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PNR - Q1 2014 Pentair Ltd. Earnings Conference Call

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OVERVIEW:

PNR reported that 1Q14 reported sales decline was 3%. Expects 2014 sales to be approx. $7.7b and EPS to be $3.85-4.00. Expects 2Q14 sales to be approx. $1.95b and EPS to be $1.02-1.05.

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PRESENTATION

Operator

Good morning. My name is Kyle and I will be your conference operator today. At this time, I'd like to welcome everyone to the Pentair Q1 2014 earnings conference call. (Operator Instructions).

Mr. Lucas, you may begin your conference.

Jim Lucas - *Pentair, Inc. - VP IR*

Thanks, and welcome to Pentair's first-quarter 2014 earnings conference call. We are glad you could join us. I am Jim Lucas, Vice President of Investor Relations, and with me today is Randy Hogan, our Chairman and Chief Executive Officer, and John Stauch, our Chief Financial Officer.

On today's call, we will provide details on our first-quarter 2014 performance, as well as our second-quarter and full-year 2014 outlook, as outlined in this morning's release.

Before we begin, let me remind you that any statements made about the Company's anticipated financial results are forward-looking statements subject to future risks and uncertainties, such as the risks outlined in Pentair's most recent 10-K and today's release. Forward-looking statements included herein are made as of today and the Company undertakes no obligation to update publicly such statements to reflect subsequent events or circumstances. Actual results could differ materially from anticipated results.

Today's webcast is accompanied by a presentation, which can be found in the investors section of Pentair's website. We will reference these slides throughout our prepared remarks. All references today will be on an adjusted basis, unless otherwise indicated, for which the non-GAAP financials are reconciled in the appendix of the presentation.

We will be sure to reserve time for questions and answers after our prepared remarks. We will target to be done in an hour. I would like to request that you limit your questions to one and a follow-up and get back in the queue for further questions, so that everyone has an opportunity to ask their questions.

I will now turn the call over to Randy.

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

Thanks, Jim. Good morning, everyone. Let me begin with our first-quarter performance on slide 4.

Before I go through the results in detail, as has been our practice since the flow control merger, I want to note that we are discussing our operating results on an adjusted basis to more clearly show the core operating performance of our businesses. With that, here are the first-quarter numbers.

First-quarter revenue grew 1% on a core basis, but showed down 3% on a reported basis, which we will explain in more detail in a moment. Adjusted operating income was up 14% and adjusted operating margin expanded 170 basis points to 11.8%. Adjusted EPS grew 26%, coming in at the high end of our expected range at $0.73.

Free cash flow was a small usage, which is normal in our first quarter. This reflects a seasonal working capital build in many of our residential businesses and, in this year's first quarter, the fact that a larger-than-average portion of revenue was generated in March, due to the slow January and February. We believe we are on track to deliver full-year free cash flow greater than 105% of net income.

During the quarter, we completed our original $1.2 billion share repurchase authorization and are now into our next $1 billion repurchase authorization.

Now let's turn to slide 5 for a more detailed look at the first-quarter results. As I stated previously, our reported sales declined 3%. The waterfall on the left-hand side of the page shows that we experienced 2 points of foreign-exchange headwind, principally the Australian dollar and the Canadian dollar, a 1-point headwind from divestitures, and another 1 point of headwind from the nonrepeating Glebe Weir project in our water transport business in Australia. We will provide more detail on this business when discussing our Flow Technologies segment.

We do not believe we were alone in seeing a slow start to the year, with weaker revenue in January and February, but the majority of our businesses experienced nice revenue acceleration in March, and early April has seen many of those trends continue.

The right half of the page shows first-quarter Pentair operating profits and margins. Operating margin expansion of 170 basis points was helped in large part by strong productivity, which includes synergies. As we've discussed in the past, in order to deliver on our targeted margin expansion of 150 basis points per year, we need to deliver on both base productivity and synergies, so we track them together.

We continued to gain momentum on both Lean and sourcing initiatives and we have identified 18 focus factories that we expect to drive additional margin gains in 2014. As we've experienced additional topline challenges, we took further repositioning actions in the first quarter to accelerate our productivity results.

Overall, while we were not satisfied with our topline performance in the first quarter, we continue to deliver on productivity and synergies and see strengthening of the topline as we enter the seasonally strong period for our Residential & Commercial businesses. Our backlog gives us further confidence in our expectation for an accelerated topline growth rate in the second half of the year, as well.

Now let's turn to slide 6 for a performance review of our largest segment, Valves and Controls. Valves and Controls' organic sales declined 7%, which follows strong double-digit growth in the fourth quarter of 2013. This segment has shown a great deal of variability quarter to quarter. We will continue to seek improvements in our forecast for the topline.

One of the ways we are doing that is by looking at longer periods for comparisons and evaluations. For instance, if we combine the fourth quarter of 2013 and the first quarter of 2014 and compare that six-month period to its prior year comparable, sales show growth of 5% year over year, as compared to the 19% gain in the fourth quarter of 2013 and the 7% decline in the first quarter this year.

A fair amount of the quarter-to-quarter swing relates to the timing of large project shipments, and we also experienced a fair amount of variability in our shorter-cycle business. All four industries served by Valves and Controls posted a decline, with sharp drops in Power and Mining. The declines in Oil & Gas were principally related to the timing of large project shipments, while the Power decline came from weaker nuclear demand. We did see some softness early in the quarter on our overall short-cycle business, but server showed solid growth in the quarter.

The right half of the page shows fourth-quarter Valves and Controls operating profits and margins. Adjusted operating margins expanded 140 basis points to 11.5%, which included $5 million in costs for the GBU's Operating Model Transformation, or OMT.

As a reminder, we expect the OMT investments in Valves and Controls to continue on an annual basis through 2016. But that investment is expected to drive nearly $80 million of annual operating income savings once completed and an overall tax benefit to Pentair of roughly 3 points through the optimization of the global Valves and Controls structure in Switzerland.

Now let's turn to slide 7 for a look at the orders and backlog for Valves and Controls. As you can see on slide 7, the Valves and Controls backlog is broken down in four key industries, three of which fall into our Energy vertical -- Oil & Gas, Power, and Mining -- and one in our Industrial vertical, which is Process.

Overall backlog remained near $1.4 billion, which is relatively consistent with where it has been since we acquired the business near the end of 2012. Orders were relatively flat in Process, Oil & Gas, and Mining, but Power showed a sharp decline in orders.

We have experienced a fair amount of quarter-to-quarter variability in sales and orders in Oil & Gas, but we still see healthy quoting activity. Industrial Process is still expected to benefit from increased capital spending related to anticipated growth in North American chemical capacity. We anticipate this will be more of a second half and 2015 benefit for our Valves and Controls business.

Power remains a wildcard, but the backlog remains relatively consistent, and despite the quarter-to-quarter volatility in orders, we expect shipments to pick up later in the year. We remain very cautious on Mining, but this is the smallest portion of Valves and Controls.

Now let's move to slide 8 for a review of Process Technologies. We indicated on our fourth-quarter earnings call that we would begin to report in four segments, as our previous Water and Fluid Solutions segment was split into Process Technologies and Flow Technologies. As a reminder, Process Technologies comprises our Filtration & Process and Aquatic Systems GBUs.

Process Technologies reported good topline growth of 5%, which included a 1-point FX translation headwind. Both the Residential & Commercial and Food & Beverage verticals grew at a double-digit rate, building on the momentum we saw in this business last year.

The right half of the page shows first-quarter Process Technologies operating profits and margins. Operating margins expanded a disappointingly modest 10 basis points to 11.7% as a result of two principal factors during the quarter. First, we saw strong shipments of larger system sales in our beverage business, which, as we indicated last quarter, has a dilutive impact on the overall segment results as these systems carry lower margins on initial installs. But they are important to building a growing installed base to drive higher-margin replacement sales in the future.

Second, our residential filtration business experienced a slow January that resulted in poorer operating leverage than normal that month, followed by a strong increase in demand in March that led to overtime and some expedited freight. We expect more normalized sales trends and greater operating margin expansion in the seasonally strong second quarter.

Now let's move to slide 9 for a look at Flow Technologies. This is the first quarter that we have reported our Flow Technologies segment, which, as a reminder, is a combination of the legacy Pentair Flow Technologies business and the Australian water business that was part of legacy flow control.

As expected, we saw a sharp decline in Flow Technologies, with sales down 7% on a reported basis. There were two main causes of this decline. We saw a 4-point headwind from the Australian dollar and another 4-point headwind from the nonrepeating Glebe Weir project in 2013. We will discuss the impact of the Australian water transport business further on the next slide.

The legacy Flow Technologies businesses actually saw modest growth in the quarter. The right half of the page shows first-quarter Flow Technologies operating profits and margins. Operating margins expanded 50 basis points to 9.9% as the impact of no project activity in Australia and the tough comp it created was nearly a full point of margin headwind in the quarter. We continue to aggressively right-size the cost structure of the Australia water transport business to reflect the reality of a much different looking business today than was expected over a year ago.

We continue to see strong productivity in the other parts of Flow Technologies, and the repositioning benefits are helping to partially offset the sharp declines experienced in water transport.

Let's now turn to slide 10 for additional color on our water transport business. Given the dramatic decline in water transport, we thought it would be helpful to explain how much of an impact the decline in the Australian economy has had on this business. When the mining industry was strong in 2012 and there were a number of large projects in Australia, this business generated over $550 million of revenue. This is about the average revenue over the five-year period -- five years prior to 2012, with the peak around $750 million in 2010.

At the time of the flow control acquisition, based on projects booked and being bid, this business was anticipated to generate over $800 million in 2015. We knew, based on the backlog and the debooking of two large projects shortly after the acquisition, that we were facing a decline in 2013, but this business has faced a significant lack of projects that has led to further declines in 2014 to historically low levels.

We have been aggressively going after restructuring in this business, but there is a fixed-cost element that on these lower sales is creating earning headwinds in 2014. As shown on this slide, the second quarter is the last expected large headwind, and this is likely to lower our overall EPS in the quarter by $0.08.

It is not realistic to expect this business to rebound anytime soon, as demand from China on the mining industry remains low and municipal investments just aren't happening. We have taken significant costs out of this business and the tough year-over-year comps diminish in the second half of the year.

A decline in Australia of this magnitude was not foreseen, but in no way does it lead us to back off of our commitment of $5 of EPS in 2015. We've stepped up the restructuring activities and driving upside performance in other businesses, and we continue to drive productivity and synergies across all of Pentair to help offset this lingering headwind. We will keep you posted on our progress.

Let's now turn to slide 11 for a look at Technical Solutions' results. Technical Solutions' sales group 1% in the quarter, where price and volume contributed 3 points of growth, offset by a 1-point headwind from FX and another 1 point from divestitures.

As a reminder, we sold our Aspen specialty motors business in the first quarter last year, so this divestiture comparison goes away in the second quarter.

This is the second consecutive quarter of growth that technical solutions has delivered, following declines in the first nine months of 2013. We saw growth in the Industrial, Residential & Commercial, and Infrastructure verticals, while Energy declined in the quarter.

After a slow start to the year, we saw daily orders rates in our electrical business accelerate in March, and this trend has continued into early April. The cold weather in the US did have some benefits for our Thermal business, but Europe experienced unseasonably warm weather and we saw weakness in Canada offsetting that. At the same time, our electronics business has benefited from improving demand and new products.

The right half of the page shows first-quarter Technical Solutions operating profits and margins. Margins were a great story yet again as adjusted operating margins expanded 210 basis points to 19.1%, with strong productivity, synergies, and operating leverage all on display during the quarter.

While Thermal is entering its seasonally slowest quarter, our Equipment Protection and electronics businesses are seeing improved momentum entering the second quarter.

Let's now turn to slide 12 for a closer look at the total Pentair growth profile. The first quarter saw solid performance in the US and Western Europe, weakness in Canada and Australia, and mixed signals in fast-growth regions. In the US, we continue to see strength in Residential & Commercial. In Western Europe, we saw a modest recovery. In the fast-growth regions, the Middle East declined due to timing of one large project, but we still expect strong growth for the full year. Southeast Asia remains mixed and we continue to see growth in China and Latin America.

Our Residential & Commercial and Food & Beverage verticals remained the bright spot. We still expect growth in all of our verticals except Infrastructure, which is weighted down by the weakness in Australia.

Energy continued its trends of lumpiness with a first-quarter decline, following a 15% gain in the fourth quarter of 2013. The first-quarter weakness was principally related to the power declines in Valves and Controls, as we discussed earlier. We continue to see strength in our Oil & Gas quoting activity, so we expect to see low single-digit growth in Energy for the year.

Industrial is down modestly in the quarter, but the improvement in our electrical daily orders rate and the continued strong quoting around the anticipated North American chemical manufacturing renaissance gives us increased confidence that Industrial will grow at a modest pace for the full year.

We are entering the seasonally strongest period for our North American Residential businesses, which follows another strong mid-single-digit growth quarter for this vertical. We also saw improvements in both the European and China Residential markets and our businesses exposed to Commercial construction are also seeing signs of improvement.

Infrastructure remains the weakest vertical, but again, this is due exclusively to Australia. Our North American break and fix business remains steady. We have seen a bottoming in desalination, and datacom, telecom, and electronics has bounced off the bottom, as evidenced by its second consecutive quarter of strong growth.

Food & Beverage is expected to see solid mid-single-digit growth this year, which follows strong double-digit growth last year. We expect continued slowness in our US agriculture-related businesses, both irrigation pump and crop spray OEM, but the aftermarket piece of crop spray remains solid. Our food service business continues to experience strong international growth and beverage systems continues to have a healthy backlog.

Please turn to slide 13, labeled Q1 assessment and full-year outlook. Before turning the call over to John to review our outlook for the second quarter and full-year 2014, I wanted to offer a summary of why we remain optimistic that we are on track to deliver on our full-year commitment.

Our topline came in a little lower than we anticipated, but this was due in large part to a slow January and February after robust growth experienced in the fourth quarter of 2013 to end the year. We saw strengthening in many of our businesses in March and that has continued into early April.

We will still have the Australian water transport headwind in the second quarter, but we expect this will be partially offset by the seasonal strength of our North American Residential businesses.

As we look out to the second half, we are seeing signs of increased capital spending by Industrial customers and we are building backlog in our Valves and Controls business. We continue to drive our productivity and synergies and have put additional action plans in place to drive even more productivity gains. And our OMT investment in Valves and Controls is on track.

Of course, we are committed to and investing in growth, which we expect to start reflecting in our results in the second half of 2014. In addition, our balance sheet remains in great shape and we are on track for another record year of free cash flow.

Our businesses that have earned the right to grow are building their acquisition pipelines. We continue to focus on the elements where we can control our own destiny, and while we still have to earn the right to talk about growth, we believe the second quarter will represent our last difficult year-over-year comparison, and of course, we have opportunities to drive further margin expansion into 2015 and beyond.

With that, I will turn the call over to John.

John Stauch - *Pentair, Inc. - EVP, CFO*

Thank you, Randy. Please turn to slide number 14, titled Q2 2014 Pentair outlook.

For the second quarter of 2014, we expect sales to be flat to down about 1% at approximately $1.95 billion. Valves and Controls is expected to be flat due to timing of current backlog and an expected ramp of short-cycle orders. Process Technologies is anticipated to be up 6% to 8% in its seasonally strongest quarter.

Flow Technologies is expected to be down approximately 20% due to the last tough comparison in our water transport business that Randy discussed in detail earlier on the call. Excluding this project, sales should be up approximately 3%. Finally, Technical Solutions is expected to be up 4% to 6%, led by our Equipment Protection and electronics businesses.

We're expecting adjusted operating income up 6% and adjusted operating margins to expand approximately 100 basis points to 14.7%. This includes about $7 million more of OMT investment in Valves and Controls and the impact of the Australian headwinds mentioned earlier. Excluding these, operating income would be up approximately 16% versus Q2 of last year.

Our EPS forecast for the second quarter is a range of $1.02 to $1.05, or an increase of roughly 13%.

Please turn to slide number 15, titled balance sheet and cash flow. Quarter-end debt was approximately $2.9 billion, or $2.7 billion on a net debt basis inclusive of global cash on hand.

In the first quarter, we returned to $300 million to shareholders in the form of dividends and share repurchases. At the end of the first quarter, we have now completed our initial $1.2 billion share repurchase authorization and have just under $900 million remaining under our current $1 billion authorization.

We are seeking authorization from our shareholders at our May annual general meeting to increase our dividend to $0.30 per share for quarter from $0.25 per share for quarter, which, if approved, will mark our 38th consecutive year of annual dividend increases.

Our ROIC ended the quarter at 10%. We continue to have a lot of opportunities on the working capital front with legacy flow control businesses and we expect to make further progress as the year continues.

Please turn to slide number 16, labeled full-year 2014 Pentair outlook. We are reiterating our full-year EPS guidance of $3.85 to $4 on approximately $7.7 billion in sales. We have moderated our growth rate by 1 point to a range of 2% to 4%, reflecting the impact of FX and the slower start in January.

Valves and Controls is now expected to grow 1% to 3% as backlogs remain strong and we continue to focus more on the short-cycle businesses. Process Technologies is expected to grow 8% to 10% with continued strength in Aquatics, beverage systems, foodservice, and an improving Residential & Commercial filtration business.

Flow Technologies is anticipated to be down 5% to 7%, related to the lack of project activity in Australia, the tough comps we discussed earlier, and FX. Excluding the water transport business, we expect Flow Technologies to grow approximately 4% to 5%.

Technical Solutions is expected to grow 4% to 6% as we see signs of business improving in the North American electrical distribution channel, strength in our electronics business, and easier comps for our Thermal business. We do not expect any megaproject activity in 2014, but as we have stated in the past, we will update accordingly at the appropriate time if any megaprojects enter the backlog.

Adjusted operating income is expected to expand to approximately $1.1 billion, which would represent a record for Pentair. We expect three of the four segments to expand operating margins in excess of 100 basis points, with only Flow Technologies not achieving that level as we continue to aggressively right-size the cost structure with the dramatically reduced demand environment in our water transport business.

Overall corporate costs are expected to be down, due to lower corporate integration costs. For the full year, we expect the tax rate to be around 23.5%, net interest expense to approximate $70 million, and the share count to be around 198.5 million. We expect EPS to expand around 22% to $3.93, at the midpoint of the guidance range. We are expecting another record year of free cash flow with at least $850 million, or greater than 105% of net income.

Kyle, can you please open the line for questions? Thank you.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Mike Halloran, Robert Baird.

Mike Halloran - *Robert W. Baird & Company, Inc. - Analyst*

Let's start on the revenue guidance. It sounds like the two main pressure points, a little bit of Canada FX and maybe some volumes there, but the predominant part is the Australia side. Maybe you could just go into a little bit more detail, and by the way, great color on slide 10 there on the year over year and some more water transport information. But maybe you could just talk about what you are seeing on the short-cycle everyday business over there, as well as what the outlook on the project activity looks like, and if there are even any projects embedded in the guidance as you look forward in that specific piece today?

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

Randy here. That business, the volume we get are really all small projects, maintenance. There is always some of that. That business has always had one or two larger projects, at least one or two, and then they would get some big ones on top of that.

This year is unprecedented in that it has none of those bigger projects, and we don't have any bigger projects coming in the forecast. That's what's different. We thought we would get a couple of those. But they went away.

Mike Halloran - *Robert W. Baird & Company, Inc. - Analyst*

Is the regular way, then -- on the regular way side, how is that business? Is that a little bit worse than expected as well right now?

John Stauch - *Pentair, Inc. - EVP, CFO*

No, that's clipping along at roughly flat or modestly up. That's, as Randy mentioned, primarily break and fix or re-establishing, fixing things that are already installed. That business has always been relatively steady.

But it's the project business, and usually at this particular point in time, we've always got two or three or we at least have meaningful ones in the front log. We're not even seeing front-log activity in Australia related to these projects.

Mike Halloran - *Robert W. Baird & Company, Inc. - Analyst*

That makes sense. And then the follow-up question, if I take out the Australia and some of the Canada pieces and things like that, it looks like the core businesses outside of that are tracking consistent, if not ahead, of your expectations on a full-year basis. You obviously have commented on some improving trends as you look through March and April here, but what gives you the confidence on the Energy side that you're going to see some improvement as you work through the year there?

And then, also, maybe just a little bit more color about some of the end markets you are starting to see improve a little bit.

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

We are getting better at seeing the businesses in our current configuration, as we look out, and we are looking at our bidding activity. In Energy, bidding activity remains strong.

The Power surprised. Nuclear valves is a nice business. And that was surprising to see the short cycle in that. So short cycle, which is repair and maintenance, was actually weaker in the nuclear business than we would have anticipated. That was really the only surprise in our Energy. But the variability quarter to quarter is not that big a surprise, because that's what we have been seeing.

So we feel good about Energy because of the bidding activity. And that's consistent across all of the GBUs that serve energy.

John Stauch - *Pentair, Inc. - EVP, CFO*

The only thing I would add to it, Michael, is I am sure like a lot of the other companies you follow, our January and February, slow start. March was very strong. And we have anticipated or put in the normalized view of what we think the year is going to be, so we're obviously monitoring April, and is April tracking more like March and how comfortable do we feel? We will have a better picture of that, obviously, as we close out Q2.

Mike Halloran - *Robert W. Baird & Company, Inc. - Analyst*

Great. Thanks, guys.

Operator

Deane Dray, Citi Research.

Deane Dray - *Citigroup - Analyst*

Can I start with a question for John? It looked like corporate expense came in lighter than what we were looking for, and right at the end of your prepared remarks, you commented that corporate is coming down with lower integration costs. But maybe, just what were the dynamics this quarter on the corporate line that might have made it more favorable?

John Stauch - *Pentair, Inc. - EVP, CFO*

Yes, so we are looking at around $23 million to $25 million this year, probably closer to $23 million each and every quarter. So we're about $1 million under that. We're going to have variability in things like stock comp timing, medical timing, and litigation. That's about the only variability we would have.

So, it wasn't a big delta. The year-over-year is the integration costs. We were obviously very heavy into the corporate integration last year, and you see that number reflected in close -- or over $30 million of expenses. That came down throughout last year.

So most of our integration activities now are all in the businesses. So we mentioned OMT; that is being absorbed in the Valves and Controls business, and most of all our Lean activities and costs that are being borne to drive the synergies are all being managed by the businesses now.

Deane Dray - *Citigroup - Analyst*

Great, and then on Process Tech, the margin hit or just the margin pressure because of the mix, maybe you could just expand on that. When you ship these larger systems, is that also because you have content that is not Pentair content and that's more of a pass through? If you could just give us some context and color regarding those kinds of shipments and what that outlook embedded is for the balance of the year.

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

It's both a lower margin, because the systems are direct to the OEMs. They are part of larger projects and they are always bid a little bit tighter. But there is also -- as we build a valve skid or we build a coal block, there is a lot more purchase pass through parts, so that's part of it, too.

John Stauch - *Pentair, Inc. - EVP, CFO*

As you know, we are doing it because we've got the membrane there that within 12 to 18 months, it's going to be replaced, and we will look for those aftermarket sales and that's much higher margin. So this is the razor, if you will. The razor blade is to come.

Deane Dray - *Citigroup - Analyst*

Yes, I would much rather see you shipping these systems as solutions as opposed to component pieces.

And then, just a quick clarification on the nuclear business. How much of that is an impact, and we have seen this elsewhere, from mothballed plants that just would have ordered these valves that just now are being mothballed, or is it lower utilization, lower maintenance spending?

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

It's some of both. Germany was down, but clearly Germany is moving away from nuclear, so those are being mothballed, so that's maintenance that isn't going to get done, unless for some reason they open them up.

At the same time, France has recommitted to another 50-year life extension for their whole nuclear fleet and they are going to be net exporters of electricity to all of Europe. But their maintenance was light. It was lighter than we would expect. US maintenance was lighter than we would have expected.

And then, there is project businesses in China and other countries that are there to ship and they just don't ship. But the mothballing factor is one. We believe we have that factored in. So the surprise was more on the maintenance side, the expected maintenance, and the shipping of projects on new installations in countries that are building them.

Deane Dray - *Citigroup - Analyst*

Great, thank you.

Operator

Steven Winoker, Sanford Bernstein.

Steven Winoker - *Sanford C. Bernstein & Company, Inc. - Analyst*

John, question for you. When you now think about how long you have had Valves and Controls and the difficulty in forecasting this business, when you look within your FP&A process and talent pool, what kind of changes are you putting in place so that -- I know there are big projects. I know you have gotten certain surprises, but nonetheless, there are a lot of highly diversified companies with similar dynamics who have maybe a more mature FP&A process in businesses like this. How far away from that are you, do you think, in terms of time to get there? Or do you think it's just going to be a tough business to ever get there?

John Stauch - *Pentair, Inc. - EVP, CFO*

I think we will definitely get there. We talk about blue chips being top priorities here, and believe me, this is Randy's top blue chip, which means it's my top blue chip, which means it's the business's top blue chip.

And right now, it's complicated. These acquisitions were acquired, and we basically have 40 individual businesses that really take sales at 128 different locations, and then those sales are put on the factories, and you can imagine some of these are in stock and some of these are make the stocks, some of these configure order, and some of these are larger projects, but this is all solvable.

And this is where our Lean tools really come in, and we have initiated and kicked off that project. So there is a financial element to this, but there is also a process element that goes all the way through the SIOP process. And as I mentioned, it's Randy's top priority, which means the business is all over it right now.

I can't tell you why they reach at the end of the quarter, so much like in Q4, and then you see the slowness this quarter and then the catch-up. I think that's their lack of confidence in what that shipment needs to be to manage those quarters. Randy, I don't know if you want to add anything.

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

We all have experience, Steve, in those kinds of businesses in our past life that with longer cycle, we should be more predictable. That's one of the benefits of a longer-cycle business.

But it is, as John said, it's a function of the fact that the businesses have not been integrated, and that's our big opportunity. That's what our OMT project is about. And beyond the OMT, to get a more granular understanding of the forecasts as they come in. It's not just in FP&A; it's the sales forecasting. It's an organizational capability. And we know how to do it. We're working on it.

Steven Winoker - *Sanford C. Bernstein & Company, Inc. - Analyst*

Great. And then on capital deployment, what is your willingness or desire to step up the repurchase part of the deployment over the next year or so?

John Stauch - *Pentair, Inc. - EVP, CFO*

We definitely have the ability to. I think we will, if we need to.

Right now, we would like to balance that with acquisitions, especially in the platforms that Randy mentioned. Green lights, they are growing nicely organically. They have a great standardized back office and right now there's a big willingness to have discussions around acquisition. There isn't agreement on price.

But that's what we'd like to do is balance this between share buyback and acquisition.

Steven Winoker - *Sanford C. Bernstein & Company, Inc. - Analyst*

And then, I'll just sneak one more in. Food & Beverage has been a fantastic contributor now for some time and offset a lot of weakness in other segments. As those segments start to come back, do you think Food & Beverage here has got this longer-term secular story where it's not like we're going to see that decrease as the other ones come up?

John Stauch - *Pentair, Inc. - EVP, CFO*

I don't think we can sustain 20% growth a year, but the reason we think we are more in the double digits on a long-term basis is we have solved something significant for the large beverage manufacturers, which is a way to filter their product, which has become a standard element, and so as they expand their breweries or rearrange the breweries, we're a big piece of that.

The other element that is in this Food & Beverage is not only our ag offering, but what we believe is aquaculture and aquaponics and a lot of other offerings.

So, we are focused on it. We have a lot of new product introductions there and we have a global offering which is really being well accepted.

Steven Winoker - *Sanford C. Bernstein & Company, Inc. - Analyst*

Great. Thanks, guys.

Operator

Shannon O'Callaghan, Nomura Securities.

Tony Wright - *Nomura Securities Intl. (America) - Analyst*

This is [Tony Wright] on Shannon's team. So first of all, I was just wondering -- I know you touched on this little bit, but the fast-growth markets have been rather lumpy in the recent quarters. Could you talk a little bit more about the moving parts there and maybe some detail around your outlook for these regions for the rest of the year?

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

Let me talk to them region by region. The Middle East is still on a long-term growth trend. We had a really big project that shipped last year in the Valves and Controls business in the Middle East, and that's [why] the Middle East looks weak. The secular trend, if you will, for our Middle East growth is quite good.

China has come back in Residential spending. It is nice to see that again in China. It had slowed down, and for us, that's in the water business, so we think that now that that's coming back, it should continue for us.

Latin America had suffered some setbacks from Brazil, but the rest of Latin America is lifting that.

What did I miss?

John Stauch - *Pentair, Inc. - EVP, CFO*

That's about it. I would say with Randy, any time you're going to see a Valves number like this, you're going to see its impact as being our largest fast-growth provider of product, it's going to have its general toll on the reporting, but the underlying water businesses right now in the fast-growth regions are seeing nice, sustained, consistent growth.

We have put a lot of investment and effort there, and I think I am with Randy. I think we feel like these markets continue to be better than they were last year, with the exception of Brazil. And I think we have a long-term growth rate here that I would call mid-single digits.

Tony Wright - *Nomura Securities Intl. (America) - Analyst*

Okay, great. And then just maybe on acquisitions, what are these main areas of priorities? Do you have a range in mind when you think in terms of size you'd be willing to do or is that a rolling target?

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

We look at everything. And as I said earlier, obviously the larger the integration effort, we would like that to be on something that's much more lean today and could accept a larger acquisition.

Tony Wright - *Nomura Securities Intl. (America) - Analyst*

Okay, great. Thanks, guys.

Operator

Steve Tusa, JPMorgan.

Steve Tusa - *JPMorgan Chase & Co. - Analyst*

Just to start, just a nitpicky question on the Process Technologies. You had two businesses that are -- I guess represent about 85% of the segment. Residential & Commercial, Food & Beverage, they were up 10%, 17%, respectively, but sales were only up 5%. What was down so much in that business or was there -- it doesn't look like it's Forex or anything like that. Am I missing something on the end-market dynamics?

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

It's the water purification, the business that serves desalination and just, if you will, the pure water side.

Steve Tusa - *JPMorgan Chase & Co. - Analyst*

So, how big is that business?

John Stauch - *Pentair, Inc. - EVP, CFO*

(multiple speakers). I am sorry. Steve, what was the question?

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

How big is that business?

John Stauch - *Pentair, Inc. - EVP, CFO*

A little over $160 million annually.

Steve Tusa - *JPMorgan Chase & Co. - Analyst*

Okay, so it must have been down a lot?

John Stauch - *Pentair, Inc. - EVP, CFO*

Yes, it was down around 20% in the quarter there.

And you also had some Energy -- we were slightly down in Energy, which is more of a timing issue in when those shipments will go out, which is -- and that was roughly down about 10%. That is about a $100 million a year business.

Steve Tusa - *JPMorgan Chase & Co. - Analyst*

Got you. And then on Valves and Controls, your profits were up $3 million this quarter on a pretty significant revenue decline. I think the guidance for the next quarter has a similar profit -- up profits on flattish revenues. Is there something -- is that like OMT flowing through? Or I'm just saying, is there something there that -- why wouldn't that be better? Why wouldn't the $3 million increase be better with flattish revenues?

John Stauch - *Pentair, Inc. - EVP, CFO*

I actually love your question, because we feel the same way.

So right now, there is a couple of million dollars more of OMT, and we do think that the productivity that we have seen the last several quarters, we believe that's going to continue to come through here. So we are looking for that increased Lean and sourcing savings, and I think that you are looking at whenever you are flat, I think businesses find it hard to forecast significant operating income on flattish growth.

Steve Tusa - *JPMorgan Chase & Co. - Analyst*

Right, okay, so the OMT is like -- I think it was $5 million in the first quarter. I think we thought it would be more like $7 million -- I know this is nitpicking, but what's the number for the second quarter in OMT?

John Stauch - *Pentair, Inc. - EVP, CFO*

Roughly $7 million.

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

It's $7 million (multiple speakers)

Steve Tusa - *JPMorgan Chase & Co. - Analyst*

Okay, so you get back to that run rate.

And then, just one last question on overall productivity. I know you have changed the slide somewhat, but getting to about $45 million in combined productivity and synergies for the quarter, I guess are the -- I know you're not going to maybe give us explicit guidance, but I would assume -- are the synergies on track here as far as what you had laid out on an annual basis? Are you still expecting the same amount of synergies from the deal?

John Stauch - *Pentair, Inc. - EVP, CFO*

Absolutely. I think the piece that we absolutely know about is the restructuring, and when you take a look at what we have done to date, we have taken roughly $200 million in charges, and that run rate on those savings would be north of $200 million and that's the piece that we absolutely have tangible confidence that we're going to achieve.

The piece that's a little harder to gauge is the Lean savings, how much is core, how much is synergies, especially when you need growth leverage to really benefit from both, and then also on the sourcing side, how much we would have gotten anyway.

But right now, I did the same math you did. We exited at $40 million. I think we picked up some incremental synergies on top of that, probably knocking on the door close to $45 million to $50 million from a run rate basis, and we continue to believe that we're going to escalate that through the year, based upon the incremental actions we even drove in Q1.

Steve Tusa - *JPMorgan Chase & Co. - Analyst*

Okay, but I guess the comp gets tougher on synergies year over year into the second quarter. Is that where the restructuring comes in?

You just did some restructuring and that reloads that, if we want to call it, a core productivity pipeline. So that does look like in the second quarter that productivity, if you parse those out and use what you had guided to previously on synergies, it does look like that steps up in the second quarter on your guidance because the revenues are obviously weaker. But in the context of those weaker revenues, the profitability still looks pretty decent in the second quarter.

So, is that the way to think about it, that the restructuring -- if we assume that the synergies were what they were, that the restructuring helps that productivity number step up in the last nine months of the year?

John Stauch - *Pentair, Inc. - EVP, CFO*

Yes, because we are getting the restructuring, we are getting the synergies, and when we start to grow on that reduced cost structure, the leverage is very nice.

Steve Tusa - *JPMorgan Chase & Co. - Analyst*

Right.

John Stauch - *Pentair, Inc. - EVP, CFO*

When we track this year, the synergies aren't the problem. We're slightly underperforming on the core, and that's related to the revenue.

We're also utilizing those incremental synergies, as you know, now to cover the water transport impact. And we anniversary that in Q2, so I feel like we are well positioned on restructuring, and when we get the growth, we're going to see some pretty nice leverage.

Steve Tusa - *JPMorgan Chase & Co. - Analyst*

One last quick one. Is this it for restructuring for the year? Are you guys done for the year?

John Stauch - *Pentair, Inc. - EVP, CFO*

We expect to be done at the end of Q2.

Steve Tusa - *JPMorgan Chase & Co. - Analyst*

Okay, so it will be more than $22 million, $23 million or something like that? (multiple speakers) you have already done.

John Stauch - *Pentair, Inc. - EVP, CFO*

I think there will be carry over into Q2, correct.

Steve Tusa - *JPMorgan Chase & Co. - Analyst*

Okay, okay, thanks.

Operator

Josh Pokrzywinski, MKM.

Josh Pokrzywinski - *MKM Partners - Analyst*

First question, on slide 10. That's helpful color, but did any of that come together or become more clear as we worked through 1Q? I guess as I look at that, a lot of that seems like it could have been more helpful to point out last quarter, so I'm just wondering how much of that is more of a recent revelation in terms of sizing up some of those things?

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

It's not recent. As we were doing the restructuring, one of the things we knew was this business was -- one of the reasons we want to consolidate GBUs is we want to take out cost structure around businesses that just didn't need the cost structure, couldn't afford the cost structure.

The new information is the fact that the expected additional one or two projects just aren't materializing. It was at that point we realized this is something we should share. So it's not a surprise.

What's the surprise is the fact that there aren't any, none of the projects that would be reasonably expected and were actually being talked about haven't materialized as a real project.

Josh Pokrzywinski - *MKM Partners - Analyst*

Got you. And then (multiple speakers)

John Stauch - *Pentair, Inc. - EVP, CFO*

This isn't a highly configured business. It's a fairly standard product that goes into our factories that maintain a fairly high fixed-cost structure, so when you get a project, you can usually start shipping it within 30 to 60 days. And so, this is the season that we usually see those projects enter at least the front log, if not the backlog, and what Randy is saying is we don't even see them in the front log, let alone the backlog.

So this was the time that we felt we needed to share with you guys what we are absorbing in the rest of the base business.

Josh Pokrzywinski - *MKM Partners - Analyst*

Got you. Now I understand.

And then just shifting over to Valves and Controls, it seems like there is a bit of a gap forming between pretty healthy quoting activity or tone from customers and orders that I think have hit a new low since -- on a quarterly basis since you guys took over the business. And then, I guess, the same question on backlog versus shipment. Backlog seems like it's pretty healthy and you get these persistent delays.

What am I missing or what is the gap there? Is it walking away from unprofitable business, like you guys have talked about? Is it a forecasting, timing issue that you're still getting your arms around? Or, I guess, are there any other unintended consequences of this transformation, like sales force attrition or anything else?

John Stauch - *Pentair, Inc. - EVP, CFO*

Not seeing that. We're feeling the same optimism in the market that everybody else is talking about.

Last Q2, we had a difficult orders quarter. We saw a little bit of recovery in Q4 last year. And I wouldn't say we're at an historical low, but we are not ecstatic about the Q1 orders, but if you take the March order rate, it was relatively strong.

So, I think -- we are hearing the same optimism in the market and we are expecting that quoting activity to turn orders, and we are tracking this to a weekly order rate and looking at the variances and doing our root cause countermeasures.

I don't think there is any systematic issue to what you have asked; I think it's a matter of getting this capital investment spent and getting those projects put into place.

Josh Pokrzywinski - *MKM Partners - Analyst*

Is there anything else, outside of nuclear, which sounds like it was a bit of a short-cycle surprise in 1Q, from a short-cycle perspective that was particularly underwhelming in the first quarter? I guess you have seen Power -- or I guess you see the Energy bounce around in general. Any other kind of quick lead time --

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John Stauch - *Pentair, Inc. - EVP, CFO*

Yes, on the short cycle, we had probably the lowest conversion of, if you will, short-cycle orders in quarter For quarter the business has seen in a while. And Mining affected that, too. Mining, if a mine is open, it's going to have maintenance. So that was lower than we would have expected. So I would say it was both Power and Mining.

Josh Pokrzywinski - *MKM Partners - Analyst*

Got you. Understood. Thanks.

Operator

Andrew Obin, Bank of America.

Andrew Obin - *BofA Merrill Lynch - Analyst*

Just a question on markets, and how should I look at performance? It seems that nuclear was a little bit weaker, Mining was weaker, Australia was weaker. If we strip that out and if we look at the forecast, what else has changed, and what are the positives and what are the negatives just another level down?

John Stauch - *Pentair, Inc. - EVP, CFO*

Yes, Europe is -- remains a slight positive. It did have a warm winter, as Randy mentioned. We had a Thermal business that obviously [was] impacted there, but the rest of our other businesses saw a slight benefit from that warm.

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

Yes, it seems to be stable and heading up, right.

John Stauch - *Pentair, Inc. - EVP, CFO*

US continues to do really well in the market. Canada was a little weaker this time. And southeast Asia and China, as Randy mentioned, as well as the Middle East from a core basis, are good, solid markets right now.

Andrew Obin - *BofA Merrill Lynch - Analyst*

You also highlighted the fact that you had some overtime in March. Is there enough time to catch up, given the construction season, or do you think we now basically have to wait until (multiple speakers)

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

That comment was really specifically to the Process Technologies segment, and particularly the water purification or US Residential. It was a US Residential and European Residential comment. And no, no problem catching up. It was just (multiple speakers)

Andrew Obin - *BofA Merrill Lynch - Analyst*

Then are we going to catch up in the second quarter (multiple speakers) or do we need to wait until second half?

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

No, look, it's building now. The second quarter and third quarter are the Residential quarters.

Andrew Obin - *BofA Merrill Lynch - Analyst*

Okay, thank you very much.

Operator

Scott Graham, Jefferies.

Scott Graham - *Jefferies & Company - Analyst*

So I calculated, John, about $76 million of productivity plus synergies, which would be net of the pricing. I think you indicated that you did about $40 million of synergies in the quarter, which would suggest, if my math is right, about $36 million of productivity, which on the sales base is over 200 basis points. Is my math about right on that?

John Stauch - *Pentair, Inc. - EVP, CFO*

Yes, I think I said about $50 million in synergies, but your $26 million is right, and then, obviously, some of that is going to offset the inflation, so we always look at two elements. We want price to offset inflation. We want productivity to offset inflation in the core.

Sometimes we don't always get there perfectly, but that's our targeted action, and so we're always looking to offset that inflation rate on a core productivity.

But yes, we are seeing that strength of operating performance, seeing good cost structure, good cost discipline management, and that's why Randy and I are optimistic. When we see the growth, we are going to get that leverage.

Scott Graham - *Jefferies & Company - Analyst*

Right, right.

John Stauch - *Pentair, Inc. - EVP, CFO*

And the growth is frustrating, because we have got platforms that are -- we have 20 product technology platforms. Half of them are growing. When we talk about growing, they're growing high single digits. We got a couple of these platforms that are in significant contraction mode.

Now the good news is most of the ones, like water transport, aren't our highest margin, but some of the ones that are growing are higher margin, and so that's part of that positive mix we expect to see, as well. But yes, I think our math is generally correct, yes.

Scott Graham - *Jefferies & Company - Analyst*

Yes, I am actually calculating off of that adjustment about 150 basis points of productivity, which is still 50 basis points about what your target is, so I just wanted to confirm that.

The next question is really more of a question for you, Randy, and once out of every three or four quarters, there is some questions surrounding the topline that maybe it should have been a couple of points higher. Could you maybe talk about some of the things that you are doing to maybe address some of the vagaries that you see in sales from time to time across the businesses? Anything that you're hatching that is new to start to build on the critical mass that you now have in this Company?

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

Sure. One of the reasons we have gone from seven GBUs to five, and then underneath the five, John mentioned that we have identified and defined and staffed 20 platforms, focused platforms, to manage profitable growth so that we can make sure we are flowing the resources to our best opportunities.

We just put that in place at the beginning of this year, and that's why John can say what he just said, which is we really do understand which ones that are leveraging us for growth and which ones are the laggards and what do we do about it. So we have much more granularity to that.

At the same time, we have invested in a growth function and we very much targeting that right now to get a better handle on the forecasting ability in Valves and Controls.

And so, really our focus right now is on growth and our growth processes. We're building the competencies and capabilities for growth that we have built in Lean. It has taken us 13 years, 14 years to get where we are on Lean, but we are among the companies that are, if I can dare say so, great at it.

We don't intend to take that long in growth. We have been working at it for a couple years. We want to see more results, more sustained results, and one of the benefits, on the flip side, of being a narrowly diversified company is we are able to still execute and perform to promises even when stuff happens.

And growth is clearly the number one agenda for me. It's the number one agenda for the Company, and that's really where I'm putting all my focus right now, to make sure that we are funding the right things. If we can just get the average growth rate up to the low end of what we believe is possible, the profit potential is amazing.

The best driver of productivity is growth, operating leverage. We get that. So between the organization changes we have made, between the way we are flowing resources and we have changed resources, it's all about to drive a more sustained growth.

Scott Graham - *Jefferies & Company - Analyst*

That was my question. Thanks a lot.

Operator

Jeffrey Hammond, KeyBanc Capital Markets.

Jeffrey Hammond - *KeyBanc Capital Markets - Analyst*

Just backing the guidance and maybe a follow-on to what another caller was asking about, but just within your guidance range, you seem like you are talking about more negatives than positives. I'm just wondering if I'm not picking up on any kind of positive offsets within the number, whether it be lower corporate expense or some additional restructuring savings that you get later in the year. Or should we just be taking our numbers down a little bit? Within the range?

John Stauch - *Pentair, Inc. - EVP, CFO*

I think we are looking at a couple things. We were hopeful that water transport would recover, but we didn't plan on it happening, right?

We never really gave Q2 guidance, so within our plans I don't think we're bringing up anything new today within water transport. We're just sharing with everybody that we doubt it's going to recover back to historical levels and be any positive contributor past the $3.85 to $4.00 guidance range that we are giving.

We continue to work all those restructuring actions, which are more than offsetting the water transport headwind, and we feel very confident that we're building the growth processes, as Randy said, that are going to generate the growth that is going to give us the leverage.

So, right now we feel like we are being really balanced. Obviously, we are managing the corporate expenses, for two reasons. One is we are keeping the spending lower as a contingency, but the other reason is there is a lot to absorb in the businesses right now in integration and they don't need more initiatives on top of what they are already driving.

So, those are all the normal things that a business goes through this cycle, Jeff, so I think we feel like we are on plan for the year and we feel like we've got enough positives to offset the negatives.

Things have been a little bit more choppy in the external markets. I don't think anybody anticipated a slower start to January. I think we scrambled, like most companies, to make that all up, absorb those cost within our productivity in Q1, as well. So, I think you are just hearing a balanced view from us, Jeff.

Jeffrey Hammond - *KeyBanc Capital Markets - Analyst*

Okay, and then just on this bidding activity, when do you think you start to see that acceleration in the order book?

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

We are (multiple speakers)

Jeffrey Hammond - *KeyBanc Capital Markets - Analyst*

In the (multiple speakers)

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

(multiple speakers) better and expecting the second half to start seeing some shipments from it.

John Stauch - *Pentair, Inc. - EVP, CFO*

Jeff, Randy has put the business on a weekly pulse cycle. You want to take a look at orders, so you want to look at your front log, which is a manageable process to have visibility into what's coming. Then you want to have a predictability on the hit rate. You want to turn that into what you expect your daily orders rate would be, and what you want to see is a day-to-day improvement against that. And clearly, given what we saw in Valves in Q1, that's where Randy has got the business targeted in Q2, and we all have visibility to how we are doing against that.

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

Right.

Jeffrey Hammond - *KeyBanc Capital Markets - Analyst*

Okay. Thanks, guys.

Operator

Brian Konigsberg, Vertical Research.

Brian Konigsberg - *Vertical Research Partners - Analyst*

Just coming back to Valves and Controls, so it sounds like you are optimistic you will start to see a better ordering environment, but I guess -- I don't know if you're getting any indications as far as the pricing of the early surge in potential orders coming to market. Typically when we see these type of cycles, it does get pretty price competitive at the beginning, and then once capacity absorption takes place, it gets better.

So I guess, A, from what you see today, do you see pricing pressure potential associated with the early projects? And how disciplined do you expect to be, associated with those bids?

John Stauch - *Pentair, Inc. - EVP, CFO*

I think Oil & Gas, as we said before, will always have a price element there. There is the most competition in that space.

I think the thing that we are looking at now is based upon our substantial productivity that we have driven, we have to have the confidence to maybe take a little bit lower gross margin, knowing that we can drive the productivity in those projects.

I can't tell you that we have lost anything over price, though, but we want to have that type of visibility to know that if we are this confident we can continue to get the productivity, does that open up an increased order book for us? Randy, I don't know if you want to comment, but I don't think there has been any of that element.

I would also say a window that we have as well is we have an actuation and controls business, which serves our competition --

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Randy Hogan - *Pentair, Inc. - Chairman, CEO*

Serves the whole industry (multiple speakers)

John Stauch - *Pentair, Inc. - EVP, CFO*

Serves the whole industry, and I can assure you that based upon their performance in the quarter, it doesn't feel like we have lost share. So, we have an inside view to the rest of the world in the valve space. We are still the world's leading valves and controls player, so we feel we are involved in every project and we feel like we're going to win our fair share here.

Brian Konigsberg - *Vertical Research Partners - Analyst*

Okay, fair enough. And then, just -- moving over to working capital, so that was a little bit more of a headwind than I thought it would be in the first quarter. Is it just related to the cadence of how activity, I guess, progressed through the quarter, and --

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Randy Hogan - *Pentair, Inc. - Chairman, CEO*

Basically, yes.

Brian Konigsberg - *Vertical Research Partners - Analyst*

Okay, that makes sense. I just have (multiple speakers)

John Stauch - *Pentair, Inc. - EVP, CFO*

(multiple speakers) more got into margins (multiple speakers)

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

If we had stuff that would have sold in January, we would have got cash for it, but it just wasn't balanced in terms of the usual mix of sales by month. That's really (multiple speakers). The quarter always is a cash usage quarter for us, just because of the nature of the business.

Brian Konigsberg - *Vertical Research Partners - Analyst*

Okay, and then just -- I know you have made comments before on bringing working capital from flow control down to more in-line levels with legacy Pentair. Is that a benefit you expect you'll see in 2014? And I guess, how much more difficult does that become if the cycle is starting to get going?

John Stauch - *Pentair, Inc. - EVP, CFO*

No, I think we made great progress in 2013. Still a long way to go. But I think we expect to make another big jump forward here in 2014. It's just receivable discipline. It's inventory discipline. And it is tracking it and managing it and being accountable to it. We think we're still going to make progress even with growth in the business.

Brian Konigsberg - *Vertical Research Partners - Analyst*

Okay, fair enough. That's about it for me. Thank you very much.

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

We are at an hour. How many people left? (multiple speakers) let's try that. Three quick ones.

Operator

Nathan Jones, Stifel.

Nathan Jones - *Stifel Nicolaus - Analyst*

Couple questions on the short-cycle Oil & Gas business. You talked about in your prepared comments that there is more variability in that business than you thought there was going to be. I think we all understand the timing issues in the long-cycle business, but what's behind that variability in that business, in your opinion?

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

Yes, what I meant -- what I was saying was in this quarter, we saw a lower short-cycle business. That was a surprise, frankly, that the, if you will, book in the quarter, ship in the quarter was the lowest conversion that we have seen, going back in history since before we owned it.

And it just seems like that in our area, in our installed base, there was a little bit of a slow start, and I don't know if that was weather-related in the US or we don't really -- there's lots of conjecture, but I can't give you root cause analysis on it, but we are certainly focused on it. That's one of the things, as John mentioned, we have some new disciplines in terms of weekly reviews on order rates. That's one of the things that we are watching to understand better.

So, I wouldn't say that's something that was worse in the first quarter than we have seen.

Nathan Jones - *Stifel Nicolaus - Analyst*

At this point, are you able to say that you expect that conversion rate to improve?

John Stauch - *Pentair, Inc. - EVP, CFO*

Absolutely.

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

We would expect it to revert to the mean. There is -- that short-cycle business is largely replacement. As long as the refineries are running, as long as work is being done, products are getting worn out, so it's the kind of thing you wouldn't expect to have a high standard deviation around.

Nathan Jones - *Stifel Nicolaus - Analyst*

That makes sense. (multiple speakers)

John Stauch - *Pentair, Inc. - EVP, CFO*

One of the things that we will have a clearer picture as we conclude the year, Randy and I both have a lot of experience in long-cycle businesses, and when you get into project and maintenance related businesses, Q1 is usually your lowest quarter and Q4 is usually your highest quarter, right?

So, one of the conjectures is the high rate of booked and shipped in Q4 of last year impacted the low rate of booked and shipped in Q1, but they were on a different fiscal year really shouldn't be an element of difference. Quarters should be quarters. And you should be responding whatever the customer demands are.

And so, we should probably see a more normalized cycle of Q1 being the lowest shipment quarter, Q4 being the highest shipment quarter, and we will see how that plays out this year. But that's what Randy and I are expecting and that's what we forecasted.

Nathan Jones - *Stifel Nicolaus - Analyst*

Okay, and you also said that you expect a ramp in short-cycle Oil & Gas as the year goes on. I know we have heard similar things from other companies. Can you just provide a little bit more color on what you are seeing out there that gives you that confidence?

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

Well, again, it's the bidding activity. And it's the quoting activity that gives us that confidence.

Nathan Jones - *Stifel Nicolaus - Analyst*

Are we seeing those turn into orders in a timely fashion?

John Stauch - *Pentair, Inc. - EVP, CFO*

That is what we are continuing to track, Nathan, which is what I was talking earlier about is we want to make sure that we are looking at those hit rates. We are looking at the time in the cycle from the time that the order goes into our front log tracking mechanism to -- I'm sorry, to the bidding goes in the front log to when it converts to an order, and we obviously have a lot more data and much more track record now that Randy and I can push the business to see.

We're very optimistic, as the market is, and we are tracking those orders, and our expectation is April is a big step up from March, and right now, we are not off of that expectation.

Nathan Jones - *Stifel Nicolaus - Analyst*

Okay, great. Thanks, guys, and thanks for taking my question.

Operator

Hamzah Mazari, Credit Suisse.

Unidentified Participant

This is [Flavio]. I am standing in for Hamzah today. Most of my questions have been answered. Thank you for taking mine. Just two very quick ones. On Valves and Controls, can you just remind us what share of sales is aftermarket short sale -- short-cycle sales over there, and how much of the growth in that business is driven by share gain?

And also some pretty quick update on if you are seeing any revenue synergies coming through or any color on that front?

John Stauch - *Pentair, Inc. - EVP, CFO*

Roughly, we would expect a normal cycle to be somewhere around 50% to 60% into what we would call the installed base, and that's mostly a like-for-like replacement against whatever spec you won, for the most part. And then, the rest would be a major expansion and/or some type of greenfield application.

Obviously, when you are in large project types of cycles, it probably shifts to more 40% in installed and 60% elsewhere.

The second part of your question, on sales synergies, we continue to be able to take these 20 product platforms now that we have the visibility, and those that are strong in Energy are trying to pull the rest with them. And we continue to be excited about the pull through opportunities that a leading product provider has to bring the rest of our product technologies through a project. So, we're as excited about that opportunity as we were when we acquired Tyco Flow.

Unidentified Participant

That's perfect. Thank you for taking my question, guys.

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

All right, thank you very much and --

John Stauch - *Pentair, Inc. - EVP, CFO*

Thanks, everybody.

Randy Hogan - *Pentair, Inc. - Chairman, CEO*

You can give the replay information, Operator. Thank you.

Operator

This concludes today's conference call. You may now disconnect.
