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DOV - Q1 2016 Dover Corp Earnings Call

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OVERVIEW:

Co. reported 1Q16 revenues of \$1.6b and EPS of \$0.64. Expects 2016 total revenue to decline 2-5% and EPS to be \$3.51-3.66.



CORPORATE PARTICIPANTS

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Deane Dray *RBC Capital Markets - Analyst*

Joseph Ritchie *Goldman Sachs - Analyst*

PRESENTATION

Operator

Good morning, and welcome to the first-quarter 2016 Dover earnings conference call.

With us today are Bob Livingston, President and Chief Executive Officer; Brad Cerepak, Senior Vice President and CFO; and Paul Goldberg, Vice President of Investor Relations.

(Operator Instructions)

As a reminder, ladies and gentlemen, this conference call is being recorded, and your participation implies consent to our recording of this call. If you do not agree with these terms, please disconnect at this time. Thank you.

I would now like to turn the call over to Mr. Paul Goldberg. Mr. Goldberg, please go ahead, sir.

Paul Goldberg - *Dover Corporation - VP of IR*

Thank you, Kristy.

Good morning, and welcome to Dover's first-quarter earnings call. With me today are Bob Livingston and Brad Cerepak.

Today's call will begin with comments from Bob and Brad on Dover's first-quarter operating and financial performance, and follow with our outlook for the remainder of 2016. We will then open the call up for questions. As a courtesy, we kindly ask that you limit yourself to one question, with a follow-up.

Please note that our current earnings release, Form 10-Q, investor supplement, and associated presentation can be found on our website, www.dovercorporation.com. This call will be available for playback through May 5, and the audio portion of this call will be archived on our website



for three months. The replay telephone number is 1-800-585-8367. When accessing the playback, you'll need to supply the following access code: 79357235.

Before we get started, I'd like to remind everyone that our comments today, which are intended to supplement your understanding of Dover, may contain certain forward-looking statements that are inherently subject to uncertainties. We caution everyone to be guided in their analysis of Dover by referring to our Forms 10-K and 10-Q for a list of factors that could cause our results to differ from those anticipated in any such forward-looking statement. Also, we undertake no obligation to publicly update or revise any forward-looking statements, except as required by law. We would also direct your attention to our website, where considerably more information on Dover can be found.

And with that, I'd like to turn this call over to Bob.

Bob Livingston - *Dover Corporation - President & CEO*

Good morning, everyone, and thank you for joining us for this morning's conference call.

As previously communicated, our first quarter was well below our initial expectations, driven by significant further reductions in activity in capital spending within our US oil and gas-related end markets. These conditions primarily impacted our Energy segment and, to a lesser extent, Fluids. The market served by Engineered Systems, and Refrigeration and Food Equipment, remained solid, resulting in organic growth of 3% in each segment.

In total, we delivered first-quarter adjusted EPS of \$0.52, and took further steps to reduce our cost and right size our businesses. In addition to introducing new products and pursuing share gains, we are increasing our restructuring actions, and have stepped up our efforts on productivity, including shared services.

Now let me share some comments on the quarter. From a geographic perspective, excluding our Energy segment, our US industrial activity remained solid and grew organically low-single digits year over year. Both our China and European markets were down sequentially, and also down organically from the prior year.

In Energy, markets further deteriorated as we moved through the quarter. Market activity levels hit new lows on continued declines in the US rig count and reduced capital spending, which, in turn, drove our first-quarter revenue and earnings down significantly. Our teams have remained resolute on actions to drive sales and share gains, and in reducing all non-essential costs, while still maintaining their engineering talent and ability to respond to customer opportunities.

Engineered Systems' organic growth was 3%. Within printing and identification, we once again posted solid results in our core marking and coding business. In the industrial platform, organic growth was broad based.

Fluids posted strong revenue growth, driven by the recent acquisitions of Tokheim, Gala, and Reduction. On an organic basis, our businesses with direct oil and gas exposure, and those businesses serving integrated energy customers, especially within retail fueling, posted declines.

Our Refrigeration and Food Equipment segment grew 3% organically, largely driven by retail refrigeration. Revenue and earnings performance was as expected, benefiting from our customer expansion efforts taken over the last several quarters.

Regarding acquisitions, we believe we have line of sight on several deals over the next few quarters in our key growth markets.

Now looking forward -- within Energy, as a result of further US market declines, we have reduced our organic revenue forecast, which is now expected to be down 27% to 30% for the full year. On a sequential basis, the first quarter was down 12%. We now expect the second quarter to sequentially decline another 10%.

In Engineered Systems, our expectations for organic growth are unchanged, driven by the leading technology and new products offered across the segment. We expect the marking and coding business to grow low- to mid-single digits, and our digital textile businesses to have double-digit growth. Within our industrial platform, we expect modest, broad-based growth.

Fluids will grow this year, driven by their recent acquisitions, which should generate roughly \$400 million in revenue in 2016. We also expect solid to strong growth from our industrial, hygienic, and pharma markets. Overall, organic revenue is expected to be a few points lower than previously forecasted, as a result of direct oil and gas exposure, lower CapEx spending from integrated energy customers, and project timing.

Finally, within Refrigeration and Food Equipment, our plans for organic revenue growth and margin improvement remain on track heading into the seasonally strong second and third quarters. Our leading technology and merchandising solutions are resulting in customer wins at several regional and national food retail chains.

In summary, we are lowering our full-year EPS guidance to reflect the impact of oil and gas markets. Our full-year guidance includes \$40 million of restructuring costs, which will deliver significant benefits on an annualized basis.

With that, I'd like to turn it over to Brad for further comments.

Brad Cerepak - *Dover Corporation - SVP & CFO*

Thanks, Bob. Good morning, everyone.

Let's start on slide 3 of the presentation deck. Today we reported first-quarter revenue of \$1.6 billion, a decrease of 5%. This result was comprised of an organic revenue decline of 7%, and an FX impact of 1%.

Growth from acquisitions of 6% less dispositions resulted in net acquisition growth of 3%. EPS was \$0.64, and includes \$0.05 of discrete tax benefits and a \$0.07 gain from a disposition.

Segment margin for the quarter was 11.7%, 180 basis points below last year. Adjusting for first-quarter restructuring of approximately \$14 million, margin was 12.5%. Restructuring activities were primarily focused within our Energy and Fluids segments.

Bookings decreased 4% over the prior year to \$1.7 billion. Within this result, acquisition growth of 4% was more than offset by the combined impact of reduced oil and gas markets, dispositions, and FX.

Organic bookings in our Engineered Systems, and Refrigeration and Food Equipment, segments grew 4% and 5%, respectively. Overall, book to bill finished at 1.03, up slightly from last year. Our backlog decreased 10% to \$1.1 billion, and was down 6% excluding dispositions.

Free cash flow was \$96 million or 6% of revenue, consistent with the prior-year first quarter. We expect to generate free cash flow of roughly 11% of revenue for the full year.

Now let's turn to slide 4. Engineered Systems, and Refrigeration and Food Equipment, both increased organic revenue 3%. This increase reflects broad-based growth across Engineered Systems, and in retail refrigeration and can-shaping businesses of Refrigeration and Food Equipment.

Fluids' organic decline of 3% was driven by oil and gas markets, and slower CapEx spending in select fluid transfer markets. Energy organic revenue was down 33% on further declines in the North American oil and gas markets. As seen on the chart, net acquisition growth was most prevalent at Fluids, with 22% growth, principally driven by Tokheim.

Now on slide 5, Energy revenue of \$283 million decreased 34%, driving earnings down from the prior year to \$11 million. Energy's results continued to be further impacted by declines in oil and gas market fundamentals, especially the US rig count.



Energy incurred an additional \$6 million in restructuring costs. Since the beginning of the oil and gas downturn in 2014, this segment has reduced their workforce by 32%, or 2,100 people.

Excluding the Q1 restructuring costs, our operating margin was 6%, reflecting volume and price declines. We expect to complete additional cost actions in the second quarter, and exit 2016 at around 10% margin. Bookings were \$273 million and book to bill was 0.97.

Turning to slide 6, Engineered Systems revenue of \$577 million increased 1% overall, reflecting organic revenue growth of 3% and unfavorable FX of 2%. Net acquisitions were neutral, where the acquisition growth of JK was essentially offset by the revenue connected with the sale of the business.

Earnings of \$94 million increased 6%, principally reflecting the benefits of productivity and organic volume leverage. Of note, \$11 million gain on the disposition was principally offset by increased costs associated with a recent factory consolidation and other one-time items.

Our printing and identification platform revenue of \$240 million increased 4%. Organic revenue was up 1%, primarily reflecting solid North American marking and coding markets. Acquisitions added 8% growth, while FX was 5% negative.

In the industrial platform, overall revenue declined 2% to \$337 million, where organic growth of 4% was offset by a 5% impact from a disposition and 1% from FX. Organic growth was broad based. We incurred \$2 million in restructuring costs in the quarter. Excluding the Q1 restructuring cost, margin was 16.6%.

Bookings of \$573 million were flat, reflecting organic bookings growth of 4% and acquisition growth of 3%, largely offset by the impact of a disposition and FX. Organically, printing and identification bookings were essentially flat, and industrial bookings increased 6%.

Book to bill for printing identification was 1.01, while industrials was 0.98. Overall, book to bill was 0.99.

Now on slide 7, within Fluids, revenue increased 17% to \$399 million, while earnings decreased 16% to \$46 million. Revenue performance reflects 22% growth from acquisitions, partially offset by a 3% decline in organic revenue and 2% from FX.

Our Fluids transfer and pumps results reflect the impact of weak oil and gas markets, reduced capital spending, and the timing of orders, partially offset by solid results in industrial, hygienic, and pharma markets. Low organic volume, the impact of acquisitions, and \$3 million of incremental restructuring costs reduced margin 460 basis points in the quarter. Excluding restructuring, and acquisition and related purchase accounting, margin was 17.5%, an increase of 70 basis points over an adjusted prior year.

Bookings were \$418 million, an increase of 23%. This result primarily reflects the positive impact of acquisitions. On an organic basis, bookings were flat. Book to bill was 1.05.

Now let's turn to slide 8. Refrigeration and Food Equipment's revenue of \$363 million declined 2% from the prior year, and earnings were \$38 million, an increase of 6%. Organic revenue growth of 3% was largely driven by wins at several retail refrigeration customers.

We also had solid results in our glass door and can-shaping equipment businesses. Overall, the disposition of our walk-in cooler product line and FX impacted revenue 5% and 1%, respectively.

Operating margin was 10.5%, an 80-basis-point increase over last year. This improvement was largely driven by the benefits of productivity and leverage on organic growth.

Bookings of \$411 million were down 2%. This result reflects 5% organic growth, offset by a 6% impact of a disposition and 1% from FX. Book to bill was 1.13, reflecting normal seasonality in the retail refrigeration market.



Going to the overview on slide 9, let me cover some highlights. Corporate expense was \$30 million and net interest expense was \$32 million, both in line with our prior forecasts. Our first-quarter tax rate was 27.9% excluding discrete tax benefits.

Now moving to slide 10, which shows our full-year guidance. As Bob mentioned, our 2016 revenue guidance has been lowered to reflect the oil and gas markets. We now expect total revenue to decrease 2% to 5%. Within this estimate, organic revenue is expected to decline 5% to 8%, a 4-point reduction from our prior forecast.

We expect net acquisitions will add approximately 4% growth, unchanged from our prior guidance. We now expect the impact of FX to be about 1% negative for the year.

At the mid-point of our guidance, adjusted segment margin is expected to be around 15%. Excluding restructuring costs, and further adjusting for acquisition and purchase accounting, margin is expected to be around 16%.

Our full-year forecast for corporate expense, interest expense, and the pre-discrete tax rate remains unchanged. Additionally, CapEx remains unchanged, as does our full-year free cash flow forecast.

From a segment perspective, Energy full-year organic revenue forecast is now expected to decline 27% to 30%. We have also reduced Fluids' organic revenue forecast, which is now expected to decline 2% to 5%. Engineered Systems, and Refrigeration and Food Equipment, is unchanged versus our prior guidance. Net acquisitions remain at 4% growth.

Turning to the bridge on slide 11, let's start with 2015 adjusted EPS of \$3.63. We now expect the year-over-year impact of restructuring costs to provide a \$0.07 benefit, reflecting total 2016 restructuring costs of \$40 million, versus \$55 million last year. Our revised forecast reflects \$20 million, or \$0.09 EPS, in incremental restructuring costs versus the prior forecast.

Performance, including changes in volume, productivity, pricing and restructuring benefits, will impact earnings \$0.09 to \$0.17. This is reduced from our previous forecast, principally driven by the effect of lower volume.

Increases in investment and compensation will impact earnings \$0.19 to \$0.22, reflecting roughly \$0.07 of reduced spend. Acquisitions less dispositions will be \$0.16 to \$0.17 accretive in total. This amount includes the operating earnings of acquisitions less dispositions, and the related gain. The carry-over benefit of prior-year share repurchases, the impact of interest, corporate expense and the tax rate are all unchanged.

Lastly, as I mentioned before, we had a discrete tax benefit of \$0.05 in the quarter. In total, we expect 2016 EPS to be \$3.51 to \$3.66, down about \$0.50 at the mid-point of our prior guidance, excluding the gain on a disposition and discrete tax benefits.

With that, I'll turn the call back over to Bob for some final thoughts.

Bob Livingston - *Dover Corporation - President & CEO*

Thanks, Brad.

As we begin the second quarter, markets remain mixed. Businesses with exposure to oil and gas continue to be impacted by historically weak markets.

Engineered Systems is benefiting from solid industrial end markets, healthy printing and coding end markets, and in continued growth in adoption of digital printing and global textile activity. Refrigeration and Food Equipment is also quite resilient, due in part to their leading retail refrigeration technologies that helps their customers capitalize on the growing trend of selling prepared and fresh food.

Within Fluids, although it's early, we are very excited about the customer response to our recent acquisitions. Within retail fueling, customers are now asking us to provide our full scope of products. We are also seeing revenue synergies at our plastics and polymer customers, with the addition of Gala and Reduction.

We will continue to execute on initiatives to help drive growth and fund investments, namely: launching new products across the entire Organization; expanding our Business with new customers and in new geographies; leveraging our Dover Excellence program to continue to drive margin, productivity and cash flow; and capitalizing on our scale through the establishment of shared service centers. In all, leveraging these growth opportunities, and executing on our internal actions, will help mitigate mixed markets, drive productivity, and redirect resources to pursue growth initiatives. We also expect to fully leverage the recovery in our oil and gas markets, when it comes.

With that, I'd like to thank our entire Dover team for staying focused on our customers. And, Paul, let's take some questions.

Paul Goldberg - *Dover Corporation - VP of IR*

Thanks, Bob.

Before we turn it back to Kristy, I'd just again like to remind you, if you can limit yourself to one question with one follow-up, that would be helpful. We have about 20 people in the question queue.

So with that, Kristy, if you can give us our first question.

QUESTIONS AND ANSWERS

Operator

Steve Winoker, Bernstein.

Steve Winoker - *Bernstein - Analyst*

Thanks and good morning, guys. Could you maybe just start talking about the pacing of the Energy revenue as we move through the year given the order dynamics? How long it takes to work through and the Energy margin progression as well?

Bob Livingston - *Dover Corporation - President & CEO*

Okay. Let's see. Steve, I think in my script I commented on our sequential decline in the first quarter of 12%, and that we are anticipating another sequential decline in the second quarter of about 10%.

You look at the second half, the second half revenue is closely aligned with what we view as the run rate for the second quarter, and I would add one color comment on that. In the second half, we do have about \$45 million of share gain revenue, sort of split evenly between the third and fourth quarter, on wins that we've won and we have line of sight to. Absent the share gain wins, the revenue in the second half would be modestly below the second quarter run rate.

On margins, for the year, margins are going to, I think at the top end of our guide, margins are about 6% or 6.5%.



Brad Cerepak - *Dover Corporation - SVP & CFO*

All in.

Bob Livingston - *Dover Corporation - President & CEO*

All in, including restructuring. The restructuring activity is very heavily loaded in the first and second quarter. Second half sees the benefits from the restructuring activity and the absence of any new restructuring actions, and we do, our guide does show that we exit 2016 with an operating margin at Energy of just about 10%.

Steve Winoker - *Bernstein - Analyst*

Okay. And just to follow that up then. If you, if conditions were not to get any worse at this point, Bob and Brad, at what point do you see, could you actually see the comps easing enough into next year that you'd actually be able to cross over into positive territory?

Bob Livingston - *Dover Corporation - President & CEO*

If activity, if we were at the trough now and activity didn't get any worse, but also assume that it doesn't get any better, then you could see the first quarter of 2017 having a revenue run rate slightly above first quarter 2016.

Steve Winoker - *Bernstein - Analyst*

Okay. Okay. All right. Well, let me leave it there given the number of questions. Thanks, guys.

Operator

Jeffrey Sprague, Vertical Research.

Jeffrey Sprague - *Vertical Research Partners - Analyst*

Good morning. Thank you, guys. I was wondering if you could address price in oil and gas and also in Fluids? It does look like you're expecting a pretty good drop through on your restructuring actions, just kind of looking at the footnotes of your bridge here. What are you anticipating for price erosion in that guide and in that payback?

Bob Livingston - *Dover Corporation - President & CEO*

So your question's specific to Energy and then the followup was Fluids?

Jeffrey Sprague - *Vertical Research Partners - Analyst*

Yes. I think, unless you've got price pressure elsewhere, but --



Bob Livingston - *Dover Corporation - President & CEO*

For first quarter in Energy, price was a negative 1% for the segment. Jeff, I would still tell you that in our guide, we still have a negative 2% to 3% price pressure for the year, but in the first quarter it was 1%. The price pressure in Fluids for the year is less than 1%. I'm going to say about 1%. I think it's actually 0.9%, to be specific. And then for the company as a whole, it's actually very, very slightly positive for the year.

Jeffrey Sprague - *Vertical Research Partners - Analyst*

That is a shockingly okay, you know, price-sounding number.

Bob Livingston - *Dover Corporation - President & CEO*

It's not that much different than what we experienced last year.

Jeffrey Sprague - *Vertical Research Partners - Analyst*

Yes. So people are behaving despite the volume declines on price?

Bob Livingston - *Dover Corporation - President & CEO*

Yes. Again, I would tell you that I gave you a number on the Energy segment, and I would repeat myself, you know, what I said last year several times. You will get it at individual product lines, and you're going to see different stories. We still continue to see price pressure in our rods business that's very similar to what we saw last year.

In fact, last year I think price pressure, priced down on the rods business last year, I think was 9% or 10%. That's not going to be as bad this year, but we're still going to see price pressure on the rod business this year, and in our diamond insert business, I think for last year, Brad, help me here, 5%, 4%, 5%, 6% last year and we are expecting another price down in our insert business this year of 3% to 5%.

Jeffrey Sprague - *Vertical Research Partners - Analyst*

So you've got positive price elsewhere in Energy, where would that be?

Bob Livingston - *Dover Corporation - President & CEO*

Bearings and compression.

Jeffrey Sprague - *Vertical Research Partners - Analyst*

Yes. And then just a quick one, just a quick one to shift gears. How quickly do you think you can ramp up Tokheim's exposure in the US, and where are you at on, you know, sourcing OPW through Tokheim, and some of that vertical integration you were looking at?

Bob Livingston - *Dover Corporation - President & CEO*

Well, with the first question about Tokheim in the US, I'm going to defer a story on that until we get together at our technology day in, what is it, Paul? Early or mid June. We're still early days on this, on the integration, the onboarding of this business, and I think we'll have a better answer for you in June than I can give you today.



But the integration of OPW and especially on the retail components business, the integration of OPW and Tokheim is moving along smoothly, and the pull through of OPW, I call it, especially the hanging hardware, is progressing as we expected. It's pretty positive.

Jeffrey Sprague - *Vertical Research Partners - Analyst*

Okay, thank you.

Operator

Julian Mitchell, Credit Suisse.

Julian Mitchell - *Credit Suisse - Analyst*

Hi, good morning. My first question is just on the Fluids guidance for the year, on the revenue line. You talk in the presentation about the split between sort of solid industrial, hygienic, and pharma, versus the oil and gas in Energy stuff. In your full-year organic guide now, what do you, how do you split out the assumed revenue deltas for each of those buckets, in terms of oil and gas?

Bob Livingston - *Dover Corporation - President & CEO*

Oh, gosh, I don't have that detail in front of me, Julian. To give you a little bit of color, I did use the descriptive phrase solid to strong, when I described industrial and hygienic and pharma. I would tell you that in the industrial part of the portfolio, you know, mid-single-digit type of growth. In the pharma and the hygienic, more so in pharma, we're seeing double-digit growth in those verticals.

And it's been, both of those verticals have been areas we've focused on building our product portfolio over the last couple of years, but they're still relatively small. But I don't, I can't give you a split for the year. I don't have that kind of detail with me.

Julian Mitchell - *Credit Suisse - Analyst*

Sure. And then if we just look at the, you know, Engineered Systems business and the industrial parts of Fluids, was there any change in sort of customer behavior in recent months, you know, since the beginning of the year, or do you say it's been fairly steady?

Bob Livingston - *Dover Corporation - President & CEO*

Well, within Engineered Systems, the comments would be slightly different between the printing and ID platform, versus the industrial platform. I don't think there's been any changes in the industrial platform. In fact, my comment in the script was that we had good organic growth in the first quarter in our industrial platform, and you note that I did not call out a single business or two like I have done in the past. The growth in the first quarter was very, very broad based in the industrial platform. Within the printing and ID platform, Markem-Imaje, I think organic growth was 3% or a little bit better, between 3% and 4%, fairly solid, you know, right on our expectations.

Interestingly enough, the strong market was not just the US. I would call it the Americas. We had strong growth from Canada through Brazil. But the entire Americas team did a very good job for Markem-Imaje in the first quarter. Little bit lower growth in Europe, but it was still positive. China was a challenge.

Now I'll answer your question about profile. I will tell you that, and I think I shared this on a call or two last year with respect to both Europe and China, we continue to see a slowdown and a deferral and a longer sales cycle, both in Europe and China, with respect to orders that are for what I



would refer to as capital goods. If it's for operating type of expenditures that, you know, products that we're selling to our customers, that activity seems to be holding up fairly well.

Julian Mitchell - *Credit Suisse - Analyst*

Very helpful. Thank you.

Operator

Nigel Coe, Morgan Stanley.

Nigel Coe - *Morgan Stanley - Analyst*

Thanks, good morning. Yes. Just a couple of quick questions on segment margins before a broader question. This, maybe Brad or Bob, Fluid margins -- so Fluid margins obviously impacted by Tokheim accounting this quarter. Can you maybe just size that for us? And also the gain on disposition, did that fall into the ES segment?

Bob Livingston - *Dover Corporation - President & CEO*

Okay. Brad can give you some detail, but I'm going to enjoy giving you a quick response on the Fluid margins, Nigel. If you strip out the acquisitions from, out of the Fluids segment that we completed in 2015, and then Tokheim in January of this year, and just look at the core business, we actually have slight margin improvement year-over-year in the first quarter. I think maybe it was modest, but still it was an improvement. I think it was 30 or 40 basis points improvement in the core operating margin.

But obviously the acquisitions are coming on board with lower margins than the core, and then we have the purchase accounting on top of that. But Brad can probably give you additional color than that.

Brad Cerepak - *Dover Corporation - SVP & CFO*

Well, the only thing I would add, for the first quarter I would add that, you know, not having the numbers on the top of my head right here, we had, you know, in the [DF] about, oh, I don't know, about \$7 million or so of restructuring costs, if I remember correctly.

If I adjust for that restructuring cost and I adjust for then the deal, you know, the margins in Fluids would be about 17.5%. So you can do the math on that and figure out what the delta is on with respect to the acquisitions.

Nigel Coe - *Morgan Stanley - Analyst*

Okay, that's --

Bob Livingston - *Dover Corporation - President & CEO*

Your other question was on the disposition?



Nigel Coe - *Morgan Stanley - Analyst*

Yes, [that's full on year].

Bob Livingston - *Dover Corporation - President & CEO*

That was within the industrial platform of DES and I think the gain that, I think we commented on this in the script. I think the gain was \$10 or \$11 million.

Brad Cerepak - *Dover Corporation - SVP & CFO*

\$11 million.

Bob Livingston - *Dover Corporation - President & CEO*

\$11 million.

Nigel Coe - *Morgan Stanley - Analyst*

Okay, good. And then just, Bob, Energy's, you know, had plus or minus 10% or more organic growth declines for six of the past eight years, and you know it looks like the next couple of years you're going to have strong double-digit growth --

Bob Livingston - *Dover Corporation - President & CEO*

You mean six of the past eight quarters?

Nigel Coe - *Morgan Stanley - Analyst*

No, eight years, if you go back to 2009. So I understand the cycle's up, cycle's down, but given that cyclical, you know, is that something you have to live with, and it still remains the growth platform going forward, or how are you thinking about Energy as part of Dover going forward?

Bob Livingston - *Dover Corporation - President & CEO*

So the question is around margins. Let me just, you'd have to start, you're going to look at it over a longer period of time looking back. You have to start by understanding the effect of product mix and acquisitions on the segment margins. And I'm not just talking about purchase accounting and amortization, but the pure business profile of the acquisitions that we've made over the last four or five years.

You go back to 2000 and 2008, 2009, the two primary businesses within our Energy platform as we reported today would be our artificial lift business and our diamond insert business. Both of which have margins then and up until 2000, up until the last, you know, up until the last nine months have had margins higher than the businesses that we've been acquiring.

So the mix has changed rather significantly. It's rather difficult to compare the business margin profile of even prior to the downturn, even in 2014 to the business profile we had in 2008. And if you want to have Paul walk that through you on a call later, then he'll be glad to do that.



Nigel Coe - Morgan Stanley - Analyst

Yes, okay, thanks a lot. It wasn't really margins, it was more cyclicity of the business, but I'll followup offline. Thanks, Bob.

Operator

Shannon O'Callaghan, UBS.

Shannon O'Callaghan - UBS - Analyst

Good morning, guys. Hey, to follow up maybe a little bit on Nigel's Fluid margins question. If we just think about kind of the margins from here in Fluids, versus the first quarter run rate, I mean, does all of that acquisition impact, is that just normal, like ongoing acquisition accounting, or was that any stuff that hit more in 1Q that's going to ease for the year, or is this kind of a good all-in-one run rate if we just adjust for the restructure?

Brad Cerepak - Dover Corporation - SVP & CFO

No. I would say that there's, you know, as is typical with three acquisitions, we have quite a bit of impact related to inventory, turnover in the first quarter that doesn't continue beyond that, but you do get to normal amortization of the goodwill and, actually, the intangibles. So the inventory piece, you know, I would say first quarter is being impacted by roughly \$6 million or \$7 million of inventory, and that doesn't repeat itself into the second or third, fourth quarters.

Shannon O'Callaghan - UBS - Analyst

Okay.

Brad Cerepak - Dover Corporation - SVP & CFO

And then if you think about margins as well on restructuring, we said restructuring is going to be \$40 million. If you think about how that's going to get spent, we had \$14 million or so in the first quarter, I would expect by the time we finish the second quarter we'll be about \$35 million or so of that \$40 million spent.

So again, as I start to look at first half, second half, even for the company, you know, the first half, second half is not traditional. What I would say is the split between first half and second half at 48-52, it's showing up in our guide right now at about a 43-57. But if you adjust for these one-offs that you're asking about and restructuring and then re-look at it at that level, you'd have closer to a 45%, 46% first half.

Shannon O'Callaghan - UBS - Analyst

Okay. That helps. And just on, you know, Bob, on your comment on, you know, sort of Energy being positioned to, you know, fully leverage any eventual recovery, price hasn't actually seemed that bad, as Jeff was saying earlier, and head count's now down 32% and we're going to be hopefully exiting the year around a 10% run rate. So what does that mean in terms of fully leveraging a recovery? I mean, in a positive scenario, but where do you really think you can get this Energy business back to, margin-wise?

Bob Livingston - Dover Corporation - President & CEO

Again, it's, if I knew what the volume was going to be next year, Shannon, I could tell you, I could give you a pretty good guess as to what the margins are going to be. It is very volume sensitive. We commented on margins and we don't -- and the EBITDA numbers are obviously in our



filings, but even as we look at our Energy segment, if we close, if we exit the fourth quarter with a 10% operating margin run rate, Shannon, our EBITDA on that business is about 20% in the fourth quarter.

And what we have tried to protect very diligently, and I commented on this in the script as well, is our engineering capability and our ability to respond pretty quickly. So when I say what we can take advantage of the recovery and leverage the recovery well, when it does come? Part of it's around our response capability. But we have taken enough fixed cost out of this business in 2015 and 2016 that the incrementals on a volume increase are going to be rather impressive.

Shannon O'Callaghan - *UBS - Analyst*

Okay. Thanks a lot, guys. Appreciate it.

Operator

(Operator Instructions)

Steve Tusa, JPMorgan.

Stephen Tusa - *JPMorgan - Analyst*

Hi, guys good morning. Just I guess, you know, a lot of numbers floating around here. For the second quarter, you guys, I think, you know, the numbers have changed a bit, but last year I think it was up, you know, EPS-wise 30% to 35% from first quarter to second quarter? I'm not even sure what number we're using. Like let's just use, I guess the \$0.52 number, or maybe like a \$0.55 to \$0.60 number, because there's a lot of moving parts here.

But is second quarter going to be, you know, better sequentially than last year, or because of the Energy dynamics, although a small impact now, or worse than it was last year seasonally? What's kind of the seasonal color when you kind of mix this all in for the second quarter?

Bob Livingston - *Dover Corporation - President & CEO*

Oh, wow. Okay. I understand the question. I haven't done that calculation, Steve. The --

Stephen Tusa - *JPMorgan - Analyst*

Well, it's just a question of if you have a view on, if you know what the second quarter is, what is that, you know, roughly year-over-year versus the first quarter? That's kind of the baseline question.

Bob Livingston - *Dover Corporation - President & CEO*

And I actually don't have the detail in front of me, Steve. I'm taking a guess to even try to answer that.

Paul Goldberg - *Dover Corporation - VP of IR*

Yes, Steve, it's Paul. I would just say that the three segments, Engineered Systems, Fluids, and Refrigeration and Food Equipment are clearly going to be improved sequentially second quarter over first quarter. Bob said Energy is going to be down 10% sequentially, so the EPS in the second quarter is going to be substantially above where we are in the first quarter, but you know, we don't give second quarter guidance.

Stephen Tusa - *JPMorgan - Analyst*

Okay. And I guess you guys talked about the Energy margin. I assume the Energy margin given the revenue declines and you talked mostly about the back half weighting some of this restructuring coming through, et cetera, I assume the Energy margin's going to be down in the second quarter?

Bob Livingston - *Dover Corporation - President & CEO*

All in, I'm not sure that's true, Steve, all in in the first quarter, including, when I say all in, including restructuring charges, I think margins were 4%, 4.1%, something like that? We actually do start to get some benefits in the second quarter from those restructuring activities that were for the most part absent in the first quarter because, Steve, most of the restructuring we took in Energy in the first quarter occurred in March.

Stephen Tusa - *JPMorgan - Analyst*

Okay and then one last question just on the --

Bob Livingston - *Dover Corporation - President & CEO*

I actually expect margins in the second quarter in Energy to be a bit better than the first.

Brad Cerepak - *Dover Corporation - SVP & CFO*

We actually took out 366 heads in the first quarter in Energy.

Bob Livingston - *Dover Corporation - President & CEO*

And most of them left in March. So you'll see that impacted into the second quarter.

Stephen Tusa - *JPMorgan - Analyst*

Okay. An then in Energy, just a followup to Nigel's question, I think what he was trying to get at was not necessarily the margins but just the cyclicity of the business.

Is there any part of that business, maybe drilling, perhaps, that's going to be a little more challenged, you know, over the next couple years? Any parts of those businesses that are up for strategic review and potential divestiture? Obviously you're not going to do the whole segment, but are there any parts of that drilling specifically that you'd evaluate as being strategic or nonstrategic for the longer term?

Bob Livingston - *Dover Corporation - President & CEO*

Good question, and it's something we look at, it's something we look at every year, not just on Energy, but beyond that I'm not going to comment.

Stephen Tusa - *JPMorgan - Analyst*

Okay. Thanks a lot.



Operator

Andrew Kaplowitz, Citigroup.

Andrew Kaplowitz - Citigroup - Analyst

Hey, good morning, guys. So I'm trying to reconcile the EPS effects of acquisitions in 2016. You have \$0.16 to \$0.17 for the year. You know you talked about this a little bit in the prepared remarks. But you had \$0.18 last quarter but your numbers now include a \$0.07 gain from the disposition, and then of course it also includes the earnings from the disposition or the loss of earnings.

So can you talk about, how are your acquisitions trending? I know it's early, but are they lower than you thought in terms of EPS contribution, or the same, or maybe a little more color there?

Brad Cerepak - Dover Corporation - SVP & CFO

Sure. So you're right. In the last forecast we had roughly \$0.18 from acquisition accretion. Where we stand today in our forecast, we're at \$0.19, so roughly it's the same number, let's say it that way. So they're trending fine. You know, some are a little bit better --

Bob Livingston - Dover Corporation - President & CEO

One's up a penny, and one's flat.

Brad Cerepak - Dover Corporation - SVP & CFO

Yes, one is up a penny, one's flat. So it's not big changes, you know, pretty consistent from our last forecast. And then, you know, the way you reconcile it, you get, you take out the gain to your point, and you add, you'll also have to, you add back the gain and then you subtract out the lost revenue and earnings of the disposition, and that's about \$0.09 or so.

Andrew Kaplowitz - Citigroup - Analyst

Okay. That's helpful. And, Bob, maybe I can ask you specifically about the Fluid transfer business. You know, if I look at that business, it did, it turned down a little bit. You mentioned oil and gas, you mentioned lower CapEx spending. You didn't specifically talk about OPW, that seems fine, but maybe just a little more color on that business. What turned down in that business?

Bob Livingston - Dover Corporation - President & CEO

Yes. OPW first quarter was lighter than we expected, and in the first quarter the softness was almost all, not entirely, but almost all in the retail area. Activity in Canada on retail fueling was significantly below expectations, and even our experience last year, thus the comm -- part of the reason why I had to comment on the integrated energy [company's] lease.

Those are some of our customers in Canada, but we also saw some project timing push outs from the first quarter to second and third from some US retail customers, who are pushing out some rebuild projects.

Andrew Kaplowitz - Citigroup - Analyst

So, Bob, how do we look at OPW for the rest of the year then, or how do you look at it?

Bob Livingston - *Dover Corporation - President & CEO*

I would say for the rest of the year our expectation is it's going to be less of a, I call it a negative year-over-year comp in the second quarter, and we're actually feeling fairly positive about the second half of the year.

Andrew Kaplowitz - *Citigroup - Analyst*

Okay. Thank you.

Operator

Deane Dray, RBC.

Deane Dray - *RBC Capital Markets - Analyst*

Thanks. Good morning, everyone. Hey, Bob, hope you give us some color in Refrigeration, those retail wins you had in the quarter, and how does that compare to any sort of seasonal expectations?

Bob Livingston - *Dover Corporation - President & CEO*

Are you asking me for the customer names? I'm not going to do that.

Deane Dray - *RBC Capital Markets - Analyst*

I did not ask for customer names, but some color as to what kind of customers or what kind of products.

Bob Livingston - *Dover Corporation - President & CEO*

For those of you who recall our comments in the first half of last year around Refrigeration, what we're seeing here in the fourth quarter and the first quarter was actually what we were expecting to see in the second quarter of last year. It just took us longer to get to this point.

As you know, we did take a significant drop down, step down in the Wal-Mart business, and the efforts by the leadership team and the sales organization at Hillphoenix has just been outstanding over the past year to deal with this shortfall, and they're covering it. They're covering it, Deane. They've done a really good job. In fact, I would say that the organic growth for the segment in the first quarter of just slightly above 3% was actually about a point better than we expected coming into the year.

And all of that upside was out of our Refrigeration business primarily, but not all, but primarily Hillphoenix. And we feel very, very good with the factory load we have right now for the seasonally-strong second quarter, and the teams are working pretty feverishly in making sure that we can make that same comment as we enter the third quarter. But we actually feel pretty positive right now about this seasonal load that we're looking at here in the second and third quarter.

Deane Dray - *RBC Capital Markets - Analyst*

Just to clarify, so on that filling the Wal-Mart hole, these wins you had here, they were new customers, and that would be considered part of that initiative that you talked about last year about --



Bob Livingston - *Dover Corporation - President & CEO*

Well no, it's not all new customers, Deane. There's a handful of new customers in there, a single handful, but some of it is just winning a larger share.

Deane Dray - *RBC Capital Markets - Analyst*

Got it. And then just a clarification on --

Bob Livingston - *Dover Corporation - President & CEO*

I will add one other color point here. Wal-Mart activity is still not where we would expect it to be, even in the remodel activity, the first few weeks of the year were actually pretty modest compared to our expectations.

March was sort of back on track, but this is a bit of a different year for Wal-Mart with respect to communication to at least us and to other suppliers that we're aware of, is that they have not announced to their supply base a detailed rollout of remodel activity for 2016. It's sort of being done a month or two at a time.(multiple speakers)

Deane Dray - *RBC Capital Markets - Analyst*

Got it. And then just to clarify on the incremental restructuring that you've announced today, what's the implied payback, and you called out the shared service centers a couple times. Is that a permanent change and how does that contribute on the cost equation?

Bob Livingston - *Dover Corporation - President & CEO*

So I'm going to have to go to Brad on the payback.

Brad Cerepak - *Dover Corporation - SVP & CFO*

Well, on the restructuring, so let's cover that for a moment. We said incremental \$20 million for a total of \$40 million. So if you think about what we had in terms of benefits in our last forecast to where we are today, the benefits on a \$20 million incremental spend is up \$50 million. I know that sounds like a big number, but in that \$50 million, I would say 50% of that is right sizing manufacturing, so that's hourly work force, variable costs. And the other 50% is what I would attribute to structural type of cost takeout, and so that's what we have in our forecast.

So, again, some of the, you'll see the footnote on one of the charts, that \$100 million now in the aggregate includes, we include all in, when we say the head counts are down 366 heads, that's also manufacturing and, you know, management and overhead-type layers as well.

Deane Dray - *RBC Capital Markets - Analyst*

And the shared service is part of the structural change?\

Bob Livingston - *Dover Corporation - President & CEO*

Well, yes and no. I mean, it's not part of a restructuring activity per se, but it is surely a structural change that we're pursuing here at Dover. We've been running pilot programs for two full years now, and this year we sort of announced here internally a couple of months ago the rollout of the

shared service approach around Dover. And it's more than just back office, it encompasses some activity around HR, some activity around finance and accounting, but it's more than just accounts payable and accounts receivable process. I think it's much more extensive than that.

And I think, actually, by the time we get to year end 2016, we'll have one segment pretty much fully transitioned to the shared service approach, and the other three, perhaps 30% to 50% transitioned to the shared surface platform. We're not -- and our guide has actually no benefits, no net benefits in our guide this year from the shared service rollout. We've got some spending and some investment that we're making this year. We are seeing some benefits, but it's not going to be a net benefit. We'll actually start to see the net benefits of this program in 2017 and 2018.

Deane Dray - *RBC Capital Markets - Analyst*

Thank you.

Operator

Joseph Ritchie, Goldman Sachs.

Joseph Ritchie - *Goldman Sachs - Analyst*

Thanks. Good morning, guys, and thanks for fitting me in. Maybe just following on that payback question. I think the genesis of the question is the fact when you take a look at your payback and what you're spending from a restructuring standpoint, it looks pretty, like really good payback relative to what other industrial companies are seeing.

So I guess maybe the question is, one, what gives you the confidence that you can get that payback, and secondly, you know, are there any obstacles that you see as you're rolling out your restructuring programs that would potentially inhibit you from seeing that same type of benefit?

Bob Livingston - *Dover Corporation - President & CEO*

Well, okay. So first off, all restructuring activity is not the same. The bulk of, not all, but the bulk of the restructuring activity we've had in Energy, both last year, 2015, as well as the first half of this year has been people related, and, my goodness, Brad, can I say almost 100% domestic? Well, maybe almost 100% North America for sure, okay? And, Joe, the payback on that is pretty high, pretty quick.

When you peel off the labor restructuring, the work force restructuring, you look at some of the fixed costs or facility consolidations we did last year and are doing again this year, in a weighting perspective, they're pretty minor compared to the benefits we're getting from the work force reduction. And the payback is longer, probably more in line with what you're referring to here when you look at the facility consolidations that we've done. But, again, most of the workforce reduction last year and this year has been North America.

Joseph Ritchie - *Goldman Sachs - Analyst*

Okay. Okay. So I guess the confidence, said another way, your confidence is pretty high in getting this benefit the rest of the year. Okay. And then maybe one follow-on question --

Bob Livingston - *Dover Corporation - President & CEO*

To give you a very discrete example, Brad mentioned that in Energy in the first quarter, work force was reduced by 366. They're either here or not, and when they're not, we know what the benefits are. I mean, it is a pretty high comfort on that.



Joseph Ritchie - *Goldman Sachs - Analyst*

Okay. All right. Fair enough. And then I guess the follow-on question there is really, since maybe focused on Energy for a second, I remember several quarters ago we talked about additional restructuring actions potentially impacting your service levels and yet, you know, we've seen additional restructuring actions that have needed to be taken on the Energy side of your business.

I guess I'm curious, you know, how are you managing that piece of your business to make sure that service levels aren't interrupted if and when we do see a recovery?

Bob Livingston - *Dover Corporation - President & CEO*

So I commented both in the script and in an earlier response, we've done as good of a job as we can to holding our engineering capability. In fact, I would say last year in 2015 we actually added resources in engineering.

The 2016 we have tweaked a bit around the edges on our service response, but we've done it in a way that we know we've got flexibility to move resources around to handle customer demands today, tomorrow, and hopefully here, whether it's the second half of this year or next year when we start to see a little bit of a recovery.

But we have tried very diligently to protect our response time, even though we have been sort of trimming in the margins. To that point, Joe, I'm going to tell you, I don't see a lot more flexibility in the second half of this year or even going into next year about restructuring activity at Energy that's in line with what we've done in the second half of last year or in the first quarter or the second quarter of this year.

You know, if there's further revenue declines, I think we can all be [discern] opportunities sort of at the margin, but I'm just being very up front with you. I do not see the opportunity to take another \$30 million of cost out of Energy in the second half of this year, even if we see a little bit of a decline in revenue.

Joseph Ritchie - *Goldman Sachs - Analyst*

Okay. That's helpful. Thanks, Bob.

Operator

Thank you. That concludes our question and answer period. I would now like to turn the call back over to Mr. Goldberg for closing remarks.

Paul Goldberg - *Dover Corporation - VP of IR*

Thank you very much. We'd just like to thank everybody for their continued interest in Dover and we look forward to speaking to you again next quarter. Have a good day. Thank you. Bye.

Operator

Thank you. That concludes today's first quarter 2016 Dover earnings conference call. You may now disconnect your lines at this time, and have a wonderful day.



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