaner transportation fuels remains
- The U.S. natural gas market, which is primarily served by our UOP Russell business, is expected to improve from 2018
- UOP is expected to deliver a strong year, driven by its strong backlog, licensing and services growth and improved market demand in gas processing after a tough 2018
- Process Solutions will continue to grow across its short-cycle businesses, as we saw in 2018
  - This is supported by short-cycle, backlog which was up over 30% at the year-end

Advanced Materials and SPS

- Finally, within Advanced Materials, we expect continued growth from Solstice and our Fluorine Products business and better execution in specialty products
- Lastly, in SPS, sales are expected to be up in the mid-single-digit range
- We expect the strong e-commerce and warehouse distribution macro trends to continue as our customers seek and implement differentiated warehouse solutions to deal with rising demand
- Our orders in Intelligrated in 2018 were up over 30% for the year

Safety Business

- In the Safety business, we anticipate growth will be driven by new product introductions within gas detection, growth in our core product lines and high risk personal protective equipment and new product launches in general safety
- In productivity, we expect strong growth, driven by backlog conversion in Intelligrated and our sensing business, new mobility product introductions and expanded software offerings
- We are also seeing growth in our lifecycle service offerings in Intelligrated, which includes maintenance, technical support and optimization services
  - That is combined with the aftermarket capabilities we acquired with Transnorm

Adjusted EPS

- Now, let's move on to slide 10
- Here, you can see the bridge of our 2018 adjusted EPS to 2019
- The spin impact, which we define as the after-tax segment profit contribution from the spins in 2018, 9 months of Transportation Systems and 10 months of Homes, net of the estimated impact of the spin indemnity assuming that it was in place all year for 2018, will be $0.62 headwind to earnings in 2019
- As you can see, the majority of our earnings improvement, $0.30 to $0.60 per share, will again come from operational gains in our businesses, driven by profitable growth, continued productivity improvements and incremental benefits from previously-funded restructuring
- You can see the remaining impacts from the share count, below-the-line items and tax rate I have already touched on will contribute approximately $0.11 per share

Q1 Guidance

Organic Sales Growth

- Now, let's move to slide 11 to discuss our first quarter guidance
- For Q1, we expect to generate 3% to 5% organic sales growth, driven principally by healthy growth in our long-cycle businesses, with a more cautious tone towards short-cycle, given the market volatility exiting 2018
- With that said, we do anticipate that the commercial aftermarket, our sensing business and productivity products and commercial fire products will continue to be strong on the short-cycle side

Segment Margins, Adjusted EPS, Tax Rate and Share Count

- We expect segment margins will expand 30 to 60BPS ex the spins, consistent with our long-term framework and 110 to 140BPS on a reported basis, aided by 80BPS of margin accretion from the absence of the two spins
- Our expected adjusted EPS range of $1.80 to $1.85 represents growth of 6% to 9% ex-spins
- We have $0.25 of earnings dilution from the spins in Q1 2018
- Our guide is based on an effective tax rate of 22% and a weighted average share count of 737mm shares for the quarter
- We feel this will be a very strong start to another successful year for Honeywell in 2019

Darius Adamczyk

Closing Remarks

We accomplished a lot in 2018 and expect great things in 2019 as well

We delivered on all our commitments, successfully completed spin-offs ahead of schedule and under budget, while still overdriving on the organic growth, margin expansion, EPS and FCF targets that we established at the end of 2017

There's significant room for continued margin expansion on the path to our long-term target of 23%

- This is aided by over $450mm of [ph] repositioning fund (30:11) in 2018 and in prior years, which will drive improvements to our cost structure, supply chain and gross margin in 2019 and beyond

Our balance sheet capacity is strong and this will provide another lever to drive outperformance in any macro environment

We're continuing the business transformation through several new initiatives, including Honeywell Digital, a unified software business in Honeywell Connected Enterprise and the increased focus on our supply chain

We are excited about 2019 and expect another great year

QUESTION AND ANSWER SECTION

<Q - Peter J. Arment>: Nice way to finish up 2018. Darius, I guess on the Aerospace, just really the momentum continues to be really impressive with organic growth of 10% in each of the past two quarters. Maybe you could talk about, I guess, the sustainability or the confidence around the bizjet volume for you. I know you mentioned 8% to 10% for this year. And on the 2019 Aerospace guidance of mid-single-digit plus, is the defense tough comp really the only headwind you're seeing in 2019? Maybe just some color there. Thanks.

<A - Darius Adamczyk>: Yeah. I mean – so, first of all, we're very confident about our Aero outlook for 2019. Our bookings have been strong. January has been strong. Yeah, the comps do get tougher and there's some short-cycle. And I think, as people saw on our outlook for Q1 and what I anticipate will be Q2, we have every bit of confidence that mid-single digit is hopefully the bottom.

But the fact is we don't know H2 and that's why the numbers are what they are. And potential government shutdowns and budgetary challenges and trade licenses potentially becoming an issue, we hope that doesn't happen, that just reflects sort of external risk. But overall, there's absolutely nothing that I'm concerned about in terms of the bookings, the growth rates, the kind of growth we're seeing in that business. And it's pervasive across all three segments, whether air transport, BGA or defense and space. So, I'm very pleased and it's not a place where I am going to be losing a lot of sleep in 2019.

<Q - Sheila Kahyaoglu>: Across your four businesses, you either have a deceleration in organic growth or flattening of sales growth. Just where are you factoring in some conservatism with a slowdown and how are you capturing that low-end of the sales growth guidance of 2%?

<A - Darius Adamczyk>: Yeah. I think it's not so much that we're capturing any conservatism in any of our businesses. I think what we have in our guidance going forward is the fact that more than 50% of our business is short-cycle. And what's different about this year than I think many years in the past is we have many more unknowns, whether it's Brexit, whether it's trade negotiations specific to China-U.S., whether it's Fed hikes in terms of what happens, whether it's government shutdowns, so just a lot of geopolitical unknowns, more than usual.

And for us to express a level of confidence around all these unknowns, around a little bit wider range than we anticipated, I think would probably indicate a level of knowledge that we currently don't have.

Now, having said that and as you can see in our Q1 outlook, we're actually front-end loaded. And if anything, we are going to be at the upper half of our revenue growth range in H1. So, actually, provided all things go as we think they will to the positive side, I think that hopefully we'll be raising the bottom of that range as we move further through the year.

But I don't see really any growth issues in any of our businesses and we expect all of them to grow in 2019.

<Q - John G. Inch>: So, how did your European business do and what's actually baked, I guess, on a growth rate? Any color there. And what's baked into your guidance for 2019 for Europe?

<A - Greg Lewis>: Yeah. John, Europe continued to be strong. In Q4, our European businesses were up 6%, which capped off a 4% organic growth for the year. So, I still think we're seeing good strong growth there. And it's pretty broad-based to be honest. SPS, probably the strongest of the bunch, but each of the businesses is growing in the mid-single digits or higher in Europe at this stage.

And as we look forward, we expect that's probably going to be still low-to-mid single digits, but as Darius mentioned, clearly, there are concerns out there. I mean Brexit in particular will have some sort of an answer in the next 60 days as to what occurs with that. And we've got a meaningful size business in the UK. So, definitely back to the concern aspects of macro signals, Europe is an area where we are waiting to see what's going to happen with Brexit in particular and what impact that may have on us.

<Q - John G. Inch>: But, Greg, that performance of 6%, that's pretty good relative to what other companies have been putting up in Europe and given sort of the slowing in Germany and stuff. Is there a mix issue that's benefiting Honeywell or new products or what do you think is attributable to why you're doing...

[indiscernible] (36:46)

<A - Greg Lewis>: Well, again, I would tell you that each – yeah, each of the businesses is performing well. So, it's not like one is – I mean SPS being the strongest of the bunch, but each of them is up mid-single digits for the year. So, it's strength across our entire portfolio.

<Q - John G. Inch>: And then, as a follow-up, last year, you guys put up the 3% to 5% core growth target. And, Darius, you flagged accelerating core growth as your number one priority. Now, I understand the economic sensitivity is around the 2% to 5% this year. But I'm just trying to think big picture what are you and how are you actually going to tackle driving Honeywell toward more of a mid-single-digit type of accelerating core growth over time? Is that meaning to go after like in, that pie the 40% that's not growing at 5% plus or do you kick start building technologies, which has been sort of a problem for a little while or more M&A? I mean, maybe just walk us a little bit of your own thoughts and maybe horizon too.

<A - Darius Adamczyk>: Yeah. Well – yeah, John, it's not any one thing. It's probably all of those.

<Q - John G. Inch>: Yeah.

<A - Darius Adamczyk>: I mean it starts with portfolio and we think that [ph] basis (37:57) upon what we've done here, we've got a more growth oriented and less cyclical portfolio. That's certainly part of it. Secondly, which is our tremendous focus on Velocity Product Development and we're launching a whole new process called [ph] Z21 (38:13), which basically is going to reduce our innovation cycle times in half, deploying more capital to R&D, because my strong belief is that part of any growth story has got to be a strong innovation engine. And that's something that we are trying to create.

Continued focus on high-growth regions, I mean we are winning in places like China and India. And even though the back half of the year, China was a little bit slower, we grew nearly double-digit in China this year. So, that continues to be a success story. Our focus on commercial excellence of our sales force is working, where we're getting better productivity out of our sales force, better performance. It's never only one thing. We're working all those levers.

And as you can see in the growth rate that we've demonstrated – granted, the markets are pretty good, but certainly without the self-help that we've administered over last couple years, there's no way we would be in that range both in 2018 and what we're projecting for 2019.

<Q - John G. Inch>: Just last, India has been a real success story. I think you flagged it again. Would you consider putting more resources or doing M&A in India in particular, a reason why is, it's much smaller than China, but it does seem to have gained a lot of traction for Honeywell. I'm just wondering what are you thinking about it.

<A - Darius Adamczyk>: Yes. No. We had lot of focus on India. I mean to give you a perspective for India, our growth in India in Q4 was 27%. So, that's tremendous. We have a big footprint there, not just from a business perspective, we have our engineering centers there of over 10,000 people. So, we feel very comfortable of our presence there. The opportunity is now to go after the mass mid-market segment and that's actually one of our core initiatives for 2019 and beyond is just not to play in the top tier, the mid-tier, but actually having a greater level of participation in mid-market segments. So, India is definitely one of the economies, which we think is going to be a great story for us in 2019 and beyond.

<Q - Gautam Khanna>: Two questions. First, just big picture M&A pipeline, what can you say about it? Is it as healthy as it's ever been or anything large that you guys are looking at? Just any commentary on the nature of the pipeline right now.

<A - Darius Adamczyk>: Yeah. I would say, large, probably not because I think that we're still very much focused on bolt-ons and not the mega deals. So, I would say that is and will continue to be our focus. We got a deal done in Q4, which was good. Transnorm was a deal of size, the kind of size we like, [ph] deployed about $0.5B of capital (41:14) to do that.

But to be honest, on my commentary, the pipeline continues to be good and we were working on a deal that recently fell through just because although there's been a little bit of a correction in the market as we saw particularly in December, that didn't really change the expectations of [indiscernible] (41:30) seller.

So, we continue to struggle valuations and the expectations, which there is a very pronounced shift up. And it's got to work in our financial model. So, we continue to be very active. The pipeline is good, but I also want to tell you that we're realistic, because we are conscious buyers and we don't like to overpay. So, we have to be certain about what we are buying and make sure that generates the right level of returns for our shareowners.

<Q - Gautam Khanna>: Appreciate it. And second question was just, if there are any supply constraints you're seeing on the Aerospace side, I remember, last year, you had some aftermarket constraints, are you seeing any pinch points emerge?

<A - Darius Adamczyk>: Yeah. No. The answer to that is yes and I would say that there is some pinch points in the supply chain emerging not just in Aerospace. Those are there and prevalent particularly in the areas like casting, et cetera. But we see similar challenge in smart energy and even in some elements of electronic supply chain. So, the pinch points on the supply chain are real. They are there. We're working through those and hope to resolve those. Frankly speaking, our results could have been even better had some of those pinch points not been there.

<Q - Julian Mitchell>: Maybe just the first question around SPS, you grew around 10% plus organically in 2018. Your slide 9 shows about mid-single-digit growth this year amidst the sort of accelerating market arrow. So, is that guidance based on anything you're seeing in the short-cycle businesses within SPS or it's simply about tough comps and the usual macro aspects that you had mentioned earlier?

<A - Greg Lewis>: Yeah. Thanks, Julian. I think it's a little bit of both. I mean, obviously, we continued to be very excited about Intelligrated and the double-digit growth rates that we achieved this year and, with a very strong backlog, expect that to continue to be strong. We did – our retail business, though not large, grew over 20% in 2018. So, that's probably going to dampen a bit with some of those comps. We still feel very positive about productivity products and Sensing and IoT with the new product introductions that they have, but those and the industrial safety businesses, they are short-cycle.

So – and when those things change, they can change quickly. And so, I think that's where we're trying to be a bit cautious, because we've seen it happen before in terms of the speed at which the short-cycle can turn on us. And so, it's not a matter of having seen it so far and being concerned about anything with our business specifically, but I would just call it a bit more caution with the environment we are in.

<Q - Julian Mitchell>: Thanks.

<A - Darius Adamczyk>: Yeah. Just to add, Julian, like Greg said, I mean majority of that business is actually short-cycle. Intelligrated is about the only business that isn't short-cycle. So, based on what we're seeing now and today and our guides for Q1, there's no warning signs for us here. Where we're positioned is just uncertainty particularly around H2.

<Q - Julian Mitchell>: Thanks. And then, my second question around PMT, any more color you'd like to provide on how you see the cadence of the large project activity within HPS in terms of the scale of any delays? And also, UOP, how are you gauging volatility there at the moment?

<A - Darius Adamczyk>: Yeah. And I like the greater stability. What we saw in Q4 a little bit was a bit of a pause on the order rates just around the volatility of oil, but kind of given the right direction movement, we are much more bullish, but despite that, I just want to quote you a couple numbers from Q4 and why I'm bullish on PMT for this year. First of all, our HPS order rates were up double digit, second of all, our UOP backlog is up 8%. So, I'm very optimistic around PMT performance for 2019.

Probably the one segment that was pretty soft was in our Advanced Materials business, the Electronic Chemicals, which electronics has been a bit weaker, some of the other companies in that segment announcing and we saw that in our Electronic Chemicals business. So, that's probably the only sort of minus that we saw in Q4, but overall, both the backlog, the order rates were good. And to be honest, especially in HPS, our global megaprojects [ph] backlog and quote (46:44) are really strong. We even booked a lot of those orders in Q4 and our orders growth was up double digit in the quarter. So, I feel pretty good about PMT for 2019.

<Q - Charles Stephen Tusa>: Just wanted to ask about...

<A - Darius Adamczyk>: [indiscernible] (47:20).

<Q - Charles Stephen Tusa>: We're not sensitive or anything like that. You mentioned kind of the next phase of the transformation and some of the footprint stuff that you're looking into. Is that something that you'll be able to kind of quantify more and speak to at this year's Investor Day or is that going to remain – I don't know what you put at the bottom of the slide like you're consulting with people or something like that about what the numbers are going to be. When will we kind of hear more about that and how big could that opportunity be?

<A - Darius Adamczyk>: Yeah. We're not putting you in the middle anymore on the call. You wind up grumpy, Steve. No, look, yeah, so the short answer is, yes, on Investor Day, there's obviously going to be a segment of that presentation. We're going to give you a lot more detail.

But I just want to be very clear that the next phase of the transformation is not just the ISC transformation. That's a very big part of it, but we kind of talked a little bit about this deck about kind of the three legs of the stool, which are ISC transformation, Honeywell Digital and Honeywell Connected Enterprises. That's sort of the next phase of the evolution of Honeywell.

And one of those three is a business and the next two are going to be ongoing for at least the next three to five years. So, this is going to give us a lot more tailwinds in terms of margins, cash generation, more efficiency of working capital, simplifications, better planning, lower capital intensity, a lot of benefits. So, we're going to provide a lot more color on that at our Investor Day.

<Q - Charles Stephen Tusa>: Are you going to give something tangible or will it be kind of like directional arrows? I mean sometimes, it sounds great, but ultimately, it doesn't like filter down to the bottom line for other companies. Just curious if you're going to like give something tangible, numbers-wise.

<A - Greg Lewis>: So, Steve, I mean oftentimes, we get asked about how long of a runway do we have for margin expansion. And to me, this is continuing to fill the portfolio of things that keeps that runway alive and well. And so, that's kind of the way I'm thinking about all these things are going to continue to contribute to our ability to drive that margin expansion well beyond 2019.

<Q - Charles Stephen Tusa>: Okay.

<A - Darius Adamczyk>: Yeah. As we kind of get deeper and deeper into the [ph] 20s (49:47), which we're very comfortable that we are going to do and you look at our framework that we presented in 2017, I talked about 30 to 50 basis point expansion, as you see from our performance as well as our guide, at the top end of the range, it's even greater than that number.

These are the kinds of things that enable us to kind of keep growing that margin machine is self-help and these internal initiatives. And the good news is we've got plenty of opportunity, because we've got a lot of work to do on the supply chain and Honeywell Digital. So, I view all of that as not bad news, but really a tremendous opportunity to continue to drive margins.

<Q - Charles Stephen Tusa>: And then, one last one, I know you guys don't want to give specific segment guidance, but maybe can you just talk about who may be above or below the averages when it comes to margin expansion for 2019, just so people are kind of calibrated? Sometimes these segments can move around a little bit and people tend to kind of pick what they want to look at as positives or negatives, so I think it's good to kind of baseline. People don't need exact numbers, but just kind of directional color around what will be above or below that kind of margin expansion or whether they will all be kind of in the middle there? That would be helpful.

<A - Greg Lewis>: Yeah. I would expect Aero and HBT to probably lead the pack in terms of the rate of expansion in 2019, but each of the segments will have a very respectable margin expansion profile. But clearly, with the rate of growth that we're seeing in Aero and leveraging the fixed costs that we have there, that's probably got a pretty sizable opportunity.

And again, HBT, with a return to growth and some new products, we see that as also having fair amount of opportunity, but each of the businesses I think will expand margins in a meaningful way in 2019.

<Q - Jeffrey Todd Sprague>: Just a couple things on maybe some of the longer cycle outlooks and the like. First on Intelligrated, obviously, you have great visibility now on 2019 on this backlog, but do you have visibility on things like front-log, bidding et cetera? Do you expect it to be a fairly active order year again in 2019 for Intelligrated?

<A - Darius Adamczyk>: Yeah. The short answer is absolutely. Because not only because of the continued strength of activity in North America, which continues to be robust, but now with the Transnorm and our enhanced capability in Europe, both from the beachhead that we've established by acquiring Transnorm, but also because if you recall, we put a lot of investments back in the 2017 and 2018 timeframe for R&D capability to have a metrics-based offering. That's complete now. So, we're very capable bidding on warehouses, et cetera. So, we continue to expect another very robust year in our Intelligrated business.

<Q - Jeffrey Todd Sprague>: And then, I was also just wondering back to this megaprojects question in HPS, you noted your orders were strong, even without some of those kind of hitting the order book. I think a lot of those projects kind of being underwritten at maybe $50 or $60 oil price. So, is it just you think there's just kind of a human reflex here that the volatility in Q4 caused people to just tap the pause button or do you see some legitimate risks to these things kind of sliding out further?

<A - Darius Adamczyk>: Yeah. I think it's just natural reaction when you see that kind of volatility like we saw in Q4 that causes people to pause, but we're actually seeing a very positive movement here in Q1. So, I think that some of those decisions will get made and we feel confident that when they do get made, we're going to have some positive outcomes for us. And even – and I was encouraged by our bookings in Q4, because despite not having booked some of those [ph] GMP (54:19) jobs, we still had a very robust orders growth.

<Q - Scott Reed Davis>: So much of the future story of Honeywell seems to relate to software in some way shape or form. I'm a little intrigued by HCE in general. And can you help us understand how centralized is the software development effort? And whenever I hear about centralized software development, I always think about [indiscernible] (54:57). It makes me want to cry or worse. But how do you still stay close to the customer and the businesses themselves and still have this type of a centralized effort and ensure that you're actually getting return on the investment?

<A - Darius Adamczyk>: Yeah. So, let me maybe just explain that. When we say centralized, that means sort of the platform, the IT stack that we call Sentience, that's what centralized that all of our connected enterprises use. But then, the actual analytics, the solutions that are provided, those are very much vertically oriented.

And the way we approach this is essentially each of those businesses end-customer focused business, whether it's connected aircraft, connected plant, connected buildings, we develop MV0, MV1, which is called single pane of glass, which is a lot of value driver solutions for end customers.

And we typically partner with a few key anchor customers to help us iterate and drive and optimize these solutions. So, we're very close to the end customers. And in fact, we develop a lot of these solutions with the end customers, but we also don't want to drive customization, but rather standardization.

So, don't think about this as something that sits at corporate at kind of a central level, it's insular and doesn't work with end customers. That's not the case. What we want to do is have end customer incumbency, while driving leverage to the IT stack called Sentience. That's really the core.

<A - Greg Lewis>: And maybe if I could just add to that, with the leadership from Que, she's applying that customer go-to-market approach across all of those connected enterprises, such that each one of them individually isn't having to develop those muscles and skillsets independent. And while these businesses are still embedded inside of four SPGs, those four SPG Presidents wouldn't possibly be able to give it the amount of time and attention that Que will be able to do as the President of HCE. So, centralized really means focus much more so than corporate.

<A - Darius Adamczyk>: Yeah. It's a very good point. Yes, because [ph] we're this close (57:22)...

<Q - Scott Reed Davis>: Now, that's helpful.

<A - Darius Adamczyk>: Yeah. Because, Scott, the way this was organized before, it still has sort of core reporting into the SPG Presidents and Que, but we gave just a lot more authority and control to Que, just because when you're running $10B or $12B business and you have something that's a fraction of that, that requires a lot of time, attention, strategy changes, agility. It's tough to manage that.

<Q - Scott Reed Davis>: Right. No, that makes sense. That's helpful. And you guys have done a nice job. So, it's not – it just requires I think a little bit explanation. But just a follow-on question really just on Intelligrated and some of the assets you bought around it. Are you close to being at the point where you can go to market together with some of these products globally or how long will it take? I mean just particularly given how regionalized some of the warehouse offerings are?

<A - Darius Adamczyk>: Yeah. The short answer, Scott, is now. We are ready. As a matter of fact, we are quoting globally. And as excited as we are about the North American market, we anticipate being – securing some jobs both in Asia this year as well as Europe. And we're ready. We've invested from an R&D perspective. The Transnorm acquisition is going to further help, but you should expect us to get some more momentum here on a global level in 2019 and a lot of those solutions are finished.

<Q - Andrew Burris Obin>: Just a question on defense, just because it was so strong. Can you give us more visibility into how sustainable some of the developments that you had in Q4 into H1? I would imagine F-35 ramp is sustainable. You mentioned space and defense. I think you mentioned aftermarket, if you could just walk us through visibility for the next six months. Thank you.

<A - Greg Lewis>: Well, I would tell you, so as you mentioned, our defense business has been growing mid-teens all four quarters of 2018. And as we look out for the next six months, the backlog growth there is also very strong. It's strong double digits, over 20%, in defense and space. So, for the next six months, as you mentioned, I think our visibility is very good to continued strength in that area.

<Q - Andrew Burris Obin>: And just maybe on China, could you just describe more color on specific markets? And just your top-down view on Chinese economy and how do you think it will progress through the year, just because you have such a big business there and you've been very knowledgeable?

<A - Darius Adamczyk>: Yeah. As I mention, our China business has been up nearly double digits, just shy of that for the year, so another solid growth year. A bit of a slowing in, I would say in Q4. But there are some very clear reasons and we understood that slowing. So let me kind of take it segment by segment.

If we think about SPS, it was terrific. It was up double-digit growth in China, no slowing. Actually, if anything, things are accelerated. In PMT, we had some tough comps. We understood that and expected that. We had some big both orders and revenue growth, so we expected that. Nothing unusual...

<A - Greg Lewis>: We doubled the business in UOP in the last two years.

<A - Darius Adamczyk>: Yeah.

<A - Greg Lewis>: So the comps is not as small.

<A - Darius Adamczyk>: Yeah, exactly. So, nothing out of the world of expectations. For HBT, as you know, we've had some challenges with the air and water segment. And frankly, some of our distributor partners got a little bit of ahead of themselves given the robust growth that they saw in 2017, and that's been a bit of a challenge for us all year. But we expect that to grow again in 2019. So we think that that's going to be behind us.

And then, with Aero, we had some, say, collections challenges, which actually limited our shipments, because our backlog was actually better than the revenues would indicate. So all in all, we're not building in a tremendous year in China, not kind of the usual Honeywell strong double-digit growth in China where we think it's going to be a little bit slow, but all of that is reflected in our guide. And we expect to grow in China in 2019 for certain. How much that's going to be? Well, we'll see. All in all, I feel pretty good about how the businesses are positioned.

<Q - Andrew Burris Obin>: And do you guys have a view on the Chinese economy bottoms in 2019?

<A - Darius Adamczyk>: Well, I think that's a million dollar – it's a bit of a million dollar question Andrew. I think a lot of that depends on we might know something better in the next 30 days, right. I mean, I think we're all watching carefully what happens on the geopolitical sphere and with the broader economy. Because as I said, we're very prepared from a tariff perspective, because that's something we can identify and should be able to do something about.

What we don't know and where we have some questions, which is, what is going to be the overall economic impact both on the economies of China, the U.S., and etcetera? I think at this juncture, it's roughly a month into the year, it's tough to call. And we'll see what happens.

<Q - Joseph Ritchie>: So, obviously, look, you guys have got a lot accomplished in 2018, congratulations. I think you know one of the areas that we haven't really focused a lot on is that specialty products business. And so maybe just a broader strategic question there, I think that business is tied to semis, electronics. How do you think about that business longer term? I know you did a lot in 2018. This business seems to be a little bit more cyclical vs. the rest of your portfolio. So maybe some thoughts around that to start would be great.

<A - Darius Adamczyk>: Yeah, well, I mean, yeah, there's some cyclicality, there's also some stability. I mean, you know about our Spectra business there which is doing quite well, Aclar business which is acyclical; our electronic materials business which is more cyclical, so it's a bit of a mixed bag, probably where given some of the challenges in the Electronics segment, probably on the lower end of that curve than we are, but I think like anything, I mean we're, we like a lot of those businesses. They'd performed for us. But as always, we're -and I guess, we pointing out during our speaker notes today, we're always assessing everything. I think some of the big things that we wanted to do that we didn't think that fit our portfolio we did in 2018, but everything is always under assessment. We're never done and we always want to kind of add and also subtract potentially. So there's no specific update to the [indiscernible] (01:05:00) business, but like I said, we're always assessing and we're going to do what's – we're making some adjustments as they fit our portfolio.

<Q - Joseph Ritchie>: Yeah, no, that's fair, Darius. Is it fair to think of that business, though, as being mostly semi-CapEx oriented?

<A - Darius Adamczyk>: It's a mixed bag. I mean, there is really a variety of different businesses and that's why it's kind of tough to talk about sort of any given one trends, because you have electronic materials, you have some defense spend, you have healthcare in there, you have consumer goods. So I mean, you have an entire variety of end markets that there's exposure in specialty products. So it's tough to say what that total blend ends up to, but yeah, this is sort of a collective mix of various end markets.

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<Q - Joseph Ritchie>: Okay. Yeah. Fair enough. And just one quick one, Greg. You mentioned the stranded costs earlier, I think the number I had was like roughly around like $340mm, $350mm.

<A - Greg Lewis>: That's right. Yeah.

<Q - Joseph Ritchie>: So the timing of those costs, I mean, is it what's remaining in 2019? First can you quantify what's left in 2019? Secondly, will we get through those costs through H1 or are they going to be kind of linear as the year progresses?

<A - Greg Lewis>: Yeah, so we've taken actions that will have eliminated about half of those costs already as we exited 2018. And as you saw in Q4 with the corporate number being flat to slightly up, that reflects Q1 not having the ability to allocate about $45mm or $50mm to those two spin businesses that are now gone, so that's a little bit about why you saw maybe a heavier number than you might have expected, but we expect that to come down over the course of the year from the first to Q4 and we will exit Q4 at a run rate by which all of those costs will be gone. So you should expect to see a bit of stair step-down. And again, keep in mind that two-thirds of it is in our net corporate costs, about a third of it was sitting in HBT, so you're not going to see $300mm number per se, but it's reflective of a step down as we go through the year.

<Q - Christopher Glynn>: I certainly don't expect to go before Steve, but possibly before Joe next time. Anyways, the question on non-res, a lot of mixed messages, people talking about low-single digits, but yesterday a peer talked about very robust commercial projects. So, just wondering what you're seeing in that space. Is that a very – a vibrant market or is it just kind of GDP limp?

<A - Darius Adamczyk>: No. I mean, if you look at our HPS business, which is probably the best indication of kind of that commercial activity up double-digit bookings in Q4, so actually very, very strong. That's good. We also want to make sure we capture the service. That's the opportunity. That business is stabilizing. I think Vimal and the entire team have put the business on the right path. We're seeing good signs. And sort of the secret to the growth there is revitalization of the NPD pipeline. And I see a lot of good things in the various segments, whether it's building products, whether it's fire, whether it's our BMS systems. So we actually expect a pretty good year. And if you take HPS as a leading indicator, that's also been a pretty good sign in Q4. So we're little bit cautious in the outlook, but given the stability that we have now and it should be a nice story for us – recovering story for us in 2019.

Darius Adamczyk

Closing Remarks

Our end markets continue to be strong and we've got simpler, more focused portfolio following completion of the spins

We continue to execute well as evidenced by our sales, margin and cash performance, with significant balance sheet capacity to deploy

We have a strong performance culture

Our say will continue to equal our do

And we're focused on continuing to outperform for our customers, our shareowners and our employees

I continue to be encouraged about what I see in each of our businesses and our people and excited for what I know will be a strong 2019

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