

Lennox International Inc.

Raising our estimates/PT on continuing commercial HVAC strength and strategic bolt-on

Key takeaways from 3Q results

- Resi declines are fading, w/ LII 3Q volumes down only 2% y/y vs. -8%/-12% in 1Q/2Q. Direct-to-contractor volumes were +MSD, reflecting improving demand + LII share gains. Suggests distributor volumes down ~15-20%; de-stocking headwinds diminished through the Q. Higher SEER supported 7pts positive mix, which combined w/ 2pts price drove 9pts top-line benefit.
- Refrigerant transition mix uplift coming late 2024/2025; higher preparatory costs expected in 1H24.
- Commercial strength continues, driven by margin exp (>900bps y/y). Volumes remain light (+2%); mgmt sees pent-up demand through '24. Expected margin trajectory includes seasonally lighter 4Q, facility investment headwinds in 1H24, and offsetting strategic pricing initiatives on components/410A equipment and volume leverage on Saltillo production ramp in 2H24.
- AES deal is small (~2% of sales) but a solid strategic fit; we estimate should be ~\$0.30 accretive to 2024.
- Mgmt raised '23 organic growth guidance 2pts to ~5% on higher resi sales (volumes -6pts) and commercial +15% (~ flat volumes).

Key investor questions

Some key go-forward questions: 1) what does Resi growth look like accounting for replacement cycle & refrigerant changes; 2) how firm is pent-up Commercial demand in a weakening '24 macro scenario; 3) what level of Comm. margins are achievable/sustainable?

Changes to our estimates

Following 3Q results, we raise EPS estimates 6-9%. Upward revisions are driven by: 1) higher Commercial margins, reflecting strong 3Q performance; 2) Resi sales beat plus price/mix uplift from refrigerant changes; and 3) incorporating AES assets, which we assume contribute ~\$100M in sales. To arrive at our \$19.55/sh 2024e, we are assuming ~5% organic growth (Resi ~HSD/ Commercial ~flat), and more moderate margin expansion of ~30bps.

Valuation: Neutral, \$405 Price Target (was \$380)

\$405 PT applies ~20x to 2024/25e EPS.

Highlights (US\$m)	12/20	12/21	12/22	12/23E	12/24E	12/25E	12/26E	12/27E
Revenues	3,634	4,194	4,718	4,967	5,082	5,326	5,626	5,879
EBIT (UBS)	502	600	664	851	918	990	1,074	1,149
Net earnings (UBS)	383	471	504	640	694	747	814	875
EPS (UBS, diluted) (US\$)	9.94	12.60	14.06	18.00	19.59	21.10	23.00	24.71
DPS (net) (US\$)	3.09	3.11	3.27	3.73	3.89	4.04	4.22	4.38
Net (debt) / cash	(847)	(1,196)	(762)	(1,012)	(540)	(67)	528	1,197
Profitability/valuation	12/20	12/21	12/22	12/23E	12/24E	12/25E	12/26E	12/27E
EBIT (UBS) margin %	13.8	14.3	14.1	17.1	18.1	18.6	19.1	19.5
ROIC (EBIT) %	68.2	68.3	89.4	98.1	74.9	73.5	73.5	74.9
EV/EBITDA (UBS core) x	18.0	19.2	12.9	14.8	13.9	12.9	12.0	11.2
P/E (UBS, diluted) x	24.8	25.1	17.3	20.3	18.7	17.3	15.9	14.8
Equity FCF (UBS) yield %	5.9	3.7	1.9	3.9	4.7	4.8	5.8	6.4
Dividend yield (net) %	1.3	1.0	1.3	1.0	1.1	1.1	1.2	1.2

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of US\$ 365.40 on 30-Oct-2023 18:38:58 EDT

Equities

Americas

Industrial, Diversified

12-month rating **Neutral**

12m price target **US\$405.00**

Prior : **US\$380.00**

Price (30 Oct 2023) **US\$365.40**

RIC: LII.N BBG: LII US

Trading data and key metrics

52-wk range US\$392.07-231.44

Market cap. US\$12.9b

Shares o/s 35.4m (COM)

Free float 84%

Avg. daily volume ('000) 87.3

Avg. daily value (m) US\$32.3

Common s/h equity (12/23E) US\$0.17b

P/BV (12/23E) 78.5x

Net debt to EBITDA (12/23E) 1.1x

EPS (UBS, diluted) (US\$)

	12/23E			
	From	To	% ch	Cons.
Q1	2.82	2.82	0	2.83
Q2	6.15	6.15	0	6.15
Q3E	4.80	5.37	12	5.37
Q4E	3.15	3.66	16	3.36
12/23E	16.94	18.00	6	17.55
12/24E	17.96	19.59	9	19.28
12/25E	19.33	21.10	9	21.43

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Figure 1: Changes to our forecasts

Financial Metric	Prior	New	% chg	Explanation
2023 EPS	\$16.94	\$18.00	6.3%	3Q beat
Sales	\$4,786	\$4,967	3.8%	Higher Resi sales
OP margin	17.2%	17.3%		Driven by Commercial OMX
2024 EPS	\$17.96	\$19.59	9.1%	Higher '23 baseline, + AES acquisition accretion
Sales	\$4,751	\$5,082	7.0%	Raise Resi volume/price assumptions; incorporate AES
OP margin	17.7%	18.3%		
2025 EPS	\$19.33	\$21.10	9.1%	Flow through of estimate changes
Sales	\$4,919	\$5,326	8.3%	
OP margin	18.2%	18.7%		
P/E multiple on PT	~20.5x	~20x		
12-month Price Target	\$ 380	\$ 405	7%	Reflects upward EPS revisions, partly offset by lower P/E applied

Source: UBS Estimates

Key takeaways

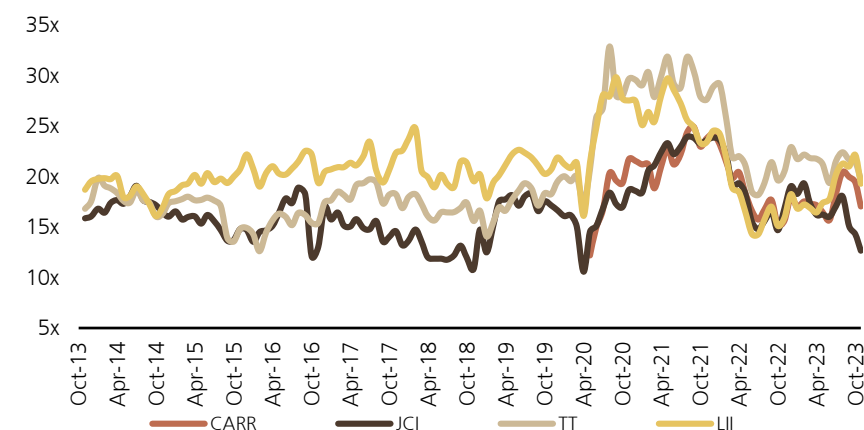
- Resi volumes are still in decline but are improving, down only 2% compared to -8%/-12% in 1Q/2Q respectively. De-stocking headwinds diminished through the Q. Meanwhile, direct-to-contractor sales volumes were +MSD reflecting healthy end-market demand + LII share gains
- Price and mix were both positive for resi in 3Q. Resi prices were +2% following June pricing actions and mix +7% benefitting from new minimum efficiency standards.
- Commercial volumes are +2% despite capacity constraints with seg. margins expanding >900bps y/y to 24%. Robust margin expansion was almost entirely driven by favorable price/mix.
- Commercial lead times are continuing to normalize and order rates remain solid. Q4 margins are expected to step down on seasonal volume declines partially offset by favorable mix/ higher margins in backlog.
- Bolt on acquisition of AES should enhance LII's capabilities in turnkey installations and refrigerant reclaim/recycling unlocking potential cross selling opportunities. Seasonality and margins are in-line with existing LII biz.
- On upcoming refrigerant transition, mgmt. noted some cost impacts in 1H24 in preparation for the transition and expect positive mix benefits to be realized in 2H24 and into 2025.
- New Saltillo Mexico factory for manufacturing commercial equipment would require some temporary working capital build in 1H24 with first production expected in mid-2024 and to be fully ramped up by 2H25.
- Revised guidance is for core revenue growth of ~5% (prior. 2%-4%) which assumes resi sales +2% (volumes -6% implying +HSD price) and commercial revenue +15% on flat volumes.

Figure 2: LII Comps

LII Business Comps	Gross Margin	EBITDA Margin		Sales CAGR							
	FY	2023	2024	2022-24	NTM	2024	2025	NTM	EV / EBITDA	2024	2025
HVAC											
Daikin	32%	14%	15%	5.8%	21.2x	20.3x	18.3x	9.9x	10.0x	9.1x	
Trane Technologies	31%	18%	18%	7.6%	19.2x	18.8x	16.9x	13.9x	13.8x	12.9x	
Carrier	27%	17%	17%	6.9%	16.7x	16.5x	15.3x	10.9x	11.2x	10.3x	
Johnson Controls	33%	15%	16%	5.7%	12.2x	12.2x	11.0x	9.1x	9.5x	9.1x	
Mean	31%	16%	16%	6.5%	17.3x	16.9x	15.4x	10.9x	11.1x	10.4x	
Median	31%	16%	17%	6.4%	17.9x	17.6x	16.1x	10.4x	10.6x	9.7x	
Lennox	27%	19%	19%	3.1%	18.4x	18.1x	16.4x	14.9x	14.4x	13.4x	

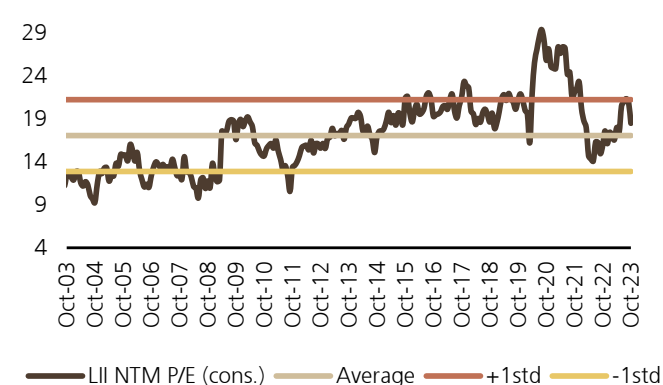
Source: FactSet, UBS estimates

Figure 3: HVAC group NTM P/E



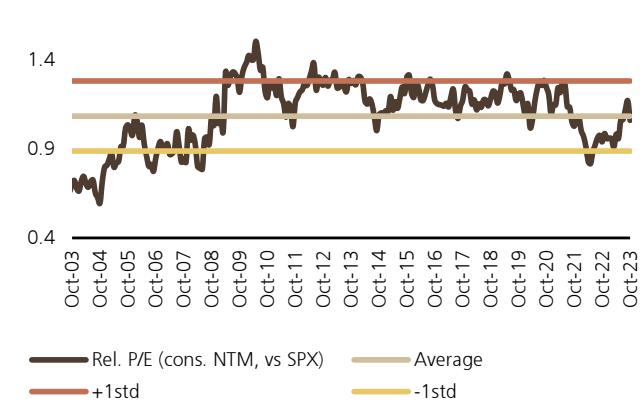
Source: FactSet, UBS

Figure 4: LII NTM P/E



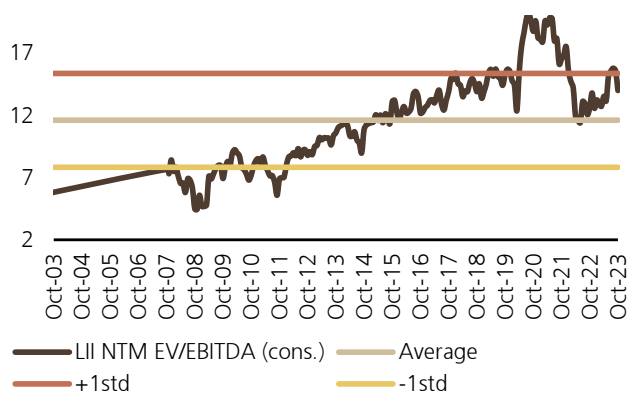
Source: FactSet, UBS

Figure 5: LII Relative P/E



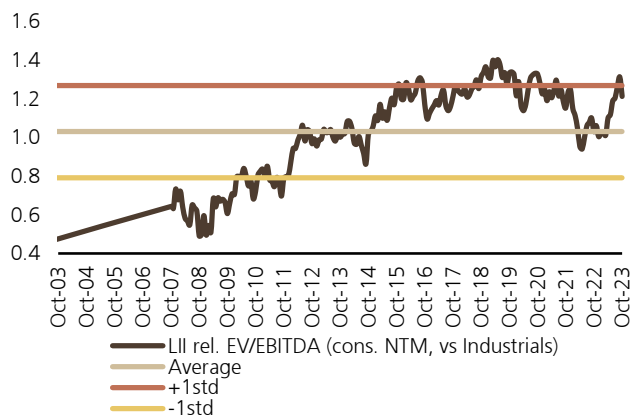
Source: FactSet, UBS

Figure 6: LII NTM EV/EBITDA



Source: FactSet, UBS

Figure 7: LII Relative EV/EBITDA



Source: FactSet, UBS

Figure 8: Guidance vs UBSe

	2023					UBSe
Sales (\$M)	15-Dec-22	31-Jan-23	27-Apr-23	28-Jul-23	26-Oct-23	\$4,967
Revenue growth						1.2%
Constant Currency growth	0%-4%	0%-4%	0%-4%	2%-4%	~5%	6.3%
FX						-0.3%
NA Resi mkt shipments	-MSD	-MSD	-MSD	-HSD	down ~6%	
NA resi revenue	flat to LSD	flat to LSD	flat to LSD	flat to LSD	up ~2%	2.4%
NA Comm'l Unitary mkt	+HSD	+HSD	+HSD		~flat	
NA Comm'l revenue	+HSD / LDD	+HSD / LDD	+HSD / LDD	+LDD	up ~15%	16.5%
Margin: EBIT ROS						17.3%
Segment EBIT						
Price/Mix (\$MM)	150	162.5	175	250	325	
Net material cost inflation (\$MM)	-15	-35	-45	-25	0	
Margin Tailwinds						
Price / Mix (\$MM)	150	150-175	175	250	325	
Commodity cost benefit (\$MM)	35	35	25	35		
Product / material cost reduction (\$MM)	30	30	30	30		
Margin Headwinds						
Component cost increases (\$MM)	80	100	100	90	>0	
SG&A inflation + incentive comp, less productivity		>0	>0	>0		
Interest expense / Other	\$55-\$60M	\$55-\$60M	\$55-\$60M	\$55-\$60M	\$55M	\$62
Corporate expense	~\$80	~\$80	~\$80	~\$95M	~\$100	\$98
Tax rate	19%-21%	19%-21%	19%-21%	19%-20%	20%	19.8%
EPS	\$14.25 - \$15.25	\$14.25 - \$15.25	\$14.25 - \$15.25	\$15.50-\$16.00	\$17.25 - \$17.75	\$18.00
CFO	\$500M-\$600M	\$500M-\$600M				\$636M
Capex	\$250M	\$250M	\$250M	~\$250M	\$250M	\$225M
FCF	\$250M-\$350M	\$250M-\$350M	\$250M-\$350M	\$300M-\$350M	\$350M-\$400M	\$411M
FCF Conversion						64%
Stock repurchase	\$100-\$200M					\$95M
Wt. avg. diluted share count	35M-36M	35M-36M	35M-36M	35M-36M	35.5M	35.6M

Source: Company Reports, UBS estimates

Figure 9: Model Summary

LII Model Summary

	2022				2023				2024				2019	2020	2021	2022	2023E	2024E
	1Q22	2Q22	3Q22	4Q22	1Q23	2Q23	3Q23	4Q23E	1Q22E	2Q22E	3Q22E	4Q22E						
Income Statement																		
Sales (\$M)	1,013.4	1,366.3	1,244.9	1,093.8	1,049.4	1,411.4	1,366.3	1,139.8	1,044.4	1,410.2	1,399.1	1,228.2	3,773.0	3,634.1	4,194.2	4,718.4	4,966.9	5,081.9
Residential HVAC	682.2	977.5	835.3	703.4	681.0	936.2	896.3	763.2	701.4	973.6	984.8	857.6	2,291.2	2,361.6	2,775.6	3,198.4	3,276.7	3,517.5
Commercial HVAC	279.5	327.4	352.3	327.2	308.7	407.5	405.5	376.6	343.0	436.6	414.3	370.6	947.4	800.8	1,188.8	1,286.4	1,498.3	1,564.4
Refrigeration	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	534.4	471.7	0.0	0.0	0.0	0.0
Sales growth (y/y)	8.9%	10.3%	17.5%	13.4%	(2.3%)	(1.7%)	4.6%	4.2%	5.5%	5.0%	7.5%	7.8%	3.0%	(3.7%)	15.4%	12.5%	1.2%	6.4%
Organic sales growth (y/y)	9.0%	11.0%	18.0%	14.0%	3.0%	3.6%	9.6%	9.0%	3.0%	3.1%	5.6%	7.0%	3.6%	(3.8%)	14.8%	12.0%	6.3%	4.7%
Residential HVAC	13.0%	17.0%	17.0%	13.0%	0.0%	(4.0%)	7.3%	8.5%	3.0%	4.0%	9.9%	12.4%	3.2%	3.2%	17.0%	15.2%	2.6%	7.3%
Commercial HVAC	(6.0%)	(13.0%)	20.0%	19.0%	10.0%	26.0%	15.1%	10.0%	3.0%	1.0%	(4.0%)	(3.8%)	5.5%	(15.5%)	7.6%	4.4%	15.5%	(1.1%)
Refrigeration	18.0%	20.0%	21.0%	10.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	1.9%	(12.7%)	16.0%	0.0%	0.0%	0.0%
Segment profit (\$M)	131.4	257.5	206.2	164.8	161.1	305.6	278.7	213.8	173.4	310.1	304.3	236.9	692.5	598.1	705.0	759.9	959.2	1,024.8
Segment margin	13.0%	18.8%	16.6%	15.1%	15.4%	21.7%	20.4%	18.8%	16.6%	22.0%	21.8%	19.3%	18.4%	16.5%	16.8%	16.1%	19.3%	20.2%
Residential HVAC	15.8%	22.1%	18.4%	16.9%	16.3%	21.6%	20.2%	17.4%	16.3%	21.6%	20.4%	17.9%	20.3%	18.1%	19.5%	18.7%	19.2%	19.3%
Commercial HVAC	8.5%	12.6%	14.9%	13.9%	16.2%	25.3%	24.0%	21.5%	17.2%	22.8%	25.0%	22.5%	17.5%	17.1%	13.8%	12.7%	22.1%	22.1%
Refrigeration	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	11.7%	7.0%	0.0%	0.0%	0.0%	0.0%
EBIT (\$M)	118.0	230.4	189.7	131.1	141.7	283.1	255.3	181.1	149.2	285.9	280.1	212.7	610.0	506.4	608.6	669.2	861.2	927.8
EBIT margin	11.6%	16.9%	15.2%	12.0%	13.5%	20.1%	18.7%	15.9%	14.3%	20.3%	20.0%	17.3%	16.2%	13.9%	14.5%	14.2%	17.3%	18.3%
EBITDA (\$M)	136.8	249.4	208.1	152.8	161.3	304.0	276.8	199.0	167.1	303.8	298.0	230.6	681.1	579.0	681.0	747.1	941.1	999.6
EBITDA margin	13.5%	18.3%	16.7%	14.0%	15.4%	21.5%	20.3%	17.5%	16.0%	21.5%	21.3%	18.8%	18.1%	15.9%	16.2%	15.8%	18.9%	19.7%
Tax rate	19.7%	19.0%	18.2%	21.7%	21.4%	17.5%	18.9%	23.2%	19.5%	19.5%	19.5%	19.5%	21.5%	19.1%	18.0%	19.4%	19.8%	19.5%
Share count (diluted)	36.5	37.5	35.5	35.6	35.6	35.6	35.7	35.4	35.4	35.4	35.4	35.4	39.4	38.6	37.4	35.8	35.6	35.4
EPS - Adjusted	\$2.36	\$5.00	\$4.10	\$2.63	\$2.82	\$6.15	\$5.37	\$3.66	\$2.99	\$6.09	\$6.06	\$4.46	\$11.16	\$9.94	\$12.60	\$14.06	\$18.00	\$19.59
EPS growth (y/y)	3.8%	9.3%	20.6%	11.7%	19.7%	22.9%	31.0%	39.1%	5.9%	(1.0%)	12.8%	21.9%	18.6%	(11.0%)	26.8%	11.6%	28.0%	8.8%
EPS - GAAP	\$2.29	\$4.96	\$3.99	\$2.65	\$2.75	\$6.10	\$3.65	\$3.66	\$2.99	\$6.09	\$6.06	\$4.46	\$10.61	\$9.25	\$12.47	\$13.87	\$16.17	\$19.59
Gross margin	26.5%	29.1%	26.8%	26.1%	29.2%	32.4%	31.4%	26.4%	29.5%	32.7%	31.7%	26.7%	27.7%	28.5%	28.3%	27.2%	30.1%	30.3%
SG&A % of sales	15.3%	12.4%	11.8%	14.2%	16.0%	12.8%	13.1%	11.0%	15.7%	12.8%	12.0%	9.9%	15.5%	15.3%	14.3%	13.3%	13.0%	12.5%
Valuation / Leverage																		
P/E	17.6x	17.1x	15.8x	14.6x	13.8x	13.7x	13.7x	13.2x	12.7x	12.6x	12.4x	12.1x	22.2x	25.0x	19.7x	17.7x	13.8x	12.7x
EV / Sales	2.0x	2.0x	2.0x	2.0x	1.9x	1.9x	1.9x	1.9x	1.9x	1.9x	1.9x	1.8x	2.5x	2.6x	2.4x	2.0x	2.0x	1.8x
EV / EBITDA	12.9x	12.5x	11.7x	10.8x	10.2x	10.2x	10.2x	10.0x	9.6x	9.6x	9.5x	9.2x	14.1x	16.6x	14.6x	12.8x	10.4x	9.3x
P / FCF	43.2x	41.9x	31.5x	22.0x	21.5x	12.1x	14.5x	15.6x	14.4x	15.7x	16.4x	16.7x	33.7x	17.9x	22.7x	44.2x	21.5x	14.4x
FCF Yield	2.3%	2.4%	3.2%	4.6%	4.6%	8.3%	6.9%	6.4%	6.9%	6.4%	6.1%	6.0%	3.0%	5.6%	4.4%	2.3%	4.7%	6.5%
Debt / EBITDA													1.2x	1.7x	1.8x	1.1x	1.2x	1.1x
Net debt / EBITDA													1.2x	1.5x	1.8x	1.0x	1.1x	0.5x
BV / share													-\$4.32	-\$0.44	-\$7.19	-\$5.67	\$4.63	\$20.75
Cash Flow																		
Cash Flow from Operations (CFO)	(97.9)	97.1	170.9	132.2	(78.8)	195.5	313.2	205.8	246.0	69.8	268.5	194.7	396.1	612.4	515.5	302.3	635.7	779.0
Capital Expenditures	(25.8)	(20.9)	(20.3)	(34.1)	(35.4)	(49.9)	(39.7)	(100.0)	(42.5)	(42.5)	(42.5)	(42.5)	(105.6)	(78.5)	(106.8)	(101.1)	(225.0)	(170.0)
Free Cash Flow (FCF, adjusted)	(123.7)	76.2	150.6	98.1	(114.2)	145.6	273.5	105.8	203.5	27.3	226.0	152.2	290.5	533.9	408.7	201.2	410.7	609.0
FCF per share (adjusted)	-\$3.39	\$2.13	\$4.24	\$2.76	-\$3.21	\$4.09	\$7.66	\$2.99	\$5.75	\$0.77	\$6.38	\$4.30	\$7.37	\$13.85	\$10.93	\$5.62	\$11.54	\$17.20
FCF conversion (adjusted)	-144%	43%	103%	105%	-114%	67%	143%	82%	192%	13%	105%	96%	66%	139%	87%	40%	64%	88%
Depreciation & Amortization	18.8	19.0	18.4	21.7	19.6	20.9	21.5	18.0	18.0	18.0	18.0	18.0	71.1	72.6	72.4	77.9	80.0	71.8
D&A / sales	2.3%	1.8%	1.9%	2.5%	2.4%	2.0%	2.3%	2.2%	2.3%	1.7%	1.7%	2.0%	2.4%	2.7%	2.3%	2.1%	2.2%	1.9%
Capital sales	2.5%	1.5%	1.6%	3.1%	3.4%	3.5%	2.9%	8.8%	4.1%	3.0%	3.0%	3.5%	2.8%	2.2%	2.5%	2.1%	4.5%	3.3%
Buyback	(200.0)	(100.0)	0.0	0.0	0.0	0.0	0.0	(95.0)	0.0	0.0	0.0	0.0	(400.0)	(117.9)	(622.1)	(300.0)	(95.0)	0.0
M&A (acquisition negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Dividend	(33.7)	(33.2)	(75.1)	0.0	(37.6)	(37.6)	(78.2)	(32.8)	(34.4)	(34.4)	(34.4)	(34.4)	(110.5)	(118.1)	(126.5)	(142.0)	(186.2)	(137.7)
Dividend yield	1.6%	1.2%	1.4%	1.2%	2.1%	1.7%	1.8%	1.6%	1.6%	2.5%	3.6%	5.2%	5.3%	6.3%	6.6%	6.9%	7.0%	4.9%
Balance Sheet																		
Cash & equivalents	34.3	57.4	40.7	52.6	40.4	51.4	132.0	110.0	279.1	272.0	463.5	581.2	37.3	123.9	31.0	52.6	110.0	581.2
Accounts receivable	603.0	782.6	708.4	608.5	642.5	843.6	694.8	761.3	817.6	1,037.0	891.6	801.7	477.8	448.3	508.3	608.5	761.3	801.7
Inventories	678.9	692.8	743.4	753.0	904.1	856.0	747.9	729.4	705.1	670.1	706.4	801.2	544.1	439.4	510.9	753.0	729.4	801.2
Accounts payable	457.3	485.6	430.5	427.3	445.0	470.1	345.8	438.7	589.4	606.8	530.3	550.4	372.4	340.3	402.1	427.3	438.7	550.4
Net working capital (\$M)	824.6	989.8	1,021.3	934.2	1,101.6	1,229.5	1,096.9	1,052.0	933.3	1,100.4	1,067.8	1,052.5	649.5	547.4	617.1	934.2	1,052.0	1,052.5
Short-term debt	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Long-term debt	1,599.5	1,681.5	1,593.4	814.2	1,010.1	817.7	1,121.6	1,121.6	1,121.6	1,121.6	1,121.6	1,121.6	849.3	970.7	1,226.5	814.2	1,121.6	1,121.6
Equity	(410.2)	(401.3)	(305.2)	(203.1)	(125.9)	62.6	159.5	164.7	239.5	424.1	607.5	734.5	(170.2)	(17.1)	(269.0)	(203.1)	164.7	734.5
Net debt	1,565.2	1,624.1	1,552.7	761.6	969.7	766.3	989.6	1,011.6	842.5	849.6	658.1	540.4	812.0	846.8	1,195.5	761.6	1,011.6	540.4
Current ratio	1.7	1.7	1.7	0.9	1.1	1.0	1.4	1.3	1.3	1.4	1.5	1.6	1.1	1.6	1.4	0.9	1.3	1.6
Interest coverage	15.9	24.5	16.9	10.3	10.3	15.9	13.6	16.2	8.4	15.7	20.4	13.9	12.3	15.4	20.8	16.4	14.0	14.3
Receivable turnover	7.6	6.0	7.1	8.4	7.6	5.9	7.0	7.3	6.8	5.3	6.3	6.5	7.9	7.8	8.8	8.4	7.3	6.5
Inventory turnover	5.2	5.7	5.5	5.4	4.3	4.4	4.6	4.7	4.3	4.5	4.8	4.6	5.2	5.3	6.3	5.4	4.7	4.6
Payable turnover	10.3	9.9	11.0	11.4	10.5	10.0	12.7	11.5	9.6	9.2	11.4	10.3	9.4	10.2	11.3	11.4	11.5	10.3
Net working capital % of sales	19.3%	22.5%	22.3%	19.8%	23.2%	25.6%	22.3%	21.2%	18.8%	22.2%	21.4%	20.7%	17.2%	15.1%	14.7%	19.8%	21.2%	20.7%
Return on average equity	-164.9%	-155.3%	-155.3%	-213.4%	-193.3%	-329.8%	-829.9%	-3335.7%	1136.4%	264.0%	173.4%	154.3%	-275.1%	-409.2%	-329.5%	-213.4%	-3335.7%	154.3%
Return on average assets	20.8%	19.6%	20.9%	21.3%	19.8%	19.8%	21.9%	23.1%	21.6%	20.1%	20.7%	20.8%	22.8%	18.8%	22.4%	21.3%	23.1%	20.8%
Return on average invested capital	36.1%	34.9%	37.7%	47.1%	33.3%	33.5%	36.3%	46.5%	35.1%	32.4%	31.6%	38.6%	50.6%	41.7%	51.7%	47.1%	46.5%	38.6%

Figure 10: LII 3Q23 Results vs prior. Consensus & UBS

Quarterly Comparison (\$M)			Delta (\$) vs. UBS	Delta (%) vs. UBS	EPS Impact	Delta (%) vs. Consensus	
	UBSe	Actuals				Consensus	Consensus
Revenues							
Residential HVAC	856.2	896.3	40.1	4.7%		845.0	6.1%
Commercial HVAC ¹	447.2	465.2	18.0			458.9	1.4%
Total Revenues	1,303.4	1,361.5	58.1	4.5%		1,281.3	6.3%
Operating Profit							
Residential HVAC	171.2	181.4	10.2	5.9%	\$0.23	159.5	13.7%
Commercial HVAC ¹	77.5	97.3	19.8	25.5%	\$0.45	86.1	13.1%
Total Segment Profit	248.7	278.7	30.0	12.0%	\$0.68	245.6	13.5%
Operating Profit	224.0	255.3				225.6	13.2%
Sales Growth							
Residential HVAC	2.5%	7.0%				1.2%	580
Commercial HVAC ¹	10.0%	15.0%				n.a.	n.a.
Total Sales Growth	35.1%	41.1%				2.9%	3820
Operating Margin							
Residential HVAC	20.0%	20.2%				18.9%	140
Commercial HVAC ¹	20.0%	24.0%				18.8%	n.a.
Total Segment Margin	20.0%	21.4%				19.2%	220
Total operating margin	18.1%	19.6%				17.6%	200
Corporate expense	(24.8)	(23.4)	1.4		\$0.03		
Other	1.0	(7.6)	(8.6)		(\$0.20)		
Net interest expense	(14.0)	(11.2)	2.8		\$0.06		
Effective tax rate	19.3%	18.9%			\$0.02		
Diluted shares	35.4	35.7			(\$0.03)		
Rounding	0.00	0.00					
EPS	\$4.80	\$5.37			11.8%	\$4.75	13.0%

Organic growth	UBSe	3Q23 Consensus	Actuals	2Q23 Actuals	
Residential HVAC	2.5%		7.0%	-4.0%	
Commercial HVAC	10.0%		15.0%	26.0%	70%
Total Lennox	4.7%	5.5%	9.4%	3.6%	30%

Source: Company Reports, FactSet, UBS estimates

Lennox International Inc. (LII.N)

	12/20	12/21	12/22	12/23E	%ch	12/24E	%ch	12/25E	12/26E	12/27E
Income Statement (US\$m)										
Revenues	3,634	4,194	4,718	4,967	5.3	5,082	2.3	5,326	5,626	5,879
Gross profit	1,034	1,189	1,285	1,494	16.3	1,541	3.1	1,629	1,738	1,834
EBITDA (UBS)	575	672	742	931	25.5	989	6.3	1,061	1,145	1,221
Depreciation & amortisation	(73)	(72)	(78)	(80)	-2.6	(72)	10.2	(72)	(72)	(72)
EBIT (UBS)	502	600	664	851	28.1	918	7.8	990	1,074	1,149
Associates & investment income	0	0	0	0	-	0	-	0	0	0
Other non-operating income	0	0	0	0	-	0	-	0	0	0
Net interest	(28)	(25)	(39)	(53)	-35.9	(56)	-6.5	(56)	(56)	(56)
Exceptionals (incl goodwill)	0	0	0	0	-	0	-	0	0	0
Pre-tax profit	474	575	625	798	27.7	862	7.9	934	1,018	1,093
Tax	(90)	(103)	(122)	(158)	-29.9	(168)	-6.5	(187)	(204)	(219)
Profit after tax	383	471	504	640	27.1	694	8.3	747	814	875
Preference dividends	0	0	0	0	-	0	-	0	0	0
Minorities	0	0	0	0	-	0	-	0	0	0
Extraordinary items	0	0	0	0	-	0	-	0	0	0
Net earnings (local GAAP)	383	471	504	640	27.1	694	8.3	747	814	875
Net earnings (UBS)	383	471	504	640	27.1	694	8.3	747	814	875
Tax rate (%)	19.1	18.0	19.4	19.8	1.7	19.5	-1.4	20.0	20.0	20.0
Per Share (US\$)										
EPS (UBS, diluted)	9.94	12.60	14.06	18.00	28.0	19.59	8.8	21.10	23.00	24.71
EPS (local GAAP, diluted)	9.94	12.60	14.06	18.00	28.0	19.59	8.8	21.10	23.00	24.71
EPS (UBS, basic)	10.01	12.67	14.11	18.08	28.1	19.59	8.4	21.10	23.00	24.71
DPS (net) (US\$)	3.09	3.11	3.27	3.73	14.0	3.89	4.4	4.04	4.22	4.38
Cash EPS (UBS, diluted) ¹	11.82	14.53	16.23	20.25	24.7	21.62	6.8	23.13	25.03	26.74
Book value per share	(0.45)	(7.34)	(5.74)	4.65	-	20.75	346.0	38.20	57.37	78.10
Average shares (diluted)	39	37	36	36	-0.7	35	-0.5	35	35	35
Balance Sheet (US\$m)										
Cash and equivalents	124	31	53	110	109.2	581	NM	1,054	1,649	2,319
Other current assets	964	1,144	1,444	1,648	14.2	1,761	6.8	1,896	1,950	2,021
Total current assets	1,088	1,175	1,497	1,758	17.5	2,342	33.2	2,950	3,599	4,340
Net tangible fixed assets	464	515	549	684	24.6	782	14.3	820	859	897
Net intangible fixed assets	187	187	186	182	-2.5	182	0.0	182	182	182
Investments / other assets	294	295	336	364	8.3	364	0.0	364	364	364
Total assets	2,033	2,172	2,568	2,988	16.4	3,670	22.8	4,316	5,003	5,782
Trade payables & other ST liabilities	701	827	1,596	1,348	-15.5	1,460	8.3	1,488	1,497	1,542
Short term debt	0	0	0	0	-	0	-	0	0	0
Total current liabilities	701	827	1,596	1,348	-15.5	1,460	8.3	1,488	1,497	1,542
Long term debt	971	1,227	814	1,122	37.8	1,122	0.0	1,122	1,122	1,122
Other long term liabilities	378	387	361	354	-1.9	354	0.0	354	354	354
Preferred shares	0	0	0	0	-	0	-	0	0	0
Total liabilities (incl pref shares)	2,050	2,441	2,771	2,823	1.9	2,935	4.0	2,964	2,973	3,018
Common s/h equity	(17)	(269)	(203)	165	-	734	346.0	1,352	2,031	2,765
Minority interests	0	0	0	0	-	0	-	0	0	0
Total liabilities & equity	2,033	2,172	2,568	2,988	16.4	3,670	22.8	4,316	5,003	5,782
Cash Flow (US\$m)										
Net income (before pref divs)	383	471	504	640	27.1	694	8.3	747	814	875
Depreciation & amortisation	73	72	78	80	2.6	72	-10.2	72	72	72
Net change in working capital	105	(85)	(334)	(153)	54.0	0	99.7	(117)	(55)	(36)
Other operating	77	96	20	166	NM	14	-91.6	24	24	24
Operating cash flow	638	555	268	733	173.6	779	6.3	726	854	935
Tangible capital expenditure	(79)	(107)	(101)	(225)	-122.6	(170)	24.4	(110)	(110)	(110)
Intangible capital expenditure	0	0	0	0	-	0	-	0	0	0
Net (acquisitions) & disposals	0	0	0	0	-	0	-	0	0	0
Other investing	(1)	0	(2)	1	-	0	-	0	0	0
Investing cash flow	(80)	(106)	(103)	(225)	-118.0	(170)	24.3	(110)	(110)	(110)
Equity dividends paid	(118)	(127)	(142)	(186)	-31.1	(138)	26.0	(143)	(149)	(155)
Share issues / (buybacks)	(118)	(622)	(300)	(95)	68.3	0	-	0	0	0
Other financing	(294)	252	92	130	41.8	0	-	0	0	0
Change in debt & pref shares	84	(6)	173	(203)	-	0	-	0	0	0
Financing cash flow	(446)	(502)	(178)	(354)	-99.1	(138)	61.1	(143)	(149)	(155)
Cash flow inc/(dec) in cash	112	(54)	(13)	154	-	471	205.2	473	595	670
FX / non cash items	(25)	(39)	34	(97)	-	0	-	0	0	0
Balance sheet inc/(dec) in cash	87	(93)	22	57	165.8	471	NM	473	595	670

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.¹ Cash EPS (UBS, diluted) is calculated using UBS net income adding back depreciation and amortization.

Lennox International Inc. (LII.N)

Valuation (x)	12/20	12/21	12/22	12/23E	12/24E	12/25E	12/26E	12/27E
P/E (local GAAP, diluted)	24.8	25.1	17.3	20.3	18.7	17.3	15.9	14.8
P/E (UBS, diluted)	24.8	25.1	17.3	20.3	18.7	17.3	15.9	14.8
P/CEPS	20.7	21.7	15.0	18.0	16.9	15.8	14.6	13.7
Equity FCF (UBS) yield %	5.9	3.7	1.9	3.9	4.7	4.8	5.8	6.4
Dividend yield (net) %	1.3	1.0	1.3	1.0	1.1	1.1	1.2	1.2
P/BV	NM	NM	NM	NM	17.6	9.6	6.4	4.7
EV/revenues (core)	2.8	3.1	2.0	2.8	2.7	2.6	2.4	2.3
EV/EBITDA (UBS core)	18.0	19.2	12.9	14.8	13.9	12.9	12.0	11.2
EV/EBIT (core)	20.6	21.6	14.4	16.1	15.0	13.9	12.8	11.9
EV/OpFCF (core)	20.8	22.9	14.9	19.5	16.8	14.4	13.3	12.4
EV/op. invested capital	14.0	14.7	12.9	15.8	11.2	10.2	9.4	8.9
Enterprise value (US\$m)	12/20	12/21	12/22	12/23E	12/24E	12/25E	12/26E	12/27E
Market cap.	9,521	12,128	8,745	12,935	12,935	12,935	12,935	12,935
Net debt (cash)	799	799	799	799	799	799	799	799
Buy out of minorities	0	0	0	0	0	0	0	0
Pension provisions/other	0	0	0	0	0	0	0	0
Total enterprise value	10,319	12,927	9,544	13,734	13,734	13,734	13,734	13,734
Non core assets	0	0	0	0	0	0	0	0
Core enterprise value	10,319	12,927	9,544	13,734	13,734	13,734	13,734	13,734
Growth (%)	12/20	12/21	12/22	12/23E	12/24E	12/25E	12/26E	12/27E
Revenue	(3.7)	15.4	12.5	5.3	2.3	4.8	5.6	4.5
EBITDA (UBS)	(15.4)	17.0	10.4	25.5	6.3	7.3	7.9	6.6
EBIT (UBS)	(17.4)	19.5	10.7	28.1	7.8	7.9	8.5	7.1
EPS (UBS, diluted)	(11.0)	26.8	11.6	28.0	8.8	7.7	9.0	7.4
Net DPS	4.6	0.8	5.0	14.0	4.4	3.8	4.5	3.7
Margins & Profitability (%)	12/20	12/21	12/22	12/23E	12/24E	12/25E	12/26E	12/27E
Gross profit margin	28.5	28.3	27.2	30.1	30.3	30.6	30.9	31.2
EBITDA margin	15.8	16.0	15.7	18.7	19.5	19.9	20.4	20.8
EBIT (UBS) margin	13.8	14.3	14.1	17.1	18.1	18.6	19.1	19.5
Net earnings (UBS) margin	10.5	11.2	10.7	12.9	13.6	14.0	14.5	14.9
ROIC (EBIT)	68.2	68.3	NM	NM	74.9	73.5	73.5	74.9
ROIC post tax	55.2	56.0	72.1	NM	60.3	58.8	58.8	59.9
ROE (UBS)	(409.2)	(329.5)	(213.4)	<-500	154.3	71.6	48.1	36.5
Capital structure & Coverage (x)	12/20	12/21	12/22	12/23E	12/24E	12/25E	12/26E	12/27E
Net debt / EBITDA	1.5	1.8	1.0	1.1	0.5	0.1	(0.5)	(1.0)
Net debt / total equity %	NM	NM	NM	NM	73.6	5.0	(26.0)	(43.3)
Net debt / (net debt + total equity) %	NM	NM	NM	86.0	42.4	4.7	(35.1)	(76.4)
Net debt/EV %	8.0	7.9	10.3	6.5	5.7	2.2	(1.7)	(6.3)
Capex / depreciation %	108.1	147.5	129.8	NM	NM	153.1	153.1	153.1
Capex / revenue %	2.2	2.5	2.1	4.5	3.3	2.1	2.0	1.9
EBIT / net interest	17.7	23.9	17.2	16.2	16.4	17.7	19.2	20.5
Dividend cover (UBS)	3.2	4.1	4.3	4.9	5.0	5.2	5.4	5.6
Div. payout ratio (UBS) %	30.9	24.6	23.2	20.6	19.9	19.2	18.4	17.7
Revenues by division (US\$m)	12/20	12/21	12/22	12/23E	12/24E	12/25E	12/26E	12/27E
Others	3,634	4,194	4,718	4,967	5,082	5,326	5,626	5,879
Total	3,634	4,194	4,718	4,967	5,082	5,326	5,626	5,879
EBIT (UBS) by division (US\$m)	12/20	12/21	12/22	12/23E	12/24E	12/25E	12/26E	12/27E
Others	502	600	664	851	918	990	1,074	1,149
Total	502	600	664	851	918	990	1,074	1,149

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.

Forecast returns

Forecast price appreciation	+10.8%
Forecast dividend yield	1.1%
Forecast stock return	+11.9%
Market return assumption	10.0%
Forecast excess return	+1.8%

Company Description

Lennox International is a leading manufacturer of heating, ventilation, air conditioning, and refrigeration (HVACR) equipment and supplies. In 2022, Lennox generated about \$4.7bn in revenue (about 95% from the US and Canada and 5% international). The company sells its Lennox brand directly to a network of independent dealers and operates ~245 Lennox stores across the US and Canada. The company also makes a smaller line of products sold under the brands Ducane, Armstrong Air, AirEase, Concord, Magic-Pak, and Advanced Distributor Products.

Valuation Method and Risk Statement

Our PT is based on relative PE valuation methodology. Multi-Industry companies are subject to risks associated with unexpected changes in the underlying global macro environment, currency movements, commodity price inflation, M&A integration, and changes in the competitive or regulatory environment. Other primary risks for Lennox include substantial exposure to the HVAC industry which is highly seasonal, exposed to raw material volatility (especially copper, steel and aluminum), demanding customers in refrigeration (supermarkets), competitively intense industries and also influenced by seasonal weather that can drive volatility quarter to quarter.

Quantitative Research Review

UBS Global Research publishes a quantitative assessment of its analysts' responses to certain questions about the likelihood of an occurrence of a number of short term factors in a product known as the 'Quantitative Research Review'. The views for this month can be found below. Views contained in this assessment on a particular stock reflect only the views on those short term factors which are a different timeframe to the 12-month timeframe reflected in any equity rating set out in this note. For previous responses please make reference to (i) previous UBS Global Research reports; and (ii) where no applicable research report was published that month, the Quantitative Research Review which can be found at <https://neo.ubs.com/quantitative>, or contact your UBS sales representative for access to the report or the Quantitative Research Team on qa@ubs.com. A consolidated report which contains all responses is also available and again you should contact your UBS sales representative for details and pricing or the Quantitative Research Team on the email above.

Lennox International Inc.

Question	Response
1. Is the industry structure facing the firm likely to improve or deteriorate over the next six months? Rate on a scale of 1-5 (1 = getting worse, 3 = no change, 5 = getting better, N/A = no view)	3
2. Is the regulatory/government environment facing the firm likely to improve or deteriorate over the next six months? Rate on a scale of 1-5 (1 = getting tougher, 3 = no change, 5 = getting better, N/A = no view)	4
3. Over the last 3-6 months in broad terms have things been improving/no change/getting worse for this stock? Rate on a scale of 1-5 (1 = getting a lot worse, 3 = not much change, 5 = getting a lot better, N/A = no view)	4
4. Relative to the current CONSENSUS EPS forecast, is the next company EPS update likely to lead to: (1 = negative surprise vs consensus, 3 = in-line with consensus, 5 = positive surprise vs consensus expectations, N/A = no view)	3
5. What's driving the difference?	
6. Relative to YOUR current earnings forecast, is there relatively greater risk at the next earnings result of: (1 = downside skew risk to earnings, 3 = equal upside or downside risk to earnings, 5 = upside skew risk to earnings, N/A = no view)	3
7. What's driving the difference?	
8. Is there an upcoming catalyst for the company over the next three months?	
9. Is there an actual or approximate date for the catalyst?	
10. Is the catalyst date an actual or approximate date?	
11. What is the catalyst?	

Required Disclosures

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Buy	FSR is > 6% above the MRA.	54%	40%
Neutral	FSR is between -6% and 6% of the MRA.	38%	42%
Sell	FSR is > 6% below the MRA.	9%	40%
Short-Term Rating	Definition	Coverage ³	IB Services ⁴
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 30 September 2023.

1:Percentage of companies under coverage globally within the 12-month rating category.

2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.

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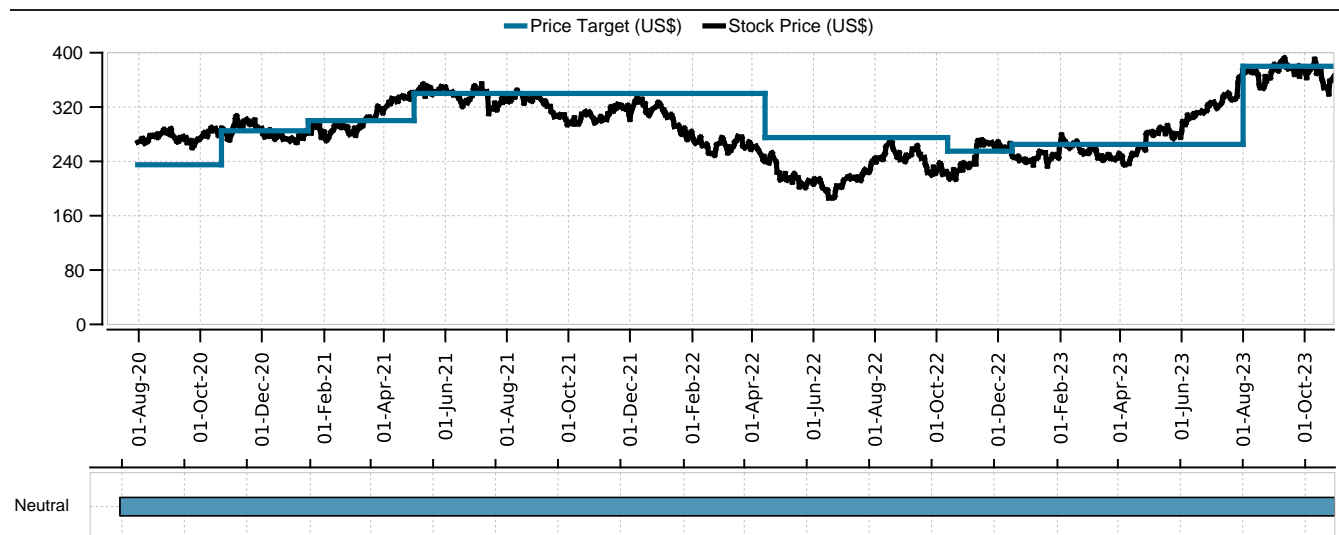
Company Name	Reuters	12-month rating	Price	Price date
Lennox International Inc. ¹⁶	LII.N	Neutral	US\$365.40	30 Oct 2023

Source: UBS Global Research; Refinitiv. All prices as of local market close. Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date.

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Lennox International Inc. (US\$)



Date	Stock Price (US\$)	Price Target (US\$)	Rating
2020-07-30	270.87	235.00	Neutral
2020-10-21	283.98	285.00	Neutral
2021-01-15	281.44	300.00	Neutral
2021-04-30	335.34	340.00	Neutral
2022-04-13	247.07	275.00	Neutral
2022-10-11	224.36	255.00	Neutral

Date	Stock Price (US\$)	Price Target (US\$)	Rating
2022-12-14	258.75	265.00	Neutral
2023-07-31	367.44	380.00	Neutral

Source: UBS Global Research; Refinitiv as of 30-Oct-2023. All prices as of local market close. Ratings as of date shown.

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