KSB Group

Half-year Financial Report 2014

CONTENTS

INTERIM MANAGEMENT REPORT FOR THE SIX MONTHS ENDED 30 JUNE 2014

MACROECONOMIC ENVIRONMENT AND SECTOR VIEW

The global economy revived slightly in the first half of 2014. In the European Union the southern European economies moved into moderate recovery, which improved the business prospects in our home market to some degree. There were also signs of growth in a number of other states. However, growth in the major emerging markets was less vigorous overall than in earlier years.

In particular, the economy in Russia stagnated in the wake of the Ukraine crisis. Political factors also affected the economy in India, where many investors held back on new projects, awaiting the outcome of the parliamentary elections, which were due to finish in May. The Brazilian economy was constrained by continuing structural problems and a reluctance to invest, causing the country's central bank to lower its forecast for annual growth from 2 % to 1.6 %. By contrast, China grew almost in line with expectations in the first half of the year and continues to aim for annual growth of 7.5 %. Measures to stimulate the economy are also intended to help.

The world's largest economy – the USA – was heavily impacted in the first quarter by the extreme winter. As a result, the International Monetary Fund (IMF) reduced its 2014 growth forecast from 2.8 % to 1.7 %.

According to the VDMA German Engineering Federation, order intake in the German mechanical engineering industry in the first half of 2014 was unchanged year on year.

BUSINESS DEVELOPMENT

In the first half of 2014 we realigned our Sales organisation, and for the first term served our customers through three separate channels – for general business, project business and products installed in systems (installed base).

We have created the technical foundation for the planned expansion of our business with standard products by launching a range of upgraded pumps and systems. These are primarily for our general business, which we are expanding by strengthening our sales network in a number of countries. In the project business, where we also supply engineered pumps and valves, demand improved slightly, although pressure on prices in the power plant business continued to be high, which impacted margins.

Increase in order volume for pumps

Order intake in the Group in the first six months rose 3.2 % to € 1,131.9 million year on year. This improvement was attributable to the increase of 7.7 % in orders received for pumps, which totalled € 765.9 million. There was a decline in order intake for valves and service, with orders for valves falling 1.8 % to € 189.5 million, and orders in the Service business unit dropping 8.2 % to € 176.5 million.

Translation of order values into the Group currency, the euro, suffered clearly from the changes in exchange rates (€ –55 million).

Orders worth € 1.9 million are attributable to the first-time consolidation of two companies in Spain and Morocco.

Group companies in Europe reported an increase of 8.8 % in order intake to € 696.9 million. This was primarily due to the development of KSB AG, which booked a number of major orders. At € 426.7 million, orders received by our German parent company were up 12.3 % year on year.

After rising sharply last year, orders at our Group companies in the Region Middle East / Africa dropped 8.6 % in the first half of 2014 to € 58.4 million. A major reason for this was developments in South Africa, where prolonged strikes led to a loss of production in various industries; in addition, the national currency lost value against the euro.

In the Region Asia, companies in China, South Korea and several countries in South-East Asia reported renewed growth in order intake. Overall, incoming orders rose 1.7 % to € 176.1 million. Higher growth in the Region was prevented by the decline in India, where investors were extremely reticent with orders in the run-up to the elections.

The weakness in the mining market made itself felt at several companies in the Region Americas / Oceania. This primarily affected our slurry pump manufacturer GIW Industries, Inc. in the USA and our companies in Chile and Australia. Our Brazilian companies, too, reported lower orders, also reflecting the depreciation of the Real against the euro. Overall, our subsidiaries in the Americas and Australia were down 8.5 % on the first six months of 2013, totalling € 200.5 million.

Currency effects reduce Group sales revenue

Consolidated Group sales revenue in the first half of 2014 amounted to € 1,011.6 million, 7.2 % lower than the previous year. Over half of this decrease of € 78.5 million (€ 51 million) was due to changes in exchange rates.

Sales revenues by the Pumps, Valves and Service business units (excluding PoC effects) were all lower year on year. Our business with pumps totalled € 644.5 million (– 11.2 %), while valves amounted to € 178.9 million (– 4,3 %). Sales revenue in the Service business unit fell to € 164.4 million (– 11.4 %).

In our European companies, sales revenue dropped 4.4 % to € 627.4 million. A key factor in this was the trend at KSB AG, which posted sales revenue (in accordance with the *HGB* German Commercial Code) of € 374.6 million, a decrease of 9.8 %. There were also significant declines in sales revenue at companies in France, Italy and Russia.

By contrast, the Region Middle East / Africa showed sales revenue up 8.9 % at € 62.4 million. This is almost entirely attributable to the strong growth at KSB Middle East FZE in Dubai, which included invoices for two major orders from Saudi Arabia and Qatar.

Our companies in the Region Asia reported sales revenue of € 142.5 million, 11.5 % lower year on year. A particular factor here was the weakness of business at our Indian companies and KSB Shanghai Pump Co. Ltd. in China. By contrast, several smaller companies in East and South-East Asia did well.

The slump in mining made itself felt at our companies in the Region Americas / Oceania, affecting sales revenue as well. In Chile, the USA and Australia, mine operators significantly reduced orders for pumps, spare parts and service. Overall, sales revenue of our American companies and KSB Australia Pty. Ltd. fell 16.8 % to € 179.3 million. One factor in this was the trend at our Brazilian companies, where growth in sales revenue was insufficient to offset the depreciation of the national currency (Real) against the group currency (euro).

The sales revenue figures include sales revenue of € 1.6 million from the two companies consolidated for the first time.

Increase in orders in hand

As sales revenue in the first six months lagged behind order intake, orders in hand rose by some € 120 million compared with year end 2013, to a total of almost € 1.3 billion. This includes long-term major orders which – depending on our customers’ construction plans – will be delivered and invoiced in two to three years.

RESULTS OF OPERATIONS, FINANCIAL POSITION AND NET ASSETS

The expectations for our business development outlined in the previous year’s management report (considerable growth in order intake, slight rise in all other key indicators) have not yet been met. A major reason is the ongoing difficult situation in the power plant business, with continuing heavy pressure on prices. Negative currency effects and postponements of project deadlines impacted the development of sales revenue. For more details see the Business Development section of this interim management report.

The decline in sales revenue (– 7.2 %) and the currency effects noted above led to a decrease (€ –28.9 million) in earnings before interest and taxes (EBIT). This applied to the two business units Pumps and Service, while EBIT in the Valves business unit rose by € 3.4 million.

Earnings before taxes (EBT) decreased by a similar amount (€ –28.1 million). As a result, return on sales (before taxes) was 2.1 %, down from 4.5 % in the comparative prior-year period. By contrast, the net financial position increased by € 49.1 million compared with 30 June 2013.

RESULTS OF OPERATIONS

Total output of operations

At € 1,031.5 million, the total output of operations was 7.3 % below the prior-year figure of € 1,112.2 million. This was influenced by the above-mentioned changes to sales revenue and somewhat smaller increases in inventories.

Income and expenses

The cost of materials decreased by € 37.2 million compared with the first six months of 2013 as a result of the drop in sales revenue. This item represents 40.6 % of the total output of operations (previous year: 41.0 %).

Due to the decrease in the number of employees, staff costs fell from € 394.2 million to € 389.4 million. Staff costs as a percentage of the lower total output of operations rose by 2.4 percentage points year on year to 37.8 %.

At € 172.7 million, other expenses were down € 10.6 million on the previous year, and remained virtually unchanged as a percentage of total output of operations. The main reasons for the decrease were the lower administrative expenses and selling expenses.

Half-year earnings

In the first six months, earnings before interest and taxes (EBIT) of the KSB Group totalled € 28.4 million (previous year: € 57.3 million). The Pumps business unit reported EBIT of € 12.3 million (previous year: € 43.9 million), the Valves business unit € 4.8 million (previous year: € 1.4 million) and the Service business unit € 4.8 million (previous year: € 12.3 million). The reconciliation effect from the measurement of construction contracts in accordance with IAS 11 changed by about € 7 million year on year.

At € 20.7 million, earnings before taxes (EBT) were also lower than the prior-year figure of € 48.8 million. The return on sales declined accordingly to 2.1 % (previous year: 4.5 %). As a result of lower earnings contributions from the German Group companies, the income tax rate fell by 3.6 percentage points to 28.0 %, down from 31.6 % in the first half of 2013. The KSB Group accordingly reported earnings after taxes of € 14.9 million (previous year: € 33.4 million).

Earnings attributable to non-controlling interests fell less sharply from € 6.9 million to € 3.8 million, which resulted in a change in the ratio to earnings after taxes from 20.5 % to 25.6 %.

Earnings attributable to shareholders of KSG AG (€ 11.1 million) were € 15.4 million lower than in the previous year (€ 26.5 million).

Earnings per ordinary share amounted to € 6.21, compared with € 15.04 in the previous year, and € 6.47 per preference share, compared with € 15.30 in 2013.

FINANCIAL POSITION

Equity

KSB Group equity has decreased from € 844.5 million (31 December 2013) to € 817.0 million. This was primarily attributable to the change in actuarial gains / losses under IAS 19 resulting from the declining discount rate. At 37.8 %, the equity ratio is now 1.5 percentage points lower than at year end 2013.

Liabilities

Liabilities have increased by € 36.9 million since year end 2013. Provisions increased by € 30.7 million, with long-term provisions for employee benefits rising € 44.5 million, mainly as a result of the change in actuarial gains / losses under IAS 19 mentioned above. By contrast, short-term provisions for employee benefits decreased by € 12.9 million, due among other reasons to lower profit sharing. The decrease in trade payables and bank loans and overdrafts contrasted with significantly higher advances received.

Investments

At € 29.4 million, investment in property, plant and equipment was slightly higher than the comparative prior-year figure of € 26.6 million. Our investments were concentrated in China, India, the USA and Europe. We maintained our policies for measuring depreciation and amortisation in the year under review.

Net financial position
The KSB Group's net financial position, i.e. the difference between interest-bearing financial assets on the one hand and financial liabilities on the other, improved by € 49.1 million compared with 30 June 2013.

Liquidity
Cash flows from operating activities amounted to € +14.1 million, compared with € +25.1 million for the first six months of the previous year. This decrease is primarily attributable to the lower half-year earnings after taxes.

Our investing activities were almost unchanged, resulting in a cash outflow in the first six months of € –32.0 million (prior-year period: € –35.0 million).

Cash flows from financing activities amounted to € –34.3 million (prior-year period: € –18.0 million), reflecting loan repayments of around € 10 million in the period under review. This compared with borrowing in the first half of 2013 of around € 15 million.

NET ASSETS
Totals assets amounted to € 2,160.9 million as at 30 June 2014, representing an increase of € 9.4 million or 0.4 % over year end 2013.

Changes in non-current assets (€ +24.6 million) are primarily attributable to higher deferred tax assets (€ +21.6 million) arising from the increase in long-term provisions for employee benefits. Property, plant and equipment increased by € 5.1 million.

Inventories totalled € 452.5 million, up from the year end 2013 level of € 423.8 million. This was primarily due to higher inventories of work in progress for orders in hand.

Receivables and other current assets totalled € 648.2 million, slightly up from the year end 2013 level (€ 644.1 million). As a result of the decrease in sales revenue, trade receivables fell by € 38.1 million. By contrast, receivables recognised by PoC rose by € 27.9 million. Other current assets also increased by € 14.2 million, due among other reasons to an increase in recoverable taxes.

The higher financing requirement for inventories and increased non-current assets impacted current financial instruments and cash and cash equivalents, which amounted to € 403.6 million (year-end 2013: € 451.4 million).

SUMMARY OF THE ECONOMIC SITUATION OF THE GROUP
The market situation was difficult, particularly in individual industries such as the energy sector and mining. There were also regional economic weaknesses, particularly in regions affected by crises.

Nevertheless we improved order intake in the Group by 3.2 %. This is due to increased order values in the Pumps business unit (+ 7.7 %). Orders were down on the previous year in the Valves (– 1.8 %) and Service (– 8.2 %) business units.

However, the development of sales revenue suffered from the postponement of current projects and the depreciation of currencies against the euro. This also had a markedly negative effect on our earnings.

The key indicators, i.e. sales revenue and earnings before interest and taxes (EBIT), were considerably down on the figures for the first half of 2013 in the Pumps and Service business units. The Valves business unit also reported a decline in sales revenue, but more than doubled its earnings year on year.

Due to the combination of the decline in business and lower earnings before taxes (EBT), the return on sales of 2.1 % was also below the comparative figure for 2013 (4.5 %). However, we improved our net financial position by around € 49 million, compared with 30 June 2013.

Despite the negative influences, the economic situation of the KSB Group at the end of the first half of 2014 provides a good basis for successfully tackling the next few years, aided by the Group's organisational realignment and the personnel measures initiated.

EMPLOYEES

The headcount for the Group at 30 June 2014 was 16,480, a decrease of 85 from the figure at 30 June 2013 (– 0.5 %). KSB AG (– 59) and KSB Service GmbH Frankenthal (– 81) in particular reduced their workforce in response to changed market conditions. New hirings were limited to exceptional cases throughout the Group. The first-time consolidation of companies resulted in an additional 42 employees.

REPORT ON EXPECTED DEVELOPMENTS

In the 2013 group management report we presented a detailed estimate of how we expect the market and our sales opportunities to develop in the current year. In the light of the development of business in the first half of 2014, we still expect a marked increase in order intake for the full year. We expect significant growth in particular in the Pumps and Valves business units, with orders in the Service business unit remaining at prior-year levels.

For the second half of 2014 we expect sales revenue to improve sharply on the first six months, although in contrast to our earlier forecast we no longer expect growth for the year as a whole, but a total moderately down on the previous year. It is likely that sales revenue will decline markedly year on year in the Pumps and Service business units, in contrast to a slight rise in the Valves business unit.

The continuing difficult earnings situation in the power plant business, negative currency effects and impending reorganisation and non-recurring costs will have a heavy impact on the Group's consolidated earnings for the year. We accordingly expect a considerable decline on the previous year for the business units' earnings before interest and taxes (EBIT).

Consolidated earnings before taxes will also be lower, probably ranging between € 60 million and € 85 million. Accordingly, the return on sales is also likely to be considerably lower than in the previous year. In our earlier report on expected developments, we expected moderate growth in earnings and return on sales.

We expect a net financial position of between € 170 million and € 190 million, virtually matching our original target of around € 200 million.

FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements. We wish to point out that actual events may differ materially from our expectations of developments if one of the uncertainties described, or other risks and uncertainties, should materialise, or if the assumptions underlying the statements prove to be inaccurate.

OPPORTUNITIES AND RISKS REPORT

In the 2013 Annual Report, we presented in detail the opportunities and risks we see facing our business. These have since undergone no significant reassessment. However, the current geopolitical situation, e.g. in Russia, could continue to affect the order situation.

AUDIT REVIEW

This interim management report – as well as the underlying condensed interim consolidated financial statements – have neither been audited nor reviewed in accordance with section 317 of the *HGB* [German Commercial Code].

PUBLICATION

The half-year financial report is published in the *Bundesanzeiger* [German Federal Gazette], as well as on our web site (www.ksb.com). A print version is also available on request.

BALANCE SHEET

ASSETS

(€ thousands)	Notes	30 June 2014	31 Dec. 2013
Non-current assets			
Intangible assets	1	112,513	111,302
Property, plant and equipment	1	448,006	442,861
Non-current financial assets	1	8,638	10,432
Investments accounted for using the equity method	1	24,980	26,617
Deferred tax assets		61,276	39,633
		655,413	**630,845**
Current assets			
Inventories	2	452,453	423,848
Receivables and other current assets	3	648,197	644,144
Current financial instruments	4	–	–
Cash and cash equivalents	4	403,606	451,438
Assets held for sale	1	1,184	1,185
		1,505,440	**1,520,615**
		2,160,853	**2,151,460**

EQUITY AND LIABILITIES

(€ thousands)	Notes	30 June 2014	31 Dec. 2013
Equity	5		
Subscribed capital		44,772	44,772
Capital reserve		66,663	66,663
Revenue reserves		586,958	618,819
Equity attributable to shareholders of KSB AG		698,393	730,254
Non-controlling interest		118,597	114,240
		816,990	**844,494**
Non-current liabilities			
Deferred tax liabilities		16,154	15,499
Provisions for employee benefits	6	457,357	412,870
Other provisions	6	15,543	15,402
Other liabilities	7	196,062	204,982
		685,116	**648,753**
Current liabilities			
Provisions for employee benefits	6	96,375	109,285
Provisions for taxes	6	8,475	4,799
Other provisions	6	60,545	65,211
Tax liabilities	7	26,319	23,645
Other liabilities	7	467,033	455,273
		658,747	**658,213**
		2,160,853	**2,151,460**

STATEMENT OF COMPREHENSIVE INCOME

INCOME STATEMENT

(€ thousands)	Notes	Six months ended 30 June 2014	Six months ended 30 June 2013
Sales revenue	8	**1,011,638**	**1,090,116**
Changes in inventories		19,241	21,300
Work performed and capitalised		669	773
Total output of operations		**1,031,548**	**1,112,189**
Other income	9	12,043	13,048
Cost of materials	10	– 418,644	– 455,829
Staff costs	11	– 389,417	– 394,163
Depreciation and amortisation expense		– 29,274	– 30,159
Other expenses	12	– 172,670	– 183,241
Other taxes		– 6,453	– 6,097
		27,133	**55,748**
Financial income	13	3,217	4,330
Financial expense	13	– 10,969	– 11,241
Income / expense from investments accounted for using the equity method	13	1,320	–
		– 6,432	**– 6,911**
Earnings before income taxes		**20,701**	**48,837**
Taxes on income	14	– 5,791	– 15,422
Earnings after income taxes		**14,910**	**33,415**
Attributable to: Non-controlling interest	15	3,811	6,858
Attributable to: Shareholders of KSB AG		**11,099**	**26,557**
Diluted and basic earnings per ordinary share (€)	17	6,21	15,04
Diluted and basic earnings per preference share (€)	17	6,47	15,30

STATEMENT OF INCOME AND EXPENSE RECOGNISED IN EQUITY

(€ thousands)	Notes	Six months ended 30 June 2014	Six months ended 30 June 2013
Earnings after income taxes		**14,910**	**33,415**
Expense and income recognised directly in equity and not reclassified to profit or loss in subsequent periods		**– 25,331**	**7,260**
Actuarial gains / losses under IAS 19	6	– 36,187	10,288
Taxes on income		10,856	– 3,028
Expense and income recognised directly in equity and reclassified to profit or loss in subsequent periods		**7,418**	**– 18,713**
Currency translation differences		9,970	– 18,521
Measurement of financial instruments		– 3,736	– 310
Taxes on income		1,184	118
Other comprehensive income		**– 17,913**	**– 11,453**
Total comprehensive income		**– 3,003**	**21,962**
Attributable to: Non-controlling interest		5,841	3,965
Attributable to: Shareholders of KSB AG		**– 8,844**	**17,997**

STATEMENT OF CHANGES IN EQUITY

(€ thousands)	Subscribed capital of KSB AG	Capital reserve of KSB AG
1 Jan. 2013	44,772	66,663
Change in accounting policies in accordance with IAS 19	–	–
1 Jan. 2013 (adjusted)	44,772	66,663
Other comprehensive income	–	–
Earnings after income taxes	–	–
Total comprehensive income	**–**	**–**
Dividends paid	–	–
Capital increases / decreases (Notes No. 5)	–	–
Change in consolidated Group / Step acquisitions	–	–
Other	–	–
30 June 2013 (adjusted)	**44,772**	**66,663**

(€ thousands)	Subscribed capital of KSB AG	Capital reserve of KSB AG
1 Jan. 2014	44,772	66,663
Other comprehensive income	–	–
Earnings after income taxes	–	–
Total comprehensive income	**–**	**–**
Dividends paid	–	–
Capital increases / decreases (Notes No. 5)	–	–
Change in consolidated Group / Step acquisitions	–	–
Other	–	–
30 June 2014	**44,772**	**66,663**

Accumulated currency translation differences (€ thousands)	Equity attributable to shareholders of KSB AG	Non-controlling interest	Total equity
Balance at 1 Jan. 2013	– 35,750	– 20,784	**– 56,534**
Change in 2013	– 15,770	– 2,751	**– 18,521**
Balance at 30 June 2013	– 51,520	– 23,535	**– 75,055**
Balance at 1 Jan. 2014	– 79,197	– 30,789	**– 109,986**
Change in 2014	7,793	2,177	**9,970**
Balance at 30 June 2014	**– 71,404**	**– 28,612**	**– 100,016**

Revenue reserves						
Other revenue reserves	Currency translation differences	Measurement of financial instruments	Actuarial gains / losses under IAS 19	Equity attributable to shareholders of KSB AG	Non-controlling interest	Total equity
720,801	– 35,750	676	–	797,162	125,807	922,969
–	–	–	– 88,893	– 88,893	– 1,570	– 90,463
720,801	– 35,750	676	– 88,893	708,269	124,237	832,506
–	– 15,653	– 33	7,126	– 8,560	– 2,893	– 11,453
26,557	–	–	–	26,557	6,858	33,415
26,557	**– 15,653**	**– 33**	**7,126**	**17,997**	**3,965**	**21,962**
– 21,240	–	–	–	– 21,240	– 12,042	– 33,282
–	–	–	–	–	–	–
6,300	– 117	–	– 119	6,064	– 2,499	3,565
– 6	–	–	–	– 6	81	75
732,412	**– 51,520**	**643**	**– 81,886**	**711,084**	**113,742**	**824,826**

Revenue reserves						
Other revenue reserves	Currency translation differences	Measurement of financial instruments	Actuarial gains / losses under IAS 19	Equity attributable to shareholders of KSB AG	Non-controlling interest	Total equity
771,825	– 79,197	3,461	– 77,270	730,254	114,240	844,494
–	7,793	– 2,405	– 25,331	– 19,943	2,030	– 17,913
11,099	–	–	–	11,099	3,811	14,910
11,099	**7,793**	**– 2,405**	**– 25,331**	**– 8,844**	**5,841**	**– 3,003**
– 21,240	–	–	–	– 21,240	– 1,777	– 23,017
–	–	–	–	–	–	–
– 1,249	–	–	–	– 1,249	–	– 1,249
– 528	–	–	–	– 528	293	– 235
759,907	**– 71,404**	**1,056**	**– 102,601**	**698,393**	**118,597**	**816,990**

STATEMENT OF CASH FLOWS

(€ thousands)	Six months ended 30 June 2014	Six months ended 30 June 2013
Cash flow	**49,291**	**64,758**
Other changes in cash flows from operating activities	– 35,215	– 39,622
Cash flows from operating activities	**14,076**	**25,136**
Cash flows from investing activities	**– 32,016**	**– 34,949**
Cash flows from financing activities	**– 34,281**	**– 18,034**
Net change in cash and cash equivalents	– 52,221	– 27,847
Effects of exchange rate changes on cash and cash equivalents	3,586	– 1,301
Effects of changes in consolidated Group	803	3,097
Cash and cash equivalents at beginning of period	451,438	401,031
Cash and cash equivalents at end of period	**403,606**	**374,980**

NOTES

I. GENERAL

The accompanying unaudited condensed interim consolidated financial statements of KSB Aktiengesellschaft, Frankenthal/Pfalz, Germany (KSB AG), have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU). They have been prepared in euros (€) on a going concern basis. Amounts in this report are generally presented in thousands of euros (€ thousands) using standard commercial rounding rules.

II. CHANGE IN ACCOUNTING PRINCIPLES

The following new or revised Standards issued by the International Accounting Standards Board (IASB) were required to be applied for the first time in financial year 2014.

IFRS 10 Consolidated Financial Statements replaces the guidelines contained in **IAS 27 Consolidated and Separate Financial Statements** on control and consolidation, and changes the definition of "control" to the extent that the same criteria are applied to all companies for the purposes of determining whether a control relationship exists or not. Control requires exposure to variable returns and the ability to affect these returns through power over an investee.

IFRS 11 Joint Arrangements affects companies involved in joint ventures or joint operations and supersedes **IAS 31 Interests in Joint Ventures**. The previously permitted pro rata consolidation method may no longer be used for joint ventures, which must now exclusively be accounted for in the consolidated financial statements using the equity method.

IFRS 12 Disclosure of Interests in Other Entities pools all of the required disclosures in the Notes in relation to subsidiaries, joint arrangements and associate companies, and also non-consolidated structured companies, in one single standard. The disclosure requirements previously set out in IAS 27, 28 and 31 have thus been replaced and additional disclosure requirements added.

The addition to **IAS 32 Financial Instruments: Presentation** clarifies the conditions for the offsetting of financial assets and liabilities in the balance sheet.

The amendment to **IAS 36 Impairment of Assets** is to eliminate any undesired consequences with regard to disclosure obligations resulting from the introduction of IFRS 13.

The amendment to **IAS 39 Financial Instruments: Recognition and Measurement** means that, subject to certain conditions, hedge accounting may be continued in cases where derivatives designated as hedging instruments have been transferred to a central clearing agent to comply with statutory provisions or regulatory rules.

The above changes to accounting principles did not (materially) affect the presentation of a true and fair view of net assets, financial position and results of operations or the disclosures in the Notes to the present condensed interim financial statements.

III. BASIS OF CONSOLIDATION

In addition to KSB AG, ten German and 86 foreign companies were fully consolidated in the interim consolidated financial statements. We used the equity method to consolidate seven associates.

The following affiliates which were acquired or founded in prior years were fully consolidated in the consolidated financial statements for the first time as of 1 January 2014:

- KSB Service Suciba, S.L.U., Loiu-Bizkaia (Spain)
- KSB POMPES ET ROBINETTERIES S.à.r.l. d'Associé unique, Casablanca (Morocco)

The changes in the consolidated Group described above contributed 0.3 % to half-year consolidated earnings and had the following impact on the interim consolidated financial statements:

(€ thousands)	2014
Non-current assets	-2,002
Current assets	1,751
Assets	**-251**
Equity	-1,249
Non-current liabilities	44
Current liabilities	954
Liabilities	**-251**

There were no changes to consolidation methods or currency translation methods.

IV. ACCOUNTING POLICIES

The accounting policies have generally not changed as against the last consolidated financial statements except for the changes described above in the "Change in accounting principles" section. They apply to all companies included in the interim consolidated financial statements.

V. BALANCE SHEET DISCLOSURES

1 Fixed assets

In the first six months of 2014 we invested € 29,437 thousand in property, plant and equipment; in the first half of 2013 the corresponding figure was € 26,635 thousand. At € 27,055 thousand, depreciation and amortisation hardly changed compared with the previous year (€ 27,396 thousand).

As in the first half of 2013, we did not recognise any impairment losses on intangible assets and items of property, plant and equipment in the period under review.

Non-current financial assets declined overall by € 3.4 million, above all due to the first-time consolidations.

2 Inventories

(€ thousands)	30 June 2014	31 Dec. 2013
Raw materials and production supplies	151,926	153,715
Work in progress	168,647	147,009
Finished goods and goods purchased and held for resale	109,284	105,152
Advance payments	22,596	17,972
	452,453	**423,848**

3 Receivables and other current assets

(€ thousands)	30 June 2014	31 Dec. 2013
Trade receivables	434,509	474,717
Receivables from other investments and associates	20,705	18,489
Receivables recognised by PoC	113,802	85,934
Receivables recognised by PoC (excl. advances received from customers PoC)	197,608	172,574
Advances received from customers (PoC)	– 83,806	– 86,640
Other receivables and other current assets	79,181	65,004
	648,197	**644,144**

Receivables from other investments include loans at the usual interest amounting to € 1,882 thousand (previous year: € 1,791 thousand). Impairment losses (write-downs) on receivables from other investments amount to € 3,107 thousand (previous year: € 3,052 thousand) and on receivables from associates, as in the previous year, to € 345 thousand.

4 Current financial instruments, cash and cash equivalents

As in the previous year, there were no current financial instruments.

Cash and cash equivalents are term deposits with short maturities and call deposits, and also current account balances. Part of the term deposits is used in Germany for hedges of credit balances prescribed by law for partial retirement arrangements and long-term working time accounts. They are available to us at any time due to the underlying contractual structure.

5 Equity

There was no change in the share capital of KSB AG as against the previous year. In accordance with the Articles of Association, it totals € 44,771,963.82, and is, as in the previous year, composed of 886,615 ordinary shares and 864,712 preference shares. Each no-par value share represents an equal notional amount of the share capital. All shares are no-par value bearer shares.

Non-controlling interest relates primarily to PAB GmbH, Frankenthal, and the interests it holds, as well as to our companies in India and China. KSB AG holds a 51 % interest in PAB GmbH, while Klein Pumpen GmbH, Frankenthal, holds a 49 % interest.

Details of the changes in equity accounts and non-controlling interest are presented in the Statement of Changes in Equity.

6 Provisions

(€ thousands)	30 June 2014	31 Dec. 2013
Employee benefits	553,732	522,155
Pensions and similar obligations	443,584	398,056
Other employee benefits	110,148	124,099
Taxes	8,475	4,799
Taxes on income	6,689	3,352
Other taxes	1,786	1,447
Other provisions	76,088	80,613
Warranty obligations and contractual penalties	43,605	43,169
Miscellaneous other provisions	32,483	37,444
	638,295	607,567

More than 95 % of the provisions for pensions result from defined benefit plans of the German Group companies. Provisions for other employee benefits relate primarily to profit-sharing, jubilee payments, compensated absence and partial retirement obligations. Miscellaneous other provisions include, inter alia, provisions for expected losses from uncompleted transactions and onerous contracts, customer bonuses, accrued costs and environmental measures.

7 Liabilities

NON-CURRENT LIABILITIES

(€ thousands)	30 June 2014	31 Dec. 2013
Financial liabilities		
Loan against borrower's note	174,724	174,682
Bank loans and overdrafts	19,852	28,507
Finance lease liabilities	1,192	1,374
Other	294	419
	196,062	204,982
Total non-current liabilities	196,062	204,982

CURRENT LIABILITIES

(€ thousands)	30 June 2014	31 Dec. 2013
Financial liabilities		
Loan against borrower's note	6,000	6,000
Bank loans and overdrafts	52,552	54,325
Finance lease liabilities	445	533
Liabilities to other investments and associates	682	903
Other	12	12
	59,691	**61,773**
Trade payables		
Trade payables to third parties	188,387	198,693
Trade payables to other investments and associates	2,420	6,073
	190,807	**204,766**
Tax liabilities	**26,319**	**23,645**
Other liabilities		
Advances received from customers	84,337	69,625
Advances received from customers (PoC)	58,565	42,321
Social security and liabilities to employees	26,094	27,074
Miscellaneous other liabilities	47,539	49,714
	216,535	**188,734**
Total current liabilities	**493,352**	**478,918**

TOTAL NON-CURRENT AND CURRENT LIABILITIES

(€ thousands)	30 June 2014	31 Dec. 2013
Total liabilities	**689,414**	**683,900**

VI. INCOME STATEMENT DISCLOSURES

8 Sales revenue

The KSB Group's consolidated sales revenue was € 1,011,638 thousand (previous year: € 1,090,116 thousand). The companies that were fully consolidated for the first time accounted for € 1,598 thousand.

The impact of the percentage of completion method pursuant to IAS 11 and the breakdown of sales revenue by product group (pumps, valves and service) is presented in the segment reporting.

9 Other income

(€ thousands)	Six months ended 30 June 2014	Six months ended 30 June 2013
Gains from asset disposals and reversals of impairment losses (write-ups)	2,063	418
Income from current assets (basically measurement effects concerning receivables)	1,807	1,170
Currency translation gains	720	912
Income from the reversal of provisions	1,354	2,383
Miscellaneous other income	6,099	8,165
	12,043	**13,048**

The changes in the consolidated Group had no material impact on other income.

10 Cost of materials

(€ thousands)	Six months ended 30 June 2014	Six months ended 30 June 2013
Cost of raw materials and production supplies consumed and of goods purchased and held for resale	388,577	424,506
Cost of purchased services	30,067	31,323
	418,644	**455,829**

The changes in the consolidated Group had no material impact on the cost of materials.

11 Staff costs

(€ thousands)	Six months ended 30 June 2014	Six months ended 30 June 2013
Wages and salaries	314,030	314,448
Social security contributions and employee assistance costs	61,111	66,787
Pension costs	14,276	12,928
	389,417	**394,163**

Pension costs are reduced by the interest component of provisions for pensions and similar obligations, which is reported as an interest cost in financial income / expense.

The companies that were fully consolidated for the first time accounted for € 613 thousand.

We employed an average of 16,532 people in the reporting period (previous year: 16,578). The changes in the consolidated Group in the year under review led to the addition of 41 people.

12 Other expenses

(€ thousands)	Six months ended 30 June 2014	Six months ended 30 June 2013
Losses from asset disposals	291	403
Losses from current assets (basically measurement effects concerning receivables)	3,892	2,730
Currency translation losses	2,135	2,277
Other staff costs	11,898	11,573
Repairs, maintenance, third-party services	39,379	41,520
Selling expenses	36,586	43,287
Administrative expenses	43,269	46,976
Rents and leases	13,776	13,680
Miscellaneous other expenses	21,444	20,795
	172,670	**183,241**

Miscellaneous other expenses relate primarily to warranties and contractual penalties.

The changes in the consolidated Group accounted for € 269 thousand.

13 Financial income / expense

(€ thousands)	Six months ended 30 June 2014	Six months ended 30 June 2013
Financial income	**3,217**	**4,330**
Income from equity investments	–	1,512
thereof from other investments	(–)	(1,257)
Interest and similar income	3,203	2,781
thereof from other investments	(26)	(33)
thereof from associates	(–)	(–)
Write-ups of financial assets	–	–
Income from the remeasurement of financial instruments	–	–
Other financial income	14	37
Financial expense	**– 10,969**	**– 11,241**
Interest and similar expenses	– 10,924	– 11,206
thereof to other investments	(–)	(–)
Write-downs of financial assets	–	–
Expenses from the remeasurement of financial instruments	– 2	–
Other financial expenses	– 43	– 35
Income / expense from investments accounted for using the equity method	1,320	–
Financial income / expense	**– 6,432**	**– 6,911**

Interest and similar expenses include the net interest cost in accordance with IAS 19 amounting to € 6,789 thousand (previous year: € 6,624 thousand). The first-time inclusion of fully consolidated companies had no material impact on the financial income / expense.

14 Taxes on income

All income-related taxes of the consolidated companies and deferred taxes are reported in this item. Other taxes are reported in the income statement after other expenses.

(€ thousands)	Six months ended 30 June 2014	Six months ended 30 June 2013
Effective taxes	14,501	17,900
Deferred taxes	– 8,710	– 2,478
	5,791	**15,422**

The first-time inclusion of fully consolidated companies had no material impact on the taxes on income.

15 Earnings after income taxes – Non-controlling interest

The non-controlling interest in net profit amounts to € 5,187 thousand (previous year: € 7,358 thousand), and the non-controlling interest in net loss amounts to € 1,376 thousand (previous year: € 500 thousand). These relate primarily to PAB GmbH, Frankenthal, Germany, and the interests it holds.

The first-time inclusion of fully consolidated companies did not have any impact on earnings after taxes attributable to non-controlling interest.

16 Research and development costs

Research and development costs in the period under review amounted to € 25,031 thousand (previous year: € 23,992 thousand).

The first-time inclusion of fully consolidated companies did not have any impact on research and development costs.

17 Earnings per share

		Six months ended 30 June 2014	Six months ended 30 June 2013
Diluted and basic earnings per ordinary share	€	6.21	15.04
Diluted and basic earnings per preference share	€	6.47	15.30

An additional dividend attributable to preference shareholders of € 0.26 (previous year: € 0.26) per share is assumed.

The first-time inclusion of fully consolidated companies had no material impact on earnings per share.

VII. FINANCIAL RISKS

We are exposed to certain financial risks as a consequence of our business activities. These risks can be classified into three areas:

On the one hand, we are exposed to **credit risk**. We define credit risk as potential default or delays in the receipt of contractually agreed payments. We are also exposed to **liquidity risk**, which is the risk that an entity will be unable to meet its financial obligations, or will be unable to meet them in full. Finally, we are exposed to **market price risk**. The risk of exchange rate or interest rate changes may adversely affect the economic position of the Group. Risks from fluctuations in securities prices are not material for us.

We limit all of these risks through an appropriate risk management system, and define how these risks are addressed through guidelines and work instructions. In addition, we monitor the current risk characteristics continuously and regularly provide the information obtained in this way to the Board of Management and the Supervisory Board in the form of standardised reports and individual analyses.

VIII. SEGMENT REPORTING

Segment reporting corresponds to our internal organisational and management structure, as well as the reporting lines to the Board of Management and the Supervisory Board. In our matrix organisation, management decisions are primarily taken on the basis of the key performance indicators – order intake, external sales revenue and earnings before interest and taxes (EBIT) – determined for the Pumps, Valves and Service business units. Reporting the relevant assets, number of employees and inter-segment sales revenue for these business units is not part of our internal reporting. The managers in charge of the business units, which are geared to product groups, have profit and loss responsibility. They identify business opportunities across markets and industries and assess our options based on current and future market requirements. They also proactively encourage the development of new products and improvements to the available range of products. In this context, they work closely with our Sales organisation and Operations.

The **Pumps** product group covers single- and multistage pumps, submersible pumps and associated control and drive systems. Applications include process engineering, building services, water and waste water transport, energy conversion and solids transport.

The **Valves** product group covers butterfly, globe, gate, control, diaphragm and ball valves, as well as associated actuators and control systems. Applications primarily include process engineering, building services, energy conversion and solids transport.

The **Service** product group covers the installation, commissioning, start-up, inspection, servicing, maintenance and repair of pumps, related systems and valves; as well as modular service concepts and system analyses for complete systems.

The amounts disclosed for the individual segments have been established in compliance with the accounting policies of the underlying interim consolidated financial statements.

Transfer prices for intercompany sales are determined on an arm’s length basis.

There were no discontinued operations in the period under review, as in the comparative period of the previous year.

The **order intake** of the business units by segment presents order intake generated with third parties and non-consolidated Group companies.

The **external sales revenue** of the business units by segment presents sales revenue generated with third parties and non-consolidated Group companies. The effects from measuring construction contracts in accordance with IAS 11 are presented separately as reconciliation effects.

The segment results show **earnings before interest and taxes (EBIT)**, including non-controlling interests. The effects from measuring construction contracts in accordance with IAS 11 are presented separately as reconciliation effects.

(€ thousands / Six months ended 30 June)	Order intake		External sales revenue		EBIT	
	2014	2013	2014	2013	2014	2013
Business unit Pumps	765,912	711,152	644,460	725,480	12,316	43,941
Business unit Valves	189,469	192,987	178,853	186,956	4,770	1,444
Business unit Service	176,493	192,222	164,433	185,556	4,822	12,264
Reconciliation	–	–	23,892	−7,876	6,514	−386
Total	**1,131,874**	**1,096,361**	**1,011,638**	**1,090,116**	**28,422**	**57,263**

The EBIT of the Pumps business unit includes depreciation and amortisation of € 19.2 million (previous year: € 17.6 million), the EBIT of the Valves business unit includes depreciation and amortisation of € 5.1 million (previous year: € 5.3 million) and the EBIT of the Service business unit includes depreciation and amortisation of € 4.9 million (previous year: € 7.3 million).

€ 294,960 thousand (previous year: € 306,662 thousand) of the sales revenue presented was generated by the companies based in Germany and € 716,678 thousand (previous year: € 783,454 thousand) by the other Group companies.

At the reporting date, the total non-current assets of the KSB Group amounted to € 462,279 thousand (year-end figure in 2013: € 457,851 thousand), with € 179,719 thousand (year-end figure in 2013: € 181,386 thousand) being attributable to the companies based in Germany and € 282,560 thousand (year-end figure in 2013: € 276,465 thousand) being attributable to the other Group companies. The non-current assets include intangible assets and property, plant and equipment. Goodwill, non-current financial instruments and deferred tax assets are not included.

IX. OTHER DISCLOSURES

Contingent liabilities (contingencies and commitments)
Contingent liabilities and other financial obligations and commitments fall within the scope of what is required to carry on normal business activities. They have not changed materially compared with those at 31 December 2013.

Related party disclosures
Pursuant to section 21(1) of the *WpHG* [*Wertpapierhandelsgesetz* – German Securities Trade Act], KSB Stiftung [KSB Foundation], Stuttgart, notified us on 21 May 2008 that its voting interest in KSB AG, Frankenthal/Pfalz, exceeded the 75.00 % threshold on 5 May 2008 and amounted to 80.24 % (711,453 voting shares) on this date. 0.54 % of the voting rights (4,782 voting shares) were held directly by KSB Stiftung, Stuttgart, and 79.70 % (706,671 voting shares) were attributed to KSB Stiftung, Stuttgart, pursuant to section 22(1), sentence 1, No. 1 of the *WpHG*. The voting rights attributed to KSB Stiftung, Stuttgart, were held by Klein Pumpen GmbH, Frankenthal.

A rental and services agreement has been entered into between KSB AG and Klein Pumpen GmbH. This resulted in the recognition of expenses of € 24 thousand (previous year: € 12 thousand) and income of € 7 thousand (previous year: none) at KSB AG in the period under review. Liabilities to Klein Pumpen GmbH as at 30 June 2014 amounted to € 57 thousand (previous year: none).

Auditors
On 14 May 2014, BDO AG Wirtschaftsprüfungsgesellschaft, based in Hamburg with an office in Frankfurt am Main, was appointed as auditors and group auditors for the financial year 2014 by the Annual General Meeting of KSB AG.

This half-year financial report has been neither reviewed nor audited in accordance with section 317 of the *HGB* [German Commercial Code].

Events after the balance sheet date
There were no reportable events after the balance sheet date.

German Corporate Governance Code
The Board of Management and Supervisory Board of KSB AG issued the current statement of compliance with the recommendations of the Government Commission on the German Corporate Governance Code in accordance with section 161 of the *AktG* [*Aktiengesetz* – German Public Companies Act]. The statement of compliance is published on our web site (www.ksb.com) and has thus been made permanently accessible.

APPROPRIATION OF THE 2013 NET RETAINED EARNINGS OF KSB AG

The Annual General Meeting on 14 May 2014 resolved to appropriate the 2013 net retained earnings of € 24,342,969.55 of KSB AG, Frankenthal, containing retained earnings brought forward of € 204,605.10, as follows:

Distribution of a dividend of € 12.00 per ordinary no-par-value share	10,639,380.00 €
and, in accordance with the Articles of Association, € 12.26 per preference no-par-value share	10,601,369.12 €
Appropriation to revenue reserves	3,000,000.00 €
Total	24,240,749.12 €
Carried forward to new account	102,220.43 €
	24,342,969.55 €

The dividend was paid out on 15 May 2014.

RESPONSIBILITY STATEMENT

To the best of our knowledge, and in accordance with the applicable interim reporting principles, the interim consolidated financial statements give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group, and the interim group management report includes a fair review of the development and performance of the business and the position of the Group, together with a description of the principal opportunities and risks associated with the expected development of the Group during the remainder of the financial year.

Frankenthal, 13 August 2014

The Board of Management

SHAREHOLDER INFORMATION

13 NOVEMBER 2014
Interim report
January – September 2014

30 JANUARY 2015
Preliminary report on financial year 2014

30 MARCH 2015
Financial press conference
67227 Frankenthal

31 MARCH 2015
Invitation to Annual General Meeting

29 APRIL 2015
Interim report
January – March 2015

7 MAY 2015
Annual General Meeting
CongressForum Frankenthal
Stephan-Cosacci-Platz 5
67227 Frankenthal

8 MAY 2015
Dividend payment

13 AUGUST 2015
Half-year financial report
January – June 2015

12 NOVEMBER 2015
Interim report
January – September 2015

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THE GLOBAL COMPACT
WE SUPPORT

As a signatory to the United Nations Global Compact, KSB is committed to endorsing the ten principles of the international community in the areas of human rights, labour standards, environmental protection and anti-corruption.

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