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EDITED TRANSCRIPT

PNR - Pentair Ltd. at KeyBanc Capital Markets Industrial, Automotive & Transportation Conference

EVENT DATE/TIME: MAY 30, 2013 / 6:00PM GMT

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CORPORATE PARTICIPANTS

John Stauch *Pentair Ltd. - EVP and CFO*

PRESENTATION

John Stauch - *Pentair Ltd. - EVP and CFO*

Okay. Ready to go? Thank you. Thank you all for joining. I'm John Stauch. I'm the Chief Financial Officer of Pentair.

All right, so, here's our forward-looking statements. I'll let you read through it really quickly.

What I'm going to do is just start and give you a little bit of background on Pentair and Tyco, and our newly formed Pentair. I'll share with you a little bit of the strategy of the Company and how we're doing on our synergy update. I'll save plenty of time for questions and answers, so that we can get through all of the questions that you have.

Just to remind everybody, last September -- it feels like a long time ago, but it's just hours ago for us -- we closed the deal with Tyco in a reverse Morris Trust to form what we think is a $7.5 billion better-positioned industrial company, that positions us nicely in energy, which is a space that we felt we needed. As we're trying to serve the world's biggest needs, clearly, energy and water come together. As 4 billion people in the world seek a better life for themselves, they're going to put a lot of pressure on two things for certain. That is global energy and global water needs.

We believe, as a company, we are well-positioned in the water space as Pentair. We believe by merging with the Tyco Flow Control assets, we have an exposure to the energy space that we're quite comfortable with now, and allows us to serve that need in a better way.

Here's what the 2012 pro forma sales would have looked like. They're not much different as we look at 2013, other than we're forecasting somewhere around $7.5 billion in revenue versus $7.3 billion on a pro forma basis. You can see that we have a nice split between water and fluid. Within that Water and Fluid Solutions segment, which is our reporting segment, we have four global business units that serve the water space.

Within the Technical Solutions, we have two global business units. One is our Equipment Protection, which is enclosures for electrical protection equipment. And the other one is the Thermal Management business that we acquired from Flow Control, which is an energy management or thermal management business.

Finally, Valves & Controls, which is both a reporting segment and a global business unit. Valves & Controls serves a variety of industries, as I'll share with you a little bit later on.

By geography, we think we have a nice diversity of offerings. We believe that we've got a huge growth position in the US and Canada, especially as we serve the growing energy needs. We believe 25% of our revenues is exposed to fast growth markets. This should allow us to organically grow faster over the next three to five years, as we're exposed to where these 4 billion people in the world are, and where those demands that they're putting on the energy and water challenges need to be served.

Finally, by vertical, you can see that our largest vertical is Energy at 28%, and our smallest is Food and Beverage. It's still a meaningful 10%. Those are our two highest growth platforms, as I'll share with you. We have a nice balance between Residential, Commercial, Industrial, and our Infrastructure offerings.

As we take a look at our key growth verticals, in Energy, we serve oil and gas, power and mining. That makes up about 28% of our sales. We believe long-term, fundamentally, this should grow somewhere around 4% to 6% on a longer-term horizon. In the Industrial space, we serve chemical, pharmaceutical, and manufacturing. Again, about 26%, and roughly a slightly slower growth rate at 2% to 3%.

Our Residential and Commercial -- which has been our largest segment for legacy Pentair, where we were quite exposed to the North American residential market, and certainly felt that negative market headwind over the last six years. We are very fortunate and excited to see the recovery happening in 2013 and our experience in that recovery. We believe that's a 5% to 8% growth market.

When we take a look at the housing market in the United States, we focus a lot on the North American housing starts, and somewhere around 700,000 currently this year, heading to 1 million and possibly 1.5 million in a normal formation year. But in China alone, we are looking at serving 6 million housing starts in 2013, and close to 6.2 million in 2014. We do water purification for these applications, and we think we're going to benefit nicely from that expansion.

As we look at Infrastructure, obviously, an area in municipal that's been hit hard globally, with global tax revenues and certainly municipal tax revenues lower. There's still a lot of needs to serve the Industrial space, the growing residential population. We see that most of that burden is being shifted right now to the industrial world, both in the form of environmental standards and creating industrial companies required to produce their own natural resources to serve their needs. Again, that's about 13% of our overall revenue, and global demand, right now, we believe is flat.

Finally, in Food and Beverage, which, we believe, will be our fastest growing segment, primarily because we have a nice agriculture offering. We are participating through our Aquatic Systems business into the aquaculture business, global fish farming to feed the needs of the global population, and make sure that they are doing it in an efficient and productive way through protein, which comes primarily in the form of fish. It's not sustainable to continue to farm fish out of the ocean, and we're seeing a significant movement happening, which creates a more efficient and cost effective way to feed the growing demands.

Finally, Food and Beverage, which for us, is beer, dairy, soft drinks, where we have unique offerings in either CO2 recovery, biogas management, and beer membrane and beverage membrane filtration for these global providers.

Here's an example in oil and gas. Certainly, I'm not going to go into the deepest elements here. I want to make sure I leave time for your questions. But we produce valves, pumps, filtration, separation products, monitoring control systems, thermal management systems, and closed solutions for anything from a pipeline and storage or drilling and production. Anything between upstream, midstream, and downstream. Our revenue is about one-third/one-third/one-third. In any given year, that can move 5 points across those three segments, but that's generally our cut of current revenue.

I'm going to go through each one of these in tremendous detail. I'm sure that you'd enjoy that. I think the takeaway from this slide is that Pentair has offerings to serve a refinery. What we want you to take away from this is we have ways to collaborate more effectively. If you take a look at a refinery example, there is about $170 million in valves opportunities in a normal refinery. About $120 million of that is product and capabilities that we can serve today with our current technologies and applications and we believe that we have a better position to gain share than our competition.

The huge opportunity around the service element is one in which we believe we can also do better. There is around $35 million a year of valve capital spend and we should get our fair share of that over the next several years.

Here's the financial targets that we laid out when we did this deal, that we reiterated in our annual operating plan and our analyst meeting, and again in our Q1 earnings release. We believe that we are seeing revenue growth accelerating. Two reasons for that. One is, we are seeing comparisons year-over-year ease and become a little bit easier on a year-over-year basis. Second, some of the markets that turned down last year, Europe being one of them, we are starting to anniversary and to lap some of that headwind that we experienced on a year-over-year basis. Finally, some of our global Industrial markets -- and as I mentioned earlier, our Residential and Commercial markets are beginning to accelerate as we head into Q2 and the end of the year.

Overall, we're looking at about $7.6 billion of revenue this year, which will be a 4% year-over-year increase on a pro forma basis. We believe operating income is going to expand around 20% to $950 million, and then clip along at about a 20% or 18% to 20% CAGR to get to $1.3 billion by 2015. As you can see, EPS this year is still estimated at $310 million to $330 million and our 2015 overall forecast is still set at $5.00 per share.

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I want to take you through how we believe we're going to achieve that, but at the same time, just remind you that when we set these targets out there, we looked at it as the base of the core operations performing at about 10% operating income expansion per year, or about 50 to 60 basis points a year -- which, by both standards, either a Tyco Flow Control standard or a Pentair standard, would have been modest performance. And then on top of that, we've sought out to achieve $235 million of synergies to create the incremental value that we believe this deal provides to us.

Here's our path for creating that shareowner value. We believe the base performance, as I said, continues to get above market growth, primarily from being exposed to Energy, Food and Beverage and the Residential and Commercial space. As I mentioned earlier, we think about 70 to 80 basis points a year of expansion on an ongoing basis from the base.

Then we've got the accelerating standardization. This is really being driven by the fact that both companies had a series of complexity in the back office. We have 115 factories, which applied Lean enterprise on. Pentair is a Lean-based culture. We've been on that journey for over 13 years under the leadership of Randy Hogan. Most of our factories are moving up the scale or moving on the Lean score. We have two plants, one that received the Shingo Prize. Another one that's competing for a Shingo Prize.

We believe that we've built that operating culture and discipline into our factories, and we continue to have a culture that promotes continuous improvement. In two of the businesses, from legacy Pentair, we moved away from the stage of factories into Lean enterprise, where the back office had become standard and one ERP platform, one global SIA process, and overall, building competency in making sure we are efficient in our use of resources and capital. The rest of the businesses are performing and beginning to migrate along that journey.

Finally, the third element at creating value is a disciplined capital allocation strategy, which, for us, is 37 straight years of increasing the dividend. Proud to be a part of a company who has done that. A company that's also committed to making sure that we are continuing to buy back so that we can take some capital off the table. As a Lean-based culture, we believe that a constrained resource is the most utilized resource. Ultimately, making sure that we are maintaining investment-grade, but looking at the opportunity to continually invest in our high growth platforms in a way that we can make and create accretive acquisitions.

Obviously, ROIC is the number one metric of any company, both in how you evaluate it and how management evaluates itself. All the things above we believe continue to enhance our ROIC, our return on invested capital.

A little history on Pentair. We were founded in 1966. Our founder just passed away about a year ago. He only knew one thing. He knew he wanted to create value and leave a footprint in life. And he left, at the age of 46, a really high-performing company to start a company, and his only goal was return money to shareowners. At the time, most of the shareowners were family and friends; but as he evolved in becoming a public company, he stumbled out of the gate at least five times on everything from paper mills to canoes to air research balloons.

We found our way as a paper company who transformed itself into having a higher set of assets, moving into equipment protection. Along the way, we realized that the strategy of the Company, the transformational capability of the Company, and ultimately, the operating principles of the Company defined itself.

As a holding company, applying those principles, it worked well, until the average cost of an acquisition started to expand. Then we moved ourselves to an operating company under Randy Hogan's leadership. We became very focused on our Pentair Integrated Management System, making sure our strategy was aligned with long-term growth perspectives. We transformed ourselves again, shifting out of power tools and migrating into a water platform.

Finally, last year, we added to that the basic flow control assets that I talked about -- ultimately, moving ourselves into high-performance. What we mean by high-performance company is one that has an aspiration to be the next great industrial company. I know that's a big statement, and we know that's a big statement, but we want to be talked about in the likes of the Danaher's, the Honeywell's, the top performing companies in their industries. We think that we have the process to do it around making sure that our Lean enterprise and our Lean way of thinking, and waking up every day and believing we can be better the next day is ingrained in all 30,000 employees.

Our tailored management process that works across the company allows us to migrate resources like we did with the Flow Control acquisition, and taking 20 of our best operating folks who are very tuned to the language of Lean, and putting them in factories and putting them in regional leadership positions within the Valves & Controls space, to create that incremental value.

Finally, making sure that our process around growth become more like our process around productivity. Growth does not have to be a game of luck. It can certainly be a game of skill. By defining the measurements and the root cause countermeasures, which are inherent in Lean, and working them into our ability to fail quickly if we're going to fail, and to make sure that we learn from those failures and apply those into an industrial rich set of products and markets to provide incremental organic growth.

We've been at that journey about three years. We've been a Lean-based company about 12 to 13 years. We're always going to be in a different spot in the journey along the tools that we bring to the toolkit. But we believe making sure we have a way to do things, which is the Pentair Integrated Management System, allows us to define the "how" for our employees.

I talked earlier about culture. It's mentioned here as a force multiplier. We believe at Pentair we are on a rapid journey to be a great company. I think most employees wake up every day and they know what they're supposed to do. Good companies and great companies at least provide a sense of leadership around how they should do it. For us, I mentioned the Pentair Integrated Management System.

A lot of companies that get it right focus on the why. We spend a lot of time at Pentair talking about what this why is. Our resounding principles that we are living by today are the fact that there are these 4 billion people in the world, and they don't want to be denied. Our simple mission as a company is to improve the quality of lives of people around the world. It's simple. It resonates. We can tell our people that we are trying to improve their life. We tell the shareowners it's improving their life. For our customers, they should see that improvement in deliveries and qualities, and making sure that our products and our innovation remains world-class.

Along the way, getting 30,000 people to engage every single day is really what Lean is about. For those of you who have been attached around the Shingo Prize and how Shingo measures the success of a Lean-based company, they look at the processes, sure; but they interview the people. When we do this in Mexico or we do this in our Moorpark operation in California, they bring dual language speakers in to make sure that they're asking everybody on the shop floor, what is it that you do? How do you do it? Why do you do it? They ask those questions to make sure you have deep-rooted beliefs. We believe that that culture that we are bringing to Flow Control is well accepted.

People in the factory resonate nicely with disciplines like Lean because it helps make their life better. They have to serve the customer. They don't want to hear the phone call of the late or past due. They don't want to deal with warranty and quality issues. That part tends to be easier. When you step out of the factory and you talk about the Lean enterprise, and you talk about making and reducing complexity, that's where it gets a little more challenging.

People like to bring their creative solutions to things. What we like to tell them is, their accounting capability might not be the creative solution we are looking for. We should agree that the standard way we do accounting, the standard way we do the back office work, should be something that we can make very simple across the organization, and create incremental value for our customers through eliminating the waste there as well.

Here is our $230 million of synergy funnel. It's set up by putting a three-year goal of $20 million of direct material out there. We have a goal of $45 million of Lean enterprise. As I mentioned earlier, we've got 115 factories. I know you're going to tell me these goals look wimpy. We've heard that multiple times. I think we would agree with you. The reason we set this up is to remind everybody we need to get the base operating performance, and we need to get the incremental synergies.

When we look at direct material, we're looking at a number that we're working from a relatively low inflation rate at the moment. We have a funnel of $100 million of savings related and identified already in direct material. We know that if we apply the processes and disciplines we have today, we are going to obtain that. We also know from experience that we tend to get anywhere from $1 million to $3 million over a three-year horizon from factory savings. Again, the $45 million assumes that there was something built in the core. But we are also making sure that people are focused on the bottom half of this chart, which is the standardization aspects.

We've already locked in the $80 million of repositioning that we took from restructuring the organization out of the gate. We've identified and announced that we've received 100% of that. And now we are working on that $55 million of back office synergy. As you take a look at the way that that ramps throughout the year, you can see that a lot of Q1 was identifying and focusing, and Q2 was starting to realize that value, and as we get into Q4, you can see $35 million quarterly rate, which steps into $140 million of already identified 2014 synergies. We believe we're making a lot of progress.

As we turn to slide 16, this is the core piece of a lot of the work that we are now engaged in. Collectively as a company -- and it's a number we're not proud of -- we have over 70 ERPs. Right? At least we acknowledge reality, and now we can get on with what we need to do about it. If you really think about a standard work company, having 70 different ways to take orders, 70 different ways to build the SIOP process, 70 different ways to pay people, 70 different ways to pay vendors, that's certainly not an effective way to do business.

We've got a goal of getting to 13 by 2016 or '17. We believe that 13 recognizes 13 effective working platforms already in the Company. This is not a goal to invent a new way or to invent the theoretical best answer. This is a pragmatic solution to taking what we know already works in businesses, and beginning to migrate these other 50 ARPs to that end state platform. We think that that's the right approach.

By doing that, we are going to get 50 ARP systems moved. Each one of those should be worth at least $1 million. We're going to move 96 accounting centers to something closer to 25 to 26. We should save $500,000 at least per accounting center. We are going to save at least $5 million in payroll vendor costs, and we're going to save at least $20 million in backroom IT costs, just related to these activities alone.

I've already identified a funnel well over $100 million related to the $55 million that we are committing to by 2015. When you hear the sense of confidence in our voice about our ability to achieve the synergies, that's what you're hearing. We've got real pragmatic solutions. We have an aligned officer team and aligned President unit. We're all acting as one team, and now we're getting after what we need to do.

The "why" related to this is because we are in high-growth platforms that are going to be very demanding in making future acquisitions. Those future acquisitions need to be accretive. They need to create incremental value for the shareowners, and they need to be simple and not add to the complexity of our organizations. By simplifying our ability as a company to integrate those acquisitions, we should be able to be much more productive in making acquisitions as we go forward.

We take a look at the capital allocation philosophy, I think it starts with the fact that we are committed to maintaining an investment grade rating. We've always been investment grade since our founding. There is no reason to think that we can't be. We weathered a very difficult storm, like most companies did, by staying disciplined and making sure that there was always a little bit of cash saved for a rainy day.

We've had 37 straight years of a dividend increase. I don't think that track record is going to come to an end any time soon. We believe that our highest ROIC comes from funding organic growth opportunities. I think we'd all agree that that's a fundamental philosophy most companies embrace. That's where you're going to get your best and highest returns.

Ultimately, looking for ways to take your high-growth platforms, and, as I mentioned, creating bolt-on acquisition opportunities that can be incrementally accretive are important. Then making sure you've got some type of repetitive share repurchase program that returns cash to shareowners, and keeps management somewhat constrained about the available cash that they have, so they can be disciplined on utilizing it.

Here is what the capital allocation looks like. Today, we sit at about $2.2 billion of net debt, which is about 2.0 times EBITDA. We're expected to generate cash flows at 100% of net income of roughly $2.4 billion. I acknowledge the fact that this does not take into account that there is an amortization piece, which should also be cash, and that there is also a working capital opportunity that should also create incremental value.

But just taking net income, we believe we are at $2.4 billion between '13, '14, and '15. We have expected dividends to pay of just over $600 million in that time frame. The remaining authorized amount of our share buyback, $900 million, would put us at about one-time leverage, which I think we'd all agree is probably not an optimal position to be in to create incremental value.

The $5.00 for EPS -- and I'll take you through it in a minute -- assumes that we would not put any of this capital back to work. So the ability to put this capital back to work, either in the form of an incremental share buyback or in putting acquisitions into our high-growth platforms, will allow us to create incremental value. We believe that we've got to be disciplined about doing that. We think we're in a position through the cash generation over the next three years to create incremental value for you.

So we look at the value creation slide on the EPS, we looked at 2012 being around $2.73. Those were just legacy Pentair earnings. Through all the gyrations of tax rates, share and equity offerings, and debt refinancing, we ended the year around $2.52 on a pro forma basis. And that's a normalized number, looking at the Company on an apples-to-apples basis and a number that we'd like to suggest that we reference as we go forward. We're not looking at 100-and-some-percent growth rates in any particular quarter, but we're focusing on how we're doing against these specific global business units that we're in.

We believe $1.00 is going to come from the base performance. That's about 10% growth per year in operating income, and about 70 to 80 basis points of margin expansion. I want to reiterate that that would be, by any standard, lower expected performance on either company, as it performed over the last several years, even with some of the tougher markets that we faced.

The synergies that we laid out, the $235 million created $0.80 of incremental value. Then the share buyback and moving the tax rate to 23% from what was just above 25% creates an incremental $0.68. That's our path to the $5.00. That does not yet include utilizing the capital that I mentioned being generated on the previous slide.

So, Q2 outlook, nothing has changed. There's no updates from when we gave our Q1 earnings call. We're looking at about $1.9 billion in revenue. We're looking at sales being up 3% to 4%, seeing a nice contribution from the Residential and Commercial side. Beginning to see some meaningful EPS accretion, both coming from the synergy contributions and also getting the share count back in line, and continuing to work on the tax rate.

Q2 is seasonally our strongest quarter, so it is a quarter that we expect to learn a lot about how the year is going to come out. We feel good about where we are, about obtaining the synergies, and how those synergies are going to read out for the rest of the year. And generally, we'll have a good market update at the end of Q2 earnings to discuss both how Q2 came out and how that impacts Q3 and Q4.

For the full year, again, no updates. We're confirming everything that we said earlier. You can see that we expect $3.10 to $3.30 as the full-year EPS. That's consistent, as I said, with multiple guidance discussions. We believe that's about 4% organic growth. You can see we're assuming about 160 basis points of margin expansion year-over-year, which is half created from the core and half created from the standardization.

In summary, we believe we have a new exciting company that is more balanced, more global, more diversified. Quite frankly, we're on the journey to be the next great industrial company and we feel good about what we're doing. Right now, we're spending most of our time training all the new employees in our organization to understand what Pentair Integrated Management System is; making sure they grasp all of the elements of the Lean enterprise and the tools that we offer; that they understand what a win-right culture means -- about making sure that we win every day, and we do it in the right way. That's meaningful and important to us. Making sure that we are creating and building one Pentair; not a series of subdivided cultures that compete against each other, but a Pentair that can be more powerful because we are collaborating with each other. We're solving things together, especially in the fast growth regions. We're known for servicing our company -- our customers well.

With that, I'd be happy to take any questions that you guys have. Again, thank you for your time and attention. For those on your phone, also thank you for listening.

Yes?

QUESTIONS AND ANSWERS

Unidentified Audience Member

(inaudible -- microphone inaccessible)?

John Stauch - *Pentair Ltd. - EVP and CFO*

Sure. The question is, what is the impact -- and just for those on the phone -- of the housing starts number on the organic growth? I think the way that -- we have about $1.2 billion of North American residential revenue today, where about 85% of that's probably serving the aftermarket or the installed base. And so the remaining piece of that, obviously, would be the new housing starts. And I can't calculate in my head really quickly here, but you probably get the rest of it about what that contribution should be.

The single housing starts matter the most to us. And we're going to get the benefit on the new housing starts in three different segments. Our Residential Flow business, which is probably $300 million to $400 million, is going to see the impact primarily when the subdivision is created in a rural area, because we do well pumps there, and a lot of the equipment related to getting that water and that water pressure to your house appropriately. It's mostly an off-grid type of application or where the grid isn't adequate.

We're going to experience in the pool business in the form of -- can't tell you this is a perfect model, but pool permits are about 10% of housing starts; it's ranged from 9% to 11% over the last 10 years, primarily because of where those houses are built. That's going to go in right before occupancy. Those are usually built along with the house.

The pool business is about $500 million related to North American Residential. The rest of the revenue is related to the Water Purification side, which usually happens after occupancy when you've tasted your water and realize you need some type of solution. It's usually when you call somebody and they come fix it. We've probably have a 45% chance that that's our equipment in that market. That's how it's going to play out.

I think the only other adjacency I would add is, we have a food service business also in our Filtration and Process, which goes along with the Residential and Commercial build. As houses go in, there's more restaurants usually put in. Those restaurants all use a food services grade water purification capability, as they're required to. That's usually a pretty good bump for us as well when Residential moves forward.

Yes?

Unidentified Audience Member

(inaudible -- microphone inaccessible)?

John Stauch - *Pentair Ltd. - EVP and CFO*

Sure. So the question is, where do the revenue synergies come from? And how is that tracking against expectations? The first thing I'll address is, this is obviously going to be the squishiest part of the calculation, right? Because as you measure things from start to end, the way it works is, we have a nice point to point -- we call it a Schedule 10, not that that's relevant, but just to let you know there's a Schedule name to it, standard work.

You start with your P&L on the left-hand side of where it was last year and kind of where it gets to on the right, and then you explain the variances along the way. For most of these elements like inflation, sometimes you see inflation go up and productivity gets better, and it's no surprise there. But it all has to end in the end spot.

On the revenue calculation, I think the best synergy we're going to have is taking our 33 different platforms that we have across these seven GBUs, and prioritizing them more effectively, so we're investing and spending time with the highest growth opportunities. Our organic growth rate against the peer group is the real measure of how we're doing in the revenue synergies.

The specific examples of how we're driving that are, there's a really nice Energy offering and a Valves & Controls sales force that both sells aftermarket and service, and also original equipment. We have a filtration capability in oil and gas, which we have maybe 8 to 10 global sales people. We are now given access to over 100 globally to sell that product. We have a very high hit rate. It's an application that we believe we're going to get more wins on. That's a synergy.

Both companies had a valve platform for Food and Beverage. Now we can bring a full suite of valves to serve the entire cold block, both for large beverages, for Pepsi and Coca-Cola, but also all the beer manufacturers around the world. We can offer that suite of products together. We've had real synergies coming at $5 million a clip from those wins, on being able to cross-sell and cross-reference those products. We're also making sure that everyone in the panel skids that we build for our oil and gas and Thermal Management businesses include our Hoffman enclosures as an offering, and making sure we're pulling those through.

What we' have on the prospecting site is making sure that we're putting all of the sales offices in the six fast growth regions together, where all the salespeople are sitting in the same buildings or at least running into each other, so that they can share the opportunities that they're working on. We're building collateral that mirrors the five vertical markets I took you through. We're going after Food and Beverage with all of our offerings, and selling Food and Beverage, and making sure we're pulling both companies products and services through.

Finally, probably the biggest one and the one that's longer on the horizon is the service element. We didn't have a service offering at Pentair that was anywhere near what the Flow Control assets brought with them. There's 86 service centers. There's over $1.5 billion of service revenue coming from the Flow Control side. All of that is dealt with through different sales and distribution centers in which we can put standard work and Lean to. We're alpha testing those. We can certainly improve the customer experience, but we can also make sure that we're enhancing those services that both sides offer.

The last one that we're working on that we're also believing is going to be a very, very bright future is our controls platform. Each company independently was working on controls. That could be anything from controls for actuation and valves, to controls and service capability for engineering and design -- which Thermal did; or controls for water quality management, which legacy Pentair had. We service and manage our pools through an iPad app, which is really simple to use. We're finding in fountains and, certainly, in commercial pool equipment, that the maintenance engineers find that to be really suitable.

It's making sure we've got all those things elevated to senior management. We have over 33 synergy ideas we're working on. We're tracking them. What we're really trying to encourage people on is part of our Rapid Growth Process. It's okay to fail, if we fail fast and we learn from our failures. And so the process of coming together and collaborating and identifying what the root cause is, and then making sure under Lean principles that we have root cause countermeasures to address what we can do better -- that's what's really important to us.

I think that's going to, as I mentioned, ultimately lead to higher organic growth, and that's the real management here. A couple that have surfaced is, do we have the right cross-incentive selling plans? Are we incentivizing two salespeople to pull each other's products through? The short answer is we're not, and we're working on a way to do it. But without that, you can't expect human nature, someone to go sell something if there's really nothing in it for them, and just bad news if that doesn't serve the customer in a way that we wanted to serve.

Does that answer your question? Yes?

Unidentified Audience Member

(inaudible -- microphone inaccessible)?

John Stauch - *Pentair Ltd. - EVP and CFO*

(laughter) You know, this is the way -- and the question is, are we seeing any signs of life in the EU Industrial? I'm probably the worst person to ask this, because we've been following what's been going on in Europe, as everybody has, I'd say for at least 24 to 36 months. Just when we see a business start to turn up, we'll see another one turn down. We don't have a consistent pattern to report out to you, without giving the specific examples.

We had a business that was growing double-digits through Q4 of last year in 2012 that turned into down double digits in Q1. At the same time, we had a business that was contracting at 15% in Europe through last year, and clipped away a 12% growth in Q1. We're in a microeconomics view here, not macroeconomics. It depends on the markets you're serving, what you're doing, and kind of how that's affected. Overall, Europe is down around 5% for us this year. I see no indications that it's worse or better than that. It is getting better, or feels like it's getting slightly better sequentially. But as I said, just when something turns positive, we'll see something turn negative.

The other market that we probably weren't as optimistic as most, was China. I don't think we're seeing China become really robust. We're seeing the same data that you are, but we are also questioning why is that not more of a pull for commodities? Why are we not seeing more commodity inflation if that's true? Why are we not seeing bigger increases in mining demand? Our eyes and ears are open there. Not a significant contribution to revenue or income for us, but at the same time, we'd like to see growth fundamentally there.

Yes?

Unidentified Audience Member

(inaudible -- microphone inaccessible)?

John Stauch - *Pentair Ltd. - EVP and CFO*

Yes. So the question is, is there anything in the market that concerns us on midstream and upstream specifically related to Valves & Controls, based upon some of the distributor reaction?

Short answer is no. However, I would say the oil and gas space continues to be our most choppy market within Valves & Controls. We're seeing off again/on again orders. There hasn't been a lot of big orders. In Valves & Controls, a big order would be anything greater than $5 million, honestly, and there's not usually a lot of those.

We are seeing more of our growth outside of the United States than we thought we would in the beginning of the year. But we are still seeing relatively decent contributions. But it's choppy. As a CFO, I'd certainly like to see more predictable consistent patterns. I know the business leaders would prefer to see it that way as well.

Both the good news and the bad news of our Valves & Controls $2.5 billion offering is they're fairly diverse. 35% of our revenue is going to be exposed to Energy. Oil and gas will be a subset of that. We're going to have a chunk of our revenue related to Industrial, and then we have a small related to mining. And mining has turned negative. Power has turned positive. Industrial process generally trending positive, and oil and gas flat to up.

I'm looking at these things sequentially, because I think we feel the best about the last nine months of data as the business provided to us. We've looked at that, we scrubbed it, we understand the margin in backlog. And we're watching it as closely as possible without looking at it too closely, to create undue angst that detracts the business from what it needs to do, which is go win more orders.

Yes?

Unidentified Audience Member

(inaudible -- microphone inaccessible)?

John Stauch - *Pentair Ltd. - EVP and CFO*

Yes. The question is around leverage, and how do we think about it in 2015 and making sure that we maintain it? You know, Randy and I are partnered on a fairly simple business model, which says that each of these businesses are treated like a sibling. They're all kind of different and all important. We obviously love some more some days than others, just like I'm sure parents think of their children -- at least I do.

One of the things that we're very careful about is to make sure we don't have peanut butter targets. Each of these businesses have unique applications and opportunities. In a couple of businesses, we want to accelerate R&D to make sure we've got the most innovative product out there. Other businesses, we probably want to prioritize and ratchet back a little bit.

We have a standard model that we want to drive at Pentair that would say, today, our operating expenses, which are the cost below gross margin, are somewhere around 22.5% of sales. Long-term, it's probably more realistically at 20%. By 2015, it gets close to about 21.5%. We're not talking about taking a lot of cost out here. At the same time, we believe the efforts around Lean and direct material sourcing should help the conversion.

As you move to more of a service orientation, and we branch out and make sure we serve our customer more effectively in the aftermarket channel, that should have higher leverage. The leverage or the incremental dropthroughs here should be accelerating, in our opinion, and not de-accelerating. They're all going to be different, but we're not looking at incrementals here that should be challenged, as we drive these synergies over the horizon.

We're not done after 2015, obviously. Our stated targets between 2015 and '16 and '17 are equally important. There's more leverage to get in '16 and '17. What we haven't done as a company is talked about factory rationalization at all. We haven't done that for two reasons. One, we want to make sure that we've got Lean standard work in every factory, so we know what we're talking about. And our ultimate goal would be to free up capacity and tuck acquisitions in. That should ultimately get us more leverage as well.

Simply put, we've been waiting forever for Residential. Residential is coming and we're going to see great returns in Residential. We'd expect that same type of success in Valves & Controls and Thermal as they continue to grow as well.

Unidentified Audience Member

(inaudible -- microphone inaccessible)?

John Stauch - *Pentair Ltd. - EVP and CFO*

Oh, balance sheet leverage, yes, I'm sorry. (laughter) Boy, you should have stopped me halfway through that question.

You know, where I'm comfortable with, and I tell the rating agency, is 2.5 times EBITDA, the way the rating agency score is kind of a sweet spot. The reason we say that is, I think that gives you enough protection if something were to happen, that you would still stay investment-grade, and be able to work your way through that dynamic. At the same time, you don't want to be underleveraged, especially at this type of borrowing rates, in a way that you're not returning to shareowners the return on the capital they expect.

You're not going to do dumb things either way to artificially hold that at that level, but I think that's kind of our target lever for Pentair, is right at 2.5 times EBITDA. As we start talking about one times, that would be silly to be at one times.

Unidentified Audience Member

(inaudible -- microphone inaccessible)?

John Stauch - *Pentair Ltd. - EVP and CFO*

Should be, yes. Okay? Any more questions? Well, I thank you for your time. I thank you for your interest in Pentair, and I look forward to spending more time with you in the future. Please maintain your applause. Thank you.