



Spring 2018 Analyst Presentation



Forward Looking Statements

This presentation contains statements that we believe are “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements generally can be identified by the use of words such as “may,” “will,” “expect,” “intend,” “estimate,” “anticipate,” “believe,” “continue,” “guidance” or words of similar meaning. All forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from those anticipated as of the date of this presentation. Important factors that could cause actual results to differ materially from these expectations include, among other things, the following: a slowdown in the growth rate of the Chinese economy or our key markets and/or a decline in the growth rate of consumer spending in China; potential weakening in the high efficiency boiler market segment in the U. S.; significant volatility in raw material prices; our inability to implement or maintain pricing actions; potential weakening in U. S. residential or commercial construction or instability in our replacement markets; foreign currency fluctuations; inability to successfully integrate or achieve our strategic objectives resulting from future acquisitions; competitive pressures on our businesses; the impact of potential information technology or data security breaches; changes in government regulations or regulatory requirements; the impact from U.S. Tax Reform and projections for effective tax rates and one-time expenses under the new law; and adverse developments in general economic, political and business conditions in the key regions of the world. Forward-looking statements included in this presentation are made only as of the date of this presentation, and the company is under no obligation to update these statements to reflect subsequent events or circumstances. All subsequent written and oral forward-looking statements attributed to the company, or persons acting on its behalf, are qualified entirely by these cautionary statements. This presentation contains certain non-GAAP financial measures as that term is defined by the SEC. Non-GAAP financial measures are generally identified by “Adjusted” (Adj.) or “Non-GAAP” .



Investment Case

- Manufacturer of residential and commercial water heaters, boilers and water treatment products
- Market share leader in major businesses
- Stable/growing North American replacement market; operating leverage as new construction recovers
- Strong balance sheet and cash flow to support future growth & share repurchase
- Strength of our premium brand, distribution, manufacturing and innovation provide clear market advantage in China
- Organic growth of 8 percent for next several years

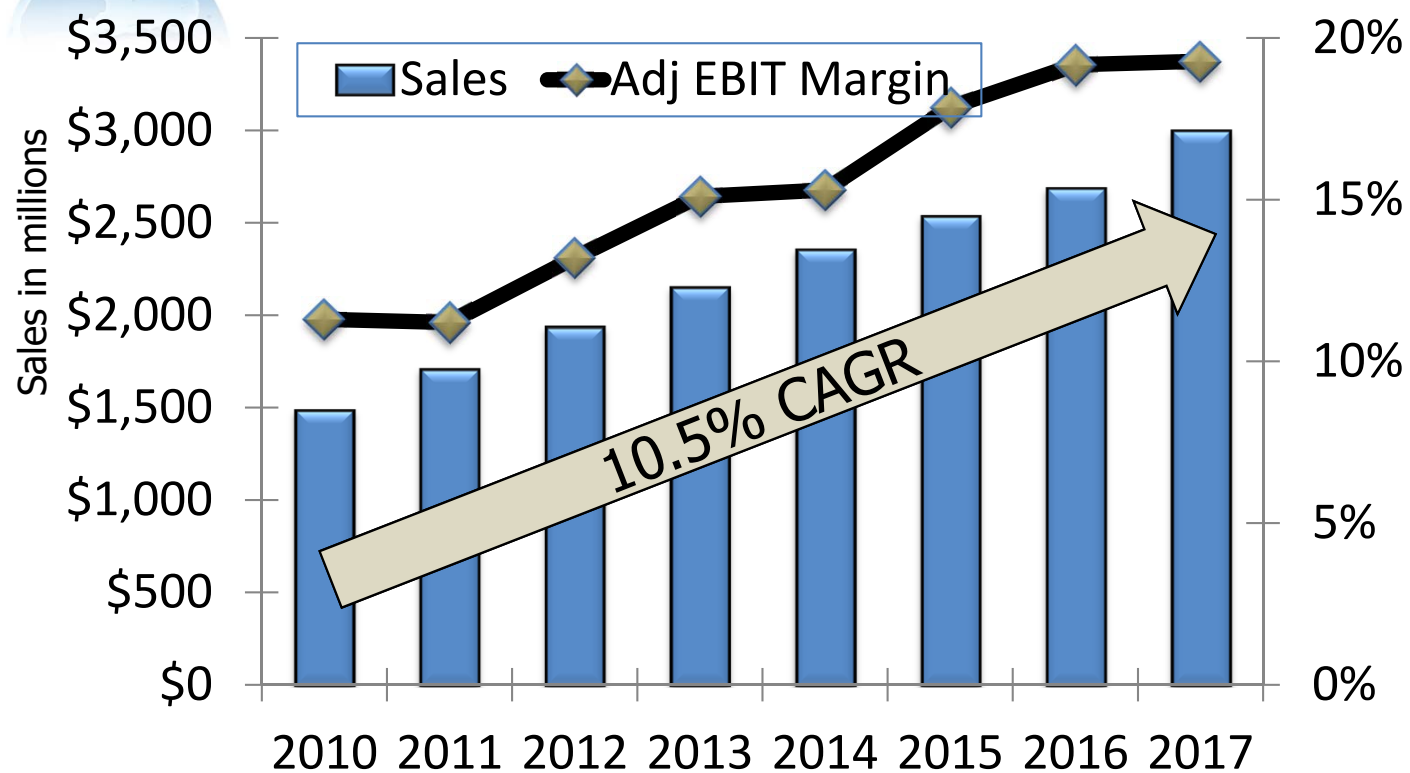
AOS

LISTED

NYSE



Sales & Adjusted Operating Margin*



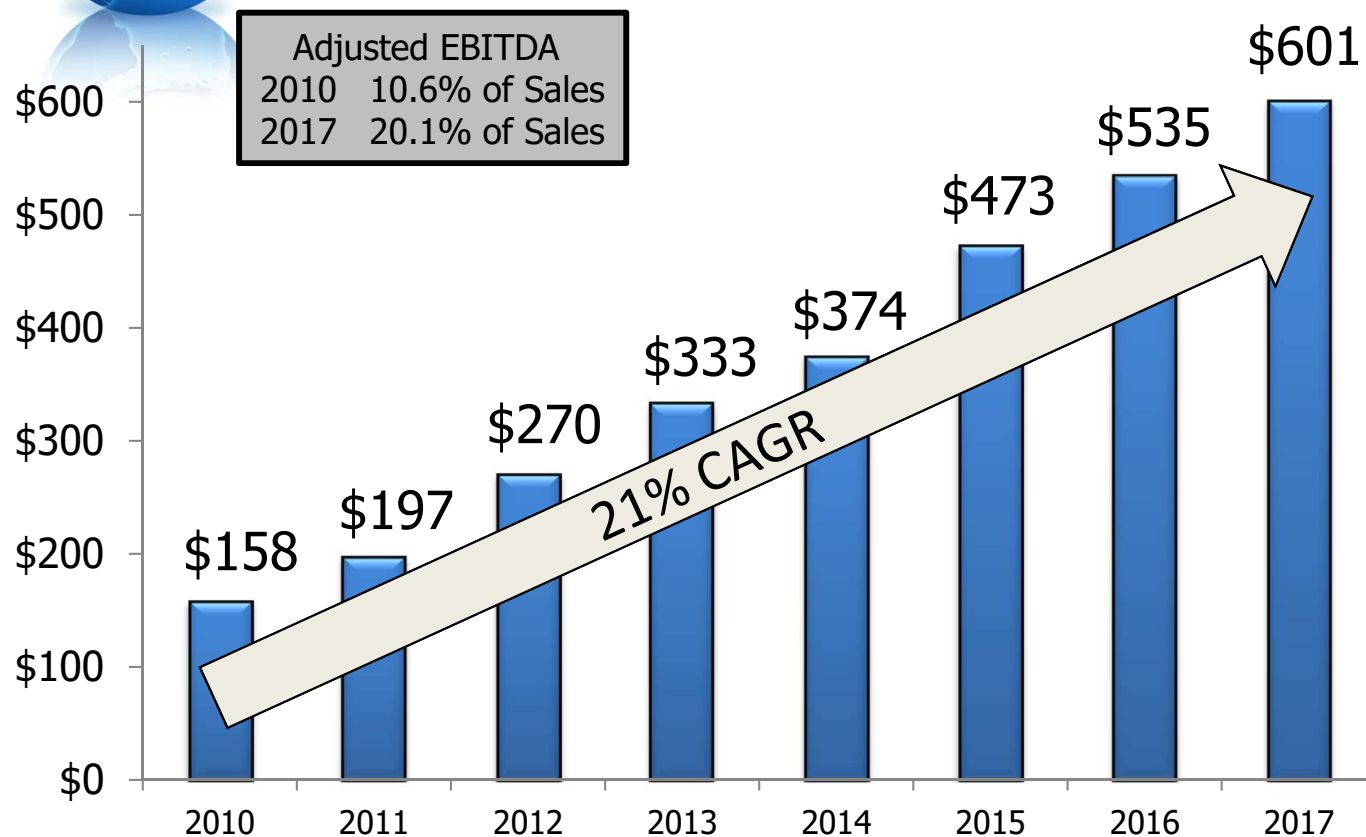
NOTE

2010 through 2014 adjusted for non-operating pension costs and certain non-recurring items

* excludes corporate expenses



Adjusted EBITDA: 21 Percent CAGR

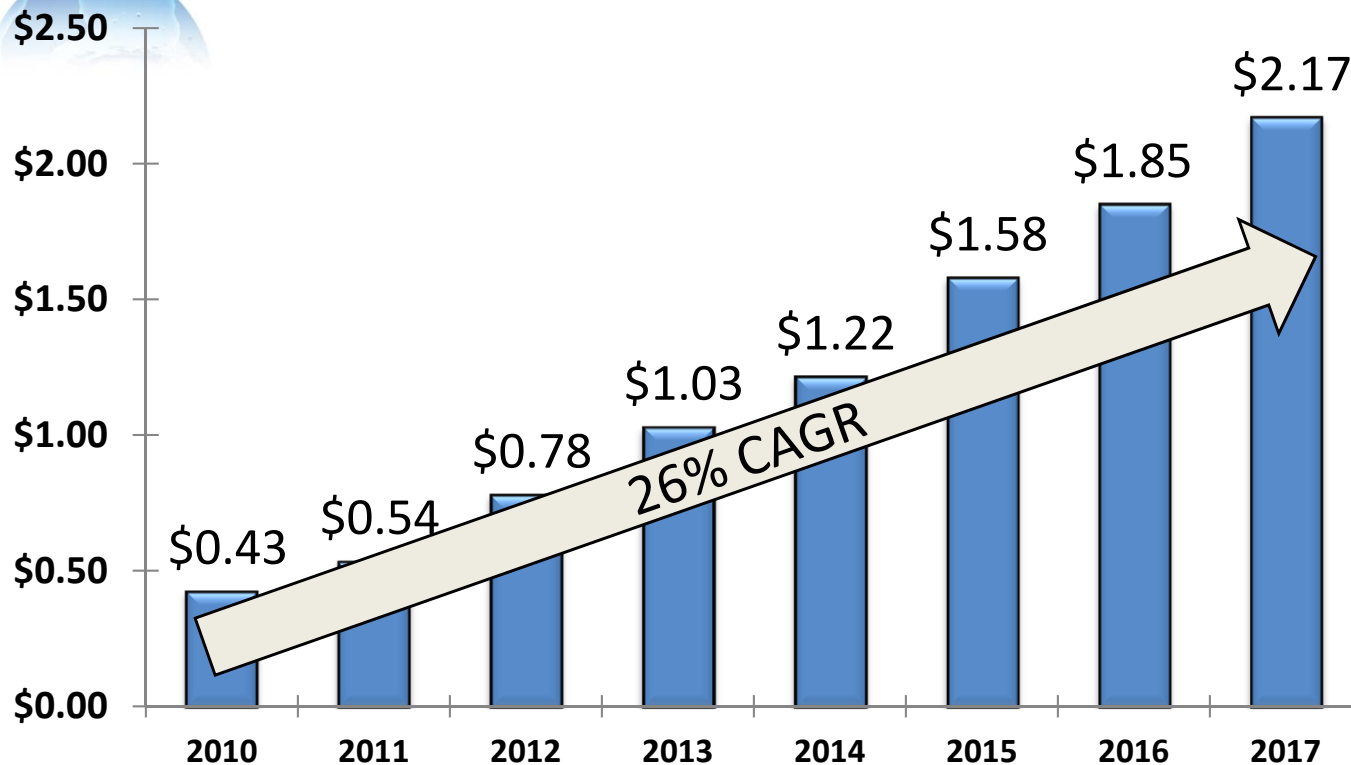


NOTE

2010 through 2014 adjusted for non-operating pension costs and certain non-recurring items



Adjusted Earnings Per Share: 26 Percent CAGR



NOTE

2010 through 2014 adjusted for non-operating pension costs and certain non-recurring items; 2017 adjusted for U.S. Tax Reform expense



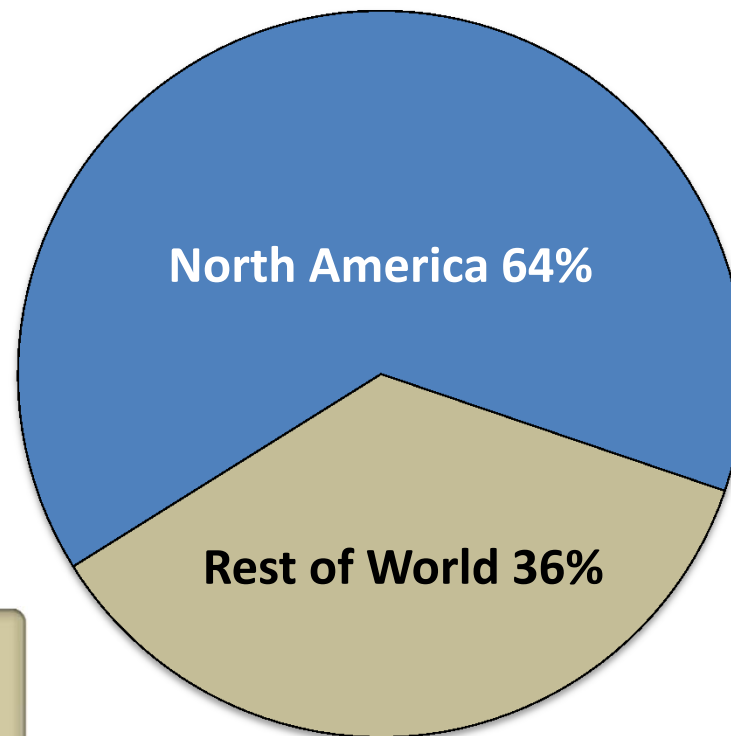
Segment Revenue

NA

- Boilers growing 10%
- Water heaters growing

ROW

- China/India = 95%
- Europe/Middle East = 5%



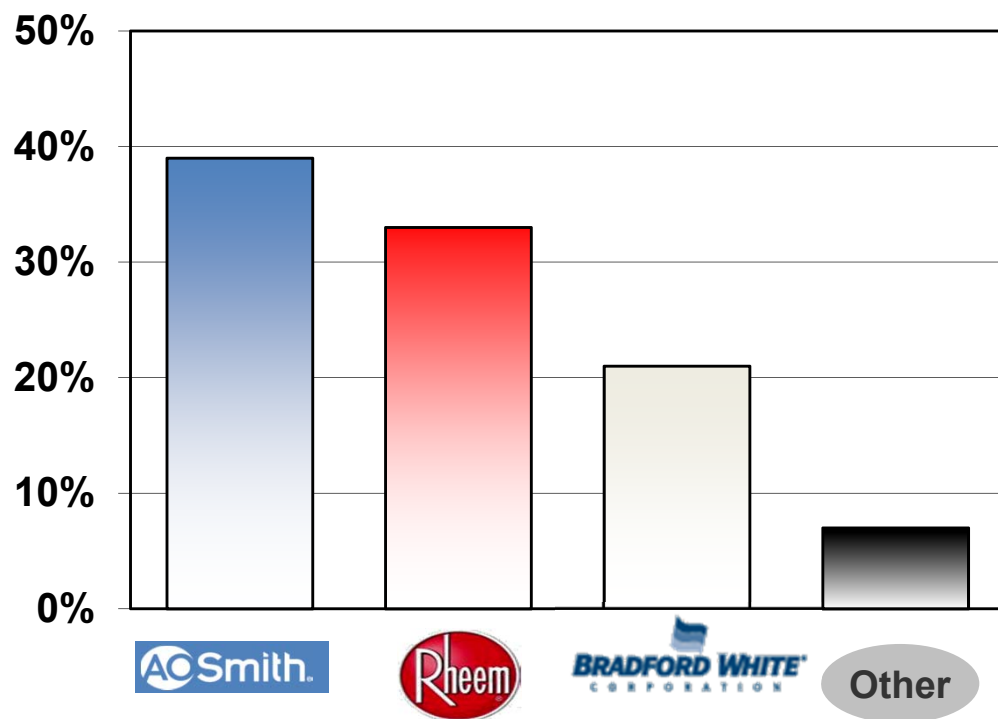
2017 full year





U.S. Water Heater Market Segment

Residential Market



AHRI data + tankless:
AOS actual shipments
and AOS estimates of
competitors' shipments

2017 market share data



U.S. Residential Water Heater Market Segment

*Wholesale channel is
“~55%” of the
market*



*Retail channel is
“~45%” of the
market*

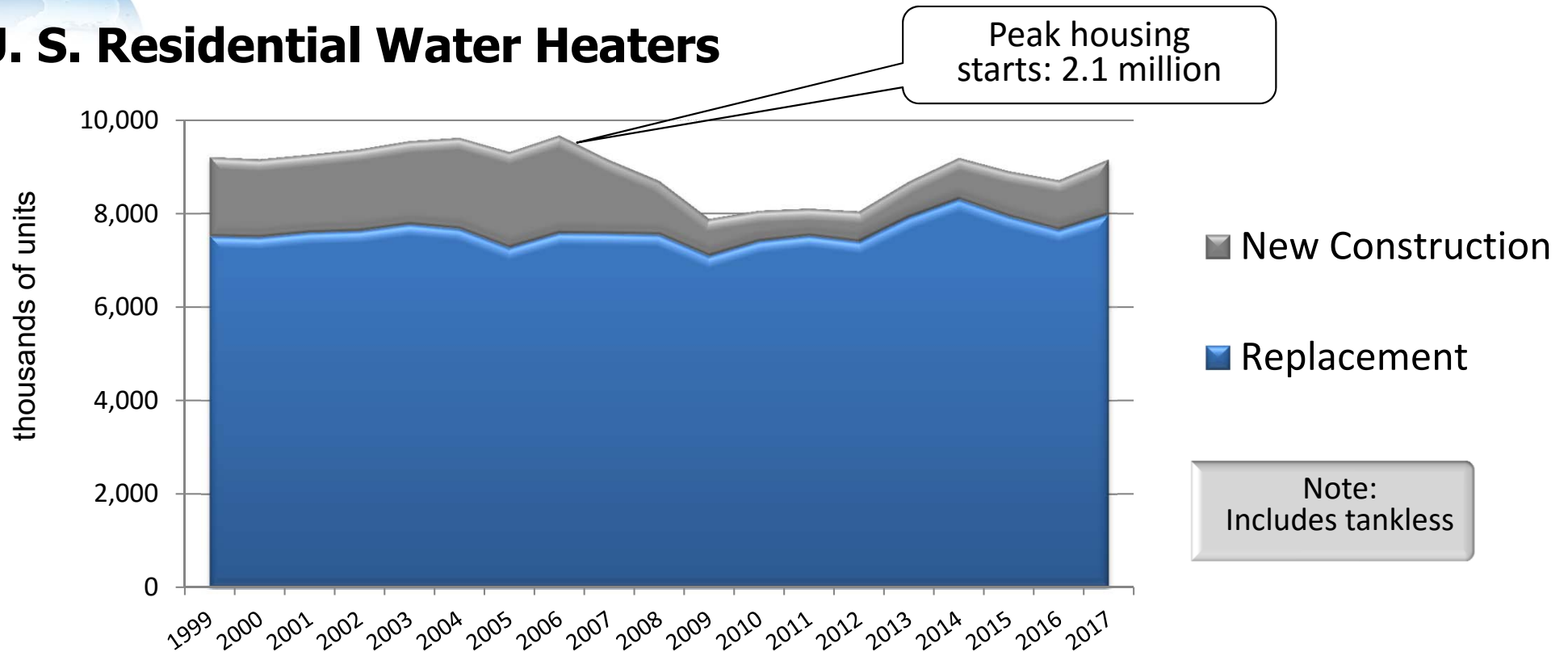
A. O. Smith's
Customers

2017 – 9.2 mm Units



Water Heaters - Strong Replacement Sales

U. S. Residential Water Heaters

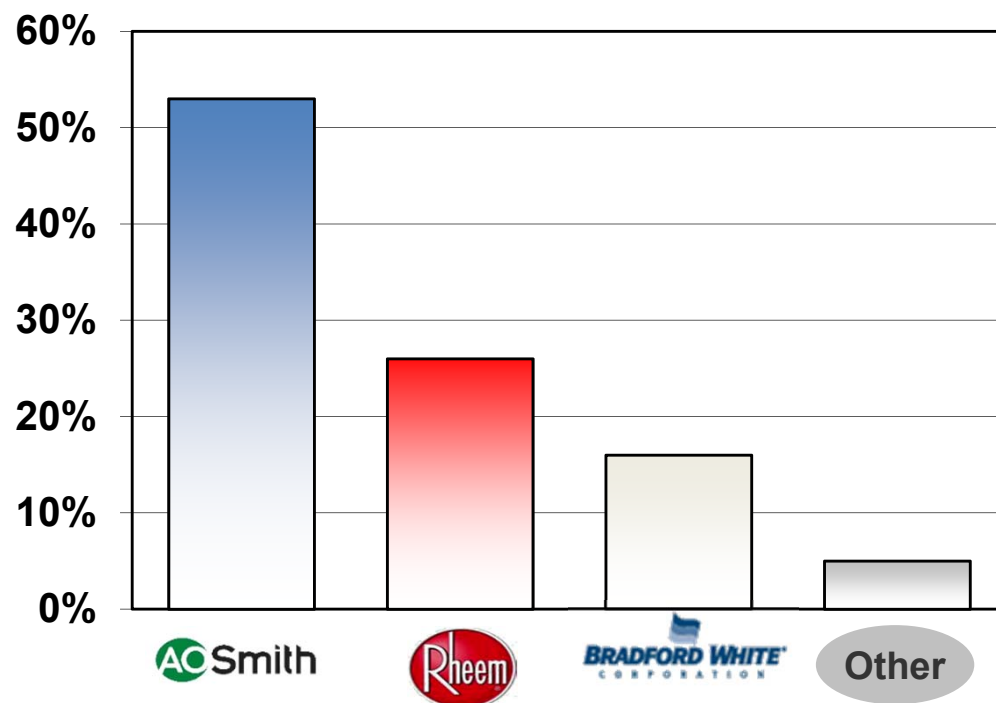




U.S. Water Heater Market Segment

Commercial Gas Market*

2017 market share data



AHRI data:

AOS actual shipments and
AOS estimate of competitors'
shipments

* Commercial gas water heater
segment as defined by AHRI,
total 2017 commercial units as
reported by AHRI = 94,000 units



Energy Efficient Cyclone

- Game changing energy efficient commercial product launched in 1997 and recently upgraded
- Up to 96% thermal efficiency dramatically lowers operating costs offering short payback
- Represents 63% of AOS commercial gas water heater revenues

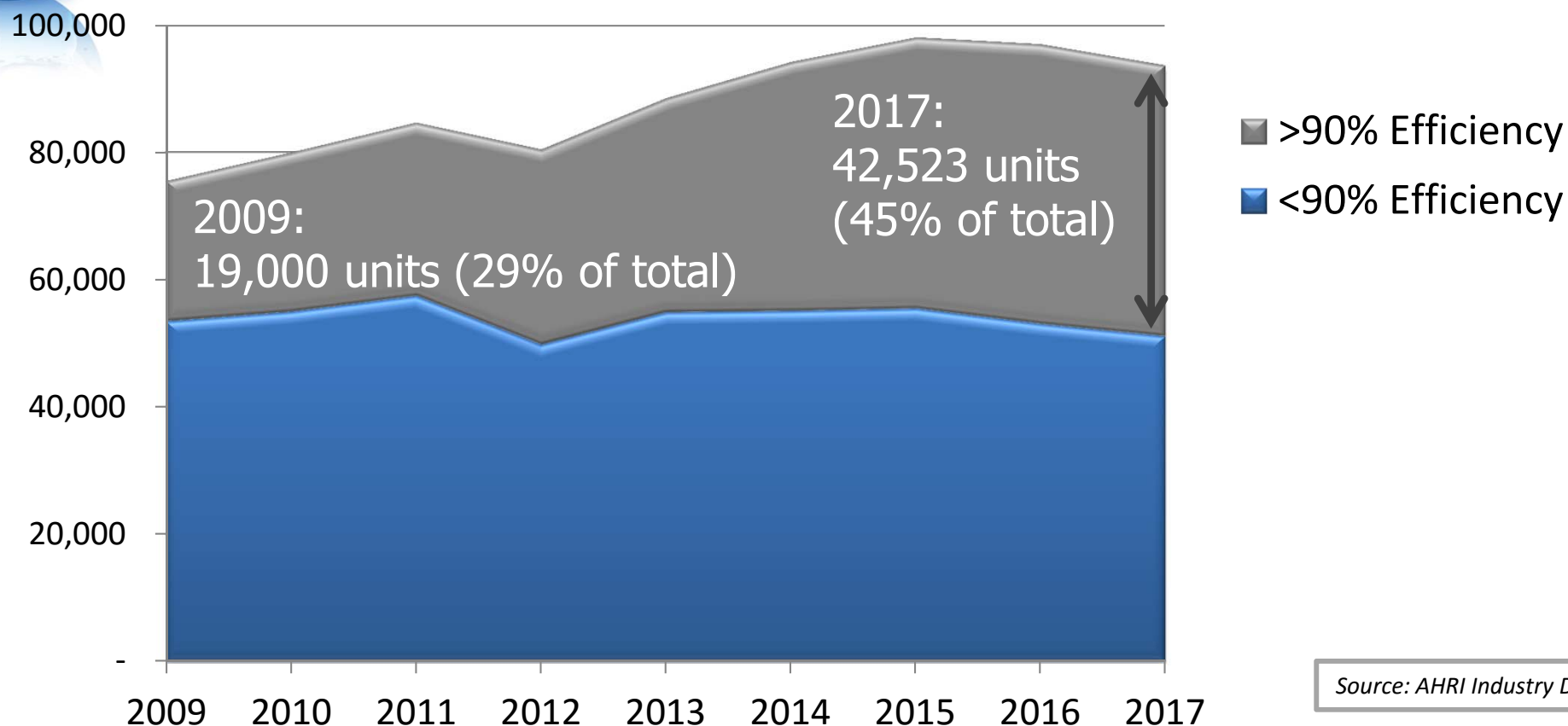


Innovation, training and 24/7 National account customer service drive market leadership



U.S. Commercial Gas Market: Energy Efficient Units more than Doubled in Seven Years to 45 percent of units sold in 2017

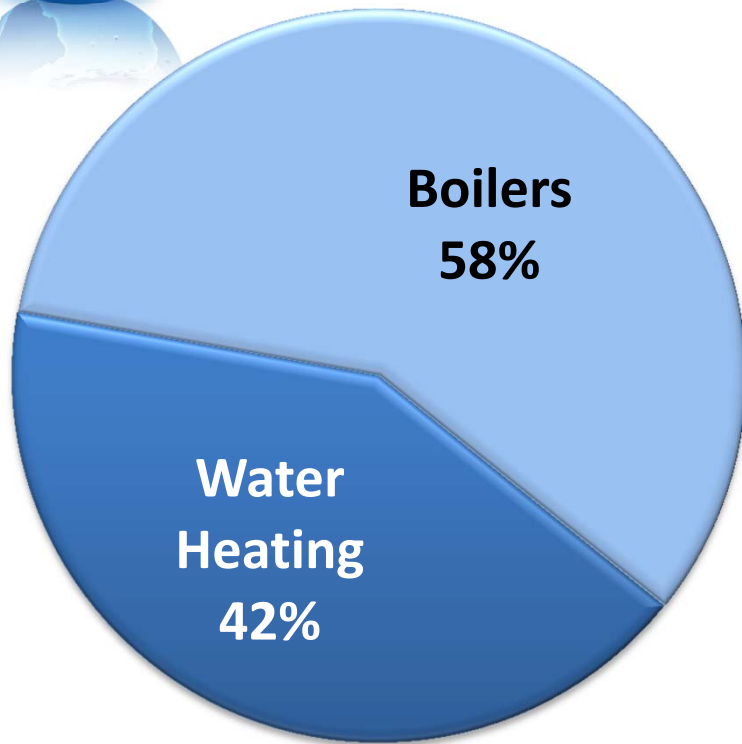
Commercial Gas Industry Units



Source: AHRI Industry Data



Lochinvar End Markets

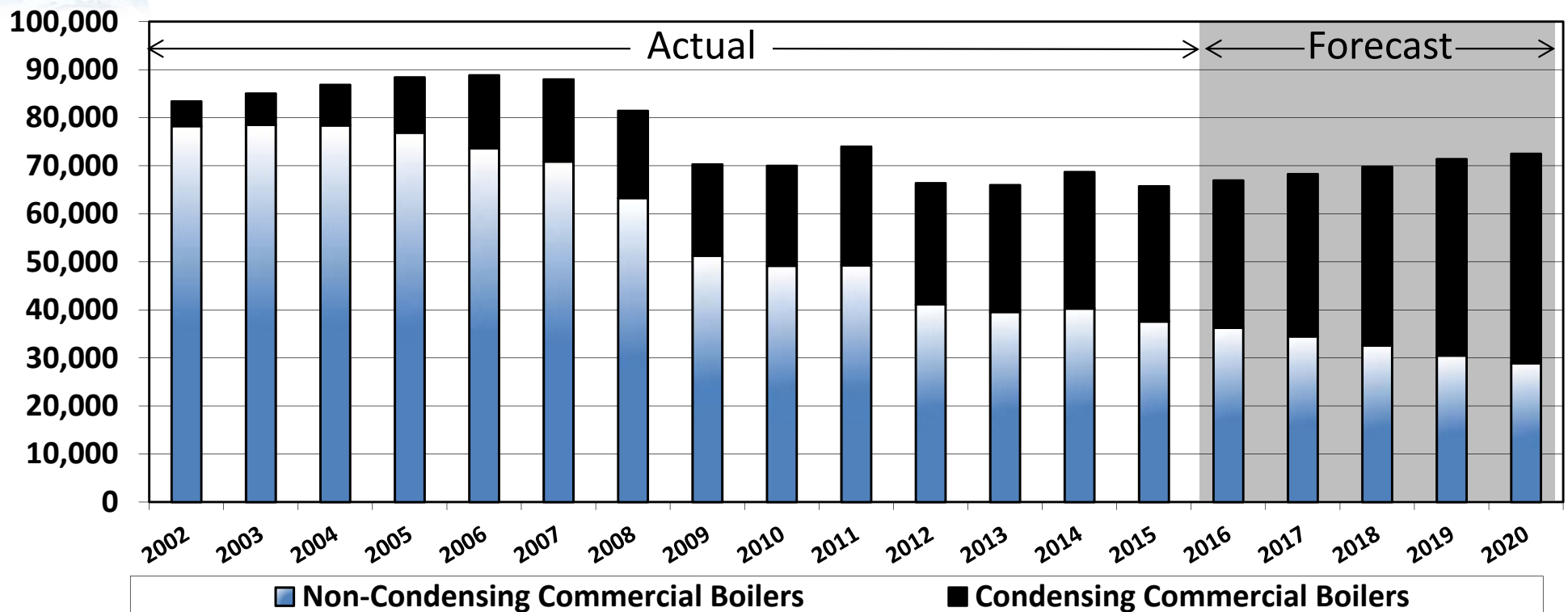


2/3 commercial end markets; 1/3 residential end markets



Trend to Higher Efficiency, Condensing Boilers – 43 percent of units sold in 2015

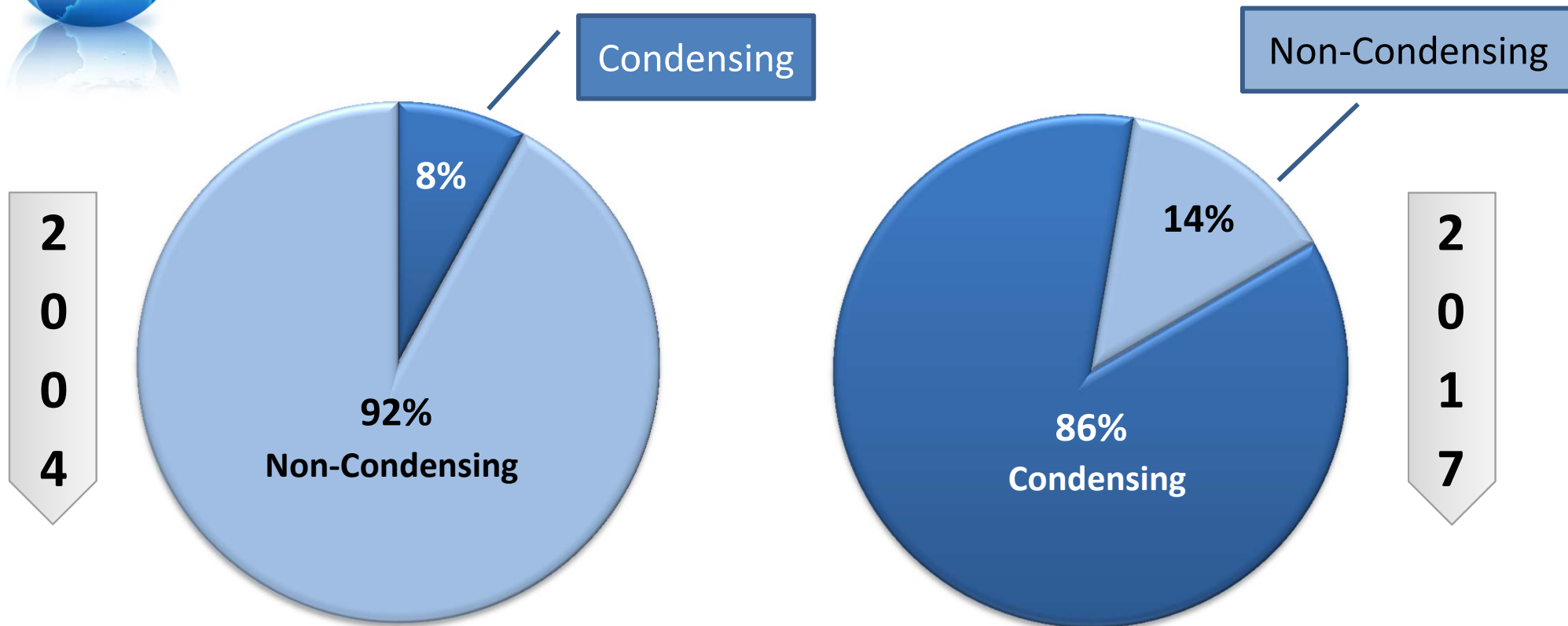
North American Commercial Boiler Volume (Units)



Source: BRG Building Solutions



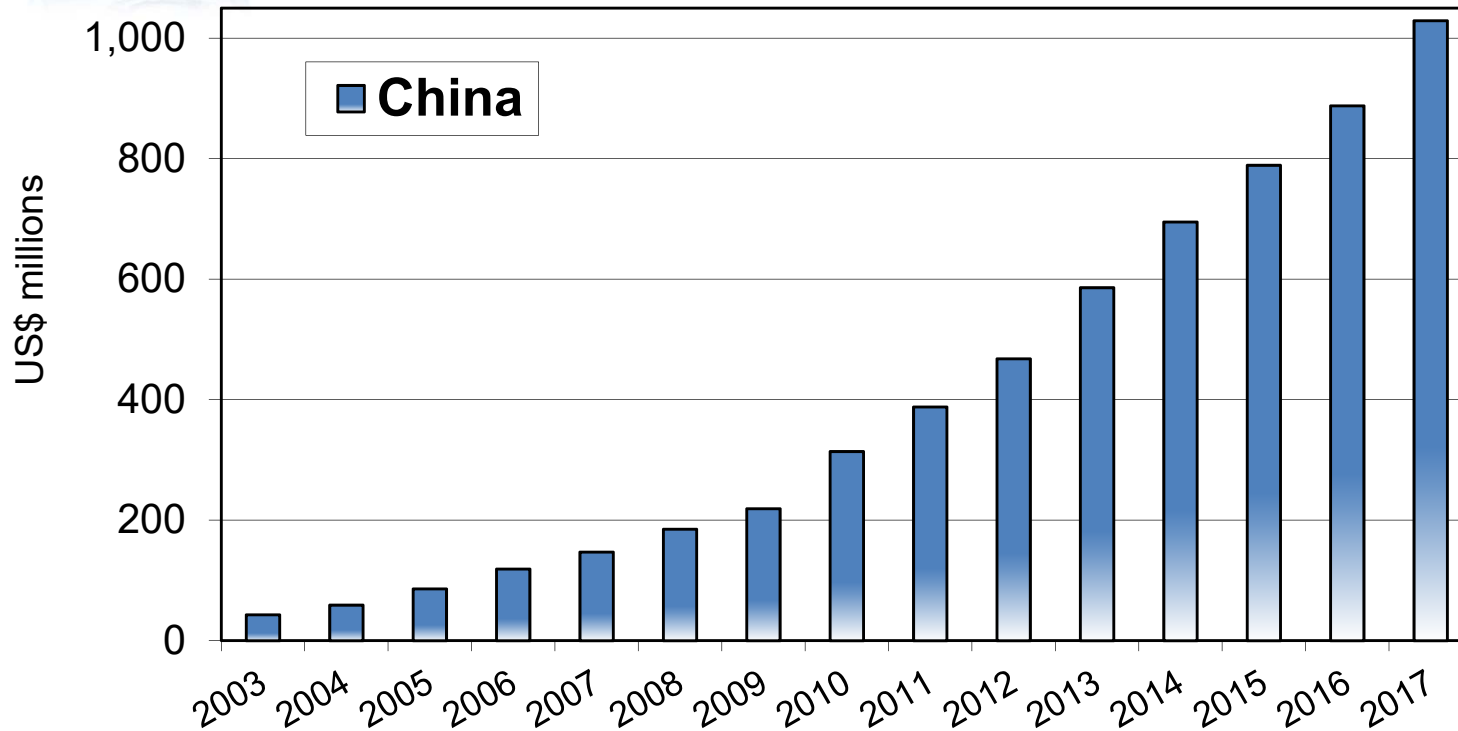
Boiler Sales Dollars* Condensing vs. Non-Condensing



*Residential Boilers & Commercial Boilers



China Exceeds \$1 B; now 34% of Sales & Growing



China sales have grown 21% (CAGR) over the last 10 years



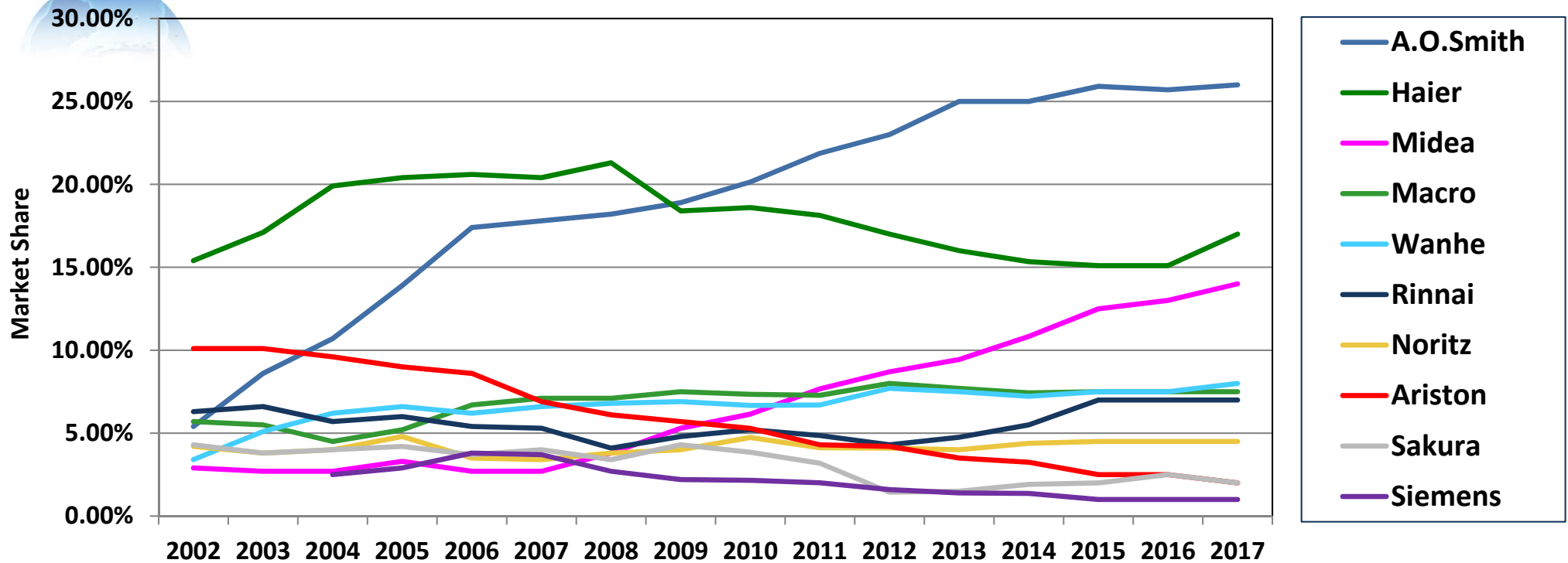
AOS China Built on:

- Premium Brand
- Extensive Distribution and Service Network
- Innovative New Products & World Class Manufacturing
- Local Management Team and Organizational Development





Fifteen Year Water Heater Market Share Trend

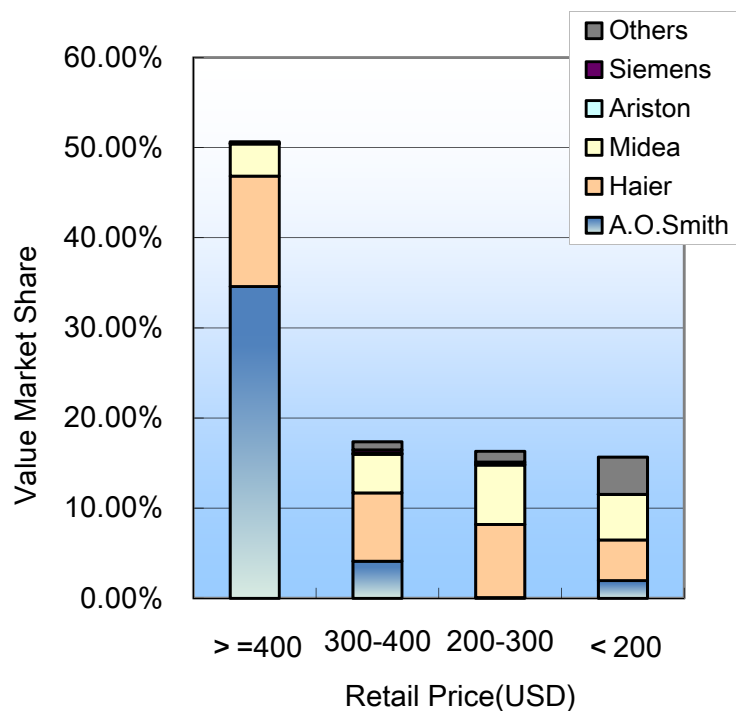


Leading residential brands measured in currency; Tier One Market: GFK - CMM data sampling several thousand largest retail stores, December 2017

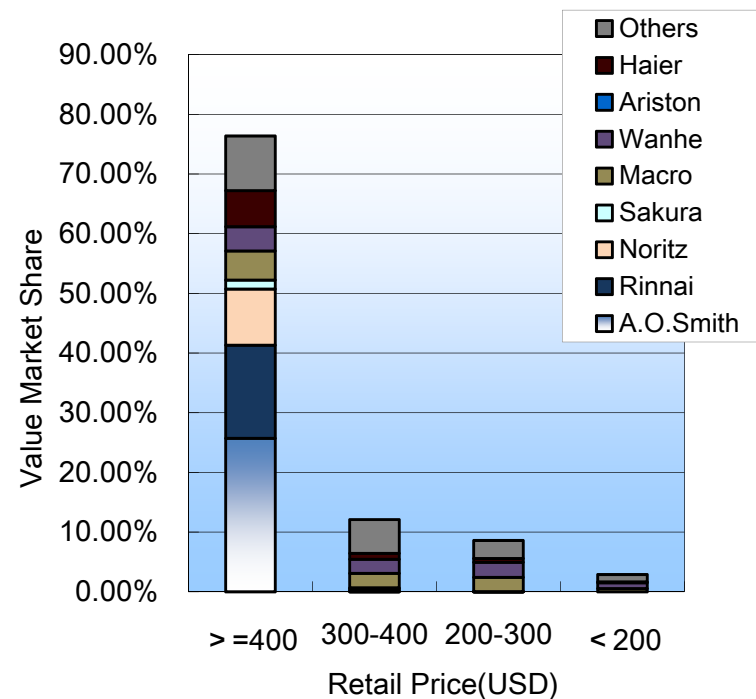


Market Share by Price Category

Electric Market Share



Gas Market Share

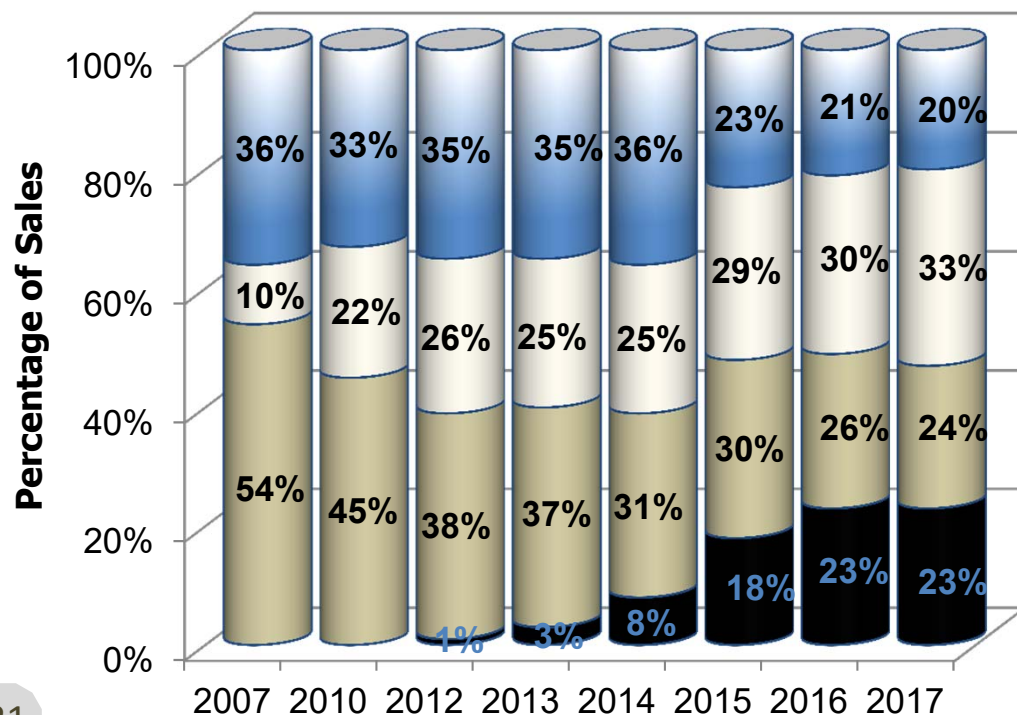


Data Source: CMM Retail Survey December 2017-150 Best Selling Models



Broad Distribution Channel

- Over 9,000 retail counters in China
- 30% of outlets in Tier 1 cities; 70% in Tier 2/3 cities



- Regional Stores
- AOS Specialty Stores
- Suning/Guomei
- E-Commerce



Product Line developed in China





Professional Team of Local Management





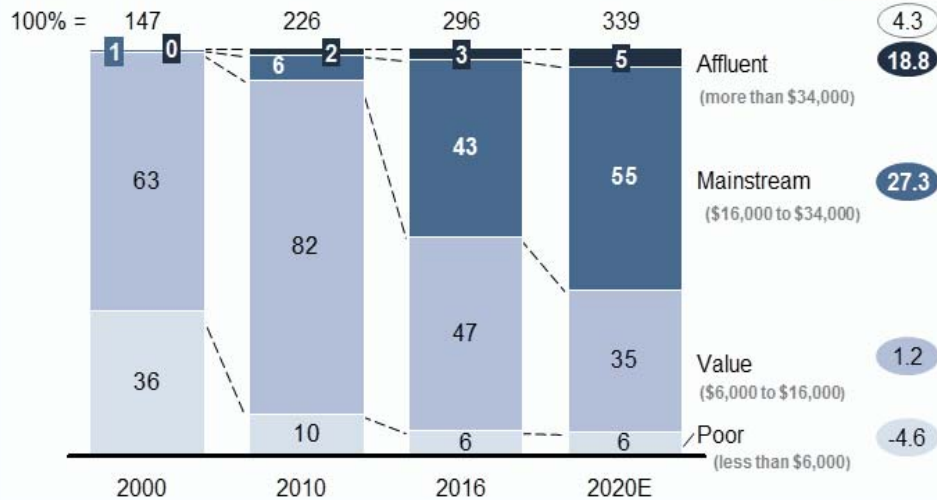
Mega Trends - China

Significant growth in AOS target demographic

Number of urban households by annual household income¹

Million households, percent

CAGR
2000-2020E, %



Brackets are defined by disposable income per urban household per year in real terms:
China's CPI rose 3.3% per year from 2010 to 2015

A. O. Smith customer demographic continues to grow rapidly

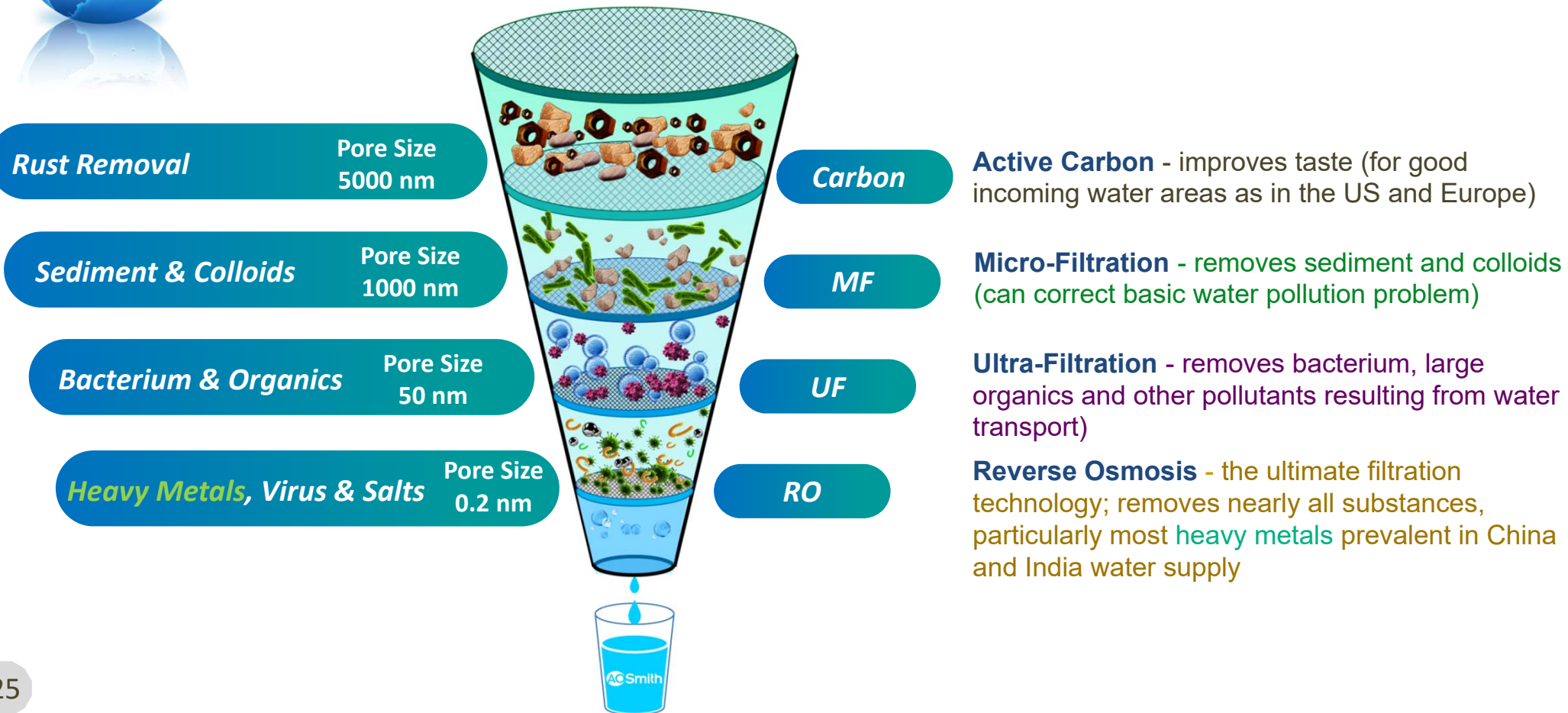
Growth of 10 times during this decade

- 2010: 18 mm households
- 2020: 200 mm households

Source: McKinsey Insights China – December 2015



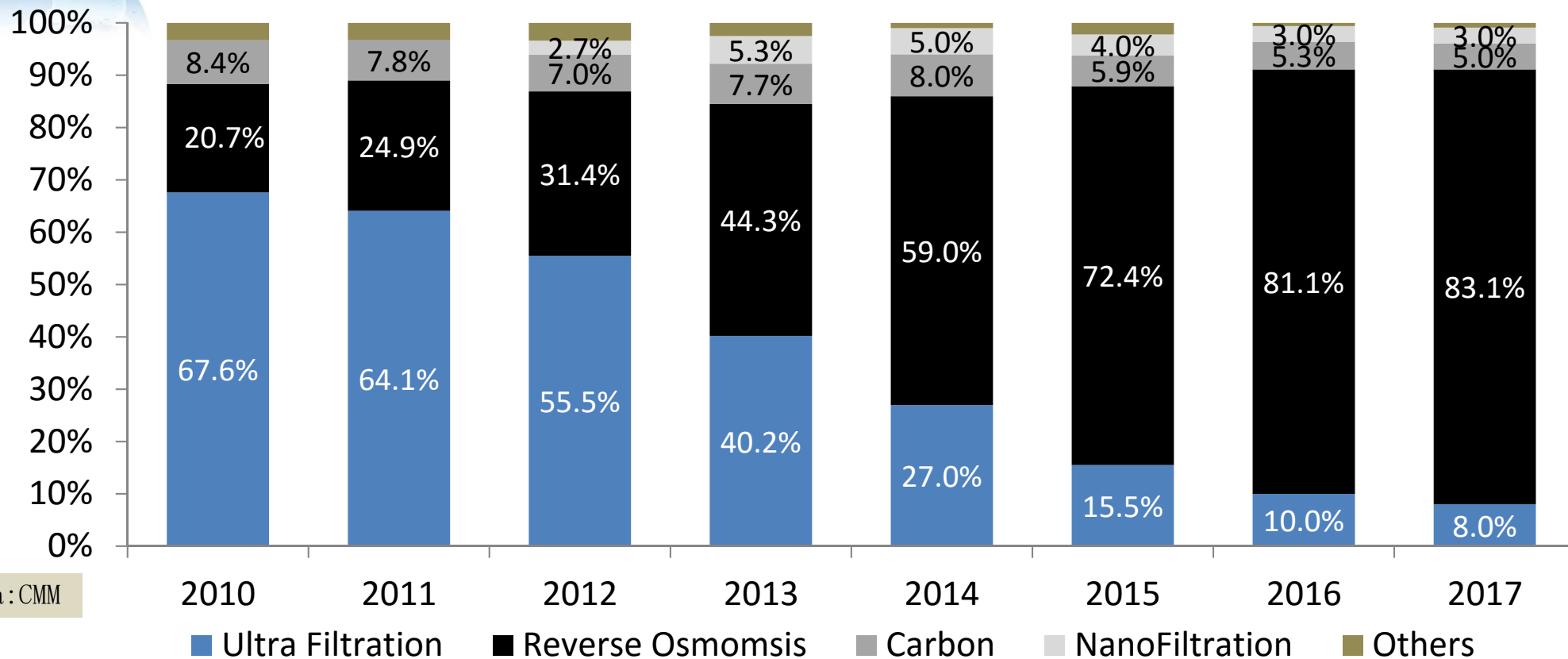
Different Water Treatment Technologies





Reverse Osmosis Is Gaining Market Share

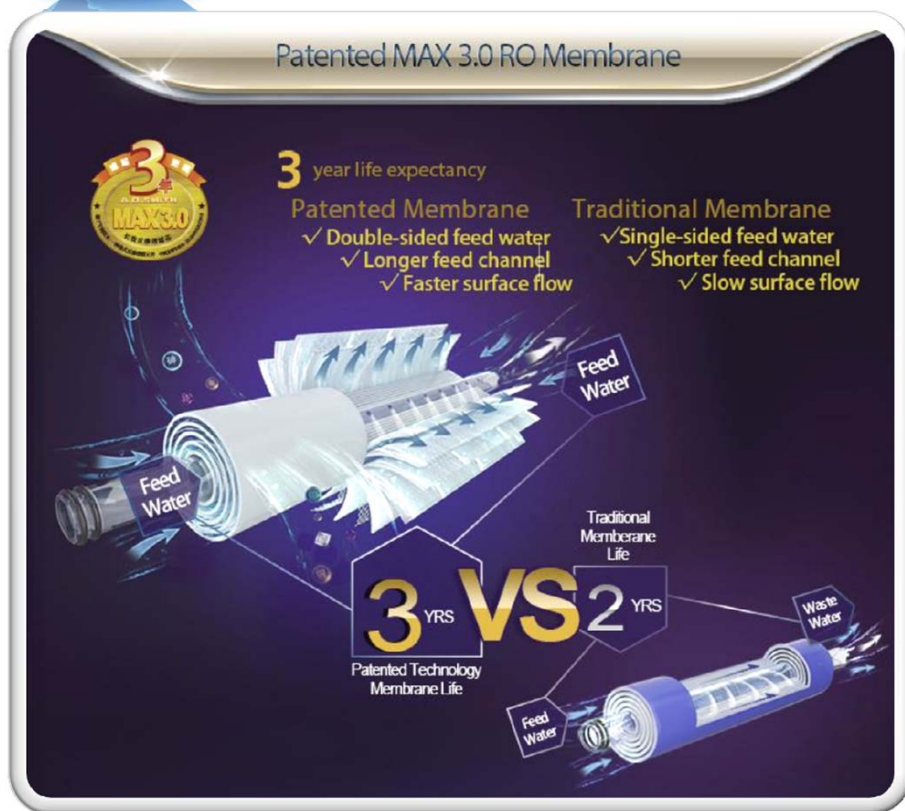
CMM Water Treatment Market by Technology



Data: CMM



Side Stream Membrane Technology

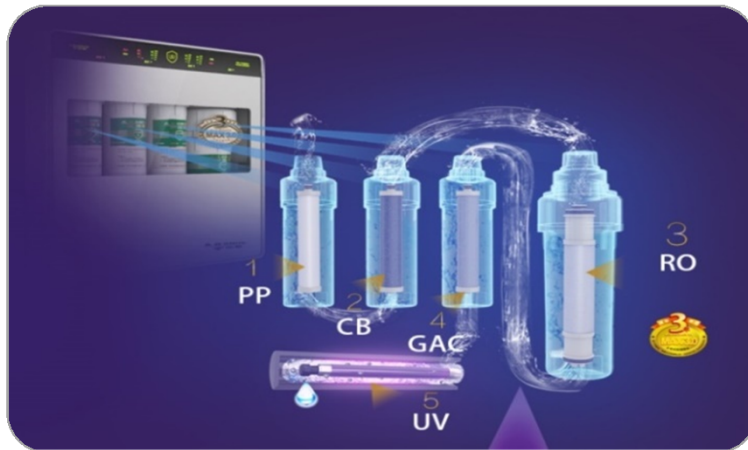


- Unique patented design
- Increases RO membrane life - industry leading three year life
- Reduces waste water up to 50 percent - 1 gallon clean to 1 gallon waste
- Provides market place differentiation

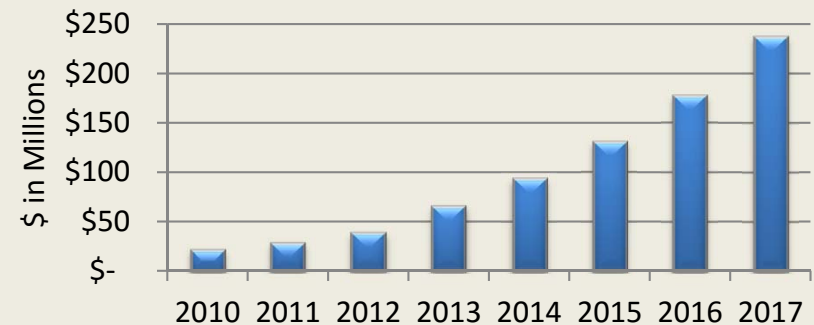


Tankless water treatment – enabled by side-stream membrane technology

- Provides immediate clean water
- Minimizes risk of post RO membrane contamination
 - No storage tank needed
- Leverages membrane rolling capabilities to produce hi-flow RO products
 - Constant flow rates up to 0.9 gallons per minute

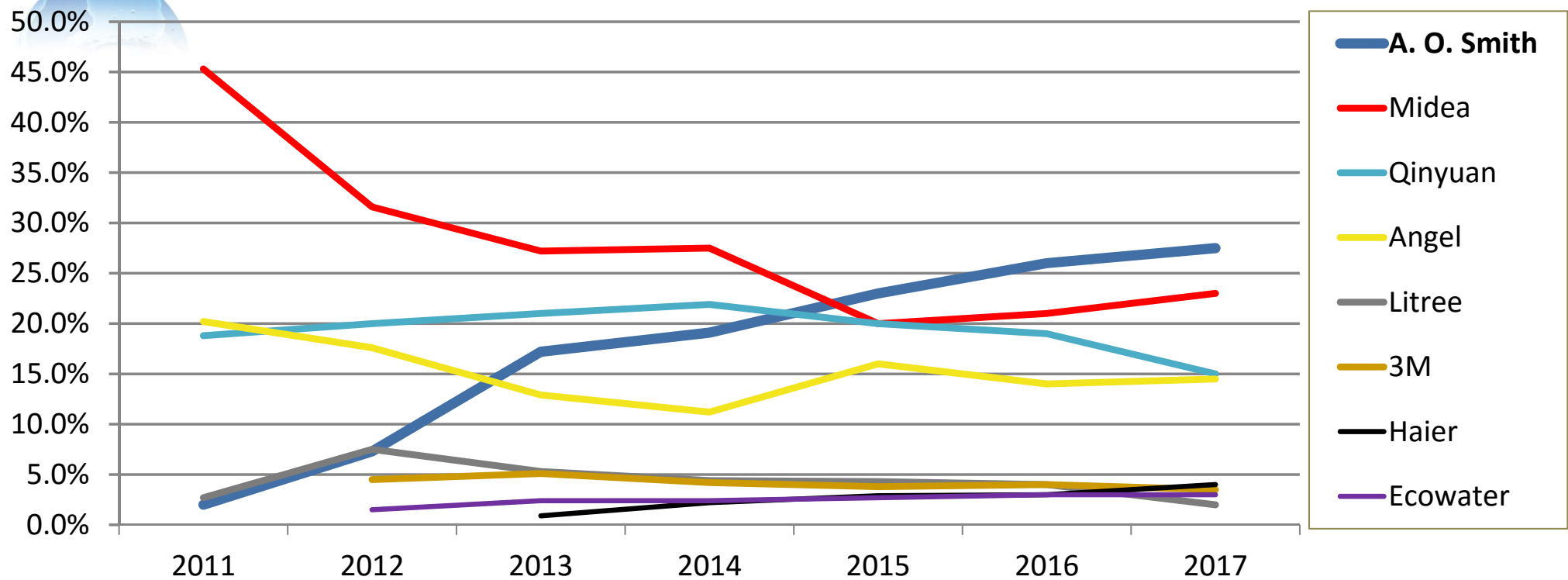


China Water Treatment Sales





Major Brands CMM Market Share By Value Water Purifier



Data Source: CMM-GFK December -2017

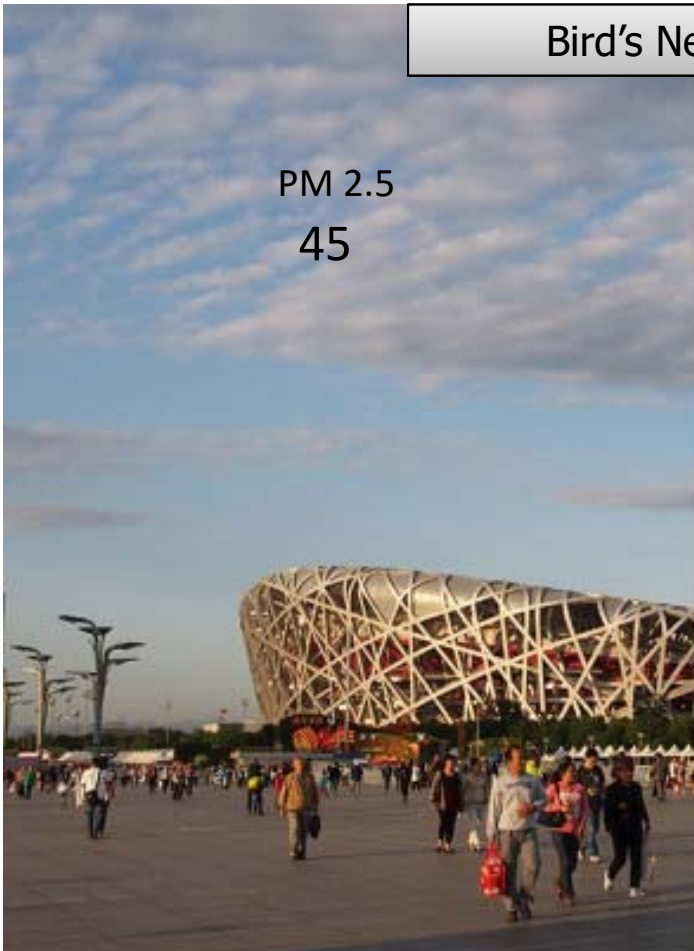


Air purifiers - the market need is clearly visible

Bird's Nest – Beijing:

PM 2.5
45

A healthy
day



PM 2.5
453

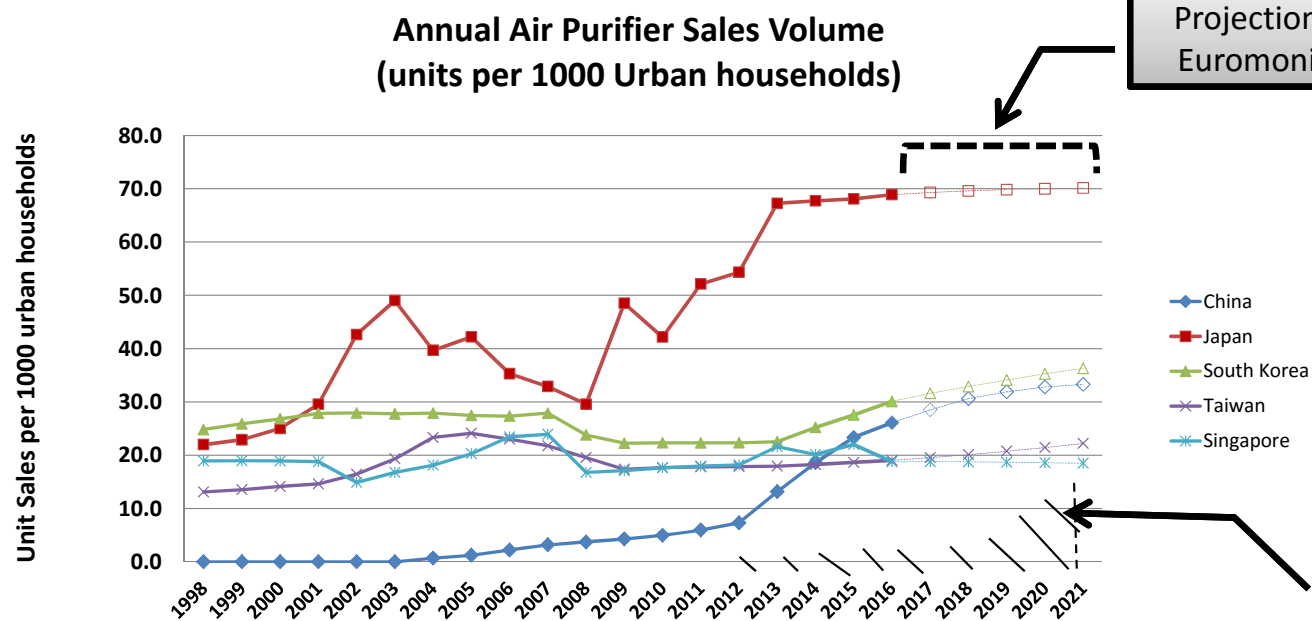
A very
unhealthy
day





China Air Purifier Market Growth Opportunity

Unit sales per 1000 Urban Households for China and its neighbors



China's air pollution may drive urban penetration closer to Japanese levels

6% household penetration overall;
21% penetration in top 23 ('first tier') cities

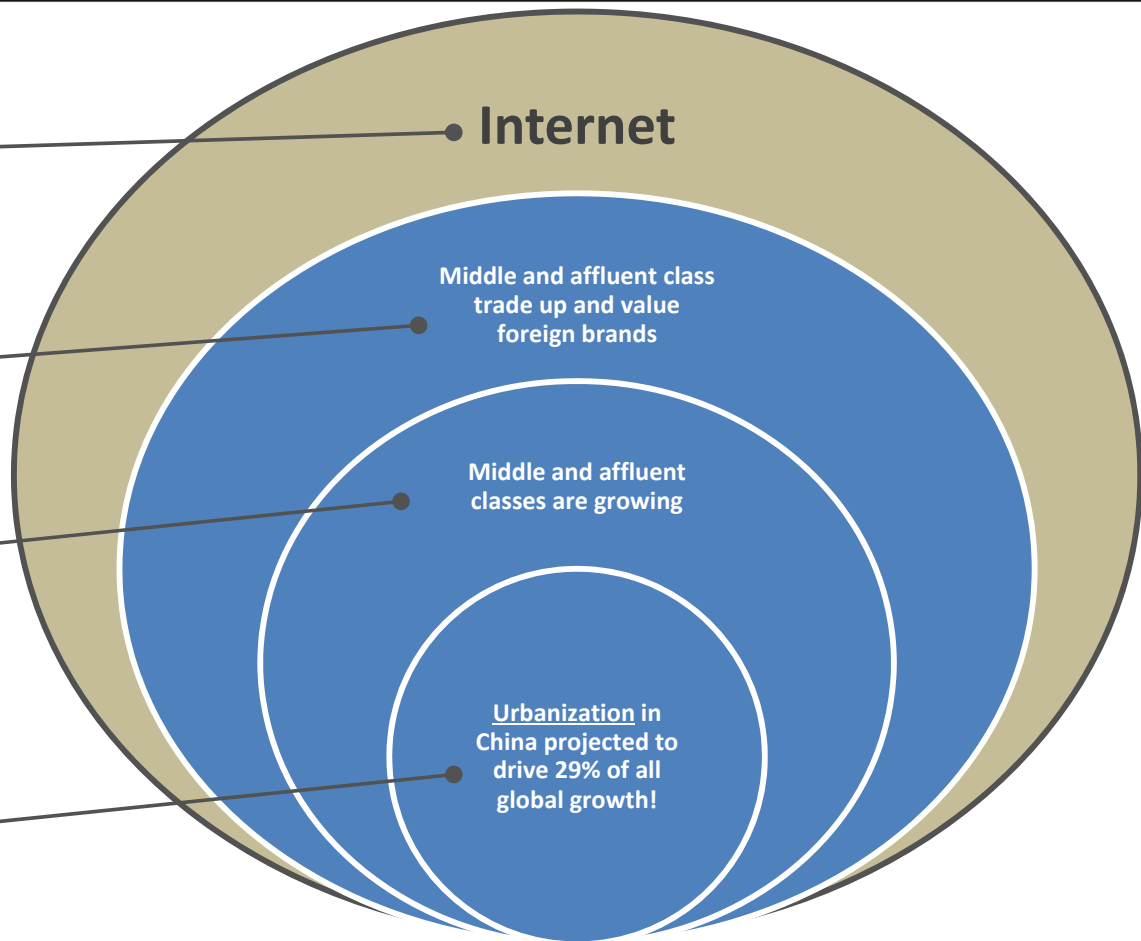
Source: Euromonitor, January 2016;

Note: For calculating penetration rate for China: assumed no replacement in the period



China Mega Trends Driving Growth

- We are positioned to reach consumers using the internet
- A. O. Smith is a strong foreign brand
- Our Premium Consumer brand is positioned for the middle and affluent classes
- A. O. Smith has manufacturing capacity and channel footprint to capitalize

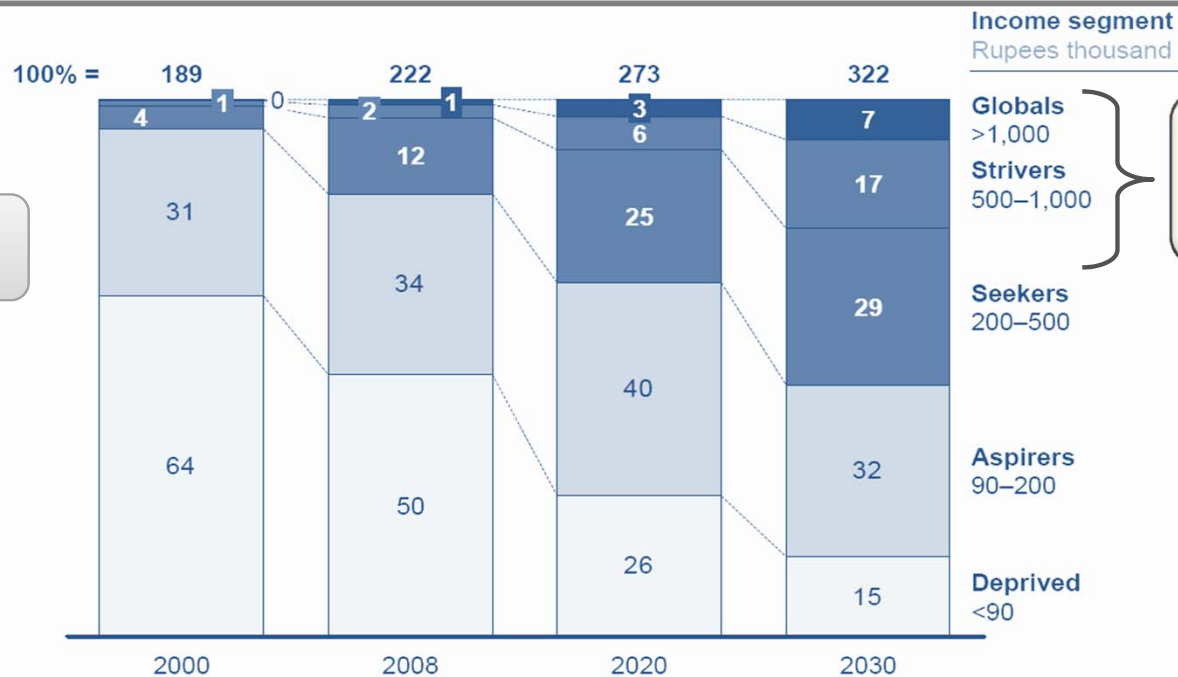




Mega Trends - India

Significant growth in AOS target demographic

Millions of households,
percent, 2000 prices



A. O. Smith target
demographic:
upper middle class

SOURCE: India Urbanization Econometric Model Updated 2010



Building Distribution



- A cities (pop >1.5 Mn) Distribution in 25 out of 25 cities
- B Class cities (pop .5 to 1.5) Mn) Distribution in 63 of 68
- Class C cities (pop .1 to .5 Mn) Distribution 316 of 400

NATIONAL RETAILERS



REGIONAL RETAILERS



Headquarters and Manufacturing (Bengaluru)



Major Distribution Locations



Business Model In India Similar to China

- Attractive Growth Demographics
- Leveraging Global Capabilities with Products Designed for the Indian Market
- Building Brand & Expanding our Distribution
- Introducing New Product Categories with Water Treatment
- Local Management

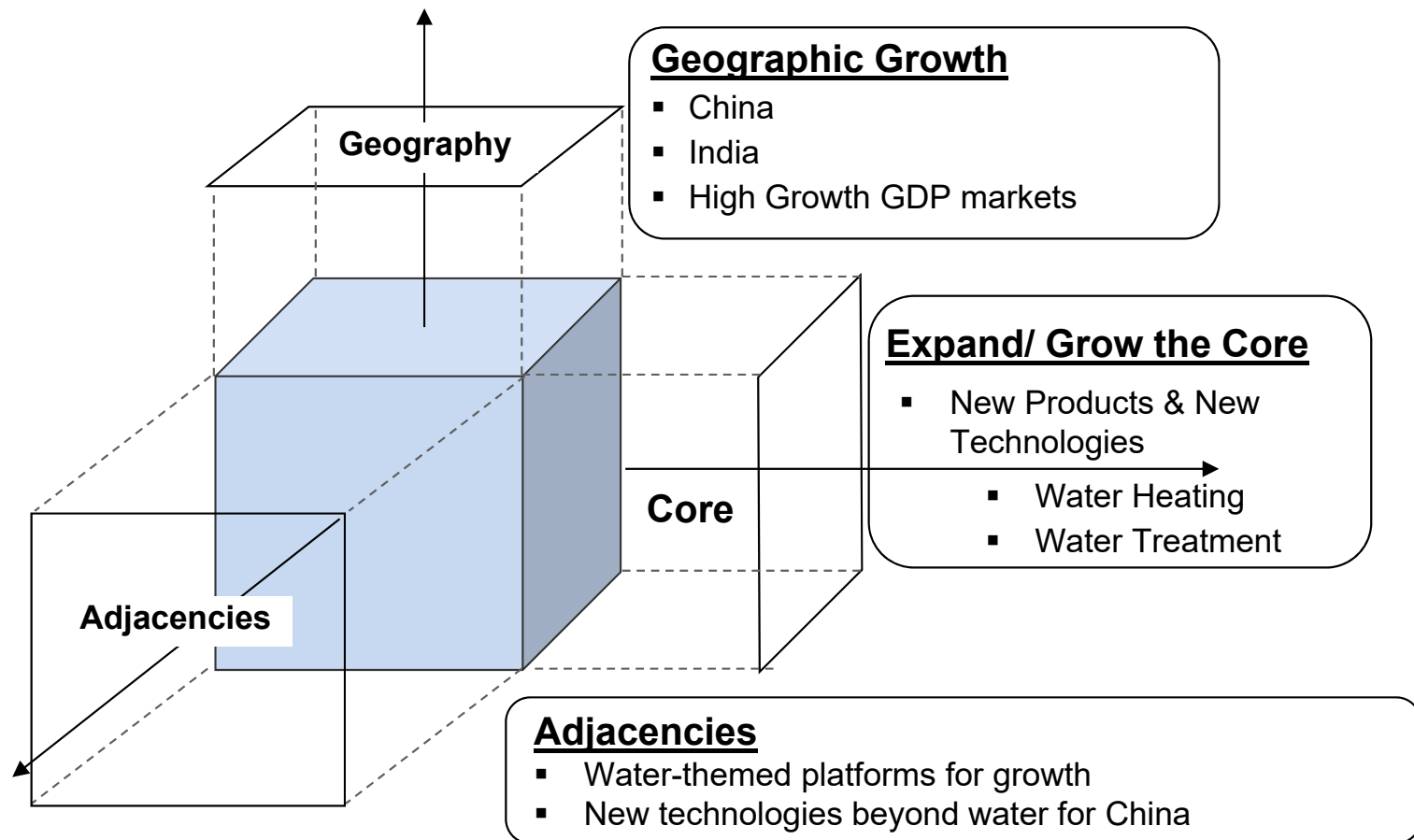


We are committed for the long term opportunity

Acquisition Strategy



Growth Strategy: Acquisitions





Investment Criteria

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

AOS

LISTED

NYSE

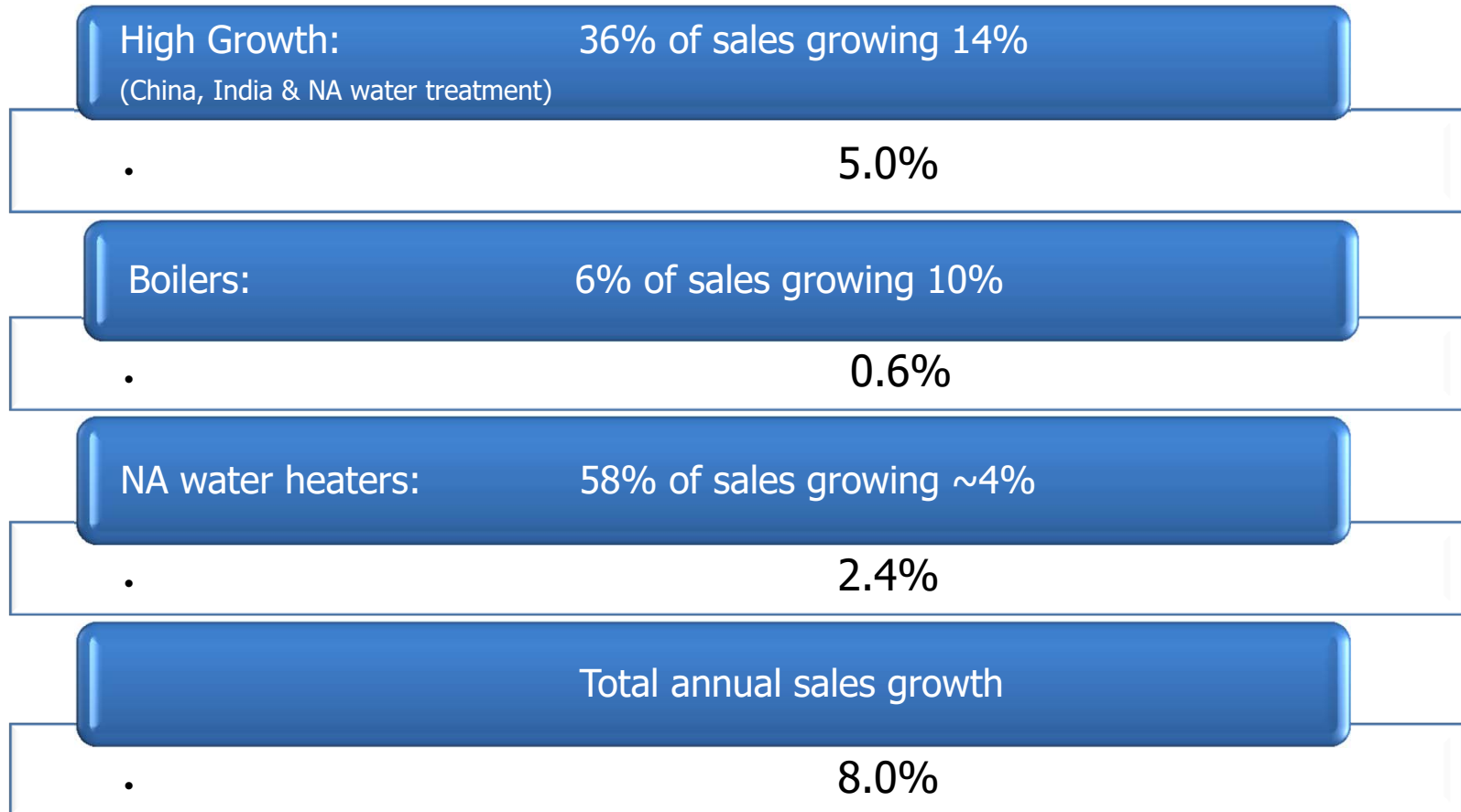


A. O. Smith's Capital Allocation Options

- Organic growth (capital expenditures)
- Acquisitions
 - \$387 million net cash
 - 15 percent leverage ratio (debt/total capital)
- Return cash to shareholders: \$260 million projected in 2018
 - Dividends
 - Increased 29 percent in first quarter 2018
 - Share repurchase
 - Expect to repurchase approximately \$135 million* in 2018 on a 10b5-1 plan and opportunistically in the open market



Growth Strategy: Organic Growth





China Growth Model





Growth and Stability

Offense

- Organic growth of 8%
 - High growth businesses growing approximately 14 percent
 - Boilers growing 10%
- Call option on NA new construction
- Significant cash and borrowing capacity for “value creating” acquisitions and share buyback

Defense

- NA water heaters and boilers ~85% replacement
- Market share leader in NA, China
- Strong balance sheet; net cash position approximately \$387 million
- Small exposure to Europe (\$50 million in revenues)

INVESTOR CONTACT

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Email: packerman@aosmith.com

APPENDIX



First Quarter Results

\$ in millions

	2018	2017	change	% chg.
Sales	\$ 788.0	\$ 740.1	\$ 47.9	6.5%
Net Earnings	98.8	87.7		
Restructuring & Impairment Expenses	<u>5.0</u>	<u>-</u>		
Adjusted Net Earnings	\$ <u><u>103.8</u></u>	\$ <u><u>87.7</u></u>	\$ 16.1	18%



First Quarter Adjusted EPS

\$ in millions

	2018	2017	change	% chg.
EPS	\$0.57	\$ 0.50		
Restructuring and Impairment Expenses	<u>0.03</u>	<u>-</u>		
Adjusted EPS	\$0.60	\$ 0.50	\$0.10	20%



First Quarter Sales

\$ in millions

	2018	2017	change	% chg.
North America	\$ 501.7	\$ 487.3	\$ 14.4	3%
Rest of World	293.8	259.5	34.3	13%
Intersegment	<u>(7.5)</u>	<u>(6.8)</u>	<u>(0.7)</u>	
Total	\$ <u>788.0</u>	\$ <u>740.0</u>	\$ <u>48.0</u>	6.5%



First Quarter Adjusted Earnings

\$ in millions, except percentages

Adjusted Segment Earnings

	2018	2017	change	% chg.
North America	\$ 112.7	\$ 104.2	\$ 8.5	8%
Rest of World	<u>36.0</u>	<u>32.4</u>	<u>3.6</u>	11%
Total Adjusted Segment Earnings	148.7	136.6	\$ 12.1	9%
Corporate	(14.3)	(14.0)	(0.3)	-2%
Interest Expense	<u>(2.3)</u>	<u>(2.2)</u>	<u>(0.1)</u>	
Adjusted Pre-tax Earnings	132.1	120.4	11.7	10%
Tax Provision	<u>(28.3)</u>	<u>(32.7)</u>		
Adjusted Net Earnings	\$ <u>103.8</u>	\$ <u>87.7</u>	\$ <u>16.1</u>	18%

Adjusted Segment Margin

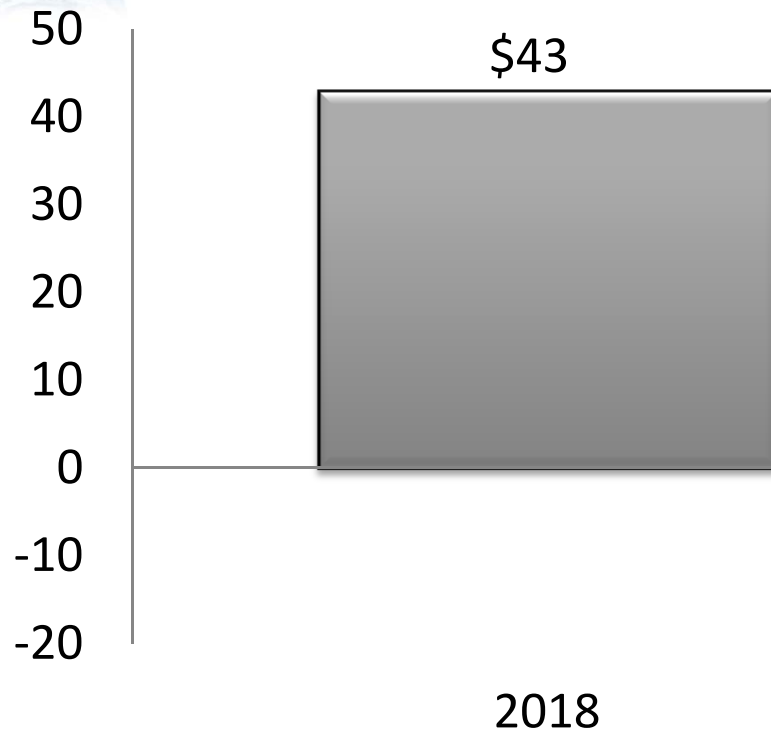
North America	22.5%	21.4%
Rest of World	12.3%	12.5%

Note: North America adjusted earnings exclude \$6.7 million of pre-tax charges for plant closing



Cash Flow from Operations

(\$ in millions)



Highlights

- Operating cash provided by operations of \$43 million
- Debt to capital ratio of 15%
- Cash balance: \$680 million
- Net cash position: \$387 million
- Stock repurchase: 520,000 shares totaling approximately \$33 million

2017



2018 EPS Guidance and 2017 EPS

As of January 30, 2018



Note: 2009 through 2014 and 2017 and 2018 are adjusted EPS and all years are adjusted for stock splits

* 2017 excludes \$0.47 per share related to U.S. tax reform

* 2018 excludes \$0.03 per share related to plant closing



2018 Assumptions

(\$ in millions)

Operating Cash Flow
Capital Expenditures
Depreciation and Amortization
Corporate/Other Expense
Effective Tax Rate
Stock Repurchase
Share Count - Diluted

2018 Projections

approximately \$475
approximately \$100
approximately \$ 80
approximately \$ 48
approximately 22%
approximately \$135*
approximately 173 million

* subject to acquisitions, cash flow and working capital needs

As of April 25, 2018



2018 Outlook

■ Tailwinds

- U.S. residential water heater industry volumes increase 250,000 to 300,000 units, including tankless;
- Boiler revenue growth of approximately ten percent
- Announced 10% average price increase on U.S. wholesale water heaters related to steel and other cost inflation effective early June
- China currency translation benefits
- Smaller expected losses in India than in 2017

■ Headwinds

- Higher steel costs
- Air purification and pre-buy negatively impact China sales
- New China water treatment plant incremental costs of approximately \$5 million



2018 Outlook - continued

- Revenue growth between 10 and 10.75 percent in USD
- Adjusted EPS between \$2.55 and \$2.61
- North America segment margin expected to be 21.75 to 22.25 percent
- Rest of World segment margin expected to expand at least 30 to 40 basis points from 2017



Adjusted Earnings and Adjusted EPS

(dollars in millions except per share data)

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

Three Months Ended
March 31,

2018

2017

Net Earnings (GAAP)

\$ 98.8

\$ 87.7

Restructuring and impairment expenses, before tax

6.7

-

Tax effect of restructuring and impairment expenses

(1.7)

-

Adjusted Earnings

\$103.8

\$ 87.7

Dilute EPS (GAAP)

\$ 0.57

\$ 0.50

Restructuring and impairment expenses per diluted share, before tax

0.04

-

Tax effect of restructuring and impairment expenses per diluted share

(0.01)

-

Adjusted EPS

\$ 0.60

\$ 0.50



Adjusted Segment Earnings

(dollars in millions)

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

Segment Earnings (GAAP)

North America
Rest of World
Inter-segment earnings elimination
Total Segment Earnings (GAAP)

Adjustments:

North America restructuring and impairment expenses
Rest of World
Inter-segment earnings elimination
Total Adjustments

Adjusted Segment Earnings

North America
Rest of World
Inter-segment earnings elimination
Total Adjusted Segment Earnings

Three Months Ended
March 31,

2018

2017

\$106.0	\$ 104.2
36.1	32.5
(0.1)	(0.1)
<u>\$142.0</u>	<u>\$ 136.6</u>
\$ 6.7	\$ -
-	-
-	-
<u>\$ 6.7</u>	<u>\$ -</u>
\$112.7	\$ 104.2
36.1	32.5
(0.1)	(0.1)
<u>\$148.7</u>	<u>\$ 136.6</u>



Adjusted 2018 EPS Guidance and Adjusted 2017 EPS

(unaudited)

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

	2018 Guidance	2017
Diluted EPS (GAAP)	\$2.52 - 2.58	\$ 1.70
Restructuring and impairment per diluted share	0.03	-
U.S. Tax Reform income tax expense per diluted share	<u>-</u>	<u>0.47</u>
Adjusted EPS	<u><u>\$2.55 - 2.61</u></u>	<u><u>\$ 2.17</u></u>



Corporate Responsibility and Sustainability – Aligns with our Values

A. O. Smith will preserve its good name



**Social
Contribution**



A. O. Smith will be a good citizen

**Environmental
Impacts**



**Ethics and
Compliance**
Fundamentals for Success



A. O. Smith will emphasize innovation



**Diverse & Safe
Workforce**

A. O. Smith will be a
good place to work



**Product
Responsibility**





Products – Efficiency, Conservation and Innovation

Energy Efficiency

- We believe our global product portfolio is the most efficient in the industry
- Our electric residential water heaters achieve efficiency factors of .95 or above
- Our highly efficient Cyclone condensing commercial water heaters represent 24% of commercial units sold
- 83 percent of Lochinvar branded boilers achieve over 90 percent thermal efficiency
- 55 percent of our China products exceed government efficiency standards

Conservation

- Our patented Reverse Osmosis (RO) membrane wastes 50 percent less water than traditional RO and represents over 90 percent of A. O. Smith branded water treatment sales





Manufacturing Plants – Reducing Energy Usage, Water Consumption and Environmental Impacts

- Chairman's Green Star award established in 2009– annual competition given to the plant which demonstrates the largest social, economic and environmental benefit over a three year period
- Johnson City, TN - plant certified Leadership in Energy and Environmental Design (LEED) Silver since 2011 and certified Energy Star ®
- Ashland City, TN - largest water heater plant in the world – reduced electricity usage by 9 percent as a result of a plant-wide lighting project in 2011 and reduced water usage by 36 percent as a result of an enhanced parts washing process implemented in 2014
- Nanjing, China – implemented an innovative pre-treatment process as an alternative to phosphorus pre-treating, reducing chemical discharges and improving corrosion resistance of our water heater tanks





People – Doing Business Safely, with Integrity and Supporting Communities

- Established in 1954, the President's Safety Award annually recognizes the plant with best record for workplace safety
- Established in 1955, the A. O. Smith Foundation supports our communities
- Guiding Principles established in 1999 describes our code of conduct and values
- Values Recognition Program established in 1995 recognizes employee contributions to community involvement

