

FLOWSERVE CORP  
Form 10-Q  
July 28, 2016

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-Q  
(Mark One)

☒ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2016  
OR

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ to \_\_\_\_\_.

Commission File No. 1-13179

FLOWSERVE CORPORATION

(Exact name of registrant as specified in its charter)

New York 31-0267900  
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

5215 N. O'Connor Blvd., Suite 2300, Irving, Texas 75039  
(Address of principal executive offices) (Zip Code)

(972) 443-6500  
(Registrant's  
telephone  
number,  
including area  
code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. ☒ Yes ☐ No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). ☒ Yes ☐ No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "accelerated filer," "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☐ Accelerated filer ☐ Non-accelerated filer ☐ (do not check if a smaller reporting company)  
Smaller reporting company ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). ☐  
Yes ☒ No

As of July 20, 2016, there were 130,379,968 shares of the issuer's common stock outstanding.



FLOWSERVE CORPORATION  
FORM 10-Q  
TABLE OF CONTENTS

|  | Page<br>No. |
|--|-------------|
| <b><u>PART I – FINANCIAL INFORMATION</u></b>   |             |
| <b><u>Item 1. Financial Statements.</u></b>  |             |
| <u>Condensed Consolidated Statements of Income and Condensed Consolidated Statements of Comprehensive Income – Three Months Ended June 30, 2016 and 2015 (unaudited)</u> | <u>1</u>    |
| <u>Condensed Consolidated Statements of Income and Condensed Consolidated Statements of Comprehensive Income – Six Months Ended June 30, 2016 and 2015 (unaudited)</u>   | <u>2</u>    |
| <u>Condensed Consolidated Balance Sheets – June 30, 2016 and December 31, 2015 (unaudited)</u>   | <u>3</u>    |
| <u>Condensed Consolidated Statements of Cash Flows – Six Months Ended June 30, 2016 and 2015 (unaudited)</u>   | <u>4</u>    |
| <u>Notes to Condensed Consolidated Financial Statements (unaudited)</u>  | <u>5</u>    |
| <b><u>Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations.</u></b>   | <u>21</u>   |
| <b><u>Item 3. Quantitative and Qualitative Disclosures About Market Risk.</u></b>  | <u>35</u>   |
| <b><u>Item 4. Controls and Procedures.</u></b>   | <u>35</u>   |
| <b><u>PART II – OTHER INFORMATION</u></b>  |             |
| <b><u>Item 1. Legal Proceedings.</u></b>   | <u>36</u>   |
| <b><u>Item 1A. Risk Factors.</u></b>   | <u>36</u>   |
| <b><u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.</u></b>   | <u>36</u>   |
| <b><u>Item 6. Exhibits.</u></b>  | <u>37</u>   |
| <b><u>SIGNATURES</u></b>   | <u>38</u>   |
| EX-31.1  |             |
| EX-31.2  |             |
| EX-32.1  |             |
| EX-32.2  |             |
| EX-101 INSTANCE DOCUMENT   |             |
| EX-101 SCHEMA DOCUMENT   |             |
| EX-101 CALCULATION LINKBASE DOCUMENT   |             |
| EX-101 LABELS LINKBASE DOCUMENT  |             |
| EX-101 PRESENTATION LINKBASE DOCUMENT  |             |
| EX-101 DEFINITION LINKBASE DOCUMENT  |             |

Table of Contents

## PART I — FINANCIAL INFORMATION

## Item 1. Financial Statements.

## FLOWSERVE CORPORATION

## CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(Amounts in thousands, except per share data)

|   | Three Months Ended June 30, |             |
|---|-----------------------------|-------------|
|   | 2016                        | 2015        |
| Sales   | \$1,026,232                 | \$1,162,247 |
| Cost of sales   | (701,508 )                  | (793,155 )  |
| Gross profit  | 324,724                     | 369,092     |
| Selling, general and administrative expense                                       | (228,529 )                  | (243,594 )  |
| Net earnings from affiliates  | 1,809                       | 2,079       |
| Operating income  | 98,004                      | 127,577     |
| Interest expense  | (15,274 )                   | (15,392 )   |
| Interest income   | 645                         | 249         |
| Other income (expense), net   | 4,735                       | (4,882 )    |
| Earnings before income taxes  | 88,110                      | 107,552     |
| Provision for income taxes  | (25,122 )                   | (30,920 )   |
| Net earnings, including noncontrolling interests                                  | 62,988                      | 76,632      |
| Less: Net loss (earnings) attributable to noncontrolling interests                | 9                           | (1,624 )    |
| Net earnings attributable to Flowserve Corporation                                | \$62,997                    | \$75,008    |
| Net earnings per share attributable to Flowserve Corporation common shareholders: |                             |             |
| Basic   | \$0.48                      | \$0.56      |
| Diluted   | 0.48                        | 0.56        |
| Cash dividends declared per share   | \$0.19                      | \$0.18      |

## CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

(Amounts in thousands)

|   | Three Months Ended June 30, |          |
|---|-----------------------------|----------|
|   | 2016                        | 2015     |
| Net earnings, including noncontrolling interests  | \$62,988                    | \$76,632 |
| Other comprehensive (loss) income:  |                             |          |
| Foreign currency translation adjustments, net of taxes of \$17,049 and \$(8,161) respectively | (28,622 )                   | 13,666   |
| Pension and other postretirement effects, net of taxes of \$(1,877) and \$(134), respectively | 3,150                       | 1,780    |
| Cash flow hedging activity, net of taxes of \$(155) and \$(1,582), respectively               | 560                         | 3,427    |
| Other comprehensive (loss) income   | (24,912 )                   | 18,873   |
| Comprehensive income, including noncontrolling interests                                      | 38,076                      | 95,505   |
| Comprehensive loss (income) attributable to noncontrolling interests                          | 9                           | (3,059 ) |
| Comprehensive income attributable to Flowserve Corporation                                    | \$38,085                    | \$92,446 |

See accompanying notes to condensed consolidated financial statements.

Table of Contents

FLOWSERVE CORPORATION  
 CONDENSED CONSOLIDATED STATEMENTS OF INCOME  
 (Unaudited)

|   | Six Months Ended June 30, |              |
|---|---------------------------|--------------|
|   | 2016                      | 2015         |
| Sales   | \$1,973,480               | \$2,176,867  |
| Cost of sales   | (1,340,755 )              | (1,476,045 ) |
| Gross profit  | 632,725                   | 700,822      |
| Selling, general and administrative expense                                       | (465,439 )                | (483,521 )   |
| Net earnings from affiliates  | 5,128                     | 3,652        |
| Operating income  | 172,414                   | 220,953      |
| Interest expense  | (29,842 )                 | (31,429 )    |
| Interest income   | 1,318                     | 1,006        |
| Other income (expense), net   | 193                       | (24,828 )    |
| Earnings before income taxes  | 144,083                   | 165,702      |
| Provision for income taxes  | (42,812 )                 | (59,426 )    |
| Net earnings, including noncontrolling interests                                  | 101,271                   | 106,276      |
| Less: Net earnings attributable to noncontrolling interests                       | (415 )                    | (3,602 )     |
| Net earnings attributable to Flowserve Corporation                                | \$100,856                 | \$102,674    |
| Net earnings per share attributable to Flowserve Corporation common shareholders: |                           |              |
| Basic   | \$0.77                    | \$0.76       |
| Diluted   | 0.77                      | 0.76         |
| Cash dividends declared per share   | \$0.38                    | \$0.36       |

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
 (Unaudited)

|   | Six Months Ended June 30, |           |
|---|---------------------------|-----------|
|   | 2016                      | 2015      |
| Net earnings, including noncontrolling interests  | \$101,271                 | \$106,276 |
| Other comprehensive income (loss):  |                           |           |
| Foreign currency translation adjustments, net of taxes of \$(3,058) and \$55,400, respectively  | 5,135                     | (92,768 ) |
| Pension and other postretirement effects, net of taxes of \$(2,619) and \$(3,525), respectively | 5,936                     | 9,671     |
| Cash flow hedging activity, net of taxes of \$(420) and \$445, respectively                     | 1,203                     | (1,719 )  |
| Other comprehensive income (loss)   | 12,274                    | (84,816 ) |
| Comprehensive income, including noncontrolling interests  | 113,545                   | 21,460    |
| Comprehensive income attributable to noncontrolling interests                                   | (1,197 )                  | (5,056 )  |
| Comprehensive income attributable to Flowserve Corporation                                      | \$112,348                 | \$16,404  |

See accompanying notes to condensed consolidated financial statements.

Table of Contents

FLOWSERVE CORPORATION  
CONDENSED CONSOLIDATED BALANCE SHEETS  
(Unaudited)

| (Amounts in thousands, except par value)  | June 30,<br>2016 | December 31,<br>2015 |
|---|------------------|----------------------|
| <b>ASSETS</b>   |                  |                      |
| Current assets:   |                  |                      |
| Cash and cash equivalents   | \$266,013        | \$366,444            |
| Accounts receivable, net of allowance for doubtful accounts of \$46,768 and \$43,936, respectively      | 945,966          | 988,391              |
| Inventories, net  | 1,057,967        | 995,565              |
| Prepaid expenses and other  | 153,416          | 125,410              |
| Total current assets  | 2,423,362        | 2,475,810            |
| Property, plant and equipment, net of accumulated depreciation of \$881,655 and \$855,214, respectively | 755,105          | 758,427              |
| Goodwill  | 1,227,218        | 1,223,986            |
| Deferred taxes  | 71,439           | 69,327               |
| Other intangible assets, net  | 222,412          | 228,777              |
| Other assets, net   | 232,136          | 224,330              |
| Total assets  | \$4,931,672      | \$4,980,657          |
| <b>LIABILITIES AND EQUITY</b>   |                  |                      |
| Current liabilities:  |                  |                      |
| Accounts payable  | \$417,218        | \$491,378            |
| Accrued liabilities   | 750,728          | 796,764              |
| Debt due within one year  | 70,656           | 60,434               |
| Total current liabilities   | 1,238,602        | 1,348,576            |
| Long-term debt due after one year   | 1,543,557        | 1,560,562            |
| Retirement obligations and other liabilities  | 387,226          | 387,786              |
| Shareholders' equity:   |                  |                      |
| Common shares, \$1.25 par value   | 220,991          | 220,991              |
| Shares authorized – 305,000   |                  |                      |
| Shares issued – 176,793   |                  |                      |
| Capital in excess of par value  | 487,775          | 494,961              |
| Retained earnings   | 3,637,837        | 3,587,120            |
| Treasury shares, at cost – 47,065 and 47,703 shares, respectively                                       | (2,082,308 )     | (2,106,785 )         |
| Deferred compensation obligation  | 8,231            | 10,233               |
| Accumulated other comprehensive loss  | (528,550 )       | (540,043 )           |
| Total Flowserve Corporation shareholders' equity  | 1,743,976        | 1,666,477            |
| Noncontrolling interests  | 18,311           | 17,256               |
| Total equity  | 1,762,287        | 1,683,733            |
| Total liabilities and equity  | \$4,931,672      | \$4,980,657          |

See accompanying notes to condensed consolidated financial statements.

Table of Contents

FLOWSERVE CORPORATION  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
 (Unaudited)

| (Amounts in thousands)  | Six Months Ended |            |
|---|------------------|------------|
|   | June 30,<br>2016 | 2015       |
| Cash flows – Operating activities:  |                  |            |
| Net earnings, including noncontrolling interests                                | \$ 101,271       | \$ 106,276 |
| Adjustments to reconcile net earnings to net cash used by operating activities: |                  |            |
| Depreciation  | 50,071           | 49,270     |
| Amortization of intangible and other assets                                     | 8,341            | 17,833     |
| Loss on divestiture of business   | 7,664            | —          |
| Excess tax benefits from stock-based payment arrangements                       | (1,843 )         | (5,858 )   |
| Stock-based compensation  | 23,965           | 17,396     |
| Foreign currency and other non-cash adjustments                                 | 5,622            | 49,794     |
| Change in assets and liabilities, net of acquisition:                           |                  |            |
| Accounts receivable, net  | 41,348           | 45,376     |
| Inventories, net  | (51,864 )        | (113,005 ) |
| Prepaid expenses and other  | (27,057 )        | (21,015 )  |
| Other assets, net   | (7,308 )         | (22,435 )  |
| Accounts payable  | (76,421 )        | (124,001 ) |
| Accrued liabilities and income taxes payable                                    | (77,210 )        | (5,473 )   |
| Retirement obligations and other  | 3,324            | 7,003      |
| Net deferred taxes  | 3,377            | 16,903     |
| Net cash flows provided by operating activities                                 | 3,280            | 18,064     |
| Cash flows – Investing activities:  |                  |            |
| Capital expenditures  | (36,912 )        | (113,794 ) |
| Payments for acquisition, net of cash acquired                                  | —                | (341,545 ) |
| Proceeds from disposal of assets  | 1,427            | 1,872      |
| Payment for divestiture of business   | (5,064 )         | —          |
| Net cash flows used by investing activities                                     | (40,549 )        | (453,467 ) |
| Cash flows – Financing activities:  |                  |            |
| Excess tax benefits from stock-based payment arrangements                       | 1,843            | 5,858      |
| Payments on long-term debt  | (30,000 )        | (20,000 )  |
| Proceeds from issuance of senior notes  | —                | 526,332    |
| Payments of deferred loan cost  | —                | (5,108 )   |
| Proceeds under other financing arrangements                                     | 19,494           | 2,902      |
| Payments under other financing arrangements                                     | (11,441 )        | (7,631 )   |
| Repurchases of common shares  | —                | (139,644 ) |
| Payments of dividends   | (48,181 )        | (45,928 )  |
| Other   | (142 )           | 160        |
| Net cash flows (used) provided by financing activities                          | (68,427 )        | 316,941    |
| Effect of exchange rate changes on cash   | 5,265            | (16,584 )  |
| Net change in cash and cash equivalents   | (100,431 )       | (135,046 ) |
| Cash and cash equivalents at beginning of period                                | 366,444          | 450,350    |
| Cash and cash equivalents at end of period                                      | \$ 266,013       | \$ 315,304 |

See accompanying notes to condensed consolidated financial statements.





Table of Contents

FLOWSERVE CORPORATION

(Unaudited)

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation and Accounting Policies

Basis of Presentation

The accompanying condensed consolidated balance sheet as of June 30, 2016, the related condensed consolidated statements of income and comprehensive income for the three and six months ended June 30, 2016 and 2015, and the condensed consolidated statements of cash flows for the six months ended June 30, 2016 and 2015, of Flowserve Corporation are unaudited. In management's opinion, all adjustments comprising normal recurring adjustments necessary for fair statement of such condensed consolidated financial statements have been made. Where applicable, prior period information has been updated to conform to current year presentation.

The accompanying condensed consolidated financial statements and notes in this Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2016 ("Quarterly Report") are presented as permitted by Regulation S-X and do not contain certain information included in our annual financial statements and notes thereto. Accordingly, the accompanying condensed consolidated financial information should be read in conjunction with the audited consolidated financial statements presented in our Annual Report on Form 10-K for the year ended December 31, 2015 ("2015 Annual Report").

Venezuela – Our operations in Venezuela primarily consist of a service center that performs service and repair activities. Our Venezuelan subsidiary's sales for the three and six months ended June 30, 2016 represented less than 0.5% of consolidated sales and its assets at June 30, 2016 represented less than 0.5% of total consolidated assets. Assets primarily consisted of United States ("U.S.") dollar-denominated monetary assets and bolivar-denominated non-monetary assets at June 30, 2016. In addition, certain of our operations in other countries sell equipment and parts that are typically denominated in U.S. dollars directly to Venezuelan customers.

We continue to experience delays in collecting payment on our accounts receivable from the national oil company in Venezuela, our primary Venezuelan customer. These accounts receivable are primarily U.S. dollar-denominated and are not disputed. However, while we have not historically had write-offs relating to this customer, the accounts receivable continue to be significantly in arrears. The increased deterioration of the social, political, economic and legal climate in 2016 has given rise to significant uncertainties about Venezuela's economic and political stability, and while we continue to conduct business with our Venezuelan customer, the volume of activity has diminished significantly in 2016 from prior year levels. Accordingly, our ability to fully collect the accounts receivable from our primary Venezuelan customer could be materially adversely impacted. We continue to discuss payments with our Venezuelan customer and currently believe the accounts receivable will be collected; however, we will continue to evaluate collectability. Our total outstanding accounts receivable with this customer was approximately 7% of our gross accounts receivable at both June 30, 2016 and December 31, 2015. Given the experienced delays in collecting payments we estimate that approximately 69% of the outstanding accounts receivable will most likely not be collected within one year and therefore has been classified as long-term within other assets, net on our June 30, 2016 condensed consolidated balance sheet as compared to 64% at December 31, 2015.

At June 30, 2016 the DICOM exchange rate (formerly SIMADI) was 628.3 bolivars to the U.S. dollar, compared with the official exchange rate of 10.0 bolivars to the U.S. dollar. As of March 31, 2015, we determined, based on our specific facts and circumstances, that the SIMADI exchange rate was the most appropriate for the remeasurement of our Venezuelan subsidiary's bolivar-denominated net monetary assets in U.S. dollars. As a result of the remeasurement, in the first quarter of 2015 we recognized a loss of \$20.6 million of which \$18.5 million was reported in other income (expense), net and \$2.1 million in cost of goods sold in our condensed consolidated statement of income and resulted in no tax benefit. As of June 30, 2016, we believe the DICOM exchange rate continues to be the most appropriate rate to remeasure the U.S. dollar value of the assets, liabilities and results of operations of our Venezuelan subsidiary.

We are continuing to assess and monitor the ongoing impact of the changes in the Venezuelan foreign exchange market on our Venezuelan operations and imports into the market, including our Venezuelan subsidiary's ability to remit cash for dividends and other payments at the DICOM exchange rate, as well as additional government actions,

political and labor unrest, or other economic conditions that may adversely impact our future consolidated financial condition or results of operations.

Accounting Policies

Significant accounting policies, for which no significant changes have occurred in the six months ended June 30, 2016, are detailed in Note 1 to our consolidated financial statements included in our 2015 Annual Report.

## Table of Contents

### Accounting Developments

#### Pronouncements Implemented

In June 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-12 "Compensation-Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period." This ASU was issued to address share-based payment awards with a performance target affecting vesting that could be achieved after the employee's requisite service period. Our adoption of ASU No. 2014-12 effective January 1, 2016 did not have an impact on our consolidated financial condition and results of operations.

In November 2014, the FASB issued ASU No. 2014-16, "Derivatives and Hedging (Topic 815): "Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share Is More Akin to Debt or to Equity." This ASU was issued to clarify and reinforce the practice of evaluating all relevant terms and features when reviewing the nature of a host contract. Our adoption of ASU No. 2014-16 effective January 1, 2016 did not have an impact on our consolidated financial condition and results of operations.

In January 2015, the FASB issued ASU 2015-01, "Income Statement - Extraordinary and Unusual Items (Subtopic 225-20): Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items." In connection with the FASB's efforts to simplify accounting standards, the FASB released new guidance on simplifying Income Statement presentation by eliminating the concept of extraordinary items from accounting principles generally accepted in the U.S. ("U.S. GAAP"). Our adoption of ASU No. 2015-01 effective January 1, 2016 did not have an impact on our consolidated financial condition and results of operations.

In February 2015, the FASB issued ASU No. 2015-02, "Consolidation (Topic 810) - Amendments to the Consolidation Analysis," which provides guidance on the analysis process companies must perform in order to determine whether a legal entity should be consolidated. Our adoption of ASU No. 2015-02 effective January 1, 2016 did not have an impact on our consolidated financial condition and results of operations.

In April 2015, the FASB issued ASU No. 2015-03, "Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs." The ASU was issued in connection with the FASB's efforts to simplify accounting standards for the presentation of debt issuance costs. The ASU requires companies to present debt issuance costs in the same manner that debt discounts are currently reported, as a direct deduction from the carrying value of that debt liability. The applicability of this requirement does not impact the recognition and measurement guidance for debt issuance costs. In August 2015, the FASB issued ASU 2015-15, "Interest - Imputation of Interest (Subtopic 835-30): Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements—Amendments to SEC Paragraphs Pursuant to Staff Announcement at June 18, 2015 EITF Meeting (SEC Update)." In this ASU the SEC staff announced that it would "not object to an entity deferring and presenting debt issuance costs as an asset and subsequently amortizing the deferred debt issuance costs ratably over the term of the line-of-credit arrangement." We adopted the provisions of ASU 2015-03 and ASU 2015-15 as of January 1, 2016. Prior period amounts have been reclassified to conform to the current period presentation. As of December 31, 2015, \$10.3 million of debt issuance costs were reclassified in our consolidated balance sheet from other assets, net to long-term debt. Our adoption of ASU No. 2015-03 and ASU No. 2015-15 did not have an impact on our consolidated results of operations.

In May 2015, the FASB issued ASU No. 2015-07, "Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent) (a consensus of the Emerging Issues Task Force)." The ASU removes the requirement to categorize all investments for which fair value is measured using the net asset value per share practical expedient within the fair value hierarchy. Our adoption of ASU No. 2015-07 effective January 1, 2016 did not have an impact on our consolidated financial condition and results of operations.

In November 2015, the FASB issued ASU No. 2015-17, Balance Sheet Classification of Deferred Taxes to simplify the presentation of deferred income taxes. The ASU requires that deferred tax liabilities and assets be classified as noncurrent on the balance sheet. We adopted ASU No. 2015-17 effective January 1, 2016 and as a result, prior period amounts have been reclassified to conform to the current period presentation. As of December 31, 2015, \$156.0 million of deferred tax assets and \$11.4 million of deferred tax liabilities were reclassified from current to noncurrent on our balance sheet. Our adoption of ASU No. 2015-17 did not have an impact on our consolidated results of

operations.

**Pronouncements Not Yet Implemented**

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers (Topic 606)" which supersedes the revenue recognition requirements in "Revenue Recognition (Topic 605)." The standard is principle-based and provides a five-step model to determine when and how revenue is recognized. The core principle is that a company should recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. There are also expanded disclosure requirements in this ASU. In

## Table of Contents

August 2015, the FASB issued ASU No. 2015-14, "Revenue from Contracts with Customers (Topic 606): Deferral of Effective Date." As a result, public entities will apply the new standard for annual reporting periods beginning after December 15, 2017, including interim periods within those reporting periods. Early adoption as of the original public entity effective date is permitted. In March 2016, the FASB issued ASU No. 2016-08, "Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations". This update is simply a clarification of the implementation guidance on principle versus agent considerations. In April 2016, the FASB issued ASU No. 2016-10, "Identifying Performance Obligations and Licensing", which amends certain aspects of ASU No. 2014-09. In May 2016, the FASB issued ASU No. 2016-11, "Rescission of SEC Guidance Because of ASU No. 2014-09 and ASU No. 2014-16; this ASU rescinds specific SEC guidance on accounting for shipping and handling fees and costs and consideration given by a vendor to a customer. Additionally, in May 2016, the FASB issued ASU No. 2016-12, "Revenue from Contracts with Customers (Topic 606), Narrow-Scope Improvements and Practical Expedients." This ASU amends and clarifies the ASU No. 2016-09 guidance on assessing collectibility, presenting sales taxes, measuring non-cash consideration, and certain transition matters. We are currently evaluating the impact of ASU No. 2014-09 and all related ASU's on our consolidated financial condition and results of operations. Although we are continuing to evaluate, upon initial qualitative evaluation, we believe some anticipated key changes upon adoption will be potentially increased "over-time" revenue recognition and potential changes to the balance sheet related to accounts receivable, contract assets and contract liabilities.

In August 2014, the FASB issued ASU No. 2014-15, "Presentation of Financial Statements - Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern." This ASU requires management to evaluate whether there are conditions or events that raise substantial doubt about the ability of a company to continue as a going concern for one year from the date the financial statements are issued or within one year after the date that the financial statements are available to be issued when applicable. Further, the ASU provides management guidance regarding its responsibility to disclose the ability of a company to continue as a going concern in the notes to the financial statements. This ASU is effective for annual periods ending after December 15, 2016, and interim periods thereafter, with early adoption permitted. The adoption of ASU No. 2014-15 is not expected to have an impact on our consolidated financial condition and results of operations.

In July 2015, the FASB issued ASU No. 2015-11, "Inventory (Topic 330): Simplifying the Measurement of Inventory." The ASU updates represent changes to simplify the subsequent measurement of inventory. Previous to the issuance of this ASU, ASC 330 required that an entity measure inventory at the lower of cost or market. The amendments of ASU 2015-11 update narrows that "market" requirement to "net realizable value," which is defined by the ASU as the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. This ASU is effective for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2016. Application of this ASU is to be made prospectively, earlier application is permitted as of the beginning of an interim or annual reporting period. The adoption of ASU No. 2015-11 is not expected to have a material impact on our consolidated financial condition and results of operations.

In January 2016, the FASB issued ASU No. 2016-01, "Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities." The ASU requires entities to measure equity investments that do not result in consolidation and are not accounted for under the equity method at fair value with changes in fair value recognized in net income. The ASU also requires an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments. The requirement to disclose the method(s) and significant assumptions used to estimate the fair value for financial instruments measured at amortized cost on the balance sheet has been eliminated by this ASU. This ASU is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. We are currently evaluating the impact of ASU No. 2016-01 on our consolidated financial condition and results of operations.

In February 2016, the FASB issued ASU No. 2016-02, "Leases (Topic 842)". The ASU requires that organizations that lease assets recognize assets and liabilities on the balance sheet for the rights and obligations created by those leases. The ASU will affect the presentation of lease related expenses on the income statement and statement of cash flows

and will increase the required disclosures related to leases. This ASU is effective for annual periods ending after December 15, 2018, and interim periods thereafter, with early adoption permitted. We are currently evaluating the impact of ASU No. 2016-02 on our consolidated financial condition and results of operations. Although we are continuing to evaluate, upon initial qualitative evaluation, we believe a key change upon adoption will be the balance sheet recognition of leased assets and liabilities. Based on our qualitative evaluation to date, we believe that any changes in income statement recognition will not be material.

In March 2016, the FASB issued ASU No. 2016-09, "Compensation - Stock Compensation (Topic 718), Improvements to Employee Share-Based Payment Accounting." The ASU affects the accounting for employee share-based payment transactions as it relates to accounting for income taxes, accounting for forfeitures, and statutory tax withholding requirements. This ASU is effective for annual periods ending after December 15, 2016, and interim periods within those periods with early adoption permitted. We are currently evaluating the impact of ASU No. 2016-09 on our consolidated financial condition and results of operations.

Table of Contents

In June 2016, the FASB issued ASU No. 2016-13, "Financial Instruments—Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments. The amendments in this ASU replace the current incurred loss impairment methodology with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. This ASU is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. We are currently evaluating the impact of ASU No. 2016-13 on our consolidated financial condition and results of operations.

## 2. Acquisition

## SIHI Group B.V.

Effective January 7, 2015, we acquired for inclusion in Industrial Product Division ("IPD"), 100% of SIHI Group B.V. ("SIHI"), a global provider of engineered vacuum and fluid pumps and related services, primarily servicing the chemical market, as well as the pharmaceutical, food & beverage and other process industries, in a stock purchase for €286.7 million (\$341.5 million based on exchange rates in effect at the time the acquisition closed and net of cash acquired) in cash. The acquisition was funded using approximately \$110 million in available cash and approximately \$255 million in initial borrowings from our Revolving Credit Facility, which was subsequently paid down with a portion of the net proceeds from our 2022 EUR Senior Notes. SIHI, based in The Netherlands, has operations primarily in Europe and, to a lesser extent, the Americas and Asia.

The purchase price was allocated to the assets acquired and liabilities assumed based on estimates of fair values at the date of acquisition and is summarized below:

|  | (Amounts<br>in<br>millions) |
|--|-----------------------------|
| Accounts receivable                                    | \$ 59.3                     |
| Inventories  | 74.0                        |
| Prepaid expenses and other                             | 17.7                        |
| Total current assets                                   | 151.0                       |
| Intangible assets                                      |                             |
| Trademarks   | 20.9                        |
| Existing customer relationships                        | 45.3                        |
| Backlog  | 8.5                         |
| Engineering drawings and other                         | 3.9                         |
| Total intangible assets                                | 78.6                        |
| Property, plant and equipment                          | 94.5                        |
| Long-term deferred tax asset                           | 11.7                        |
| Investments in affiliates                              | 7.3                         |
| Total assets   | 343.1                       |
| Current liabilities                                    | (88.0 )                     |
| Noncurrent liabilities                                 | (114.7 )                    |
| Net assets   | 140.4                       |
| Goodwill   | 201.1                       |
| Purchase price, net of cash acquired of \$23.4 million | \$ 341.5                    |

The excess of the acquisition date fair value of the total purchase price over the estimated fair value of the net assets was recorded as goodwill. Goodwill of \$201.1 million represents the value expected to be obtained from strengthening Flowserve's portfolio of products and services through the addition of SIHI's engineered vacuum and fluid pumps, as well as the associated aftermarket services and parts. The goodwill related to this acquisition is recorded in the IPD segment and is not expected to be deductible for tax purposes. The trademarks are primarily indefinite-lived intangibles. As of date of acquisition existing customer relationships, engineering drawings and backlog had expected weighted average useful lives of 10 years, 10 years and less than one year, respectively. In total, amortizable intangible assets have a weighted average useful live of approximately 9 years.

### 3. Stock-Based Compensation Plans

We maintain the Flowserve Corporation Equity and Incentive Compensation Plan (the "2010 Plan"), which is a shareholder-approved plan authorizing the issuance of up to 8,700,000 shares of our common stock in the form of restricted shares, restricted share units and performance-based units (collectively referred to as "Restricted Shares"), incentive stock options, non-statutory



Table of Contents

stock options, stock appreciation rights and bonus stock. Of the 8,700,000 shares of common stock authorized under the 2010 Plan, 3,152,773 were available for issuance as of June 30, 2016. The long-term incentive program was amended to allow Restricted Shares granted after January 1, 2016 to employees who retire and have achieved at least 55 years of age and 10 years of service to continue to vest over the original vesting period. No stock options have been granted since 2006.

Restricted Shares – Awards of Restricted Shares are valued at the closing market price of our common stock on the date of grant. The unearned compensation is amortized to compensation expense over the vesting period of the restricted shares. We had unearned compensation of \$36.2 million and \$30.2 million at June 30, 2016 and December 31, 2015, respectively, which is expected to be recognized over a weighted-average period of approximately two years. These amounts will be recognized into net earnings in prospective periods as the awards vest. The total fair value of Restricted Shares vested during the three months ended June 30, 2016 and 2015 was \$1.8 million and \$1.6 million, respectively. The total fair value of Restricted Shares vested during the six months ended June 30, 2016 and 2015 was \$38.1 million and \$39.3 million, respectively.

We recorded stock-based compensation expense of \$5.2 million (\$8.0 million pre-tax) and \$5.5 million (\$8.3 million pre-tax) for the three months ended June 30, 2016 and 2015, respectively. We recorded stock-based compensation expense of \$15.7 million (\$24.0 million pre-tax) and \$11.5 million (\$17.4 million pre-tax) for the six months ended June 30, 2016 and 2015, respectively.

The following table summarizes information regarding Restricted Shares:

|        |                  |  |
|--------|------------------|--|
|        | Six Months Ended |  |
|        | June 30, 2016    |  |
|        | Weighted         |  |
|        | Average          |  |
| Shares | Grant-Date       |  |
|        | Fair             |  |
|        | Value            |  |

Number of unvested shares:

|                               |            |          |
|-------------------------------|------------|----------|
| Outstanding - January 1, 2016 | 1,540,843  | \$ 58.14 |
| Granted                       | 885,165    | 39.44    |
| Vested                        | (695,843 ) | 54.81    |
| Canceled                      | (114,502 ) | 52.55    |
| Outstanding - June 30, 2016   | 1,615,663  | \$ 49.72 |

Unvested Restricted Shares outstanding as of June 30, 2016, includes approximately 873,000 units with performance-based vesting provisions. Performance-based units are issuable in common stock and vest upon the achievement of pre-defined performance targets, primarily based on our average annual return on net assets over a three-year period as compared with the same measure for a defined peer group for the same period. Most units were granted in three annual grants since January 1, 2014 and have a vesting percentage between 0% and 200% depending on the achievement of the specific performance targets. Compensation expense is recognized ratably over a cliff-vesting period of 36 months, based on the fair market value of our common stock on the date of grant, as adjusted for anticipated forfeitures. During the performance period, earned and unearned compensation expense is adjusted based on changes in the expected achievement of the performance targets. Vesting provisions range from 0 to approximately 1,671,000 shares based on performance targets. As of June 30, 2016, we estimate vesting of approximately 908,000 shares based on expected achievement of performance targets.

#### 4. Derivative Instruments and Hedges

Our risk management and foreign currency derivatives and hedging policy specifies the conditions under which we may enter into derivative contracts. See Notes 1 and 6 to our consolidated financial statements included in our 2015 Annual Report and Note 6 of this Quarterly Report for additional information on our derivatives. We enter into foreign exchange forward contracts to hedge our cash flow risks associated with transactions denominated in currencies other than the local currency of the operation engaging in the transaction. All designated foreign exchange

hedging instruments are highly effective as of June 30, 2016.

Foreign exchange contracts designated as hedging instruments had a notional value of \$10.2 million and \$21.0 million, at June 30, 2016 and December 31, 2015, respectively. Foreign exchange contracts with third parties not designated as hedging instruments had a notional value of \$404.4 million and \$376.3 million, at June 30, 2016 and December 31, 2015, respectively. At June 30, 2016, the length of foreign exchange contracts currently in place ranged from one day to 19 months.

We are exposed to risk from credit-related losses resulting from nonperformance by counterparties to our financial instruments. We perform credit evaluations of our counterparties under foreign exchange contracts agreements and expect all counterparties to meet their obligations. We have not experienced credit losses from our counterparties.

Table of Contents

The fair value of foreign exchange contracts not designated as hedging instruments are summarized below:

|                                   | June 30, December 31, |          |
|-----------------------------------|-----------------------|----------|
| (Amounts in thousands)            | 2016                  | 2015     |
| Current derivative assets         | \$ 6,726              | \$ 2,364 |
| Noncurrent derivative assets      | 23                    | —        |
| Current derivative liabilities    | 1,242                 | 3,196    |
| Noncurrent derivative liabilities | 221                   | 441      |

The fair value of foreign exchange contracts designated as hedging instruments are summarized below:

|                                | June 30, December 31, |       |
|--------------------------------|-----------------------|-------|
| (Amounts in thousands)         | 2016                  | 2015  |
| Current derivative assets      | \$ —                  | \$ 26 |
| Current derivative liabilities | 71                    | 1,448 |

Current and noncurrent derivative assets are reported in our condensed consolidated balance sheets in prepaid expenses and other and other assets, net, respectively. Current and noncurrent derivative liabilities are reported in our condensed consolidated balance sheets in accrued liabilities and retirement obligations and other liabilities, respectively.

The impact of net changes in the fair values of foreign exchange contracts are summarized below:

|                           | Three Months   |         | Six Months     |          |
|---------------------------|----------------|---------|----------------|----------|
|                           | Ended June 30, |         | Ended June 30, |          |
| (Amounts in thousands)    | 2016           | 2015    | 2016           | 2015     |
| Gain recognized in income | \$4,300        | \$1,901 | \$6,361        | \$26,981 |

Gains and losses recognized in our condensed consolidated statements of income for foreign exchange contracts are classified as other expense, net.

In March 2015, we designated €255.7 million of our €500.0 million Euro senior notes discussed in Note 5 as a net investment hedge of our investments in certain of our international subsidiaries that use the Euro as their functional currency. We used the spot method to measure the effectiveness of our net investment hedge. Under this method, for each reporting period, the change in the carrying value of the Euro senior notes due to remeasurement of the effective portion is reported in accumulated other comprehensive loss on our condensed consolidated balance sheet and the remaining change in the carrying value of the ineffective portion, if any, is recognized in other income (expense), net in our condensed statement of income. We evaluate the effectiveness of our net investment hedge on a prospective basis at the beginning of each quarter. We did not record any ineffectiveness for the six months ended June 30, 2016.

#### 5. Debt

Debt, including capital lease obligations, consisted of:

|   | June 30,    | December 31, |
|---|-------------|--------------|
| (Amounts in thousands, except percentages)  | 2016        | 2015(1)      |
| 1.25% EUR Senior Notes due March 17, 2022, net of unamortized discount and debt issuance costs of \$6,636 and \$7,034                       | \$548,564   | \$535,966    |
| 4.00% USD Senior Notes due November 15, 2023, net of unamortized discount and debt issuance costs of \$3,158 and \$3,339                    | 296,842     | 296,661      |
| 3.50% USD Senior Notes due September 15, 2022, net of unamortized discount and debt issuance costs of \$4,149 and \$4,445                   | 495,851     | 495,555      |
| Term Loan Facility, interest rate of 1.88% at June 30, 2016 and 1.86% at December 31, 2015, net of debt issuance costs of \$952 and \$1,181 | 254,048     | 283,819      |
| Capital lease obligations and other borrowings  | 18,908      | 8,995        |
| Debt and capital lease obligations  | 1,614,213   | 1,620,996    |
| Less amounts due within one year  | 70,656      | 60,434       |
| Total debt due after one year   | \$1,543,557 | \$1,560,562  |

(1) Prior period information has been updated to conform to presentation requirements as prescribed by ASU No. 2015-03, "Interest - Imputation of Interest (Subtopic 835-30).

#### Senior Credit Facility

As discussed in Note 10 to our consolidated financial statements included in our 2015 Annual Report, our credit agreement provides for an initial \$400.0 million term loan ("Term Loan Facility") and a \$1.0 billion revolving credit facility ("Revolving Credit Facility" and, together with the Term Loan Facility, the "Senior Credit Facility") with a maturity date of October 14, 2020. As of June 30, 2016 and December 31, 2015, we had no amounts outstanding under the Revolving Credit Facility. We had outstanding letters of credit of \$103.4 million and \$105.2 million at June 30, 2016 and December 31, 2015, respectively, which contributed to the reduction of our borrowing capacity to \$877.3 million and \$894.8 million, respectively. Our compliance with applicable financial covenants under the Senior Credit Facility is tested quarterly, and we complied with all applicable covenants as of June 30, 2016.

We may prepay loans under our Senior Credit Facility in whole or in part, without premium or penalty, at any time. A commitment fee, which is payable quarterly on the daily unused portions of the Senior Credit Facility, was 0.150% (per annum) during the period ended June 30, 2016. During the six months ended June 30, 2016, we made scheduled repayments of \$30.0 million under our Term Loan Facility. We have scheduled repayments of \$15.0 million due in each of the next four quarters on our Term Loan Facility.

#### Fair Value

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Where available, fair value is based on observable market prices or parameters or derived from such prices or parameters. Where observable prices or inputs are not available, valuation models may be applied. Assets and liabilities recorded at fair value in our condensed consolidated balance sheets are categorized by hierarchical levels based upon the level of judgment associated with the inputs used to measure their fair values. Recurring fair value measurements are limited to investments in derivative instruments. The fair value measurements of our derivative instruments are determined using models that maximize the use of the observable market inputs including interest rate curves and both forward and spot prices for currencies, and are classified as Level II under the fair value hierarchy. The fair values of our derivatives are included in Note 4.

Our financial instruments are presented at fair value in our condensed consolidated balance sheets, with the exception of our long-term debt. The estimated fair value of our long-term debt, excluding the Senior Notes, approximates the carrying value and is classified as Level II under the fair value hierarchy. The carrying value of our debt is included in Note 5. The estimated fair value of our Senior Notes at June 30, 2016 was \$1,372.1 million compared to the carrying value of \$1,341.3 million. The estimated fair value of the Senior Notes is based on Level I quoted market rates. The carrying amounts of our other financial instruments (e.g., cash and cash equivalents, accounts receivable, net, accounts payable and short-term debt) approximated fair value due to their short-term nature at June 30, 2016 and December 31, 2015.

#### 7. Inventories

Inventories, net consisted of the following:

|                                   | June 30,    | December   |
|-----------------------------------|-------------|------------|
| (Amounts in thousands)            | 2016        | 31, 2015   |
| Raw materials                     | \$390,533   | \$390,998  |
| Work in process                   | 769,040     | 739,227    |
| Finished goods                    | 256,897     | 235,083    |
| Less: Progress billings           | (273,501 )  | (285,582 ) |
| Less: Excess and obsolete reserve | (85,002 )   | (84,161 )  |
| Inventories, net                  | \$1,057,967 | \$995,565  |



Table of Contents

## 8. Earnings Per Share

The following is a reconciliation of net earnings of Flowserve Corporation and weighted average shares for calculating net earnings per common share. Earnings per weighted average common share outstanding was calculated as follows:

|  | Three Months<br>Ended June 30, |           |
|--|--------------------------------|-----------|
| (Amounts in thousands, except per share data)                  | 2016                           | 2015      |
| Net earnings of Flowserve Corporation                          | \$62,997                       | \$75,008  |
| Dividends on restricted shares not expected to vest            | 2                              | 3         |
| Earnings attributable to common and participating shareholders | \$62,999                       | \$75,011  |
| Weighted average shares:                                       |                                |           |
| Common stock   | 130,180                        | 133,742   |
| Participating securities                                       | 274                            | 495       |
| Denominator for basic earnings per common share                | 130,454                        | 134,237   |
| Effect of potentially dilutive securities                      | 456                            | 594       |
| Denominator for diluted earnings per common share              | 130,910                        | 134,831   |
| Earnings per common share:                                     |                                |           |
| Basic  | \$0.48                         | \$0.56    |
| Diluted  | 0.48                           | 0.56      |
|  | Six Months Ended<br>June 30,   |           |
| (Amounts in thousands, except per share data)                  | 2016                           | 2015      |
| Net earnings of Flowserve Corporation                          | \$100,856                      | \$102,674 |
| Dividends on restricted shares not expected to vest            | 3                              | 6         |
| Earnings attributable to common and participating shareholders | \$100,859                      | \$102,680 |
| Weighted average shares:                                       |                                |           |
| Common stock   | 129,981                        | 134,065   |
| Participating securities                                       | 318                            | 513       |
| Denominator for basic earnings per common share                | 130,299                        | 134,578   |
| Effect of potentially dilutive securities                      | 563                            | 815       |
| Denominator for diluted earnings per common share              | 130,862                        | 135,393   |
| Earnings per common share:                                     |                                |           |
| Basic  | \$0.77                         | \$0.76    |
| Diluted  | 0.77                           | 0.76      |

Diluted earnings per share above is based upon the weighted average number of shares as determined for basic earnings per share plus shares potentially issuable in conjunction with stock options and Restricted Shares.

## 9. Legal Matters and Contingencies

## Asbestos-Related Claims

We are a defendant in a substantial number of lawsuits that seek to recover damages for personal injury allegedly caused by exposure to asbestos-containing products manufactured and/or distributed by our heritage companies in the past. While the overall number of asbestos-related claims has generally declined in recent years, there can be no assurance that this trend will continue, or that the average cost per claim will not further increase. Asbestos-containing materials incorporated into any such products were encapsulated and used as internal components of process equipment, and we do not believe that any significant emission of asbestos fibers occurred during the use of this equipment.

Our practice is to vigorously contest and resolve these claims, and we have been successful in resolving a majority of claims with little or no payment. Historically, a high percentage of resolved claims have been covered by applicable insurance or indemnities from other companies, and we believe that a substantial majority of existing claims should continue to be covered by insurance or indemnities. Accordingly, we have recorded a liability for our estimate of the

most likely settlement of asserted claims and a related receivable from insurers or other companies for our estimated recovery, to the extent we believe that the amounts of

11

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## Table of Contents

recovery are probable and not otherwise in dispute. While unfavorable rulings, judgments or settlement terms regarding these claims could have a material adverse impact on our business, financial condition, results of operations and cash flows, we currently believe the likelihood is remote.

Additionally, we have claims pending against certain insurers that, if resolved more favorably than reflected in the recorded receivables, would result in discrete gains in the applicable quarter. We are currently unable to estimate the impact, if any, of unasserted asbestos-related claims, although future claims would also be subject to then existing indemnities and insurance coverage.

### United Nations Oil-for-Food Program

In mid-2006, the French authorities began an investigation of over 170 French companies, of which one of our French subsidiaries was included, concerning suspected inappropriate activities conducted in connection with the United Nations Oil for Food Program. As previously disclosed, the French investigation of our French subsidiary was formally opened in the first quarter of 2010, and our French subsidiary filed a formal response with the French court. In July 2012, the French court ruled against our procedural motions to challenge the constitutionality of the charges and quash the indictment. Hearings occurred on April 1-2, 2015, and the Company presented its defense and closing arguments. On June 18, 2015, the French court issued its ruling dismissing the case against the Company and the other defendants. However, on July 1, 2015, the French prosecutor lodged an appeal. We currently do not expect to incur additional case resolution costs of a material amount in this matter. However, if the French authorities ultimately take enforcement action against our French subsidiary regarding its investigation, we may be subject to monetary and non-monetary penalties, which we currently do not believe will have a material adverse financial impact on our company.

### Other

We are currently involved as a potentially responsible party at five former public waste disposal sites in various stages of evaluation or remediation. The projected cost of remediation at these sites, as well as our alleged "fair share" allocation, will remain uncertain until all studies have been completed and the parties have either negotiated an amicable resolution or the matter has been judicially resolved. At each site, there are many other parties who have similarly been identified. Many of the other parties identified are financially strong and solvent companies that appear able to pay their share of the remediation costs. Based on our information about the waste disposal practices at these sites and the environmental regulatory process in general, we believe that it is likely that ultimate remediation liability costs for each site will be apportioned among all liable parties, including site owners and waste transporters, according to the volumes and/or toxicity of the wastes shown to have been disposed of at the sites. We believe that our financial exposure for existing disposal sites will not be materially in excess of accrued reserves.

As previously disclosed in our 2015 Annual Report, we terminated an employee of an overseas subsidiary after uncovering actions that violated our Code of Business Conduct and may have violated the Foreign Corrupt Practices Act. We completed our internal investigation into the matter, self-reported the potential violation to the United States Department of Justice (the "DOJ") and the SEC, and continue to cooperate with the DOJ and SEC. We previously received a subpoena from the SEC requesting additional information and documentation related to the matter and are in the process of responding. We currently believe that this matter will not have a material adverse financial impact on the Company, but there can be no assurance that the Company will not be subjected to monetary penalties and additional costs.

We are also a defendant in a number of other lawsuits, including product liability claims, that are insured, subject to the applicable deductibles, arising in the ordinary course of business, and we are also involved in other uninsured routine litigation incidental to our business. We currently believe none of such litigation, either individually or in the aggregate, is material to our business, operations or overall financial condition. However, litigation is inherently unpredictable, and resolutions or dispositions of claims or lawsuits by settlement or otherwise could have an adverse impact on our financial position, results of operations or cash flows for the reporting period in which any such resolution or disposition occurs.

Although none of the aforementioned potential liabilities can be quantified with absolute certainty except as otherwise indicated above, we have established reserves covering exposures relating to contingencies, to the extent believed to be reasonably estimable and probable based on past experience and available facts. While additional exposures



beyond these reserves could exist, they currently cannot be estimated. We will continue to evaluate and update the reserves as necessary and appropriate.

Table of Contents

## 10. Retirement and Postretirement Benefits

Components of the net periodic cost for retirement and postretirement benefits for the three months ended June 30, 2016 and 2015 were as follows:

|  | U.S.<br>Defined<br>Benefit<br>Plans |        | Non-U.S.<br>Defined<br>Benefit<br>Plans |        | Postretirement<br>Medical<br>Benefits |        |
|--|-------------------------------------|--------|---|--------|---------------------------------------|--------|
| (Amounts in millions)                        | 2016                                | 2015   | 2016                                    | 2015   | 2016                                  | 2015   |
| Service cost                                 | \$5.4                               | \$5.9  | \$1.7                                   | \$2.0  | \$—                                   | \$—    |
| Interest cost                                | 4.7                                 | 4.2    | 3.0                                     | 2.9    | 0.3                                   | 0.3    |
| Expected return on plan assets               | (5.9 )                              | (6.0 ) | (2.6 )                                  | (3.0 ) | —                                     | —      |
| Amortization of prior service cost           | 0.1                                 | 0.1    | —                                       | —      | 0.1                                   | 0.1    |
| Amortization of unrecognized net loss (gain) | 1.3                                 | 2.3    | 1.1                                     | 1.3    | (0.1 )                                | (0.2 ) |
| Net periodic cost recognized                 | \$5.6                               | \$6.5  | \$3.2                                   | \$3.2  | \$0.3                                 | \$0.2  |

Components of the net periodic cost for retirement and postretirement benefits for the six months months ended June 30, 2016 and 2015 were as follows:

|  | U.S.<br>Defined<br>Benefit Plans |         | Non-U.S.<br>Defined<br>Benefit<br>Plans |        | Postretirement<br>Medical<br>Benefits |        |
|--|----------------------------------|---------|---|--------|---------------------------------------|--------|
| (Amounts in millions)                        | 2016                             | 2015    | 2016                                    | 2015   | 2016                                  | 2015   |
| Service cost                                 | \$11.3                           | \$12.1  | \$3.5                                   | \$4.2  | \$—                                   | \$—    |
| Interest cost                                | 9.5                              | 8.5     | 5.9                                     | 6.2    | 0.6                                   | 0.6    |
| Expected return on plan assets               | (12.0 )                          | (12.1 ) | (5.3 )                                  | (6.0 ) | —                                     | —      |
| Amortization of prior service cost           | 0.2                              | 0.2     | —                                       | —      | 0.1                                   | 0.1    |
| Amortization of unrecognized net loss (gain) | 2.5                              | 4.6     | 2.4                                     | 2.6    | (0.2 )                                | (0.3 ) |
| Net periodic cost recognized                 | \$11.5                           | \$13.3  | \$6.5                                   | \$7.0  | \$0.5                                 | \$0.4  |

## 11. Shareholders' Equity

**Dividends** – On February 15, 2016, our Board of Directors authorized an increase in the payment of quarterly dividends on our common stock from \$0.18 per share to \$0.19 per share payable beginning on April 8, 2016. On February 16, 2015, our Board of Directors authorized an increase in the payment of quarterly dividends on our common stock from \$0.16 per share to \$0.18 per share payable beginning on April 10, 2015. Generally, our dividend date-of-record is in the last month of the quarter, and the dividend is paid the following month. Any subsequent dividends will be reviewed by our Board of Directors and declared in its discretion dependent on its assessment of our financial situation and business outlook at the applicable time.

**Share Repurchase Program** – On November 13, 2014, our Board of Directors approved a \$500.0 million share repurchase authorization. Our share repurchase program does not have an expiration date, and we reserve the right to limit or terminate the repurchase program at anytime without notice.

We had no repurchases of shares of our outstanding common stock for the three months ended June 30, 2016 compared to 1,072,421 shares repurchased for \$59.7 million, during the three months ended June 30, 2015. We had no repurchases of shares of our outstanding common stock for the six months ended June 30, 2016 compared to 2,454,446 shares repurchased for \$139.6 million, during the six months ended June 30, 2015. As of June 30, 2016 we had \$160.7 million of remaining capacity under our current share repurchase program.

## 12. Income Taxes

For the three months ended June 30, 2016, we earned \$88.1 million before taxes and provided for income taxes of \$25.1 million resulting in an effective tax rate of 28.5%. For the six months ended June 30, 2016, we earned \$144.1 million before taxes and provided for income taxes of \$42.8 million, resulting in an effective tax rate of 29.7%. The effective tax rate varied from the U.S. federal statutory rate for the three and six months ended June 30, 2016

primarily due to the net impact of foreign operations.

13

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Table of Contents

For the three months ended June 30, 2015, we earned \$107.6 million before taxes and provided for income taxes of \$30.9 million resulting in an effective tax rate of 28.7%. For the six months ended June 30, 2015, we earned \$165.7 million before taxes and provided for income taxes of \$59.4 million resulting in an effective tax rate of 35.9%. The effective tax rate varied from the U.S. federal statutory rate for the three months ended June 30, 2015 primarily due to the net impact of foreign operations. The effective tax rate varied from the U.S. federal statutory rate for the six months ended June 30, 2015 primarily due to tax impacts of the realignment programs and the Venezuelan exchange rate remeasurement loss, partially offset by the net impact of foreign operations.

It is reasonably possible that within the next 12 months the effective tax rate will be impacted by the resolution of some or all of the matters audited by various taxing authorities. It is also reasonably possible that we will have the statute of limitations close in various taxing jurisdictions within the next 12 months. As such, we estimate we could record a reduction in our tax expense of approximately \$11 million within the next 12 months.

**13. Segment Information**

The following is a summary of the financial information of the reportable segments reconciled to the amounts reported in the condensed consolidated financial statements:

**Three Months Ended June 30, 2016**

| (Amounts in thousands)      | Engineered<br>Product<br>Division | Industrial<br>Product<br>Division | Flow<br>Control<br>Division | Subtotal—Reportable<br>Segments | Eliminations<br>and All<br>Other | Consolidated<br>Total |
|-----------------------------|-----------------------------------|-----------------------------------|-----------------------------|---------------------------------|----------------------------------|-----------------------|
| Sales to external customers | \$ 502,720                        | \$ 208,132                        | \$ 315,380                  | \$ 1,026,232                    | \$ —                             | \$ 1,026,232          |
| Intersegment sales          | 9,052                             | 6,899                             | 1,805                       | 17,756                          | (17,756)                         | —                     |
| Segment operating income    | 65,257                            | 5,485                             | 48,450                      | 119,192                         | (21,188)                         | 98,004                |

**Three Months Ended June 30, 2015**

| (Amounts in thousands)      | Engineered<br>Product<br>Division | Industrial<br>Product<br>Division | Flow<br>Control<br>Division | Subtotal—Reportable<br>Segments | Eliminations<br>and All<br>Other | Consolidated<br>Total |
|-----------------------------|-----------------------------------|-----------------------------------|-----------------------------|---------------------------------|----------------------------------|-----------------------|
| Sales to external customers | \$ 558,334                        | \$ 248,659                        | \$ 355,254                  | \$ 1,162,247                    | \$ —                             | \$ 1,162,247          |
| Intersegment sales          | 12,431                            | 12,156                            | 1,111                       | 25,698                          | (25,698)                         | —                     |
| Segment operating income    | 86,227                            | 7,070                             | 54,489                      | 147,786                         | (20,209)                         | 127,577               |

**Six Months Ended June 30, 2016**

| (Amounts in thousands)      | Engineered<br>Product<br>Division | Industrial<br>Product<br>Division | Flow<br>Control<br>Division | Subtotal—Reportable<br>Segments | Eliminations<br>and All<br>Other | Consolidated<br>Total |
|-----------------------------|-----------------------------------|-----------------------------------|-----------------------------|---------------------------------|----------------------------------|-----------------------|
| Sales to external customers | \$966,946                         | \$394,836                         | \$611,698                   | \$ 1,973,480                    | \$ —                             | \$ 1,973,480          |
| Intersegment sales          | 18,665                            | 17,646                            | 4,473                       | 40,784                          | (40,784)                         | —                     |
| Segment operating income    | 123,638                           | 9,483                             | 87,300                      | 220,421                         | (48,007)                         | 172,414               |

**Six Months Ended June 30, 2015**

| (Amounts in thousands)          | Engineered<br>Product<br>Division | Industrial<br>Product<br>Division | Flow<br>Control<br>Division | Subtotal—Reportable<br>Segments | Eliminations<br>and All<br>Other | Consolidated<br>Total |
|---------------------------------|-----------------------------------|-----------------------------------|-----------------------------|---------------------------------|----------------------------------|-----------------------|
| Sales to external customers     | \$1,031,747                       | \$463,371                         | \$681,749                   | \$ 2,176,867                    | \$ —                             | \$ 2,176,867          |
| Intersegment sales              | 23,177                            | 20,812                            | 1,778                       | 45,767                          | (45,767)                         | —                     |
| Segment operating income (loss) | 155,056                           | (6,269)                           | 109,204                     | 257,991                         | (37,038)                         | 220,953               |

Table of Contents

## 14. Accumulated Other Comprehensive Loss

The following table presents the changes in accumulated other comprehensive loss ("AOCL"), net of tax for the three months ended June 30, 2016 and 2015:

|  | 2016                                  |   |                            |             | 2015                                  |   |                            |             |
|--|---------------------------------------|---|----------------------------|-------------|---------------------------------------|---|----------------------------|-------------|
| (Amounts in thousands)                                     | Foreign currency translation items(1) | Pension and other post-retirement effects | Cash flow hedging activity | Total(1)    | Foreign currency translation items(1) | Pension and other post-retirement effects | Cash flow hedging activity | Total(1)    |
| Balance - April 1  | \$(379,665)                           | \$(117,675)                               | \$(2,815)                  | \$(500,155) | \$(344,967)                           | \$(127,507)                               | \$(10,356)                 | \$(482,830) |
| Other comprehensive (loss) income before reclassifications | (28,622)                              | 1,317                                     | 65                         | (27,240)    | 13,666                                | (675)                                     | 1,648                      | 14,639      |
| Amounts reclassified from AOCL                             | —                                     | 1,833                                     | 495                        | 2,328       | —                                     | 2,455                                     | 1,779                      | 4,234       |
| Net current-period other comprehensive (loss) income       | (28,622)                              | 3,150                                     | 560                        | (24,912)    | 13,666                                | 1,780                                     | 3,427                      | 18,873      |
| Balance - June 30  | \$(408,287)                           | \$(114,525)                               | \$(2,255)                  | \$(525,067) | \$(331,301)                           | \$(125,727)                               | \$(6,929)                  | \$(463,957) |

(1) Includes foreign currency translation adjustments attributable to noncontrolling interests of \$3.5 million and \$1.3 million at April 1, 2016 and 2015 and \$3.5 million and \$2.7 million at June 30, 2016 and 2015, respectively. Includes net investment hedge gain of \$4.4 million and loss of \$6.5 million, net of deferred taxes, for the three months ended June 30, 2016 and 2015, respectively. Amounts in parentheses indicate debits.

The following table presents the reclassifications out of AOCL:

| (Amounts in thousands)                   | Affected line item in the statement of income | Three Months Ended June 30, |           |
|--|---|-----------------------------|-----------|
|  |   | 2016(1)                     | 2015(1)   |
| Cash flow hedging activity               |   |                             |           |
| Foreign exchange contracts               |   |                             |           |
|  | Sales   | \$(660)                     | \$(2,522) |
|  | Tax benefit                                   | 165                         | 743       |
|  | Net of tax                                    | \$(495)                     | \$(1,779) |
| Pension and other postretirement effects |   |                             |           |
| Amortization of actuarial losses(2)      |   | \$(2,476)                   | \$(3,507) |
| Prior service costs(2)                   |   | (154)                       | (156)     |
|  | Tax benefit                                   | 797                         | 1,208     |
|  | Net of tax                                    | \$(1,833)                   | \$(2,455) |

(1) Amounts in parentheses indicate decreases to income. None of the reclass amounts have a noncontrolling interest component.

(2) These accumulated other comprehensive loss components are included in the computation of net periodic pension cost. See Note 10 for additional details.

Table of Contents

The following table presents the changes in AOCL, net of tax for the six months ended June 30, 2016 and 2015:

| (Amounts in thousands)                                     | 2016<br>Foreign<br>currency<br>translation<br>items(1) | Pension and<br>other<br>post-retiremen<br>effects | Cash<br>flow<br>hedging<br>activity | Total(1)    | 2015<br>Foreign<br>currency<br>translation<br>items(1) | Pension and<br>other<br>post-retiremen<br>effects | Cash<br>flow<br>hedging<br>activity | Total(1)    |
|--|--|---|-------------------------------------|-------------|--|---|-------------------------------------|-------------|
| Balance - January 1  | \$(413,422)  | \$(120,461 )                                      | \$(3,458)                           | \$(537,341) | \$(238,533)  | \$(135,398 )                                      | \$(5,210)                           | \$(379,141) |
| Other comprehensive income (loss) before reclassifications | 5,135  | 2,378   | 594                                 | 8,107       | (92,768 )  | 4,785   | (6,705 )                            | (94,688 )   |
| Amounts reclassified from AOCL                             | —  | 3,558   | 609                                 | 4,167       | —  | 4,886   | 4,986                               | 9,872       |
| Net current-period other comprehensive income (loss)       | 5,135  | 5,936   | 1,203                               | 12,274      | (92,768 )  | 9,671   | (1,719 )                            | (84,816 )   |
| Balance - June 30  | \$(408,287)  | \$(114,525 )                                      | \$(2,255)                           | \$(525,067) | \$(331,301)  | \$(125,727 )                                      | \$(6,929)                           | \$(463,957) |

(1) Includes foreign currency translation adjustments attributable to noncontrolling interests of \$2.7 million and \$1.3 million at January 1, 2016 and 2015 and \$3.5 million and \$2.7 million at June 30, 2016 and 2015, respectively. Includes net investment hedge losses of \$3.9 million and \$8.6 million, net of deferred taxes, for the six months ended June 30, 2016 and 2015, respectively. Amounts in parentheses indicate debits.

The following table presents the reclassifications out of AOCL:

| (Amounts in thousands)                   | Affected line item in the statement of income | Six Months Ended<br>June 30, |           |
|--|---|------------------------------|-----------|
|  |   | 2016(1)                      | 2015(1)   |
| Foreign currency translation items       |   |                              |           |
| Cash flow hedging activity               |   |                              |           |
| Foreign exchange contracts               | Other expense, net                            | \$—                          | \$(3,327) |
|  | Sales   | (814 )                       | (3,704 )  |
|  | Tax benefit                                   | 205                          | 2,045     |
|  | Net of tax                                    | \$(609 )                     | \$(4,986) |
| Pension and other postretirement effects |   |                              |           |
| Amortization of actuarial losses(2)      |   | \$(4,789)                    | \$(6,931) |
| Prior service costs(2)                   |   | (305 )                       | (354 )    |
|  | Tax benefit                                   | 1,536                        | 2,399     |
|  | Net of tax                                    | \$(3,558)                    | \$(4,886) |

(1) Amounts in parentheses indicate decreases to income. None of the reclass amounts have a noncontrolling interest component.

(2) These accumulated other comprehensive loss components are included in the computation of net periodic pension cost. See Note 10 for additional details.

At June 30, 2016, we expect to recognize a loss of \$1.5 million, net of deferred taxes, into earnings in the next twelve months related to designated foreign exchange contracts based on their fair values at June 30, 2016.



Table of Contents

15. Realignment Programs

In the first quarter of 2015, we initiated a realignment program ("R1 Realignment Program") to reduce and optimize certain non-strategic QRCs and manufacturing facilities from the SIHI acquisition. In the second quarter of 2015, we initiated a second realignment program ("R2 Realignment Program") to better align costs and improve long-term efficiency, including further manufacturing optimization through the consolidation of facilities, a reduction in our workforce, the transfer of activities from high-cost regions to lower-cost facilities and the divestiture of certain non-strategic assets.

The R1 Realignment Program and the R2 Realignment Program (collectively the "Realignment Programs") consist of both restructuring and non-restructuring charges. Restructuring charges represent costs associated with the relocation or reorganization of certain business activities and facility closures and include related severance costs.

Non-restructuring charges are primarily employee severance associated with workforce reductions to reduce redundancies. Expenses are primarily reported in cost of sales ("COS") or selling, general and administrative expense ("SG&A"), as applicable, in our condensed consolidated statements of income. We anticipate a total investment in these programs of approximately \$400 million, including projects still under final evaluation. We anticipate that the majority of any remaining charges will be incurred throughout 2016 and 2017.

Table of Contents

Generally, the aforementioned charges will be paid in cash, except for asset write-downs, which are non-cash charges. The following is a summary of total charges, net of adjustments, related to the Realignment Programs:

| Three Months Ended June 30, 2016 |                                   |                                   |                             |                                 |                                  |                       |
|----------------------------------|-----------------------------------|-----------------------------------|-----------------------------|---------------------------------|----------------------------------|-----------------------|
| (Amounts in thousands)           | Engineered<br>Product<br>Division | Industrial<br>Product<br>Division | Flow<br>Control<br>Division | Subtotal—Reportable<br>Segments | Eliminations<br>and All<br>Other | Consolidated<br>Total |
| Restructuring Charges            |                                   |                                   |                             |                                 |                                  |                       |
| COS                              | \$3,335                           | \$2,294                           | \$2,180                     | \$ 7,809                        | \$ —                             | \$ 7,809              |
| SG&A                             | 6,411                             | 77                                | 177                         | 6,665                           | 32                               | 6,697                 |
|                                  | \$9,746                           | \$2,371                           | \$2,357                     | \$ 14,474                       | \$ 32                            | \$ 14,506             |
| Non-Restructuring Charges        |                                   |                                   |                             |                                 |                                  |                       |
| COS                              | \$1,038                           | \$2,489                           | \$(141 )                    | \$ 3,386                        | \$ —                             | \$ 3,386              |
| SG&A                             | 1,199                             | (208 )                            | 126                         | 1,117                           | 1,129                            | 2,246                 |
|                                  | \$2,237                           | \$2,281                           | \$(15 )                     | \$ 4,503                        | \$ 1,129                         | \$ 5,632              |
| Total Realignment Charges        |                                   |                                   |                             |                                 |                                  |                       |
| COS                              | \$4,373                           | \$4,783                           | \$2,039                     | \$ 11,195                       | \$ —                             | \$ 11,195             |
| SG&A                             | 7,610                             | (131 )                            | 303                         | 7,782                           | 1,161                            | \$ 8,943              |
|                                  | \$11,983                          | \$4,652                           | \$2,342                     | \$ 18,977                       | \$ 1,161                         | \$ 20,138             |
| Three Months Ended June 30, 2015 |                                   |                                   |                             |                                 |                                  |                       |
| (Amounts in thousands)           | Engineered<br>Product<br>Division | Industrial<br>Product<br>Division | Flow<br>Control<br>Division | Subtotal—Reportable<br>Segments | Eliminations<br>and All<br>Other | Consolidated<br>Total |
| Restructuring Charges            |                                   |                                   |                             |                                 |                                  |                       |
| COS                              | \$110                             | \$5,311                           | \$1,019                     | \$ 6,440                        | \$ —                             | —\$ 6,440             |
| SG&A                             | 122                               | 2,690                             | 2,342                       | 5,154                           | —                                | 5,154                 |
| Income tax expense               | —                                 | 500                               | —                           | 500                             | —                                | 500                   |
|                                  | \$232                             | \$8,501                           | \$3,361                     | \$ 12,094                       | \$ —                             | —\$ 12,094            |
| Non-Restructuring Charges        |                                   |                                   |                             |                                 |                                  |                       |
| COS                              | \$7,069                           | \$927                             | \$5,091                     | \$ 13,087                       | \$ —                             | —\$ 13,087            |
| SG&A                             | 2,160                             | 1,262                             | 3,924                       | 7,346                           | —                                | 7,346                 |
|                                  | \$9,229                           | \$2,189                           | \$9,015                     | \$ 20,433                       | \$ —                             | —\$ 20,433            |
| Total Realignment Charges        |                                   |                                   |                             |                                 |                                  |                       |
| COS                              | \$7,179                           | \$6,238                           | \$6,110                     | \$ 19,527                       | \$ —                             | —\$ 19,527            |
| SG&A                             | 2,282                             | 3,952                             | 6,266                       | 12,500                          | —                                | \$ 12,500             |
| Income tax expense               | —                                 | 500                               | —                           | 500                             | —                                | \$ 500                |
|                                  | \$9,461                           | \$10,690                          | \$12,376                    | \$ 32,527                       | \$ —                             | —\$ 32,527            |

Table of Contents

| Six Months Ended June 30, 2016 |                                 |                                   |                             |                                 |                                  |                       |
|--------------------------------|---------------------------------|-----------------------------------|-----------------------------|---------------------------------|----------------------------------|-----------------------|
| (Amounts in thousands)         | Engineer<br>Product<br>Division | Industrial<br>Product<br>Division | Flow<br>Control<br>Division | Subtotal—Reportable<br>Segments | Eliminations<br>and All<br>Other | Consolidated<br>Total |
| Restructuring Charges          |                                 |                                   |                             |                                 |                                  |                       |
| COS                            | \$4,855                         | \$ 2,110                          | \$ 2,287                    | \$ 9,252                        | \$ —                             | \$ 9,252              |
| SG&A                           | 8,818                           | 1,789                             | 336                         | 10,943                          | 32                               | 10,975                |
|                                | \$13,673                        | \$ 3,899                          | \$ 2,623                    | \$ 20,195                       | \$ 32                            | \$ 20,227             |
| Non-Restructuring Charges      |                                 |                                   |                             |                                 |                                  |                       |
| COS                            | \$1,137                         | \$ 4,283                          | \$ 3,719                    | \$ 9,139                        | \$ 15                            | \$ 9,154              |
| SG&A                           | 978                             | 400                               | 1,590                       | 2,968                           | 1,259                            | 4,227                 |
|                                | \$2,115                         | \$ 4,683                          | \$ 5,309                    | \$ 12,107                       | \$ 1,274                         | \$ 13,381             |
| Total Realignment Charges      |                                 |                                   |                             |                                 |                                  |                       |
| COS                            | \$5,992                         | \$ 6,393                          | \$ 6,006                    | \$ 18,391                       | \$ 15                            | \$ 18,406             |
| SG&A                           | 9,796                           | 2,189                             | 1,926                       | 13,911                          | 1,291                            | 15,202                |
|                                | \$15,788                        | \$ 8,582                          | \$ 7,932                    | \$ 32,302                       | \$ 1,306                         | \$ 33,608             |
| Six Months Ended June 30, 2015 |                                 |                                   |                             |                                 |                                  |                       |
| (Amounts in thousands)         | Engineer<br>Product<br>Division | Industrial<br>Product<br>Division | Flow<br>Control<br>Division | Subtotal—Reportable<br>Segments | Eliminations<br>and All<br>Other | Consolidated<br>Total |
| Restructuring Charges          |                                 |                                   |                             |                                 |                                  |                       |
| COS                            | \$110                           | \$ 18,639                         | \$ 1,019                    | \$ 19,768                       | \$                               | —\$ 19,768            |
| SG&A                           | 122                             | 10,245                            | 2,342                       | 12,709                          | —                                | 12,709                |
| Income tax expense             | —                               | 5,500                             | —                           | 5,500                           | —                                | 5,500                 |
|                                | \$232                           | \$ 34,384                         | \$ 3,361                    | \$ 37,977                       | \$                               | —\$ 37,977            |
| Non-Restructuring Charges      |                                 |                                   |                             |                                 |                                  |                       |
| COS                            | \$7,069                         | \$ 927                            | \$ 5,091                    | \$ 13,087                       | \$                               | —\$ 13,087            |
| SG&A                           | 2,160                           | 1,894                             | 3,924                       | 7,978                           | —                                | 7,978                 |
|                                | \$9,229                         | \$ 2,821                          | \$ 9,015                    | \$ 21,065                       | \$                               | —\$ 21,065            |
| Total Realignment Charges      |                                 |                                   |                             |                                 |                                  |                       |
| COS                            | \$7,179                         | \$ 19,566                         | \$ 6,110                    | \$ 32,855                       | \$                               | —\$ 32,855            |
| SG&A                           | 2,282                           | 12,139                            | 6,266                       | 20,687                          | —                                | 20,687                |
| Income tax expense             | —                               | 5,500                             | —                           | 5,500                           | —                                | 5,500                 |
|                                | \$9,461                         | \$ 37,205                         | \$ 12,376                   | \$ 59,042                       | \$                               | —\$ 59,042            |

Table of Contents

The following is a summary of total inception to date charges, net of adjustments, related to the Realignment Programs:

| (Amounts in thousands)           | Inception to Date           |                                 |                       | Subtotal-Reportable Segments | Eliminations and All Other | Consolidated Total |
|----------------------------------|-----------------------------|---------------------------------|-----------------------|------------------------------|----------------------------|--------------------|
|                                  | Engineered Product Division | Industrial Product Division (1) | Flow Control Division |                              |                            |                    |
| <b>Restructuring Charges</b>     |                             |                                 |                       |                              |                            |                    |
| COS                              | \$ 14,818                   | \$ 22,556                       | \$ 11,588             | \$ 48,962                    | \$ —                       | \$ 48,962          |
| SG&A                             | 16,293                      | 11,048                          | 7,947                 | 35,288                       | 32                         | 35,320             |
| Income tax expense               | —                           | 8,900                           | —                     | 8,900                        | —                          | 8,900              |
|                                  | \$ 31,111                   | \$ 42,504                       | \$ 19,535             | \$ 93,150                    | \$ 32                      | \$ 93,182          |
| <b>Non-Restructuring Charges</b> |                             |                                 |                       |                              |                            |                    |
| COS                              | \$ 11,403                   | \$ 12,444                       | \$ 12,302             | \$ 36,149                    | \$ 15                      | \$ 36,164          |
| SG&A                             | 7,509                       | 6,548                           | 5,003                 | 19,060                       | 1,259                      | 20,319             |
|                                  | \$ 18,912                   | \$ 18,992                       | \$ 17,305             | \$ 55,209                    | \$ 1,274                   | \$ 56,483          |
| <b>Total Realignment Charges</b> |                             |                                 |                       |                              |                            |                    |
| COS                              | \$ 26,221                   | \$ 35,000                       | \$ 23,890             | \$ 85,111                    | \$ 15                      | \$ 85,126          |
| SG&A                             | 23,802                      | 17,596                          | 12,950                | 54,348                       | 1,291                      | 55,639             |
| Income tax expense               | —                           | 8,900                           | —                     | 8,900                        | —                          | 8,900              |
|                                  | \$ 50,023                   | \$ 61,496                       | \$ 36,840             | \$ 148,359                   | \$ 1,306                   | \$ 149,665         |

(1) Includes \$39.1 million of restructuring charges, primarily COS, related to the R1 Realignment Program.

Restructuring charges represent costs associated with the relocation or reorganization of certain business activities and facility closures and include costs related to employee severance at closed facilities, contract termination costs, asset write-downs and other costs. Severance costs primarily include costs associated with involuntary termination benefits. Contract termination costs include costs related to termination of operating leases or other contract termination costs. Asset write-downs include accelerated depreciation of fixed assets, accelerated amortization of intangible assets, divestiture of certain non-strategic assets and inventory write-downs. Other costs generally include costs related to employee relocation, asset relocation, vacant facility costs (i.e., taxes and insurance) and other charges.

The following is a summary of restructuring charges, net of adjustments, for the Realignment Programs:

| Three Months Ended June 30, 2016 |                  |                      |                   |                 |                  |
|----------------------------------|------------------|----------------------|-------------------|-----------------|------------------|
| (Amounts in thousands)           | Severance        | Contract Termination | Asset Write-Downs | Other           | Total            |
| COS                              | \$ 3,311         | \$ —                 | \$ 1,615          | \$ 2,883        | \$ 7,809         |
| SG&A                             | (1,897 )         | —                    | 2,608             | 5,986           | 6,697            |
| <b>Total</b>                     | <b>\$ 1,414</b>  | <b>\$ —</b>          | <b>\$ 4,223</b>   | <b>\$ 8,869</b> | <b>\$ 14,506</b> |
| Three Months Ended June 30, 2015 |                  |                      |                   |                 |                  |
| (Amounts in thousands)           | Severance        | Contract Termination | Asset Write-Downs | Other           | Total            |
| COS                              | \$ 6,284         | \$ —                 | \$ 107            | \$ 49           | \$ 6,440         |
| SG&A                             | 4,444            | —                    | 634               | 76              | 5,154            |
| Income tax expense               | —                | —                    | —                 | 500             | 500              |
| <b>Total</b>                     | <b>\$ 10,728</b> | <b>\$ —</b>          | <b>\$ 741</b>     | <b>\$ 625</b>   | <b>\$ 12,094</b> |

Table of Contents

## Six Months Ended June 30, 2016

| (Amounts in thousands) | Severance | Contract Termination | Asset Write-Downs | Other   | Total    |
|------------------------|-----------|----------------------|-------------------|---------|----------|
| COS                    | \$3,372   | \$ —                 | \$ 2,533          | \$3,347 | \$9,252  |
| SG&A                   | 1,856     | —                    | 2,644             | 6,475   | 10,975   |
| Total                  | \$5,228   | \$ —                 | \$ 5,177          | \$9,822 | \$20,227 |

## Six Months Ended June 30, 2015

| (Amounts in thousands) | Severance | Contract Termination | Asset Write-Downs | Other   | Total    |
|------------------------|-----------|----------------------|-------------------|---------|----------|
| COS                    | \$19,612  | \$ —                 | \$ 107            | \$49    | \$19,768 |
| SG&A                   | 11,999    | —                    | 634               | 76      | 12,709   |
| Income tax expense     | —         | —                    | —                 | 5,500   | 5,500    |
| Total                  | \$31,611  | \$ —                 | \$ 741            | \$5,625 | \$37,977 |

The following is a summary of total inception to date restructuring charges, net of adjustments, related to the Realignment Programs:

## Inception to Date

| (Amounts in thousands) | Severance | Contract Termination | Asset Write-Downs | Other    | Total (1) |
|------------------------|-----------|----------------------|-------------------|----------|-----------|
| COS(1)                 | \$37,344  | \$ 609               | \$ 6,021          | \$4,988  | \$48,962  |
| SG&A                   | 25,376    | 43                   | 2,688             | 7,213    | 35,320    |
| Income tax expense     | —         | —                    | —                 | 8,900    | 8,900     |
| Total                  | \$62,720  | \$ 652               | \$ 8,709          | \$21,101 | \$93,182  |

(1) Includes \$39.1 million of restructuring charges, primarily COS, related to the R1 Realignment Program.

The following represents the activity, primarily severance, related to the restructuring reserve for the Realignment Programs:

| (Amounts in thousands)                         | R1<br>Realignment<br>Program | R2<br>Realignment<br>Program | Total    |
|--|------------------------------|------------------------------|----------|
| Balance at December 31, 2015                   | \$ 25,156                    | \$ 33,147                    | \$58,303 |
| Charges  | 976                          | 3,792                        | 4,768    |
| Cash expenditures                              | (1,294)                      | (3,999)                      | (5,293)  |
| Other non-cash adjustments, including currency | (877)                        | (1,162)                      | (2,039)  |
| Balance at March 31, 2016                      | \$ 23,961                    | \$ 31,778                    | \$55,739 |
| Charges  | 2,371                        | 2,681                        | 5,052    |
| Cash expenditures                              | (3,305)                      | (1,348)                      | (4,653)  |
| Other non-cash adjustments, including currency | (5,370)                      | (4,424)                      | (9,794)  |
| Balance at June 30, 2016                       | \$ 17,657                    | \$ 28,687                    | \$46,344 |

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements, and notes thereto, and the other financial data included elsewhere in this Quarterly Report. The following discussion should also be read in conjunction with our audited consolidated financial statements, and notes



## Table of Contents

thereto, and "Management's Discussion and Analysis of Financial Condition and Results of Operations" ("MD&A") included in our 2015 Annual Report.

### EXECUTIVE OVERVIEW

#### Our Company

We believe that we are a world-leading manufacturer and aftermarket service provider of comprehensive flow control systems. We develop and manufacture precision-engineered flow control equipment integral to the movement, control and protection of the flow of materials in our customers' critical processes. Our product portfolio of pumps, valves, seals, automation and aftermarket services supports global infrastructure industries, including oil and gas, chemical, power generation and water management, as well as general industrial markets where our products and services add value. Through our manufacturing platform and global network of Quick Response Centers ("QRCs"), we offer a broad array of aftermarket equipment services, such as installation, advanced diagnostics, repair and retrofitting. We currently employ approximately 18,000 employees in more than 50 countries.

Our business model is significantly influenced by the capital spending of global infrastructure industries for the placement of new products into service and aftermarket services for existing operations. The worldwide installed base of our products is an important source of aftermarket revenue, where products are expected to ensure the maximum operating time of many key industrial processes. Over the past several years, we have significantly invested in our aftermarket strategy to provide local support to drive customer investments in our offerings and use of our services to replace or repair installed products. The aftermarket portion of our business also helps provide business stability during various economic periods. The aftermarket business, which is served by our network of 188 QRCs located around the globe, provides a variety of service offerings for our customers including spare parts, service solutions, product life cycle solutions and other value-added services. It is generally a higher margin business compared to our original equipment business and a key component of our profitable growth strategy.

Our operations are conducted through three business segments that are referenced throughout this MD&A:

• **EPD** for long lead-time, custom and other highly-engineered pumps and pump systems, mechanical seals, auxiliary systems and replacement parts and related services;

• **IDP** for engineered and pre-configured industrial pumps and pump systems and related products and services; and

• **FCD** for engineered and industrial valves, control valves, actuators and controls and related services.

Our business segments share a focus on industrial flow control technology and have a high number of common customers. These segments also have complementary product offerings and technologies that are often combined in applications that provide us a net competitive advantage. Our segments also benefit from our global footprint and our economies of scale in reducing administrative and overhead costs to serve customers more cost effectively. For example, our segment leadership reports to our Chief Operating Officer ("COO") and the segments share leadership for operational support functions, such as research and development, marketing and supply chain.

The reputation of our product portfolio is built on more than 50 well-respected brand names such as Worthington, IDP, Valtek, Limitorque, Durco, Edward, Anchor/Darling, SIHI, Halberg and Durametallc, which we believe to be one of the most comprehensive in the industry. Our products and services are sold either directly or through designated channels to more than 10,000 companies, including some of the world's leading engineering, procurement and construction ("EPC") firms, original equipment manufacturers, distributors and end users.

We continue to leverage our QRC network to be positioned as near to customers as possible for service and support in order to capture valuable aftermarket business. Along with ensuring that we have the local capability to sell, install and service our equipment in remote regions, it is equally imperative to continuously improve our global operations.

We continue to expand our global supply chain capability to meet global customer demands and ensure the quality and timely delivery of our products. Additionally, we continue to devote resources to improving the supply chain processes across our business segments to find areas of synergy and cost reduction and to improve our supply chain management capability to ensure it can meet global customer demands. We also remain focused on improving on-time delivery and quality, while managing warranty costs as a percentage of sales across our global operations, through the assistance of a focused Continuous Improvement Process ("CIP") initiative. The goal of the CIP initiative, which include lean manufacturing, six sigma business management strategy and value engineering, is to maximize service fulfillment to customers through on-time delivery, reduced cycle time and quality at the highest internal productivity.

During 2015 and thus far in 2016, we have been challenged by broad-based capital spending declines, originating in the oil and gas industry, heightened pricing pressures and negative currency impacts caused by a stronger U.S. dollar. This was further compounded by economic and geo-political conditions in Latin America, the Middle East and China. In addition, we experienced



Table of Contents

lower than expected activity levels in our aftermarket business due to deferred spending of our customers' repair and maintenance budgets. We expect that the current environment will persist throughout 2016.

To better align costs and improve long-term efficiency, we initiated Realignment Programs to accelerate both short- and long-term strategic plans, including targeted manufacturing optimization through the consolidation of facilities, SG&A efficiency initiatives, transfer of activities from high-cost regions to lower-cost facilities and the divestiture of certain non-strategic assets. At the completion of the programs, we expect a 15% to 20% reduction in our global workforce, relative to early 2015 workforce levels. With an expected near-term investment of approximately \$400 million, including projects still under final evaluation, we expect the results of our realignment programs will deliver annualized run-rate savings of approximately \$230 million. In addition, we are focusing on our ongoing low-cost sourcing, including greater use of third-party suppliers and increasing our lower-cost, emerging market capabilities.

**RESULTS OF OPERATIONS — Three months ended June 30, 2016 and 2015**

Throughout this discussion of our results of operations, we discuss the impact of fluctuations in foreign currency exchange rates. We have calculated currency effects on operations by translating current year results on a monthly basis at prior year exchange rates for the same periods.

In the first quarter of 2015, we initiated a realignment program to reduce and optimize certain non-strategic QRCs and manufacturing facilities from the SIHI acquisition. In the second quarter of 2015, we initiated a realignment program to better align costs and improve long-term efficiency, including further manufacturing optimization through the consolidation of facilities, a reduction in our workforce, the transfer of activities from high-cost regions to lower-cost facilities and the divestiture of certain non-strategic assets.

The total charges for Realignment Programs by segment are detailed below for the three months ended June 30, 2016 and 2015:

| (Amounts in thousands)            | Three Months Ended June 30, 2016  |                                   |                             |                                 | Eliminations<br>and All<br>Other | Consolidated<br>Total |
|-----------------------------------|-----------------------------------|-----------------------------------|-----------------------------|---------------------------------|----------------------------------|-----------------------|
|                                   | Engineered<br>Product<br>Division | Industrial<br>Product<br>Division | Flow<br>Control<br>Division | Subtotal—Reportable<br>Segments |                                  |                       |
| Total Realignment Program Charges |                                   |                                   |                             |                                 |                                  |                       |
| COS                               | \$4,373                           | \$4,783                           | \$ 2,039                    | \$ 11,195                       | \$ —                             | \$ 11,195             |
| SG&A                              | 7,610                             | (131 )                            | 303                         | 7,782                           | 1,161                            | 8,943                 |
|                                   | \$11,983                          | \$4,652                           | \$ 2,342                    | \$ 18,977                       | \$ 1,161                         | \$ 20,138             |
| Three Months Ended June 30, 2015  |                                   |                                   |                             |                                 |                                  |                       |
| (Amounts in thousands)            | Engineered<br>Product<br>Division | Industrial<br>Product<br>Division | Flow<br>Control<br>Division | Subtotal—Reportable<br>Segments | Eliminations<br>and All<br>Other | Consolidated<br>Total |
| Total Realignment Program Charges |                                   |                                   |                             |                                 |                                  |                       |
| COS                               | \$7,179                           | \$6,238                           | \$ 6,110                    | \$ 19,527                       | \$ —                             | \$ 19,527             |
| SG&A                              | 2,282                             | 3,952                             | 6,266                       | 12,500                          | —                                | 12,500                |
| Income tax expense                | —                                 | 500                               | —                           | 500                             | —                                | 500                   |
|                                   | \$9,461                           | \$10,690                          | \$12,376                    | \$ 32,527                       | \$ —                             | \$ 32,527             |

Table of Contents

The total charges for Realignment Programs by segment are detailed below for the six months ended June 30, 2016 and 2015:

| (Amounts in thousands)            | Six Months Ended June 30, 2016 |                             |                       |                              | Eliminations and All Other | Consolidated Total |
|-----------------------------------|--------------------------------|-----------------------------|-----------------------|------------------------------|----------------------------|--------------------|
|                                   | Engineered Product Division    | Industrial Product Division | Flow Control Division | Subtotal—Reportable Segments |                            |                    |
| Total Realignment Program Charges |                                |                             |                       |                              |                            |                    |
| COS                               | \$5,992                        | \$ 6,393                    | \$ 6,006              | \$ 18,391                    | \$ 15                      | \$ 18,406          |
| SG&A                              | 9,796                          | 2,189                       | 1,926                 | 13,911                       | 1,291                      | 15,202             |
|                                   | \$15,788                       | \$ 8,582                    | \$ 7,932              | \$ 32,302                    | \$ 1,306                   | \$ 33,608          |
| Six Months Ended June 30, 2015    |                                |                             |                       |                              |                            |                    |
| (Amounts in thousands)            | Engineered Product Division    | Industrial Product Division | Flow Control Division | Subtotal—Reportable Segments | Eliminations and All Other | Consolidated Total |
| Total Realignment Program Charges |                                |                             |                       |                              |                            |                    |
| COS                               | \$7,179                        | \$19,566                    | \$ 6,110              | \$ 32,855                    | \$ —                       | \$ 32,855          |
| SG&A                              | 2,282                          | 12,139                      | 6,266                 | 20,687                       | —                          | 20,687             |
| Income tax expense                | —                              | 5,500                       | —                     | 5,500                        | —                          | 5,500              |
|                                   | \$9,461                        | \$37,205                    | \$ 12,376             | \$ 59,042                    | \$ —                       | \$ 59,042          |

We anticipate a total investment in these Realignment Programs of approximately \$400 million, including projects still under final evaluation. Since inception of the Realignment Programs in 2015, we have incurred charges of \$149.7 million and we expect to incur the majority of the remaining charges throughout 2016 and 2017.

Based on actions under our Realignment Programs, we estimate that we have achieved cost savings of approximately \$43 million for the six months ended June 30, 2016, of which approximately half was in COS with the remainder in SG&A. Upon completion of the Realignment Programs, we expect annual run-rate cost savings of approximately \$230 million, with a portion achieved in 2016 and a larger portion achieved in 2017. Actual savings could vary from expected savings, which represent management's best estimate to date.

## Consolidated Results

## Bookings, Sales and Backlog

| (Amounts in millions) | Three Months Ended June 30, |           |
|-----------------------|-----------------------------|-----------|
|                       | 2016                        | 2015      |
| Bookings              | \$975.4                     | \$1,115.4 |
| Sales                 | 1,026.2                     | 1,162.2   |
| (Amounts in millions) | Six Months Ended June 30,   |           |
|                       | 2016                        | 2015      |
| Bookings              | \$1,896.7                   | \$2,157.1 |
| Sales                 | 1,973.5                     | 2,176.9   |

We define a booking as the receipt of a customer order that contractually engages us to perform activities on behalf of our customer with regard to manufacturing, service or support. Bookings recorded and subsequently canceled within the year-to-date period are excluded from year-to-date bookings. Bookings for the three months ended June 30, 2016 decreased by \$140.0 million, or 12.6%, as compared with the same period in 2015. The decrease included negative currency effects of approximately \$28



Table of Contents

million. The decrease was primarily driven by the oil and gas industry, and to a lesser extent, the general and power generation industries. The decrease was due to customer original equipment bookings.

Bookings for the six months ended June 30, 2016 decreased by \$260.4 million, or 12.1%, as compared with the same period in 2015. The decrease included negative currency effects of approximately \$67 million. The decrease was primarily driven by the oil and gas industry, and to a lesser extent, the chemical and general industries. The decrease was primarily due to customer original equipment bookings.

Sales for the three months ended June 30, 2016 decreased by \$136.0 million, or 11.7%, as compared with the same period in 2015. The decrease included negative currency effects of approximately \$23 million. The decrease was more heavily weighted toward original equipment sales with decreased sales into every region except the Middle East. Net sales to international customers, including export sales from the U.S., were approximately 64% and 65% of total sales for the three months ended June 30, 2016 and 2015, respectively.

Sales for the six months ended June 30, 2016 decreased by \$203.4 million, or 9.3%, as compared with the same period in 2015. The decrease included negative currency effects of approximately \$70 million. The decrease was more heavily weighted toward original equipment sales with decreased sales into every region except the Middle East. Net sales to international customers, including export sales from the U.S., were approximately 63% and 65% of total sales for the six months ended June 30, 2016 and 2015, respectively.

Backlog represents the aggregate value of booked but uncompleted customer orders and is influenced primarily by bookings, sales, cancellations and currency effects. Backlog of \$2,102.8 million at June 30, 2016 decreased by \$70 million, or 3.2%, as compared with December 31, 2015. Currency effects provided an increase of approximately \$27 million. Approximately 29% of the backlog at June 30, 2016 was related to aftermarket orders.

## Gross Profit and Gross Profit Margin

|   |  | Three Months     |         |
|---|--|------------------|---------|
|   |  | Ended June 30,   |         |
| (Amounts in millions, except percentages) |  | 2016             | 2015    |
| Gross profit                              |  | \$324.7          | \$369.1 |
| Gross profit margin                       |  | 31.6 %           | 31.8 %  |
|   |  | Six Months Ended |         |
|   |  | June 30,         |         |
| (Amounts in millions, except percentages) |  | 2016             | 2015    |
| Gross profit                              |  | \$632.7          | \$700.8 |
| Gross profit margin                       |  | 32.1 %           | 32.2 %  |

Gross profit for the three months ended June 30, 2016 decreased by \$44.4 million, or 12.0%, as compared with the same period in 2015. Gross profit margin for the three months ended June 30, 2016 of 31.6% decreased from 31.8% for the same period in 2015. The decrease in gross profit margin was primarily attributed to the negative impact of decreased sales on our absorption of fixed manufacturing costs, unfavorable impacts of short-term operational inefficiencies related to the initial execution of certain realignment programs, lower margin projects that shipped from backlog and increased accrued broad-based annual incentive compensation, partially offset by savings achieved and decreased charges related to our Realignment Programs, the negative impact of margins on acquired SIHI backlog and inventory ("Purchase Price Adjustments") in 2015 that did not recur and a mix shift to higher margin aftermarket sales. Aftermarket sales increased to approximately 44% of total sales, as compared with approximately 42% of total sales for the same period in 2015.

Gross profit for the six months ended June 30, 2016 decreased by \$68.1 million, or 9.7%, as compared with the same period in 2015. Gross profit margin for the six months ended June 30, 2016 of 32.1% decreased from 32.2% for the

same period in 2015. The decrease in gross profit margin was primarily attributed to the negative impact of decreased sales on our absorption of fixed manufacturing costs, unfavorable impacts of short-term operational inefficiencies related to the initial execution of certain realignment programs, lower margin projects that shipped from backlog and increased accrued broad-based annual incentive compensation, partially offset by savings achieved and decreased charges related to our Realignment Programs and the negative impact of SIHI Purchase Price Adjustments in 2015 that did not recur. Aftermarket sales increased to approximately 44% of total sales, as compared with approximately 43% of total sales for the same period in 2015.

Table of Contents

## Selling, General and Administrative Expense

|   | Three Months<br>Ended June 30, |         |   |  |
|---|--------------------------------|---------|---|--|
| (Amounts in millions, except percentages) | 2016                           | 2015    |   |  |
| SG&A                                      | \$228.5                        | \$243.6 |   |  |
| SG&A as a percentage of sales             | 22.3                           | % 21.0  | % |  |
|   | Six Months Ended<br>June 30,   |         |   |  |
| (Amounts in millions, except percentages) | 2016                           | 2015    |   |  |
| SG&A                                      | \$465.4                        | \$483.5 |   |  |
| SG&A as a percentage of sales             | 23.6                           | % 22.2  | % |  |

SG&A for the three months ended June 30, 2016 decreased by \$15.1 million, or 6.2%, as compared with the same period in 2015. Currency effects yielded a decrease of approximately \$3 million. SG&A as a percentage of sales for the three months ended June 30, 2016 increased 130 basis points as compared with the same period in 2015 due primarily to lower sales leverage and increased accrued broad-based annual incentive program compensation, partially offset by savings achieved and decreased charges related to our Realignment Programs and lower SIHI integration costs.

SG&A for the six months ended June 30, 2016 decreased by \$18.1 million, or 3.7%, as compared with the same period in 2015. Currency effects yielded a decrease of approximately \$11 million. SG&A as a percentage of sales for the six months ended June 30, 2016 increased 140 basis points as compared with the same period in 2015 due primarily to lower sales leverage and increased accrued broad-based annual and long-term incentive program compensation, partially offset by savings achieved and decreased charges related to our Realignment Programs and lower SIHI integration costs.

## Net Earnings from Affiliates

|                              | Three<br>Months<br>Ended<br>June 30, |       |
|------------------------------|--------------------------------------|-------|
| (Amounts in millions)        | 2016                                 | 2015  |
| Net earnings from affiliates | \$1.8                                | \$2.1 |
|                              | Six<br>Months<br>Ended<br>June 30,   |       |
| (Amounts in millions)        | 2016                                 | 2015  |
| Net earnings from affiliates | \$5.1                                | \$3.7 |

Net earnings from affiliates for the three months ended June 30, 2016 decreased \$0.3 million, or 14.3%, as compared with the same period in 2015. The decrease was primarily a result of decreased earnings of our EPD joint venture in Japan.

Net earnings from affiliates for the six months ended June 30, 2016 increased \$1.4 million, or 37.8%, as compared with the same period in 2015. The increase was primarily a result of increased earnings of our EPD joint venture in South Korea.

Operating Income and Operating Margin

|   | Three Months<br>Ended June 30, |   |         |   |
|---|--------------------------------|---|---------|---|
| (Amounts in millions, except percentages) | 2016                           |   | 2015    |   |
| Operating income                          | \$98.0                         |   | \$127.6 |   |
| Operating income as a percentage of sales | 9.5                            | % | 11.0    | % |
|   | Six Months Ended<br>June 30,   |   |         |   |
| (Amounts in millions, except percentages) | 2016                           |   | 2015    |   |
| Operating income                          | \$172.4                        |   | \$221.0 |   |
| Operating income as a percentage of sales | 8.7                            | % | 10.2    | % |

Table of Contents

Operating income for the three months ended June 30, 2016 decreased by \$29.6 million, or 23.2%, as compared with the same period in 2015. The decrease included negative currency effects of approximately \$2 million. The decrease was primarily a result of the \$44.4 million decrease in gross profit, partially offset by a \$15.1 million decrease in SG&A.

Operating income for the six months ended June 30, 2016 decreased by \$48.6 million, or 22.0%, as compared with the same period in 2015. The decrease included negative currency effects of approximately \$8 million. The decrease was primarily a result of the \$68.1 million decrease in gross profit, partially offset by a \$18.1 million decrease in SG&A.

## Interest Expense and Interest Income

|                       | Three Months<br>Ended June 30, |          |
|-----------------------|--------------------------------|----------|
| (Amounts in millions) | 2016                           | 2015     |
| Interest expense      | \$(15.3)                       | \$(15.4) |
| Interest income       | 0.6                            | 0.2      |
|                       | Six Months<br>Ended June 30,   |          |
| (Amounts in millions) | 2016                           | 2015     |
| Interest expense      | \$(29.8)                       | \$(31.4) |
| Interest income       | 1.3                            | 1.0      |

Interest expense for the three and six months ended June 30, 2016 decreased \$0.1 million and \$1.6 million, respectively as compared with the same periods in 2015. The \$1.6 million decrease for the six months was primarily attributable to decreased commitments and borrowings under our Revolving Credit Facility in the first half of 2016, as compared to the same period in 2015.

## Other Income (Expense), Net

|                             | Three<br>Months<br>Ended June<br>30, |          |
|-----------------------------|--------------------------------------|----------|
| (Amounts in millions)       | 2016                                 | 2015     |
| Other income (expense), net | \$4.7                                | \$(4.9)  |
|                             | Six Months<br>Ended June<br>30,      |          |
| (Amounts in millions)       | 2016                                 | 2015     |
| Other income (expense), net | \$0.2                                | \$(24.8) |

Other income, net for the three months ended June 30, 2016 increased \$9.6 million from a loss of \$4.9 million in 2015, due primarily to a \$8.4 million increase in gains from transactions in currencies other than our sites' functional currencies and a \$2.5 million increase in gains arising from transactions on foreign exchange contracts. The net change was primarily due to the foreign currency exchange rate movements in the Brazilian real, Mexican peso and Euro in relation to the U.S. dollar during the three months ended June 30, 2016, as compared with the same period in 2015.

Other income, net for the six months ended June 30, 2016 increased \$25.0 million from a loss of \$24.8 million in 2015, due primarily to a \$47.0 million decrease in losses from transactions in currencies other than our sites'



functional currencies, partially offset by a \$20.6 million decrease in gains arising from transactions on foreign exchange contracts. The net change was primarily due to the foreign currency exchange rate movements in the Brazilian real and Euro in relation to the U.S. dollar during the six months ended June 30, 2016, as compared with the same period in 2015, and the \$18.5 million loss as a result of the remeasurement of our Venezuelan bolivar-denominated net monetary assets in the first quarter of 2015 that did not recur.

Table of Contents

## Tax Expense and Tax Rate

|   | Three Months   |        |
|---|----------------|--------|
|   | Ended June 30, |        |
| (Amounts in millions, except percentages) | 2016           | 2015   |
| Provision for income taxes                | \$25.1         | \$30.9 |
| Effective tax rate                        | 28.5 %         | 28.7 % |
|   | Six Months     |        |
|   | Ended June 30, |        |
| (Amounts in millions, except percentages) | 2016           | 2015   |
| Provision for income taxes                | \$42.8         | \$59.4 |
| Effective tax rate                        | 29.7 %         | 35.9 % |

Our effective tax rate of 28.5% for the three months ended June 30, 2016 was comparable to the same period in 2015. The effective tax rate varied from the U.S. federal statutory rate for the three months ended June 30, 2016 primarily due to the net impact of foreign operations.

Our effective tax rate of 29.7% for the six months ended June 30, 2016 decreased from 35.9% for the same period in 2015. The decrease was primarily due to tax impacts of our Realignment Programs and the Venezuelan exchange rate remeasurement loss in the first quarter of 2015 that did not recur. The effective tax rate varied from the U.S. federal statutory rate for the six months ended June 30, 2016 primarily due to the net impact of foreign operations.

## Other Comprehensive Income (Loss)

|                                   | Three Months |          |
|-----------------------------------|--------------|----------|
|                                   | Ended June   |          |
|                                   | 30,          |          |
| (Amounts in millions)             | 2016         | 2015     |
| Other comprehensive (loss) income | \$(24.9)     | \$18.9   |
|                                   | Six Months   |          |
|                                   | Ended June   |          |
|                                   | 30,          |          |
| (Amounts in millions)             | 2016         | 2015     |
| Other comprehensive income (loss) | \$12.3       | \$(84.8) |

Other comprehensive loss for the three months ended June 30, 2016 increased \$43.8 million from income of \$18.9 million in 2015. The increased loss was primarily due to the foreign currency exchange rate movements of the Euro, Brazilian real, British pound and Mexican peso versus the U.S. dollar during the three months ended June 30, 2016, as compared with the same period in 2015.

Other comprehensive income for the six months ended June 30, 2016 increased \$97.1 million from a loss of \$84.8 million in 2015. The increased income was primarily due to the foreign currency exchange rate movements of the Euro, Brazilian real, British pound and Mexican peso versus the U.S. dollar during the six months ended June 30, 2016, as compared with the same period in 2015.

## Business Segments

We conduct our operations through three business segments based on type of product and how we manage the business. We evaluate segment performance and allocate resources based on each segment's operating income. The key operating results for our three business segments, EPD, IPD and FCD, are discussed below.

## Engineered Product Division Segment Results

Our largest business segment is EPD, through which we design, manufacture, distribute and service custom and other highly-engineered pumps and pump systems, mechanical seals, auxiliary systems and spare parts (collectively referred to as "original equipment"). EPD includes longer lead-time, highly-engineered pump products and shorter cycle engineered pumps and mechanical seals that are generally manufactured more quickly. EPD also manufactures replacement parts and related equipment and provides a full array of replacement parts, repair and support services (collectively referred to as "aftermarket"). EPD primarily operates in the oil and gas, power generation, chemical, water management and general industries. EPD operates in 47 countries with 32

Table of Contents

manufacturing facilities worldwide, 10 of which are located in Europe, 10 in North America, seven in Asia and five in Latin America, and it has 127 QRCs, including those co-located in manufacturing facilities and/or shared with FCD.

| (Amounts in millions, except percentages)         | Three Months<br>Ended June 30, |         |   |  |
|---|--------------------------------|---------|---|--|
|   | 2016                           | 2015    |   |  |
| Bookings  | \$465.5                        | \$575.3 |   |  |
| Sales   | 511.8                          | 570.8   |   |  |
| Gross profit                                      | 164.9                          | 189.9   |   |  |
| Gross profit margin                               | 32.2                           | % 33.3  | % |  |
| Segment operating income                          | 65.3                           | 86.2    |   |  |
| Segment operating income as a percentage of sales | 12.8                           | % 15.1  | % |  |

| (Amounts in millions, except percentages)         | Six Months Ended<br>June 30, |           |   |  |
|---|------------------------------|-----------|---|--|
|   | 2016                         | 2015      |   |  |
| Bookings  | \$889.9                      | \$1,070.6 |   |  |
| Sales   | 985.6                        | 1,054.9   |   |  |
| Gross profit                                      | 323.0                        | 355.5     |   |  |
| Gross profit margin                               | 32.8                         | % 33.7    | % |  |
| Segment operating income                          | 123.6                        | 155.1     |   |  |
| Segment operating income as a percentage of sales | 12.5                         | % 14.7    | % |  |

Bookings for the three months ended June 30, 2016 decreased by \$109.8 million, or 19.1%, as compared with the same period in 2015. The decrease included negative currency effects of approximately \$24 million. The decrease in customer bookings was primarily driven by the oil and gas and general industries. Bookings decreased \$42.1 million into the Middle East, \$27.3 million into Latin America, \$20.4 million into North America and \$19.6 million into Asia Pacific. The decrease was more heavily weighted towards customer original equipment bookings. Interdivision bookings (which are eliminated and are not included in consolidated bookings as disclosed above) decreased \$1.7 million.

Bookings for the six months ended June 30, 2016 decreased by \$180.7 million, or 16.9%, as compared with the same period in 2015. The decrease included negative currency effects of approximately \$47 million. The decrease in customer bookings was primarily driven by the oil and gas and general industries, partially offset by an increase in the power generation industry. Bookings decreased \$51.9 million into the Middle East, \$47.9 million into Latin America, \$29.9 million into North America, \$19.6 million into Europe, \$12.6 million into Africa and \$8.7 million into Asia Pacific. The decrease was more heavily weighted towards customer original equipment bookings. Interdivision bookings (which are eliminated and are not included in consolidated bookings as disclosed above) decreased \$4.7 million.

Sales for the three months ended June 30, 2016 decreased \$59.0 million, or 10.3%, as compared with the same period in 2015. The decrease included negative currency effects of approximately \$20 million. The decrease was more heavily weighted towards original equipment sales, resulting from decreased sales of \$25.2 million into Latin America, \$23.8 million into North America, \$6.5 million into Africa, \$6.5 million into the Middle East and \$2.1 million into Asia Pacific, partially offset by increased sales of \$4.9 million into Europe. Interdivision sales (which are eliminated and are not included in consolidated sales as disclosed above) decreased \$3.4 million.

Sales for the six months ended June 30, 2016 decreased \$69.3 million, or 6.6%, as compared with the same period in 2015. The decrease included negative currency effects of approximately \$52 million. The decrease was more heavily weighted towards aftermarket sales, resulting from decreased sales of \$46.7 million into Latin America and \$21.3 million into North America. Interdivision sales (which are eliminated and are not included in consolidated sales as disclosed above) decreased \$4.5 million.

Gross profit for the three months ended June 30, 2016 decreased by \$25.0 million, or 13.2%, as compared with the same period in 2015. Gross profit margin for the three months ended June 30, 2016 of 32.2% decreased from 33.3% for the same period in 2015. The decrease in gross profit margin was primarily attributable to the negative impact of

decreased sales on our absorption of fixed manufacturing costs, partially offset by savings achieved and decreased charges related to our Realignment Programs and a mix shift to higher margin aftermarket sales.

Gross profit for the six months ended June 30, 2016 decreased by \$32.5 million, or 9.1%, as compared with the same period in 2015. Gross profit margin for the six months ended June 30, 2016 of 32.8% decreased from 33.7% for the same period in 2015.

Table of Contents

The decrease in gross profit margin was primarily attributable to the negative impact of decreased sales on our absorption of fixed manufacturing costs, partially offset by savings achieved and decreased charges related to our Realignment Programs.

Operating income for the three months ended June 30, 2016 decreased by \$20.9 million, or 24.2%, as compared with the same period in 2015. The decrease included negative currency effects of approximately \$2 million. The decrease was due to a \$25.0 million decrease in gross profit, partially offset by a \$4.5 million decrease in SG&A (including a decrease due to currency effects of approximately \$2.7 million). The decrease in SG&A is primarily due to lower selling-related expenses as compared to the same period in 2015.

Operating income for the six months ended June 30, 2016 decreased by \$31.5 million, or 20.3%, as compared with the same period in 2015. The decrease included negative currency effects of approximately \$6 million. The decrease was due to a \$32.5 million decrease in gross profit, partially offset by \$0.1 million decrease in SG&A (including a decrease due to currency effects of approximately \$8 million). The decrease in SG&A is due to lower selling-related expenses as compared to the same period in 2015.

Backlog of \$1,074.8 million at June 30, 2016 decreased by \$82.5 million, or 7.1%, as compared with December 31, 2015. Currency effects provided an increase of approximately \$22 million. Backlog at June 30, 2016 and December 31, 2015 included \$9.3 million and \$10.5 million, respectively, of interdivision backlog (which is eliminated and not included in consolidated backlog as disclosed above).

**Industrial Product Division Segment Results**

Through IPD, we design, manufacture, distribute and service engineered, pre-configured industrial pumps and pump systems, including submersible motors (collectively referred to as "original equipment"). Additionally, IPD manufactures replacement parts and related equipment, and provides a full array of support services (collectively referred to as "aftermarket"). IPD primarily operates in the oil and gas, chemical, water management, power generation and general industries. IPD operates 21 manufacturing facilities, five of which are located in the U.S., 11 in Europe, four in Asia, one in Latin America and it operates 33 QRCs worldwide, including 20 sites in Europe, six in the U.S., three in Latin America and four in Asia, including those co-located in manufacturing facilities.

|   | Three Months<br>Ended June 30, |         |    |  |
|---|--------------------------------|---------|----|--|
|   | 2016                           | 2015    |    |  |
| (Amounts in millions, except percentages)         |                                |         |    |  |
| Bookings  | \$212.3                        | \$205.3 |    |  |
| Sales   | 215.0                          | 260.8   |    |  |
| Gross profit                                      | 50.6                           | 58.8    |    |  |
| Gross profit margin                               | 23.5                           | % 22.5  | %  |  |
| Segment operating income                          | 5.5                            | 7.1     |    |  |
| Segment operating income as a percentage of sales | 2.6                            | % 2.7   | %  |  |
|   | Six Months Ended<br>June 30,   |         |    |  |
|   | 2016                           | 2015    |    |  |
| (Amounts in millions, except percentages)         |                                |         |    |  |
| Bookings  | \$420.0                        | \$452.8 |    |  |
| Sales   | 412.5                          | 484.2   |    |  |
| Gross profit                                      | 100.8                          | 101.7   |    |  |
| Gross profit margin                               | 24.4                           | % 21.0  | %  |  |
| Segment operating income (loss)                   | 9.5                            | (6.3)   | )  |  |
| Segment operating income as a percentage of sales | 2.3                            | % (1.3) | )% |  |

Bookings for the three months ended June 30, 2016 increased by \$7.0 million, or 3.4%, as compared with the same period in 2015. The increase included negative currency effects of less than \$1 million. The increase in customer bookings was primarily driven by the chemical, water management and general industries, partially offset by decreased customer bookings in the power generation and oil and gas industries. Bookings increased \$14.3 million into the Middle East and \$3.6 million into North America, partially offset by decreased bookings of \$8.8 million into Asia Pacific and \$2.7 million into Latin America. The increase was primarily driven by aftermarket bookings.

Interdivision bookings (which are eliminated and are not included in consolidated bookings as disclosed above) decreased \$4.0 million.

Bookings for the six months ended June 30, 2016 decreased by \$32.8 million, or 7.2%, as compared with the same period in 2015. The decrease included negative currency effects of approximately \$6 million. The decrease in customer bookings was

30

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## Table of Contents

primarily driven by the oil and gas and power generation industries. Bookings decreased \$9.0 million into Europe, \$8.6 million into Asia Pacific and \$6.0 million into North America. The decrease was driven by customer original equipment bookings. Interdivision bookings (which are eliminated and are not included in consolidated bookings as disclosed above) decreased \$3.9 million.

Sales for the three months ended June 30, 2016 decreased \$45.8 million, or 17.6%, as compared with the same period in 2015. The decrease included negative currency effects of approximately \$2 million and was primarily driven by customer original equipment sales. Customer sales decreased \$11.7 million into Europe, \$10.9 million into Asia Pacific, \$9.6 million into North America and \$9.6 million into Latin America. Interdivision sales (which are eliminated and are not included in consolidated sales as disclosed above) decreased \$5.3 million when compared to the same period in 2015.

Sales for the six months ended June 30, 2016 decreased \$71.7 million, or 14.8%, as compared with the same period in 2015. The decrease included negative currency effects of approximately \$8 million and was primarily driven by customer original equipment sales. Customer sales decreased \$27.1 million into Europe, \$25.3 million into Asia Pacific and \$11.3 million into Latin America. Interdivision sales (which are eliminated and are not included in consolidated sales as disclosed above) decreased \$3.2 million when compared to the same period in 2015.

Gross profit for the three months ended June 30, 2016 decreased by \$8.2 million, or 13.9%, as compared with the same period in 2015. Gross profit margin for the three months ended June 30, 2016 of 23.5% increased from 22.5% for the same period in 2015. The increase in gross profit margin was primarily attributable to savings achieved and decreased charges related to our Realignment Programs, the negative impact of Purchase Price Adjustments in 2015 that did not recur and a mix shift to higher margin aftermarket sales, partially offset by the negative impact of decreased sales on our absorption of fixed manufacturing costs and the unfavorable impact of short-term operational inefficiencies related to the initial execution of certain realignment programs.

Gross profit for the six months ended June 30, 2016 decreased by \$0.9 million, or 0.9%, as compared with the same period in 2015. Gross profit margin for the six months ended June 30, 2016 of 24.4% increased from 21.0% for the same period in 2015. The increase in gross profit margin was primarily attributable to savings achieved and decreased charges related to our Realignment Programs and the negative impact of Purchase Price Adjustments in 2015 that did not recur, partially offset by the negative impact of decreased sales on our absorption of fixed manufacturing costs.

Operating income for the three months ended June 30, 2016 decreased by \$1.6 million, as compared with the same period in 2015. The decrease included currency benefits of less than one million. The decrease was primarily due to the \$8.2 million decrease in gross profit, partially offset by a \$6.4 million decrease in SG&A related primarily to decreased charges related to our Realignment Programs and lower SIHI integration costs.

Operating income for the six months ended June 30, 2016 increased by \$15.8 million, as compared with the same period in 2015. The increase included negative currency effects of approximately \$1 million. The increase was primarily due to a \$16.2 million decrease in SG&A related primarily to savings achieved and decreased charges related to our Realignment Programs and lower SIHI integration costs.

Backlog of \$433.9 million at June 30, 2016 increased by \$9.3 million, or 2.2%, as compared with December 31, 2015. Currency effects provided a increase of approximately \$4.8 million. Backlog at June 30, 2016 and December 31, 2015 included \$14.5 million and \$15.7 million, respectively, of interdivision backlog (which is eliminated and not included in consolidated backlog as disclosed above).

### Flow Control Division Segment Results

Our second largest business segment is FCD, which designs, manufactures and distributes a broad portfolio of engineered-to-order and configured-to-order isolation valves, control valves, valve automation products, boiler controls and related services. FCD leverages its experience and application know-how by offering a complete menu of engineered services to complement its expansive product portfolio. FCD has a total of 58 manufacturing facilities and QRCs in 25 countries around the world, with five of its 26 manufacturing operations located in the U.S., 13 located in Europe, seven located in Asia Pacific and one located in Latin America. Based on independent industry sources, we believe that FCD is the fourth largest industrial valve supplier on a global basis.





Table of Contents

|   | Three Months<br>Ended June 30, |         |   |  |
|---|--------------------------------|---------|---|--|
| (Amounts in millions, except percentages)         | 2016                           | 2015    |   |  |
| Bookings  | \$312.9                        | \$355.5 |   |  |
| Sales   | 317.2                          | 356.4   |   |  |
| Gross profit                                      | 108.3                          | 123.7   |   |  |
| Gross profit margin                               | 34.1                           | % 34.7  | % |  |
| Segment operating income                          | 48.5                           | 54.5    |   |  |
| Segment operating income as a percentage of sales | 15.3                           | % 15.3  | % |  |

|   | Six Months Ended<br>June 30, |         |   |  |
|---|------------------------------|---------|---|--|
| (Amounts in millions, except percentages)         | 2016                         | 2015    |   |  |
| Bookings  | \$622.6                      | \$678.0 |   |  |
| Sales   | 616.2                        | 683.5   |   |  |
| Gross profit                                      | 207.3                        | 242.7   |   |  |
| Gross profit margin                               | 33.6                         | % 35.5  | % |  |
| Segment operating income                          | 87.3                         | 109.2   |   |  |
| Segment operating income as a percentage of sales | 14.2                         | % 16.0  | % |  |

Bookings for the three months ended June 30, 2016 decreased \$42.6 million, or 12.0%, as compared with the same period in 2015. The decrease included negative currency effects of approximately \$3 million. The decrease in customer bookings was primarily driven by the oil and gas and chemical industries. Customer bookings decreased \$32.6 million into North America and \$22.6 million into the Middle East, partially offset by an increase of \$10.4 million into Europe. The decrease was due to original equipment bookings.

Bookings for the six months ended June 30, 2016 decreased \$55.4 million, or 8.2%, as compared with the same period in 2015. The decrease included negative currency effects of approximately \$14 million. The decrease in customer bookings was primarily driven by the oil and gas and chemical industries. Customer bookings decreased \$45.6 million into North America and \$23.9 million into the Middle East, partially offset by an increase of \$15.9 million into Latin America. The decrease was primarily due to original equipment bookings.

Sales for the three months ended June 30, 2016 decreased \$39.2 million, or 11.0%, as compared with the same period in 2015. The decrease included negative currency effects of approximately \$1 million and was primarily driven by decreased customer original equipment sales. Sales decreased \$25.0 million into Europe, \$11.8 million into Asia Pacific, \$11.4 million into North America and \$6.7 million into Latin America, partially offset by increased sales of \$13.2 million into the Middle East.

Sales for the six months ended June 30, 2016 decreased \$67.3 million, or 9.8%, as compared with the same period in 2015. The decrease included negative currency effects of approximately \$9 million and was primarily driven by decreased customer original equipment sales. Sales decreased \$31.5 million into Asia Pacific, \$30.4 million into Europe, \$30.4 million into North America and \$12.4 million into Latin America, partially offset by increased sales of \$30.5 million into the Middle East.

Gross profit for the three months ended June 30, 2016 decreased by \$15.4 million, or 12.4%, as compared with the same period in 2015. Gross profit margin for the three months ended June 30, 2016 of 34.1% decreased from 34.7% for the same period in 2015. The decrease in gross profit margin was primarily attributable to the negative impact of decreased sales on our absorption of fixed manufacturing costs and lower margin projects that shipped from backlog, partially offset by savings achieved and decreased charges related to our Realignment Programs.

Gross profit for the six months ended June 30, 2016 decreased by \$35.4 million, or 14.6%, as compared with the same period in 2015. Gross profit margin for the six months ended June 30, 2016 of 33.6% decreased from 35.5% for the same period in 2015. The decrease in gross profit margin was primarily attributable to the negative impact of decreased sales on our absorption of fixed manufacturing costs and lower margin projects that shipped from backlog, partially offset by savings achieved and decreased charges related to our Realignment Programs compared to the same period in 2015.

Operating income for the three months ended June 30, 2016 decreased by \$6.0 million, or 11.0%, as compared with the same period in 2015. The decrease included negative currency effects of less than \$1 million. The decrease was primarily attributable to the \$15.4 million decrease in gross profit, partially offset by decreased SG&A of \$9.4 million. The decrease in SG&A was due to savings achieved and decreased charges related to our Realignment Programs and lower selling-related expenses as compared to the same period in 2015.

Table of Contents

Operating income for the six months ended June 30, 2016 decreased by \$21.9 million, or 20.1%, as compared with the same period in 2015. The decrease included negative currency effects of approximately \$1 million. The decrease was primarily attributable to the \$35.4 million decrease in gross profit, partially offset by decreased SG&A of \$13.6 million. The decrease in SG&A was primarily due to savings achieved and decreased charges related to our Realignment Programs and lower selling-related expenses as compared to the same period in 2015.

Backlog of \$627.7 million at June 30, 2016 increased by \$5.7 million, or 0.9%, as compared with December 31, 2015.

Currency effects provided an increase of less than \$1 million.

**LIQUIDITY AND CAPITAL RESOURCES****Cash Flow and Liquidity Analysis**

|  | Six Months<br>Ended June<br>30, |         |
|--|---------------------------------|---------|
| (Amounts in millions)                                  | 2016                            | 2015    |
| Net cash flows provided by operating activities        | \$3.3                           | \$18.1  |
| Net cash flows used by investing activities            | (40.5)                          | (453.5) |
| Net cash flows (used) provided by financing activities | (68.4)                          | 316.9   |

Existing cash, cash generated by operations and borrowings available under our existing Revolving Credit Facility are our primary sources of short-term liquidity. We monitor the depository institutions that hold our cash and cash equivalents on a regular basis, and we believe that we have placed our deposits with creditworthy financial institutions. Our sources of operating cash generally include the sale of our products and services and the conversion of our working capital, particularly accounts receivable and inventories. Our cash balance at June 30, 2016 was \$266.0 million, as compared with \$366.4 million at December 31, 2015.

Our cash balance decreased by \$100.4 million to \$266.0 million at June 30, 2016 as compared with December 31, 2015. The cash used during the first six months of 2016 included \$48.2 million in dividend payments, \$36.9 million in capital expenditures and \$30.0 million of payments on long-term debt.

For the six months ended June 30, 2016, our cash provided by operating activities was \$3.3 million, as compared with \$18.1 million for the same period in 2015. Cash flow used by working capital decreased for the six months ended June 30, 2016, due primarily to decreased uses of cash related to inventory and accounts payable, partially offset by increased uses of cash related to accrued liabilities and income tax payable as compared to the same period in 2015.

Decreases in accounts receivable provided \$41.3 million of cash flow for the six months ended June 30, 2016 as compared with \$45.4 million for the same period in 2015. The decrease in accounts receivable was partially attributable to lower sales during the period as compared to the same period in 2015. As of June 30, 2016, our days' sales outstanding ("DSO") was 87 days as compared with 85 days as of June 30, 2015. We continue to experience delays in collecting payment on our accounts receivable from the national oil company in Venezuela, our primary Venezuelan customer. These accounts receivable are primarily U.S. dollar-denominated and are not disputed.

However, while we have not historically had write-offs relating to this customer, the accounts receivable continue to be significantly in arrears. The increased deterioration of the social, political, economic and legal climate in 2016 has given rise to significant uncertainties about Venezuela's economic and political stability, and while we continue to conduct business with our Venezuelan customer, the volume of activity has diminished significantly in 2016 from prior year levels. Accordingly, our ability to fully collect the accounts receivable from our primary Venezuelan customer could be materially adversely impacted. We continue to discuss payments with our Venezuelan customer and currently believe the accounts receivable will be collected; however, we will continue to evaluate collectability. Our total outstanding accounts receivable with this customer was approximately 7% of our gross accounts receivable at both June 30, 2016 and December 31, 2015. Given the experienced delays in collecting payments we estimate that approximately 69% of the outstanding accounts receivable will most likely not be collected within one year and therefore has been classified as long-term within other assets, net on our June 30, 2016 condensed consolidated balance sheet as compared to 64% at December 31, 2015.

Increases in inventory used \$51.9 million and \$113.0 million of cash flow for the six months ended June 30, 2016 and June 30, 2015, respectively. Inventory turns were 2.7 times at June 30, 2016, compared with 2.8 times for the same period in 2015. Our calculation of inventory turns does not reflect the impact of advanced cash received from our customers. Decreases in accounts payable used \$76.4 million of cash flow for the six months ended June 30, 2016 as compared with \$124.0 million for the same period in 2015. Decreases in accrued liabilities and income taxes payable used \$77.2 million of cash flow for the six months ended June 30, 2016 as compared with \$5.5 million for the same period in 2015.

Cash flows used by investing activities during the six months ended June 30, 2016 were \$40.5 million as compared with \$453.5 million for the same period in 2015. Cash outflows for the same period in 2015 resulted primarily from payments for the SIHI acquisition of \$341.5 million. In the second quarter of 2016 we divested of a non-strategic foundry business which resulted

## Table of Contents

in a cash outflow of \$5.1 million and a loss of \$7.7 million. Capital expenditures during the six months ended June 30, 2016 were \$36.9 million, a decrease of \$76.9 million as compared with the same period in 2015. Our capital expenditures are generally focused on strategic initiatives to pursue new markets, geographic expansion, information technology infrastructure, ongoing scheduled replacements and upgrades and cost reduction opportunities. In 2016, total capital expenditures are expected to be between \$105 million and \$115 million.

Cash flows used by financing activities during the six months ended June 30, 2016 were \$68.4 million as compared with a source of cash of \$316.9 million for the same period in 2015. Cash outflows during the six months ended June 30, 2016 resulted primarily from \$48.2 million of dividend payments and \$30.0 million of payments on long-term debt. Cash inflows for the same period in 2015 resulted primarily from the \$526.3 million net proceeds from the issuance of the 2022 Euro Senior Notes, partially offset by the repurchase of \$139.6 million of common shares and \$45.9 million in dividend payments.

Our Senior Credit Facility matures in October 2020. Approximately 12% of our outstanding Term Loan Facility is due to mature in the remainder of 2016 and approximately 24% in 2017. As of June 30, 2016, we had available capacity of \$877.3 million on our \$1.0 billion Revolving Credit Facility. Our Revolving Credit Facility is committed and held by a diversified group of financial institutions.

During the six months ended June 30, 2016 and 2015, we contributed \$7.0 million and \$6.0 million, respectively, to our U.S. pension plan. At December 31, 2015 our U.S. pension plan was fully funded as defined by applicable law. After consideration of our funded status, we currently anticipate making approximately \$13 million in contributions to our U.S. pension plan in 2016, excluding direct benefits paid. We continue to maintain an asset allocation consistent with our strategy to maximize total return, while reducing portfolio risks through asset class diversification.

At June 30, 2016, \$260.1 million of our total cash balance of \$266.0 million was held by foreign subsidiaries, \$146.9 million of which we consider permanently reinvested outside the U.S. Based on the expected near-term liquidity needs of our various geographies and our currently available sources of domestic short-term liquidity, we currently do not anticipate the need to repatriate any permanently reinvested cash to fund domestic operations that would generate adverse tax results. However, in the event this cash is needed to fund domestic operations, we estimate the full \$146.9 million could be repatriated resulting in a U.S. cash tax liability between \$5.0 million and \$15.0 million. Should we be required to repatriate this cash, it could limit our ability to assert permanent reinvestment of foreign earnings and invested capital in future periods.

Considering our current debt structure and cash needs, we currently believe cash flows generated from operating activities combined with availability under our Revolving Credit Facility and our existing cash balance will be sufficient to meet our cash needs for the next 12 months. Cash flows from operations could be adversely affected by economic, political and other risks associated with sales of our products, operational factors, competition, fluctuations in foreign exchange rates and fluctuations in interest rates, among other factors. See "Cautionary Note Regarding Forward-Looking Statements" below.

On November 13, 2014, our Board of Directors approved a \$500.0 million share repurchase authorization, of which as of June 30, 2016, we have \$160.7 million of remaining capacity. While we intend to continue to return cash through dividends and/or share repurchases for the foreseeable future, any future returns of cash through dividends and/or share repurchases will be reviewed individually, declared by our Board of Directors and implemented by management at its discretion, depending on our financial condition, business opportunities and market conditions at such time.

### Acquisition

We regularly evaluate acquisition opportunities of various sizes. The cost and terms of any financing to be raised in conjunction with any acquisition, including our ability to raise economical capital, is a critical consideration in any such evaluation.

Note 2 to our condensed consolidated financial statements included in this Quarterly Report contains a discussion of our acquisition.

### Financing

#### Credit Facilities

See Note 10 to our consolidated financial statements included in our 2015 Annual Report and Note 5 to our condensed consolidated financial statements included in this Quarterly Report for a discussion of our Senior Credit Facility and covenants related to our Senior Credit Facility. We complied with all covenants through June 30, 2016.

**CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

Management's discussion and analysis of financial condition and results of operations are based on our condensed consolidated financial statements and related footnotes contained within this Quarterly Report. Our critical accounting policies used in the preparation of our condensed consolidated financial statements were discussed in "Item 7.

Management's Discussion and Analysis

## Table of Contents

of Financial Condition and Results of Operations" of our 2015 Annual Report. These critical policies, for which no significant changes have occurred in the six months ended June 30, 2016, include:

Revenue Recognition;

Deferred Taxes, Tax Valuation Allowances and Tax Reserves;

Reserves for Contingent Loss;

Retirement and Postretirement Benefits; and

Valuation of Goodwill, Indefinite-Lived Intangible Assets and Other Long-Lived Assets.

The process of preparing condensed consolidated financial statements in conformity with U.S. GAAP requires the use of estimates and assumptions to determine certain of the assets, liabilities, revenues and expenses. These estimates and assumptions are based upon what we believe is the best information available at the time of the estimates or assumptions. The estimates and assumptions could change materially as conditions within and beyond our control change. Accordingly, actual results could differ materially from those estimates. The significant estimates are reviewed quarterly with the Audit Committee of our Board of Directors.

Based on an assessment of our accounting policies and the underlying judgments and uncertainties affecting the application of those policies, we believe that our condensed consolidated financial statements provide a meaningful and fair perspective of our consolidated financial condition and results of operations. This is not to suggest that other general risk factors, such as changes in worldwide demand, changes in material costs, performance of acquired businesses and others, could not adversely impact our consolidated financial condition, results of operations and cash flows in future periods. See "Cautionary Note Regarding Forward-Looking Statements" below.

### ACCOUNTING DEVELOPMENTS

We have presented the information about pronouncements not yet implemented in Note 1 to our condensed consolidated financial statements included in this Quarterly Report.

### Cautionary Note Regarding Forward-Looking Statements

This Quarterly Report includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, which are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995, as amended. Words or phrases such as, "may," "should," "expects," "could," "intends," "plans," "anticipates," "estimates," "believes," "predicts" or other similar expressions are intended to identify forward-looking statements, which include, without limitation, statements concerning our future financial performance, future debt and financing levels, investment objectives, implications of litigation and regulatory investigations and other management plans for future operations and performance.

The forward-looking statements included in this Quarterly Report are based on our current expectations, projections, estimates and assumptions. These statements are only predictions, not guarantees. Such forward-looking statements are subject to numerous risks and uncertainties that are difficult to predict. These risks and uncertainties may cause actual results to differ materially from what is forecast in such forward-looking statements, and include, without limitation, the following:

- a portion of our bookings may not lead to completed sales, and our ability to convert bookings into revenues at acceptable profit margins;

- changes in the global financial markets and the availability of capital and the potential for unexpected cancellations or delays of customer orders in our reported backlog;

- our dependence on our customers' ability to make required capital investment and maintenance expenditures;



risks associated with cost overruns on fixed fee projects and in accepting customer orders for large complex custom engineered products;

the substantial dependence of our sales on the success of the oil and gas, chemical, power generation and water management industries;

the adverse impact of volatile raw materials prices on our products and operating margins;

- economic, political and other risks associated with our international operations, including military actions or trade embargoes that could affect customer markets, particularly North African, Russian and Middle Eastern markets and global oil and gas producers, and non-compliance with U.S. export/reexport control, foreign corrupt practice laws, economic sanctions and import laws and regulations;

increased aging and slower collection of receivables, particularly in Latin America and other emerging markets;

our exposure to fluctuations in foreign currency exchange rates, particularly the Euro and British pound and in hyperinflationary countries such as Venezuela;

our furnishing of products and services to nuclear power plant facilities and other critical applications;

potential adverse consequences resulting from litigation to which we are a party, such as litigation involving asbestos-containing material claims;

a foreign government investigation regarding our participation in the United Nations Oil-For-Food Program;

expectations regarding acquisitions and the integration of acquired businesses;

our relative geographical profitability and its impact on our utilization of deferred tax assets, including foreign tax credits;

the potential adverse impact of an impairment in the carrying value of goodwill or other intangible assets;

our dependence upon third-party suppliers whose failure to perform timely could adversely affect our business operations;

the highly competitive nature of the markets in which we operate;

environmental compliance costs and liabilities;

potential work stoppages and other labor matters;

access to public and private sources of debt financing;

our inability to protect our intellectual property in the U.S., as well as in foreign countries;

obligations under our defined benefit pension plans;

risks and potential liabilities associated with cyber security threats; and

our inability to execute and realize the expected financial benefits of our strategic manufacturing optimization and other cost-saving initiatives.

These and other risks and uncertainties are more fully discussed in the risk factors identified in "Item 1A. Risk Factors" in Part I of our 2015 Annual Report and Part II of this 10-Q, and may be identified in our Quarterly Reports on Form 10-Q and our other filings with the SEC and/or press releases from time to time. All forward-looking statements included in this document are based on information available to us on the date hereof, and we assume no obligation to update any forward-looking statement.

### Item 3. Quantitative and Qualitative Disclosures about Market Risk.

We have market risk exposure arising from changes in interest rates and foreign currency exchange rate movements in foreign exchange contracts. We are exposed to credit-related losses in the event of non-performance by counterparties to financial instruments, but we currently expect our counterparties will continue to meet their obligations given their current creditworthiness.

#### Interest Rate Risk

Our earnings are impacted by changes in short-term interest rates as a result of borrowings under our Senior Credit Facility, which bear interest based on floating rates. At June 30, 2016, we had \$255.0 million of variable rate debt obligations outstanding under our Senior Credit Facility with a weighted average interest rate of 1.88%. A hypothetical change of 100 basis points in the interest rate for these borrowings, assuming constant variable rate debt levels, would have changed interest expense by \$1.3 million for the six months ended June 30, 2016.

#### Foreign Currency Exchange Rate Risk

A substantial portion of our operations are conducted by our subsidiaries outside of the U.S. in currencies other than the U.S. dollar. Almost all of our non-U.S. subsidiaries conduct their business primarily in their local currencies, which are also their functional currencies. Foreign currency exposures arise from translation of foreign-denominated assets and liabilities into U.S. dollars and from transactions, including firm commitments and anticipated transactions, denominated in a currency other than a non-U.S. subsidiary's functional currency. In March 2015, we designated €255.7 million of our €500.0 million 2022 Euro Senior Notes as a net investment hedge of our investments in certain of our international subsidiaries that use the Euro as their functional currency. Generally, we view our investments in foreign subsidiaries from a long-term perspective and use capital structuring techniques to manage our investment in foreign subsidiaries as deemed necessary. We realized net (losses) gains associated with foreign currency translation of \$(28.6) million and \$13.7 million for the three months June 30, 2016 and 2015 and \$5.1 million and \$(92.8) million for the six months ended June 30, 2016 and 2015, which are included in other comprehensive income (loss). We employ a foreign currency risk management strategy to minimize potential changes in cash flows from unfavorable foreign currency exchange rate movements. Where available, the use of foreign exchange contracts allows us to mitigate transactional exposure to exchange rate fluctuations as the gains or losses incurred on the foreign exchange contracts will offset, in whole or in part, losses or gains on the underlying foreign currency exposure. Our policy allows foreign currency coverage only for identifiable foreign currency exposures and beginning in the fourth quarter of 2013 instruments that meet certain criteria are designated for hedge accounting. As of June 30, 2016, we had a U.S. dollar equivalent of \$414.6 million in aggregate notional amount outstanding in foreign exchange contracts with third parties, as compared with \$397.3 million at December 31, 2015. Transactional currency gains and losses arising from transactions outside of our sites' functional currencies and changes in fair value of non-designated foreign exchange contracts are included in our consolidated results of operations. We recognized foreign currency net gains (losses) of \$5.7 million and \$(5.1) million for the three months ended June 30, 2016 and 2015, respectively, and \$2.1 million and \$(24.3) million for the six months ended June 30, 2016 and 2015, respectively, which are included in other income (expense), net in the accompanying condensed consolidated statements of income.

Based on a sensitivity analysis at June 30, 2016, a 10% change in the foreign currency exchange rates for the six months ended June 30, 2016 would have impacted our net earnings by approximately \$6 million. This calculation assumes that all currencies change in the same direction and proportion relative to the U.S. dollar and that there are no indirect effects, such as changes in non-U.S. dollar sales volumes or prices. This calculation does not take into account the impact of the foreign currency exchange contracts discussed above.

### Item 4. Controls and Procedures.

#### Disclosure Controls and Procedures

Disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act) are controls and other procedures that are designed to ensure that the information that we are required to disclose in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods

specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

In connection with the preparation of this Quarterly Report, our management, under the supervision and with the participation of our principal executive officer and principal financial officer, carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures as of June 30, 2016. Based on this evaluation, our principal executive officer and principal financial officer concluded that our disclosure controls and procedures were effective at the reasonable assurance level as of June 30, 2016.

#### Changes in Internal Control Over Financial Reporting

There have been no changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act) during the quarter ended June 30, 2016 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents**PART II — OTHER INFORMATION****Item 1. Legal Proceedings.**

We are party to the legal proceedings that are described in Note 9 to our condensed consolidated financial statements included in "Item 1. Financial Statements" of this Quarterly Report, and such disclosure is incorporated by reference into this "Item 1. Legal Proceedings." In addition to the foregoing, we and our subsidiaries are named defendants in certain other ordinary routine lawsuits incidental to our business and are involved from time to time as parties to governmental proceedings, all arising in the ordinary course of business. Although the outcome of lawsuits or other proceedings involving us and our subsidiaries cannot be predicted with certainty, and the amount of any liability that could arise with respect to such lawsuits or other proceedings cannot be predicted accurately, management does not currently expect the amount of any liability that could arise with respect to these matters, either individually or in the aggregate, to have a material adverse effect on our financial position, results of operations or cash flows.

**Item 1A. Risk Factors.**

There are numerous factors that affect our business and results of operations, many of which are beyond our control. In addition to other information set forth in this Quarterly Report, careful consideration should be given to "Item 1A. Risk Factors" in Part I and "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" in Part II of our 2015 Annual Report, which contain descriptions of significant factors that might cause the actual results of operations in future periods to differ materially from those currently expected or desired.

There have been no material changes in risk factors discussed in our 2015 Annual Report and subsequent SEC filings. The risks described in this Quarterly Report, our 2015 Annual Report and in our other SEC filings or press releases from time to time are not the only risks we face. Additional risks and uncertainties are currently deemed immaterial based on management's assessment of currently available information, which remains subject to change; however, new risks that are currently unknown to us may surface in the future that materially adversely affect our business, financial condition, results of operations or cash flows.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.**

Note 11 to our condensed consolidated financial statements included in this Quarterly Report includes a discussion of our share repurchase program and payment of quarterly dividends on our common stock.

During the quarter ended June 30, 2016 we had no repurchases of common shares. As of June 30, 2016, we have \$160.7 million of remaining capacity under our current share repurchase program. The following table sets forth the activity for each of the three months during the quarter ended June 30, 2016:

| Period       | Total<br>Number<br>of Shares<br>Tendered | Average<br>Price<br>per<br>Share | Total<br>Number of<br>Shares<br>Purchased<br>as<br>Part of<br>Publicly<br>Announced<br>Program | Maximum<br>Number of<br>Shares (or<br>Approximate<br>Dollar<br>Value) That<br>May Yet<br>Be<br>Purchased<br>Under<br>the Program<br>(in millions) |
|--------------|--|----------------------------------|--|---|
| April 1 - 30 | 12,883                                   | (1) \$42.61                      | —  | \$ 160.7  |
| May 1 - 31   | 3,347                                    | (2) 46.09                        | —  | 160.7   |
| June 1 - 30  | 1,809                                    | (1) 50.92                        | —  | 160.7   |
| Total        | 18,039                                   | \$ 47.59                         | —  |   |

(1) Shares tendered by employees to satisfy minimum tax withholding amounts for Restricted Shares.

Represents 355 shares that were tendered by employees to satisfy minimum tax withholding amounts for Restricted  
(2) Shares at an average price per share of \$44.47, and 2,992 shares purchased at a price of \$46.12 per share by a rabbi  
trust that we established in connection with our director deferral plans, pursuant to which non-employee directors  
may elect to defer directors' quarterly cash compensation to be paid at a later date in the form of common stock.

Table of Contents

Item 6. Exhibits.

A list of exhibits filed or furnished as part of this Quarterly Report on Form 10-Q is set forth on the Exhibits Index immediately following the signature page of this report and is incorporated herein by reference.

37

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Table of Contents

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

FLOWSERVE CORPORATION

Date: July 28, 2016 /s/ Mark A. Blinn

Mark A. Blinn

President and Chief Executive Officer

(Principal Executive Officer)

Date: July 28, 2016 /s/ Karyn F. Ovelmen

Karyn F. Ovelmen

Executive Vice President and Chief Financial Officer

(Principal Financial Officer)

Table of Contents

Exhibits Index

| Exhibit No. | Description  |
|-------------|--|
| 3.1         | Restated Certificate of Incorporation of Flowserve Corporation (incorporated by reference to Exhibit 3.1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2013). |
| 3.2         | Flowserve Corporation By-Laws, as amended and restated effective May 19, 2016 (incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K dated May 20, 2016).      |
| 31.1+       | Certification of Principal Executive Officer pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.                       |
| 31.2+       | Certification of Principal Financial Officer pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.                       |
| 32.1++      | Certification of Principal Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.   |
| 32.2++      | Certification of Principal Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.   |
| 101.INS     | XBRL Instance Document   |
| 101.SCH     | XBRL Taxonomy Extension Schema Document  |
| 101.CAL     | XBRL Taxonomy Extension Calculation Linkbase Document  |
| 101.LAB     | XBRL Taxonomy Extension Label Linkbase Document  |
| 101.PRE     | XBRL Taxonomy Extension Presentation Linkbase Document   |
| 101.DEF     | XBRL Taxonomy Extension Definition Linkbase Document   |

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+ Filed herewith.

++ Furnished herewith.