

REGAL BELOIT CORP  
Form 10-Q  
November 06, 2017

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

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF  
1934

for the quarterly period ended September 30, 2017 or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF  
1934

Commission file number 001-07283

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

Wisconsin 39-0875718  
(State of other jurisdiction of (IRS Employer  
incorporation) Identification No.)  
200 State Street, Beloit, Wisconsin 53511  
(Address of principal executive office)  
(608) 364-8800  
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.

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

YES  NO

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer  Accelerated Filer   
Non-accelerated filer  (Do not check if a smaller reporting company) Smaller Reporting Company   
Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES  NO

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As of November 2, 2017 there were 44,304,003 shares of the registrant's common stock, \$.01 par value per share, outstanding.

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REGAL BELOIT CORPORATION  
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## CAUTIONARY STATEMENT

Certain statements made in this Quarterly Report on Form 10-Q are “forward-looking statements” intended to qualify for the safe harbor from liability established by the Private Securities Litigation Reform Act of 1995. Forward-looking statements are based on management’s expectations, beliefs, current assumptions, and projections. When used in this Quarterly Report on Form 10-Q, words such as “may,” “will,” “expect,” “intend,” “estimate,” “forecast,” “anticipate,” “believe,” “should,” “project” or “plan” or the negative thereof or similar words are intended to identify forward-looking statements. These forward-looking statements are not guarantees of future performance and are subject to risks, uncertainties, assumptions and other factors, some of which are beyond our control, which could cause actual results to differ materially from those expressed or implied by such forward-looking statements. Those factors include, but are not limited to:

- uncertainties regarding our ability to execute our restructuring plans within expected costs and timing;
  - increases in our overall debt levels as a result of the acquisition of the Power Transmission Solutions business of Emerson Electric Co. ("PTS") or otherwise and our ability to repay principal and interest on our outstanding debt;
  - actions taken by our competitors and our ability to effectively compete in the increasingly competitive global electric motor, drives and controls, power generation and mechanical motion control industries;
  - our ability to develop new products based on technological innovation and marketplace acceptance of new and existing products;
  - fluctuations in commodity prices and raw material costs;
  - our dependence on significant customers;
  - issues and costs arising from the integration of acquired companies and businesses including PTS and the timing and impact of purchase accounting adjustments;
  - prolonged declines in oil and gas up stream capital spending;
  - economic changes in global markets where we do business, such as reduced demand for the products we sell, currency exchange rates, inflation rates, interest rates, recession, government policies, including policy changes affecting taxation, trade, immigration and the like, and other external factors that we cannot control;
  - product liability and other litigation, or claims by end users, government agencies or others that our products or our customers’ applications failed to perform as anticipated, particularly in high volume applications or where such failures are alleged to be the cause of property or casualty claims;
  - unanticipated liabilities of acquired businesses;
  - unanticipated costs or expenses we may incur related to product warranty issues;
  - our dependence on key suppliers and the potential effects of supply disruptions;
  - infringement of our intellectual property by third parties, challenges to our intellectual property and claims of infringement by us of third party technologies;
  - effects on earnings of any significant impairment of goodwill or intangible assets;
  - cyclical downturns affecting the global market for capital goods;
  - and
- other risks and uncertainties including but not limited to those described in “Risk Factors” in our Annual Report on Form 10-K and from time to time in our reports filed with US Securities and Exchange Commission.

Shareholders, potential investors, and other readers are urged to consider these factors in evaluating the forward-looking statements and cautioned not to place undue reliance on such forward-looking statements. The forward-looking statements included in this Quarterly Report on Form 10-Q are made only as of the date of this report, and we undertake no obligation to update these statements to reflect subsequent events or circumstances. Additional information regarding these and other risks and factors is included in Part I - Item 1A - Risk Factors in our Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 1, 2017.



## PART I—FINANCIAL INFORMATION

## ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

## REGAL BELOIT CORPORATION

## CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(Amounts in Millions, Except Per Share Data)

	Three Months Ended		Nine Months Ended	
	September 30, 2017	October 1, 2016	September 30, 2017	October 1, 2016
Net Sales	\$856.9	\$ 809.6	\$2,539.6	\$ 2,466.4
Cost of Sales	629.9	577.9	1,874.0	1,794.4
Gross Profit	227.0	231.7	665.6	672.0
Operating Expenses	133.0	141.9	413.8	421.5
Income From Operations	94.0	89.8	251.8	250.5
Interest Expense	13.5	14.4	42.6	44.2
Interest Income	0.7	1.1	2.7	3.4
Income Before Taxes	81.2	76.5	211.9	209.7
Provision For Income Taxes	17.6	15.4	46.4	47.5
Net Income	63.6	61.1	165.5	162.2
Less: Net Income Attributable to Noncontrolling Interests	1.4	1.5	4.0	4.4
Net Income Attributable to Regal Beloit Corporation	\$62.2	\$ 59.6	\$161.5	\$ 157.8
Earnings Per Share Attributable to Regal Beloit Corporation:				
Basic	\$1.40	\$ 1.33	\$3.62	\$ 3.53
Assuming Dilution	\$1.39	\$ 1.32	\$3.59	\$ 3.51
Cash Dividends Declared Per Share	\$0.26	\$ 0.24	\$0.76	\$ 0.71
Weighted Average Number of Shares Outstanding:				
Basic	44.4	44.8	44.7	44.7
Assuming Dilution	44.8	45.0	45.0	45.0

See accompanying Notes to Condensed Consolidated Financial Statements

REGAL BELOIT CORPORATION  
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
 (Unaudited)  
 (Dollars in Millions)

	Three Months Ended September 30, 2017		September 1, 2016		Nine Months Ended September 30, 2017		September 1, 2016	
Net Income	\$63.6	\$ 61.1			\$165.5	\$ 162.2		
Other Comprehensive Income (Loss) Net of Tax:								
Foreign Currency Translation Adjustments	24.6	(2.4	)		93.1	(9.2	)	
Hedging Activities:								
Increase (Decrease) in Fair Value of Hedging Activities, Net of Tax Effects of \$5.5 Million and \$(3.8) Million for the Three Months ended September 30, 2017 and October 1, 2016 and \$23.5 Million and \$(9.2) Million for the Nine Months ended September 30, 2017 and October 1, 2016 Respectively	8.8	(6.3	)		38.2	(15.1	)	
Reclassification of Losses included in Net Income, Net of Tax Effects of \$(0.2) Million and \$4.6 Million for the Three Months ended September 30, 2017 and October 1, 2016 and \$6.0 Million and \$14.3 Million for the Nine Months ended September 30, 2017 and October 1, 2016 Respectively	(0.1	)	7.7		9.9	23.4		
Pension and Post Retirement Plans:								
Reclassification Adjustments for Pension and Post Retirement Benefits included in Net Income, Net of Tax Effects of \$0.2 Million and \$0.3 Million for the Three Months Ended September 30, 2017 and October 1, 2016 and \$0.6 Million and \$0.9 Million for the Nine Months Ended September 30, 2017 and October 1, 2016, Respectively	0.4	0.5			1.2	1.8		
Other Comprehensive Income (Loss)	33.7	(0.5	)		142.4	0.9		
Comprehensive Income	97.3	60.6			307.9	163.1		
Less: Comprehensive Income Attributable to Noncontrolling Interests	2.0	1.6			5.6	4.0		
Comprehensive Income Attributable to Regal Beloit Corporation	\$95.3	\$ 59.0			\$302.3	\$ 159.1		
See accompanying Notes to Condensed Consolidated Financial Statements								

REGAL BELOIT CORPORATION  
CONDENSED CONSOLIDATED BALANCE SHEETS  
(Unaudited)  
(Dollars in Millions, Except Per Share Data)

	September 30, 2017	December 31, 2016
<b>ASSETS</b>		
Current Assets:		
Cash and Cash Equivalents	\$ 186.6	\$ 284.5
Trade Receivables, Less Allowances of \$10.2 Million in 2017 and \$11.5 Million in 2016	527.3	462.2
Inventories	734.9	660.8
Prepaid Expenses and Other Current Assets	181.4	124.5
Total Current Assets	1,630.2	1,532.0
Net Property, Plant and Equipment	633.7	627.5
Goodwill	1,475.2	1,453.2
Intangible Assets, Net of Amortization	682.4	711.7
Deferred Income Tax Benefits	28.7	22.4
Other Noncurrent Assets	13.8	11.7
Total Assets	\$ 4,464.0	\$ 4,358.5
<b>LIABILITIES AND EQUITY</b>		
Current Liabilities:		
Accounts Payable	\$ 417.2	\$ 334.2
Dividends Payable	11.5	10.7
Current Hedging Obligations	9.1	49.0
Accrued Compensation and Employee Benefits	78.8	70.1
Other Accrued Expenses	117.7	137.0
Current Maturities of Long-Term Debt	100.6	100.6
Total Current Liabilities	734.9	701.6
Long-Term Debt	1,113.8	1,310.9
Deferred Income Taxes	158.6	97.7
Noncurrent Hedging Obligations	0.6	17.6
Pension and Other Post Retirement Benefits	102.8	106.5
Other Noncurrent Liabilities	50.9	46.0
Commitments and Contingencies (see Note 12)		
Equity:		
Regal Beloit Corporation Shareholders' Equity:		
Common Stock, \$.01 par value, 100.0 Million Shares Authorized, 44.3 Million and 44.8 Million Shares Issued and Outstanding in 2017 and 2016, Respectively	0.4	0.4
Additional Paid-In Capital	874.5	904.5
Retained Earnings	1,571.5	1,452.0
Accumulated Other Comprehensive Loss	(177.3	) (318.1 )
Total Regal Beloit Corporation Shareholders' Equity	2,269.1	2,038.8
Noncontrolling Interests	33.3	39.4
Total Equity	2,302.4	2,078.2
Total Liabilities and Equity	\$ 4,464.0	\$ 4,358.5

See accompanying Notes to Condensed Consolidated Financial Statements.



REGAL BELOIT CORPORATION  
CONDENSED CONSOLIDATED STATEMENTS OF EQUITY  
(Unaudited)  
(Dollars in Millions, Except Per Share Data)

	Common Stock \$.01 Par Value	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Non- controlling Interests	Total Equity
Balance as of January 2, 2016	\$ 0.4	\$ 900.8	\$ 1,291.1	\$ (255.0 )	\$ 45.5	\$ 1,982.8
Net Income	—	—	157.8	—	4.4	162.2
Other Comprehensive Income (Loss)	—	—	—	1.3	(0.4 )	0.9
Dividends Declared (\$0.71 Per Share)	—	—	(31.7 )	—	—	(31.7 )
Stock Options Exercised, Including Income Tax Benefit and Share Cancellations	—	(2.1 )	—	—	—	(2.1 )
Dividends Declared to Noncontrolling Interests	—	—	—	—	(0.3 )	(0.3 )
Share-based Compensation	—	10.1	—	—	—	10.1
Purchase of Subsidiary Shares from Noncontrolling Interest	—	(7.2 )	—	(2.7 )	(9.7 )	(19.6 )
Balance as of October 1, 2016	\$ 0.4	\$ 901.6	\$ 1,417.2	\$ (256.4 )	\$ 39.5	\$ 2,102.3

	Common Stock \$.01 Par Value	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Non- controlling Interests	Total Equity
Balance as of December 31, 2016	\$ 0.4	\$ 904.5	\$ 1,452.0	\$ (318.1 )	\$ 39.4	\$ 2,078.2
Net Income	—	—	161.5	—	4.0	165.5
Other Comprehensive Income	—	—	—	140.8	1.6	142.4
Dividends Declared (\$0.76 Per Share)	—	—	(33.9 )	—	—	(33.9 )
Stock Options Exercised	—	(3.3 )	—	—	—	(3.3 )
Stock Repurchase	—	(37.0 )	(8.1 )	—	—	(45.1 )
Dividends Declared to Noncontrolling Interests	—	—	—	—	(11.7 )	(11.7 )
Share-based Compensation	—	10.3	—	—	—	10.3
Balance as of September 30, 2017	\$ 0.4	\$ 874.5	\$ 1,571.5	\$ (177.3 )	\$ 33.3	\$ 2,302.4

See accompanying Notes to Condensed Consolidated Financial Statements.

REGAL BELOIT CORPORATION  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
 (Unaudited)  
 (Dollars in Millions)

	Nine Months Ended	
	September 30, 2017	October 1, 2016
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net Income	\$ 165.5	\$ 162.2
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities (Net of Acquisitions and Divestitures):		
Depreciation and Amortization	103.1	116.6
(Gain) Loss on Sale or Disposition of Assets, Net	(2.0 )	0.9
Share-Based Compensation Expense	10.3	10.1
Exit of Business	3.9	—
Gain on Sale of Businesses	(0.1 )	(11.6 )
Change in Operating Assets and Liabilities, Net of Acquisitions and Divestitures	(45.7 )	52.2
Net Cash Provided By Operating Activities	235.0	330.4
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Additions to Property, Plant and Equipment	(49.0 )	(46.1 )
Sales of Investment Securities	0.9	43.2
Purchases of Investment Securities	(0.9 )	(53.7 )
Proceeds from Sale of Businesses	1.1	25.5
Proceeds from Sale of Assets	5.9	1.6
Net Cash Used In Investing Activities	(42.0 )	(29.5 )
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Borrowings Under Revolving Credit Facility	938.4	447.0
Repayments Under Revolving Credit Facility	(926.9 )	(437.0 )
Proceeds from Short-Term Borrowings	18.2	20.9
Repayments of Short-Term Borrowings	(18.2 )	(27.7 )
Proceeds from Long-Term Borrowings	0.3	—
Repayments of Long-Term Borrowings	(212.2 )	(218.1 )
Dividends Paid to Shareholders	(33.1 )	(31.3 )
Shares Surrendered for Taxes	(3.7 )	(2.2 )
Proceeds from the Exercise of Stock Options	0.4	0.5
Payments of Contingent Consideration	(5.3 )	—
Repurchase of Common Stock	(45.1 )	—
Distributions to Noncontrolling Interests	(11.7 )	(0.3 )
Purchase of Subsidiary Shares from Noncontrolling Interest	—	(19.6 )
Net Cash Used In Financing Activities	(298.9 )	(267.8 )
<b>EFFECT OF EXCHANGE RATES ON CASH AND CASH EQUIVALENTS</b>	<b>8.0</b>	<b>(4.4 )</b>
Net Increase (Decrease) in Cash and Cash Equivalents	(97.9 )	28.7
Cash and Cash Equivalents at Beginning of Period	284.5	252.9
Cash and Cash Equivalents at End of Period	\$ 186.6	\$ 281.6
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION</b>		
Cash Paid For:		
Interest	\$ 46.8	\$ 46.7
Income taxes	\$ 45.0	\$ 54.6

See accompanying Notes to Condensed Consolidated Financial Statements.

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REGAL BELOIT CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2017

(Unaudited)

1. BASIS OF PRESENTATION

The accompanying (a) condensed consolidated balance sheet of Regal Beloit Corporation (the "Company") as of December 31, 2016, which has been derived from audited consolidated financial statements, and (b) unaudited interim condensed consolidated financial statements as of September 30, 2017 and for the three and nine months ended September 30, 2017 and October 1, 2016, have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and note disclosures normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States ("GAAP"), have been condensed or omitted pursuant to those rules and regulations, although the Company believes that the disclosures made are adequate to make the information not misleading.

It is suggested that these condensed consolidated financial statements be read in conjunction with the consolidated financial statements and the notes thereto included in the Company's 2016 Annual Report on Form 10-K filed on March 1, 2017.

In the opinion of management, all adjustments considered necessary for a fair presentation of financial results have been made. Except as otherwise discussed, such adjustments consist of only those of a normal recurring nature.

Operating results for the three and nine months ended September 30, 2017 are not necessarily indicative of the results that may be expected for the entire fiscal year ending December 30, 2017.

The condensed consolidated financial statements have been prepared in accordance with GAAP, which require the Company to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and revenues and expenses during the periods reported. Actual results could differ from those estimates. The Company uses estimates in accounting for, among other items, allowance for doubtful accounts; excess and obsolete inventory; share-based compensation; acquisitions; product warranty obligations; pension and post retirement assets and liabilities; derivative fair values; goodwill and other asset impairments; health care reserves; retirement benefits; rebates and incentives; litigation claims and contingencies, including environmental matters; and income taxes. The Company accounts for changes to estimates and assumptions when warranted by factually based experience.

The Company operates on a 52/53 week fiscal year ending on the Saturday closest to December 31.

New Accounting Standards

In August 2017, the Financial Accounting Standards Board (the "FASB") issued Accounting Standards Update ("ASU") 2017-12, Derivatives and Hedging (Topic 815) - Targeted Improvements to Accounting for Hedging Activities. The amendments in this update better align an entity's risk management activities and financial reporting for hedging relationships through changes to both the designation and measurement guidance for qualifying hedging relationships and the presentation of hedge results. The ASU is effective for annual periods beginning after December 15, 2018, and interim periods within those annual periods. The Company plans to adopt this pronouncement for fiscal years beginning December 30, 2018. Early adoption is permitted. The Company is currently evaluating the impact of the pending adoption of this standard on its consolidated financial statements.

In May 2017, the FASB issued ASU 2017-09, Stock Compensation - Scope of Modification Accounting. The ASU amends the scope of modification accounting for share-based payment arrangements. The ASU provides guidance on the types of changes to the terms or conditions of share-based payment awards to which an entity would be required to apply modification accounting under Accounting Standards Codification ("ASC") 718. Specifically, an entity would not apply modification accounting if the fair value, vesting conditions, and classification of the awards are the same immediately before and after the modification. The ASU is effective for annual periods beginning after December 15, 2017, and interim periods within those annual periods. Early adoption is permitted and prospective application is required. The Company plans to adopt this pronouncement for fiscal years beginning December 31, 2017 and will

consider the impact that this standard may have on future share based award changes, should they occur.

In February 2017, the FASB issued ASU 2017-07, Compensation - Retirement Benefits: Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost. The ASU amends current guidance to require employers that present a measure of operating income in their statement of income to include only the service cost component of net periodic pension cost and net periodic postretirement benefit cost in operating expenses (together with other employee compensation costs). The other components of net benefit cost, including amortization of prior service cost/credit, and settlement and curtailment effects, are to be included in nonoperating expenses. Employers that do not present a measure of operating income are required to include the service cost component in the same line item as other employee compensation costs. The ASU also stipulates that only the

service cost component of net benefit cost is eligible for capitalization. The changes, which respond to input from financial statement users, are intended to classify costs according to their natures, and better align the effect of defined benefit plans on operating income with International Financial Reporting Standards. The ASU is effective for annual periods beginning after December 15, 2017, and interim periods within those annual periods. The Company plans to adopt this pronouncement for fiscal years beginning December 31, 2017. The ASU will impact the components of income before taxes but will not impact the amount of income before taxes.

In February 2016, the FASB issued ASU 2016-02, Leases. The core principle of ASU 2016-02 is that an entity should recognize on its balance sheet assets and liabilities arising from a lease. In accordance with that principle, ASU 2016-02 requires that a lessee recognize a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying leased asset for the lease term. The recognition, measurement, and presentation of expenses and cash flows arising from a lease by a lessee will depend on the lease classification as a finance or operating lease. This new accounting guidance is effective for fiscal years beginning after December 15, 2018 under a modified retrospective approach and early adoption is permitted. The Company has identified a six step process to successfully implement the new Lease standard: Form a task force to become experts and take the lead on understanding and implementing the new Lease standard; Update lease inventories; Decide on transition method; Review legal agreements and debt covenants; Consider IT needs; Discuss with stakeholders. The Company is currently evaluating the impact the adoption of ASU 2016-02 will have on its consolidated financial statements and has commenced the first step of identifying a task force to take the lead in implementing the new Lease standard.

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606), a comprehensive new revenue recognition standard that supersedes current revenue recognition requirements. This update requires the Company to recognize revenue at amounts that reflect the consideration to which the Company expects to be entitled in exchange for those goods or services at the time of transfer. The new standard will also require additional qualitative and quantitative disclosures about contracts with customers, significant judgments made in applying the revenue guidance, and assets recognized from the costs to obtain or fulfill a contract. ASU No. 2014-09 (and related updates) will become effective for the Company at the beginning of its 2018 fiscal year. The standard allows the option of using either a full retrospective or a modified retrospective approach for the adoption of the standard. The Company plans to adopt this accounting standard update using the modified retrospective method which will result in a cumulative effect adjustment to retained earnings as of January 1, 2018.

The Company has identified a four step process to implement the new revenue standard - data gathering, assessment, solution development, and solution implementation. The Company has substantially completed step one, data gathering and step two, assessment. The Company expects to be complete with step three, solution development and step four, solution implementation by the first quarter of 2018. The Company has not finalized the impact on reported revenues and earnings of adopting the new standard, however, the Company does not expect the new revenue standard to have a material impact on the Company's pattern of revenue recognition, operating revenue, results of operations or financial position. The Company is in the process of drafting updated accounting policies, evaluating new disclosure requirements, and identifying and implementing appropriate changes to its business processes, systems and controls to support revenue recognition and disclosure under the new guidance.

In March 2016, the FASB issued ASU 2016-09, Compensation-Stock Compensation: Improvements to Employee Share-Based Payment Accounting. The new guidance includes multiple provisions intended to simplify various aspects of the accounting for share-based payments. The provisions include:

- a. recording all tax effects associated with stock-based compensation through the income statement, as opposed to recording certain amounts in other paid-in capital, which eliminates the requirement to calculate a "windfall pool";
- allowing entities to withhold shares to satisfy the employer's statutory tax withholding requirement up to the highest marginal tax rate applicable to employees rather than the employer's minimum statutory rate, without requiring liability classification for the award;

- c. modifying the requirement to estimate the number of awards that will ultimately vest by providing an accounting policy election to either estimate the number of forfeitures or recognize forfeitures as they occur;
- d. changing certain presentation requirements in the statement of cash flows, including removing the requirement to present excess tax benefits as an inflow from financing activities and an outflow from operating activities, and requiring the cash paid to taxing authorities arising from withheld shares to be classified as a financing activity; and
- e. the assumed proceeds from applying the treasury stock method when computing earnings per share is amended to exclude the amount of excess tax benefits that previously would have been recognized in additional paid-in capital.

The Company adopted the provisions of ASU 2016-09 on January 1, 2017. As a result of adopting the standard, the Changes in Operating Assets and Liabilities, Net of Acquisitions and Divestitures line in the Cash Flows From Operating Activities section on the Condensed Consolidated Statements of Cash Flows and the Shares Surrendered for Taxes line in the Cash Flows from Financing Activities section were both adjusted by \$2.2 million for 2016. The presentation on the Condensed Consolidated Statements of Cash Flows for shares surrendered by employees to meet the minimum statutory withholding requirement and excess

tax benefits were applied retrospectively. In addition, the Excess Tax Expense from Share-Based Compensation lines in the Cash Flows from Operating Activities section and the Cash Flows from Financing Activities section were removed. The Company removed the excess tax benefits from the calculation of dilutive shares on a prospective basis. In addition, the Company began recording all tax effects associated with stock-based compensation through the income statement on a prospective basis. The Company did not have any awards classified as liability awards due to the statutory tax withholding requirements as of January 1, 2017. The Company made an accounting policy election to continue to estimate forfeitures as it had previously.

## 2. OTHER FINANCIAL INFORMATION

### Inventories

The approximate percentage distribution between major classes of inventories was as follows:

	September 30, December 31,	
	2017	2016
Raw Material and Work in Process	48%	45%
Finished Goods and Purchased Parts	52%	55%

Inventories are stated at cost, which is not in excess of market. Cost for approximately 53% of the Company's inventory at September 30, 2017, and 55% at December 31, 2016 was determined using the LIFO method.

### Property, Plant and Equipment

Property, plant, and equipment by major classification was as follows (dollars in millions):

	Useful Life in Years	September 30, December 31,	
		2017	2016
Land and Improvements		\$ 78.9	\$ 76.7
Buildings and Improvements	3 - 50	294.8	280.4
Machinery and Equipment	3 - 15	979.2	929.9
Property, Plant and Equipment		1,352.9	1,287.0
Less: Accumulated Depreciation		(719.2 )	(659.5 )
Net Property, Plant and Equipment		\$ 633.7	\$ 627.5
Other			

As part of the purchase agreement of the 2008 acquisition of the Wuxi Hwada Motor Co., the Company agreed that if certain relocation compensation was received for the relocation of the business, the Company would pay a portion of that compensation to the seller as part of a deferred contingent purchase price. During the first quarter of 2017, a final deferred contingent purchase price payment of \$5.3 million was made under this agreement.

## 3. ACQUISITIONS AND DIVESTITURES

There were no acquisition related expenses for the nine months ended September 30, 2017 and October 1, 2016.

### 2016 Acquisitions

#### Elco Purchase

On January 18, 2016, the Company purchased the remaining shares owned by the joint venture partner in its Elco Group B.V. ("Elco") joint venture increasing the Company's ownership from 55.0% to 100.0% for \$19.6 million. The purchase price of Elco is reflected as a component of equity.

### 2016 Divestitures

#### Mastergear Worldwide



On June 1, 2016, the Company sold its Mastergear Worldwide ("Mastergear") business to Rotork PLC for a purchase price of \$25.7 million. Mastergear was included in the Company's Power Transmission Solutions segment. Gains related to the sale of \$0.1 million and \$11.6 million were recorded as a reduction to Operating Expenses in the Condensed Consolidated Statements of Income during fiscal 2017 and 2016, respectively.

Venezuelan Subsidiary

On July 7, 2016, the Company sold the assets of its Venezuelan subsidiary, which had been included in the Company's Commercial and Industrial Systems segment, to a private company for \$3.0 million. Of this amount, \$1.0 million was received on the transaction closing date and \$2.0 million is being received in 24 monthly installments. The Company may receive additional amounts in the future related to certain accounts receivable of this business. The gains will be recognized as the cash is received. The Company wrote down its investment and ceased operations of this subsidiary in 2015.

4. ACCUMULATED OTHER COMPREHENSIVE LOSS

Foreign currency translation adjustments, hedging activities and pension and post retirement benefit adjustments are included in Equity in Accumulated Other Comprehensive Loss ("AOCI").

The changes in AOCI by component for the three and nine months ended September 30, 2017 and October 1, 2016 were as follows (in millions):

	Three Months Ended September 30, 2017			Total
	Hedging Activities	Pension and Post Retirement Benefit Adjustments	Foreign Currency Translation Adjustments	
Beginning Balance	\$(1.7 )	\$( 35.5 )	\$( 173.2 )	\$(210.4)
Other Comprehensive Income (Loss) before Reclassifications	14.3	(0.2 )	24.2	38.3
Tax Impact	(5.5 )	—	—	(5.5 )
Amounts Reclassified from Accumulated Other Comprehensive Loss	(0.3 )	0.6	—	0.3
Tax Impact	0.2	(0.2 )	—	—
Net Current Period Other Comprehensive Income	8.7	0.2	24.2	33.1
Ending Balance	\$7.0	\$( 35.3 )	\$( 149.0 )	\$(177.3)

	Three Months Ended October 1, 2016			Total
	Hedging Activities	Pension and Post Retirement Benefit Adjustments	Foreign Currency Translation Adjustments	
Beginning Balance	\$(40.6)	\$( 33.6 )	\$( 181.6 )	\$(255.8)
Other Comprehensive Income (Loss) before Reclassifications	(10.1 )	0.1	(2.6 )	(12.6 )
Tax Impact	3.8	—	—	3.8
Amounts Reclassified from Accumulated Other Comprehensive Loss	12.3	0.8	—	13.1
Tax Impact	(4.6 )	(0.3 )	—	(4.9 )
Net Current Period Other Comprehensive Income (Loss)	1.4	0.6	(2.6 )	(0.6 )
Ending Balance	\$(39.2)	\$( 33.0 )	\$( 184.2 )	\$(256.4)



	Nine Months Ended September 30, 2017			
	Hedging Activities	Pension and Post Retirement Benefit Adjustments	Foreign Currency Translation Adjustments	Total
Beginning Balance	\$(41.1)	\$ (36.0 )	\$ (241.0 )	\$(318.1)
Other Comprehensive Income (Loss) before Reclassifications	61.7	(0.5 )	92.0	153.2
Tax Impact	(23.5 )	—	—	(23.5 )
Amounts Reclassified from Accumulated Other Comprehensive Loss	15.9	1.8	—	17.7
Tax Impact	(6.0 )	(0.6 )	—	(6.6 )
Net Current Period Other Comprehensive Income	48.1	0.7	92.0	140.8
Ending Balance	\$7.0	\$ (35.3 )	\$ (149.0 )	\$(177.3)

	Nine Months Ended October 1, 2016			
	Hedging Activities	Pension and Post Retirement Benefit Adjustments	Foreign Currency Translation Adjustments	Total
Beginning Balance	\$(47.5)	\$ (35.4 )	\$ (172.1 )	\$(255.0)
Other Comprehensive Income (Loss) before Reclassifications	(24.3 )	0.6	(9.4 )	(33.1 )
Tax Impact	9.2	—	—	9.2
Amounts Reclassified from Accumulated Other Comprehensive Loss	37.7	2.7	—	40.4
Tax Impact	(14.3 )	(0.9 )	—	(15.2 )
Net Current Period Other Comprehensive Income (Loss)	8.3	2.4	(9.4 )	1.3
Purchase of Subsidiary Shares from Noncontrolling Interest	—	—	(2.7 )	(2.7 )
Ending Balance	\$(39.2)	\$ (33.0 )	\$ (184.2 )	\$(256.4)

The Condensed Consolidated Statements of Income line items affected by the hedging activities reclassified from accumulated other comprehensive loss in the tables above are disclosed in Note 13 of Notes to Condensed Consolidated Financial Statements.

The reclassification amounts for pension and post retirement benefit adjustments in the tables above are part of net periodic benefit costs recorded in Operating Expenses (see also Note 8 of Notes to Condensed Consolidated Financial Statements).

## 5. GOODWILL AND INTANGIBLE ASSETS

### Goodwill

As required, the Company performs an annual impairment test of goodwill as of the end of the October fiscal month or more frequently if events or circumstances change that would more likely than not reduce the fair value of its reporting units below their carrying value.

The following information presents changes to goodwill during the nine months ended September 30, 2017 (in millions):

	Total	Commercial and Industrial Systems	Climate Solutions	Power Transmission Solutions
Balance as of December 31, 2016	\$1,453.2	\$ 540.6	\$ 341.8	\$ 570.8
Translation Adjustments	22.0	8.9	1.1	12.0
Balance as of September 30, 2017	\$1,475.2	\$ 549.5	\$ 342.9	\$ 582.8
Cumulative Goodwill Impairment Charges	\$275.7	\$ 244.8	\$ 7.7	\$ 23.2

Intangible Assets

Intangible assets consisted of the following (in millions):

	Weighted Average Amortization Period (Years)	September 30, 2017		December 31, 2016	
		Gross Value	Accumulated Amortization	Gross Value	Accumulated Amortization
Amortizable Intangible Assets:					
Customer Relationships	16	\$718.8	\$ 240.1	\$703.6	\$ 201.6
Technology	13	191.8	118.0	189.7	109.5
Trademarks	15	32.7	25.3	31.8	23.3
Patent and Engineering Drawings	5	16.6	16.6	16.6	16.6
Non-Compete Agreements	8	8.4	8.3	8.3	8.1
		968.3	408.3	950.0	359.1
Non-Amortizable Trade Names		122.4	—	120.8	—
		\$1,090.7	\$ 408.3	\$1,070.8	\$ 359.1

Amortization expense recorded for the three and nine months ended September 30, 2017 was \$13.9 million and \$41.9 million, respectively. Amortization expense recorded for the three and nine months ended October 1, 2016 was \$15.6 million and \$47.0 million, respectively. Amortization expense for 2017 is estimated to be \$55.9 million.

Estimated expected future annual amortization for intangible assets is as follows (in millions):

Year	Estimated Amortization
2018	\$ 53.9
2019	53.5
2020	50.4
2021	42.6
2022	41.0

## 6. BUSINESS SEGMENTS

Commercial and Industrial Systems produces medium and large motors, commercial and industrial equipment, generator and custom drives and systems. These products serve markets including commercial Heating, Ventilation, and Air Conditioning ("HVAC"), pool and spa, standby and critical power and oil and gas systems.



Climate Solutions produces small motors, controls and air moving solutions serving markets including residential and light commercial HVAC, water heaters and commercial refrigeration.

Power Transmission Solutions manufactures, sells and services belt and chain drives, helical and worm gearing, mounted and unmounted bearings, couplings, modular plastic belts, conveying chains and components, hydraulic pump drives, large open gearing and specialty mechanical products serving markets including beverage, bulk handling, metals, special machinery, energy, aerospace and general industrial.

The Company evaluates performance based on the segment's income from operations. Corporate costs have been allocated to each segment based on the net sales of each segment. The reported external net sales of each segment are from external customers.

The following sets forth certain financial information attributable to the Company's operating segments for the three and nine months ended September 30, 2017 and October 1, 2016 (in millions):

	Commercial and Industrial Systems	Climate Solutions	Power Transmission Solutions	Eliminations	Total
Three Months Ended September 30, 2017					
External Sales	\$ 408.0	\$ 256.0	\$ 192.9	\$ —	\$856.9
Intersegment Sales	16.4	5.0	0.5	(21.9 )	—
Total Sales	424.4	261.0	193.4	(21.9 )	856.9
Gross Profit	98.0	65.8	63.2	—	227.0
Operating Expenses	68.4	27.0	37.6	—	133.0
Income from Operations	29.6	38.8	25.6	—	94.0
Depreciation and Amortization	15.2	5.5	13.6	—	34.3
Capital Expenditures	8.6	3.1	3.6	—	15.3
Three Months Ended October 1, 2016					
External Sales	\$ 389.4	\$ 250.5	\$ 169.7	\$ —	\$809.6
Intersegment Sales	10.8	5.7	1.1	(17.6 )	—
Total Sales	400.2	256.2	170.8	(17.6 )	809.6
Gross Profit	105.4	71.4	54.9	—	231.7
Operating Expenses	69.2	29.2	43.5	—	141.9
Income from Operations	36.2	42.2	11.4	—	89.8
Depreciation and Amortization	17.7	4.9	15.0	—	37.6
Capital Expenditures	9.6	2.6	2.2	—	14.4

	Commercial and Industrial Systems	Climate Solutions	Power Transmission Solutions	Eliminations	Total
Nine Months Ended September 30, 2017					
External Sales	\$ 1,196.6	\$ 774.2	\$ 568.8	\$ —	\$2,539.6
Intersegment Sales	52.2	19.2	3.4	(74.8 )	—
Total Sales	1,248.8	793.4	572.2	(74.8 )	2,539.6
Gross Profit	285.5	194.8	185.3	—	665.6
Operating Expenses	209.5	84.6	119.7	—	413.8
Income from Operations	76.0	110.2	65.6	—	251.8
Depreciation and Amortization	45.2	16.6	41.3	—	103.1
Capital Expenditures	30.3	9.7	9.0	—	49.0
Nine Months Ended October 1, 2016					
External Sales	\$ 1,161.7	\$ 744.8	\$ 559.9	\$ —	\$2,466.4
Intersegment Sales	33.5	17.9	3.1	(54.5 )	—
Total Sales	1,195.2	762.7	563.0	(54.5 )	2,466.4
Gross Profit	295.2	192.3	184.5	—	672.0
Operating Expenses	212.2	89.4	119.9	—	421.5
Income from Operations	83.0	102.9	64.6	—	250.5
Depreciation and Amortization	56.6	17.6	42.4	—	116.6
Capital Expenditures	26.5	10.1	9.5	—	46.1

The following table presents identifiable assets information attributable to the Company's operating segments as of September 30, 2017 and December 31, 2016 (in millions):

	Commercial and Industrial Systems	Climate Solutions	Power Transmission Solutions	Total
Identifiable Assets as of September 30, 2017	\$ 1,905.7	\$ 934.8	\$ 1,623.5	\$4,464.0
Identifiable Assets as of December 31, 2016	\$ 1,872.7	\$ 881.8	\$ 1,604.0	\$4,358.5

## 7. DEBT AND BANK CREDIT FACILITIES

The Company's indebtedness as of September 30, 2017 and December 31, 2016 was as follows (in millions):

	September 30, 2017	December 31, 2016
Term Facility	\$ 686.1	\$ 798.1
Senior Notes	500.0	600.0
Multicurrency Revolving Facility	29.6	18.0
Other	5.1	5.1
Less: Debt Issuance costs	(6.4 )	(9.7 )
	1,214.4	1,411.5
Less: Current Maturities	100.6	100.6
Non-Current Portion	\$ 1,113.8	\$ 1,310.9

The Credit Agreement



In connection with the Company's acquisition of the Power Transmission Solutions business of Emerson Electric Co. (the "PTS Acquisition"), on January 30, 2015, the Company entered into a Credit Agreement (the "Credit Agreement") with JPMorgan Chase Bank, N.A., as Administrative Agent and the lenders named therein, providing for a (i) 5-year unsecured term loan facility in the principal amount of \$1.25 billion (the "Term Facility") and (ii) a 5-year unsecured multicurrency revolving facility in the principal amount of \$500.0 million (the "Multicurrency Revolving Facility"), including a \$100.0 million letter of credit sub facility, available for general corporate purposes. Borrowings under the Credit Agreement bear interest at floating rates based upon indices determined by the currency of the borrowing, plus an applicable margin determined by reference to the Company's consolidated funded debt to consolidated EBITDA ratio or at an alternative base rate.

The Term Facility was drawn in full on January 30, 2015 in connection with the closing of the PTS Acquisition. The loan under the Term Facility requires quarterly amortization at a rate starting at 5.0% per annum, increasing to 7.5% per annum after two years and further increasing to 10.0% per annum for the last two years of the Term Facility, unless previously prepaid. The weighted average interest rate on the Term Facility was 2.7% and 2.5% for the three and nine months ended September 30, 2017 and 2.0% for the three and nine months ended October 1, 2016. The Credit Agreement requires the Company prepay the loans under the Term Facility with 100% of the net cash proceeds received from specified asset sales and borrowed money indebtedness, subject to certain exceptions.

At September 30, 2017, the Company had borrowings under the Multicurrency Revolving Facility in the amount of \$29.6 million, \$29.8 million of standby letters of credit issued under the facility, and \$440.6 million of available borrowing capacity. The average daily balance in borrowings under the Multicurrency Revolving Facility was \$97.8 million and \$105.4 million, and the weighted average interest rate on the Multicurrency Revolving Facility was 2.7% and 2.5% for the three and nine months ended September 30, 2017, respectively. The average daily balance in borrowings under the Multicurrency Revolving Facility was \$29.7 million and \$45.1 million and the weighted average interest rate on the Multicurrency Revolving Facility was 1.9% for the three and nine months ended October 1, 2016. The Company pays a non-use fee on the aggregate unused amount of the Multicurrency Revolving Facility at a rate determined by reference to its consolidated funded debt to consolidated EBITDA ratio.

#### Senior Notes

At September 30, 2017, the Company had \$500.0 million of senior notes (the "Notes") outstanding. The Notes consist of \$500.0 million in senior notes (the "2011 Notes") in a private placement which were issued in seven tranches with maturities from seven to twelve years and carry fixed interest rates. As of September 30, 2017, \$400.0 million of the 2011 Notes are included in Long-Term Debt and \$100.0 million of the 2011 Notes are included in Current Maturities of Long-Term Debt on the Condensed Consolidated Balance Sheets. The Company repaid the remaining \$100.0 million of its 2007 Notes in August, 2017.

Details on the Notes at September 30, 2017 were (in millions):

	Principal	Interest Rate	Maturity
Fixed Rate Series 2011A	100.0	4.1%	July 14, 2018
Fixed Rate Series 2011A	230.0	4.8 to 5.0%	July 14, 2021
Fixed Rate Series 2011A	170.0	4.9 to 5.1%	July 14, 2023
	\$ 500.0		

The Company had an interest rate swap agreement to manage fluctuations in cash flows resulting from interest rate risk (see also Note 13 of Notes to the Condensed Financial Statements). The remaining interest rate swap agreement terminated in August, 2017.

#### Compliance with Financial Covenants

The Credit Agreement and the Notes require the Company to meet specified financial ratios and to satisfy certain financial condition tests. The Company was in compliance with all financial covenants contained in the Notes and the Credit Agreement as of September 30, 2017.

Other Notes Payable

At September 30, 2017, other notes payable of approximately \$5.1 million were outstanding with a weighted average interest rate of 5.2%. At December 31, 2016, other notes payable of approximately \$5.1 million were outstanding with a weighted average rate of 5.6%.

Based on rates for instruments with comparable maturities and credit quality, which are classified as Level 2 inputs (see also Note 14 of Notes to the Condensed Consolidated Financial Statements), the approximate fair value of the Company's total debt was \$1,244.2 million and \$1,433.4 million as of September 30, 2017 and December 31, 2016, respectively.

## 8. POST RETIREMENT PLANS

The Company's net periodic benefit cost was comprised of the following components (in millions):

	Three Months Ended		Nine Months Ended	
	September 30, 2017	October 1, 2016	September 30, 2017	October 1, 2016
Service Cost	\$ 1.8	\$ 2.0	\$ 5.4	\$ 6.1
Interest Cost	2.5	2.6	7.3	7.7
Expected Return on Plan Assets	(2.8 )	(3.0 )	(8.4 )	(8.9 )
Amortization of Prior Service Cost and Net Actuarial Loss	0.6	0.8	1.8	2.7
Net Periodic Benefit Cost	\$ 2.1	\$ 2.4	\$ 6.1	\$ 7.6

The estimated net actuarial loss and prior service cost for post retirement plans that will be amortized from AOCI into net periodic benefit cost during the 2017 fiscal year is \$2.2 million and \$0.2 million, respectively.

For the three months ended September 30, 2017 and October 1, 2016, the Company contributed \$6.0 million and \$6.8 million, respectively, to post retirement plans. For the nine months ended September 30, 2017 and October 1, 2016, the Company contributed \$8.2 million and \$9.0 million, respectively, to post retirement plans. The Company expects to make total contributions of \$9.4 million in 2017. The Company contributed a total of \$10.4 million in fiscal 2016. The assumptions used in the valuation of the Company's post retirement plans and in the target investment allocation have remained the same as those disclosed in the Company's 2016 Annual Report on Form 10-K filed on March 1, 2017.

## 9. SHAREHOLDERS' EQUITY

### Repurchase of Common Stock

The Company acquired and retired 300,000 shares of its common stock in the quarter ended September 30, 2017, at an average cost of \$77.84 per share for a total cost of \$23.4 million. The Company acquired and retired 576,804 shares of its common stock in the nine months ended September 30, 2017, at an average cost of \$78.12 per share for a total cost of \$45.1 million. The repurchases were made under the 3.0 million share repurchase program approved by the Company's Board of Directors in November, 2013. There are approximately 1.7 million shares of the Company's common stock available for repurchase under this program.

### Share-Based Compensation

The majority of the Company's annual share-based incentive awards are made in the fiscal second quarter.

The Company recognized approximately \$3.3 million and \$3.0 million in share-based compensation expense for the three months ended September 30, 2017 and October 1, 2016, respectively. Share-based compensation expense was \$10.3 million and \$10.1 million for the nine months ended September 30, 2017 and October 1, 2016, respectively. The total income tax benefit recognized in the Consolidated Statements of Income for share-based compensation expense was \$1.3 million and \$1.1 million for the three months ended September 30, 2017 and October 1, 2016, respectively. The total income tax benefit recognized in the Consolidated Statements of Income for share-based compensation expense was \$3.9 million and \$3.8 million for the nine months ended September 30, 2017 and October 1, 2016,

respectively. The Company recognizes compensation expense on grants of share-based compensation awards on a straight-line basis over the vesting period of each award. As of September 30, 2017, total unrecognized compensation cost related to share-based compensation awards was approximately \$27.9 million, net of estimated forfeitures, which the Company expects to recognize over a weighted average period of approximately 2.2 years.

Approximately 1.0 million shares were available for future grant under the 2013 Equity Incentive Plan at September 30, 2017.

### Stock Appreciation Rights

The Company uses stock settled stock appreciation rights (“SARs”) as a form of share-based incentive awards. SARs are the right to receive stock in an amount equal to the appreciation in value of a share of stock over the base price per share that generally vest over 5 years and expire 10 years from the grant date. All grants are made at prices equal to the fair market value of the stock on the grant date. For the nine months ended September 30, 2017 and October 1, 2016, expired and canceled shares were immaterial.

The table below presents share-based compensation activity for the nine months ended September 30, 2017 and October 1, 2016 (in millions):

	September 30, 2017	October 1, 2016
Total intrinsic value of share-based incentive awards exercised	\$ 3.7	\$ 1.1
Cash received from stock option exercises	0.4	0.5
Income tax benefit (expense) from the exercise of stock options	0.7	(0.2 )
Total fair value of share-based incentive awards vested	4.3	4.9

The assumptions used in the Company's Black-Scholes valuation related to grants for options and SARs were as follows:

	2017	2016
Per share weighted average fair value of grants	\$23.73	\$15.22
Risk-free interest rate	2.0 %	1.4 %
Expected life (years)	7.0	7.0
Expected volatility	27.9 %	29.6 %
Expected dividend yield	1.2 %	1.7 %

The average risk-free interest rate is based on US Treasury security rates in effect as of the grant date. The expected dividend yield is based on the projected annual dividend as a percentage of the estimated market value of the Company's common stock as of the grant date. The Company estimated the expected volatility using a weighted average of daily historical volatility of the Company's stock price over the expected term of the award. The Company estimated the expected term using historical data adjusted for the estimated exercise dates of unexercised awards.

Following is a summary of share-based incentive plan grant activity (options and SARs) for the nine months ended September 30, 2017.

Number of Shares Under Options and SARs	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (years)	Aggregate Intrinsic Value (in millions)
Exercisable at December 31, 2016	1,610,499	\$ 63.16		
Granted	195,207	80.72		
Exercised	(160,771 )	53.18		
Forfeited	(10,239 )	65.13		
Expired	(9,485 )	64.21		
Outstanding at September 30, 2017	1,625,211	\$ 66.24	5.9	\$ 20.9
Exercisable at September 30, 2017	964,171	\$ 64.14	4.1	\$ 14.3

Compensation expense recognized related to options and SARs was \$3.2 million for the nine months ended September 30, 2017.

As of September 30, 2017, there was \$11.0 million of unrecognized compensation cost related to non-vested options and SARs that is expected to be recognized as a charge to earnings over a weighted average period of 3.5 years.

The amount of options expected to vest is materially consistent with those outstanding and not yet exercisable.



Restricted Stock Awards and Restricted Stock Units

Restricted stock awards ("RSA") and restricted stock units ("RSU") consist of shares or the rights to shares of the Company's stock. The awards are restricted such that they are subject to substantial risk of forfeiture and to restrictions on their sale or other transfer. As defined in the individual grant agreements, acceleration of vesting may occur under a change in control, or death, disability or normal retirement of the grantee.

Following is a summary of RSA award activity for the nine months ended September 30, 2017:

	Shares	Weighted Average Fair Value at Grant Date	Weighted Average Remaining Contractual Term (years)
Unvested RSAs at December 31, 2016	19,593	\$ 57.43	0.4
Granted	13,941	80.70	
Vested	(19,593)	57.43	
Unvested RSAs at September 30, 2017	13,941	\$ 80.70	0.6

RSAs vest on the first anniversary of the grant date, provided the holder of the shares is continuously employed by or in the service of the Company until the vesting date. Compensation expense recognized related to the RSAs was \$0.8 million for the nine months ended September 30, 2017.

As of September 30, 2017, there was \$0.7 million of unrecognized compensation cost related to non-vested RSAs that is expected to be recognized as a charge to earnings over a weighted average period of 0.6 years.

Following is a summary of RSU award activity for the nine months ended September 30, 2017:

	Shares	Weighted Average Fair Value at Grant Date	Weighted Average Remaining Contractual Term (years)
Unvested RSUs at December 31, 2016	277,863	\$ 69.23	1.7
Granted	75,905	80.48	
Vested	(81,265)	74.98	
Forfeited	(7,108)	67.92	
Unvested RSUs at September 30, 2017	264,995	\$ 70.72	1.9

RSUs vest on the third anniversary of the grant date, provided the holder of the RSUs is continuously employed by the Company until the vesting date. Compensation expense recognized related to the RSUs was \$4.7 million for the nine months ended September 30, 2017.

As of September 30, 2017, there was \$10.0 million of unrecognized compensation cost related to non-vested RSUs that is expected to be recognized as a charge to earnings over a weighted average period of 1.9 years.

Performance Share Units

Performance share unit ("PSU") awards consist of shares or the rights to shares of the Company's stock which are awarded to employees of the Company. These shares are payable upon the determination that the Company achieved certain established performance targets and can range from 0% to 200% of the targeted payout based on the actual results. PSUs have a performance period of 3 years. As set forth in the individual award agreements, acceleration of vesting may occur under a change in control, death or disability. There are no voting rights associated with PSUs until vesting occurs and a share of stock is issued. Some of the PSU awards are valued using a Monte Carlo simulation method as of the grant date while others are valued using the closing market price as of the grant date depending on the performance criteria for the award.

The assumptions used in the Company's Monte Carlo simulation related to grants for performance share units were as follows:

	September 30, 2017		October 1, 2016	
Risk-free interest rate	1.6	%	0.9	%
Expected life (years)	3.0		3.0	
Expected volatility	24.0	%	23.0	%
Expected dividend yield	1.3	%	1.7	%

Following is a summary of PSU award activity for the nine months ended September 30, 2017:

Shares	Weighted Average Fair Value at Grant Date	Weighted Average Remaining Contractual Term (years)
Unvested PSUs at December 31, 2016	133,340	2.0
Granted	48,066	90.82
Vested	(110)	83.74
Forfeited	(21,780)	81.76
Unvested PSUs at September 30, 2017	155,116	2.1

Compensation expense for awards granted is recognized based on the Monte Carlo simulation value or the expected payout ratio depending upon the performance criterion for the award, net of estimated forfeitures. Compensation expense recognized related to PSUs was \$1.6 million for the nine months ended September 30, 2017. Total unrecognized compensation expense for all PSUs granted as of September 30, 2017 is estimated to be \$6.2 million recognized as a charge to earnings over a weighted average period of 2.1 years.

#### 10. INCOME TAXES

The effective tax rate for the three months ended September 30, 2017 was 21.7% versus 20.2% for the three months ended October 1, 2016. The effective tax rate for the nine months ended September 30, 2017 was 21.9% versus 22.7% for the nine months ended October 1, 2016. The change in the effective tax rate for the three months ended September 30, 2017 was primarily driven by the mix of earnings and the favorable adjustments related to the finalization of the 2015 US federal income tax return. The change in the effective tax rate for the nine months ended September 30, 2017 was primarily driven by the mix of earnings and the favorable adjustments related to the 2016 finalization of the 2015 US federal income tax return, partially offset by the 2016 gain derived from the sale of the Mastergear business. The lower effective rate as compared to the 35.0% statutory Federal income tax rate is driven by lower foreign tax rates.

As of September 30, 2017 and December 31, 2016, the Company had approximately \$10.4 million and \$10.0 million, respectively, of unrecognized tax benefits, all of which would impact the effective income tax rate if recognized.

Potential interest and penalties related to unrecognized tax benefits are recorded in income tax expense.

With few exceptions, the Company is no longer subject to US Federal and state/local income tax examinations by tax authorities for years prior to 2012, and the Company is no longer subject to non-US income tax examinations by tax authorities for years prior to 2010.

#### 11. EARNINGS PER SHARE

Diluted earnings per share is computed based upon earnings applicable to common shares divided by the weighted-average number of common shares outstanding during the period adjusted for the effect of other dilutive securities. Options for common shares where the exercise price was above the market price have been excluded from the calculation of effect of dilutive securities shown below; the amount of the anti-dilutive shares were 0.5 million and 1.4 million for the three months ended September 30, 2017 and October 1, 2016, respectively, and 0.4 million and 1.3 million for the nine months ended September 30, 2017 and October 1, 2016, respectively. The following table reconciles the basic and diluted shares used in earnings per share calculations for the three and nine months ended September 30, 2017 and October 1, 2016 (in millions):

	Three Months Ended		Nine Months Ended	
	September 30, 2017	October 1, 2016	September 30, 2017	October 1, 2016
Denominator for Basic Earnings Per Share	44.4	44.8	44.7	44.7
Effect of Dilutive Securities	0.4	0.2	0.3	0.3
Denominator for Diluted Earnings Per Share	44.8	45.0	45.0	45.0

## 12. CONTINGENCIES

One of the Company's subsidiaries that it acquired in 2007 is subject to numerous claims filed in various jurisdictions relating to certain sub-fractional motors that were primarily manufactured through 2004 and that were included as components of residential and commercial ventilation units manufactured and sold in high volumes by a third party. These ventilation units are subject to product safety requirements and other potential regulation of their performance by government agencies such as the US Consumer Product Safety Commission ("CPSC"). The claims generally allege that the ventilation units were the cause of fires. The Company has recorded an estimated liability for incurred claims. Based on the current facts, the Company cannot assure that these claims, individually or in the aggregate, will not have a material adverse effect on its subsidiary's financial condition. The Company's subsidiary cannot reasonably predict the outcome of these claims, the nature or extent of any CPSC or other remedial actions, if any, that the Company's subsidiary may need to undertake with respect to motors that remain in the field, or the costs that may be incurred, some of which could be significant.

The Company is, from time to time, party to litigation and other legal or regulatory proceedings that arise in the normal course of its business operations and the outcomes of which are subject to significant uncertainty, including product warranty and liability claims, contract disputes and environmental, asbestos, intellectual property, employment and other litigation matters. The Company's products are used in a variety of industrial, commercial and residential applications that subject the Company to claims that the use of its products is alleged to have resulted in injury or other damage. Many of these matters will only be resolved when one or more future events occur or fail to occur. Management conducts regular reviews, including updates from legal counsel, to assess the need for accounting recognition or disclosure of these contingencies, and such assessment inherently involves an exercise in judgment. The Company accrues for exposures in amounts that it believes are adequate, and the Company does not believe that the outcome of any such lawsuit individually or collectively will have a material effect on the Company's financial position, its results of operations or its cash flows.

The Company recognizes the cost associated with its standard warranty on its products at the time of sale. The amount recognized is based on historical experience. The following is a reconciliation of the changes in accrued warranty costs for the three and nine months ended September 30, 2017 and October 1, 2016 (in millions):

	Three Months Ended		Nine Months Ended	
	September 30, 2017	October 1, 2016	September 30, 2017	October 1, 2016
Beginning Balance	\$ 18.1	\$ 19.2	\$ 20.3	\$ 19.1
Less: Payments	(4.7 )	(5.9 )	(17.5 )	(15.6 )
Provisions	4.0	7.2	14.5	17.0
Translation Adjustments	0.1	—	0.2	—
Ending Balance	\$ 17.5	\$ 20.5	\$ 17.5	\$ 20.5

These liabilities are included in Other Accrued Expenses and Other Noncurrent Liabilities on the Consolidated Balance Sheet.

## 13. DERIVATIVE INSTRUMENTS

The Company is exposed to certain risks relating to its ongoing business operations. The primary risks managed using derivative instruments are commodity price risk, currency exchange risk, and interest rate risk. Forward contracts on

certain commodities are entered into to manage the price risk associated with forecasted purchases of materials used in the Company's manufacturing process. Forward contracts on certain currencies are entered into to manage forecasted cash flows in certain foreign currencies. Interest rate swaps were previously utilized to manage interest rate risk associated with the Company's floating rate borrowings.

The Company is exposed to credit losses in the event of non-performance by the counterparties to various financial agreements, including its commodity hedging transactions, foreign currency exchange contracts and interest rate swap agreements. Exposure to counterparty credit risk is managed by limiting counterparties to major international banks and financial institutions meeting established credit guidelines and continually monitoring their compliance with the credit guidelines. The Company does not obtain collateral or other security to support financial instruments subject to credit risk. The Company does not anticipate non-performance by its counterparties, but cannot provide assurances. The Company recognizes all derivative instruments as either assets or liabilities at fair value in the statement of financial position. The Company designates commodity forward contracts as cash flow hedges of forecasted purchases of commodities, currency forward contracts as cash flow hedges of forecasted foreign currency cash flows and interest rate swaps as cash flow hedges of forecasted LIBOR-based interest payments. There were no significant collateral deposits on derivative financial instruments as of September 30, 2017.

#### Cash flow hedges

For derivative instruments that are designated and qualify as a cash flow hedge, the effective portion of the gain or loss on the derivative is reported as a component of AOCI and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative representing either hedge ineffectiveness or changes in market value of derivatives not designated as hedges are recognized in current earnings. At September 30, 2017, the Company had \$(0.1) million of derivative losses on closed hedge instruments in AOCI that will be realized in earnings when the hedged items impact earnings. At December 31, 2016, the Company had \$(7.5) million, net of tax, of derivative losses on closed hedge instruments in AOCI that was subsequently realized in earnings when the hedged items impacted earnings.

As of September 30, 2017, the Company had the following currency forward contracts outstanding (with maturities extending through October 2019) to hedge forecasted foreign currency cash flows (in millions):

	Notional Amount (in US Dollars)
Chinese Renminbi	\$ 218.0
Mexican Peso	164.9
Euro	63.8
Indian Rupee	37.7
Canadian Dollar	51.3
Australian Dollar	13.2
Thai Baht	7.1
British Pound	9.9

As of September 30, 2017, the Company had the following commodity forward contracts outstanding (with maturities extending through December 2018) to hedge forecasted purchases of commodities (notional amounts expressed in terms of the dollar value of the hedged item (in millions):

	Notional Amount
Copper	\$ 64.0
Aluminum	4.5

Fair values of derivative instruments as of September 30, 2017 and December 31, 2016 were (in millions):

	September 30, 2017			
	Prepaid Expenses and Other Current Assets	Other Noncurrent Assets	Current Hedging Obligations	Noncurrent Hedging Obligations
Designated as hedging instruments:				
Currency contracts	\$9.5	\$ 4.9	\$ 8.2	\$ 0.6
Commodity contracts	6.5	0.2	0.3	—
Not designated as hedging instruments:				
Currency contracts	3.4	—	0.6	—
Commodity contracts	0.1	—	—	—
Total Derivatives	\$19.5	\$ 5.1	\$ 9.1	\$ 0.6

	December 31, 2016			
	Prepaid Expenses and Other Current Assets	Other Noncurrent Assets	Current Hedging Obligations	Noncurrent Hedging Obligations
Designated as hedging instruments:				
Interest rate swap contracts	\$—	\$ —	\$ 3.3	\$ —
Currency contracts	1.3	0.4	39.7	17.6
Commodity contracts	4.7	—	—	—
Not designated as hedging instruments:				
Currency contracts	1.5	—	6.0	—
Commodity contracts	2.6	—	—	—
Total Derivatives	\$10.1	\$ 0.4	\$ 49.0	\$ 17.6

The effect of derivative instruments on the Condensed Consolidated Statements of Income and Comprehensive Income (pre-tax) was as follows (in millions):

Derivatives Designated as Cash Flow Hedging Instruments

	Three Months Ended September 30, 2017				October 1, 2016			
	Commodity Forwards	Currency Forwards	Interest Rate Swaps	Total	Commodity Forwards	Currency Forwards	Interest Rate Swaps	Total
Gain (Loss) recognized in Other Comprehensive Income (Loss)	\$6.8	\$ 7.0	\$ 0.5	\$14.3	\$(0.5)	\$(9.9)	\$ 0.3	\$(10.1)
Amounts reclassified from Other Comprehensive Income (Loss):								
Gain recognized in Net Sales	—	0.3	—	0.3	—	0.1	—	0.1
Gain (Loss) recognized in Cost of Sales	2.8	(2.2)	—	0.6	(2.4)	(8.8)	—	(11.2)

Loss recognized in Interest Expense	—	—	(0.6 )	(0.6 )	—	—	(1.2 )	(1.2 )
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	Nine Months Ended September 30, 2017				October 1, 2016			
	Commodity Forwards	Currency Forwards	Interest Rate Swaps	Total	Commodity Forwards	Currency Forwards	Interest Rate Swaps	Total
Gain (Loss) recognized in Other Comprehensive Income (Loss)	\$ 11.3	\$ 49.9	\$ 0.5	\$ 61.7	\$ 1.6	\$ (25.5 )	\$ (0.4 )	\$ (24.3)
Amounts reclassified from Other Comprehensive Income (Loss):								
Gain recognized in Net Sales	—	0.7	—	0.7	—	0.1	—	0.1
Gain (Loss) recognized in Cost of Sales	7.5	(21.3 )	—	(13.8 )	(12.1)	(22.0 )	—	(34.1 )
Loss recognized in Interest Expense	—	—	(2.8 )	(2.8 )	—	—	(3.7 )	(3.7 )

The ineffective portion of hedging instruments recognized during the three and nine months ended September 30, 2017 and October 1, 2016, respectively, was immaterial.

Derivatives Not Designated as Cash Flow Hedging Instruments (in millions):

	Three Months Ended			
	September 30, 2017		October 1, 2016	
	Commodity Forwards	Currency Forwards	Commodity Forwards	Currency Forwards
Gain (Loss) recognized in Cost of Sales	\$(0.8)	\$ —	—	\$ —
Gain (Loss) recognized in Operating Expenses	—	2.9	—	—

  

	Nine Months Ended			
	September 30, 2017		October 1, 2016	
	Commodity Forwards	Currency Forwards	Commodity Forwards	Currency Forwards
Gain (Loss) recognized in Cost of Sales	\$(0.6)	\$ —	\$ 0.2	\$ —
Gain (Loss) recognized in Operating Expenses	—	10.6	—	(0.7 )

The net AOCI hedging component balance of \$7.0 million gain at September 30, 2017 includes \$6.5 million of net current deferred gains expected to be realized in the next twelve months.

The Company's commodity and currency derivative contracts are subject to master netting agreements with the respective counterparties which allow the Company to net settle transactions with a single net amount payable by one party to another party. The Company has elected to present the derivative assets and derivative liabilities on the Condensed Consolidated Balance Sheets on a gross basis for the periods ended September 30, 2017 and December 31, 2016.

The following table presents the derivative assets and derivative liabilities presented on a net basis under enforceable master netting agreements (in millions):

	September 30, 2017		
	Gross		
	Amounts	Derivative	Derivative
	as	Contract	Contracts
	Presented	Amounts	as
	in the	Subject to	Presented
	Condensed	Right of	on a Net
	Consolidated	Offset	Basis
	Balance		
	Sheet		
Prepaid Expenses and Other Current Assets:			
Derivative Currency Contracts	\$12.9	\$ (5.4 )	\$ 7.5
Derivative Commodity Contracts	6.6	(0.3 )	6.3
Other Noncurrent Assets:			
Derivative Currency Contracts	4.9	(0.5 )	4.4
Derivative Commodity Contracts	0.2	—	0.2
Current Hedging Obligations:			
Derivative Currency Contracts	8.8	(5.4 )	3.4
Derivative Commodity Contracts	0.3	(0.3 )	—
Noncurrent Hedging Obligations:			
Derivative Currency Contracts	0.6	(0.5 )	0.1
	December 31, 2016		
	Gross		
	Amounts	Derivative	Derivative
	as	Contract	Contracts
	Presented	Amounts	as
	in the	Subject to	Presented
	Condensed	Right of	on a Net
	Consolidated	Offset	Basis
	Balance		
	Sheet		

## 14. 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 (exit price). The inputs used to measure fair value are classified into the following hierarchy:

- Level 1 Unadjusted quoted prices in active markets for identical assets or liabilities
- Level 2 Unadjusted quoted prices in active markets for similar assets or liabilities, or  
Unadjusted quoted prices for identical or similar assets or liabilities in markets that are not active, or  
Inputs other than quoted prices that are observable for the asset or liability
- Level 3 Unobservable inputs for the asset or liability

The Company uses the best available information in measuring fair value. Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

The fair values of cash equivalents and short-term deposits approximate their carrying values as of September 30, 2017 and December 31, 2016, due to the short period of time to maturity and are classified using Level 1 inputs. The fair values of trade receivables and accounts payable approximate the carrying values due to the short period of time to maturity. See Note 7 of Notes to Condensed Consolidated Financial Statements for disclosure of the approximate fair value of the Company's debt at September 30, 2017 and December 31, 2016.

The following table sets forth the Company's financial assets and liabilities that were accounted for at fair value on a recurring basis as of September 30, 2017 and December 31, 2016 (in millions):

	September 30, 2017	December 31, 2016	Classification
Assets:			
Prepaid Expenses and Other Current Assets:			
Derivative Currency Contracts	\$ 12.9	\$ 2.8	Level 2
Derivative Commodity Contracts	6.6	7.3	Level 2
Other Noncurrent Assets:			
Assets Held in Rabbi Trust	5.6	5.4	Level 1
Derivative Currency Contracts	4.9	0.4	Level 2
Derivative Commodity Contracts	0.2	—	Level 2
Liabilities:			
Current Hedging Obligations:			
Interest Rate Swap	—	3.3	Level 2
Derivative Currency Contracts	8.8	45.7	Level 2
Derivative Commodity Contracts	0.3	—	Level 2
Noncurrent Hedging Obligations:			
Derivative Currency Contracts	0.6	17.6	Level 2

Level 1 fair value measurements for assets held in a Rabbi Trust are unadjusted quoted prices.

Level 2 fair value measurements for derivative assets and liabilities are measured using quoted prices in active markets for similar assets and liabilities. Interest rate swaps are valued based on the discounted cash flows for the LIBOR forward yield curve for a swap with similar contractual terms. Foreign currency forwards are valued based on exchange rates quoted by domestic and foreign banks for similar instruments. Commodity forwards are valued based on observable market transactions of forward commodity prices.

During the nine months ended September 30, 2017, there were no transfers between classification Levels 1, 2 or 3.



### 15. RESTRUCTURING AND RELATED COSTS

The Company incurred restructuring and restructuring related costs on projects beginning in 2014. Restructuring costs include employee termination and plant relocation costs. Restructuring-related costs include costs directly associated with actions resulting from our Simplification initiatives, such as asset write-downs or accelerated depreciation due to shortened useful lives in connection with site closures, discretionary employment benefit costs and other facility rationalization costs. Restructuring costs for employee termination expenses are generally required to be accrued over the employees remaining service period while restructuring costs for plant relocation costs and restructuring-related costs are generally required to be expensed as incurred.

The following is a reconciliation of provisions and payments for the restructuring projects for the three and nine months ended September 30, 2017 and October 1, 2016 (in millions):

	Three Months Ended		Nine Months Ended	
	September 30, 2017	October 1, 2016	September 30, 2017	October 1, 2016
Beginning Balance	\$ 1.3	\$ 1.4	\$ 0.6	\$ 1.3
Provision	1.6	1.1	12.5	4.2
Less: Payments	(1.7 )	(1.3 )	(11.9 )	(4.3 )
Ending Balance	\$ 1.2	\$ 1.2	\$ 1.2	\$ 1.2

The following is a reconciliation of restructuring and restructuring-related costs for the restructuring projects for the three and nine months ended September 30, 2017 and October 1, 2016, respectively (in millions):

	Three Months Ended					
	September 30, 2017			October 1, 2016		
	Cost of Sales	Operating Expenses	Total	Cost of Sales	Operating Expenses	Total
Restructuring Costs:						
Employee Termination Expenses	\$ 0.1	\$ 0.1	\$ 0.2	\$ —	\$ (0.1 )	\$ (0.1 )
Facility Related Costs	1.1	0.2	1.3	(0.1 )	1.1	1.0
Other Expenses	—	0.1	0.1	0.2	—	0.2
Total Restructuring Costs	\$ 1.2	\$ 0.4	\$ 1.6	\$ 0.1	\$ 1.0	\$ 1.1
Restructuring Related Costs:						
Other Employment Benefit Expenses	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Total Restructuring Related Costs	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Total Restructuring and Restructuring Related Costs	\$ 1.2	\$ 0.4	\$ 1.6	\$ 0.1	\$ 1.0	\$ 1.1

	Nine Months Ended					
	September 30, 2017			October 1, 2016		
	Cost of Sales	Operating Expenses	Total	Cost of Sales	Operating Expenses	Total
Restructuring Costs:						
Employee Termination Expenses	\$ 2.5	\$ 1.4	\$ 3.9	\$ 0.4	\$ —	\$ 0.4
Facility Related Costs	3.4	0.5	3.9	0.4	1.5	1.9
Other Expenses	3.9	0.1	4.0	0.8	—	0.8
Total Restructuring Costs	\$ 9.8	\$ 2.0	\$ 11.8	\$ 1.6	\$ 1.5	\$ 3.1
Restructuring Related Costs:						
Other Employment Benefit Expenses	\$ 0.7	\$ —	\$ 0.7	\$ 0.5	\$ 0.6	\$ 1.1
Total Restructuring Related Costs	\$ 0.7	\$ —	\$ 0.7	\$ 0.5	\$ 0.6	\$ 1.1

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Total Restructuring and Restructuring Related Costs \$10.5\$ 2.0 \$12.5 \$2.1\$ 2.1 \$4.2

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The following table shows the allocation of Restructuring Costs by segment for the three and nine months ended September 30, 2017 and October 1, 2016 (in millions):

	Total	Commercial and Industrial Systems	Climate Solutions	Power Transmission Solutions
Restructuring Costs - Three Months Ended September 30, 2017	\$ 1.6	\$ 1.2	\$ 0.3	\$ 0.1
Restructuring Costs - Three Months Ended October 1, 2016	\$ 1.1	\$ 0.2	\$ 0.2	\$ 0.7

	Total	Commercial and Industrial Systems	Climate Solutions	Power Transmission Solutions
Restructuring Costs - Nine Months Ended September 30, 2017	\$12.5	\$ 9.8	\$ 2.0	\$ 0.7
Restructuring Costs - Nine Months Ended October 1, 2016	\$4.2	\$ 1.0	\$ 2.0	\$ 1.2

The Company's current restructuring activities are expected to continue into 2018. The Company expects to record aggregate future charges of approximately \$8.3 million which includes \$1.3 million of employee termination expenses and \$7.0 million of facility related and other costs.

#### 16. SUBSEQUENT EVENT

The Company has evaluated subsequent events from September 30, 2017 through the date of this report. The Company is not aware of any subsequent events that would require recognition or disclosure.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Unless the context requires otherwise, references in this Item 2 to "we," "us," "our" or the "Company" refer collectively to Regal Beloit Corporation and its subsidiaries.

### Overview

Regal Beloit Corporation (NYSE: RBC), based in Beloit, Wisconsin (USA), is a leading manufacturer of electric motors, electrical motion controls, power generation and power transmission products serving markets throughout the world.

### Operating Segments

Our company is comprised of three operating segments: Commercial and Industrial Systems, Climate Solutions and Power Transmission Solutions.

A description of the three operating segments is as follows:

- Commercial and Industrial Systems produces medium and large motors, commercial and industrial equipment, generator and custom drives and systems. These products serve markets including commercial Heating, Ventilation, and Air Conditioning ("HVAC"), pool and spa, standby and critical power and oil and gas systems.
- Climate Solutions produces small motors, controls and air moving solutions serving markets including residential and light commercial HVAC, water heaters and commercial refrigeration.

Power Transmission Solutions manufactures, sells and services belt and chain drives, helical and worm gearing, mounted and unmounted bearings, couplings, modular plastic belts, conveying chains and components, hydraulic pump drives, large open gearing and specialty mechanical products serving markets including beverage, bulk handling, metals, special machinery, energy, aerospace and general industrial.

### Components of Profit and Loss

**Net Sales.** We sell our products to a variety of manufacturers, distributors and end users. Our customers consist of a large cross-section of businesses, ranging from Fortune 100 companies to small businesses. A number of our products are sold to Original Equipment Manufacturers ("OEM's"), who incorporate our products, such as electric motors, into products they manufacture, and many of our products are built to the requirements of our customers. The majority of our sales derive from direct sales, but a significant portion derives from sales made by manufacturer's representatives, who are paid exclusively on commission. Our product sales are made via purchase order, long-term contract, and, in some instances, one-time purchases. Many of our products have broad customer bases, with the levels of concentration of revenues varying from division to division.

Our level of net sales for any given period is dependent upon a number of factors, including (i) the demand for our products; (ii) the strength of the economy generally and the end markets in which we compete; (iii) our customers' perceptions of our product quality at any given time; (iv) our ability to timely meet customer demands; (v) the selling price of our products; and (vi) the weather. As a result, our total revenue has tended to experience quarterly variations and our total revenue for any particular quarter may not be indicative of future results.

We use the term "organic sales" to refer to sales from existing operations excluding (i) sales from acquired businesses recorded prior to the first anniversary of the acquisition less the amount of sales attributable to any divested businesses ("acquisition sales"), and (ii) the impact of foreign currency translation. The impact of foreign currency translation is determined by translating the respective period's sales (excluding acquisition sales) using the same currency exchange rates that were in effect during the prior year periods. We use the term "organic sales growth" to refer to the increase in our sales between periods that is attributable to organic sales. We use the term "acquisition growth" to refer to the increase in our sales between periods that is attributable to acquisition sales.

**Gross Profit.** Our gross profit is impacted by our levels of net sales and cost of sales. Our cost of sales consists of costs for, among other things (i) raw materials, including copper, steel and aluminum; (ii) components such as castings, bars, tools, bearings and electronics; (iii) wages and related personnel expenses for fabrication, assembly and logistics personnel; (iv) manufacturing facilities, including depreciation on our manufacturing facilities and equipment, taxes, insurance and utilities; and (v) shipping. The majority of our cost of sales consists of raw materials and components. The price we pay for commodities and components can be subject to commodity price fluctuations. We attempt to mitigate this through fixed-price agreements with suppliers and our hedging strategies. We are currently reducing the number of our suppliers we use in order to leverage the better prices and terms that can be obtained with higher volume orders. A large amount of our suppliers are in North America. As we expand production and our geographic footprint, we expect it may be advantageous to increase our use of foreign suppliers. When we experience commodity price increases, we have tended to announce price increases to our customers who purchase via purchase order, with such increases generally taking effect a period of time after the public announcements. For those sales we make under long-term contracts, we tend to include material price formulas that specify quarterly or semi-annual price adjustments based on a variety of factors, including commodity prices.

Outside of general economic cyclicality, our different business units experience different levels of variation in gross margin from quarter to quarter based on factors specific to each division. For example, a portion of our Climate Solutions segment manufactures products that are used in air conditioning applications. As a result, our sales for that business tend to be lower in the first and fourth quarters and higher in the second and third quarters. In contrast, our Commercial and Industrial Systems segment and our Power Transmission Solutions segment have a broad customer base and a variety of applications, thereby helping to mitigate large quarter-to-quarter fluctuations outside of general economic conditions.

**Operating Expenses.** Our operating expenses consist primarily of (i) general and administrative expenses; (ii) sales and marketing expenses; (iii) general engineering and research and development expenses; and (iv) handling costs

incurred in conjunction with distribution activities. Personnel related costs are our largest operating expense.

Our general and administrative expenses consist primarily of costs for (i) salaries, benefits and other personnel expenses related to our executive, finance, human resource, information technology, legal and operations functions; (ii) occupancy expenses; (iii) technology related costs; (iv) depreciation and amortization; and (v) corporate-related travel. The majority of our general and administrative costs are for salaries and related personnel expenses. These costs can vary by division given the location of our different manufacturing operations.

Our sales and marketing expenses consist primarily of costs for (i) salaries, benefits and other personnel expenses related to our sales and marketing function; (ii) internal and external sales commissions and bonuses; (iii) travel, lodging and other out-of-pocket expenses associated with our selling efforts; and (iv) other related overhead.

Our general engineering and research and development expenses consist primarily of costs for (i) salaries, benefits and other personnel expenses; (ii) the design and development of new energy efficiency products and enhancements; (iii) quality assurance and testing; and (iv) other related overhead. Our research and development efforts tend to be targeted toward developing new products that would allow us to maintain or gain additional market share, whether in new or existing applications. While these costs make up an insignificant portion of our operating expenses in the Power Transmission Solutions segment, they are more substantial in our Commercial and Industrial Systems and Climate Solutions segments. In particular, a large driver of our research and development efforts in these two segments is energy efficiency, which generally means using less electrical power to produce more mechanical power.

**Operating Profit.** Our operating profit consists of the segment gross profit less the segment operating expenses. In addition, there are shared operating costs that cover corporate, engineering and IT expenses that are consistently allocated to the operating segments and are included in the segment operating expenses. Operating profit is a key metric used to measure year over year improvement of the segments.

**Restructuring and Related Costs.** Beginning in 2014, we announced the closure of several of our manufacturing and warehouse facilities and consolidation into existing facilities to simplify manufacturing operations in our Commercial and Industrial Systems, Climate Solutions and Power Transmission Solutions segments. As a result of these closures, we incurred restructuring and restructuring-related costs. Restructuring costs includes employee termination and plant relocation costs. Restructuring-related costs includes costs directly associated with actions resulting from our simplification initiatives, such as asset write-downs or accelerated depreciation due to shortened useful lives in connection with site closures, discretionary employment benefit costs and other facility rationalization costs. Restructuring costs for employee termination expenses are generally required to be accrued over the employees remaining service period while restructuring costs for plant relocation costs and restructuring-related costs are generally required to be expensed as incurred.

#### Outlook

Our order trends remain positive, and we continue to expect low single digit organic sales growth for the full year.

#### Results of Operations

##### Three Months Ended September 30, 2017 Compared to October 1, 2016

Net sales increased \$47.3 million or 5.8% for the third quarter 2017 compared to the third quarter 2016. The increase consisted of an organic sales growth increase of 5.2% and a positive foreign currency translation impact of 0.7%. Gross profit decreased \$4.7 million or 210 basis points as a percentage of net sales for the third quarter 2017 as compared to the third quarter 2016 primarily due to an increase in the last-in, first-out (“LIFO”) reserve of \$2.7 million and commodity inflation, partially offset by the sales volume increase. Operating expenses for the third quarter 2017 decreased \$8.9 million or 6.3% as compared to the same period in the prior year due to a \$2.8 million gain on sale of assets, lower amortization expense and leveraging of costs on the increased sales volume.

Commercial and Industrial Systems Segment net sales for the third quarter 2017 were \$408.0 million, an increase of \$18.6 million or 4.8% as compared to the third quarter 2016. The increase consisted of an organic sales growth increase of 4.0% driven by broad strength in the North American commercial and industrial end markets, growth in Asia and improvement in oil and gas. In addition, foreign currency translation had a positive impact of 0.8%. Gross profit decreased \$7.4 million or 310 basis points as a percentage of net sales for the third quarter 2017 as compared to the third quarter 2016 primarily driven by an increase in the LIFO reserve of \$1.5 million and commodity inflation, which were partially offset by the sales volume increase. Operating expenses for the third quarter 2017 were \$68.4 million which was 1.2% lower as compared to the same period in the prior year mainly due to lower amortization expense and lower discretionary spending.

Climate Solutions Segment net sales were \$256.0 million, an increase of 2.2% compared to third quarter 2016. The increase consisted of an organic sales growth increase of 1.9% driven by growth in North American residential HVAC new equipment up modestly and strength in Europe, Middle East and Asia. Foreign currency translation had a positive

0.3% impact on the net sales for the third quarter 2017. Gross profit decreased \$5.6 million or 280 basis points as a percentage of net sales as compared to the prior year primarily driven by an increase in the LIFO reserve of \$1.2 million and commodity inflation, which were partially offset by the sales volume increase. Operating expenses for the third quarter 2017 were \$27.0 million compared to \$29.2 million in the third quarter 2016. The \$2.2 million or 120 basis point as a percent of net sales decrease was primarily due to the leveraging of costs on the increased sales volume and lower discretionary spending.

Power Transmission Solutions Segment net sales for the third quarter 2017 were \$192.9 million or a 13.7% increase compared to third quarter 2016 net sales of \$169.7 million. The increase consisted of an organic sales growth increase of 12.8% primarily driven by strength in oil and gas, distribution and renewable energy. Foreign currency translation had a positive impact of 0.9%.

Gross profit for the third quarter 2017 increased \$8.3 million or 15.1% primarily due to the increase in sales volume. Operating expenses for the third quarter 2017 decreased \$5.9 million as compared to the third quarter 2016 primarily due to a \$2.8 million gain on sale of assets, decrease in restructuring charges, and lower discretionary spending.

Nine Months Ended September 30, 2017 Compared to October 1, 2016

Net sales increased \$73.2 million or 3.0% for the nine months ended September 30, 2017 compared to the nine months ended October 1, 2016. The increase consisted of an organic sales growth increase of 3.5%, offset by a negative impact from sales of the divested Mastergear Worldwide (“Mastergear”) business of 0.4% and a negative foreign currency translation impact of 0.2%. Gross profit for the nine months ended September 30, 2017 decreased \$6.4 million or 1.0% compared to the nine months ended October 1, 2016 primarily due to increased restructuring charges and an increase in the LIFO reserve of \$2.7 million, partially offset by the increase in sales volume. Operating expenses for the nine months ended September 30, 2017 decreased \$7.7 million or 80 basis point as a percent of net sales as compared to the same period in the prior year due to a \$3.5 million gain on sale of assets, decrease in amortization expense, lower discretionary spending and leveraging of costs on the increased sales volume. The prior year included a \$11.6 million gain on the sale of the Mastergear business.

Commercial and Industrial Systems Segment net sales increased \$34.9 million or 3.0% for the nine months ended September 30, 2017 compared to the nine months ended October 1, 2016. The increase consisted of an organic sales growth increase of 3.3% that was offset by a negative foreign currency translation impact of 0.3%. The organic sales increase was primarily driven by strength in Asia, North American oil and gas and industrial end market demand.

Gross profit for nine months ended 2017 decreased \$9.7 million or 3.3% primarily due to the impact of increased restructuring charges resulting from the exit of a non-core business and an increase in the LIFO reserve of \$1.5 million that was offset by the increased sales volume. Operating expenses for the nine months ended September 30, 2017 decreased \$2.7 million or 1.3% compared to the nine months ended October 1, 2016 primarily due to a \$0.7 million gain on sale of assets, lower amortization expenses and lower discretionary spending.

Climate Solutions Segment net sales increased \$29.4 million or 3.9% for the nine months ended September 30, 2017 compared to the nine months ended October 1, 2016. The increase consisted of an organic sales growth increase of 4.0% and a negative foreign currency translation impact of 0.1%. The organic sales increase was primarily driven by growth in North American residential HVAC, Europe and Asia. Gross profit increased \$2.5 million or 1.3% primarily due to higher volumes. Operating expenses for the nine months ended September 30, 2017 decreased \$4.8 million or 110 basis point as a percent of net sales as compared to the nine months ended October 1, 2016 due to lower amortization expenses, lower discretionary spending and leveraging of costs on the increased sales volume.

Power Transmission Solutions Segment net sales increased \$8.9 million or 1.6% for the nine months ended September 30, 2017 compared to the nine months ended October 1, 2016. The increase consisted of an organic sales growth increase of 3.3% that was offset by a negative foreign currency translation impact of 0.1% and a negative impact from sales of the divested Mastergear business of 1.6%. Improved oil and gas and renewable energy end market demand contributed to the organic sales increase. Gross profit for the nine months ended September 30, 2017 increased \$0.8 million or 0.4% compared to the nine months ended October 1, 2016 primarily due to the higher sales volume.

Operating expenses for the nine months ended September 30, 2017 decreased \$0.2 million or 40 basis point as a percent of net sales due to a \$2.8 million gain on the sale of assets, decrease in restructuring charges and leveraging of costs on the increased sales volume. The prior year included a \$11.6 million gain on the sale of the Mastergear business.

	Three Months Ended		Nine Months Ended		
	September 30, 2017	October 1, 2016	September 30, 2017	October 1, 2016	
(Dollars in Millions)					
Net Sales:					
Commercial and Industrial Systems	\$408.0	\$389.4	\$1,196.6	\$1,161.7	
Climate Solutions	256.0	250.5	774.2	744.8	
Power Transmission Solutions	192.9	169.7	568.8	559.9	
Consolidated	\$856.9	\$809.6	\$2,539.6	\$2,466.4	
Gross Profit as a Percent of Net Sales:					
Commercial and Industrial Systems	24.0	% 27.1	% 23.9	% 25.4	%
Climate Solutions	25.7	% 28.5	% 25.2	% 25.8	%
Power Transmission Solutions	32.8	% 32.4	% 32.6	% 33.0	%
Consolidated	26.5	% 28.6	% 26.2	% 27.2	%
Operating Expenses as a Percent of Net Sales:					
Commercial and Industrial Systems	16.8	% 17.8	% 17.5	% 18.3	%
Climate Solutions	10.5	% 11.7	% 10.9	% 12.0	%
Power Transmission Solutions	19.5	% 25.6	% 21.0	% 21.4	%
Consolidated	15.5	% 17.5	% 16.3	% 17.1	%
Income from Operations as a Percent of Net Sales:					
Commercial and Industrial Systems	7.3	% 9.3	% 6.4	% 7.1	%
Climate Solutions	15.2	% 16.8	% 14.2	% 13.8	%
Power Transmission Solutions	13.3	% 6.7	% 11.5	% 11.5	%
Consolidated	11.0	% 11.1	% 9.9	% 10.2	%
Income from Operations	\$94.0	\$89.8	\$251.8	\$250.5	
Interest Expense	13.5	14.4	42.6	44.2	
Interest Income	0.7	1.1	2.7	3.4	
Income before Taxes	81.2	76.5	211.9	209.7	
Provision for Income Taxes	17.6	15.4	46.4	47.5	
Net Income	63.6	61.1	165.5	162.2	
Less: Net Income Attributable to Noncontrolling Interests	1.4	1.5	4.0	4.4	
Net Income Attributable to Regal Beloit Corporation	\$62.2	\$59.6	\$161.5	\$157.8	

The effective tax rate for the three months ended September 30, 2017 was 21.7% versus 20.2% for the three months ended October 1, 2016. The effective tax rate for the nine months ended September 30, 2017 was 21.9% versus 22.7% for the nine months ended October 1, 2016. The effective tax rate for the nine months ended September 30, 2017 was 21.9% versus 22.7% for the nine months ended October 1, 2016. The change in the effective tax rate for the three months ended September 30, 2017 was primarily driven by the mix of earnings and the favorable adjustments related to the 2016 finalization of the 2015 US federal income tax return. The change in the effective tax rate for the nine months ended September 30, 2017 was primarily driven by the mix of earnings and the favorable adjustments related to the finalization of the 2015 US federal income tax return, partially offset by the 2016 gain derived from the sale of the Mastergear business. The lower effective rate as compared to the 35.0% statutory Federal income tax rate is driven

by lower foreign tax rates.

Liquidity and Capital Resources

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## General

Our principal source of liquidity is cash flow provided by operating activities. In addition to operating income, other significant factors affecting our cash flow include working capital levels, capital expenditures, dividends, share repurchases, acquisitions, availability of debt financing, and the ability to attract long-term capital at acceptable terms.

Cash flow provided by operating activities was \$235.0 million for the nine months ended September 30, 2017, a \$95.4 million decrease from the nine months ended October 1, 2016. The decrease was primarily the result of the higher investment in net working capital for the nine months ended September 30, 2017 as compared to the nine months ended October 1, 2016.

Cash flow used in investing activities was \$42.0 million for the nine months ended September 30, 2017 versus \$29.5 million for the nine months ended October 1, 2016. The change was driven by the \$25.5 million received for the sale of our Mastergear business in the nine months ended October 1, 2016.

Cash flow used in financing activities was \$298.9 million for the nine months ended September 30, 2017, compared to \$267.8 million provided by financing activities for the nine months ended October 1, 2016. Net debt repayments of \$200.4 million were made during the nine months ended September 30, 2017, compared to net debt repayments of \$214.9 million made during the nine months ended October 1, 2016. We paid \$33.1 million in dividends to shareholders in the nine months ended September 30, 2017, compared to \$31.3 million for the nine months ended October 1, 2016. Cash used for share repurchases was \$45.1 million for the nine months ended September 30, 2017. There were no share repurchases for the nine months ended October 1, 2016.

Our working capital was \$895.3 million at September 30, 2017, compared to \$830.4 million at December 31, 2016. At September 30, 2017 and December 31, 2016, our current ratio (which is the ratio of our current assets to current liabilities) was 2.2:1. Our working capital increased primarily due to an increase in Trade Receivables of \$65.1 million and a \$74.1 million increase in Inventories which was partially offset by a \$83.0 million increase in Accounts Payable. We paid our \$100.0 million 2007 private placement debt due in August using existing cash as well as cash generated from operations and \$100.0 million of our 2011 private placement debt due in July, 2018 moved from a long-term classification to a current classification at September 30, 2017 compared to December 31, 2016.

The following table presents selected financial information and statistics as of September 30, 2017 and December 31, 2016 (in millions):

	September 30, 2017	December 31, 2016
Cash and Cash Equivalents	\$ 186.6	\$ 284.5
Trade Receivables, Net	527.3	462.2
Inventories	734.9	660.8
Working Capital	895.3	830.4
Current Ratio	2.2:1	2.2:1

At September 30, 2017, our cash and cash equivalents totaled \$186.6 million. At September 30, 2017, \$182.9 million of our cash was held by foreign subsidiaries and could be used in our domestic operations if necessary. The repatriation of cash from certain foreign subsidiaries could have adverse net tax consequences on us should we be required to pay and record US income taxes and foreign withholding taxes on such funds. We periodically evaluate our cash held outside the US and may pursue opportunities to repatriate certain foreign cash amounts to the extent that we do not incur unfavorable net tax consequences. During the nine months ended September 30, 2017, we have repatriated \$154.3 million of foreign cash.

Substantially all of our expenses are paid in cash, often with payment term provisions that include early payment discounts and time elements. We believe that our ability to generate positive cash flow coupled with our available revolving credit balance will be sufficient to fund our operations for the foreseeable future. We focus on optimizing our investment in working capital through improved and enforced payment terms, maintaining an optimal level of inventory and operational efficiencies. Additionally, we believe that our capital expenditures for maintenance of equipment and facilities will be consistent with prior levels and not present a funding challenge.

We will, from time to time, maintain excess cash balances which may be used to (i) fund operations, (ii) repay outstanding debt, (iii) fund acquisitions, (iv) pay dividends, (v) make investments in new product development programs, (vi) repurchase our common stock, or (vii) fund other corporate objectives.

### Credit Agreement

In connection with the PTS Acquisition, on January 30, 2015, we entered into a new Credit Agreement (the “Credit Agreement”) with JPMorgan Chase Bank, N.A., as Administrative Agent and the lenders named therein, providing for a (i) 5-year unsecured term loan facility in the principal amount of \$1.25 billion (the “Term Facility”) and (ii) a 5-year unsecured multicurrency revolving facility in the principal amount of \$500.0 million (the “Multicurrency Revolving Facility”), including a \$100 million letter of credit sub facility available for general corporate purposes. Borrowings under the Credit Agreement bear interest at floating rates based upon indices determined by the currency of the borrowing, plus an applicable margin determined by reference to our consolidated funded debt to consolidated EBITDA ratio or at an alternative base rate.

The Term Facility was drawn in full on January 30, 2015 in connection with the closing of the PTS Acquisition. The loan under the Term Facility requires quarterly amortization at a rate starting at 5.0% per annum, increasing to 7.5% per annum after two years and further increasing to 10.0% per annum for the last two years of the Term Facility, unless previously prepaid. The weighted average interest rate on the Term Facility was 2.7% and 2.5% for the three and nine months ended September 30, 2017, respectively and 2.0% for the three and nine months ended October 1, 2016. The Credit Agreement requires we prepay the loans under the Term Facility with 100% of the net cash proceeds received from specified asset sales and borrowed money indebtedness, subject to certain exceptions.

At September 30, 2017, we had borrowings under the Multicurrency Revolving Facility in the amount of \$29.6 million, \$29.8 million of standby letters of credit issued under the facility, and \$440.6 million of available borrowing capacity. The average daily balance in borrowings under the Multicurrency Revolving Facility was \$97.8 and \$105.4 million, and the weighted average interest rate on the Multicurrency Revolving Facility was 2.7% and 2.5% for the three and nine months ended September 30, 2017, respectively. The average daily balance in borrowings under the Multicurrency Revolving Facility was \$29.7 million and \$45.1 million, and the weighted average interest rate on the Multicurrency Revolving Facility was 1.9% for the three and nine months ended October 1, 2016, respectively. We pay a non-use fee on the aggregate unused amount of the Multicurrency Revolving Facility at a rate determined by reference to its consolidated funded debt to consolidated EBITDA ratio.

### Senior Notes

At September 30, 2017, we had \$500.0 million of senior notes (the “Notes”) outstanding. The Notes consist of \$500.0 million in senior notes (the “2011 Notes”) in a private placement which were issued in seven tranches with maturities from seven to twelve years and carry fixed interest rates. As of September 30, 2017, \$400.0 million of the 2011 Notes are included in Long-Term Debt and \$100.0 million of the 2011 Notes are included in Current Maturities of Long-Term Debt on the Condensed Consolidated Balance Sheets. We repaid the remaining \$100.0 million of the 2007 Notes in August, 2017.

Details on the Notes at September 30, 2017 were (in millions):

	Principal	Interest Rate	Maturity
Fixed Rate Series 2011A	100.0	4.1%	July 14, 2018
Fixed Rate Series 2011A	230.0	4.8 to 5.0%	July 14, 2021
Fixed Rate Series 2011A	170.0	4.9 to 5.1%	July 14, 2023
	\$ 500.0		

We had an interest rate swap agreement to manage fluctuations in cash flows resulting from interest rate risk (see also Note 13 of Notes to the Condensed Financial Statements). The remaining interest rate swap agreement terminated in August, 2017.

### Compliance with Financial Covenants

The Credit Agreement and the Notes require us to meet specified financial ratios and to satisfy certain financial condition tests. We were in compliance with all financial covenants contained in the Notes and the Credit Agreement as of September 30, 2017.

Other Notes Payable

At September 30, 2017, other notes payable of approximately \$5.1 million were outstanding with a weighted average interest rate of 5.2%. At December 31, 2016, other notes payable of approximately \$5.1 million were outstanding with a weighted average rate of 5.6%.

Based on rates for instruments with comparable maturities and credit quality, which are classified as Level 2 inputs (see also Note 14 of Notes to the Condensed Consolidated Financial Statements), the approximate fair value of our total debt was \$1,244.2 million and \$1,433.4 million as of September 30, 2017 and December 31, 2016, respectively.

#### Critical Accounting Policies

Our disclosures of critical accounting policies, which are contained in our Annual Report on Form 10-K for the year ended December 31, 2016, have not materially changed since that report was filed.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to market risk relating to our operations due to changes in interest rates, foreign currency exchange rates and commodity prices of purchased raw materials. We manage the exposure to these risks through a combination of normal operating and financing activities and derivative financial instruments such as interest rate swaps, commodity cash flow hedges and foreign currency forward exchange contracts. All hedging transactions are authorized and executed pursuant to clearly defined policies and procedures, which strictly prohibit the use of financial instruments for speculative purposes.

All qualified hedges are recorded on the balance sheet at fair value and are accounted for as cash flow hedges, with changes in fair value recorded in accumulated other comprehensive income (loss) ("AOCI") in each accounting period. An ineffective portion of the hedges change in fair value, if any, is recorded in earnings in the period of change.

#### Interest Rate Risk

We are exposed to interest rate risk on certain of our short-term and long-term debt obligations used to finance our operations and acquisitions. At September 30, 2017, excluding the impact of interest rate swaps, we had \$504.8 million of fixed rate debt and \$709.6 million of variable rate debt. We have utilized interest rate swaps to manage fluctuations in cash flows resulting from exposure to interest rate risk on forecasted variable rate interest payments. The remaining interest rate swap agreement terminated in August, 2017.

We have floating rate borrowings, which expose us to variability in interest payments due to changes in interest rates. A hypothetical 10% change in our weighted average borrowing rate on outstanding variable rate debt at September 30, 2017 would result in a \$1.2 million change in after-tax annualized earnings. We had entered into a pay fixed/receive floating interest rate swap to manage fluctuations in cash flows resulting from interest rate risk related to the floating rate interest on our 2007 Notes which were paid in August, 2017. This interest rate swap had been designated as a cash flow hedge against forecasted interest payments.

As of December 31, 2016, an interest rate swap liability of \$(3.3) million was included in Current Hedging Obligations. The unrealized loss on the effective portion of the contract, net of tax, of \$(2.1) million as of December 31, 2016, respectively, was recorded in AOCI. The interest rate swap matured on August 23, 2017.

#### Foreign Currency Risk

We are exposed to foreign currency risks that arise from normal business operations. These risks include the translation of local currency balances of foreign subsidiaries, intercompany loans with foreign subsidiaries and transactions denominated in foreign currencies. Our objective is to minimize our exposure to these risks through a combination of normal operating activities and the utilization of foreign currency exchange contracts to manage our exposure on the forecasted transactions denominated in currencies other than the applicable functional currency. Contracts are executed with credit worthy banks and are denominated in currencies of major industrial countries. We do not hedge our exposure to the translation of reported results of foreign subsidiaries from local currency to United States dollars.

#### Derivatives

As of September 30, 2017, derivative currency assets (liabilities) of \$12.9 million, \$4.9 million, \$(8.8) million and \$(0.6) million, are recorded in Prepaid Expenses and Other Current Assets, Other Noncurrent Assets, Current Hedging Obligations, and Noncurrent Hedging Obligations, respectively. As of December 31, 2016, derivative currency assets

(liabilities) of \$2.8 million, \$0.4 million, \$(45.7) million and \$(17.6) million, are recorded in Prepaid Expenses and Other Current Assets, Other Noncurrent Assets, Current Hedging Obligations, and Noncurrent Hedging Obligations, respectively. The unrealized gains (losses) on the contracts of \$3.5 million net of tax, and \$(34.4) million net of tax, as of September 30, 2017 and December 31, 2016 respectively, were recorded in AOCI. At September 30, 2017, we had \$(2.3) million, net of tax, of derivative currency losses on closed hedge instruments in AOCI that will be realized in earnings when the hedged items impact earnings. At December 31, 2016, we had \$(8.0) million of

derivative currency losses on closed hedge instruments in AOCI that will be realized in earnings when the hedged items impacted earnings.

The following table quantifies the outstanding foreign exchange contracts intended to hedge non-US dollar denominated receivables and payables and the corresponding impact on the value of these instruments assuming a hypothetical 10% appreciation/depreciation of their counter currency on September 30, 2017 (in millions):

Currency	Notional Amount	Fair Value	Gain (Loss) From	
			10% Appreciation of Counter Currency	10% Depreciation of Counter Currency
Chinese Renminbi	\$ 218.0	\$ 8.9	\$ 21.8	\$ (21.8)
Mexican Peso	164.9	(1.0)	16.5	(16.5)
Euro	63.8	(0.2)	6.4	(6.4)
Indian Rupee	37.7	2.1	3.8	(3.8)
Canadian Dollar	51.3	(1.0)	5.1	(5.1)
Australian Dollar	13.2	(0.4)	1.3	(1.3)
Thai Baht	7.1	—	0.7	(0.7)
British Pound	9.9	—	1.0	(1.0)

Gains and losses indicated in the sensitivity analysis would be offset by gains and losses on the underlying forecasted non-US dollar denominated cash flows.

#### Commodity Price Risk

We periodically enter into commodity hedging transactions to reduce the impact of changing prices for certain commodities such as copper and aluminum based upon forecasted purchases of such commodities. Qualified hedge transactions are designated as cash flow hedges and the contract terms of commodity hedge instruments generally mirror those of the hedged item, providing a high degree of risk reduction and correlation.

#### Derivatives

Derivative commodity assets (liabilities) of \$6.6 million, \$0.2 million, and \$(0.3) million were recorded in Prepaid Expenses and Other Current Assets, Other Noncurrent Assets and Current Hedging Obligations, respectively, at September 30, 2017. Derivative commodity assets of \$7.3 million are recorded in Prepaid Expenses at December 31, 2016. The unrealized gains on the effective portion of the contracts of \$3.6 million net of tax and \$2.9 million net of tax, as of September 30, 2017 and December 31, 2016, respectively, were recorded in AOCI. At September 30, 2017, we had \$2.2 million, net of tax, of derivative commodity gains on closed hedge instruments in AOCI that will be realized in earnings when the hedged items impact earnings. At December 31, 2016, there was \$0.5 million, net of tax, of derivative commodity gains on closed hedge instruments in AOCI that were realized into earnings when the hedged items impacted earnings.

The following table quantifies the outstanding commodity contracts intended to hedge raw material commodity prices and the corresponding impact on the value of these instruments assuming a hypothetical 10% appreciation/depreciation of their prices on September 30, 2017 (in millions):

Commodity	Notional Amount	Fair Value	Gain (Loss) From	
			10% Appreciation of Commodity Prices	10% Depreciation of Commodity Prices
Copper	\$ 64.0	\$ 6.0	\$ 6.4	\$ (6.4)
Aluminum	4.5	0.5	0.5	(0.5)

Gains and losses indicated in the sensitivity analysis would be offset by the actual prices of the commodities.

The net AOCI balance of \$7.0 million gain at September 30, 2017 includes \$6.5 million of net current deferred gains expected to be realized in the next twelve months.

#### Counterparty Risk

We are exposed to credit losses in the event of non-performance by the counterparties to various financial agreements, including our interest rate swap agreements, foreign currency exchange contracts and commodity hedging transactions. We manage exposure to counterparty credit risk by limiting our counterparties to major international banks and financial institutions meeting established credit guidelines and continually monitoring their compliance with the credit guidelines. We do not obtain collateral or other security to support financial instruments subject to credit risk. We do not anticipate non-performance by our counterparties, but cannot provide assurances.

### ITEM 4. CONTROLS AND PROCEDURES

#### Disclosure Controls and Procedures

The Company's management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the period covered by this report. Based on such evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, the Company's disclosure controls and procedures were effective to ensure that (a) information required to be disclosed in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission, and (b) information required to be disclosed by us in the reports the Company files or submits under the Exchange Act is accumulated and communicated to our management, including its Chief Executive Officer and its Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

#### Internal Control Over Financial Reporting

There were no changes in the Company's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## PART II—OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

There have been no material changes in the legal matters described in Part I, Item 3 of the Company's Annual Report on Form 10-K for the year ended December 31, 2016, which is incorporated here by reference.

### ITEM 1A. RISK FACTORS

Our business and financial results are subject to numerous risks and uncertainties. The risk and uncertainties have not changed materially from those reported in Item 1A in our 2016 Annual Report on Form 10-K for the year ended December 31, 2016, which is incorporated here by reference. For additional information regarding risks and uncertainties facing the Company, please also see the information provided under the header "Cautionary Statement" contained in this Quarterly Report on Form 10-Q.

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

The following table contains detail related to the repurchase of our common stock based on the date of trade during the quarter ended September 30, 2017.

2017 Fiscal Month	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as a Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May be Purchased Under the Plans or Programs
July 2 to Aug 5	1,568	\$ 84.03	—	2,043,196
Aug 6 to Sep 2	301,416	77.82	300,000	1,743,196
Sep 3 to Sep 30	274	79.38	—	1,743,196
	303,258		300,000	

Under our equity incentive plans, participants may pay the exercise price or satisfy all or a portion of the federal, state and local withholding tax obligations arising in connection with plan awards by electing to (a) have the Company withhold shares of common stock otherwise issuable under the award, (b) tender back shares received in connection with such award or (c) deliver other previously owned shares of common stock, in each case having a value equal to the exercise price or the amount to be withheld. During the quarter ended September 30, 2017, we acquired 3,258 shares in connection with transactions pursuant to equity incentive plans.

In November, 2013, the Board of Directors approved the repurchase of up to 3.0 million shares of our common stock, which repurchase authority has no expiration date. Management is authorized to effect purchases from time to time in the open market or through privately negotiated transactions. During the quarter ended September 30, 2017, we acquired 300,000 shares pursuant to this authorization. We have entered into a Rule 10b5-1 trading plan for the purpose of repurchasing shares under this authorization, and certain of our purchases under the authorization during the quarter were made pursuant to the Rule 10b5-1 trading plan.

ITEM 6. EXHIBITS

Exhibit Number	Exhibit Description
12	Computation of Ratio of Earnings to Fixed Charges.
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certifications of the Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350.
101	The following materials from Regal Beloit Corporation's Quarterly Report on Form 10-Q for the quarter ended September 30, 2017, formatted in XBRL (Extensible Business Reporting Language): (i) the Condensed Consolidated Statements of Income, (ii) the Condensed Consolidated Statements of Comprehensive Income, (iii) the Condensed Consolidated Balance Sheets, (iv) the Condensed Consolidated Statements of Equity, (v) the Condensed Consolidated Statements of Cash Flows, and (vi) Notes to Condensed Consolidated Financial Statements.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

REGAL BELOIT CORPORATION  
(Registrant)

/s/ Charles A. Hinrichs  
Charles A. Hinrichs  
Vice President  
Chief Financial Officer  
(Principal Financial Officer)

/s/ Robert A. Lazzerini  
Robert A. Lazzerini  
Vice President  
Corporate Controller  
(Principal Accounting Officer)

Date: November 6, 2017

INDEX TO EXHIBITS

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