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CORPORATE PARTICIPANTS

Zac Nagle *Ingersoll-Rand PLC - VP of IR*

Mike Lamach *Ingersoll-Rand PLC - Chairman & CEO*

Sue Carter *Ingersoll-Rand PLC - SVP & CFO*

CONFERENCE CALL PARTICIPANTS

Shannon O'Callaghan *UBS - Analyst*

Nigel Coe *Morgan Stanley - Analyst*

Steve Tusa *JPMorgan - Analyst*

Joe Ritchie *Goldman Sachs - Analyst*

Andrew Obin *BofA Merrill Lynch - Analyst*

Deane Dray *RBC Capital Markets - Analyst*

Seth Garcia *Citigroup - Analyst*

Steve Winoker *Sanford C. Bernstein & Co. - Analyst*

PRESENTATION

Operator

Good morning. My name is Tracy, and I will be your conference operator today. At this time, I would like to welcome everyone to the Ingersoll-Rand fourth-quarter and FY16 earnings conference call.

(Operator Instructions)

Now I would like to introduce Mr. Zac Nagle, Vice President of Investor Relations. You may begin your conference.

Zac Nagle - ***Ingersoll-Rand PLC - VP of IR***

Thanks, operator. Good morning. Thank you for joining us for Ingersoll-Rand's fourth-quarter and FY16 earnings conference call. This call is also being webcast on our website at ingersollrand.com, where you will find the accompanying presentation. We're also recording and archiving this call on our website.

Please go to slide 2. Statements made in today's call that are not historical facts are considered forward-looking statements and are made pursuant to the Safe Harbor Provisions of Federal Securities Law. Please see our SEC filings for a description of some of the factors that may cause actual results to differ materially from anticipated results. This presentation also includes non-GAAP measures which are explained in the financial tables attached to our news release.

The participants on this morning's call are Mike Lamach, Chairman and CEO, and Sue Carter, Senior Vice President and CFO. With that, please go to slide 3, and I will turn the call over to Mike.

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

Thanks, Zac, and thank you to everyone for joining us today. 2016 was another great year for Ingersoll-Rand, a record year, and we hit the mark on all the critical financial metrics. We'll get into some more detail on that in just a minute.

I would like to start this morning by talking about our business strategy and how that has enabled us to deliver another year of top-tier performance in 2016. Then, Sue will discuss performance in the fourth quarter, we'll give some color on our 2017 markets and guidance, and I will close with addressing topics we know are on the minds of investors, before Sue and I take your questions.

As I said, 2016 was a record year for Ingersoll-Rand. It follows a multi-year pattern of consistently strong operating and financial performance driven by our strategic framework of sustained growth, operational excellence, excellent cash flow conversion, and a commitment to our winning culture. Our strategic objective is to drive profitable growth through leadership positions in growing markets that are durable because they address a global imperative to dramatically reduce energy demand and resource constraints in buildings, homes, industrial, and transport markets around the world.

Turning to slide 4, in 2016 we extended our multi-year record of top-quartile performance on organic revenue growth, incremental margins, earnings growth, free cash flow, and total shareholder return. We delivered free cash flow of approximately $1.3 billion on 3% organic revenue growth, and operating margin expansion of 60 basis points to 11.6%. Free cash flow was 121% of adjusted net income and more than $5 per outstanding share.

Adjusted operating margin leverage was 44%. Adjusted continuing EPS of $4.13 was up 11%, demonstrating the strong leverage of the Business.

We also retained a strong balance sheet with good optionality, while at the same time returning significant cash to shareholders, paying roughly $350 million in dividends and executing $250 million in share buybacks. We continued our long history of raising our corporate dividend, and in 2016 we raised our quarterly dividend by approximately 40% through two increases from $0.29 per share to $0.40 per share. We are now at $1.60 annualized per share.

I said throughout 2016 that rigorous execution would serve us well, drive leverage in the P&L, and deliver strong cash flow and margin expansion, even in a low growth environment. We followed our business operating system to capture growth, improve costs, and drive productivity, all of which translated into 60 basis points of margin expansion.

2016 growth was led by North American commercial and residential HVAC. The teams here are doing a phenomenal job of share gain and margin expansion. We anticipate this momentum to continue into 2017.

While North American HVAC led the growth, we made deliberate choices in the selection of growth programs across the whole portfolio, and then we operationally led those programs through product growth teams. We see break-out results with this strategy. The average growth rate for our model product growth teams was more than twice our overall Company average growth rate for the year.

We also drove significant innovation, launching more than 80 new products and services in 2016, with introductions happening in nearly every business and region. We realized benefits of new product and technology investments as the offerings supported our 2016 growth, share gains, and margin expansion. I emphasize this to demonstrate our commitment to organic long-term strategic investment and innovation to remain ahead of our customers' expectations, the competition, and the regulatory environment.

And heading into 2017, we haven't slowed down with our focus on product growth teams. A couple of weeks ago, we launched our personal transportation vehicle called Onward to the consumer market, resulting in a 10% order increase above our initial launch plan.

Getting back to 2016, we also continued our multi-year trend of service, parts, and solutions growth in both segments. HVAC aftermarket outpaced equipment growth annually with high single-digit growth, ex foreign exchange.

In Compression Technologies, we also realized 3% growth in our aftermarket business. This consistent performance against our strategy to deliver higher service penetration across our segments helps build strong relationships with customers and a more resilient business portfolio. As anticipated, we continue to see more and more growth within our portfolio stemming from smart, wireless, and digitally connected solutions in 2016 that are more reliable, more cost effective, and energy efficient.

Each one of our business units is executing a digital strategy, and we are a recognized leader in this area. Our Energy Services and Controls business, for example, is actively servicing 6,500 connected buildings. We are one of the top providers in the space. Anticipated growth rate here is approximately 30% for 2017.

The diversity of our business portfolio helps to mitigate cyclicality in our end markets, which has enabled us to sustain strong performance over time. Growth teams dedicated to our lines of business help us create real value using a wide range of technologies and innovation. Our objective is to take advantage of growth when the market is in an upswing, and to build on our competitiveness in difficult markets.

Moving to slide 5, the measure of our success is represented by our financial results and total return to our shareholders. Slide 5 demonstrates our consistent performance over time and the metrics that matter to our shareholders, whether it's revenue growth, adjusted EPS growth, cash flow, ROIC, or adjusted operating margin improvement. 2016 was another excellent year that extends this track record, a record year and one we're proud of. Now I would like to turn the call over to Sue to comment on the fourth quarter.

Sue Carter - ***Ingersoll-Rand PLC - SVP & CFO***

Thank you, Mike. Please go to slide number 6. I would like to begin with a summary of main points to take away from today's call. As Mike discussed, 2016 was a very strong year for Ingersoll-Rand and marked another year of continued top-tier performance on free cash flow, organic revenue growth, operating margin improvement, and earnings-per-share growth.

While we recognize the fourth quarter contained more one-offs and noise than any of us would have liked, and distorted our fourth-quarter earnings report, fundamentally it was still a strong quarter for the Company relative to our core businesses. There shouldn't be any significant read-through to our go-forward results.

Free cash flow was more than $350 million in the quarter, bringing our 2016 free cash flow to $1.35 billion, which is up 37% versus 2015, or more than 120% of our adjusted net income. From a segment perspective, the combined climate and industrial segments' adjusted operating income results were solid and a bit better than our expectations for the quarter.

Our bookings performance was very strong, with commercial and residential HVAC leading the way, with both at low-teens growth. Residential revenues increased low teens. Operating margins also expanded in both businesses. We were pleased with our Industrial Business performance, which showed slow but steady adjusted margin improvement after hitting a low in the first quarter.

We continue to take additional actions on operational excellence initiatives, increased commercial focus on aftermarket parts and service offerings, and took additional cost reduction activities to improve operating results going forward. EPS in the quarter was negatively impacted by discrete items in G&A, negative other operating income, and taxes, as I will discuss on the next slide.

Please go to slide 7. We've provided a bridge from the fourth-quarter guidance range we provided on our Q3 earnings call to our actual Q4 results. As I noted earlier, our segment operating performance was in line with our expectations, actually about $0.01 better.

We incurred higher-than-expected corporate costs primarily due to stock-based and other incentive-based compensation given our strong cash flow performance and stock performance in 2016, and from increased information technology infrastructure and security expenditures. These items combined for a negative impact of about $0.04.

We expect our corporate G&A expenses to come back down to a more normalized run rate of about $60 million per quarter in 2017. We also incurred higher-than-expected non-operating costs as a result of foreign exchange losses related to the balance sheet given the strengthening of the US dollar, which had a non-cash impact of $0.01.

Lastly, we had a higher-than-expected mix of earnings from high-tax jurisdictions, which impacted us by about $0.03. While this was a significant negative in the fourth quarter, our adjusted tax rate for the year of 21.4% was on the low side of the 21% to 22% range we updated on our second-quarter call. I feel good about the effective tax rate. And more importantly, we expect the rate to remain in the 21% to 22% range for 2017 as well.

Please go to slide number 8. Top-line organic growth of 2% was solid, highlighted by our North America HVAC businesses. Operating margins, and adjusted operating income plus depreciation and amortization, were both down, primarily driven by industrial segment margin declines and the higher-than-expected costs we previously discussed.

Please go to slide 9. Organic orders were very strong in the fourth quarter, up 7%, led by our climate segment and partially offset by modest declines in our industrial segment. Climate bookings were up in every region and business globally, and up 10% overall.

Organic commercial HVAC bookings were up low teens in Equipment, with strong results from both Unitary and Applied products. We also continued to drive excellent growth in service, controls, and contracting with low-teens growth in the quarter. Residential bookings continued to be exceptional, up low teens.

Organic transport orders were up mid-single digits, primarily driven by growth in Europe, partially offset by declines in marine equipment and auxiliary power units. We also had mid-single-digit increase in North America trailer orders in the fourth quarter. On balance, the industrial businesses' bookings were flat to down slightly in the quarter, reflecting some stabilization in end markets.

Please go to slide number 10. This slide provides a directional view of our segment revenue performance by region. In our Climate segment, revenue was strong in North America, flat in Asia, and down in Europe, Middle East and Africa, and Latin America. In our Industrial segment, overall performance was down low-single digits, primarily due to difficult comparisons with 2015 on large air compressor shipments in North America, and Europe, Middle East and Africa. Revenues improved in Latin America and Asia. Overall, North America revenues were up mid-single digits, and international revenues were down mid-single digits, netting a positive 2% organic revenue growth rate for the Enterprise.

Please go to slide number 11. Q4 operating margin declined 50 basis points, primarily due to headwinds resulting from material inflation in steel, and higher corporate costs in the quarter. On a year-over-year basis, lower industrial margins also contributed to the decline. Volume and mix was positive in the quarter.

Please go to slide number 12. Overall climate performance was strong in the quarter, with organic revenues up 4% and adjusted operating margins up 70 basis points to 13.6%. Strong revenue growth in both commercial and residential HVAC was partially offset by transport revenues, which were down mid-single digits in the quarter, primarily due to weak auxiliary power unit and marine markets partially offset by growth in aftermarket and in Asia.

Climate operating margins expanded 70 basis points year over year. Favorable volume, mix, and productivity was partially offset by material inflation headwinds and continued investment in the business.

Please go to slide 13. Fourth-quarter industrial margins declined by 220 basis points compared with 2015, while organic revenues declined 3%. Revenues were down mid-single digits in compressors, with growth in aftermarket. Other industrial products were down by high-single digits, with Material Handling showing the largest decline -- more than 50% -- owing to its significant oil-and-gas exposure. Small electric vehicles were up slightly in the quarter from growth in Golf.

Industrial's operating margin of 10.5% was down 220 basis points versus the prior year, but in line or slightly ahead of our expectations for the quarter. Looking forward, we expect margins to improve in 2017 given ongoing margin improvement actions, although we do expect some quarterly variability due to cyclicality.

Please go to slide 14. Excellent full-year 2016 free cash flow of $1.3 billion improved 37% versus the prior year, and was over 120% of net income. Strong operating income and working capital improvement were the primary drivers of the improvement. For the quarter, working capital as a percentage of revenue was 3.4% versus our 2016 goal of 4%, and improved 80 basis points versus 2015.

We have a proud history of returning cash to shareholders. Since 2011, our free cash flow as a percentage of net income has averaged 100%. Over the same time frame, we've returned more than $6.5 billion in cash to shareholders through dividends of $1.5 billion and share buybacks of $5.1 billion.

Please go to slide 15. Our strong cash performance in 2016 will enable us to, one, invest in our Business as our number-one priority. These include investments in innovation and in strategic growth programs, as Mike outlined earlier. In addition to the core strategic investments, we're also investing in long-term growth through innovative and differentiated products in areas such as wireless, controls for buildings as a resource, intelligent monitoring, and self-healing systems, just to name a few.

Two, we've paid an annual dividend for 106 years and have consistently raised this dividend over time. Over the past five years we've raised our annual dividend at a 20% compound annual growth rate. In 2016 we raised our annualized dividend from $1.16 to $1.60 per share, or nearly 40%.

Three, we also spent $250 million repurchasing sweeping shares sufficient to offset dilution. Four, additionally in 2016 we continued to develop and vet a pipeline of potential acquisition targets. And five, lastly, in 2016 we strengthened our balance sheet, which provides stability and optionality as our markets evolve. We also maintain a BBB credit rating, which at this time we believe is appropriate for the Company.

We will continue to create long-term value for our shareholders through a dynamic capital allocation strategy as we have consistently done for years. And with that I will turn it back to Mike to discuss our market outlook as we begin our guidance conversation.

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

Thanks, Sue. And if you move to slide 17 we will begin our guidance conversation with some color around our end markets. As always, our intention is to give you our best view as we know it today, and how that translates to our revenue outlook for 2017. We've broken it down by major end markets and geographies.

We expect North American commercial HVAC and residential HVAC to show continuing growth. In North America, 50% of our commercial business is parts, service, and controls, and we are seeing strong demand in all these areas, as well as for upgrades and energy retrofits. Residential replacement, which makes up approximately 80% of the total market, closed the year on a strong note, and we expect to see continuing growth next year in both replacement and new construction.

Commercial HVAC markets in EMEA and Asia are expected to be flat. We expect Latin America to be up mid- to high-single digits.

Transport markets in the Americas will be down from lower volumes for trailers and auxiliary power units, partially offset by trucks. North American trailer volumes are expected to decline by low teens. Transport in Europe is expected to be up, based on truck and trailer sales, and a bottoming of the marine container market. Asia Pacific was up high teens last year, and we expect continued growth in 2017 on its smaller base.

Global industrial markets are generally improving but still remain soft. We believe we are seeing a bottoming trend in our general industrial markets in the US and the Eurozone, as PMIs have improved over the last several months.

We have also seen some order improvement in our short-cycle industrial businesses. While this is a positive, the modest rise in industrial production suggests a gradual recovery, with bumps along the way. Industrial markets in Asia remain under pressure, due to excess capacity in many key industries.

The large engineered compressor market is expected to show signs of improvement due to stabilizing activity in energy markets and heavy industry. While expecting year-over-year orders to be up, revenue will decline due to depressed 2016 order levels and the average lead time of 12 to 18 months for this type of product. Excluding these longer lead time products, we expect our industrial segment to be flat to slightly up.

Golf and utility vehicle markets are generally flat to slightly up across all regions. Golf is expected to be flat, and we expect to see some growth in our consumer and utility vehicle markets.

All the growth forecasts shown are on an organic basis. We are forecasting mid-single-digit growth in Commercial HVAC in total, mid-single-digit growth in Residential HVAC which is essentially North American business for us, and revenues down low-single digits in Transport. We expect Compression Technologies and Industrial Products, which includes our power tools, material handling, and fluid management businesses, to be down low-single digits. We expect Club Car to be up low-single digits.

With that overview as a backdrop, we'll move into 2017 guidance. Before Sue takes you through guidance, I know some of you know that we recently completed in-depth interviews with the investment community to better understand how Ingersoll-Rand is perceived and what we might do better to improve in our communications. We just received the results and we will be incorporating changes that reflect investor feedback going forward. Thank you to all of you who participated.

One of the changes highlighted in the feedback was investor preference for the timing of Company guidance. Overwhelmingly, investors said they had a preference for annual guidance with quarterly updates, versus quarterly guidance. We have adopted this, beginning with the annual guidance for 2017.

Annual guidance is also much more aligned with the way in which we make decisions and manage the Business internally with our focus on building a better business over the long term. For those of you who prefer quarterly guidance, we'll get through the transition together and make sure it goes as smoothly as it can. And now I will turn it over to Sue with specifics on guidance.

Sue Carter *- Ingersoll-Rand PLC - SVP & CFO*

Thanks, Mike. Please go to slide 18. Moving on to our guidance, we expect total organic revenues to be up approximately 3% in 2017. We expect the climate segment to continue to show good growth of approximately 4% organic.

For the industrial segment, we expect the markets overall to be pretty flat, but for our organic revenues to be down slightly given the high volume of large compressors we shipped out of backlog in 2016, which will make for tougher compares in 2017. The difference between our organic and reported revenue contemplates about 1 percentage point of negative foreign exchange from a strengthening US dollar outlook.

For the Enterprise, we expect adjusted operating margins of between 12.2% and 12.6%. We expect adjusted operating margins for the climate segment to be in the range of 14.5% to 15%, and in the range of 11% to 12% for the industrial segment.

Please go to slide 19. We expect continuing adjusted earnings per share for 2017 to be in the range of $4.30 to $4.50, excluding about $0.15 of restructuring. The Company also provides the following guidance. Share count is expected to be approximately 262 million shares. Target free cash flow is 100% of net income. The tax rate is expected to be between 21% and 22%. Corporate, general and administrative expenses are expected to be approximately $240 million, and capital expenditures are expected to be approximately $250 million.

Please go to slide 20. Relative to the Company's plans for capital allocation, investing in the Business is our highest priority, so we continue to make investments in innovation and growth in things like wireless and digital, and connected capabilities, productivity, sustainability, and in our employees, just to name a few areas.

Paying a highly competitive dividend is also a key priority for us, and based on our most recent dividend raise last October to $1.60 per share, we expect to spend approximately $420 million on dividends in 2017. In 2017 we're also targeting spending approximately $1.5 billion between a combination of share buybacks and acquisitions. Maintaining a strong balance sheet also remains a priority, and provides us optionality as our markets continue to evolve.

Let's go to slide 21, and now I would like to turn the call back over to Mike to discuss a few of the key topics we know are on the minds of investors as we enter 2017.

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

Thanks, Sue. The first topic discussed is our US manufacturing base. I think you're all aware we operate on a region-of-use philosophy. We localize manufacturing and the supply chain to help us achieve greater speed to market and implement local product preferences. 95% of Ingersoll-Rand products sold in the US are manufactured in the US.

Regarding components, we are likely less exposed as compared to other diversified industrials, because of our focus on lean, and in particular, cycle time reduction. We've actually, through the years, been willing to sacrifice on price for faster delivery, meaning the source is coming from within the US. I think this issue is a bigger issue for companies that are importing finished goods into the US, such as consumer products or electronic companies. We are definitely a net exporter.

The second topic is around the US corporate tax rate. As you know, approximately 65% of our revenues are derived from the US, and therefore, we pay a significant amount of US corporate taxes. If there is a reduction in the US corporate tax rate, we would expect to benefit from it.

Turning to slide 22, I know we'll receive questions on the status of Industrial. Fourth quarter was above the guidance we gave in revenue and operating margin. We saw growth in several vertical markets, including food, pharma, and tech, as well as with our compressor aftermarket business which was up 3%, as I mentioned earlier. However, we continue to see soft markets in large compressors and in the energy markets.

We have seen some bottoming with orders for our shorter-cycle businesses, such as power tools and fluid management, both up in the fourth quarter. As I indicated earlier, we expect industrial markets to stabilize in 2017, although we cannot declare a definitive turning point. Excluding large compressors, we expect industrial to be flat to slightly up, and we do expect realized margin expansion through our operational excellence initiatives, new product launches, restructuring actions, and ongoing cost reductions.

Covering our transport business, you will recall last year we had a better-than-anticipated first half, and decline in activity in the second half, as we expected. For 2017 overall, we expect Thermo King revenues to be down low-single digits year over year. The North American trailer industry is expected to be down low teens year over year. We're also expecting a continuation for a relatively soft market for auxiliary power units and marine containers. Those declines will be partially offset by gains in Europe, Asia, and aftermarket revenues. Through restructuring and efficiency, we would expect only a minor erosion of record 2016 operating margins.

Going to slide 23, I will touch on currency as a headwind for us in 2017. About 35% or $4.8 billion of our revenues are outside of the US. Our 2017 forecast has built in the continuing strength of the US dollar, which will impact us most notably in the euro and Asian currencies. Overall we expect a 1% drag on our revenues from currency translation, which will have about a $0.10 negative impact on our EPS.

And finally, we know material inflation is top of mind. We have 10 basis points positive price covering material inflation in our guidance. And of course, we're working to increase that even further. We have been through various cycles. We have a strong history of capturing price to material inflation. This long track record of managing price demonstrates to shareholders the discipline that exists with our people, systems, and processes.

So, in closing, on slide 24, we've built a stronger, more valuable, and less cyclical Ingersoll-Rand. I'm proud of our employees who delivered a record 2016 performance, and that make us a more sustainable company in every way. I am confident in our Management team to execute our 2017 plan. We will maximize growth, and focus on productivity and costs where markets are not accelerating.

Our commercial and residential HVAC businesses are strong and focused on growth areas with equipment, controls, and service. Our transport refrigeration business is diverse and agile, and will execute their strategy, as they typically do. Our industrial businesses are focused on margin expansion as markets stabilize. As a result, I'm confident we'll continue to deliver top-tier financial performance.

With that, Sue and I will now be happy to take your questions.

QUESTION AND ANSWER

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

(Operator Instructions)

Your first question comes from the line of Shannon O'Callaghan from UBS. Your line is now open.

Shannon O'Callaghan - ***UBS - Analyst***

Good morning, guys.

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

Good morning, Shannon.

Shannon O'Callaghan - ***UBS - Analyst***

Hey, Mike, or maybe Sue, on the free cash flow, just remind us why it was so particularly strong in 2016? The working capital performance was great, looks like capex was a little bit lower, you're bringing that up? Just maybe refresh us on the dynamics of why you see that still being strong in 2017 but not quite a version of 2016?

Sue Carter - ***Ingersoll-Rand PLC - SVP & CFO***

Shannon, that's a great question for us. Free cash flow was really strong in 2016, because we really focused on all of the basic fundamentals. What we wanted was, we wanted our operating income to flow through to cash flow. So we were very focused on making sure that on the accounts receivable side that our terms for our customers were balanced with our terms for our suppliers.

We went after disputes. We went and talked to our customers that had past dues. We worked with the supply base on accounts payable terms, and we also did a lot of work on our inventory processes as part of the business operating system.

So we really, really focused on getting the operating income to drop through, getting the working capital to a level that was not only good but also sustainable, and then our spending on other items, we didn't limit anything on capex, to your point. We didn't do anything like that. We asked for good investments as a part of the business.

So we actually, you know, used free cash flow in a very good way in 2016, and we had a very good result. And I think another point to give you on -- not only was free cash flow excellent based on the performance of each of our businesses and the corporate folks, but it was also pretty evenly measured throughout 2016 as opposed to being a very lumpy free cash flow. So I think everything came together for that in 2016.

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

Sue won't say this but I'll say it. She did a great job, and her team, training the organization, something we had fun with called In the Know On Cash Flow. We had everybody in the organization go through that with the purpose to explain that everybody in the Company has something to do with cash flow.

People got excited about it, stories really started pushing through. I think that level of engagement is a factor somewhere in this that made a big difference around people really exceeding this.

Shannon O'Callaghan - ***UBS - Analyst***

Then, Mike, maybe on the strength on those climate bookings -- up 10% organic looks like you're gaining some share and have made a lot of new product investments? When you look across either the product type of Applied Unitary or the regions, any particular area that you feel you're particularly well positioned in terms of share gain?

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

Shannon, we just -- it was amazing in that it was across the globe, and it was across Unitary Applied and Controls, and Service. We were just across the board. We didn't have a single pocket of weakness anywhere in the world, which is reassuring to us. That's a broad-based approach, and that, I think, gave us confidence around the guidance we gave for the year around pretty good growth continuing into 2017.

Shannon O'Callaghan - ***UBS - Analyst***

Okay, great. Thanks.

Operator

Your next question comes from the line of Nigel Coe with Morgan Stanley. Your line is now open.

Nigel Coe - ***Morgan Stanley - Analyst***

Yes, thanks, good morning, guys. Great detail, by the way. Appreciate all the extra color in the slides. So I just wanted to come back to Shannon's question on the outgrowth? It does feel like you're gaining share pretty much across the board.

So a question that comes up a lot is how sustainable is that dynamic, and maybe you could just touch on what do you think is driving that outgrowth, particularly within commercial HVAC? And then equally, it does feel like you're lagging your big competitor in compression? Maybe just touch on that as well, Mike?

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

Yes. First, I would say, Nigel, that you have to go back and realize that it's been investments sustained over time and product launches occurring at a high rate for some time. I think we've got the best channel in the world, in terms of the people out there that are systems experts capable of bringing stuff to market.

We've got the largest, that we know of, field service force in the world around HVAC systems, over 4,500 people out delivering, that are employees of the Company. You combine that all together with investments in digital, and I feel like it's been not a flash in the pan around something happening in the fourth quarter. It's been good for a long time.

It's up to us to continue to innovate and continue the investment channel. Half the investments or more that we're making in 2017 go back into the channel itself, not just into product. When you look at compression technology, similar investments happening there, and we're seeing good growth on the service side.

You had passed reference to Copco, you have to look at Copco, and there's a five-point swing just in currency. Copco would have shown a three-point gain. We show a two-point headwind in currency, five-point net.

When you back out and look at organic growth, I think they were minus five, we were minus four. There's always subtleties in the business. But we're all in the compressor business looking forward to brighter days. I don't think there's a read-through when you do the side by side math between Copco and us around a difference in performance.

Nigel Coe - ***Morgan Stanley - Analyst***

Okay, that was pretty helpful. And then on the capital allocation, the $1.5 billion of the target, what does that mean? Does that mean that there's an ambition to deploy that amount but if there's no opportunities you won't? How do you think about that toggle between M&A and share buybacks? And this time next year if you haven't deployed that capital, why would that be?

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

Yes, I think you had it right in your note this morning, Nigel. $1.5 billion is what we're saying we're targeting to deploy in 2017. And $250 million of that, we've already said, look, that's going to control any kind of dilution in share count, leaves $1.25 billion left, and we're going to be really smart about how to deploy that.

So very patient, very selective around the M&A front, and we're going to be patient around share repurchase. But between the two we expect to deploy $1.25 billion. And we're just going to update you as we go through the year.

It's difficult to forecast that on an EPS basis because, certainly on share count, it matters when and where you buy shares during the year, if they're averaged back in. M&A clearly on a GAAP basis, EPS accretion is difficult to see in a partial year, maybe even within the first full year. So it's difficult to forecast that, it’s dependent on the actual target.

Nigel Coe - ***Morgan Stanley - Analyst***

Okay, that's helpful. Thanks.

Operator

Your next question comes from the line of Steve Tusa from JPMorgan. Your line is now open.

Steve Tusa - ***JPMorgan - Analyst***

Hey, guys, good morning.

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

Good morning, Steve.

Steve Tusa - ***JPMorgan - Analyst***

Just a follow-up to Shannon's question on free cash flow -- you talked about how you kind of focused this year on all these moving parts? I guess, is 2017 -- was there some pull-forward into 2016? 2017 is down.

I wouldn't have expected it to be down that much. You have talked about the conversion rate as being sustainable and obviously above 100% is good, but just down year-over-year by the magnitude. Just curious if there was anything unusual about that 2016 performance?

Sue Carter - ***Ingersoll-Rand PLC - SVP & CFO***

No, there was really nothing that was unusual about the 2016 performance, Steve. What I did is, I looked at 2017, as I did a couple of things. One, on working capital, I was really allowing working capital to go back up to around the 4% level. And I will tell you why.

As our markets are a little bit lumpy, choppy, some of them recovering, I want to make sure that our businesses have the option to have inventory on hand so that not only can we meet customer requirements, but that we can meet on-time delivery requirements. So I'm giving us room for a little more working capital, and really I'm primarily talking about inventory in terms of 2017.

The other part of that is our capital expenditures are actually going up a bit year-over-year. I gave you a guide of $250 million. And really the majority of the increase in the capex year-over-year is really in our factories, in productivity producing projects, and things like primarily precision machining, and in the factory. So I gave a little room for all of that, and that really takes it down to the $1.1 billion to $1.2 billion level.

Steve Tusa - ***JPMorgan - Analyst***

Okay, that makes some sense. Then the restructuring you guys are doing, you know, it's a bit of a step-up. Just curious as to why you're stepping that up now, given the strong kind of volume picture on orders? Where specifically is that going?

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

Steve, so fundamentally on that, we're really going to discuss sort of where that's going as we deploy it, because we want to make sure that we're in front of that internally versus speaking to it externally. In a lot of the cases where we've been sort of on the fence with doing some things, we found opportunities within those business cases.

Examples might be where real estate values would have changed on the underlying idea, and so there might be an opportunity to consolidate a footprint that we didn't have in the past. So there's a fair bit of that going on as well. So we've got sort of ideas around that $50 million, and we're going to update you as we go but it's a good place holder for now.

Steve Tusa - ***JPMorgan - Analyst***

And the payback on that?

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

Yes. On the $50 million, we'll probably see $10 million in 2017, then we'll go to something more full run rate, probably $20 million in 2018 on that $50 million.

Steve Tusa - ***JPMorgan - Analyst***

Great. One last question, just on the first quarter. Maybe my clients are going to hate me because they don't want guidance anymore, but I think it's good to at least have a nice framework out there. Normal seasonality, at least how we calculate it, gets me into kind of the low to mid-50% from an EPS perspective? Is that too far off?

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

From a seasonality perspective, Steve, we went back over five years, and we're pretty much now I think dialing in. So first quarter usually is kind of 10% to 12% of the EPS for the year, then we're kind of a front half-back half 45%, 55% sort of Company. You shouldn't get too far off with that sort of math.

Steve before you cut off, too, I want to thank you for spending so much time as you did at the AHR Show [with their team]. They really appreciated you stopping and spending time with them.

Steve Tusa - ***JPMorgan - Analyst***

Oh, thanks. I love HVAC. You know that.

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

We do, too.

Operator

Your next question comes from the line of Joe Ritchie, Goldman Sachs. Your line is now open.

Joe Ritchie - ***Goldman Sachs - Analyst***

Hey, good morning, guys.

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

Good morning.

Joe Ritchie - ***Goldman Sachs - Analyst***

First, so I guess my first question is maybe just touch a little bit on price cost? Clearly a little bit of a headwind in 4Q, and talk a little bit about what kind of pricing you think you can get through across your portfolio in 2017? And to the extent that you can talk about cadence, that would be helpful as well?

Sue Carter - ***Ingersoll-Rand PLC - SVP & CFO***

Let me start out and give you some basic parameters around this. So we knew going into Q4 that we were going to be in an inflationary environment for steel. Pricing did not offset the inflation in the fourth quarter, so we were down 40 basis points as you saw on the slides and heard from our commentary.

As we look at 2017, we've got that currently pegged at price over material inflation at about 10 basis points, really working towards trying to get back to our norm of 20 to 30 basis points. But let me talk a little bit about what's happening in 2017. So if you think about what drives the material inflation, it's really all around steel.

The non ferrous, so the copper and aluminum, first of all were locked about 68% on copper going into 2017, but those should be relatively flat. So neither inflationary or deflationary as we see it right now. Steel has two components to it, one of which is just the raw commodity that's there, and then an even bigger part of that is actually the tier 2 materials that contain steel that become inflationary.

One of the questions that I ask our group and wanted to pass on as we think about that is, my question was can we just really negotiate with the supply base and part of this is really on how we've done contracts and written in escalation clauses. So long story short, steel and components that contain steel are going to be inflationary in 2017, and like I say, we'll continue to work price as we go throughout the organization.

Now, when you think about price and you think about different areas, we've been successful at getting price in both of our segments in 2016, and I think we'll get price in both segments in 2017. Asia is going to be tough. That one is an interesting market. Some of the others, again, price is not for us just a catalog and a price on a particular item.

We're baking price into every engineered-to-order type of project as we go along. So again, pricing is going to be a work in progress. I think there is going to be a little pressure on that as we go into 2017, but inflation comes from steel.

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

Joe, recognizing you've been with us now a couple of years, but if you go back all the way to 2010, I know personally, even late 2009, we put in place and have been adapting and training to all the methods and tools for pricing and systems around the Company. So there is a lot of rigor in the operating system around that, a lot of reporting, remediation, and mitigation around that.

So on a topic like this, you would have to go back to a seven-year record of every year being able to deliver on that. I don't suggest that it's going to change in 2017, so it's a little bit here on the benefit of the doubt associated with the tools and the method, the training that we've done over the years.

Joe Ritchie - ***Goldman Sachs - Analyst***

That's helpful. Maybe my one follow-up, maybe just switching gears to Thermo for a second, orders turned positive this quarter? I know that you are calling for North America truck-trailer to be down low teens in 2017?

Your largest competitor, who we just saw at the same conference I think is forecasting down mid single-digits. Is there any reason why there would be either a lag or a change in the trajectory that either of you see for 2017?

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

Two factors that always play here. One is around which set of customers are buying and which are not. You will see anomalies quarter to quarter about kind of who came to the table. In the fourth quarter certainly our customers came to the table and placed orders, which is great.

The second really piece of this thing is that it's awfully early to call. ACT is saying 43,000 units. We've got about 40,000. If you went right back to ACT, now you're in that range that our competitor would have outlined for you. We tend to think historically, with the exception of last year, that they kind of met in the middle somewhere.

So we're although more conservative with a 40,000 unit ACT number versus 43,000. That's probably explaining the difference in how we're seeing the market.

Joe Ritchie - ***Goldman Sachs - Analyst***

Fair enough. Thanks, guys.

Operator

Your next question comes from the line of Andrew Obin with Bank of America. Your line is now open.

Andrew Obin - ***BofA Merrill Lynch - Analyst***

Yes, good morning, guys.

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

Good morning, Andrew.

Sue Carter - ***Ingersoll-Rand PLC - SVP & CFO***

Good morning.

Andrew Obin - ***BofA Merrill Lynch - Analyst***

Just a question about this fourth quarter reinvestment on security and IT? Could you just talk a little bit more about it? And second, I'm just really curious, what was the timing of the decision to make this reinvestment?

And what I am trying to understand, we're starting to get a sense that companies are getting more comfortable with growth and actually for the first time in several years, are choosing to put money into their businesses again. And I was just trying to understand if that's what's happening at Ingersoll-Rand or if there was something else?

Mike Lamach *- Ingersoll-Rand PLC - Chairman & CEO*

Yes, one of the things, Andrew, when it comes to infrastructure and cybersecurity - which are often related - I think once you have the idea that you need to do something or want to do something, I think that common thinking would be that sooner is typically better than later, if you think that you've got something you want to plug. That's generally sort of the thought process, the management decision to do that.

It's also why, frankly, you should always understand we're trying to do the right things for the long run, not for the quarter. So that in and of itself may not have been the difference. I mean, it was more the other discrete items that are difficult if not impossible to forecast -- stock based comp, incentive comp certainly fit that, taxed by legal entity as opposed to tax by geography or business unit.

It’s more nuanced. But that's one where generally speaking if you need to spend it, sooner is typically better than later. That's been our approach.

Sue Carter *- Ingersoll-Rand PLC - SVP & CFO*

I would add just a little bit to that, Andrew, in terms of if you look at the full year of 2016, we started out the year, and we obviously talked pretty regularly to all of the teams around the Company, and we really said, you know, don't let our costs get out ahead of what the revenue profile is.

So if you looked at corporate costs for really the first three-quarters of 2016, you would see that our run rate was actually under what would be typical for a $240 million year. That doesn't mean because you're under you should go out and do some things. But it also adds to part of the thinking when you get to an area where you have some items that you need to spend money on, you go forward.

Say for the year, our costs, whether it's in IT, whether it's in legal, HR, finance, whatever part of our functional spending, are actually flat from 2015 to 2016 and actually will be flat into 2017. So there's also a little bit of a timing element that is a part of that, too. It doesn't explain the difference in the guidance, but I also wanted to give you some context of what we were thinking as we went into the fourth quarter.

Mike Lamach *- Ingersoll-Rand PLC - Chairman & CEO*

Just to be clear with what Sue said, so 2015, 2016 and 2017, the core functional costs have been absolutely flat, which is our objective. All the swing you see are in things like stock-based comp, pensions, adjustments that are really happening around those core functional costs.

Andrew Obin *- BofA Merrill Lynch - Analyst*

Got you. The other thing you made a specific commentary about, seasonality on Industrial in 2017? And you did call it out, so what's different versus history on this quarterly variability in the industrials business?

Mike Lamach *- Ingersoll-Rand PLC - Chairman & CEO*

Andrew, the only comparison I think we made was comparing Q4 2016 to Q4 2015, because Q4 2015 had that mammoth load of Cameron shipments, which drove the difficult comp for quarter 4. Not a lot of seasonality in industrial beyond that which we would call out.

With the exception that for some reason, with large compressors, the kind that are put into gas and energy applications, have tended to have been more fourth quarter loaded. But I'm not sure that's an actual seasonal phenomenon as opposed to when we're booking and shipping orders.

Andrew Obin *- BofA Merrill Lynch - Analyst*

Just to correct, I guess I misunderstood. So there is nothing different about industrial seasonality in 2017?

Sue Carter *- Ingersoll-Rand PLC - SVP & CFO*

No, Andrew. I think the comment that we were actually making, and perhaps we didn't make it as well as we thought, was that what we didn't want anyone to do was to take and draw a straight line on margin improvement each and every quarter in the industrial business.

We were saying that it could be a little bit lumpy from quarter to quarter, and would follow its typical pattern. So we just didn't want anybody to get concerned if there was some variation there. So it was a pretty simple comment that might have been confusing.

Andrew Obin *- BofA Merrill Lynch - Analyst*

Terrific. Thank you so much.

Operator

Your next question comes from the line of Deane Dray with RBC.

Deane Dray *- RBC Capital Markets - Analyst*

Good morning, everyone. I was hoping to get a little bit more color on the residential bookings at up low teens? Maybe some color regarding the product, the mix, where the SEER preferences look to be in 2017, and was there any pre-buy involved?

Mike Lamach *- Ingersoll-Rand PLC - Chairman & CEO*

No pre-buy involved. I think you know that the res product is fundamentally 100% new over the past three years. We've got a few little things that we're tweaking, and we found that as the mix is moved, the 14 SEER and above, this is playing really well in our dealer base.

So I think this is just going back to the commercial discussion. It's been long-term investment, getting the product portfolio right. Long-term investment on repositioning our dealer base to be able to sell low, medium, high price point product, penetration into the residential construction market, penetration into the owner occupied, but nonresident market, which is another market that we've had some good success with.

So good hard product development, channel development, and sticking to a strategy over the long run.

Sue Carter *- Ingersoll-Rand PLC - SVP & CFO*

And I think, Deane, you asked the question on SEER. As we went through 2016, the 13 and 14 SEER combined for roughly 40% of our revenue, then the 15 SEER and greater was a smaller percent. So really what you saw was the 13 SEER go into the 14 product and the 15 and above sort of stayed the same.

Deane Dray *- RBC Capital Markets - Analyst*

Got it. And just as a follow-up there was an interesting development recently with your primary competitor in golf carts investing in Arctic cat. So does that change your thinking in any way of how you want to be positioned? You did mention the new product launch of Onward.

I went online just now and took a look at it -- those are pretty cool rims for a golf cart. But it looks like it's an organic focus for you all with Club Car, but maybe some comments there?

Mike Lamach *- Ingersoll-Rand PLC - Chairman & CEO*

Yes, it looks better with the lift kit, too, Deane, so look at that picture. [laughter]

That's what you need, big wheels and a lift kit. That's what I'm going to get. Anyway, no, it's an organic focus because we think the brand's got legs. We think that we've always focused on golf and utility, and it's a real concerted effort to penetrate the consumer low-speed vehicle market and personal vehicle market.

This is golf and car communities, small vehicle communities. This is hospitality and recreation venues. This isn't 65 miles an hour running through rough country.

Deane Dray - ***RBC Capital Markets - Analyst***

Got it. Thank you.

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

You're welcome.

Operator

Your next question comes from the line of Andrew Kaplowitz with Citi. Your line is now open.

Seth Garcia - ***Citigroup - Analyst***

Good morning, guys, this is Seth Garcia on for Andy. Last quarter you talked about expecting Asia HVAC markets to be flat to down in 2017, and 3Q bookings were flat but bookings in Asia HVAC were high teens this quarter -- so can you talk about what your expectations are for Asia HVAC in 2017?

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

Well, it was a really great fourth quarter. I think that you are going to see sort of a more moderate view toward Asia, kind of mid single-digit in Asia for the full year. So it just happened to be -- the opportunity booked a tremendous amount of orders. With the small group of customers that are buying large, and it's going to be lumpy, but I still think it's going to be a cycle, and you are going to see sort of mid single-digit at the end of the day.

Seth Garcia - ***Citigroup - Analyst***

Got it. That makes sense. In the industrial segment, material handling seems to still be under pressure, but can you talk about your visibility to a bottoming in the material handling market as oil prices continue to recover?

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

Yes, it has to do with really the count of offshore rigs increasing. That's probably the biggest determinant. Land rigs have an effect, but the content that we provide in the land rig versus an offshore rig are going to be dramatically different. Until you see really a utilization of offshore rigs, you are not going to see a full recovery in that business.

Incredible margins, fantastic business. That's why it hurts when it's actually down. You really have a dramatic effect on the margins for the segment. Frankly, it's about a point in the fourth quarter. So small business, big impact. We love it when it's up. It hurts when it's down.

Seth Garcia - ***Citigroup - Analyst***

Got it. Thanks so much.

Operator

Your next question comes from the line of Steven Winoker with Bernstein. Your line is open.

Steve Winoker *- Sanford C. Bernstein & Co. - Analyst*

Thanks for fitting me in. Mike, I'm over at AHR right now, and one of the things that strikes me is, most people I talk to are seeing growth in VRF in North America on the order of 15% to 20%, depending on how you count it. I know you have talked in the past, about maybe 25% of the market volume going through your channels, but one thing that has been apparent is a lot of that is non-Trane product really and the actual Trane content sounds pretty low.

I've seen other folks successfully transition to their own content, or their joint venture content that they own part of, et cetera. What's your plan and strategy here? It's one of the only places you don't really own it and not vertically integrated, it seems like a big opportunity?

Mike Lamach *- Ingersoll-Rand PLC - Chairman & CEO*

Yes, Steve, look, one of the things here is we have a very definitive plan of what we're doing. I'm not going to disclose it here for strategic reasons to do that, but I will tell you that it’s a source of investment in Q4, it's a large business in Asia and it's growing, and we make and co-develop our own product there with partners.

Here our growth rates are higher than the rates you're reporting, so we're seeing higher growth rates in our unitary business and higher growth rates than what you are seeing. Our focus is on the VRF business, not on the mini split business. That's where the value is. That's where controls matter. That's where hybrid systems come into play.

That's where our channel works and where service is a possibility. So again, our focus on VRF, you've seen Trane-branded product there in the US. Mini splits, we're a little bit more agnostic in that we serve the market. We're not as caught up in whether that says Trane, or Trane and somebody else, or somebody else, going through our market.

Steve Winoker *- Sanford C. Bernstein & Co. - Analyst*

That's helpful. Also back to the cash flow discussion for 2017, so at the midpoint it looks like that 100% conversion, Sue, you talked about 4% working capital target. But Mike, I think it's a decade now almost that we've been talking about lean conversion and much, much better inventory and other management.

So maybe a little flavor here on why couldn't you keep it at a lower inventory level to still meet channel demand, or is it just the shift in inventory from raws and working process to finish goods? What's going on there?

Mike Lamach *- Ingersoll-Rand PLC - Chairman & CEO*

I think that whether it's 3.6% or 4%, and whether inventory turns are 6.8% or 6.9%, really isn't what we're trying to do. What we're trying to do is get 100% on-time customer shipments. Cycle times that competitors can't deal with and pick up all the discretionary business that's out there to get.

And we want a balance between the two. As long as we're growing margins and growing share, we feel like it's a good formula. So the place to put the gas down isn't on creating a problem where you're inadvertently creating a situation where you're not competing in the area that you want to compete.

Steve, you know us as well as anybody, that really that cycle time conversion, and that compression and cycle time is worth something. Not just working capital but on growth and operating margins. So that's always been our focus. And so whether it's 3.6% or 4%, it's not as important to us.

We know it's already, if not the best, it's certainly top quartile, top quartile inventory turns. Our return on invested capital last year was almost 24% as a Company, cash flow return on invested was 24%. Let's grow the Company and let's grow margins.

Steve Winoker *- Sanford C. Bernstein & Co. - Analyst*

Yes. No, that's great. I just wanted to make sure that you've had tremendous traction in this area. I just want to see that the pedal is still pushed down.

Mike Lamach - ***Ingersoll-Rand PLC - Chairman & CEO***

It will never let up, I promise you as long as I'm breathing, it will never let up.

Steve Winoker - ***Sanford C. Bernstein & Co. - Analyst***

Excellent, thanks.

Operator

There are no further questions at this time. I would now like to turn the call back over to Zac Nagle for any closing comments.

Zac Nagle - ***Ingersoll-Rand PLC - VP of IR***

I would like to thank everyone for joining on today's call, and thank you for your interest in Ingersoll-Rand. As always, we will be available in the coming days and weeks to take any questions that you may have. So feel free to give us a call, and we will also be on the road quite a bit this year, so we look forward to meeting you in person. Thank you, and have a great day.

Operator

This concludes today's conference call. You may now disconnect.