FLOWSERVE CORP
Form 10-Q
April 30, 2015

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

FORM 10-Q
(Mark One)

þ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2015

OR

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

Commission File No. 1-13179

FLOWSERVE CORPORATION
(Exact name of registrant as specified in its charter)

New York	31-0267900
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
5215 N. O’Connor Blvd., Suite 2300, Irving, Texas	75039
(Address of principal executive offices)	(Zip Code)

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

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

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

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

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

Smaller reporting company ¨

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

As of April 23, 2015, there were 134,450,872 shares of the issuer’s common stock outstanding.

FLOWSERVE CORPORATION
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PART I — FINANCIAL INFORMATION

Item 1. Financial Statements.

FLOWSERVE CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

(Amounts in thousands, except per share data)	Three Months Ended March 31,	
	2015	2014
Sales	$1,014,620	$1,068,136
Cost of sales	(682,890)	(691,014)
Gross profit	331,730	377,122
Selling, general and administrative expense	(239,927)	(216,227)
Net earnings from affiliates	1,573	3,431
Operating income	93,376	164,326
Interest expense	(16,037)	(15,149)
Interest income	758	331
Other expense, net	(19,946)	(2,905)
Earnings before income taxes	58,151	146,603
Provision for income taxes	(28,506)	(38,015)
Net earnings, including noncontrolling interests	29,645	108,588
Less: Net earnings attributable to noncontrolling interests	(1,979)	(854)
Net earnings attributable to Flowserve Corporation	$27,666	$107,734
Net earnings per share attributable to Flowserve Corporation common shareholders:		
Basic	$0.21	$0.78
Diluted	0.20	0.78
Cash dividends declared per share	$0.18	$0.16

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

(Amounts in thousands)	Three Months Ended March 31,	
	2015	2014
Net earnings, including noncontrolling interests	$29,645	$108,588
Other comprehensive (loss) income		
Foreign currency translation adjustments, net of taxes of $63,561 and $(1,786), respectively	(106,434)	2,951
Pension and other postretirement effects, net of taxes of $1,692 and $(938), respectively	7,891	2,779
Cash flow hedging activity, net of taxes of $2,027 and $(71), respectively	(5,146)	168
Other comprehensive (loss) income	(103,689)	5,898
Comprehensive (loss) income, including noncontrolling interests	(74,044)	114,486
Comprehensive loss attributable to noncontrolling interests	(1,997)	(1,030)
Comprehensive (loss) income attributable to Flowserve Corporation	$(76,041)	$113,456

See accompanying notes to condensed consolidated financial statements.

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FLOWSERVE CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

(Amounts in thousands, except par value)	March 31, 2015	December 31, 2014
ASSETS		
Current assets:		
Cash and cash equivalents	$333,776	$450,350
Accounts receivable, net of allowance for doubtful accounts of $27,125 and $25,469, respectively	1,015,544	1,082,447
Inventories, net	1,118,940	995,564
Deferred taxes	158,803	158,912
Prepaid expenses and other	133,275	106,890
Total current assets	2,760,338	2,794,163
Property, plant and equipment, net of accumulated depreciation of $813,562 and $836,981, respectively	752,015	693,881
Goodwill	1,214,919	1,067,255
Deferred taxes	27,840	31,419
Other intangible assets, net	247,550	146,337
Other assets, net	249,019	234,965
Total assets	$5,251,681	$4,968,020
LIABILITIES AND EQUITY		
Current liabilities:		
Accounts payable	$484,542	$611,715
Accrued liabilities	783,758	794,072
Debt due within one year	58,739	53,131
Deferred taxes	13,727	12,957
Total current liabilities	1,340,766	1,471,875
Long-term debt due after one year	1,620,782	1,101,791
Retirement obligations and other liabilities	525,991	452,511
Shareholders' equity:		
Common shares, $1.25 par value	220,991	220,991
Shares authorized – 305,000		
Shares issued – 176,793		
Capital in excess of par value	471,516	495,600
Retained earnings	3,418,920	3,415,738
Treasury shares, at cost – 43,136 and 42,444 shares, respectively	(1,885,594)	(1,830,919)
Deferred compensation obligation	10,145	10,558
Accumulated other comprehensive loss	(484,114)	(380,406)
Total Flowserve Corporation shareholders' equity	1,751,864	1,931,562
Noncontrolling interests	12,278	10,281
Total equity	1,764,142	1,941,843
Total liabilities and equity	$5,251,681	$4,968,020

See accompanying notes to condensed consolidated financial statements.

FLOWSERVE CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

(Amounts in thousands)	Three Months Ended March 31,	
	2015	2014
Cash flows – Operating activities:		
Net earnings, including noncontrolling interests	$29,645	$108,588
Adjustments to reconcile net earnings to net cash used by operating activities:		
Depreciation	24,600	23,058
Amortization of intangible and other assets	9,244	4,305
Gain on sale of business	—	(13,403)
Excess tax benefits from stock-based payment arrangements	(5,800)	(8,353)
Stock-based compensation	9,095	9,916
Foreign currency and other non-cash adjustments	28,539	7,541
Change in assets and liabilities, net of acquisitions		
Accounts receivable, net	59,396	77,264
Inventories, net	(117,848)	(76,990)
Prepaid expenses and other	(22,781)	(6,897)
Other assets, net	(2,330)	4,025
Accounts payable	(131,208)	(132,503)
Accrued liabilities and income taxes payable	2,698	(77,552)
Retirement obligations and other	14,432	(4,437)
Net deferred taxes	9,117	773
Net cash flows used by operating activities	(93,201)	(84,665)
Cash flows – Investing activities:		
Capital expenditures	(83,967)	(31,663)
Payments for acquisition, net of cash acquired	(341,545)	—
Proceeds from disposal of assets	1,649	301
Proceeds from sale of business, net of cash divested	—	46,805
Net cash flows (used) provided by investing activities	(423,863)	15,443
Cash flows – Financing activities:		
Excess tax benefits from stock-based payment arrangements	5,800	8,353
Payments on long-term debt	(10,000)	(10,000)
Proceeds from issuance of senior notes	523,418	—
Payments of deferred loan cost	(1,005)	—
Proceeds under other financing arrangements	7,190	3,288
Payments under other financing arrangements	(5,207)	(1,479)
Repurchases of common shares	(79,899)	(109,605)
Payments of dividends	(21,686)	(19,387)
Other	264	(385)
Net cash flows provided (used) by financing activities	418,875	(129,215)
Effect of exchange rate changes on cash	(18,385)	(951)
Net change in cash and cash equivalents	(116,574)	(199,388)
Cash and cash equivalents at beginning of period	450,350	363,804
Cash and cash equivalents at end of period	$333,776	$164,416

See accompanying notes to condensed consolidated financial statements.

FLOWSERVE CORPORATION
(Unaudited)
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation and Accounting Policies

Basis of Presentation

The accompanying condensed consolidated balance sheet as of March 31, 2015, the related condensed consolidated statements of income and comprehensive income for the three months ended March 31, 2015 and 2014, and the condensed consolidated statements of cash flows for the three months ended March 31, 2015 and 2014, of Flowserve Corporation are unaudited. In management’s opinion, all adjustments comprising normal recurring adjustments necessary for fair statement of such condensed consolidated financial statements have been made.

The accompanying condensed consolidated financial statements and notes in this Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2015 ("Quarterly Report") are presented as permitted by Regulation S-X and do not contain certain information included in our annual financial statements and notes thereto. Accordingly, the accompanying condensed consolidated financial information should be read in conjunction with the consolidated financial statements presented in our audited Annual Report on Form 10-K for the year ended December 31, 2014 ("2014 Annual Report").

Venezuela – Our operations in Venezuela generally consist of a service center that performs service and repair activities. Our Venezuelan subsidiary's sales for the three months ended March 31, 2015 represented less than 1% of consolidated sales and its assets at March 31, 2015 represented less than 0.5% of total consolidated assets. Assets primarily consisted of United States ("U.S.") dollar-denominated monetary assets and bolivar-denominated non-monetary assets at March 31, 2015. In addition, certain of our operations in other countries sell equipment and parts that are typically denominated in U.S. dollars directly to Venezuelan customers.

We have experienced delays in collecting payment on our accounts receivable from the national oil company in Venezuela, our primary Venezuelan customer. These accounts receivable are primarily U.S. dollar-denominated and are not disputed, and we have not historically had write-offs relating to this customer. Our total outstanding accounts receivable with this customer were approximately 9% of our gross accounts receivable at March 31, 2015. Given the experienced delays in collecting payments we estimate that approximately 50% of the outstanding accounts receivable will most likely not be collected within one year and therefore has been classified as long-term within other assets, net on our March 31, 2015 condensed consolidated balance sheet.

In the first quarter of 2014, the Venezuelan government expanded the use of periodic auctions for U.S. dollars conducted under the Complementary System of Foreign Currency Administration ("SICAD I"). At March 31, 2015 the SICAD I exchange rate was 12.0 bolivars to the U.S. dollar, compared with the official exchange rate of 6.3 bolivars to the U.S. dollar ("Official"). In addition, during the second quarter of 2014 the Venezuelan government created a third currency exchange mechanism ("SICAD II"). In February 2015, the Venezuelan government created a new currency exchange mechanism, SIMADI, which replaced the SICAD II mechanism. At March 31, 2015, the SIMADI exchange rate was 192 bolivars to the U.S. dollar.

As of March 31, 2015, we have determined, based on our specific facts and circumstances, that the SIMADI exchange rate was the most appropriate for the remeasurement of our Venezuelan subsidiary's bolivar-denominated net monetary assets in U.S. dollars. As a result of the remeasurement we recognized a loss of $20.6 million during the three months ended March 31, 2015, of which $18.5 million was reported in other expense, net and $2.1 million in cost of goods sold in our condensed consolidated statement of income and resulted in no tax benefit.

We are continuing to assess and monitor the ongoing impact of the changes in the Venezuelan foreign exchange market on our Venezuelan operations and imports into the market, including our Venezuelan subsidiary's ability to remit cash for dividends and other payments at the SIMADI exchange rate, as well as additional government actions, political and labor unrest, or other economic conditions that may adversely impact our future consolidated financial condition or results of operations.

Accounting Policies

Significant accounting policies, for which no significant changes have occurred in the three months ended March 31, 2015, are detailed in Note 1 to our consolidated financial statements included in our 2014 Annual Report.

Accounting Developments

Pronouncements Implemented

In June 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-11 "Transfers and Servicing (Topic 860): Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures." This ASU

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changes the accounting for repurchase-to-maturity transactions and linked repurchase financings so that such transactions will now be accounted for as secured borrowings. This accounting change is effective for the first interim or annual period beginning after December 15, 2014 and early adoption is not permitted. There are also new disclosure requirements in this ASU. Our adoption of ASU No. 2014-11 did not have an impact on our consolidated financial condition and results of operations.

Pronouncements Not Yet Implemented

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers (Topic 606)" which supersedes the revenue recognition requirements in "Revenue Recognition (Topic 605)." The standard is principle-based and provides a five-step model to determine when and how revenue is recognized. The core principle is that a company should recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. There are also expanded disclosure requirements in this ASU. For public entities ASU 2014-09 is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period and allows for either full retrospective adoption or modified retrospective adoption. We are currently evaluating the impact of ASU No. 2014-09 on our consolidated financial condition and results of operations.

In June 2014, the FASB issued ASU No. 2014-12 "Compensation-Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period." This ASU was issued to address share-based payment awards with a performance target affecting vesting that could be achieved after the employee’s requisite service period. This ASU is effective for annual periods and interim periods within those annual periods beginning after December 15, 2015. This ASU may be applied either (a) prospectively to all awards granted or modified after the effective date or (b) retrospectively to all awards with performance targets that are outstanding as of the beginning of the earliest annual period presented in the financial statements and to all new or modified awards thereafter. The adoption of ASU No. 2014-12 is not expected to have a material impact on our consolidated financial condition and results of operations.

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

In November 2014, the FASB issued ASU 2015-01, “Income Statement-Extraordinary and Unusual Items (Subtopic 225-20): Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items.” In connection with the FASB's efforts to simplify accounting standards, the FASB released new guidance on simplifying Income Statement presentation by eliminating the concept of extraordinary items from U.S. GAAP. With the issuance of this ASU the FASB determined that the elimination of the concept of extraordinary items from U.S. GAAP would reduce the cost and complexity on the application of accounting standards, while maintaining or improving the usefulness of information included in financial statements. The adoption of ASU No. 2015-01 is not expected to have an impact on our consolidated financial condition and results of operations.

In February 2015, the FASB issued ASU No. 2015-02, "Consolidation (Topic 810) - Amendments to the Consolidation Analysis,” which provides guidance on the analysis process companies must perform in order to determine whether a legal entity should be consolidated. The new ASU simplifies U.S. GAAP by eliminating entity specific consolidation guidance for limited partnerships. It also revises other aspects of the consolidation analysis, to include the ownership assessment of variable interest entities (VIEs), fee arrangements and how related parties are assessed. The amendments rescind the indefinite deferral of FASB Statement 167, Amendments to FASB Interpretation No. 46(R), for certain investment funds and replace it with a permanent scope exception for money market funds. ASU 2015-02 is effective for periods beginning after December 15, 2015. Early adoption is permitted, including adoption in an interim period. We are currently evaluating the impact of ASU No. 2015-02 on our consolidated financial condition and results of operations.

In April 2015, the FASB issued ASU No. 2015-03, "Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs.” The ASU was issued in connection with the FASB's efforts to simplify accounting standards for the presentation of debt issuance costs. The amendments of this ASU require companies to present debt issuance costs the same manner that present debt discounts are currently reported, as a direct deduction from the carrying value of that debt liability. The applicability of this requirement does not impact the recognition and measurement guidance for debt issuance costs. ASU 2015-03 is effective for periods beginning after December 15, 2015. Early adoption is allowed for financial statements that have yet to be issued. The adoption of ASU No. 2015-03 is not expected to have a material impact on our consolidated financial condition and results of operations.

2. Acquisition and Disposition

SIHI Group B.V.

Effective January 7, 2015, we acquired for inclusion in Industrial Product Division ("IPD"), 100% of SIHI Group B.V. ("SIHI"), a global provider of engineered vacuum and fluid pumps and related services, primarily servicing the chemical market, as well as the pharmaceutical, food & beverage and other process industries, in a stock purchase for €286.7 million ($341.5 million based on exchange rates in effect at the time the acquisition closed and net of cash acquired) in cash. The acquisition was funded using approximately $110 million in available cash and approximately $255 million in initial borrowings from our Revolving Credit Facility, which was subsequently paid down with a portion of the net proceeds from our 2022 EUR Senior Notes discussed in Note 5. SIHI, based in the Netherlands, has operations primarily in Europe and, to a lesser extent, the Americas and Asia.

The fair value of assets acquired and liabilities assumed has been recorded on a preliminary basis. We will continue to evaluate the initial fair values, which may be adjusted as additional information relative to the fair values of the assets and liabilities becomes available. We currently do not anticipate material adjustments in future periods. The preliminary allocation of the purchase price is summarized below:

	(Amounts in millions)
Accounts receivable	$56.2
Inventories	74.0
Prepaid expenses and other	17.2
Total current assets	147.4
Intangible assets	
Trademarks	20.9
Existing customer relationships	45.3
Backlog	8.5
Engineering drawings and other	3.9
Total intangible assets	78.6
Property, plant and equipment	87.5
Long-term deferred tax asset	10.7
Investments in affiliates	11.6
Total assets	335.8
Current liabilities	(87.0)
Noncurrent liabilities	(101.7)
Net assets	147.1
Goodwill	194.4
Purchase price, net of cash acquired of $23.4 million	$341.5

The excess of the acquisition date fair value of the total purchase price over the estimated fair value of the net assets was recorded as goodwill. Goodwill of $194.4 million represents the value expected to be obtained from strengthening Flowserve’s portfolio of products and services through the addition of SIHI's engineered vacuum and fluid pumps, as well as the associated aftermarket services and parts. The goodwill related to this acquisition is recorded in the IPD segment and is not expected to be deductible for tax purposes. The trademarks are primarily indefinite-lived intangibles. Existing customer relationships, engineering drawings and backlog have expected weighted average useful lives of 10 years, 10 years and less than one year, respectively. In total, amortizable intangible assets have a weighted average useful live of approximately 9 years.

Subsequent to January 7, 2015, the revenues and expenses of SIHI have been included in our condensed consolidated statement of income. The SIHI acquisition generated sales of approximately $67 million for the three months ended March 31, 2015 and decreased earnings by approximately $24 million, including $5.0 million in acquisition-related costs. SIHI's sales (unaudited) were approximately €270 million during its fiscal year ended November 30, 2014. No proforma financial information has been presented due to immateriality.

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Naval OY

Effective March 31, 2014, we sold our Flow Control Division's ("FCD") Naval OY ("Naval") business to a Finnish valve manufacturer. The sale included Naval's manufacturing facility located in Laitila, Finland and a service and support center located in St. Petersburg, Russia. The cash proceeds for the sale totaled $46.8 million, net of cash divested, and resulted in a $13.4 million pre-tax gain recorded in selling, general and administrative expense in the condensed consolidated statements of income. Net sales related to the Naval business totaled $8.2 million in the first quarter of 2014.

3. Stock-Based Compensation Plans

We maintain the Flowserve Corporation Equity and Incentive Compensation Plan (the "2010 Plan"), which is a shareholder-approved plan authorizing the issuance of up to 8,700,000 shares of our common stock in the form of restricted shares, restricted share units and performance-based units (collectively referred to as "Restricted Shares"), incentive stock options, non-statutory stock options, stock appreciation rights and bonus stock. Of the 8,700,000 shares of common stock authorized under the 2010 Plan, 4,310,368 were available for issuance as of March 31, 2015. The Flowserve Corporation 2004 Stock Compensation Plan expired on June 22, 2014, with 827,835 shares unissued. No stock options have been granted since 2006.

Restricted Shares – Awards of Restricted Shares are valued at the closing market price of our common stock on the date of grant. The unearned compensation is amortized to compensation expense over the vesting period of the restricted shares. We had unearned compensation of $49.5 million and $30.6 million at March 31, 2015 and December 31, 2014, respectively, which is expected to be recognized over a weighted-average period of approximately two years. These amounts will be recognized into net earnings in prospective periods as the awards vest. The total fair value of Restricted Shares vested during the three months ended March 31, 2015 and 2014 was $37.8 million and $32.9 million, respectively.

We recorded stock-based compensation expense of $6.0 million ($9.1 million pre-tax) and $6.5 million ($9.9 million pre-tax) for the three months ended March 31, 2015 and 2014, respectively.

The following table summarizes information regarding Restricted Shares:

	Three Months Ended March 31, 2015	
	Shares	Weighted Average Grant-Date Fair Value
Number of unvested shares:		
Outstanding - January 1, 2015	1,856,548	$52.29
Granted	570,193	56.07
Vested	(892,407)	42.31
Canceled	(71,277)	60.62
Outstanding - March 31, 2015	1,463,057	$59.44

Unvested Restricted Shares outstanding as of March 31, 2015, includes approximately 744,000 units with performance-based vesting provisions. Performance-based units are issuable in common stock and vest upon the achievement of pre-defined performance targets, primarily based on our average annual return on net assets over a three-year period as compared with the same measure for a defined peer group for the same period. Most units were granted in three annual grants since January 1, 2013 and have a vesting percentage between 0% and 200% depending on the achievement of the specific performance targets. Compensation expense is recognized ratably over a cliff-vesting period of 36 months, based on the fair market value of our common stock on the date of grant, as adjusted for anticipated forfeitures. During the performance period, earned and unearned compensation expense is adjusted based on changes in the expected achievement of the performance targets. Vesting provisions range from 0 to approximately 1,444,000 shares based on performance targets. As of March 31, 2015, we estimate vesting of approximately 909,000 shares based on expected achievement of performance targets.

4. Derivative Instruments and Hedges

Our risk management and foreign currency derivatives and hedging policy specifies the conditions under which we may enter into derivative contracts. See Notes 1 and 6 to our consolidated financial statements included in our 2014

Annual Report and Note 6 of this Quarterly Report for additional information on our derivatives. We enter into foreign exchange forward and swap contracts to hedge our cash flow risks associated with transactions denominated in currencies other than the local currency of the operation engaging in the transaction. All designated foreign exchange hedging instruments are highly effective as of March 31, 2015.

Foreign exchange contracts designated as hedging instruments had a notional value of $81.0 million and $125.9 million, at March 31, 2015 and December 31, 2014, respectively. Foreign exchange contracts with third parties not designated as hedging instruments had a notional value of $498.9 million and $421.1 million, at March 31, 2015 and December 31, 2014, respectively. At March 31, 2015, the length of foreign exchange contracts currently in place ranged from two days to 34 months.

Also as part of our risk management program, we enter into interest rate swap agreements to hedge exposure to floating interest rates on certain portions of our debt. At March 31, 2015 and December 31, 2014, we had $25.0 million and $40.0 million, respectively, of notional amount in outstanding interest rate swaps with third parties. All interest rate swaps are highly effective. At March 31, 2015, the maximum remaining length of any interest rate swap contract in place was approximately 3 months.

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

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

(Amounts in thousands)	March 31, 2015	December 31, 2014
Current derivative assets	$21,534	$11,709
Noncurrent derivative assets	15	6
Current derivative liabilities	15,212	6,168
Noncurrent derivative liabilities	435	348

The fair value of interest rate swaps and foreign exchange contracts designated as hedging instruments are summarized below:

(Amounts in thousands)	March 31, 2015	December 31, 2014
Current derivative liabilities	$10,674	$6,952
Noncurrent derivative liabilities	846	411

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

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

	Three Months Ended March 31,	
(Amounts in thousands)	2015	2014
Gain recognized in income	$25,080	$1,544

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

The impact of net changes in the fair values of interest rate swaps in cash flow hedging relationships are immaterial for disclosures purposes.

In March 2015, we designated €255.7 million of our €500.0 million Euro senior notes discussed in Note 5 as a net investment hedge of our investments in certain of our international subsidiaries that use the Euro as their functional currency. We used the spot method to measure the effectiveness of our net investment hedge. Under this method, for each reporting period, the change in the carrying value of the Euro senior notes due to remeasurement of the effective portion is reported in accumulated other comprehensive loss on our condensed consolidated balance sheet and the remaining change in the carrying value of the ineffective portion, if any, is recognized in other expense, net in our condensed statement of income. We evaluate the effectiveness of our net investment hedge on a prospective basis at the beginning of each quarter. We did not record any ineffectiveness for the three months ended March 31, 2015.

5. Debt

Debt, including capital lease obligations, consisted of:

(Amounts in thousands, except percentages)	March 31, 2015	December 31, 2014
1.25% EUR Senior Notes due March 17, 2022, net of unamortized discount	$532,957	$—
4.00% USD Senior Notes due November 15, 2023, net of unamortized discount	298,761	298,731
3.50% USD Senior Notes due September 15, 2022, net of unamortized discount	498,503	498,460
Term Loan Facility, interest rate of 1.52% at March 31, 2015 and 1.51% at December 31, 2014	320,000	330,000
Capital lease obligations and other borrowings	29,300	27,731
Debt and capital lease obligations	1,679,521	1,154,922
Less amounts due within one year	58,739	53,131
Total debt due after one year	$1,620,782	$1,101,791

Senior Notes

On March 17, 2015, we completed a public offering of €500.0 million of Euro senior notes in aggregate principal amount due March 17, 2022 ("2022 EUR Senior Notes"). The 2022 EUR Senior Notes bear an interest rate of 1.25% per year, payable each year on March 17, commencing on March 17, 2016. The 2022 EUR Senior Notes were priced at 99.336% of par value, reflecting a discount to the aggregate principal amount. The net proceeds of the offering were €494.0 million ($523.4 million based on exchange rates in effect at the time the offering closed). We used a portion of the net proceeds of the 2022 EUR Senior Notes to ultimately fund the acquisition of SIHI described in Note 2 and anticipate utilizing the remaining portion for other general corporate purposes.

Senior Credit Facility

As discussed in Note 10 to our consolidated financial statements included in our 2014 Annual Report, on October 4, 2013 we amended our existing credit agreement that provided for a $400.0 million term loan (“Term Loan Facility”) and a $1.0 billion revolving credit facility (“Revolving Credit Facility” and, together with the Term Loan Facility, the “Senior Credit Facility”) with a maturity date of October 4, 2018. As of March 31, 2015 and December 31, 2014, we had no amounts outstanding under the Revolving Credit Facility. We had outstanding letters of credit of $78.9 million and $76.8 million at March 31, 2015 and December 31, 2014, respectively, which reduced our borrowing capacity to $921.1 million and $923.2 million, respectively. Our compliance with applicable financial covenants under the Senior Credit Facility is tested quarterly, and we complied with all covenants at March 31, 2015.

We may prepay loans under our Senior Credit Facility in whole or in part, without premium or penalty, at any time. A commitment fee, which is payable quarterly on the daily unused portions of the Senior Credit Facility, was 0.175% (per annum) during the period ended March 31, 2015. During the three months ended March 31, 2015, we made scheduled repayments of $10.0 million under our Term Loan Facility. We have scheduled repayments of $10.0 million due in the next two quarters, $15.0 million in the fourth quarter of 2015 and $15.0 million in the first quarter of 2016 on our Senior Credit Facility. Our Senior Credit Facility bears a floating rate of interest, and we have $25.0 million of notional amount of interest rate swaps at March 31, 2015 to hedge exposure to floating interest rates.

Our Senior Notes and Senior Credit Facility were fully and unconditionally and jointly and severally guaranteed by certain of our 100% owned domestic subsidiaries. Pursuant to the terms of the indentures governing the Senior Notes any guarantees on such debt were subject to release if the Company satisfactorily achieved and met the following guaranty release conditions: (a) obtains a ratings of BBB (stable outlook) or better from S&P and Baa2 (stable outlook) or better from Moody’s and (b) our domestic subsidiaries do not guarantee any material indebtedness. On February 27, 2015 Standard & Poor's Ratings Services raised its corporate credit and senior unsecured debt ratings rating on the Company to BBB from BBB-, with a stable outlook. As of March 11, 2015 Moody’s Investors Services' corporate credit and senior unsecured debt ratings rating on the Company was Baa2, with a stable outlook. As a result, the guarantees of the Senior Notes and Senior Credit Facility were released as of March 26, 2015 upon the discharge of the terms of the note indentures and Senior Credit Facility agreement; therefore, the Company is exempt from disclosing supplemental guarantor financial information in accordance with Rule 3-10 of Regulation S-X, promulgated under the Securities Act of 1933.

6. Fair Value

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

Our financial instruments are presented at fair value in our condensed consolidated balance sheets, with the exception of our long-term debt. The estimated fair value of our long-term debt, excluding the Senior Notes, approximates the carrying value and is classified as Level II under the fair value hierarchy. The carrying value of our debt is included in Note 5. The estimated fair value of our Senior Notes at March 31, 2015 was $1,345.4 million compared to the carrying value of $1,330.2 million. The estimated fair value of the Senior Notes is based on Level I quoted market rates. The carrying amounts of our other financial instruments (e.g., cash and cash equivalents, accounts receivable, net, accounts payable and short-term debt) approximated fair value due to their short-term nature at March 31, 2015 and December 31, 2014.

7. Inventories

Inventories, net consisted of the following:

(Amounts in thousands)	March 31, 2015	December 31, 2014
Raw materials	$427,937	$352,928
Work in process	748,713	687,343
Finished goods	265,807	265,439
Less: Progress billings	(245,418)	(230,058)
Less: Excess and obsolete reserve	(78,099)	(80,088)
Inventories, net	$1,118,940	$995,564

8. Earnings Per Share

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

	Three Months Ended March 31,	
(Amounts in thousands, except per share data)	2015	2014
Net earnings of Flowserve Corporation	$27,666	$107,734
Dividends on restricted shares not expected to vest	3	3
Earnings attributable to common and participating shareholders	$27,669	$107,737
Weighted average shares:		
Common stock	134,388	137,123
Participating securities	530	611
Denominator for basic earnings per common share	134,918	137,734
Effect of potentially dilutive securities	1,036	1,136
Denominator for diluted earnings per common share	135,954	138,870
Earnings per common share:		
Basic	$0.21	$0.78
Diluted	0.20	0.78

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

For the three months ended both March 31, 2015 and 2014, no options to purchase common stock were excluded from the computation of potentially dilutive securities.

9. Legal Matters and Contingencies

Asbestos-Related Claims

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

Our practice is to vigorously contest and resolve these claims, and we have been successful in resolving a majority of claims with little or no payment. Historically, a high percentage of resolved claims have been covered by applicable insurance or indemnities from other companies, and we believe that a substantial majority of existing claims should continue to be covered by insurance or indemnities. Accordingly, we have recorded a liability for our estimate of the most likely settlement of asserted claims and a related receivable from insurers or other companies for our estimated recovery, to the extent we believe that the amounts of recovery are probable and not otherwise in dispute. While unfavorable rulings, judgments or settlement terms regarding these claims could have a material adverse impact on our business, financial condition, results of operations and cash flows, we currently believe the likelihood is remote. Additionally, we have claims pending against certain insurers that, if resolved more favorably than reflected in the recorded receivables, would result in discrete gains in the applicable quarter. We are currently unable to estimate the impact, if any, of unasserted asbestos-related claims, although future claims would also be subject to then existing indemnities and insurance coverage.

United Nations Oil-for-Food Program

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

In addition to the governmental investigation referenced above, on June 27, 2008, the Republic of Iraq filed a civil suit in federal court in New York against 93 participants in the United Nations Oil-for-Food Program, including us and our two foreign subsidiaries that participated in the program. There have been no material developments in this case since it was initially filed. We intend to vigorously contest the suit, and we believe that we have valid defenses to the claims asserted. While we cannot predict the outcome of the suit at the present time, we do not currently believe the resolution of this suit will have a material adverse financial impact on our company.

Other

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

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

Although none of the aforementioned potential liabilities can be quantified with absolute certainty except as otherwise indicated above, we have established reserves covering exposures relating to contingencies, to the extent believed to be reasonably estimable and probable based on past experience and available facts. While additional exposures beyond these reserves could exist, they currently cannot be estimated. We will continue to evaluate and update the reserves as necessary and appropriate.

10. Retirement and Postretirement Benefits

Components of the net periodic cost for retirement and postretirement benefits for the three months ended March 31, 2015 and 2014 were as follows:

	U.S. Defined Benefit Plans		Non-U.S. Defined Benefit Plans		Postretirement Medical Benefits	
(Amounts in millions)	2015	2014	2015	2014	2015	2014
Service cost	$6.2	$5.7	$2.2	$1.7	$—	$—
Interest cost	4.3	4.4	3.3	3.7	0.3	0.3
Expected return on plan assets	(6.1)	(5.5)	(3.0)	(2.7)	—	—
Amortization of prior service cost	0.1	0.1	—	0.1	—	—
Amortization of unrecognized net loss (gain)	2.3	2.0	1.3	1.7	(0.1)	(0.4)
Net periodic cost (benefit) recognized	$6.8	$6.7	$3.8	$4.5	$0.2	$(0.1)

11. Shareholders' Equity

Dividends – On February 16, 2015, our Board of Directors authorized an increase in the payment of quarterly dividends on our common stock from $0.16 per share to $0.18 per share payable beginning on April 10, 2015. On February 17, 2014, our Board of Directors authorized an increase in the payment of quarterly dividends on our common stock from $0.14 per share to $0.16 per share payable quarterly beginning on April 11, 2014. Generally, our dividend date-of-record is in the last month of the quarter, and the dividend is paid the following month. Any subsequent dividends will be reviewed by our Board of Directors and declared in its discretion dependent on its assessment of our financial situation and business outlook at the applicable time.

Share Repurchase Program – On November 13, 2014, our Board of Directors approved a $500.0 million share repurchase authorization, which included approximately $175 million of remaining capacity under the prior $750.0 million share repurchase authorization. Our share repurchase program does not have an expiration date, and we reserve the right to limit or terminate the repurchase program at anytime without notice.

We repurchased 1,382,025 shares of our outstanding common stock for $79.9 million, and 1,436,423 shares for $109.6 million, during the three months ended March 31, 2015 and 2014, respectively. As of March 31, 2015, we have $384.5 million of remaining capacity under our current share repurchase program.

12. Income Taxes

For the three months ended March 31, 2015, we earned $58.2 million before taxes and provided for income taxes of $28.5 million resulting in an effective tax rate of 49.0%. The effective tax rate varied from the U.S. federal statutory rate for the three months ended March 31, 2015 primarily due to tax impacts of our realignment program and the Venezuelan exchange rate remeasurement loss.

For the three months ended March 31, 2014, we earned $146.6 million before taxes and provided for income taxes of $38.0 million, resulting in an effective tax rate of 25.9%. The effective tax rate varied from the U.S. federal statutory rate for the three months ended March 31, 2014 primarily due to the net impact of foreign operations and the lapse of the statute of limitations in certain jurisdictions.

As of March 31, 2015, the amount of unrecognized tax benefits increased by $8.1 million from December 31, 2014. With limited exception, we are no longer subject to U.S. federal income tax audits for years through 2012, state and local income tax audits for years through 2009 or non-U.S. income tax audits for years through 2007. We are currently under examination for various years in Austria, Germany, India, Italy, Singapore, the U.S. and Venezuela.

It is reasonably possible that within the next 12 months the effective tax rate will be impacted by the resolution of some or all of the matters audited by various taxing authorities. It is also reasonably possible that we will have the statute of limitations close in various taxing jurisdictions within the next 12 months. As such, we estimate we could record a reduction in our tax expense of approximately $11.0 million within the next 12 months.

13. Segment Information

During the three months ended March 31, 2015, we made composition changes to our Engineered Product Division ("EPD") and IPD reportable segments to take into consideration the acquisition of SIHI that was finalized on January 7, 2015. Effective January 1, 2015, certain activities, primarily related to engineered pumps and seals, that were previously included in the IPD business segment will now be reported in the EPD business segment. These changes did not materially impact segment results or segment assets. We did not change our business segments, management structure, chief operating decision maker or how we evaluate segment performance and allocate resources. Prior periods were retrospectively adjusted to conform to the new reportable segment composition. The following is a summary of the financial information of the reportable segments reconciled to the amounts reported in the condensed consolidated financial statements:

Three Months Ended March 31, 2015

(Amounts in thousands)	Engineered Product Division	Industrial Product Division	Flow Control Division	Subtotal–Reportable Segments	Eliminations and All Other	Consolidated Total
Sales to external customers	$473,413	$214,711	$326,496	$ 1,014,620	$—	$1,014,620
Intersegment sales	10,747	8,655	667	20,069	(20,069)	—
Segment operating income (loss)	68,828	(13,338)	54,715	110,205	(16,829)	93,376

Three Months Ended March 31, 2014

(Amounts in thousands)	Engineered Product Division	Industrial Product Division	Flow Control Division	Subtotal–Reportable Segments	Eliminations and All Other	Consolidated Total
Sales to external customers	$510,311	$175,994	$381,831	$ 1,068,136	$—	$1,068,136
Intersegment sales	13,785	10,190	1,107	25,082	(25,082)	—
Segment operating income	81,353	18,788	83,133	183,274	(18,948)	164,326

14. Accumulated Other Comprehensive Loss

The following table presents the changes in accumulated other comprehensive loss ("AOCL"), net of tax for the three months ended March 31, 2015 and 2014:

	2015				2014			
(Amounts in thousands)	Foreign currency translation items(1)	Pension and other post-retirement effects	Cash flow hedging activity	Total(1)	Foreign currency translation items(1)	Pension and other post-retirement effects	Cash flow hedging activity	Total(1)
Balance - January 1	$(238,533)	$(135,398)	$(5,210)	$(379,141)	$(89,953)	$(129,528)	$(814)	$(220,295)
Other comprehensive (loss) income before reclassifications	(106,434)	5,501	(8,353)	(109,286)	(2,509)	298	24	(2,187)
Amounts reclassified from AOCL	—	2,390	3,207	5,597	5,460	2,481	144	8,085
Net current-period other comprehensive (loss) income	(106,434)	7,891	(5,146)	(103,689)	2,951	2,779	168	5,898
Balance - March 31	$(344,967)	$(127,507)	$(10,356)	$(482,830)	$(87,002)	$(126,749)	$(646)	$(214,397)

(1) Includes foreign currency translation adjustments attributable to noncontrolling interests of $1.3 million and $1.2 million at January 1, 2015 and 2014 and $1.3 million and $1.4 million at March 31, 2015 and 2014. Includes accumulated net investment hedge losses of $2.1 million, net of deferred taxes, at March 31, 2015. Amounts in parentheses indicate debits.

The following table presents the reclassifications out of AOCL:

		Three Months Ended March 31,	
(Amounts in thousands)	Affected line item in the statement of income	2015(1)	2014(1)
Foreign currency translation items			
Release of cumulative translation adjustments due to sale of business	Selling, general and administrative expense	$—	$(5,460)
	Tax benefit	—	—
	Net of tax	$—	$(5,460)
Cash flow hedging activity			
Foreign exchange contracts	Other expense, net	$(3,327)	$—
	Sales	$(1,182)	$(230)
	Tax benefit	1,302	86
	Net of tax	$(3,207)	$(144)
Pension and other postretirement effects			
Amortization of actuarial losses(2)		$(3,424)	$(3,427)
Prior service costs(2)		(156)	(118)
	Tax benefit	1,190	1,064
	Net of tax	$(2,390)	$(2,481)

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

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

At March 31, 2015, we expect to recognize a loss of $7.1 million, net of deferred taxes, into earnings in the next twelve months related to designated cash flow hedges based on their fair values at March 31, 2015.

15. Realignment Program

In the first quarter of 2015, we initiated a realignment program to reduce and optimize certain non-strategic QRC and manufacturing facilities primarily resulting from the SIHI acquisition. We expect total charges will be $39.0 million for approved plans, of which $26.3 million has been incurred through March 31, 2015. We anticipate that the majority of the charges will be incurred through the remainder of 2015 and early 2016.

The realignment program consists of both restructuring and non-restructuring charges. Restructuring charges represent costs associated with the relocation or reorganization of certain business activities and facility closures and primarily represent employee severance. Non-restructuring charges are costs incurred to improve operating efficiency and reduce redundancies and primarily represent employee severance. Expenses are primarily reported in COS or SG&A, as applicable, in our condensed consolidated statements of income.

Realignment charges, net of adjustments, were $26.3 million and $1.0 million for the three months ended March 31, 2015 and 2014, respectively. Of the 2015 charges, $20.6 million was recorded in IPD and $0.6 million in EPD, and $5.0 million was reported in income tax expense in our condensed consolidated statement of income for the three months ended March 31, 2015. The majority of these charges are restructuring in nature.

Generally, the aforementioned charges will be paid in cash, except for asset write-downs, which are non-cash charges. There were no asset write-downs for the three months ended March 31, 2015. The majority of the cash payments will be incurred through the remainder of 2015 and early 2016. The restructuring reserve related to our realignment programs was $21.2 million and $1.1 million at March 31, 2015 and December 31, 2014, respectively. Other than the aforementioned realignment charges there was no significant activity related to the restructuring reserve during the three months ended March 31, 2015.

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

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements, and notes thereto, and the other financial data included elsewhere in this Quarterly Report. The following discussion should also be read in conjunction with our audited consolidated financial statements, and notes thereto, and "Management’s Discussion and Analysis of Financial Condition and Results of Operations" ("MD&A") included in our 2014 Annual Report.

EXECUTIVE OVERVIEW

Our Company

We believe that we are a world-leading manufacturer and aftermarket service provider of comprehensive flow control systems. We develop and manufacture precision-engineered flow control equipment integral to the movement, control and protection of the flow of materials in our customers’ critical processes. Our product portfolio of pumps, valves, seals, automation and aftermarket services supports global infrastructure industries, including oil and gas, chemical, power generation and water management, as well as general industrial markets where our products and services add value. Through our manufacturing platform and global network of Quick Response Centers ("QRCs"), we offer a broad array of aftermarket equipment services, such as installation, advanced diagnostics, repair and retrofitting. We currently employ approximately 20,000 employees in more than 50 countries.

Our business model is significantly influenced by the capital spending of global infrastructure industries for the placement of new products into service and aftermarket services for existing operations. The worldwide installed base of our products is an important source of aftermarket revenue, where products are expected to ensure the maximum operating time of many key industrial processes. Over the past several years, we have significantly invested in our aftermarket strategy to provide local support to drive customer investments in our offerings and use of our services to replace or repair installed products. The aftermarket portion of our business also helps provide business stability during various economic periods. The aftermarket business, which is served by our network of 192 QRCs located around the globe, provides a variety of service offerings for our customers including spare parts, service solutions, product life cycle solutions and other value-added services. It is generally a higher margin business compared to our original equipment business and a key component of our profitable growth strategy.

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

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

- IPD for engineered and pre-configured industrial pumps and pump systems and related products and services; and
- FCD for engineered and industrial valves, control valves, actuators and controls and related services.

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

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

We continue to build on our geographic breadth through our QRC network with the goal to be positioned as near to customers as possible for service and support in order to capture valuable aftermarket business. Along with ensuring that we have the local capability to sell, install and service our equipment in remote regions, it is equally imperative to continuously improve our global operations. We continue to expand our global supply chain capability to meet global customer demands and ensure the quality and timely delivery of our products. We continue to devote resources to improving the supply chain processes across our business segments to find areas of synergy and cost reduction and to improve our supply chain management capability to ensure it can meet global customer demands. We also remain focused on improving on-time delivery and quality, while managing warranty costs as a percentage of sales across our global operations, through the assistance of a focused Continuous Improvement Process ("CIP") initiative. The goal of the CIP initiative, which includes lean manufacturing, six sigma business management strategy and value engineering, is to maximize service fulfillment to customers through on-time delivery, reduced cycle time and quality at the highest internal productivity.

Our pursuit of major capital projects globally and our investments in localized customer service remain key components of our long-term growth strategy, and also provide stability during various economic periods. We believe that our commitment to localize service support capabilities close to our customers' operations through our QRC network has enabled us to grow our market share in the aftermarket portion of our business. We believe that with our customer relationships, global presence and highly-regarded technical capabilities, we will continue to have opportunities in our core industries; however, we face ongoing challenges affecting many companies in our industry with a significant multinational presence, such as economic, political, currency and other risks.

During the first three months of 2015, we were challenged by broad-based capital spending declines, originating in the oil and gas industry, and negative currency impacts caused by a stronger U.S. dollar. This was further compounded by economic and geo-political conditions in Latin America and the Middle East, and by strikes in several U.S. refineries. In addition, we experienced reduced activity levels in our aftermarket business due to deferred spending of our customers' repair and maintenance budgets.

Our solid operational foundation enables us to take advantage of market conditions and maintain solid margins and our competitive position going forward. To better align costs and improve long-term efficiency, we plan to accelerate both short- and long-term strategic plans, including further targeted manufacturing optimization, through the transfer of activities from high-cost regions to lower-cost facilities, and SG&A efficiency initiatives. We estimate an approximate 5% reduction in our global workforce. With an expected additional near-term investment of approximately $100 million, we expect the results of these actions will deliver annualized run-rate savings of approximately $70 million beyond the synergies associated with the SIHI acquisition.

RESULTS OF OPERATIONS — Three months ended March 31, 2015 and 2014

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

As discussed in Note 2 to our condensed consolidated financial statements included in this Quarterly Report, effective January 7, 2015, we acquired for inclusion in IPD, 100% of SIHI, a global provider of engineered vacuum and fluid pumps and related services. The impact of the acquisition of SIHI for the three months ended March 31, 2015 includes bookings of $85.2 million, sales of $66.8 million, gross profit (loss) of $(0.6) million, operating loss of $32.8 million (including acquisition-related costs of $5.0 million and realignment costs of $21.3 million) and period end backlog of $127.2 million.

As discussed in Note 2 to our condensed consolidated financial statements included in this Quarterly Report, effective March 31, 2014 we sold our FCD Naval business to a Finnish valve manufacturer.

As discussed in Note 15 to our condensed consolidated financial statements included in this Quarterly Report, during the three months ended March 31, 2015, we initiated a realignment program to reduce and optimize certain non-strategic QRC and manufacturing facilities primarily resulting from the SIHI acquisition. We expect total charges will be $39.0 million for approved plans, of which $26.3 million has been incurred through March 31, 2015. We anticipate that the majority of the charges will incurred through the remainder of 2015 and early 2016.

The realignment program consists of both restructuring and non-restructuring charges. Restructuring charges represent costs associated with the relocation or reorganization of certain business activities and facility closures and primarily represent employee severance. Non-restructuring charges are costs incurred to improve operating efficiency and reduce redundancies and primarily represent employee severance. Expenses are primarily reported in COS or SG&A, as applicable, in our condensed consolidated statements of income.

Realignment charges, net of adjustments, were $26.3 million and $1.0 million for the three months ended March 31, 2015 and 2014, respectively. Of the 2015 charges $20.6 million was recorded in IPD and $0.6 million in EPD, and $5.0 million was reported in income tax expense in our condensed consolidated statement of income for the three months ended March 31, 2015. The majority of these charges are restructuring in nature. Upon completion of the realignment program, we expect annual cost savings of approximately $11 million, with a portion realized in 2016. Generally, the aforementioned charges will be paid in cash, except for asset write-downs, which are non-cash charges. There were no asset write-downs for the three months ended March 31, 2015. The majority of the cash payments related to our realignment program will be incurred through the remainder of 2015 and early 2016. The restructuring reserve related to our realignment programs was $21.2 million and $1.1 million at March 31, 2015 and December 31, 2014, respectively. Other than the aforementioned realignment charges there was no significant activity related to the restructuring reserve during the three months ended March 31, 2015.

Consolidated Results

Bookings, Sales and Backlog

	Three Months Ended March 31,	
(Amounts in millions)	2015	2014
Bookings	$ 1,042.6	$ 1,193.9
Sales	1,014.6	1,068.1

We define a booking as the receipt of a customer order that contractually engages us to perform activities on behalf of our customer with regard to manufacturing, service or support. Bookings recorded and subsequently canceled within the year-to-date period are excluded from year-to-date bookings. Bookings for the three months ended March 31, 2015 decreased by $151.3 million, or 12.7%, as compared with the same period in 2014. The decrease included negative currency effects of approximately $81 million. The decrease during the three months ended March 31, 2015 was primarily driven by the oil and gas industry, and to a lesser extent, chemical, general industries and the power generation industries. The decrease was more heavily weighted toward customer original equipment bookings. Excluding the $85.2 million impact of SIHI, bookings for the three months ended March 31, 2015 decreased by $236.5 million, or 19.8%, as compared with the same period in 2014.

Sales for the three months ended March 31, 2015 decreased by $53.5 million, or 5.0%, as compared with the same period in 2014. The decrease included negative currency effects of approximately $88 million. The decrease was more heavily weighted towards original equipment sales, and decreased sales into Asia Pacific, Latin America and the Middle East were partially offset by increased sales into North America. Net sales to international customers, including export sales from the U.S., were approximately 64% and 68% of total sales for the three months ended March 31, 2015 and 2014, respectively. Excluding the $66.8 million impact of SIHI, sales for the three months ended March 31, 2015 decreased by $120.3 million, or 11.3%, as compared with the same period in 2014.

Backlog represents the aggregate value of booked but uncompleted customer orders and is influenced primarily by bookings, sales, cancellations and currency effects. Backlog of $2,689.4 million at March 31, 2015 decreased by $14.8 million, or 0.5%, as compared with December 31, 2014. Currency effects provided a decrease of approximately $129 million. Approximately 25% of the backlog at March 31, 2015 was related to aftermarket orders. Excluding the $127.2 million impact of SIHI, backlog decreased by $142.0 million, or 5.3%, as compared with December 31, 2014.

Gross Profit and Gross Profit Margin

	Three Months Ended March 31,			
(Amounts in millions, except percentages)	2015		2014	
Gross profit	$331.7		$377.1	
Gross profit margin	32.7	%	35.3	%

Gross profit for the three months ended March 31, 2015 decreased by $45.4 million, or 12.0%, as compared with the same period in 2014. Gross profit margin for the three months ended March 31, 2015 of 32.7% decreased from 35.3% for the same period in 2014. The decrease in gross profit margin was primarily attributed to the negative impact of margins on acquired SIHI backlog and inventory ("Purchase Price Adjustments"), $13.2 million of charges related to our realignment program, and to a lesser extent, certain lower margin projects that shipped from backlog, as compared with the same period in 2014, partially offset by a mix shift to higher margin aftermarket sales. Aftermarket sales increased to approximately 44% of total sales, as compared with approximately 43% of total sales for the same period in 2014.

Selling, General and Administrative Expense ("SG&A")

	Three Months Ended March 31,			
(Amounts in millions, except percentages)	2015		2014	
SG&A	$239.9		$216.2	
SG&A as a percentage of sales	23.6	%	20.2	%

SG&A for the three months ended March 31, 2015 increased by $23.7 million, or 11.0%, as compared with the same period in 2014 and included the impact of $32.1 million of SIHI SG&A. Currency effects yielded a decrease of approximately $18 million. SG&A as a percentage of sales for the three months ended March 31, 2015 increased 340 basis points as compared with the same period in 2014 due primarily to $8.1 million of charges related to our realignment program, $5.0 million of SIHI acquisition-related costs and the $13.4 million gain from the sale of the Naval business in the first quarter of 2014 that did not recur.

Net Earnings from Affiliates

	Three Months Ended March 31,	
(Amounts in millions)	2015	2014
Net earnings from affiliates	$1.6	$3.4

Net earnings from affiliates for the three months ended March 31, 2015 decreased $1.8 million, or 52.9%, as compared with the same period in 2014. The decrease was primarily a result of decreased earnings of our EPD joint venture in South Korea.

Operating Income and Operating Margin

	Three Months Ended March 31,			
(Amounts in millions, except percentages)	2015		2014	
Operating income	$93.4		$164.3	
Operating income as a percentage of sales	9.2	%	15.4	%

Operating income for the three months ended March 31, 2015 decreased by $70.9 million, or 43.2%, as compared with the same period in 2014. The decrease included negative currency effects of approximately $12 million. The decrease was primarily a result of the $45.4 million decrease in gross profit and the $23.7 million increase in SG&A.

Interest Expense and Interest Income

	Three Months Ended March 31,	
(Amounts in millions)	2015	2014

Interest expense	$(16.0)	$(15.1)
Interest income	0.8	0.3

Interest expense for the three months ended March 31, 2015 increased $0.9 million as compared with the same period in 2014. The increase was primarily attributable to interest expense associated with the initial borrowings from our Revolving Credit Facility that was used to partially fund the SIHI acquisition. At March 31, 2015, approximately 82% of our total debt was at fixed interest rates, after the effects of $25.0 million of notional interest rate swaps.

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Other Expense, Net

	Three Months Ended March 31,	
(Amounts in millions)	2015	2014
Other expense, net	$(19.9)	$(2.9)

Other expense, net for the three months ended March 31, 2015 increased $17.0 million as compared with the same period in 2014, due primarily to a $40.5 million increase in losses arising from transactions in currencies other than our sites' functional currencies, including the impact of the $18.5 million loss as a result of the remeasurement of our Venezuelan bolivar-denominated net monetary assets, partially offset by a $23.5 million increase in gains on foreign exchange contracts. The net change, excluding the Venezuelan exchange rate remeasurement loss, is primarily due to the foreign currency exchange rate movements of the Brazilian real and Euro in relation to the U.S. dollar during the three months ended March 31, 2015, as compared with the same period in 2014.

Tax Expense and Tax Rate

	Three Months Ended March 31,	
(Amounts in millions, except percentages)	2015	2014
Provision for income taxes	$28.5	$38.0
Effective tax rate	49.0%	25.9%

Our effective tax rate of 49.0% for the three months ended March 31, 2015 increased from 25.9% for the same period in 2014. The effective tax rate varied from the U.S. federal statutory rate for the three months ended March 31, 2015 primarily due to tax impacts of the realignment program and the Venezuelan exchange rate remeasurement loss.

Other Comprehensive (Loss) Income

	Three Months Ended March 31,	
(Amounts in millions)	2015	2014
Other comprehensive (loss) income	$(103.7)	$5.9

Other comprehensive loss for the three months ended March 31, 2015 increased $109.6 million to a loss of $103.7 million as compared to income of $5.9 million in 2014. The increase was primarily due to the weakening of the Euro versus the U.S. dollar during the three months ended March 31, 2015, as compared with the same period in 2014.

Business Segments

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

Effective January 1, 2015, we made composition changes to our EPD and IPD reportable segments to take into consideration the acquisition of SIHI. Certain operations that were previously included in the IPD reportable segment are reported in the EPD reportable segment to align with how operations are managed and reported. Prior periods were retrospectively adjusted to conform to the new reportable segment composition. These changes did not materially impact segment results. In addition, IPD includes operations of SIHI acquired in January 2015.

Engineered Product Division Segment Results

Our largest business segment is EPD, through which we design, manufacture, distribute and service custom and other highly-engineered pumps and pump systems, mechanical seals, auxiliary systems and spare parts (collectively referred to as "original equipment"). EPD includes longer lead-time, highly-engineered pump products and shorter cycle engineered pumps and mechanical seals that are generally manufactured more quickly. EPD also manufactures replacement parts and related equipment and provides a full array of replacement parts, repair and support services (collectively referred to as "aftermarket"). EPD primarily operates in the oil and gas, power generation, chemical, water management and general industries. EPD operates in 48 countries with 33 manufacturing facilities worldwide, ten of which are located in Europe, 11 in North America, seven in Asia and five in Latin America, and it has 130 QRCs, including those co-located in manufacturing facilities.

	Three Months Ended March 31,	
(Amounts in millions, except percentages)	2015	2014
Bookings	$495.4	$628.2
Sales		