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CORPORATE PARTICIPANTS

Anthony F. O'Brien *Raytheon Technologies Corporation - Executive VP & CFO*

CONFERENCE CALL PARTICIPANTS

Myles Alexander Walton *UBS Investment Bank, Research Division - MD & Senior Analyst*

PRESENTATION

Myles Alexander Walton - *UBS Investment Bank, Research Division - MD & Senior Analyst*

Welcome to the UBS Industrials and Transportation Conference. I'm Myles Walton, and I'm the aerospace and defense and airlines analyst here at UBS. It's really my pleasure to kick off this conference this morning with the Chief Financial Officer of Raytheon Technologies, Toby O'Brien.

Toby, welcome. I know you have a disclosure statement and maybe some opening remarks, and then we'll get right into the discussion after that. So with that, Toby, I'll hand the mic over to you.

Anthony F. O'Brien - *Raytheon Technologies Corporation - Executive VP & CFO*

Okay. Thanks, Myles. Yes, let me start with the formalities here. During the discussions today, I may make forward-looking statements such as comments on future plans, objectives and expected performance. These are subject to risks and uncertainties that could cause our actual actions or results to differ greatly. You should consult our SEC filings for a description of those risks and uncertainties.

So just a few introductory comments, as you said, Myles, here. Obviously, a little over a month ago, we completed the merger. We have a focused A&D company, it's balanced and diversified between defense and commercial; and geographically as well; heavily focused on technology and innovation. Both legacy UTC and Raytheon had really good, strong starts to the year, but that's in the rear view mirror now, and it's clear that the balance of the year is under significant pressure. Notwithstanding that and the challenges, we continue to be well positioned to deliver value over the long term.

We entered the merger in a strong position financially, with plenty of liquidity to make it through the storm, \$8.5 billion of cash, \$25 billion in net debt. That was expected, so no surprises there. We have revolvers in place with up to about \$7 billion of availability, and there's another \$2 billion of net proceeds or cash that we expect before year end from some divestitures. We're committed to returning the \$18 billion to \$20 billion of capital to shareowners over the next 4 years.

The reason we came together here, 3 reasons, right: Technology, talent and balance. The defense businesses remain strong and resilient, not just on the legacy Raytheon side, but UTC as well. And although there is pressure on the commercial side, a couple of things to think about. At Pratt, the GTF fleet, the GTF-powered fleet, has reached 5 million flight hours. Collins is doing a great job and remains on track to generate the \$600 million of gross synergies associated with UTC's acquisition of Rockwell Collins late in 2018.

We have strong businesses, some are a little bit more challenged on the commercial aerospace side right now, but each of our businesses is a leader in their respective markets. They're well positioned to generate significant value over the long term by combining technologies to generate revenue synergies across all of our businesses. Throughout our company's history, we've weathered a lot of storms and challenges, and we'll come out of this one stronger. We're very excited about the future of the company and the ability to drive sustainable long-term value creation.

With that, we can jump into the questions.

QUESTIONS AND ANSWERS

Myles Alexander Walton - UBS Investment Bank, Research Division - MD & Senior Analyst

Great. So maybe first, just set a stage for us on the demand side in the commercial aerospace, half of the house. And as for the near term, understanding that you're not providing guidance, but maybe some comments about what you're hearing from the OEMs, what you're hearing from airline customers or any additional color over the last month since your earnings call.

Anthony F. O'Brien - Raytheon Technologies Corporation - Executive VP & CFO

Yes. Sure. So you're right, we're obviously not providing our traditional outlook at this time, given all the uncertainty affecting our commercial aero business. Let me start, I'll kind of do a rundown. I'll hit on defense first real quick because, as I mentioned, defense remains strong. We generally see the year playing out consistent how we saw it at the beginning of the year. We did provide an outlook at the time for the RIS and RMD segments. And operationally, we expect solid revenue and profit growth from those businesses this year. Similarly, on the Pratt and Collins side, their defense businesses represented just shy of 30% of 2019 sales. And there, we continue to see mid single-digit organic revenue grew -- growth in 2020 for the defense pieces.

As you think about the commercial aero business in the balance of the year, so Q2 through Q4, right now, we could see both the OE and aftermarket revenues down about 50% or so. As we've talked about, we're continuing to monitor this as we go through Q2, where OE is down in line with the OEM production changes, and the aftermarket is generally down consistent with or in line with traffic. The recovery here clearly looks more like a U. Our expectation or our outlook right now is the steepest drop in sales here in Q2, followed by a gradual recovery, but Q3 will still be tough.

And when you think about the trough, TSA check-ins were down about 95% in April, we talked about that previously. They improved, but only slightly, in May, to down about 90%. So you can't get too much worse than that. The shape and the pace of the recovery in the airline financial conditions will be the critical factors, monitoring how things play out.

To that end, what we're hearing and seeing from our airline customers, probably no surprise. They have significant reduction in their fleet utilizations. They're grounding aircraft. They have accelerated some retirements and deferred, and in some cases, canceled new aircraft deliveries. You'd also expect, and they are, shifting to cash-conservation behaviors, which includes things such as deferring engine maintenance, requesting extended payment terms, deferring delivery of new aircraft and spare engines and requesting discounts on engine maintenance.

So a lot of moving pieces, but we're going to continue to monitor the trends, work closely with our customers. And as we've discussed, as the volumes decline, we are actively mitigating our cost and adjusting our production schedules accordingly.

Myles Alexander Walton - UBS Investment Bank, Research Division - MD & Senior Analyst

And Toby, maybe while we're on the topic of trends, you're about 2/3 way through the Q2 now. Do you mind providing any update that you're seeing there? Any additional thoughts for 2Q in specific?

Anthony F. O'Brien - Raytheon Technologies Corporation - Executive VP & CFO

Yes, sure. Yes. So again, let me start with defense, because I think that's maybe the simpler story here, right? Again, no major impacts operationally. The one thing I will point out about Q2 on the defense side, and we talked about this and we had some charts on the earnings call on it, that for the legacy Raytheon businesses, now RIS and RMD, they will have an impact of the stub period, which was the time between when Raytheon's Q1 ended and the merger of April 3, as well as from the accounting related to the merger.

The stub period would impact Q2 sales by around \$400 million and reduced profit by a little over \$40 million. And due to the EAC impacts and the percent completes being reset to 0 for the RIS and RMD backlog programs, we won't see the flow-through on the productivity efficiencies we typically do, which could be \$100 million to \$150 million impact in Q2. On the commercial business side, the trends that we saw in April, they

continue into May. And we still believe Q2 will be the worst quarter within the year. And we do believe there will be a gradual recovery later in the year, which we've talked about.

I think the one thing now I'd point out, that we now expect both Pratt and Collins to experience negative operating profit in Q2 as repair intake and shop visit inductions are significantly reduced. We're seeing under-absorption in our factories being realized, and we're also seeing airline financial condition deteriorate in some cases, including some bankruptcies.

To put some numbers around it, perhaps, some metrics around it. Quarter-to-date on the aero metrics, they're down anywhere from 60% to 70% for Pratt engine inductions, and Collins is seeing aftermarket metrics down between 50% and 60% as well. And I think the thing to keep in mind here is that the decrements will be the most challenging in Q2 as we implement and ramp in the balance of the year our cost-mitigation actions. And when I think about that and kind of integrate it up, if you will, all of this now, I'd expect our adjusted EPS to only be slightly positive in Q2.

I'd also say, and this is consistent with our prior thinking, free cash flow will be an outflow in Q2 in the range of \$1.5 billion. We continue to see the majority of the benefit from the \$4 billion worth of cash conservation efforts impacting Q3 and Q4. And not a surprise, but for a little bit more color, that outflow is obviously driven by the commercial aero side of the portfolio, and it's partially offset by positive free cash flow on the defense side.

Myles Alexander Walton - UBS Investment Bank, Research Division - MD & Senior Analyst

Okay. That's a lot of information, and super helpful. I wonder, can we calibrate a couple of those things? So first, you talked about the \$2 billion cost actions and \$4 billion of cash conservation. How should we think about those buckets?

And I think you alluded to the cadence of those, being the impact -- the positive impacts not happening until you get later in the year and into next year. But maybe provide some color on both differentiating the \$2 billion of cost versus the \$4 billion of cash conservation, and maybe provide some clarity on those 2 buckets.

Anthony F. O'Brien - Raytheon Technologies Corporation - Executive VP & CFO

Sure. So let me start with the cost part of the equation there. The way to think of the cost is it's -- the big moving pieces there are reductions to our E&D by about \$450 million. We've deferred merits. We've implemented targeted furloughs, reducing salaries for corporate, Pratt and Collins salaried employees and curtailing discretionary spending. If I bridge that over to the cash conservation actions in addition to the impact of the cost actions, there's about an \$875 million reduction in CapEx, with the majority of it coming from Collins and Pratt. And then obviously, we're working to try to mitigate smartly elements of working capital where there is clearly significant headwind that we're dealing with here.

You got it right, and I'll just kind of reaffirm what we said before about the cadence of these actions. Maybe a little bit of benefit in Q2, but certainly no more than, call it, 10%; probably about 1/4 of it in Q3; and the balance, over 60%, in Q4. I would say that these actions, both the cost and cash are -- we're calibrating these to the demand in the current environment, including the input we're getting from conversations with our customers. And we still don't see a full recovery until some time out in 2022.

And while these are immediate actions that we're taking, we will continue to monitor, and if need be, look to take additional actions. They're tough measures, but they're the right things to do for the business, given the times that we're operating in.

Myles Alexander Walton - UBS Investment Bank, Research Division - MD & Senior Analyst

And Toby, maybe just characterize the kind of actions, whether they're the kind of permanent cost structure actions or they're temporary that come back with volume. Just maybe characterize how much of this is a persistent benefit.



Anthony F. O'Brien - Raytheon Technologies Corporation - Executive VP & CFO

Yes. So I think the way to think of the cost actions and even the cash conservation actions, they're really more in the variable category as opposed to the fixed, and that over time, we would expect to have some of those costs come back as volumes return. That said, I think it's been my personal experience in times like these, you're maybe always able to eke out a little bit of ongoing or continuous benefit, but none of these actions here today contemplate shuttering of factories, closing of factories or anything of that nature there. They're all timing-related.

Even the timing in variable -- even the E&D and CapEx reductions, while we won't just run out and restart projects, because we want to understand the viability of the ones that we're deferring, we will look to potentially reengage in those projects at an appropriate time if the business case around them still makes sense.

And again, the reason we're not driving it, the fixed costs, is kind of twofold. One, we don't view this as a permanent situation. Again, whether it's middle of '22, end of '22, when things start coming back and we want to be prepared for that. And we also have a strong defense business, as we've talked about. We're moving resources around where appropriate and where we can to satisfy demand on the defense side as well. So we're trying to balance all of that in the decisions we're making.

Myles Alexander Walton - UBS Investment Bank, Research Division - MD & Senior Analyst

Okay. And then maybe just tie it back to what's been somewhat of a -- it's hard to give cash flow color without giving cash flow guidance, but you guys have tried it. So let me ask you to try it again and just maybe give us the walking pieces for 2020, given the cash conservation measures, the working capital swing and kind of what it looks like for whatever you want to describe a pro forma full year or the remaining 3 quarters, however you want to put it.

Anthony F. O'Brien - Raytheon Technologies Corporation - Executive VP & CFO

Sure. So a lot of moving pieces, as you just said, for sure. But the way we're thinking of it, it's kind of a 3-part equation. And again, as I mentioned, the defense side, and let me start there, which is I think the easier part of the story, and take a look at the legacy Raytheon business, stand-alone, inclusive of its former capital structure and corporate costs.

Back in last year, in 2019, we generated about \$3.5 billion of free cash flow. And there's always some puts and takes, and that's no different this year. But we'd expect similar free cash flow this year in that \$3.5 billion range. As we said, the defense side remains healthy and stable. So that's kind of part 1 of the equation.

For part 2, the legacy UTC aerospace businesses, coincidentally, if you look at 2019 on a similar basis, as I just described, the legacy Raytheon business would have generated about \$3.5 billion as well of free cash flow. But in 2020, we're obviously seeing significant headwinds on the commercial side of the house, not just from a sales and profit perspective, but as you alluded to or mentioned, also as it relates to working capital. And again, we're balancing what we can do with working capital and the rapid decline in volume with long lead times on some of our materials that could be up to 12 to 18 months as well as with the health of the supply base. And those working capital impacts are significant, think billions, right? Not -- we're not talking nickels and dimes, we're talking about a significant impact.

From a broad stroke perspective, the goal we have for the UTC legacy commercial aero businesses is to be breakeven free cash flow for this year. And the pieces of that, again, are the headwinds that I just described on the commercial aero side, partially offset by cash generation from the defense pieces of Pratt and Collins as well as the benefit of the cash, the \$4 billion cash actions. So that's part 2, legacy aero, net-net, kind of sort of breakeven.

And then the third part of it is that we have about \$1.2 billion to \$1.4 billion of onetime cash costs for the rest of the year. That is about half related to cash taxes from our divestitures, which will flow through cash from operations, and the other half related to a combination of separation, merger and restructuring costs this year. And given the significant cost actions, we expect to see higher restructuring this year. Some of that could continue into 2021 related to some of the actions and the synergies.

So overall, if you take the 3 pieces, \$3.5 billion, 0, and then a negative impact of \$1.2 billion to \$1.4 billion, you get about \$2 billion of free cash flow for the year. But again, I'll just remind everyone, there's still a lot of unknowns out there. Really, the shape of the recovery certainly being the biggest one that is yet to play out. And that's why we didn't give a formal outlook. But hopefully, the pieces here can help people think of it a little bit, or at least help folks understand how we're thinking of it.

Myles Alexander Walton - UBS Investment Bank, Research Division - MD & Senior Analyst

No, that's super helpful, Toby. And then I guess the one -- the other thing that people are trying to resolve around is, what does that mean for '21? Given you haven't given guidance for 2020, I'm not suggesting you should even give guidance for 2021. But maybe that working capital dynamic, which, as you mentioned, is not nickels and dimes, it's billions.

And one of the motivations, or one of the principles, I guess, of the UTC aero cos was to get the inventory turns higher over time, and that was going to actually be a significant driver of cash flow expansion. So maybe just talk about the idiosyncratic working capital in the near term and its amount of headwind to this year and perhaps tailwind to next. And then how intact are those goals of getting inventories higher in commercial co?

Anthony F. O'Brien - Raytheon Technologies Corporation - Executive VP & CFO

Yes, sure. So clearly, it's -- working capital is a considerable headwind for us. As I just mentioned, in the billions. And it's -- just so people understand, right, it's the speed, the magnitude of the decline in air travel that has almost instantaneously resulted in reductions in OE production rates and the decline in the aftermarket, and we cannot offset it within the year. A lot of our supply chain have long lead times, so think 12 to 18 months. And again, that's not something we can turn off instantaneously. We still have material coming in through the door, across the docks, we're paying our suppliers. And so we're going to obviously have more inventory than we need for a period of time.

And we're also balancing the health of the supply base, as I mentioned earlier, right? We want -- when we come out of this -- and again, it's not a matter of if, it's when, we need our supply base there with us. So it is a balancing act. The UTC aero, the legacy business and their inventory turns last year, they turned about 4x. This year, we're going to be well below that range. We do feel we're taking the appropriate and significant actions here to realign the supply to the demand. But again, you can't stop this on a dime because of the long-lead parts and the health of the supply chain.

So we'll clearly have more inventory than we would want to this year. And we would expect next year there to be more of a tailwind in this area, albeit tied to the demand, right, and the timing of when that demand comes back and how we can meet it. And we are confident it will come back. So again, we expect the overall to tie it back, right, cash flow for the UTC aerospace businesses to be breakeven, sizable outflow for the year and a sizable outflow in Q2, where the headwinds here are the most challenging.

Myles Alexander Walton - UBS Investment Bank, Research Division - MD & Senior Analyst

And is -- that swing in working capital year-on-year from 2020 into 2021 as you see it today, is it in that \$1 billion-plus range? I mean, is that the size of the swing we're looking at?

Anthony F. O'Brien - Raytheon Technologies Corporation - Executive VP & CFO

It's all tied back, Myles, to the timing and the shape of the recovery. I would just leave it for now as we're continuing to model a bunch of different scenarios. And again, there's a lot of unknowns still to play out. We'll have more insight into that, I think, here in another 1.5 months on our Q2 call. But I would just leave it at, we would expect it to be a headwind at this point in time. And as we have more clarity around it, we'll try to provide more color for everyone.

Myles Alexander Walton - *UBS Investment Bank, Research Division - MD & Senior Analyst*

Okay. Another area of questions that I get, and I'm sure you do, is around the aftermarket exposure idiosyncratically at Pratt, particularly as it relates to some of the older planes and engine retirements that can take place; and then secondarily, maybe on the slightly more discretionary businesses at Collins. And maybe if you can -- you sort of gave us some color on 2Q in terms of the aftermarket trends. But maybe just give us a little bit deeper slice into the 2 businesses.

Anthony F. O'Brien - *Raytheon Technologies Corporation - Executive VP & CFO*

Sure, sure. Let me start with Collins and maybe try to put things in perspective for folks. I think we've talked about this a little bit, but it's a good reminder. So about 35% of Collins is aftermarket in a typical year, like last year in 2019. And I think as folks know, the business is more platform-agnostic with their systems being found nose-to-tail on both narrow-body and wide-body fleets. And much of the Collins product is, as we say, on condition versus the more scheduled cycles, that engine overhauls, are on at Pratt, right? And that means that Collins aftermarket trends more directly with the actual aircraft usage. And again, given the sudden decline in air traffic, the Collins aftermarket should see an immediate and most likely severe impact. As the recovery plays out and more aircraft get put back into use, we should start to see a recovery as well. But there could be a lag, maybe give or take 6 months.

In the case of Pratt, it's more, I think, about volume -- not of volume, a platform discussion. And the Pratt aftermarket really can be broken down into 3 pieces. The first being the V2500, which makes up about half of their large commercial engine aftermarket. There's about 6,000 engines out there, average life of around 11 years. And I think, more importantly, about 1/3 of the fleet hasn't seen its first shop visit. So there's still a lot of aftermarket there to be had, albeit pushed out a bit here. And we do remain confident in this fleet and do expect a full -- a full recovery out over time.

The second bucket for Pratt to think about is we do have some wide-body exposure on the PW2000 and PW4000 engines. Combined, that's about 20% to 25% of Pratt's aftermarket. There will continue to be accelerated retirements, but I think, again, to put it in perspective, these engines, the 2000s and 4000s, are around 20 to 25 years old and we were already expecting the aftermarket here to start and to continue to wind down. And margins are normally more healthy, if you will, for a fully learned out engine, but given the age of the fleet, there's also other alternatives around used material that's available, discounted maintenance programs that incentivize offering an older engine. So you got to kind of balance all that out.

And then the balance of the aftermarket, the remaining roughly 25%, is made up of the GP7000, the GTF and some other overhaul work. Lower margins here, think more wrench-turning. And then the GTF, of course, is still in the retrofit and warranty phase.

So as you think about this and what it means, we've assumed some level of early retirements of the older platforms in our overall aftermarket assumption being down 50% for the rest of the year. But at the same time, with fuel prices low, that's good for older platforms as customers think about how to utilize and deploy their assets in this constrained environment.

The other point here, the early retirements that have been announced that folks have heard about, they're effectively pulling things forward by a year or 2, not call it 5 to 10 years. Some of the retirements could also get converted to cargo, which is very active in this environment as well.

So with that, the key to our aftermarket, obviously, is that airplanes are flying, and that drives the need for repairs and overhauls, even if the planes aren't fully loaded to capacity. So hopefully, that gives you a little bit of color and insight for bigger picture rather than just the near-term trends for the aftermarket.

Myles Alexander Walton - UBS Investment Bank, Research Division - MD & Senior Analyst

Yes, that does. And maybe put it into context, if you can, Toby, I think you and Greg both talked about 2022 is more sort of a normalized environment. Does that normalized environment anticipate whatever used service material has been put through the system is no longer a material headwind, whatever retirements have taken place? Just maybe define what normal is or what the vision for 2022 actually looks like.

Anthony F. O'Brien - Raytheon Technologies Corporation - Executive VP & CFO

Yes. So obviously, we continue to refine these assumptions and outlooks as we go along. But we are taking into account the retirements, right, especially the accelerated retirements. Our plans, pre-COVID, would have already taken into account what we knew to be different customers' plans to either retire fleets and/or we were accounting for our experience on the older fleets relative to the impact of used parts, discounted maintenance program. So that would all be factored in as best we can to our, call it, 2022 and beyond thinking as well.

Myles Alexander Walton - UBS Investment Bank, Research Division - MD & Senior Analyst

Okay. Got it. And maybe on the GTF quickly. The program has got great accolades as it relates to fuel burn. It's obviously had some durability issues through its first 5 million hours of flight. There were performance-improvement packages that were to be implemented, I believe, this summer, which were going to show some of the kind of the early recoveries against those durability issues. How are those improvement packages going? Are they still on track? And when do you think you'd be able to see some of the fruits of the labor?

Anthony F. O'Brien - Raytheon Technologies Corporation - Executive VP & CFO

Yes. So if there is any silver lining in the environment that we're in here today, it is likely around the GTF and the retrofits that you're referring to there, the implementation of those packages. What we are doing is we are utilizing available -- what is now available shop capacity to fix the issues in the fleet this year, right? So it's given us the opportunity to ensure our customer fleets are healthy and well positioned as we exit the year. Our goal is to have the majority of the GTF engines to be at that latest configuration with the enhancements and the improvements by the end of the year as the recovery starts to play out. So we feel we're going to take advantage of the time and the capacity that's available here, and the GTF will be very well positioned for the future.

Myles Alexander Walton - UBS Investment Bank, Research Division - MD & Senior Analyst

Okay. And maybe to just quickly transition gears to the defense side for a bit. The -- give me some outlook -- or give us some color on the outlook as it relates to RIS and RMD on future bookings or bookings ahead that we should keep an eye on. Any disturbances you're seeing in the international environment? And also maybe just touch on the defense business at Pratt and Collins that probably didn't get as much play when it was inside of UTX, the bigger UTX.

Anthony F. O'Brien - Raytheon Technologies Corporation - Executive VP & CFO

Yes, sure. So we've talked about before that at the RTX level, we've got a record \$70 billion defense backlog. \$51 billion of that -- about \$51 billion of that was from RIS and RMD. One thing, just kind of maybe looking back or recapping a little bit, because between Q4 and Q1, on the legacy Raytheon side, there was a lot going on, 2 real big franchise wins that we've had, LTAMDS and LRSO. And I think, as you know, Myles, when we talk about franchises, we talk about programs that are going to last 20-plus years. And here, the LTAMDS win has potential lifetime value, I think conservatively, north of \$20 billion; and in the case of LRSO, north of \$10 billion. LTAMDS, we won in Q4 of last year; and LRSO, we were selected back in April. Not big dollars near term, but over the long haul, very key.

We also had been talking a lot about our standard missile franchise. And between Q4 and Q1, we've seen about \$5 billion or north of \$5 billion worth of bookings, 2 5-year multiyears, 1 on the SM-6 back in Q4. And then on the SM-3 Block IB here back in Q1. In addition to that -- and both of

those were around \$2 billion, a little bit more. And then in addition to that, we kind of had, not formally, but a mini-multiyear related to production for the SM-3 Block IIA, which is the most recent variant of the standard missile family, where we got about 3 years' worth of production over the last 6 months. So again, about \$5 billion in total, all of which provides great line of sight from a production point of view for the next 7 or 8 years for that business, for -- and for that product line.

I want to touch on classified for a second here. We've talked about historically and it hasn't changed, classified is important. It funds the next-generation technologies that are going to ultimately drive the long-term growth of our future franchises with production awards, i.e., think LTAMDS and LRSO. That remains a key focus for us. We're very much aligned with the National Defense strategy. Nothing's changed there.

On the international side, for the legacy Raytheon, things remain consistent with the plan we set at the beginning of the year, with about 30% of the bookings expected to be international. From a timing point of view, we're doing well. We're ahead of where we expect it to be coming out of Q1. The big award internationally in Q1 was about \$500 million for Patriot air and missile defense capability for the Kingdom of Bahrain. Bahrain is the 17th nation to buy Patriot. And by midyear, coming out of Q2, we could be 2/3 of the way to meeting our international plan, with the most significant award, and we do expect it either in late Q2 or early Q3, being for around \$2 billion for the TPY-2 system for KSA.

We're not really seeing any decrease in demand, generally speaking, on the international market. We've been pretty consistent in talking about how, even in all different environments, economic conditions, it's the threat environment that's going to drive the demand. And I would tell you, that continues to be the case, and we continue to be well positioned on the defense side of things, whether it be domestically or internationally, in priority areas.

On the legacy -- on the UTC side of the house, with the Pratt and Collins defense businesses I mentioned earlier, their outlook for the year hasn't changed. Still expect strong mid-single-digit organic growth there. So overall, the defense business is humming in this environment.

Myles Alexander Walton - UBS Investment Bank, Research Division - MD & Senior Analyst

That's helpful, Toby. There's one topic that's come up recently, because you're getting closer to 2022, on the tax headwind that could occur because of the research expense rule requiring amortization versus expensing. Have you guys sized that? What are you thinking is the outcome? Have you any color there?

Anthony F. O'Brien - Raytheon Technologies Corporation - Executive VP & CFO

Yes. So I know you're talking about the -- from the Tax Cut and Jobs Act, the requirement to capitalize the research and experimental expenses and amortize those over 5 years instead of expensing them annually.

Myles Alexander Walton - UBS Investment Bank, Research Division - MD & Senior Analyst

Exactly.

Anthony F. O'Brien - Raytheon Technologies Corporation - Executive VP & CFO

So yes, we've looked at that. I would tell you, we're supportive of efforts that are ongoing to reassess and potentially reverse this. And the reason being, we do believe the immediate expensing is a feature that's important to the tax system in order to help drive that U.S.-based research activity and innovation. And obviously, this isn't unique to A&D. This law impacts all industries, especially, with significant R&D expense. From an RTX point of view, all else equal, out in 2022, our estimate is it could be about a \$2 billion impact to cash taxes with the delayed deduction and having to amortize over 5 years. And then obviously that impact would reduce each year after that. And ultimately, after 5 years, you kind of be back to where you started from. But that's how we see it right now today.

Myles Alexander Walton - UBS Investment Bank, Research Division - MD & Senior Analyst

Okay. All right. And maybe at a high level, we're coming to the top of the hour, one of the things that was, I guess, an easier thought process exercise during the formation of the company was this \$18 billion to \$20 billion of capital return over 3 years. It's now over 4 years and there was a modest connection of that \$18 billion to \$20 billion over 3 years being deployed and sort of linked to some way, obviously, to the free cash flow you were going to generate over those 3 years.

How much of the -- how much should we be thinking about the free cash flow you were going to generate over those 3 years, returning it to cash flow -- to shareholders? How much of a connection is there to what you're thinking about over the next 4 years? As that's kind of the new extension of where this capital deployment strategy is going to be.

Anthony F. O'Brien - Raytheon Technologies Corporation - Executive VP & CFO

Yes, sure. So I won't repeat because it was in my opening comments, but big picture, we've got a strong liquidity position as we entered the merger. And I think one comment I'll make here is that looking at this revised time frame, it's just another prudent step that is needed to ensure we maintain the ample liquidity and ample flexibility. The Board is confident in our liquidity and cash flow going forward. They approved the dividend about a month ago.

And the way we're thinking about it, if you take 4 years of dividends, just directionally, that would be about \$12 billion. And that would leave \$6 billion to \$8 billion for share buybacks that would likely occur primarily in years 3 and 4, given the current environment. We're committed to a robust capital return to shareowners. And clearly, if the recovery were to happen more quickly, we would revisit that time frame.

I think the other couple of pieces to think about relative to capital allocation. One, around M&A. I think we've talked about the merger really completes the picture for having a premier aerospace and defense system supplier. We'll always look at M&A. It will always kind of be on the agenda for key technologies that can be added to the portfolio and/or to secure a supply chain, but it's not necessarily a priority in the near term. We're focused on liquidity, the cost reductions, et cetera. And then even in the longer term, we do not need large-scale M&A as we already have the size, scale and technologies. So again, we're focused on our synergies, returning capital to shareowners.

And then the last piece, I'd say, pensions. I think we've got a good handle on that. About \$500 million that we're going to be funding this year related to qualified plans and nonqualified and postretirement plans. We do still have about \$2 billion from the legacy Raytheon on cash recovery this year and no contributions on the legacy UTC qualified plans, not only for this year, for 5 years.

So when you step back from it, you can largely see that where we expect to allocate our capital is in the form of return to shareowners over that next 4 years.

Myles Alexander Walton - UBS Investment Bank, Research Division - MD & Senior Analyst

All right. Great. Well, I really appreciate this, Toby. I think it was a good discussion, and I think we'll stop it there. So thanks again.

Anthony F. O'Brien - Raytheon Technologies Corporation - Executive VP & CFO

All right, Myles. Thanks for having us. Appreciate it.

Myles Alexander Walton - UBS Investment Bank, Research Division - MD & Senior Analyst

Take care. Bye-bye.

Anthony F. O'Brien - Raytheon Technologies Corporation - Executive VP & CFO

All right. We'll talk to later.

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