Trane Technologies (TT)

Updated March 8th, 2020 by Eli Inkrot

Key Metrics

Current Price:	$113	**5 Year CAGR Estimate:**	2.1%	**Market Cap:**	$27.5 B
Fair Value Price:	$80	**5 Year Growth Estimate:**	7.0%	**Ex-Dividend Date:**	03/12/20
% Fair Value:	141%	**5 Year Valuation Multiple Estimate:**	-6.6%	**Dividend Payment Date[1]:**	03/31/20
Dividend Yield:	1.9%	**5 Year Price Target**	$112	**Years Of Dividend Growth[1]:**	9
Dividend Risk Score:	X	**Retirement Suitability Score:**	X	**Last Dividend Increase:**	8.2%

Overview & Current Events

Prior to February 29th, 2020, Ingersoll-Rand Plc was an industrial manufacturer, founded in 1871, focused on products, services, and solutions to enhance the quality, energy efficiency and comfort of air in homes and buildings, along with transporting and protecting food and perishable items. The business was operated under two segments: Climate (roughly ~80% of the business) and Industrial (~20% of the business).

On April 30th, 2019 Ingersoll-Rand announced a definitive agreement to merge its industrial segment with Gardner Denver Holdings (GDI) and spin-off this segment to shareholders.

On February 29th, 2020 this transaction was completed, with Gardner Denver taking the Ingersoll-Rand name and ticker, along with the Ingersoll-Rand and Club Car brands. The remaining Climate portion of the business was renamed Trane Technologies (ticker: TT) and began trading on March 2nd, 2020. This is the business we will focus on in this report. Trane Technologies is a pure-play global climate innovator. Through the company's leading Trane and Thermo King brands, the company provides products and services to bring efficient and sustainable climate solutions to buildings, homes and transportation. The $27 market cap company employees 36,000 people worldwide.

On January 29th, 2020 Ingersoll-Rand released Q4 2019 results for the period ending December 31st, 2019. For the quarter Ingersoll-Rand reported $4.15 billion in net revenue, a 6.6% increase, driven by a 6.1% increase in the Climate segment and an 8.2% increase in the Industrial segment. Adjusted operating income equaled $502 million, compared to $469 million previously, while adjusted earnings-per-share totaled $1.40 versus $1.32 in the year ago quarter. For the year, Ingersoll-Rand generated $16.6 billion in revenue, a 5.9% increase compared to 2018. Adjusted operating income equaled $2.23 billion compared to $2.01 billion previously, while earnings-per-share totaled $6.37 versus $5.61 in 2018.

Full year 2020 guidance for Trane Technologies, now trading with the ticker "TT" was provided, which excludes the Industrial segment that has combined with Gardner Denver. The company expects $13.5 - $13.7 billion in revenue and a 15.3% - 15.7% adjusted operating margin, along with debt repayment and share repurchases.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	$2.23	$2.82	$3.29	$2.08	$3.33	$3.73	$4.13	$4.52	$5.61	$6.37	***$5.00***	***$7.00***
DPS	$0.28	$0.59	$0.64	$0.84	$1.00	$1.16	$1.36	$1.70	$1.96	$2.12	***$2.12***	***$2.96***
Shares[2]	328	297	296	278	263	261	259	249	242	244	***244***	***230***

Note that the historical numbers show the previously combined Ingersoll-Rand business, while our forecast only incorporates the new Trane Technologies, hence the decline in earnings for this year.

From 2008 through 2019, Ingersoll-Rand grew earnings-per-share by a compound rate of 8.2% per annum. This is a reasonable historical barometer as it incorporates a full business cycle (the company generates solid profits, but it is susceptible to economic cyclicality). We have forecast 7% earnings growth for Trane Technologies over the intermediate term.

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[1] Estimate

[2] In millions.

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Moving forward Trane Technologies has a healthy growth outlook due to the continued expansion of the global economy, as well as a strong North American housing market. Another long-term growth catalyst is technology and innovation designed to solve climate-related issues. We are upbeat on the growth prospects of both the business and the industry, but we are cognizant of its cyclical nature.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	16.7	14.3	12.9	28.1	18.1	16.7	15.6	19.0	16.6	17.8	***22.5***	***16.0***
Avg. Yld.	0.8%	1.5%	1.5%	1.4%	1.7%	1.9%	2.1%	2.0%	2.1%	1.9%	***1.9%***	***2.6%***

Since 2010 (excluding 2013 when reported earnings dipped) shares of Ingersoll-Rand traded hands with an average P/E ratio of about 16 times earnings. We think this is a fair starting multiple for Trane Technologies as well, weighing the solid growth prospects with the occasional cyclicality and unknown of the new pure-play company. This would imply a fair amount of valuation headwind from this point.

Meanwhile, the dividend has room to grow, but the starting yield is more or less average at this point.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	13%	21%	19%	40%	30%	31%	33%	38%	35%	33%	***42%***	***42%***

Trane Technologies' competitive advantages are its strong brands and investments in product innovation.

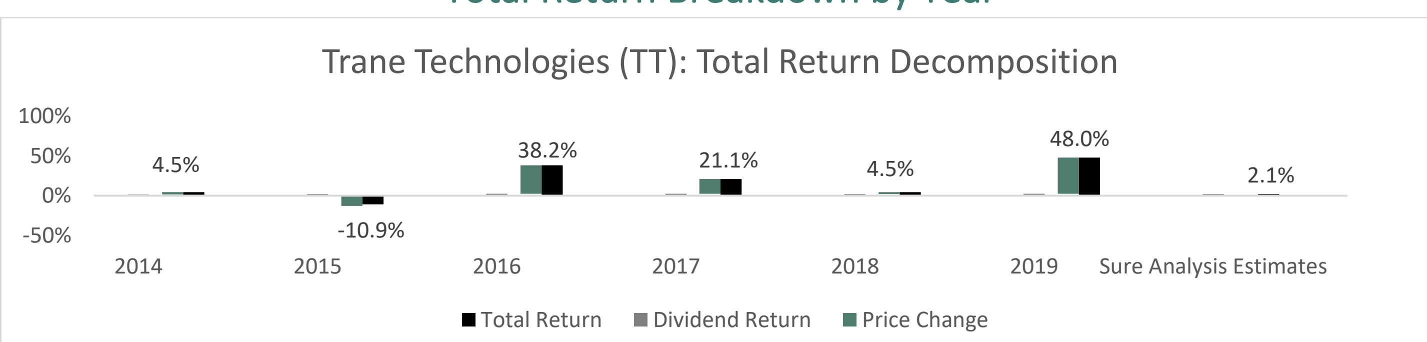
During the last recession Ingersoll-Rand reported earnings-per-share of $2.69, $1.41, $2.23 and $2.82 for the 2008 through 2011 stretch. Additionally, the dividend was reduced from $0.50 in 2009 down to $0.28 in 2010. We expect Trane Technologies to perform similarly. While the bounce back performance is admirable, the company is still sensitive to economic downturns. Moreover, rising inflation and tariffs could provide additional risks.

At yearend, on a pro-forma basis, Trane Technologies held $3.2 billion in cash, $7.0 billion in current assets and $18.2 billion in total assets (with goodwill and intangibles making up 46% of assets) against $4.2 billion in current liabilities and $12.1 billion in total liabilities. Long-term debt stood at $4.9 billion.

Final Thoughts & Recommendation

Trane Technologies is a new pure-play climate solutions company. While the name is new, this company carries forward the majority of the legacy Ingersoll-Rand shareholders' economic interest. The business has performed well since the last recession, but we are mindful of the possibility of lackluster results should (or perhaps more accurately when) another recession comes along. We forecast 2.1% total returns, driven by 7% growth and the 1.9% dividend yield, offset by a valuation headwind. We rate shares as a hold.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	14,001	12,761	11,988	12,351	12,891	13,301	13,509	4,198	5,668	16,599
Gross Profit	3,941	3,481	3,455	3,628	3,909	4,023	4,201	4,386	4,821	5,147
Gross Margin	28.1%	27.3%	28.8%	29.4%	30.3%	30.2%	31.1%	31%	30.8%	31.0%
SG&A Exp.	2,680	2,395	2,383	2,523	2,504	2,532	2,598	2,721	2,903	3,130
D&A Exp.	437	359	334	334	332	364	352	353	362	397
Operating Profit	1,261	1,086	1,072	1,105	1,405	1,492	1,603	,665	1,917	2,018
Op. Margin	9.0%	8.5%	8.9%	8.9%	10.9%	11.2%	11.9%	12%	12.2%	12.2%
Net Profit	642	343	1,019	619	932	665	1,476	1,303	1,338	1,411
Net Margin	4.6%	2.7%	8.5%	5.0%	7.2%	5.0%	10.9%	9.2%	8.5%	8.5%
Free Cash Flow	516	970	952	849	740	639	1,339	1,302	1,042	1,665
Income Tax	228	45	56	189	294	541	282	80	281	354

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	19991	18844	18482	17658	17299	16718	17397	18173	17915	20,492
Cash & Equivalents	1014	1161	708	1937	1705	737	1715	1549	903	1,304
Acc. Receivable		2136	1870	2072	2119	2151	2223	2477	2679	2,798
Inventories	1401	1278	1144	1166	1359	1411	1386	1555	1678	1,712
Goodwill & Int.	11433	10438	9543	9463	9174	9656	9444	9679	9594	10,932
Total Liabilities	11932	11828	11253	10527	11253	10838	10679	10966	10850	13,180
Accounts Payable	1319	1224	1019	1163	1290	1249	1334	1556	1705	1,809
Long-Term Debt	3684	3643	3229	3521	4224	4218	4070	4064	4091	5,573
Total Equity	7964	6928	7148	7069	5987	5817	6644	7140	N/A	7,312
D/E Ratio	0.46	0.53	0.45	0.50	0.71	0.73	0.61	0.57	N/A	0.76

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	3.2%	1.8%	5.5%	3.4%	5.3%	3.9%	8.7%	7.3%	7.4%	7.3%
Return on Equity	8.5%	4.6%	14.5%	8.7%	14.3%	11.3%	23.7%	18.9%	N/A	19.7%
ROIC	5.6%	3.1%	9.6%	5.9%	8.9%	6.5%	14.1%	11.8%	N/A	11.7%
Shares Out.	328	297	296	278	263	261	259	249	250	244
Revenue/Share	41.20	37.61	38.60	41.40	47.00	49.67	51.62	55.01	62.65	67.92
FCF/Share	1.52	2.86	3.07	2.85	2.70	2.39	5.12	5.05	4.17	6.81

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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