Operator: Good day and thank you for standing by. Welcome to the Linde plc Third Quarter 2021 Earnings Teleconference. At this, all participants are in a listen only mode. Please be advised that today's conference is being recorded. After the speaker’s presentation, there will be a question-and-answer session. I would now like to hand the conference over to Mr. Juan Pelaez, Head of Investor Relations. Please go ahead, sir.

Juan Pelaez: Thanks, (David). Good morning, everyone, and thank you for attending our 2021 third quarter earnings call and webcast. I'm Juan Pelaez, Head of Investor Relations, and I'm joined this morning by Steve Angel, Chief Executive Officer; Matt White, Chief Financial Officer; and Sanjiv Lamba, Chief Operating Officer.

Today's presentation materials are available on our Web site at linde.com in the Investors section. Please read the forward-looking statement disclosure on page two of the slides and note that it applies to all statements made during this teleconference.

The reconciliations of the adjusted numbers are in the appendix of this presentation. Steve will provide some opening remarks, and then Sanjiv and Matt will give an update on Linde's business outlook and third quarter performance, after which, we will wrap up with Q&A. Let me turn the call over to Steve.

Stephen Angel: Thanks, Juan, and good morning, everyone. Linde employees delivered another solid quarter, continuing Q2's record EPS performance, despite increasingly challenging market conditions. Operating cash flow and return on capital reached record levels, and our project backlog nearly doubled, providing a strong foundation for high-quality, long-term growth.

We also stepped up our commitment to reducing our greenhouse gases emissions footprint, and Sanjiv will share that road map with you. But frankly, this isn't something new. It's what we committed to our shareholders since the merger and had been delivering on ever since, irrespective of the macro environment.

Most of you know this, but I think it bears repeating: our operating culture runs deep at Linde, our people take great pride in demonstrating continuous improvement across the key operating metrics in their business. The best day of the month for our management team is when we review the operating performance of each of our regional business units.

This is what we do for fun in Danbury, among other things. While I'm sure you've seen the announcement earlier this week where I will become the Chairman of the Board, and Sanjiv will become CEO effective
March 1. His appointment is the culmination of a diligent three-year succession planning process, in which Sanjiv clearly demonstrated he was the right choice to lead this company going forward.

I will continue to provide guidance, both from the perspective of a Director and a significant shareholder. But my primary responsibility shifts to chairing the Board of Directors, while Sanjiv takes over day-to-day management of the company.

Supporting Sanjiv is a highly capable and experienced leadership team. I have been CEO for 15 years, and I have never felt better about how the company is positioned. Obviously, our strategy is working well and the team is executing at a high level.

Some say we are a well-oiled machine. I wouldn't disagree. We are a company for all seasons, and I’m confident Linde’s best days lie ahead. Before handing off to Sanjiv, I would like to take a moment and thank Wolfgang Reitzle for his partnership and bringing our highly successful merger to fruition, and our directors and investors for their continuing support.

Lastly, I want to thank our employees worldwide for creating the leading industrial gases and engineering company in the world. I'll now hand the call over to Sanjiv.

Sanjiv Lamba: Thank you, Steve. I’m honored to be given the opportunity to lead this outstanding company into the future. I appreciate your confidence and support over the years. Before I jump into the slides, I wanted to build on Steve’s comment of a seamless leadership transition.

Here at Linde, we are proud of our industry-leading performance, which starts with living our core values while maintaining a disciplined execution culture. As CEO, I fully intend to build upon our foundation.

My focus will be on areas that are aligned with the interest of our shareholders: profitable growth, optimize the business, cash generation and, of course, the truth serum for our industry, ROC. Linde will remain focused on the things that create value for Linde owners such as strong pricing and productivity culture, an active commitment to sustainability, a disciplined investment philosophy, a shareholder-friendly capital policy, and of course, pursuing high-quality and sustainable growth initiatives with emphasis on ROC.

Ultimately, it's about being the best-performing industrial gases and engineering company in the world. Stated differently, you can expect a seamless transition with minimal change.

Now with that said, let’s move on to slide 3 for an update on our growth initiatives. Last quarter, I mentioned some key growth drivers, including the secured project backlog, accretive base CapEx investments and the strength of our growth in low-capital intensity areas such as health care, food and beverage, engineering and our packaged gas business.
Today, I’m happy to report that our project backlog has increased from $7.5 billion to $13.4 billion or up 81% sequentially from the last quarter. You will recall, this backlog only includes contractually secured incremental growth with fixed payments to ensure targeted returns.

We’re also beginning to see a return of the capital cycle, especially in upstream operations, such as natural gas production. That bodes well for our overall pipeline of opportunities.

On top of that, the electronics sector continues to be very active. We recently announced a $600 million investment -- sale of gas investment indeed to supply a world-class fab in Phoenix, Arizona. This is supply only the first phase of this project, and we expect to see further opportunities as that area builds out.

Overall, I’m pleased to see how the entire Linde team has come together and is leveraging our combined strengths to secure high-quality growth opportunities through our leading high-density industrial gas network combined with the world-class engineering capabilities.

This backlog, combined with our supply network density, enables profitable and secured growth for years to come. Now before moving to the quarterly results, I want to update you on Linde’s new and more ambitious greenhouse gas emission goals.

A good way to stop this is to first explain the role our products play in people’s lives and the overall economy. You’ll find this on slide 4. We make products that are critical for society, products such as medical oxygen for hospitals, ultra high-purity nitrogen for semiconductors, liquid nitrogen for food freezing, krypton to insulate windows and hydrogen to produce cleaner fuels, to give you just a few examples.

In order to make these products, we expect to have a total of 39 million metric tons of Scope 1 and Scope 2 emissions this year. As you know, the production of gases require significant amounts of electricity. When such electricity is generated using hydrocarbons, we’re penalized for those indirect emissions called Scope 2 emissions.

We also have Scope 1 emissions, which are significantly lower than our Scope 2 emissions, but are significant nonetheless. Now these emissions are largely as a result of using natural gas to make hydrogen, which is used by refiners to produce cleaner fuels.

Our gases play a critical role in the economy. In addition to saving lives, improving energy efficiency, increasing shelf life, our products also help our customers eliminate or reduce greenhouse gas emissions.

In 2020, we generated a total of 37 million metric tons of emissions to make products that helped our customers avoid more than twice our emissions or 85 million metric tons of CO2 equivalent. In other words, without Linde’s products, there would be significantly higher net carbon emissions in our world.
At Linde, we have been doing our part to support our planet for many decades, but we know we need to do more. In 2019, we set a goal to reduce the carbon intensity of Linde 35% by 2028. We are well ahead of that goal and expect to exceed it, which is, of course, good news.

But an intensity goal doesn’t fully address the absolute Scope 1 and Scope 2 emissions. So we are determined to continue on our mission of making our world more productive, enabling our customers to decarbonize and commit to reducing our own carbon footprint.

With that in mind, I’d like to announce Linde’s new medium- and long-term emission goals, which you will find on slide 5. The first goal is to achieve a 35% reduction in our Scope 1 and Scope 2 emissions by the year 2035 or simply 35 by 35.

To achieve this goal, we must materially reduce our Scope 1 emissions, which are driven by hydrogen production. We will do this by focusing our efforts on carbon capture and sequestration, developing blue and green hydrogen production and progressively transitioning to a zero-emission fleet.

Our Scope 2 emissions are related to electricity consumption. Today, we consume approximately 45 terawatt hours of power, a 1/3 of which is from renewable and low-carbon sources. In order to achieve the 35 by 35 goal, we will triple, triple our renewable and low-carbon power sourcing by 2035 through new PPAs and by supporting renewable energy projects with offtake agreements and even co-investment.

To put this goal in perspective, the amount of renewable energy we were planned to purchase is equivalent of all the power consumed annually in New York City. That’s a big number.

Of course, in addition to that, we will continue improving the energy efficiency of our plants as well. These goals are being embedded across the entire global organization, being reviewed as part of our operating rhythm and will be incorporated into our annual variable compensation.

This is what gives me the confidence in our ability to deliver these goals, which is no different than how we would approach anything of importance in our company. Now in addition to the 35 by 35 goal, we are also committed to pursuing our goal of becoming climate-neutral by 2050. We will do our part to achieve this goal, but we also need strong policy support and regulatory support.

Let me summarize this journey on Slide 6. We have defined a road map to reach climate neutrality. The road map is underpinned by numerous initiatives and milestones, which will be embedded into our operating system, providing us the greatest opportunity for success.

Going forward, we will continue to share our progress, ensuring accountability and transparency for our stakeholders.
I'll now turn it over to Matt to walk you through the numbers.

Matt White: Thanks, Sanjiv. Please turn to slide 7 for an overview of the third quarter results. Sales of $7.7 billion increased 12% over last year, and 1% from the second quarter. Cost pass-through, which represents the contractual billing of energy cost variances, primarily in the on-site business, rose 3% over last year and 2% sequentially.

Recall that cost pass-through has no effect on profit dollars, but will impact profit margins as we gross up or down sales and variable costs. Foreign exchange was a 2% tailwind versus prior year, but a 1% headwind sequentially, as most currencies have recently devalued against the U.S. dollar.

Excluding these items, underlying sales grew 11% over prior year and 1% sequentially. The 8% volume increase over last year was broad-based across all geographies and end markets, as we continue to see recovery from the pandemic.

Sequentially, volumes are flat as contribution from project start-ups were mostly offset by lower volumes in China. Pricing levels are up 3% from last year and 1% from the second quarter, as we continue to adjust merchant and packaged gas product pricing in line with local inflation.

Note that some of these contracts have lagging recovery mechanisms, which may not take effect for two to six months, depending upon the terms and conditions.

Operating margin of 23.6% is 150 basis points above 2020, but 60 basis points below the high mark set in the second quarter. Excluding the impact of cost pass-through, operating margin would have increased 220 basis points above last year and had a negligible decline sequentially.

As mentioned, merchant and package cost recovery can lag one to two quarters. So going forward, I expect continued pricing momentum.

EPS of $2.73 is up 27% over last year from higher volumes and price over a relatively stable cost base. As both Steve and Sanjiv mentioned, Linde has a strong productivity culture, which enables consistent profit growth, irrespective of the economic climate.

This is also evident in the 16.7% return on capital, which represents another record as profit continues to grow double-digit percent over a flat capital base. The reason we’ve been able to maintain such a steady capital base is due to a combination of disciplined capital management and healthy cash generation, which I’ll cover on slide 8.

You can see to the left, our operating cash progression resulting in a record level of $2.6 billion in the third quarter. The three main drivers are stronger earnings, timing benefits from last quarter and engineering
contract prepayments. In light of the record sale of plant backlog, I anticipate further project repayments into the next few quarters.

As far as how we allocated year-to-date cash, the pie chart to the right shows $2.3 billion invested into the business and $4.8 billion distributed back to shareholders through dividends and stock repurchases.

Note that investments exclude sale of plan, since we are paid in advance for engineering projects, which means that we are committing much larger amounts toward contractually secured growth than what’s shown on this chart. In addition to generating significant surplus cash we have access to very attractive capital through the debt markets.

In September, we issued almost EUR2 billion at 5-, 12- and 30-year maturities, with all-in coupons of 0%, 0.38% and 1%, respectively. Overall, the combination of excess cash generation and low-cost incremental debt gives us a high degree of confidence to maintain shareholder-friendly allocation policies over the long term.

I’ll wrap things up with guidance on slide 9. The fourth quarter EPS guidance range of $2.60 to $2.70 is 13% to 17% above last year and 38% to 43% above 2019. Consistent with prior quarters, we believe it’s important to distinguish true multiyear growth from mere recovery of 2020 recessionary conditions.

Versus the third quarter, this range represents a sequential decrease due to normal seasonal declines plus an estimated 1% foreign currency headwind. Underlying volumes are assumed to be roughly in line with the third quarter, but if current conditions hold, I’d expect to be at the upper end of this range.

This quarterly update results in a new full year guidance of $10.52 to $10.62, which represents a growth rate of 28% to 29% over 2020 and 43% to 45% over 2019.

In summary, another solid quarter despite some challenging conditions. And regardless of the macro, we remain confident in Linde’s ability to continue delivering industry-leading performance.

I’d now like to turn the call over to Q&A.

Operator: Thank you. If you would like to ask a question, please signal by pressing star 1 on your telephone keypad. If you are using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Again, press star 1 to ask a question. We’ll pause for just a moment to allow everyone an opportunity to signal for questions. We’ll take our first question from Bob Koort with Goldman Sachs.

Bob Koort: Good morning, thanks very much. I was wondering if you guys could comment a little bit on the hydrogen markets and your engagement there with customers and partners, how that may have evolved over the last several quarters? Maybe from the context of -- from the outside, it just seems like there’s a
massive broadening of participation as people start reaching for that opportunity. Just maybe give us some insights into how you've seen that evolving at Linde.

Sanjiv Lamba: Thanks, Bob. I'll take that very quickly. I agree with you that there's been significant and continuing momentum in the space. And I'm very pleased to suggest that we are seeing a reflection of that in the activities that we are actively pursuing. I'll start off by just describing what the opportunity pipeline looks like because that's reflective of the level of activity that Linde is seeing and then talk a little bit about the particular areas where we see some of that momentum reflected now.

So starting over the projects that we're looking at. As you know, we run this monthly call on the Hydrogen Council that Linde runs internally. We've got about 260 projects in our pipeline. We've got a probability weighted sort of conservatively probability weighted number in terms of investment decisions of up to $4-plus billion now. And these are decisions we expect to see happen in the next three years or so.

In the past, you've heard me say that we expect to see us investing about $1 billion a year roughly in this space. And then on top of that, there may be some mega projects that come along as well. So that's just to give you a sense of the level of activity that there is happening around that space.

Now remember, and I've said this before, Bob, so you'll kind of recall Linde has a unique position in what is happening in the evolving space around clean energy. We've kind of described to you previously, under decarbonization, we look at carbon solutions and we look at hydrogen. In the hydrogen space, we obviously are very mindful and interested in the developments around blue hydrogen.

We see that as a very important transition in this clean energy road map that lies ahead. And this is where we are seeing significant pickup in terms of activity. We are currently involved in a number of projects, which have a range of investments and those are progressing well. And again, for projects in this space to make sense, you need 3 things to be happening.

You need the technology provider, in this case, that is us, for carbon capture. You need partnerships to ensure that you're then looking at sequestration effectively with partners who have long-standing experience and knowledge of that space. We're currently actively pursuing those as well.

And of course, third, very importantly, you need an offtaker. You need a partner who is willing to stay in the game and actually offtake the blue hydrogen that comes off that and is able to create some value as a result of that.

For us, those three things are very important. And again, I'm pleased to say that we're seeing those partnerships actually take -- gather a lot of momentum as we move forward. I'll kind of stop there for a moment and give you -- see if that answered your question.
Bob Koort: Yes. That's very helpful. What about the competitive intensity is that landscape has been populated with more and more companies maybe trying to edge in on the turf that has historically belonged to the industrial gas companies?

Sanjiv Lamba: So the way I'd answer that, I think, Bob, is just to kind of remind you, a lot of -- so firstly, lots of announcements. I think you see them, we see them every day. And every morning, I wake up to this long list of announcements that are happening. A large number of people who make those announcements have either never seen or heard of hydrogen before this.

Most of them don't even understand that we have a colorless molecule that obviously is now defined by very, very many colors. But putting that aside in terms of experience and expertise. The reality is there will be a number of players who will make a difference in this space. And as part of that, you will see a range of outcomes.

You will see us competing where we need to, and you will see us partnering with a number of those as well. This is an area that requires strong partnerships for that initial momentum and the ecosystem development to really happen. And I see that development happened where we are kind of speaking to a range of partners across different areas helping move this along.

So I don't particularly kind of see this as a space that you're going to see the intensity of competition being any different to what we see otherwise.

Bob Koort: Very helpful. Thanks, Sanjiv.

Operator: We'll take our next question from Duffy Fischer with Barclays.

Duffy Fischer: Yes, good morning. First, I just want to say congrats to Sanjiv on great promotion, and thank you to Steve for the decade and a half. And I think from an investor standpoint, maybe even more from the way the transition was handled, almost picture perfect. So thank you, guys, all for that. I guess my question is around Lincare and maybe the medical business in general.

If you go back before COVID started and just kind of analyze how that business has developed with COVID as kind of a driver, how do you see that business structurally different today? And how much has it grown through that period relative to the rest of the business?

Sanjiv Lamba: Duffy, thanks. Let me get into it. And I'll start off by just taking a step back and outlining the health care space that we operate in and also reminding everyone that we have strong leadership in that space.

So we think of our health care business in two different areas. We look at hospital care, where we are the primary provider of medical gases to hospitals, and of course, a home care business, where as you
referenced, Lincare is a very, very important player in the U.S., but we obviously have smaller home care businesses elsewhere in the world as well.

So thinking structurally about that business, let me just kind of say to you, there are two things happening as we speak. Obviously, you've heard us talk about how we've -- how that business is supported and saved lives and supported hospitals and patients at home over the last 18-plus months now.

So clearly, it's played a very important role. Lincare, in particular, in the U.S. was almost seen as a second line of defense supporting COVID patients at home through the respiratory offerings that we have. What has happened as a consequence of the pandemic is that a number of regulators and governments have, in the best way to describe it is, woken up to the realities of how they need to manage this more professionally in terms of storage, in terms of piping, in terms of infrastructure necessary for these high levels of medical gases and oxygen, in particular, to be delivered to their infrastructure and network.

We have been participating in many of those conversations. In fact, most governments have reached out to us seeking support and help in structuring those conversations, and we are obviously leading many of those conversations across the world today where we are helping governments and regulators make sure that they have a well thought through infrastructure program and a development process around how they will manage this going forward.

A kind of pandemic preparedness a little bit late in the day, but nonetheless important to make sure for the future. The reason I mentioned this is because this means as we move forward, we're going to see continuing activity in this space, we will be participating in those activities and expecting a level of growth out of that.

We've said this before, Duffy, you've heard us describe mid-single-digit growth for our healthcare business overall, and I still maintain that we will see that. Obviously, in the Lincare world, in particular, tuck-in acquisition is something that we are very interested and excited about.

So we'll continue to see those come through, adding on to that mid-single digit or contributing to that mid-single digit that I referenced earlier on as well. So I do see this a solid secular growth trend. I see it progressing with a strong mid-single-digit growth that I described earlier on, and I see us seeing kind of areas in the world where we will see that probably grow it -- not probably, will grow at a higher pace, Asia being one such example.

Again, because of the strength of our footprint there, we have the ability to make sure that we leverage that footprint for that incremental growth in Asia as an example.

Duffy Fischer: Terrific. And then maybe just a quick one. As we start to look into 2022, when you look at just the new project growth coming on stream, how will that impact 2022 relative to what we've seen over the last couple of years?
Sanjiv Lamba: All right. So I have to say I expected that question, so that's good. Now so I want to maybe take a step back and just go back to what we said maybe a couple of earnings calls before, right? We committed to delivering a 10-plus percent EPS growth for the midterm.

As you can imagine, I feel pretty confident about that today as I'm sitting here. It's obviously supported by this very strong backlog that you just referenced. I had to say that this strong backlog will provide us with mid-single-digit EPS growth, if you like, for the next four years or so.

So that's a pretty strong contributor right there for you. Now on 2022 specifically, Duffy, I'm going to say to you that in about three weeks' time, we're going to spend three whole days with every region around the world going through our planning meeting. Steve mentioned to you how we have fun in Danbury, this is going to be one of those fun events.

We will review, we will dissect, we'll analyze their numbers and then in the end, we'll agree with them what they need to deliver for 2022. So I'm looking forward to coming back in January and giving you an update on the outlook and our guidance for 2022 once we've had this meeting.

Duffy Fischer: Great, thank you.

Operator: We'll take our next question from Nicola Tang with Exane BNP Paribas.

Nicola Tang: Thanks, everyone. Congratulations to both Steve and Sanjiv. First I'll ask a question on China. I think Matt, in your prepared remarks, you talked about volume weakness in China. I was wondering if you could comment on what you're seeing on the ground there in terms of sort of direct and indirect impacts from the energy control measures, I guess, both in terms of today -- the impact today and in terms of -- with respect to future investment opportunities?

And then the second question was on engineering, and congrats on this very big project. I think you used to talk about kind of mid -- or low to mid-teens through the cycle kind of margin. But we've been tracking above that for some time now.

And so I was wondering whether there's any reason to assume that this new business would be at a different margin to what we've been seeing in the recent past?

Matt White: Sure. Hi, Nicola, I can take this one. So starting with China, yes, to your point, we did see some volume curtailments as you would expect, with the power outages. We do feel very confident about our customer base. They're still paying the MTOP. These are Tier 1 customers. This is something you've seen, as you probably know, in prior times in China when there are some centrally managed slowdowns.
So from that perspective, yes, there were reductions on a sequential basis. Now if you look at the APAC segment, you actually see volumes are up 2% sequentially, and the primary driver there is because our backlog pretty much offset any of that China sequential decline.

And then the rest of our APAC business still performed quite well on growth, including some seasonal growth that we tend to see in the South Pacific. So from that perspective, yes, we had some of that. We anticipate a little bit of that to continue here into the fourth quarter.

So when we talked about volumes assumed to be flat sequentially into our guidance range, it does take into account some continuing just volume softness based on this. But overall, we feel very good about our asset base. We see this as temporary. And to some extent, we tend to come out stronger on these things with our customer base. So we'll see how that plays out.

On the engineering, you're exactly right, I mean, we have been operating kind of mid-teens or a little better. And as you can imagine, as you know, this business has pretty much a negative working capital. So what you see on the margins can be a pretty good indication of the type of returns you get or can even be a little better just based on the cash profile.

So very good business that we have. We're very excited to have this backlog. It will contribute to growth. We tend to focus more on the E&P side as well, which helps with the risk management. So from this perspective, we still see margins kind of in this, I'll call it, low- to mid-teens, and we'll see how it plays out though over the cycle. You will always have timing in how you recognize the percent completion.

So quarter-to-quarter, it's always tough to gauge on any particular one. But over the multiyear process, we still think that kind of low double-digit to mid-teens is still a reasonable estimate through this business as it kind of goes through the cycles.

Nicola Tang: Thank you. And if I may ask a follow-up question around sort of energy costs and not specifically related to China, but more globally. Obviously, with your business, it's clear in terms of the pass-through effect or the large pass-through effect. But I was wondering if you're seeing any impact on your customers deciding to idle or reduce production at their own facilities because of their own higher operating costs?

Matt White: Yes, sure. I can handle that one, Nicola. As you can imagine, on the on-site, business, we have our fixed payments, whether it's a facility payment or an MTOP. So from that perspective, we tend not to really have much risk to the production volumes given that it's not really anything I would be overly concerned with.

In fact, if anything, what we've seen, especially on our more industrial customers, they tend to run harder. You could think steel, you could think refining, given the environment they're in and the margins that they're making on some of these products.
As far as the merchant and package -- realizing package, it's a high rent business, so the volatility of the customers' demand will really only affect the gas molecules. And what we're seeing, especially in Americas and parts of Europe still seeing pretty strong growth across that package business. So I think that's been quite good.

But on the merchant side, no, we really haven't seen any significant negative changes. It's been up pretty much across the board. And you could imagine the customers want to produce, right? They want to make as much product as they can in this environment, given their opportunity to get some pricing.

So from that perspective, we haven't seen any material effect on that. There may be some small pockets, but nothing that's coming up to the aggregate level.

Nicola Tang: All right. Thank you so much.

Operator: We'll take our next question from Tony Jones with Redburn.

Tony Jones: Yes, good morning, everybody. I wanted to come back on the margins. So on an ex cost pass-through basis, margins are up all regions, in some cases, materially. Just wanted to check whether there are any positives in there that we should be thinking about that could reverse as we go into 2022? And are we getting now also to a stage where this is about as good as it gets? Thank you.

Stephen Angel: You want to answer that?

Sanjiv Lamba: Yes, I can answer that. So Tony, that's right. You can see the margins moving up. Ex pass-through year-on-year, our margins are up and a strong showing by all the segments within that. So I think we see that momentum of what we've been working on kind of playing out in Q3.

Now I don't really -- as I mentioned earlier on, we're going into the planning cycle on 2022. I have to say one of the variables as we think about this is, how does inflation play out and how do energy costs play out in the year ahead? I don't really want to be forecasting that, to be honest.

But what I do want to give you is some assurance on the pricing, which then clearly then flows into the margin piece and addresses your question, which is you can expect us to always be keeping pace with inflation, global inflation, and that really is a reflection of how we will do that management around the pass-through elements, in particular, and pricing beyond that.

And that's what will then come back through the leverage we have down to the operating margin that you'll see. So hopefully, we'll come back and tell you in January what we think is the outlook for 2022 with a bit more precision. But for now, you can expect us to keep pace on the pricing side with any cost inflation that we see.
Stephen Angel: Just to add a comment to what Sanjiv said, this is Steve. I think as we go forward, I don’t like to ever hear the word peak margins because I don’t never believe in peak margins. And when we say our best days are ahead, you got to keep in mind that we are going through a period where there’s been a tremendous amount of cost that came through the system, mostly in the form of power. If you were to look at EMEA, for example, costs increased 25% to 30% between Q2 and Q3.

So that’s a lot of cost that comes at you at once. We instantly pass that through, as Matt mentioned, on the on-site piece, but it takes a few months up to six months to be able to recover all of that through the merchant and the packaged business.

But if you think going forward over time, and you’ve heard us describe this model before, we take the top line, and we’re able to leverage that through pricing and productivity to deliver increased EBIT margins over the long term. And we’ve been able to do that for many years, and that’s really going to be the model that we will be in going forward, especially as we clear this immediate wave of cost inflation that’s coming through the system, and we deal with that in a very positive way in the coming quarters.

Tony Jones: Thank you. That’s really helpful. And if I could, just a small follow up on the 35 by 35 targets, I appreciate that also the update there. We’ve heard from some chemical companies that there’s like extra costs or CapEx required to get sustainability targets. Is that going to be the case for Linde? And maybe if so, you could help us think a bit about what that could look like? Thank you.

Sanjiv Lamba: So Tony, as we’ve put those targets up and we’ve built a road map around that, clearly, you would have seen in our description of how we want to achieve that. We are working - our mission here is to support our customers in their decarbonization attempt and ensuring that we have the technology and the solutions necessary for that. Now we make those commitments, keeping in mind the broader decarbonization trend that is happening.

And of course, in our support of that, we will need to make investments along the way, which we look at on a project-by-project basis. And each of those investments we’ve said this previously, obviously, need to kind of live up to our investment criteria.

They will, of course, be supported by incentives and carbon pricing or carbon penalties as the case might be, which actually makes that economic case necessary for that transition to successfully happen as we move forward. So I fully expect us to kind of see those economically feasible cases work out, ones that will actually have to meet our investment criteria as we support this broader transition for industry.

As you know well, Tony, whatever we emit ourselves is really there to ensure that we’re helping our customers either abate, avoid or completely eliminate emissions, and that goal continues to be what we’ll focus on going forward.
Tony Jones: Thank you, that’s great.

Operator: We’ll take our next question from Peter Clark with Société Générale.

Peter Clark: Yes. Thank you again. Congratulations to Sanjiv and Steve for one hell of a deal. And I guess the share price reflected the thought that went in the transition there. I’ve got two big picture questions really.

Looking at the engineering backlog and the way it’s grown, I think, Steve, you were commenting not so long ago that you saw a 50-50 as sort of a very nice mix in terms of what was internal, what was external. Obviously, as the cycle is picking up, with scoring now we’re at 75-25, just your thoughts on that, except obviously, you’re looking at your return criteria, et cetera, but just your thoughts on that as we go through the cycle?

And the second one is your comments about best days ahead, hopefully. Obviously, your return on capital now is 200 basis points above where Praxair were 10 years ago at the peak. Just wondering your thoughts on the return on capital, obviously, a lot of momentum to support that, but how you see this sort of on a structural basis as we move forward?

Are we structurally higher now with the -- all the benefits of the merger against what we thought we could get in gases prior to that? Those are my two questions. Thank you.

Stephen Angel: Well, given I’m not going to be the CEO past March 1, I really don’t want to provide too much long-range thinking about return on capital. But I think if you go back to what I said about being able to take growth, convert it to higher levels of profitability, good capital management.

Over the time, we should be able to march the return on capital number up a little higher. With respect to the 50-50 comment, if you think about -- when we book sale of gas projects, they typically are in the hundreds of millions of dollar range. So if you look at the TSMC project, that $600 million of capital investment that would be tied for our largest with Samsung. So when we see sale of gas, it tends to be -- that’s a very big project.

And clearly, we landed some very large projects, third-party projects with Linde Engineering, and that obviously shifted the weighting in terms of whatever that is, 75%, 80% of the total backlog is -- third-party sales is driven by these very large projects.

Matt alluded to this. These very large projects have very strong contractual terms. They’re very high-quality contracts, I will say. We have cash flows that -- incoming cash flows that certainly are well ahead of our cost outlays as we work through these projects. So they’re excellent projects, and we’re delighted to have them.
**Peter Clark:** Thank you.

Operator: We'll take our next question from David Begleiter with Deutsche Bank.

**David Begleiter:** Thank you. Looking at EMEA in Q3, can you quantify the amount of power costs that were not pass-through or captured during the quarter?

**Matt White:** Yes. So David, this is Matt. That's not a number we're going to provide publicly. But I think if you look at kind of the sequential margin profile and you adjust for the stated cost pass-through, that obviously associates itself with the on-site business. Some of those differentials could -- of the remaining amount are things that we would want to be going chasing related to some timing related.

And as you can imagine, EMEA has a much larger package and merchant percent than on-site. So that will also play into having a larger proportion of cost that need to be captured on a delay. And one thing I just want to be clear on is, this lag is normal. This lag is inherent in the industry.

We have faced this lag since our inception going back decades. It just so happens in this particular quarter, the movement of the energy prices, the movement of some of these numbers are faster in a shorter time period. So given that, you're going to have some recovery, that will be next quarter and the quarter after.

But EMEA would be probably disproportionately larger than most other regions with that lag, just given the packaged and merchant exposure.

**David Begleiter:** Got it. And given that, would you expect price mix to accelerate further in Q4 from the 3% we had in Q3?

**Matt White:** So as I stated in the prepared remarks, yes, we absolutely anticipate and expect the pricing momentum to continue, and this is something that as we go and recover this that will play into it. So that's our expectation.

**David Begleiter:** Thank you.

Operator: We'll take our next question from Jeff Zekauskas with JPMorgan.

**Jeff Zekauskas:** Thanks very much. The backlog and first sale of plant went up $6 billion sequentially. Can you talk about what it is that you're going to build? If you can talk about the customers, that would be great. If you can't, but how did it grow so much? And does that mean that your CapEx order of magnitude is now going to be, I don't know, $5.5 billion higher than you thought over a number of years to execute that?
And then lastly, so if you're getting, I don't know, $480 million into your cash flow statement from prepayments, but I take it that, that then will -- you'll fund that with capital expenditures later on. So in a certain sense, your cash flow from operations is overstated. Can you talk about those issues?

Matt White: Yes. Maybe I could start with the cash and then Sanjiv could talk about the backlog project itself. So just to make sure we level-set and get the accounting correct. This is sale of plant, so this never touches CapEx. This is under percent completion accounting. So what happens is the backlog that we have actually translates essentially 1:1 to sales, $1 backlog equals $1 sales.

And as we construct it, it goes to inventory and then when we meet the criteria, it's released out of inventory to sales. So therefore, it never actually hits CapEx, given the nature of how the structure works. And then as the prepayments come in, they sit on the balance sheet as a liability.

And then obviously, we work and deliver the performed work, which then goes against that liability to relieve that liability as we deliver. So this is a classic percent completion accounting style. So given that - - and maybe let's talk about the cash flow real quick. In this business, in this industry of engineering and percent completion, when you're in a declining backlog, what tends to happen is your cash outflows are obviously higher than your inflows because you are delivering on the work, the engineering, the procurement and you basically think of like a book-to-bill ratio, right?

So as your book-to-bill ratio starts to drop and drop and drop, you're going to have more cash outflow than inflow. Now that trend is reversed. So we've actually had more outflow than inflow over the last few quarters because we were building off a backlog that was shrinking.

Now it has grown dramatically, that process is reversing. As I mentioned in the prepared remarks, we have a few quarters. We expect some prepayments given the size and increase of this. And then we'll work them down over the next several years as the outflows go, but you still have more backlog that if you win, it can mitigate that.

So that's how to think about this. It's not in CapEx. That's why I said in the prepared remarks, the growth that we have is much greater than what's being shown in CapEx because of this delivery. And as Sanjiv had mentioned, we're going to be probably mid-single digit in terms of our contribution. So hopefully, that makes sense, but I can hand it off to Sanjiv to talk about the project.

Sanjiv Lamba: Thanks, Matt. So Jeff, let me just kind of talk through the project a little bit and give you a little bit of color on that. So we have the $6 billion incremental two large wins that we're talking about are the reason why you're seeing this significant buildup in our backlog.

We are very happy with these projects, I have to tell you. They are with a very high-quality customer. I am going to name the customer now just for you, which is Gazprom. It's a customer with whom we have
excellent relationships. We have got great experience thus far. We have got solid contract terms, which makes us pretty comfortable around taking on these large projects.

Also, as Matt kind of referenced, strong cash flows. I want to remind you also that these cash flows tend to come in, the inflows are ahead of any commitments we make. So we tend to be net positive as far as our cash curves are concerned. And of course, it's in an area where we've got good experience of execution. So again, you put all of that together, that's kind of the projects.

Now what are we building? Let me just give you a little bit of color on that. So we are building some GPPs. So these are gas processing plants for Gazprom at the site called Ust-Luga. And we're also building a separate project also at that same site, which is a separate win, but an important one also is an LNG plant for them.

I expect natural gas developments will continue given the energy kind of challenges that the world is seeing. And this is kind of a major milestone as Gazprom have continued down the path of investing in that space.

Jeff Zekauskas: Okay. Great. And then secondly, I think your cash balance was $4.7 billion. Is that too much? What should your normal cash balance be as you manage your cash flows?

Matt White: Yes, Jeff, I can answer that. Well, when you’re getting paid to take commercial paper for 65 basis points, you do end up with a little bit of a grossing up of your cash and CP. So yes, we're still getting paid up to five years on the curve with Europe. So our cash balances are swelling a little bit.

Now those are U.S. dollar cash balances. So they are earning a return, but we're also earning a return on what we're borrowing. So at this point, that is causing a bit of the swelling.

But as you've seen between our projects that we're undertaking, between some of the shareholder-friendly actions we're taking, we're going to keep working those cash balances down.

Jeff Zekauskas: Okay, great. Thank you so much.

Operator: We'll take our next question from Geoff Haire with UBS.

Geoff Haire: Hi, thanks very much for the opportunity. I just wanted to ask a sort of slightly longer-term question and maybe to Sanjiv. Obviously, the sustainability targets you've put out are great but I think you did mention that to achieve the sort of 20 -- the 35 by 35, you need government support. What happens if you don't get it? What can you do yourself without any government support, particularly thinking about green hydrogen and other sorts of areas?
Sanjiv Lamba: Thanks, Geoff. It's a good question. So I think when you think about the sustainability targets that we've put out there, 35 by 35, there is -- you have to think about the framework within which this is happening. So clearly, there are activities that we can undertake and we are undertaking today, which will continue to move in that direction.

These are efficiency programs. This is about fleet replacement, et cetera. So there are a number of initiatives that are ongoing and will continue to -- we'll continue to work towards, which will execute towards that. But it's also correct to say that even today, there are government initiatives of the government incentives available. So we're not suggesting that there is a complete void over here and then we need a complete kind of remake of that.

In the U.S., we have the 45Q that is being effectively utilized to look at investment profiles like this. Now I have to be honest and tell you that I'd much rather that 45Q, which currently provides $45 to $50 per tonne of CO2, be anywhere between $90 to $110 per CO2. That's where I would see the inflection point with momentum for development of these projects would significantly ramp up because there'd be an economic case for it.

In Europe, clearly, there's the ETS, the trading scheme that is currently valuing CO2 anywhere between EUR60 to EUR65 per ton. So again, as we see that move forward, where there is a plan similarly in Canada and South Korea and Australia, I could name a number of countries where these incentives or penalties are coming into play today.

So we're working in that environment. We think that more support is necessary. But there isn't a complete lack of support. So a number of our projects will be relying on the support infrastructure that's available through the incentives and penalties to leverage all that to continue down that decarbonization trend. And of course, as we look longer term to carbon neutrality in our assumption when we think about our road map, clearly, we've got some levels of support available.

They range anywhere between $100 to $200 per ton of CO2 in equivalent terms, longer term to make sure that we get to that level of the neutrality that we're talking about -- climate neutrality that we're talking about as being the goal that we achieved by then.

Stephen Angel: I'll just put a point on Sanjiv's excellent response to that. If you think about decarbonization and the cost of capturing the cost of sequestration, it can vary $80 to $120, something like that. And to really tip the scales in terms of capital investment to decarbonize, you're going to need something like that in terms of a carbon price. So up until now, the 45Q can work in certain projects. It's $50, the low carbon fuel standard in California provides some support, too.

But as we look forward to really make meaningful strides of decarbonization, you're going to need a stronger carbon price. That's our view.
**Geoff Haire:** Thank you.

**Operator:** Our next question comes from P.J. Juvekar with Citi.

**P.J. Juvekar:** Yes. Hi, good morning. On your slide 18 or the slide on blue hydrogen, is that where you’re seeing some order activity today? And then looking at your joint venture with ITM in electrolyzers, how do you see blue versus green hydrogen backlog, let’s say, in the next five years? And are your industrial customers wanting to go to blue hydrogen first before thinking about green hydrogen?

**Sanjiv Lamba:** P.J., the way I’m going to answer that question is to kind of take you back a step and just to remind you of some of the messaging that we provided in the previous earnings call. So I’ve said before that when people think about what hydrogen is most appropriate, one of the things you have to think about is the strength individual countries have, the assets that they have, where countries today have -- hydrocarbon assets have natural gas as an asset.

We firmly believe that they will pursue the path of blue hydrogen because that is the most meaningful way to kind of move forward on this transition. The reason it’s meaningful is because it’s to scale. It can be done today, and we’re not waiting for technology developments to happen.

And I’ll talk about ITM in a minute, but you’ll hear me reflect that comment over there as well. So the answer is where we see that natural gas resource available in the U.S. and Canada, Australia, Russia, Middle East, we believe -- we know that those countries are actively pursuing, and we are looking at a number of counterparties over there as partners looking at some of those developments ourselves.

So -- and the slide 18 gives you a sense that Linde Engineering’s technology portfolio allows us to be able to flex any technical solution. We are uniquely positioned to provide that technical solution for blue hydrogen output, whether it’s using an SMR, whether it’s using an ATR or whether it’s using gasifier. We have the ability and technology to provide the technology packages, execute them and operate them ourselves because of the expertise we have.

So that’s as far as blue hydrogen is concerned, and I do see a lot of momentum building up in that space, and we are very active in that space as well.

Let’s talk about ITM and order kind of intake and backlog going forward. Now you’re asking me to project five years out. I have to tell you, the only thing I’m going to project five years out is to tell you that the technology road map that we have going with ITM through our joint venture with them is to make sure that, that product scales up and that product then has the capital efficiency and operating efficiency in scale up to be able to then execute projects of a reasonable size.

I’m going to give you a very quick example of that. So today, as we are building as you know, you’ve heard us announce this before. We’re building a 24-megawatt electrolyzer complex there. Those 24
megawatts will come from 2-megawatt modules. That’s the largest PEM electrolyzer module available in the world today.

We’re working with ITM to scale that up. We are hoping to scale that up based on our technology road map in literally months to 5 megawatts and then beyond that to 20 megawatts, et cetera.

At that point in time, a 100-megawatt module, again, projects that we are actively working on today that are getting some preferential positioning as far as some European funding is concerned as well. Those will then move from 50 units of 2 megawatts, which you can imagine on the most efficient structure, to maybe 5 units or 20 units of 5 megawatts or 5 units of 20 megawatts as scale-up happens along the way.

So the fact that, that scale up is happening, the fact that the technology road map is providing that capital efficiency and economies of scale is happening right now and preparing us for what’s likely to happen in the next five years, I don’t want to speculate at this stage as to what that likely backlog might look like five years down the road, but clearly, I’m encouraged by the developments I see.

**P.J. Juvekar:** Great. Thank you for the detailed answer. As you look at this technology road map and green hydrogen costs coming down, where do you see that? I know Steve had commented on some numbers maybe a year ago. And what about this production tax credit of $3 for green hydrogen? How would that play out? Thank you.

**Sanjiv Lamba:** P.J., that production tax credit is actually very -- it will be a very good supporting mechanism. We talked earlier on about in the previous question about how we see the incentives support the development that $3 per kg will be a good support mechanism. We obviously have to read the rules and it hasn’t yet come through.

So I’m looking with some eagerness to that coming through and getting an understanding of how that -- how those rules come into play. But that would be encouraging. Clearly, we believe that there is an opportunity here for us to move forward.

Steve mentioned to you in the past that if we get hydrogen, blue or green, green, obviously more challenged in this reference, at about between $1 to $2 per kg, it’s at that point that you see an inflection point and you see widespread adoption of technologies utilizing hydrogen and really hydrogen becoming a reasonable fuel in the portfolio fuels we’ll have, we’ll always have fossil fuel, at least for many decades ahead. But it will be a more important part of that portfolio of fuels and energy basket as it will.

**Steve, do you want to add something?**

**Stephen Angel:** Okay, Sanjiv, I’ll add something. So yes, just to build on that, I mean, if you were to look at the cost of hydrogen today and you were to use the U.S. Gulf Coast, which obviously, we produce a lot of hydrogen, we use a lot of hydrogen in the U.S. Gulf Coast. Gray hydrogen is about $1.30 a kilogram, and
that's at $5.50 natural gas. Carbon capture would add another $0.40, $0.50, maybe you're in the $1.7 range sort. And if you think about green, it's like about $4.5 a kilogram.

And out of that, probably $2.50, you call it, is the renewable power cost. And so if renewable power was free, then you would still have $2. And we all know renewable power isn't free. So we have some work to do to bring those costs down in terms of capital costs, operating costs. And as you were to work that down below that $2 number, then you've got a chance to have something competitive.

So you need the combination of low-cost renewable, low-cost capital, lower cost operate low-cost capital and better efficiencies and then you can drive that number lower. And I would say ideally below $2, but certainly in that range would be is what's needed.

**P.J. Juvekar:** Great, thank you for the color and congratulations.

**Operator:** And our last question comes from Vincent Andrews with Morgan Stanley. Mr. Andrews, please go ahead with your question.

**Juan Pelaez:** (David), it looks like he has an issue. I think with that, we can wrap it up.

**Operator:** Okay.

**Juan Pelaez:** For everyone on the line, thank you so much for attending today's call. For your reference, a copy of our transcript will be posted on our Web site within the next 24 hours.

Thank you for listening. And anything else, let me know. Take care.

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