



Third Quarter 2014 Results



# Forward Looking Statements

This presentation contains statements that we believe are “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements generally can be identified by the use of words such as “may,” “will,” “expect,” “intend,” “estimate,” “anticipate,” “believe,” “continue,” “guidance” or words of similar meaning. All forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from those anticipated as of the date of this presentation. Important factors that could cause actual results to differ materially from these expectations include, among other things, the following: uncertain costs, savings and timeframes associated with the implementation of the new enterprise resources planning system; potential weakening in the high efficiency boiler segment in the U. S.; the ability to execute our acquisition strategy; significant volatility in raw material prices; competitive pressures on the company’s businesses; inability to implement pricing actions; instability in the company’s replacement markets; strength or duration of any recoveries in U. S. residential or commercial construction; a further slowdown in the growth of the Chinese economy; foreign currency fluctuations and adverse general economic conditions and capital market deterioration.

Forward-looking statements included in this presentation are made only as of the date of this presentation, and the company is under no obligation to update these statements to reflect subsequent events or circumstances. All subsequent written and oral forward-looking statements attributed to the company, or persons acting on its behalf, are qualified entirely by these cautionary statements. This presentation contains certain non-GAAP financial measures as that term is defined by the SEC. Non-GAAP financial measures are generally identified by “Adjusted” (Adj.) or “Non-GAAP” .

# Notice Regarding Financial Information



- ▶ This presentation contains non-GAAP financial information. Reconciliations from GAAP to non-GAAP measures are contained in the appendix of this presentation.
- ▶ All information should be read in conjunction with the historical financial statements and financial information contained in A. O. Smith's Annual Report on Form 10-K, periodic reports on Form 10-Q and Form 8-K, and public announcements of financial information.
- ▶ Copies of these reports are available on the Investor Relations section of A. O. Smith's website at <http://www.aosmith.com/investors/>



## Third Quarter Highlights

- ▶ Third quarter sales of \$582 million
  - Revenue 8.5 percent higher
  - China sales up 16 percent
- ▶ Adjusted earnings of \$.59 per share
  - Increase of 9 percent over \$.54 per share last year
- ▶ Cash returned to shareholders
  - YTD share repurchase totaled \$87 million
  - 25 percent dividend increase in January
  - On track to return approximately \$160 million this year
- ▶ First ERP “go live” successful



# Third Quarter Results

	2014	2013	change	% chg.
Sales	\$ 581.6	\$ 536.2	\$ 45.4	8.5%
Net Earnings	50.6	46.2		
Non-operating Pension (after-tax)	2.9	3.2		
Other adjustments (see below)	-	1.0		
Adjusted Earnings	\$ 53.5	\$ 50.4	\$ 3.1	6%

Other adjustments (after-tax)  
 2013: \$1.0 restructuring & impairment expenses

(\$ in millions)



## Third Quarter Adjusted EPS

	2014	2013	change	% chg.
EPS	\$0.56	\$0.50		
Non-operating Pension	0.03	0.03		
Other adjustments (see below)	<u>-</u>	<u>0.01</u>		
Adjusted EPS	<u><u>\$0.59</u></u>	<u><u>\$0.54</u></u>	\$ 0.05	9%

Other adjustments:  
2013: \$.01 per share restructuring & impairment expenses



# Third Quarter Sales

	2014	2013	change	% chg.
North America	\$ 392.4	\$ 370.1	\$ 22.3	6%
Rest of World	198.5	175.2	\$ 23.3	13%
Intersegment	<u>(9.3)</u>	<u>(9.1)</u>	<u>\$ (0.2)</u>	
Total	<u>\$ 581.6</u>	<u>\$ 536.2</u>	<u>\$ 45.4</u>	8.5%

(\$ in millions)



## Third Quarter Adjusted Earnings

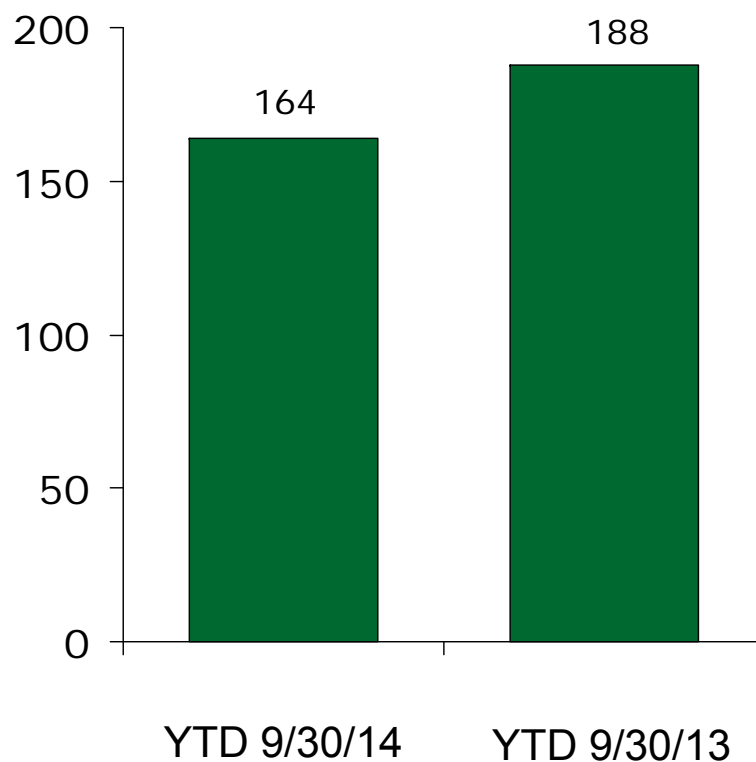
	2014	2013	change	% chg.
North America	\$ 56.3	\$ 56.6	\$ (0.3)	-1%
Rest of World	<u>30.0</u>	<u>26.9</u>	<u>3.1</u>	12%
Total Operating	86.3	83.5	2.8	3%
Adjusted Corporate	(10.6)	(14.3)	3.7	26%
Interest Expense	<u>(1.5)</u>	<u>(1.4)</u>	<u>(0.1)</u>	-7%
Adjusted Pre-tax Earnings	74.2	67.8	6.4	9%
Income Tax Expense	<u>(20.7)</u>	<u>(17.4)</u>	<u>(3.3)</u>	-19%
Adjusted Earnings	<u><u>\$ 53.5</u></u>	<u><u>\$ 50.4</u></u>	<u><u>\$ 3.1</u></u>	6%
<u>Adjusted Operating Margin</u>				
North America	14.3%	15.3%		
Rest of World	15.1%	15.4%		

(\$ in millions, except margins)





# Operating Cash Flow



\$ in millions

## Third Quarter Highlights

- ▶ Cash flow of \$164 million
- ▶ Debt to capital ratio of 16%
- ▶ Cash balance: \$524 million
- ▶ Net cash position: \$269 million
- ▶ Year - to - date stock repurchase: 1.8 million shares totaling \$87 million



# Adjusted 2014 EPS Guidance and Adjusted 2013 EPS

The following is a reconciliation of diluted EPS to adjusted EPS (non-GAAP) (all items are net of tax):

	2014 Guidance	2013
<b>Diluted EPS (GAAP)</b>	\$2.23 - \$2.27	\$ 1.83
Non-operating pension costs per diluted share	0.14	0.13
Settlement income per diluted share	-	(0.07)
Restructuring and impairment expenses per diluted share	-	0.17
<b>Adjusted EPS</b>	<u>\$2.37 - \$ 2.41</u>	<u>\$ 2.06</u>

*As of October 21, 2014*



## 2014 Outlook: 140 year Anniversary

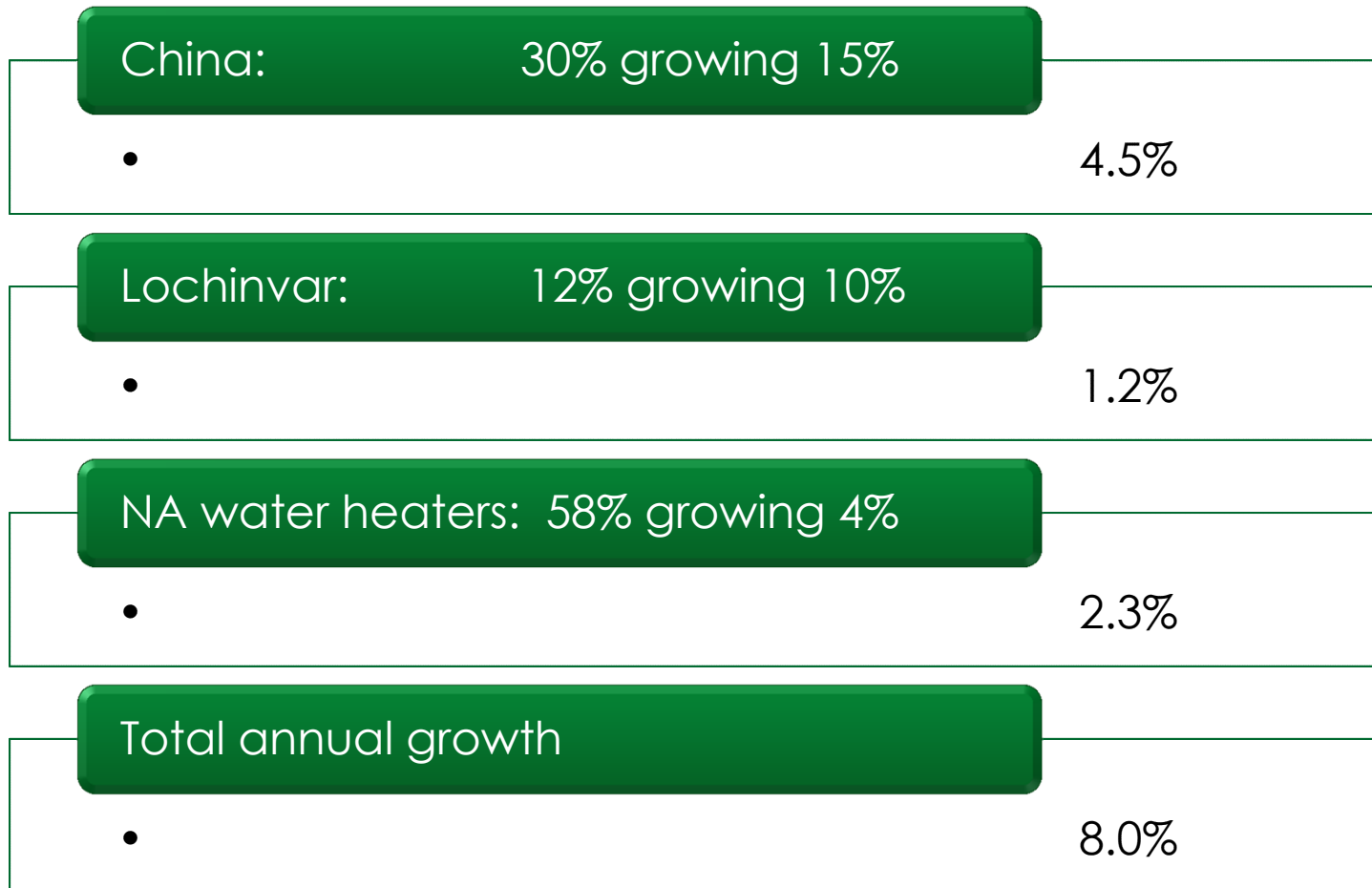
- ▶ China revenue grows over 17 percent
  - China water treatment gaining traction
- ▶ Lochinvar branded annual sales growth approximately 10 percent
  - Transition in North America to higher efficiency boilers continues
- ▶ U. S. construction/retrofit benefit
- ▶ Wholesale price increase effective May 1
- ▶ Incremental enterprise resources planning expense of \$3 to 4 million in Q4

*October 21, 2014*

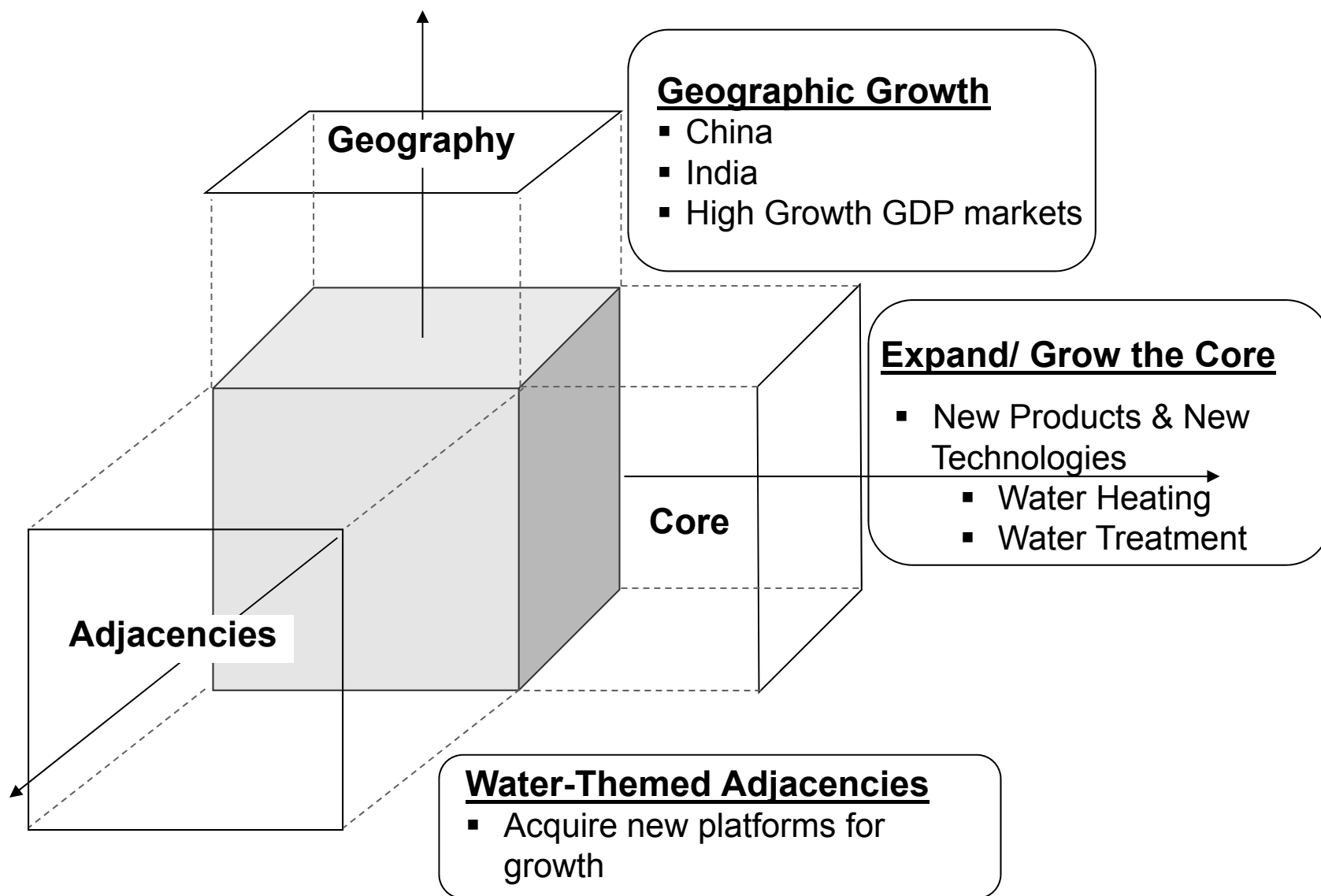
# China Growth Model : 2X GDP



# Growth Strategy: Organic Growth



# Growth Strategy: Acquisitions





# Investment Criteria

- ▶ Value creation opportunities
- ▶ ROIC in excess of cost of capital by second or third year
- ▶ Meet risk adjusted IRR hurdle rates
- ▶ Margin accretion with growth rates higher than U. S. GDP
- ▶ Accretive to earnings in the first year





*Answers to your questions...*







# Appendix





# Adjusted 2014 EPS Guidance and Adjusted 2013 EPS

The following is a reconciliation of diluted EPS to adjusted EPS (non-GAAP) (all items are net of tax):	2014 Guidance	2013
<b>Diluted EPS (GAAP)</b>	\$2.23 - \$2.27	\$ 1.83
Non-operating pension costs per diluted share	0.14	0.13
Restructuring and impairment expenses per diluted share	-	0.17
Settlement income per diluted share	_____ -	<u>(0.07)</u>
<b>Adjusted EPS</b>	<u>\$2.37 - 2.41</u>	<u>\$ 2.06</u>

*As of October 21, 2014*



# Adjusted Earnings & Adjusted EPS

(dollars in millions, except per share data)

The following is a reconciliation of net earnings and diluted EPS to adjusted earnings (non-GAAP) and adjusted EPS (non-GAAP):

	Three Months Ended September 30,	
	2014	2013
<b>Net Earnings (GAAP)</b>	\$ 50.6	\$ 46.2
Non-operating pension costs, before tax	4.9	5.2
Tax effect of non-operating pension costs	(2.0)	(2.0)
Restructuring and impairment expenses, before tax	-	1.3
Tax effect of restructuring and impairment expenses	-	(0.3)
Settlement income, before tax	-	-
Tax effect of settlement income	-	-
<b>Adjusted Earnings</b>	<u>\$ 53.5</u>	<u>\$ 50.4</u>
<b>Diluted EPS (GAAP)</b>	\$ 0.56	\$ 0.50
Non-operating pension costs per diluted share, before tax	0.05	0.05
Tax effect of non-operating pension costs per diluted share	(0.02)	(0.02)
Restructuring and impairment expenses per diluted share, before tax	-	0.01
Tax effect of restructuring and impairment expenses per diluted share	-	-
Settlement income per diluted share, before tax	-	-
Tax effect of settlement income per diluted share	-	-
<b>Adjusted EPS</b>	<u>\$ 0.59</u>	<u>\$ 0.54</u>



# Adjusted Earnings & Adjusted EPS

(dollars in millions, except per share data)

The following is a reconciliation of net earnings and diluted EPS to adjusted earnings (non-GAAP) and adjusted EPS (non-GAAP):

	Nine Months Ended September 30,	
	2014	2013
<b>Net Earnings (GAAP)</b>	\$ 154.6	\$ 127.3
Non-operating pension costs, before tax	14.7	14.8
Tax effect of non-operating pension costs	(5.8)	(5.7)
Restructuring and impairment expenses, before tax	-	18.2
Tax effect of restructuring and impairment expenses	-	(4.6)
Settlement income, before tax	-	(11.0)
Tax effect of settlement income	-	4.2
<b>Adjusted Earnings</b>	<u>\$ 163.5</u>	<u>\$ 143.2</u>
<b>Diluted EPS (GAAP)</b>	\$ 1.69	\$ 1.37
Non-operating pension costs per diluted share, before tax	0.16	0.16
Tax effect of non-operating pension costs per diluted share	(0.06)	(0.06)
Restructuring and impairment expenses per diluted share, before tax	-	0.19
Tax effect of restructuring and impairment expenses per diluted share	-	(0.05)
Settlement income per diluted share, before tax	-	(0.12)
Tax effect of settlement income per diluted share	-	0.05
<b>Adjusted EPS</b>	<u>\$ 1.79</u>	<u>\$ 1.54</u>



# Adjusted Segment Operating Earnings

(dollars in millions)

The following is a reconciliation of reported segment operating earnings to adjusted segment operating earnings (non-GAAP):

## Segment Operating Earnings (GAAP)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
North America	\$ 53.0	\$ 51.5	\$ 171.5	\$ 160.6
Rest of World	30.0	26.9	84.3	67.6
Inter-segment earnings elimination	-	(0.1)	-	(0.1)
<b>Total Segment Operating Earnings (GAAP)</b>	<b>\$ 83.0</b>	<b>\$ 78.3</b>	<b>\$ 255.8</b>	<b>\$ 228.1</b>
<b>Adjustments:</b>				
North America	\$ 3.3	\$ 5.2	\$ 11.0	\$ 18.3
Rest of World	-	-	-	-
<b>Total Adjustments</b>	<b>\$ 3.3</b>	<b>\$ 5.2</b>	<b>\$ 11.0</b>	<b>\$ 18.3</b>
<b>Adjusted Segment Operating Earnings</b>				
North America	\$ 56.3	\$ 56.7	\$ 182.5	\$ 178.9
Rest of World	30.0	26.9	84.3	67.6
Inter-segment earnings elimination	-	(0.1)	-	(0.1)
<b>Total Adjusted Segment Operating Earnings</b>	<b>\$ 86.3</b>	<b>\$ 83.5</b>	<b>\$ 266.8</b>	<b>\$ 246.4</b>

Additional Information:

## Adjustments: North America Segment

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Non-operating pension costs	\$ 3.3	\$ 3.9	\$ 11.0	\$ 11.1
Restructuring and impairment expenses	-	1.3	-	18.2
Settlement income	-	-	-	(11.0)
<b>Total North America Segment Adjustments</b>	<b>\$ 3.3</b>	<b>\$ 5.2</b>	<b>\$ 11.0</b>	<b>\$ 18.3</b>