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# Otis Worldwide Corp. (OTIS)

Q2 2024 Earnings Call

## CORPORATE PARTICIPANTS

**Michael Rednor**

*Vice President-Investor Relations, Otis Worldwide Corp.*

**Judith F. Marks**

*Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

**Anurag Maheshwari**

*Chief Financial Officer & Executive Vice President, Otis Worldwide Corp.*

**Cristina Méndez**

*Senior Vice President-Finance & Chief Financial Officer-EMEA, Otis Worldwide Corp.*

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## OTHER PARTICIPANTS

**Jeffrey Todd Sprague**

*Analyst, Vertical Research Partners LLC*

**Nigel Coe**

*Analyst, Wolfe Research LLC*

**Julian Mitchell**

*Analyst, Barclays Capital, Inc.*

**C. Stephen Tusa**

*Analyst, JPMorgan Securities LLC*

**Joseph O'Dea**

*Analyst, Wells Fargo Securities LLC*

**Justin Pellegrino**

*Analyst, Melius Research LLC*

**Nick Housden**

*Analyst, RBC Capital Markets*

**Jack Ayers**

*Analyst, TD Securities (USA) LLC*

**Miguel Borrega**

*Analyst, Exane BNP Paribas*

## MANAGEMENT DISCUSSION SECTION

**Operator:** Good morning and welcome to Otis's Second Quarter 2024 Earnings Conference Call. This call is being carried live on the Internet and recorded for replay. Presentation materials are available for download from Otis's website at [www.otis.com](http://www.otis.com).

I'll now turn it over to Michael Rednor, Vice President, Investor Relations.

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### Michael Rednor

*Vice President-Investor Relations, Otis Worldwide Corp.*

Thank you, Sara. Welcome to Otis's second quarter 2024 earnings conference call. On the call with me today are Judy Marks; Anurag Maheshwari, and Cristina Méndez. Please note, except where otherwise noted, the company will speak to results from continuing operations excluding restructuring and significant non-recurring items. A reconciliation of these measures can be found in the appendix of the webcast. We also remind listeners that the presentation contains forward-looking statements which are subject to risks and uncertainties. Otis's SEC filings, including our Form 10-K, and quarterly reports on Form 10-Q, provide details on important factors that could cause actual results to differ materially.

Now I'd like to turn the call over to Judy.

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### Judith F. Marks

*Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

Thank you, Mike, and good morning, afternoon, and evening everyone. Thank you for joining us. I hope all are safe and well. I'd like to welcome Cristina Méndez, who is joining us this morning on our earnings call. Cristina is an experienced executive who's been leading our finance team as CFO in the EMEA region for the past two and a half years, while also leading our global finance transformation under our UpLift program. I look forward to my partnership with Cristina to drive growth, operational execution, and value for our customers, colleagues and shareholders. I want to also take this opportunity to thank Anurag for his leadership and for all his contributions to our company, our services growth, and in championing our long term strategy.

Now, for earnings, starting with Q2 highlights on slide 3. Otis delivered a solid second quarter in the face of current economic challenges within China as the Service segment continued to drive strong performance. Service organic sales grew mid-single digits. Overall adjusted profit margin expanded by 110 basis points, and adjusted EPS grew 15%, marking our fourth consecutive quarter of 10% or greater adjusted EPS growth. With Service as our primary growth driver, we have set ourselves up well for the future by delivering maintenance portfolio growth of 4.2% and building our modernization backlog by 17% in the quarter. As a result of our steady business execution and capital allocation strategies, we generated \$353 million in adjusted free cash flow, and returned \$300 million to shareholders through share repurchases in the quarter, taking year-to-date repurchases to \$600 million.

In June, we published our 2023 ESG report, outlining our progress towards our 13 ESG goals, explaining how this progress advances our business strategy while driving value for stakeholders. Importantly, this report includes a detailed description of our Scope 1, 2, and 3 greenhouse gas emission reduction goals. And we've continued to make progress towards our goals in 2024, including recently receiving ISO 45001 Certification, the international

standard that specifies the requirements and good practices for effective occupational health and safety management systems at our factory in São Bernardo, Brazil.

Moving to our orders performance on slide 4. New Equipment orders were down 11% in the second quarter. High single digit growth in EMEA, driven by mid-teens growth in the Middle East, and low to mid-single digit growth in Asia-Pacific, was more than offset by a mid-teens decline in the Americas and a double digit decline in China. Our New Equipment backlog at constant currency was down 3% versus the prior year. In the Americas, we are seeing the impact of elevated interest rates on our New Equipment orders. In China, economic softness severely impacted our New Equipment orders, while orders grew in both Asia-Pacific, due to continued strength in the region, and EMEA, as our investment in product and coverage continues to perform well.

In our Services (sic) [Service] (00:04:44) segment, progress continued to pace with portfolio growth above 4% for the seventh consecutive quarter, along with 14% modernization orders growth, and continued growth in our modernization backlog, which increased 17% at constant currency. We had several exciting customer highlights in the second quarter, thanks to the dedication of our colleagues across all of our regions. In India, at the heart of the city of Delhi, Otis will install 12 sky rise units at the iconic Unity The Amaryllis Versace. Designed by Versace Home, this luxury development is one of the tallest residential buildings in Delhi.

We continue to perform well in the infrastructure segment, as evidenced by our next three major project highlights. In the United States, Otis is supporting the expansion of Terminal 3 West at San Francisco International Airport. As part of this project, Otis will install 15 new Gen3 elevators and 13 Link escalators while modernizing two elevators. SFO served more than 50 million passengers in 2023, and these upgrades will increase overall passenger capacity and international access.

In Germany, we are installing eight escalators for our long established customer, the City of Stuttgart. We'll dismantle the non-OTIS escalators that are currently in use and install our heavy traffic public escalators at four metro stations in the city center. In China, we've continued our more than 30-year relationship with the Shanghai Metro, booking several contracts in the quarter that total more than 475 units, including 311 escalators and moving walks for Line 23, 32 elevators, and 115 escalators for the new Chongqing Line, and 19 elevators for an extension of Line 12.

Turning to Q2 results on slide 5, Otis delivered net sales of \$3.6 billion, with organic sales down 1%. Adjusted operating profit, excluding a \$15 million foreign exchange headwind, was up \$38 million, driven by the Service segment. Adjusted EPS grew approximately 15% or \$0.14 in the quarter, driven by strong operational performance, and improvement in our tax rate. Benefits from minority interest and a lower share count offset headwinds from foreign exchange translation, and an increase in interest expense.

With that, I'll turn it over to Anurag to walk through our results in more detail.

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## Anurag Maheshwari

*Chief Financial Officer & Executive Vice President, Otis Worldwide Corp.*

Thank you, Judy. Starting with Q2 segment sales performance on slide 6. Total organic sales were down 1% in the quarter, driven by New Equipment, which was down 9% compared to the prior year. APAC grew approximately 10%, driven by strong performances in Southeast Asia and India, while the Americas grew low single digit. EMEA experienced a low single digit decline due to continued weakness in Central Europe, while China declined double digits, largely due to the deterioration in market conditions.

New Equipment pricing was strong outside of China, up low to mid-single digits. China remains under intense price pressure, and although pricing in China was down year-over-year, it came in approximately flat sequentially, while the cost environment remains deflationary. Service sales were \$2.2 billion, with organic sales growth of 5.1%, marking over three years of mid-single digit or greater growth in every quarter.

We grew in all regions at all lines of business, including approximately 5% in maintenance and repair as a result of strong portfolio growth, solid repair volumes and maintenance pricing, which was up 3.5 points, excluding the impact of mix and churn. Driven by continued double digit growth in Asia Pacific, mod organic sales increased about 6% in the quarter, and 8% in the first half.

Turning to Q2 segment operating performance on slide 7, New Equipment operating profit of \$110 million was down \$6 million at constant currency, mainly due to the impacts of lower volume and mix headwinds. Pricing outside of China, productivity, including benefits from UpLift, and commodity tailwinds largely offset the volume and mix impacts, netting to improved margins of 30 basis points to 7.7%, ahead of our expectation.

Service operating profit of \$538 million increased \$51 million at constant currency as drop through on higher volume, favorable pricing, and productivity, including benefits from UpLift, more than offset annual wage inflation. This led to margin expansion of 110 basis points in the quarter. Our focus on cost control, alongside the ramp of UpLift initiatives drove lower SG&A absolute dollars, while improving our adjusted SG&A as a percent of sales by 30 basis points year-over-year.

For the first half, despite an inflationary environment, our SG&A dollars reduced by approximately \$30 million and improved by 30 basis points as a percent of sales. We are very pleased with our progress in UpLift across the three levers we've outlined, with benefits ramping quicker than anticipated. Our streamlined functional structure is yielding productivity benefits while allowing us to leverage our global scale to drive cost savings, especially with our digital technology operations, and other indirect spend. With solid Service performance, and while navigating a challenging New Equipment environment, we expanded overall operating profit margins by 110 basis points, and grew adjusted EPS \$0.14 or 15%.

Shifting to cash, despite lower New Equipment orders, we generated \$353 million of free cash flow in the second quarter and we expect to largely reverse the working capital build by year end. Overall, we had a very strong first half performance, overcoming weakness in the China market. We grew organic sales 1.2%, led by performance in the Americas, EMEA and Asia Pacific, which were up mid-single digits, as well as strength in our Service segment. This growth, in conjunction with good traction on UpLift, productivity, pricing, and commodity tailwinds helped us expand margins by 100 basis points and grow EPS 13%, positioning us well for the second half.

Let me now turn it back to Judy to discuss our 2024 outlook.

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## Judith F. Marks

*Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

Now on slide 8, before turning to our updated 2024 financial outlook, let me briefly update you on our industry outlook. For the New Equipment market, our expectations for the Americas and EMEA remain unchanged, down low single digit in units. We now expect Asia to be down high single digits in units versus the prior outlook of down mid-single digits, driven by weakness in China. There is no change to our outlook for Asia-Pacific as the region has continued to perform well. We're revising China to be down 10% to down 15% as activity is weaker than we previously expected.

While New Equipment markets remain under pressure, we continue to see strength in the Service market, with low single digit growth in the Americas and EMEA, and mid-single digit growth in Asia. The global install base is expected to grow mid-single digits in 2024, adding roughly 1 million units from units that were installed within the last two years, and are now rolling off their warranty period.

Turning to Otis's 2024 financial outlook, we now expect sales in the range of \$14.3 billion to \$14.5 billion, with organic sales growth of 1% to 3%. While we see continued strength in the Service business for the remainder of the year, this decrease in organic sales versus our prior outlook is driven by New Equipment, which Anurag will discuss in a moment.

Adjusted operating profit is in line with prior expectations, still expected to be up \$135 million to \$175 million at actual currency, and up \$160 million to \$190 million at constant currency. Adjusted EPS is now expected in the range of \$3.85 to \$3.90, up 9% to 10%, with \$0.02 improvement versus the low end of the prior guide, driven by strong operational performance, and a benefit from a lower share count. We anticipate adjusted free cash flow to come within a range of \$1.5 billion to \$1.6 billion.

Before handing it back to Anurag to outline the 2024 segment outlook in more detail, let me turn to slide 9 to provide an update on Project UpLift and our progress to date. We now anticipate run rate savings of \$175 million by mid-2025, as we have made solid progress executing on the program. Two areas where we're seeing additional benefit versus our prior expectations are through further streamlining of our global operating model, and incremental optimization of indirect spend in areas such as digital technology and infrastructure. As we exit 2024, our anticipated end year savings are now slated to be approximately \$60 million, with a 2024 exit run rate of approximately \$100 million. Overall, program is on track, we're performing well versus our internal benchmarks and timeline, and we look forward to sharing additional updates with you in the coming quarters.

Anurag, over to you.

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## Anurag Maheshwari

*Chief Financial Officer & Executive Vice President, Otis Worldwide Corp.*

Thank you, Judy. Taking a more detailed look at our outlook and starting with sales on slide 10. We now expect total organic sales to be up 1% to 3%. Overall, New Equipment organic sales are now expected to be down mid-single digits from market-driven decline in China, which we now expect to be down approximately 20%. The outlook for the Americas, EMEA and Asia Pacific remains unchanged, up mid-single digits combined. Service organic sales are anticipated to grow 6% to 7%, in line with prior guidance. This includes maintenance and repair within a range of 5.5% to 6.5%. And for modernization, we anticipate growth of 8% to 9% as solid orders momentum and an expanding backlog provide good line of sight to achieve approximately 10% growth in the second half.

Turning to slide 11. At constant currency, operating profits should grow \$160 million to \$190 million, unchanged versus prior expectations, with improving contributions from Service and productivity, including UpLift, offsetting New Equipment volume and mix headwinds. In Service, we now expect operating profit margin to expand approximately 75 basis points, an increase of 25 basis points versus the prior guide, driven by solid volumes and even better productivity.

For New Equipment, despite the weakness in China, operating profit margin is expected to be roughly flat versus the prior year, a change versus our prior estimate of flat to up 10 basis points. Productivity and pricing are offsetting the added volume and mix impact from a weaker China outlook. We now expect overall adjusted operating profit margin expansion of 80 basis points as a result of Service volume, productivity, and pricing

tailwinds. This represents a 30-basis point improvement versus our prior outlook. Turning to cash flow, we expect to achieve adjusted free cash flow in the range of \$1.5 billion to \$1.6 billion with net income growth, partially offset by changes in working capital.

Moving to the 2024 EPS bridge on slide 12. We have raised the low end of our outlook for adjusted EPS by \$0.02 to a range of \$3.85 to \$3.90. At the midpoint, this is \$0.34 of EPS growth versus the prior year, driven by operational performance. At constant currency, we expect approximately \$0.32 of operating profit growth level loaded between the first and the second half. Reductions in the effective tax rate and a lower share count more than offset headwinds from higher interest expense and Forex.

In closing, first half results demonstrate our ability to continue performing despite macro headwinds. There is a lot in our control in the second half, and we are focused on growing our portfolio, leveraging our expanding mod backlog, while ramping on the UpLift program, and driving productivity throughout the organization. This sets us up well to achieve a full year outlook of approximately 10% EPS growth, in line with our medium term guide.

With that, Sara, please open the line for questions.

## QUESTION AND ANSWER SECTION

**Operator:** Thank you. [Operator Instructions] Your first question comes from the line of Jeff Sprague with Vertical Research Partners. Your line is open.

**Jeffrey Todd Sprague**

*Analyst, Vertical Research Partners LLC*

Thank you. Good morning, Judy, Anurag and Cristina.

Q

**Judith F. Marks**

*Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

Good morning, Jeff.

A

**Jeffrey Todd Sprague**

*Analyst, Vertical Research Partners LLC*

Good morning. I guess, first, Anurag, we're going to miss you, but I'm guessing we're not really going to miss you, but do you have anything to say about what your plans are?

Q

**Anurag Maheshwari**

*Chief Financial Officer & Executive Vice President, Otis Worldwide Corp.*

There's more to come here, but focused on closing the earnings call right now and a smooth transition with Cristina. Thanks for the question, Jeff.

A

**Jeffrey Todd Sprague**

*Analyst, Vertical Research Partners LLC*

Awesome. Judy, can we drill a little bit more just into China? Obviously, it's kind of readily apparent, things are just challenging there from a macro standpoint. But I think you noted Service was growing mid-single digit in Asia.

Q

I don't know if you said China. If you did, I missed it. Maybe just give us a little bit more color on sort of the counteractions you're taking there to kind of support and drive profitability in-country.

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**Judith F. Marks**

*Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

A

Yeah, thanks, Jeff. And great to be with you this morning. Our Service business in China, specifically, units are up high teens for another quarter. Mod orders are up high single digit, mod sales are up double digit, and we're really pleased with the pivot we've made. And now this is now a multi-year strategy we've been implementing to have a greater focus and yield in China on Service. Almost a third of our revenue now in China is in Service. And that's twice what it was when we spun.

Our portfolio has more than doubled and is up again this quarter, as I said, high teens. So, our service strategy is coming up nicely, and we're seeing the acceleration of mod in China and anticipate that to continue to move double digit as we look out into the medium term for China. The New Equipment market does remain weak. We called it down 15% for the second quarter after being down 10% in the first quarter, but with what we know on the ground from Sally and the team, for the full year, we're saying it's going to be down 10% to 15%.

Our team has done a really nice job in being able to manage the cost side in a very competitive market, but that market this year we're saying for China is going to be between 425,000 and 450,000 units. Again, focused on growing Service, continuing to drive out cost in a deflationary environment, but always balancing price and volume so that we make sure that our backlog remains healthy in China. 425,000 to 450,000 units is still a very nicely sized market, but this is the third year of decreases, and I think our strategy and implementation has pivoted to Service to be able to reflect that.

It's why we took our guide down in terms of top line revenue now to be organic 1% to 3%. That is all driven by this New Equipment decline there, but as you could see with our profitability this quarter for the first half, even our profit margin expansion in New Equipment, despite being down several hundred million dollars of revenue, you're seeing the resilience in not just our Service-driven model, but I think you're seeing, again, sustained quarter-after-quarter, year-after-year performance in those items that we control.

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**Jeffrey Todd Sprague**

*Analyst, Vertical Research Partners LLC*

Q

Great. Thank you for all that color. Appreciate it. I'll pass the baton.

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**Operator:** Your next question comes from the line of Nigel Coe with Wolfe Research. Your line is open.

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**Nigel Coe**

*Analyst, Wolfe Research LLC*

Q

Thanks. Good morning. And Anurag, you'll be missed, but again I'm pretty sure you're going to pop up somewhere soon. Cristina, congratulations on the promotion. So, just want to pick up on the baton on the China question. I'm just wondering, is there any change in your strategy which has been clearly focused on gaining the share, and is there now more of a focus on preserving margin there? And I'm just curious on the NCI, kind of expense being flat at \$100 million. That seems to indicate that China EBIT is actually holding up rather well. So, just curious if there's a change in strategy and that comment on margins.

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**Judith F. Marks**

*Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

A



Yeah, let me take the first one and I'll turn over to Anurag, although we're kind of fighting over the second one because we both want to answer it. So Nigel, it's no change in strategy. What you're probably not seeing behind the scenes is how our team has, again, continued to pivot. We continue to do product introductions and we continue to drive delivery in terms of our orders through our agents and distributors. Our agents and distributors, again, think about 2,400 of them, a lot of them have also taken on modernization as well. So, we've expanded their remit so that we continue to prepare for the future, which is going to be a more mod-heavy future regardless of what happens structurally on the New Equipment side.

So, the strategies, it's on track. We know what we're doing there. We've had significant China share gain since spin, but we're not going to take on loss-making units for the sake of share gain. And that's something I've been telling you now quarter after quarter, and we're going to be consistent with that methodology versus giving up price and then having that negative piece in the backlog. We just don't think that's – we don't need that for our business, and we don't think it's wise. But Anurag, I'll let you touch on the second half.

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**Anurag Maheshwari**

*Chief Financial Officer & Executive Vice President, Otis Worldwide Corp.*

A

Yeah. Thanks, Judy. So, Nigel, if you look at the New Equipment market in China, it is clearly challenging and the revenue in the second quarter was down as well, double-digit as we said. Okay. The reason you don't see on the NCI line is because we're able to manage the volume headwind through productivity, through growing our Service business. And it's not only all across all the other regions, it's also in China as well. So, we do what we can control. So, from a margin perspective and a profit perspective, we've been able to preserve it.

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**Judith F. Marks**

*Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

A

Yeah. The last thing I'll add on NCI is our Middle East business has picked up at a very good pace. It's one of several highlights for EMEA, and you see EMEA orders are up, EMEA is strong in revenue, and EMEA is a large modernization opportunity for us, including the Middle East. Outside of China, the majority of our remaining NCI is in the Middle East, Nigel.

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**Nigel Coe**

*Analyst, Wolfe Research LLC*

Q

Okay. That's great. Thanks. That's great color. And then, one quick one for Anurag. I want to make sure that he works before he leaves. So, the free cash flow kept down to [ph] \$1.5 billion (00:26:01). Is that a function really of the New Equipment weakness we're seeing, and therefore we're seeing kind of a headwind on advance payable – advance deposits from customers? Is that really what's happening here or is there something else we need to consider?

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**Anurag Maheshwari**

*Chief Financial Officer & Executive Vice President, Otis Worldwide Corp.*

A

Yeah, thanks. I think you got it pretty much, but let me give a little bit more color, right? In the first half, we built about \$300 million of working capital and probably due to two reasons. The first reason, what you mentioned, on New Equipment orders, we typically receive down payments and that order environment has obviously been challenging for the first half. But second, which I think is the largest driver, is that the Service business grew faster than the New Equipment business and we tend to be cash ahead in New Equipment while we collect in Service after we perform the work.

So, these two are the drivers which got us to build \$300 million of working capital. So, for the back half of the year, we expect to generate about \$825 million in GAAP net income. And if you reverse about \$200 million or more in working capital, that will get us closer to the \$1.6 billion. We, of course, will look to do better like the same way as we did in the second half of last year, and especially in receivables. And if the New Equipment orders do a little bit better than expected, then this could be a source of upside and we could get us to about \$1.6 billion of free cash.

**Nigel Coe***Analyst, Wolfe Research LLC*

Q

That's great. Thank you.

**Operator:** Your next question comes from the line of Julian Mitchell with Barclays. Your line is open.

**Julian Mitchell***Analyst, Barclays Capital, Inc.*

Q

Hi, good morning and congratulations to Anurag and Cristina. Maybe just my first question is really on that New Equipment organic sales outlook sort of globally and then more with a focus on the Americas, I suppose, not so much China. So, the backlog was down 3% year-on-year in June, your sales are down, I think in the back half in New Equipment, mid-single digits. But I wondered kind of how much of a lead time now we're getting from that backlog into your revenues for 2025.

If I look at the Americas, for example, your TTM orders were down mid-teens in New Equipment, but you're still guiding revenue this year up mid-single. So, in something like the Americas, does the confluence of those two things mean 2025 sales in New Equipment are almost certainly down a reasonable amount and then any sort of broader global color on that?

**Judith F. Marks***Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

A

Sure, Julian. I think it's a great question and very, very – it's the right analysis. Let me first give you an overview of New Equipment backlog around the globe, and then let me specifically dive into the Americas. We were down 3% and our 12-month rolling New Equipment orders are obviously down 7.7%. The Americas backlog, though, is up low single-digit. EMEA is up low single-digit. Asia-Pac is up mid-teens, and China is down obviously, which is driving Asia down for the broader picture.

Our New Equipment outlook right now is to exit 2024 at the company level, flattish to slightly down as we expect, backlog could fall in the second half, but it's really going to get defined by the New Equipment second-half orders. And our line of sight to second-half orders look strong, especially in the Americas and some other region. And let me just tell you, we have about an 18-month line of sight to the Americas, the majority of it being North America, in terms of performing our backlog. And as I said, the Americas backlog is up low single-digit. The New Equipment sales in the Americas came in as expected in the second quarter, low single-digit, year-on-year comps as well as major projects. We anticipate that picking up in the second half.

We also anticipate the New Equipment orders in the second half for the Americas to be positive. We can see that based on proposal activity, we can see that based on awards we have that haven't yet been booked, and we believe you'll see that starting to come through in the third quarter.

**Julian Mitchell**

*Analyst, Barclays Capital, Inc.*

Q

That's very helpful. Thank you. And then, just maybe a more sort of near-term fiddly question, just maybe for Anurag, as we think about that second half outlook, do we just assume kind of sequentially EPS is down both quarters Q3 and Q4 to a similar degree? Any sort of color on that second half intra-quarter split?

**Anurag Maheshwari**

*Chief Financial Officer & Executive Vice President, Otis Worldwide Corp.*

A

I'll just start off with the first half, second half, and Cristina can give more color on Q3 as well. So, we've done about \$1.94 of EPS in the first half, and midpoint of our guide is \$3.88, which implies another \$1.94 in the second half, right? So from an operational perspective, it's equal between the first half and the second half. Cristina will give a little bit more color on Q3.

**Cristina Méndez**

*Senior Vice President-Finance & Chief Financial Officer-EMEA, Otis Worldwide Corp.*

A

Thank you, Anurag. Happy to give you some color on Q3. So with interest expenses at the current run rate and tax rate growing to 27% in Q3, would expect roughly EPS flat in the quarter. That would mean that full year EPS will go up \$0.34. That is the midpoint of the guide, and that means [ph] \$0.22 (00:31:44) up in the first half, probably flat in Q3, and just over \$0.10 in Q4.

**Julian Mitchell**

*Analyst, Barclays Capital, Inc.*

Q

That's great. Thank you.

**Judith F. Marks**

*Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

A

Yeah, and Julian, let me just correct myself quickly. The backlog total ex-China is up low single-digit, but the Americas backlog is down.

**Julian Mitchell**

*Analyst, Barclays Capital, Inc.*

Q

Got it. Thank you.

**Operator:** Your next question comes from the line of Steve Tusa with JPMorgan. Your line is open.

**C. Stephen Tusa**

*Analyst, JPMorgan Securities LLC*

Q

Hey, good morning.

**Judith F. Marks**

*Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

A

Hi, Steve.

**C. Stephen Tusa**

*Analyst, JPMorgan Securities LLC*

Q

Again, Anurag, thanks for all the help, and congrats on all the promotions there, everybody. Just a question on China, what are you guys seeing price-wise there, and at what stage does that start to impact backlog margin? And then, is there any risk that, that market gets to the point where it starts impacting services growth as basically just your pipeline there of installs that then come off warranty a couple of years later start to be a headwind to services growth? I know it's still a small part of the global portion, but just those two questions, price and margins, and then when it starts to impact services growth.

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**Judith F. Marks**

*Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

A

Yeah, well, let me take price and when it impacts services, and I'll let Anurag comment on margins. It is a very competitive environment in China. Pricing is challenged and is down, I would say, roughly 10%, but the costs are coming down. So again, in a deflationary environment, whether it's commodities, whether it's the productivity that we're doing, we're pulling costs out. We've got tailwinds on commodities and we're driving productivity. So, we'll continue to monitor that. Steve, I think we are seeing – we've been saying it's competitive there now for three years on pricing, I don't anticipate that changing, but our team continues to respond well on the cost side.

In terms of how that converts, when you look at our Service portfolio in China, again, we're now – we said last quarter we were over 400,000 units. We're now at about 415,000 units, growing nicely. A lot of that's conversion, and our conversion rates are doing well in China. We're pleased with that continuing to move up as we've set in our medium-term guide. But part of that's also recapturing and adding on non-Otis units. So at 425,000 units, we've got a 4% market share. So there's ample opportunity for us to bring non-Otis units and Otis units that aren't under our portfolio back. So, all those activities are going to happen simultaneously, and we believe we can continue mid-teens to high-teens growth in China portfolio for the medium term. So, we don't believe that's going to roll into a service impact for us. Anurag?

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**Anurag Maheshwari**

*Chief Financial Officer & Executive Vice President, Otis Worldwide Corp.*

A

Yeah. Thanks. As Judy mentioned, right, so one of the biggest drivers for us is going to be on the margin side volume for sure on Service. If you look at the market over the past three years, it's been down, but the reason our portfolio grew is because of conversion rates improving, and there's still more to come on the conversion rates as it goes along. So, I think we feel fairly confident on the volume growth over there. On the cost side, clearly, the earlier question that Nigel asked as well, the reason why the NCI was where it was because of how we're able to maintain our profitability is looking at a cost piece. One is we are fortunate in China to be in a deflationary economy in terms of supply chain, so that helps us, but also we've looked at the footprint that we have both in terms of the branches, in terms of facilities, and we'll continue to take a look at it to kind of bring the cost down. So, we feel a combination of volume and productivity, and on the cost side will help us keep the margins or maybe expand the margins going forward.

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**C. Stephen Tusa**

*Analyst, JPMorgan Securities LLC*

Q

Great. Thanks a lot.

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**Operator:** Your next question comes from the line of Joe O'Dea with Wells Fargo. Your line is open.

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**Joseph O'Dea**

*Analyst, Wells Fargo Securities LLC*

Q

Hi, good morning. I wanted to ask about the modernization backlog, and if you could talk about the pricing within that backlog and what kind of line of sight you have to continue margin expansion in mod and any quantification of that, that we could see over the next few quarters.

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**Judith F. Marks**

*Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

A

Yeah, Joe, listen, we added delivering modernization value as a fifth strategic imperative last year to really mobilize the company to industrialize how we're doing mod and to take us from a position that you know where mod margins were below New Equipment to a place where not only would they meet New Equipment margins but exceed them. We did that last quarter and first quarter. We've repeated that this quarter with our medium term guide to get mod margins up to at least double digit, and 10% as a starting point. We are on that trajectory. I'm pleased with that progress.

The orders for mod continue to do well. Our company's responding very well. We're putting together the right kits to meet the customer needs as the demand signal is growing significantly. What we need to do is take those orders and that backlog, which is up 17% and the orders were up 13.8% with growth in all regions, and we need to – while we're continuing to grow orders, we need to grow our conversion to sales in modernization. And we need to pick up that pace with installers. We need to pick up that pace with the kits now being supplied from our new industrialized processes. It's early days there, but you're going to continue to see that.

So, mod margins heading in the right direction on the trajectory we had shared. And we continue to see the mod strategy is intact. And you're going to continue to see significant modernization growth quarter-after-quarter, and I believe year-after-year as we go through the medium term and beyond.

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**Joseph O'Dea**

*Analyst, Wells Fargo Securities LLC*

Q

And then, can you just talk to China, kind of cycle perspective, when you talk about a market 425,000, 450,000 units and down for a few years now. Just kind of any indications you see around where that can go, how you get comfortable with, at least at a volume level, market doesn't get much worse.

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**Judith F. Marks**

*Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

A

Yeah, so again, it's been three straight years. We peaked at about 650,000 units a year, and now we're guiding to 425,000 to 450,000 for this year, which is a pretty significant drop. And yet, if you look at our team's profitability across these three years and the return from our China team, I couldn't be more proud of how they've taken cost out. They're continuing to look at areas, UpLift, structural facilities, infrastructure organization, as Anurag alluded to. So, we've dealt with that well while simultaneously growing our Service business. So, you're going to see more and more service there over time.

Listen, I can't and won't call a bottom. I don't know what that is. The Chinese government has put into play many simultaneous activities to try to stimulate both local government financing, as recent as the third plenary, as well as the PBOC reduced rates this week, multiple activities. To-date, we have not seen that change consumer sentiment or the buying sentiment in properties yet. There is still a demand for hundreds of millions of Chinese residents to move from rural to urban. So, we don't believe that will change. That's the plan and the path that the Chinese government has been on now for two decades and we believe that's going to continue. And we think we've got the right strategy and we've sized the business and moved more to Service and modernization to be able to handle that.

I will share, Joe, earlier this week, we actually hosted Premier Li at one of our facilities in TEDA in the Tianjin region. It was a proud moment for us to host the premier. And what we focused on, as you can imagine, was beyond all of the automation we have and how Otis has been a part of China and will be celebrating 40 years there this fall, we did focus on urban renewal and modernization and our ability to continue to drive energy efficient solutions, especially as China modernizes. 10 million units in the install base in China that are now aging and it's going to create a significant modernization demand that we are preparing for, and I would tell you we're ready for now.

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**Joseph O'Dea**

*Analyst, Wells Fargo Securities LLC*

Q

That's great color. Thank you.

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**Operator:** Your next question comes from the line of Rob Wertheimer with Melius Research. Your line is open.

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**Justin Pellegrino**

*Analyst, Melius Research LLC*

Q

Good morning, everybody. This is Justin Pellegrino on for Rob, and congratulations to Cristina and Anurag, again. Our question is kind of around mods as well, and there's been continued impressive growth. Can you just put that in context of sales effort? Is that more outreach? And I know, Judy, you touched on looking for better conversions. Is it more market awareness of the product? Can you just tell us what's kind of driving that impressive growth? Thanks.

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**Judith F. Marks**

*Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

A

Yeah, I mean, one of the clear areas, Justin, is just literally aging equipment and obsolescence and demand. I mean, of the 20 plus million, 22 million units in the install base, over 7 million are 20 plus years older, and many of those 30 plus years older. The largest market for that right now is in EMEA, and we're excited with our offerings there. What makes this different now is we're getting away from custom mod and bespoke mod and industrializing this. And when we introduced our Gen3 product to the market a year or two ago, we did it with the vision that we would have that offering modular, available across the globe, a connected offering that would not just fulfil New Equipment drives, whether it's Gen360 in EMEA and now China, but Gen3 globally that we could then also package as a modernization opportunity.

So, as we brought out these products, the beauty of it is, as we're educating the New Equipment sales team, we're educating the mod sales team. And as our installation crews from New Equipment are more familiar with Gen3, now they're doing Gen3 mod. So, we're attacking every part of this while attacking the cost side, because now we're buying Gen3 at scale from our sub-suppliers and the manufacturing elements we do ourselves, and all of it is coming together nicely, which is driving the margins.

But from a sales standpoint, we've simplified it. We have these relationships with customers. Think about our Service portfolio at 2.3 million units, just on our portfolio. We have relationships with these Service customers every day. Those are our mod customers. And when we go on portfolio, most of that work we can talk about, we can help them capital plan, we can create if there's obsolescence, we can be more – it can be more proactive than reactive. And all of that is coming together at a time when the demand is growing. So, we're ready for this. And I think you're seeing – I know you're seeing those results in mod, and you're going to continue to see them.

**Justin Pellegrino***Analyst, Melius Research LLC*

Wonderful. Thank you.

Q

**Operator:** Your next question comes from the line of Nick Housden with RBC Capital Markets. Your line is open.

**Nick Housden***Analyst, RBC Capital Markets*

Yeah, hi, Judy, Anurag, Cristina. Yeah, thanks for taking the question. I'd like to ask about the maintenance and repair business. So, the 4.9% organic growth, I mean, it's not a bad number overall, but it does look like the slowest growth in quite a few quarters. So, I'm just wondering if you can maybe provide some color about what's going on there and whether it's maybe some of the above-trend growth that we've been seeing in the repair business coming off. Thanks.

Q

**Judith F. Marks***Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

Yeah, I think you somewhat answered it, Nick. We have been seeing double-digit repair business now for three years. Originally, it was the post-COVID snapback, but then we've just seen really healthy repair growth. We believe that growth is going to grow again in the second half of the year. So, it's not lumpy, but on occasion, again, we've guided in the past that as maintenance grows, you should think of repair growth as 1 point higher than that. That would say, as our portfolio grows 4-plus-percent, repair should grow 5-plus-percent. We've been exceeding 10% now for almost three years in repairs, so I think it's fair to think a little high single digit more for the second half, and that's a fair expectation.

A

**Nick Housden***Analyst, RBC Capital Markets*

Okay. Great.

Q

**Anurag Maheshwari***Chief Financial Officer & Executive Vice President, Otis Worldwide Corp.*

Yeah, the only thing I'm – just one thing, if I could just add to that is, if you look at the comp from last year where the second quarter was the highest in terms of repair growth, the repair, as Judy has mentioned, is still growing at very good high-single digit, if not double digit in the back half of the year.

A

**Nick Housden***Analyst, RBC Capital Markets*

Okay. Great. And then, Judy, I think you mentioned 10% lower prices in China, I'm guessing year-over-year. Is that a like-for-like comment, or is that price and mix? Because I think the 10% number is similar to what one of the competitors called out recently.

Q

**Judith F. Marks***Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

Yeah, it's year-over-year, and it's like-for-like.

A

**Nick Housden***Analyst, RBC Capital Markets*

Okay. Great. Thank you very much.

Q

**Operator:** Your next question comes from the line of Gautam Khanna with TD Cowen. Your line is open.

**Jack Ayers***Analyst, TD Securities (USA) LLC*

Hi, guys. How's it going? This is Jack Ayers on for Gautam today.

Q

**Judith F. Marks***Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

Hi, Jack.

A

**Jack Ayers***Analyst, TD Securities (USA) LLC*

And Anurag and Cristina, yeah, congrats everyone on the transitions here. It's been a pleasure working with you, Anurag. So, a quick question, just, Judy, if you can maybe square us on some of the New Equipment order trends, just by geography. Totally understand China and America weakness, but looks pretty good in EMEA and Asia Pacific, ex-China. So, maybe if you can maybe just square us just the divergence there. And then, back to the pricing comment, I guess, is that 10% down like-for-like, is that just kind of like organic pricing down? Are you seeing any poor actors maybe trying to gain share or maybe just hit on the ISPs if that's kind of influencing pricing trends in China? Just any color there would be helpful. Thanks.

Q

**Judith F. Marks***Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

Yeah, Jack, on your second question, the ISPs don't play in the New Equipment pricing. So, we're not seeing anyone, any of the other OEMs, from what we can see in the market, operating any differently than we've seen them operate in the past. Let me give you some color though on EMEA and APAC because they deserve that color. It's been really nice to see in a challenging EMEA market, we're performing really well in terms of orders. Obviously, watching interest rates and everything going on there, but for the quarter, our Central Europe business performed well, our Southern Europe business performed well, and our Middle East business has performed very well. France and UK were a little weaker, but the backlog's solid. And there, you've now seen, whether it's 12 months, last quarter, this quarter, our EMEA team's doing a really nice job, again, in a challenging market when you think about other macro trends that we don't control.

A

Our Asia-Pacific business, in the second quarter, we saw some slowing in India, but that was because of the ongoing elections. That is going to pick up significantly for the second half of the year. Korea, still some challenges. Taiwan, a little down, but our orders were up in Japan and Australasia, and the backlog is up very healthy. So, we expect Americas to snap back in third quarter and second half of the year in orders. We expect continued significant orders growth in Asia-Pacific. And our EMEA team, again, whether it's by our operating units, by our sales team, major projects, volume business, our Gen360 products doing very well, and I'm really pleased on the infrastructure segments globally.

You saw the three we called out, whether it's Shanghai Metro, Stuttgart, or San Francisco. There are many more infrastructure jobs that we've been winning, and that gives us the opportunity, whether it's, again, low-rise, mid-



rise, high-rise, or escalators, it's our full product line. And with those infrastructure jobs, we tend to get longer service commitments as well. So all of those trends, again, Americas will snap back, China will remain challenged, and the other two businesses will continue to perform well as we see the second half of the year. And as I shared, I think it was one of the early questions, and maybe it was even Julian's, is this is where we'll know how 2025 looks. So, we'll know based on backlog how we look in 2025 and 2026 a little as we exit 2024 based on those orders in the backlog for the second half.

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**Jack Ayers**

*Analyst, TD Securities (USA) LLC*

Okay. Great. Thanks, Judy. Appreciate it.

Q

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**Judith F. Marks**

*Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

You bet.

A

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**Operator:** Your next question comes from the line of Miguel Borrega with BNP Paribas. Your line is open.

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**Miguel Borrega**

*Analyst, Exane BNP Paribas*

Hi, good morning, everyone. Thanks for taking my questions. The first one on New Equipment, can you give us some kind of color on why the margin expanded despite revenues being down 9%? Is this purely on the back of a better mix with China down double digits and Americas up, or is there was something else within Q2 that lifted the margin? I would imagine China margin is not up, and you mentioned New Equipment pricing outside of China being up low to mid-single digit, did that contribute to a higher New Equipment margin outside of China?

Q

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**Anurag Maheshwari**

*Chief Financial Officer & Executive Vice President, Otis Worldwide Corp.*

Thanks for the question. So, firstly, just to ground everyone, China New Equipment is our largest margin region in Otis. So, it's actually, when China volume goes down, it's a mix headwind for us. It's not a mix tailwind for us. [indiscernible] (00:51:32) was able to offset the mix, which is [ph] actually quite (00:51:35) substantial for the quarter, because if you look at our revenue down a couple of \$100 million, and that too, essentially, in China on the New Equipment side, and that causes about a \$40 million, \$50 million headwind. We were able to offset that because of pricing and our backlog from the other regions, which was positive, commodities, productivity, and the benefits of UpLift. So, we control what we can control, and as we've gone through this call, China is an important New Equipment market, we all appreciate that, but I think the other regions, plus productivity, have been more than able to offset that as a result of which you saw the margin expansion.

A

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**Judith F. Marks**

*Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

Yeah. Good afternoon, Miguel. This is Judy. Just one other thing I think it's important to know is that, as we look at China for this year, China revenue, all in, versus Otis revenue will be 15% or less. So, it's continued – what that says is, we're going to grow organically 1% to 3% in revenue, and that means the other three regions are growing, while China and – denominator is growing, while China continues to obviously run into some economic headwinds, especially in New Equipment.

A

**Miguel Borrega**

*Analyst, Exane BNP Paribas*

Q

That's great. Thank you. And then, the second one, just to understand a little bit better the organic growth in maintenance, 4.9%, given that the portfolio growth was 4.2%. So, aside from repairs, is there anything else that contributed to the slower growth relative to the other quarters, the 70 basis points above portfolio growth? Can you provide some color on price, mix and churn, and how has that changed over previous quarters?

**Anurag Maheshwari**

*Chief Financial Officer & Executive Vice President, Otis Worldwide Corp.*

A

Yeah, the portfolio growth, 4.2%, consistent previous quarters. The pricing, 3.5%, adjusting from without mix and churn, that's also pretty consistent. The reason it's a little bit on a relative level, 4.9% slower growth, is because of the comp from the previous year driven by repair business. So, if you look at, as we go into the second half, portfolio will continue to grow at 4-plus-percent, pricing looks good, repair should be back to high single-digit, double-digit, and a combination of that will get us towards the 6.5%, 7%.

**Miguel Borrega**

*Analyst, Exane BNP Paribas*

Q

Thank you very much.

**Operator:** This concludes the question-and-answer session. I'll turn the call to Judy for closing remarks.

**Judith F. Marks**

*Chairman, President & Chief Executive Officer, Otis Worldwide Corp.*

Thank you, Sara. Our results in the first half reflect the strength of our Service-driven business model as we remain focused on delivering value for our shareholders in the balance of 2024 and beyond. I want to once again thank Anurag and wish him well in his future endeavors, while also expressing my excitement to partner with Cristina, as together we both look forward to meeting with investors and analysts in the near future. Everyone, please stay safe and well. Thank you very much.

**Operator:** This concludes today's conference call. Thank you for joining. You may now disconnect your lines.

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