Ladies and gentlemen, thank you for standing by and welcome to the Lockheed Martin Second Quarter 2017 Earnings Results Conference Call. For the conference, all the participant lines are in a listen-only mode. There will be an opportunity for your questions. Instructions will be given at that time. [Operator instructions]. As a reminder, today's call is being recorded.

I'll turn the conference now to Mr. Greg Gardner, Vice President of Investor Relations. Please go ahead, sir.

Greg Gardner

Thank you, John, and good morning. I'd like to welcome everyone to our second quarter 2017 earnings conference call. Joining me today on the call are Marillyn Hewson, our Chairman, President and Chief Executive Officer; and Bruce Tanner, our Executive Vice President and Chief Financial Officer.

Statements made in today's call that are not historical fact are considered forward-looking statements and are made pursuant to the safe harbor provisions of federal securities law. Actual results may differ materially from those projected in the forward-looking statements. Please see today's press release and our SEC filings for a description of some of the factors that may cause actual results to differ materially from those in the forward-looking statements. We have posted charts on our website today that we plan to address during the call to supplement our comments. Please access our website at www.lockheedmartin.com and click on the Investor Relations link to view and follow the charts.

With that, I'd like to turn the call over to Marillyn.

Marillyn Hewson

Thanks, Greg. Good morning, everyone, and thank you for joining us on the call today as we review our second quarter results and our increased outlook for 2017. As today's release illustrates, we had strong results this quarter, operationally and financially. Our strong year to date financial performance also enabled us to increase our full year 2017 guidance for sales, operating profit, and earnings per share. These results reflect a high level of execution being achieved across our businesses in providing critical products and services to our customers while returning outstanding value to stockholders. It is particularly noteworthy that our quarterly cash flows exceeded last year's second quarter by nearly $200 million when we adjust for the $125 million of IS&GS cash that was included in the 2016 results.

Our team continues to progress toward our full year objective in growth in sales, EPS, and cash from operations, and I thank our team for their dedication to our mission. Chris will cover the financial results in detail a little later. However, I want to touch on two events which occurred after our accounting quarter closed that point to the strength of our portfolio and the significant growth opportunities they provide. First, in our Rotary and Mission Systems business area, our Sikorsky line of business secured a $3.8 billion, five year contract for 257 Black Hawk helicopters to be delivered to the US Army, as well as to the Saudi Arabian National Guard. This award marks Sikorsky's ninth multiple year contract with the US government and includes options for an additional 103 aircraft, bringing the potential value to over $5 billion. We are honored to have the opportunity to continue providing rotary aircraft in support of the important missions of the US Army and our international customer.

Second, our Aeronautics business area received an F-35 award on LRIP 11, which includes funding for 74 US jets and totaled nearly $5.6 billion. This brings the total quantity of US aircraft authorized for LRIP 11 to 91 planes, a growth of 36 fighter jets from LRIP 10 US government order, and represents a 65% increase from the prior lot. We anticipate a separate order - a separate award later this quarter, which will add additional aircraft for our international F-35 partners and foreign military sales customers. The recent US award demonstrates continued evidence of the strong support the F-35 has earned, and we look forward to finalizing these contracts as we progress to full rate production.

Turning briefly to Defense budgets, the FY17 DOD budget appropriations have been enacted and were consistent with the bipartisan budget agreement of 2015, bringing Defense Department base budget funding to approximately $524 billion, as well as overseas contingency operations funding to about $83 billion. We're pleased to see that our programs continue to be well supported, as seen by the legislation increasing F-35 aircraft and Black Hawk helicopter quantities. The higher levels for both the base and OCO budgets, reflect a growing level of bipartisan recognition of rising global security threats and the need for additional budget resources. The additional funding for FY17 will help begin to address some of the acute budget needs to recapitalize our defense assets and respond to the global security environment.

Also, the president released his request for the FY18 DOD budget. This included $574 billion for the base budget, an increase of nearly 10% from the FY17 appropriations and 3% from the prior presidential base budget submission. Additionally, both the House and Senate Armed Services Committees, have released their fiscal year '18 National Defense Authorization Act markups, both of which greatly exceeded the president's request. And the House has since passed their version by a wide margin. While we recognize - while we realize that these proposals exceed the current budget caps, we are encouraged to see the recognition that our defense budgets require increased levels of funding. We are hopeful that bipartisan agreement can be reached to rescind or modify the budget caps and fund our military at the levels needed to address the current set of world threats.

Moving on, I'd like to highlight several operational successes we achieved on our F-35 program, and then briefly comment on the recent historic announcements from the US and Kingdom of Saudi Arabia governments to bolster global security. The program featured two milestones that highlight the growing international nature of the Joint Strike Fighter. The first Japanese assembled F-35A conventional takeoff and landing variant, was unveiled at the Final Assembly and Checkout or FACO facility in Nagoya, Japan. This aircraft marks the first of nearly 40 jets that will be produced for the Japanese Ministry of Defense at this location.

Similarly, the first F-35B variant to be assembled outside the United States, was rolled out in Italy from the Cameri FACO facility. Cameri has already delivered multiple F-35A versions and is slated to produce over 100 aircraft in total. Together, these two events underscore the benefits of the multinational partnerships that have been forged as we work to provide fifth generation capabilities to both US and coalition forces.

Keeping with the F-35 program, we were also proud to spotlight our F-35A at the Paris Air Show last month. The CTOL variant performed its inaugural aerial demonstration, showcasing its aerobatic maneuvering and the jet's raw power to climb and run. I watched, along with the rest of the amazed crowd, at the Le Bourget Airport as the aircraft flawlessly executed 90 degree climbs, remarkable angle of attack displays, and several unique moves that only a fifth generation fighter could accomplish, all of which shine a bright light on the impressive capabilities this unrivaled stealth fighter provides. As the crowd erupted into applause, I could not have been more proud of what our Lockheed Martin team, together with the US government, the JPO organization, international partners, industry teammates, and hundreds of suppliers have been able to accomplish.

Before I conclude, I'd like to take a moment to say a few words about the unprecedented announcements that President Trump and his majesty King Salman of the kingdom of Saudi Arabia, made in Riyadh in May. As part of those announcements, the kingdom expressed its intent to procure more than $28 billion worth of Lockheed Martin products and services, including air and missile defense products such as THAAD batteries and PAC-3 missiles, Multi-Mission Surface Combatant Ships, variants of our Littoral Combat Ship, C-130J aircraft and various other defense related capabilities and solutions. These announcements reflect the strength of the relationship that our corporation has built with the kingdom over the past 50 years. In addition, the request touched each of our four business areas, demonstrating the breadth and depth of our offerings and the growth potential that our portfolio brings.

Finally, I would like to acknowledge our Space Systems team, as they mark the one year anniversary of the Juno spacecraft orbiting the planet Jupiter. Images from the Juno orbiter graced the cover of the May issue of Science Magazine, delivering breathtaking views of the giant planet's polar region. The mission also included measurements of the magnetic and gravitational fields and unique perspectives on the atmospheric and weather environments of Jupiter's surface. Scientists are excited at the initial in depth results being provided, as well as with the potential new discoveries that may be made in the upcoming experiments. We believe our continuous commitment to innovation and our long term partnership with NASA have contributed to these remarkable achievements and we are proud to be a part of this ambitious undertaking.

I'll now turn the call over to Bruce to review our second quarter financial performance in more detail, and then we'll open up the line for your question.

Bruce Tanner

Thanks, Marillyn and good morning everyone. I'll be making remarks based on the web charts that we included with our earnings release today. Let's begin with chart three and an overview of our results. We're pleased with our performance in the quarter. Sales of $12.7 billion were slightly ahead of our expectations and showed solid growth over last year's results. Our operating profit and earnings per share results were also ahead of our expectations, while cash from operations was in line with what we were expecting. We continued our strong cash deployment actions and we increased our full year outlook for sales, operating profit and earnings per share. So we had a very solid second quarter and a nice rebound from some of the performance issues we had in the first quarter.

On chart four we compare our sales and segment operating profit in the second quarter of this year with last year's results. Sales were $1.1 billion higher this quarter compared with the last year, with most of that growth coming from the Aeronautics and Space Systems business areas. Aeronautics growth was driven by higher volume from the F-35 and C-130 programs, and an additional C-5 delivery this quarter compared with last year. Space Systems growth was driven by the inclusion of the atomic weapons establishment sales in the quarter compared with none in the second quarter of last year. Segment operating profit was $55 million higher this quarter compared to last year. This was driven by higher volume and improved performance of the F-35 program and Aeronautics, improved performance across multiple lines of business within RMS, and these were partially offset by lower equity earnings from United Launch Alliance and Space Systems.

Turning to chart five, we'll discuss our earnings per share in the quarter. EPS from continuing operations of $3.23, was about 10% higher than the results from a year ago, reflecting both higher operating earnings and lower share count this year compared with last year.

On chart six we'll compare our cash from operations this quarter versus our results from 2016. We generated more than $1.5 billion of cash in the quarter, over $70 million more than we did in the second quarter of last year. But as Marillyn said in her remarks, that understates our relative performance as last year's results included around $125 million of cash generated by IS&GS, which was not divested until August of last year. On a year to date basis, our $3.2 billion of cash generated, is also about $70 million higher than our results from the first half of 2016, but last year's amount included nearly $300 million of cash generated by IS&GS.

Chart seven shows the cash returns to stockholders in the quarter. Subtracting capital expenditures in the quarter from our cash from operations, our free cash flow was just under $1.3 billion, and we returned slightly more than $1 billion to stockholders, about equally split between share repurchases and dividends. This cash deployment represents 81% of our free cash flow in the quarter.

On chart eight, we want to make you aware of two large awards that took place shortly after the end of the quarter that are not reflected in our reported backlog level. The largest award was for the F-35 LRIP 11 UCA for domestic aircraft that Marillyn mentioned and was worth $5.6 billion. The second award was for the multi-year IX by Black Hawk helicopters and was worth $3.8 billion. Both of these awards occurred within two weeks after the quarter close and their combined values would have pushed our backlog above $100 billion for the quarter had they occurred just a few days earlier.

Chart nine provides our updated outlook for the year. We increased sales by $300 million, with all of that increase coming from the Space Systems business due to the higher volume we're seeing this year. We increased segment operating profit by $35 million, with $20 million of the increase coming from our Aeronautics business and $15 from Space Systems. Aeronautics increase recognizes better than planned performance so far this year, while the Space Systems increase is primarily volume driven. We had an improvement in our unallocated costs worth $25 million, driven mostly by a reduction to a previously established reserve. While these improvements in our - with these improvements in our operating profit, we increased our earnings per share by $0.15. And lastly, we’re maintaining our cash from operations outlook at equal to or greater than $6 billion.

Charts 10 and 11 show our revised outlooks by business area for both sales and segment operating profit. I covered the revisions in the outlook in the prior discussions.

Chart 12 provides a reconciliation of our prior EPS outlook to our current outlook. The $35 million increase in segment operating profit, increases our expected EPS by about $0.10, while the $25 million decrease in unallocated expense, improves the EPS by around $0.05, resulting in a revised outlook for the year of $12.30 to $12.60. This new range is higher than the guidance we provided when we began this year, more than offsetting the setbacks we experienced in the first quarter.

Finally, we have our summary on chart 13. Our quarter results for sales, profit, EPS and cash from operation, were all either in line or ahead of our expectations. That resulted in the increased outlook that we just discussed. We are well positioned to achieve our full year goals and as we look ahead to the third quarter earnings call, we'll provide our initial trend information for 2018. As a reminder, the new revenue recognition rule will be effective for us starting in January and will be incorporated into our trend information.

With that, we're ready for your questions. John?

Question-and-Answer Session

Operator

Thank you. [Operator instructions]. First, we go to the line of Sam Pearlstein with Wells Fargo. Please go ahead.

Sam Pearlstein

Good morning. Bruce, always a lot of focus on the cash flow, and there's been a lot of discussion about the capital spending at various defense contracts. Your CapEx is certainly up over the last few years, and up year-over-year. How should we think about that in future years? And what's going to dictate that? Is this F-35 volume or the contract wins or losses like TX? What’s going to dictate kind of the levels of CapEx we see over the next few years?

Bruce Tanner

Sam, thanks for that question. It’s a good question. As we looked at our long range planning from last year, that covers basically 2017, ’18, and ’19, 2017 is sort of a peak in terms of the capital expenditures for the corporation. And that reflects a number of things, some restructuring that we're doing within our Space Systems business, moving some of the work around within locations, within Space Systems, and it also reflects the last tranche of investments required to get the F-35 sort of fully capitalized. It increased in, I’ll say between 2015 and maybe years prior to going forward because we added Sikorsky into the portfolio, which obviously has higher capital expenditure requirements than did the IS&GS business, which really had practically immaterial capital expenditure requirements. So if you start to sort of think of 2017 as sort being the high point, at least as we look at it today, going forward we would expect that number to slightly decrease going forward and within that slight decrease going forward, there are some requirements for additional new capital for some of the wins, one of which you described in your question, but that's sort of more than offset by the reductions in the other capital expenditures required, including F-35.

Operator

Our next question is from Noah Poponak with Goldman Sachs. Please go ahead.

Noah Poponak

Hey, good morning everyone. Bruce, how should we think about Aeronautics' organic revenue growth in 2018? Just because now you are going to have a pretty tough just growth comparison. You’ll have more F-35 growth, but you had mentioned before other aircraft in the segment being headwinds, not sure if those have moved around. And then if you could just perhaps tie that into - a few quarters ago, you talked about staying in the 3% to 5% total Company growth range, but 2018 maybe being at the low end of that. Just wanted to check back in if that was still sort of the case. Thanks.

Bruce Tanner

Thanks, Noah. So Aero’s organic growth, I think what I said previously or what you said that I said previously in earlier quarters, still is true today. We're still looking - I’ll probably answer your second question first. We're still looking at the total company, about the 3% to 5% growth going forward, and’18 is a little less than that and actually in ’19, as we sit here today, it probably picks back up. And a lot of that is because as - to your first question, in 2018, we're actually seeing a drop off because we have the end of the F-16 production line, at least based on current orders at the end of our - close to the end of 2017. We have no new production F-16s planned for 2018 as we sit here today, and that's not in the numbers that we've talked about previously. We also have the end of the C-5 program in the early part of 2018, and so those two events are kind of bringing down Aeronautics organic growth. You're still seeing tremendous growth potential in both the production and sustainment programs for Aeronautics for the F-35 program, but the other two are slightly, as I said, dissipating some of that growth. And that's one of the reasons why in 2019 we kind of bounce back as we're operating off of a lower compare, if you will, in 2018.

Operator

Our next question is from Howard Rubel with Jefferies. Please go ahead.

Howard Rubel

Thank you very much. I want to change a little bit from operations, talk strategy for a moment, and there's two things related. One, Marillyn, you've started to make some investments outside of your core that look like they are complementary, and maybe you could address that and talk about how significant a commitment it could be. And then related to that is, from a longer-term point of view, you have to think about people and what are going on there, and how do you think about succession planning?

Marillyn Hewson

Excellent questions, Howard. Things that I - both of which I have spent a lot of time on, on a regular basis. So thank you for the question. From the strategy standpoint, our focus is on growth. We've been very clear about that. We think we've got a lot of opportunity to continue to grow. We see our international growth increasing from what today is about 20 - in 2016 was about 27% of our sales, 30% and we'll continue to see that growth. The demand around the world is high for not only F-35, but missile defense. One of our F-16 C-130s, other defensive systems that we have, as well as our opportunities in space based situational awareness, et cetera. So that growth, we have been - in terms of your comment about outside our core, the complementary, I would say that our commercial satellites, our commercial helicopters, those that we're doing with the LM-100J, which is the commercial version of the C-130, those are absolutely areas to move in commercial but very closely aligned. And then of course the hybrid airship is another opportunity for us. So those all are in line with our core competences and our capabilities, but moving into similar - more into the commercial space and aligning with that.

Long term, we're always focused on our talent management, our talent development. It is an ongoing part of our business. And in terms of succession planning, as you look at the leadership team that we have at

Lockheed Martin, very seasoned, very strong, talented team that is - that I'm really proud to be a part of the team and working collectively with them on how we’re executing our strategy for the corporation. But at all times we’re looking at building that pipeline of talent into the business. And yes, we also look at that talent from the standpoint of its diversity. And so I'm proud to say that 21% of our leaders are women and we continue to bring more talent in from that regard. So succession planning is something that we continue to look at as a company and it's an ongoing effort for us. Thanks for the question.

Operator

And next we go to Rob Spingarn with Credit Suisse. Please go ahead.

Rob Spingarn

Good morning. I wanted to ask, as you go into next year, and we think about - going back to the cash flow, Sam asked about the CapEx. And you talked I think at the tail end of last quarter, about trying to - ex-pension contribution, perhaps cash flow could be - operating cash flow could be flattish with this year. Bruce, does that still work with the multi-year on the Black Hawk and the quantity adjustments that are happening there? And any other new incremental information that we have since last time?

Bruce Tanner

I think the answer is no. it doesn't change, Rob as far as our thinking is concerned relative to the way you've described 2018. Sans pension contribution, I would expect operating cash flow for the corporation to look pretty similar to this year. And again we talked about, after those pension contributions both in 2018 and 2019, but if you add the cash from those years along with 2017, we expect to be in excess of $15 billion. We're off to a great start obviously this year in 2017 and we’ll give you more insight into what we're looking for ’18 and maybe a little beyond as we talk to you on the next quarter call.

Operator

Our next question is from Ron Epstein with Banc of America Merrill Lynch. Please go ahead.

Ron Epstein

Good morning guys. I just want to maybe talk about some business opportunities, the first of which would be the TX and JSTARS. How's that going and when would you expect a decision made on those?

Marillyn Hewson

Sure. I'll take those. We're looking at where the Air Force is and TX and JSTARS, they're looking at - they've set an award in the fourth quarter of this year. Obviously we never know until they actually do it, and so we couldn't say, but that's what they've outlined is the fourth quarter of 2017 for JSTARS and TX. And then we see some other near term awards that we're hoping to see in September, October timeframe, ones like the Special Operations Forces Global Logistics Support Services that we're unencumbered on that today and us being - it's in competition and we hope to see that award. It's got total program value with options of up to $8 billion. Our Ground Based Strategic Defense is another one that we would look to have to see an award coming here in the fourth quarter. And we're hoping as we look at the Saudi operations, the opportunity that we have there that potentially we could see a fat award sometime late in the year, early next year.

And then another would be LRSO, the Long-Range Standoff Missile. That is also looking at September timeframe. And let's see. Another would be, the Saudis are looking at getting the search and rescue and S70i helicopter award that we expect in September timeframe as well. So several awards in the near term. I think I rattled off six or seven of them just there. And so we're excited. And Bruce, you have some other thoughts?

Bruce Tanner

Yes. Just maybe one to address the question of the star - the start of your question, Ron. You should think of most of these as we've already submitted the proposals. So you sort of ask, what's the status? Well, the status is I think we're all sort of waiting and for the most part, the government is evaluating ours along with everyone else's proposal, and we sit anxiously waiting to see the results of that. but there's not much we can do at this point as I said because almost every one of the ones that Marillyn - if not all of them, that Marillyn just rattled off for - we've already submitted the proposals for those.

Operator

Our next question is from Doug Harned with Bernstein. Please go ahead.

Finbar Sheehy

Hi. It's Finbar Sheehy for Doug. In your press release, you talked about higher sustainment activities in the quarter for the F-35. Can you talk to us about how big those are now, relative to total F-35 revenues and how you expect that's going to evolve over the next few years? Maybe how big a percentage of F-35 revenues will sustainment be, say, by the end of the decade? And how do margins on sustainment compare to the incremental margins you are getting now on new aircraft?

Bruce Tanner

I'll trying that, Finbar. So sustainment is growing fairly rapidly. I mean I want to say it's not quite growing this year at the same pace as is production, but it's growing dramatically over last year's numbers. I mean you should think of this as in the sort of high teens sorts of numbers. So it's growing incrementally and it'll continue to do that for a number of years as we set up more and more bases, both around the United States, but as well internationally as international customer start letting down the aircraft in their home location. So that growth is going to continue. I don't have the exact split, but I want to say if you look at sustainment out of the total F-35 production, I want to say it's probably 20%, 25% as large as the production volume on an annual basis, something like that. And it stays at those sorts of levels for the next few years. So as production grows over the next couple of years to its peak when we hit full rate production, I would expect that the sustainment will sort of follow suit there.

And then your last question, Finbar, was relative to the margins and how we do on sustainment contracts. And I'll tell you, we do about the same on the F-35 sustainment as we do on production. That might change somewhat in the future going forward, but at least historically and where we sit today, they're pretty comfortable without a whole lot of difference between them.

Operator

Next we go to Seth Seifman with JPMorgan. Please go ahead.

Seth Seifman

Thanks very much and good morning. I wanted to ask about the SAR that came out last week and the change in peak quantity of the Air Force buy in the out years. It came down from 80 to 60, but we're talking about numbers that are pretty far out there in 2022, 2023 time frame. So I'm wondering how you are looking at that, what implications you think it might have, whether it's a change that you expect to stick around.

Marillyn Hewson

I'll take that, Seth. Thanks for the question. I would just say first off, we haven't really seen the SAR. I mean we know that it's been submitted to Congress. We know there's been top level readout from the JPO, but the fact sheet that came out on it. And I think in that, the Joint Program Office highlighted the fact that the reason that the numbers were changing were predominantly due to a change in the procurement profile of the Air Force jets, which is the largest volume buyer for the Air Force. And - but frankly, we just - I know that in my discussions with the Air Force, there's a desire to buy as many as they can, as quickly as they can. So I haven't got an official position from them that they've reduce their procurement profile. That just happens to be what's in that select acquisition report that came out going. I mean certainly lots of opportunity to change the quantities as you can see just with what's in the budget deliberations right now, the adds that are coming forward on the F-35 for the various services. We think it's still in - we'll still see potentially some upside on it. So that would be my take. Bruce, anything you want to add?

Bruce Tanner

Another thing I might offer just for a little perspective. I think you had it right, Seth in that the planned peak volumes for the USAF are sort of far out there right now. Just to give you some perspective on that, we're still in discussions with the Joint Program Office relative to a potential block buy. And the numbers that have been thrown out for that block buy, and this is just again to put some perspective over three LRIPs, is about 400 and - between 440 and think of it as five - 450 or so aircraft over that three year LRIP period. So nearly 150 aircraft per year and that's what we're talking about for LRIPs 12, 13 and 14. So these are literally right around the corner. That's 150 aircraft, with the USAF buying 48 aircraft in each of those three fiscal years. So the cut to 80, to 60, we're not even approaching the 60 yet, and we're building aircraft of quantities of 150 per fiscal year.

So as Marillyn said, a lot of opportunities to change quantities between now and then. And it will be interesting, once we do see the full SAR report, how much of that was sort of budgetarily really driven, with the potential to change that budget that much that further - that far out, excuse me, versus I'll say a quantity difference. And if I read the fact sheet right actually from the JPO, I think the actual total quantity of US government buys for F-35s went up coincidentally enough by about 13 aircraft for additional Marine Corps buys. So pushing up to the right, but again as Marillyn said, lots of opportunity to change those values between now and then.

Operator

Our next question is from George Shapiro with Shapiro Research. Please go ahead.

George Shapiro

Good morning. Can you hear me?

Marillyn Hewson

Barely, George. Try again.

George Shapiro - Shapiro Research

On the F-35, the incremental margin was 17%. So did you increase the margin on the LRIP 9 or 10, or both? And then also the deliveries were flat with last year, and down from Q1. So I would think that we'd be starting to see increases here, given the deliveries are going to be higher. So what's happening there? Thanks.

Bruce Tanner

Yes. George, I'll try those. So incremental margins, I didn't do the calculation that you just cited, but you're probably right. Your math is always good, George. And we did have a couple of pick-ups. I think we actually - you asked which specific LRIP we had some risk retirements or step ups, and we actually had, I want to say three separate LRIPs. And you should think of these as somewhat older LRIP contracts or LRIP numbers. I believe two of the three were five - LRIPs five and seven. So this is sort of reflecting the fact that we're closing out or getting ready to sort of close out some of those lots. The ones you talked about, the more current ones, Lot 9 and so forth and Lot 10, we're getting good performance on those, but that's probably step ups that we look forward to in the coming years as - coming quarters, as opposed to this quarter here.

And then as far as deliveries, George, now the way I look at that, I think there's - I think we're planning 66 aircraft to be delivered for the year. And what may not be clear in that number is there's only - the biggest lion's share of that, 61 of those are being delivered out of Fort Worth. The other five are going to be delivered out of the international locations that Marillyn talked, the FACO in Nagoya, Japan and the other FACO in Italy. So none of those five aircraft have yet to deliver, although they've rolled out as Marillyn said. So all those are out in front of us. And as you look at where we ended the first half of the year, we'd actually delivered 29 aircraft. That number is a little deceptive because we closed the quarter actually on June 25 as opposed to the end of the month and we actually had some deliveries between then and the end of the month. As we sit here today, George, I want to say we've delivered 34 aircraft so far and I think we're on track to deliver 36 by the end of this month. So we're actually progressing essentially right on track on the domestic deliveries. And we do expect those five international deliveries to all take place in the second half. So short set, I think we're tracking to our expectations relative to 66 aircraft for the year.

Operator

Our next questions from Pete Skibitski with Drexel Hamilton. Please go ahead.

Pete Skibitski

Good morning guys. I had a further F-35 and Aeronautics margin question. Just because, Bruce, it seems like the F-35 has been kind of less of a headwind maybe than you expected going into this year. And I know some of it's on better performance at the international facilities and whatnot. But as you look out into 2018, it will be a bigger part of the mix, F-35 and Aeronautics. Do you have any confidence probably yet to say that this year is kind of the trough for Aeronautics margin, and we'll start to expand as we go out on higher F-35? Or is there still some uncertainty in some of the latest LRIP lots?

Bruce Tanner

Just to be clear, Pete, you’re talking about a trough for Aeronautics or a trough for F-35? You were talking about Aeronautics I presume, right?

Pete Skibitski - Drexel Hamilton

Correct. Correct.

Bruce Tanner

You know what, I'm not sure I want to call that in this quarter, Pete. I’ll feel a whole lot better. We do our planning between now and the third quarter. And when we give you the trend information in 2018, I will surely address that then. But I don't think your question is that far off the mark. If the answer is not yes, that's probably where we'd expect the trough, the answer is it’s probably pretty close to that, maybe ’18 but we'll take a look at that when we give you the trend information in October.

Pete Skibitski - Drexel Hamilton

Okay, fair enough. Thank you.

Bruce Tanner

Yes, and I should say, in any event we would still expect there - even if it was a trough, I don't see it dropping below 10%. The only question is we've had some, to your point, some pick-ups earlier this year is, can we match that next year going forward? But again I’ll give you a lot more insight in the October call. Thanks.

Operator

Next we go to David Strauss with UBS. Please go ahead.

David Strauss

Thanks. Good morning. Thanks for taking my question. Bruce, I guess first a clarification. The 3% to 5% revenue growth, and talking about maybe being at the lower end of that in 2018, does that include the change in revenue recognition? That's the clarification. And then thinking about cash conversion, free cash flow conversion over the next couple of years, you've obviously got pension cash moving down. But then as we look out towards the end of the decade, you have - your FAS expense is going to come down. Could you just talk about the progression of how you're seeing free cash flow conversion over the next maybe - towards the end of the decade? Thanks.

Bruce Tanner

David, I'm actually glad you asked that clarification on the 3% to 5% were sort of based on current rev-rec methodology. Although we've give more information on this when we have the results, when we give the trend information in October. But at the least preliminarily (indiscernible) pulling together in anticipation of that rev-rec changing, we're kind of I'll say running rev-rec in addition to the normal methodology for the first quarter and second quarter. I haven't seen the second quarter results yet. But so far everything is indicating that you would think we should see a whole lot of difference. And part of the reason for that is a lot of the units of delivery are what we call POT, Passage on Title transfer where we essentially record sales upon delivery. As long as you're sort of delivering at a constant rate and the program is not at the end of its life if you will, then you wouldn't expect to see a large swing, even when you've converted over to a percentage of cost or cost to cost methodology, and that's sort of our expectation. We don't see a large drop off or a large increase or decrease in our POT deliveries there. So most importantly on our rev-rec, F-35 is not - does not change one bit and that's obviously the biggest driver of Aeronautics and for that matter, sales for the corporation. So I'm hopeful having said that, Dave, that the 3% to 5% sort of works under either methodology, the current methodology or the new rev-rec methodology is what I'm trying to say and we'll see what that looks like when we provide the trend information in '18 as I keep saying.

Relative to the free cash flow conversion, we teed this up. In the past, David, you and I have had a couple of conversations on this. We - I think the - we talked about FAS income. You sort of brought that up. In 2020 - the 2020 timeframe is the end of the accruals relative to our pension trust going forward. So essentially the trust becomes completely frozen at that point in time. And because you lose the service cost, we actually end up getting FAS income in that point in time. As far as cash is concerned, we will expect to see cash contribution, the ERISA contributions continue to increase through that period of time. But we would also expect to see CAS recoveries in our price that are government contracts increase by about a similar amount. So we still expect to have a tailwind associated with pension cash and free cash flow literally going out. I think it’s still consistent what we showed maybe as much as a year ago that all the way out through 2025, at least as we sit here today, we expect to have some tailwind from pension dynamics relative to our cash flow going forward, and that's still what we see today.

Operator

Our next question is from Cai Von Rumohr with Cowen & Company. Please go ahead.

Cai Von Rumohr

Yes. Thank you very much. So since your first quarter, it looks like your foreign sales prospects have improved. Can you update us in terms of what you're looking for, for book to bill this year and any color on next year? And secondly, you mentioned a lot of the foreign potentials. You didn't mention some of the NATO missile defense potentials such as Romania, Sweden, for the Patriot system and MEADS. Thank you very much.

Bruce Tanner

Cai, I’ll take a stab at that and Marillyn can add some color to it if she wants to. So relative to the first question and how we're doing, we're actually tracking hopefully better or better than planned relative to international orders today. I don't have necessarily the book to bill for the year, but I mean trying to do this math in my head, I think we're slightly ahead of book to bill as we sit here today, meaning international order are higher than international sales to date. I would expect that to be the case at the end of the year. A lot of that obviously is predicated on whether or not we get sort of the first tranche of the KSA, the Kingdom of Saudi Arabia orders that Marillyn talked about, those $28 billion worth of orders. There's the potential that some of those can come in between now and the end of the year. It's not obviously clear that they will. There’s obviously some congressional notifications and the like that has to take place and getting the funding employees to do that. But there is that possibility.

Now, even without that, I still think we'll probably be, probably in a positive situation book to bill because we won't have the sales for that either for international business there. So having said that, as we look out in the future, and you didn’t ask this question, Cai, but we still think we've got a chance to end the year potentially at around $100 billion of backlog if some of these, especially the Kingdom of Saudi Arabia orders come in this year, as opposed to next year. But even without that, 95 to 100 is probably what we're expecting, and again more on the international side than the sales for the year. So a positive book to bill.

You asked about the air missile defense. We're still in conversations with Germany right now, the MEADS opportunity there. There's a stated objective to get that negotiation complete by the end of this year. We'll see if that actually closes then, but if not then, I would hope that that closes at least in the early part of 2018. And obviously there's Poland with the Patriot sale and we'll do a lot of the PAC-3 - all the PAC-3 missile associated with that sale. You mentioned some other NATO countries. I’ll let Marillyn maybe jump in and give you a little more insight than I can provide to you.

Marillyn Hewson

Sure. You mentioned Poland, Rumania and others. I mean of course we have Aegis Ashore, which is US system that’s been placed in Europe, but that's an opportunity. Missile defenses, there's a strong demand in Europe, as well as in other parts of the world, Asia Pacific and the Middle East where we continue to see opportunities. JASSM was an opportunity from the standpoint of Poland. And so there - you're exactly right. There continues to be in the NATO environment missile defense opportunities for us to continue to meet, as well as for other parts of the world. And I think as we have recently done the THAAD test out of Alaska, that was a very successful test. In fact, 14 out of 14 on THAAD, one that I'm sure that many countries will take a look at, at the successful capability of that to take out a ballistic missile. And so that being an opportunity that we've talked about that currently in South Korea, protecting that area in Guam. But certainly Japan and other countries will continue to look at THAAD as a capability in the European market as well.

Operator

Our next question is from Myles Walton with Deutsche Bank. Please go ahead.

Myles Walton

Thanks. Good morning. On space, you raised the sales guidance there. And just curious on your outlook for space in general, going here in 2017, where the uptick was coming from. And then if ’18, this gives you any indication that it's actually got some growth in it. And then conversely, the incremental margins looked a little light, 5% incremental margins. Is that just to absorb the commercial satellite charges, or something else? Thanks.

Bruce Tanner

I’ll try those, Myles. So we’re pleased with where space is heading this year in terms of sales. It’s - as I said in the prepared remarks, it's a little higher than our expectations. And obviously we increased the guidance for the year. It’s a little higher than what we expected when we started the year. I do think that portends well for 2018 growth. And there's some of that coming from our special programs business and there are some opportunities there that we have to see how they play out that will drive that either higher or not as high, depending on the outcome of those opportunities.

And then relative to the incremental margin, you have that right, Myles and that is reflective of the fact that some of that volume was offset by the commercial satellite charge that we did take in the quarter. And that's probably worth talking maybe a little bit about, only because it - that sounds like a bad item to have a charge on the commercial satellite. But this is really taking our old legacy A2100 satellite bus, which we've had for a number of decades and really providing a technology refresh of that legacy satellite. So it's sort of updating it to the current state of the art. We’re putting a whole lot of new technologies and capabilities into it, everything from power capabilities and increases to the propulsion on the satellite, the electronics. We've got a new solar array, new power regulator. So a lot of different items all being sort of put together. And unfortunately the satellite where this happened to be the first article for production, was the largest commercial satellite we ever built, or will have ever built.

And so - well, that's the bad news. The good news is, is this new configuration satellite has already resulted in new orders from the US government. And I look at it as this is something that we had to do. We had to refresh that product line and while I'd prefer it not to be on a fixed price commercial international contract I have to sort of cut your teeth on, we're glad that we're doing this now because this will position us to have a foundation for new satellite offerings hopefully for years to come.

Operator

Next we go to with Stifel. Please go ahead.

Joe DeNardi

Thanks very much. Bruce, wondering if you could just talk about capital deployment. From a leverage standpoint, are you comfortable with where you are now, and we should just assume that all of the free cash flow gets split up between the buyback and dividend? Or do you see some deleveraging over the next year or two?

Bruce Tanner

Yes. So good question, Joe. That’s something we’re - we obviously talk every September with our board relative to future deployment actions relative to dividends, but before that session, before we have those discussions and we discuss that sort of strategic view with our board of directors, I’ll say the expectation is it's sort of more the same in terms of our deployment actions. We do have some near term debt retirements coming up starting in 2018. We’ll come - that's something that we’ll guide you towards relative to the trend information ’18 as far as our thinking relative. To refinancing that or paying that off. But our expectation is we probably do some deleveraging as I sit here today going forward in the near term. Those aren't huge chunks of debt, but some of these frankly are the very short term financing that we did actually to finance the Sikorsky transaction

Operator

Next we’ll go to Peter Arment with Baird. Please go ahead.

Peter Arment

Good morning Marillyn and Bruce. Bruce, just sticking on Sikorsky, which you just mentioned - total military helicopter deliveries were down about 18% year to date. How are you thinking about that for the balance of the year? And then in the context of obviously the new multiyear with the US Army and Saudi, how should we think about the government deliveries going forward?

Bruce Tanner

Yes. So this question, Peter, that's actually something I looked at as I was prepping for the call also. The first half deliveries of Black Hawks are down. And at least as I post that with our team at RMS, that really is just because of the timing of the contract deliveries in the current multi-year eight Black Hawk order profile. Even though we're down as you pointed out relative to last year, the expectation is that we still expect to actually deliver more Black Hawks this year than we did last year, just not a huge number, just a handful there. But we would expect to catch up and actually have sort of sequential growth in Black Hawk deliveries, with fourth quarter obviously being the highest by quite a bit relative to the first quarter. A little bit of a different pattern than what we saw in 2016, but that is the contractual pattern. And I didn't look close enough to see if that's because of the types of aircraft we have. We have some MEDEVAC helos versus utility helicopters and that might be part of it as well. But all sort of expected and that is the plan going forward again to sort of finish the year higher than we did this year.

You also asked about - there was another part of your question, Peter. I think you asked about 2018 relative to the multiyear nine. the multiyear nine, I think in - and I haven't got my head exactly around the deliveries next year, but I think they're fairly complement - maybe a little less than this year, but not hugely less. Alternatively as we look forward, the biggest - bigger drop off frankly is in the Romeo helicopters. These are the Naval Hawk helicopters if you will. That's sort of coming to a much lower number of production aircraft delivery like maybe by a third or so or more reduction next year. So one thing that we're watching to see if we can get some rebound on that is from the Kingdom of Saudi Arabia. One of the items that was in that, actually two of the items that was in that $28 billion that Marillyn referenced before was for additional Black Hawks on top of what's in the multi-year nine Black Hawk deal today. And an additional - or additional Romeos are the Naval Hawk helicopters as well. So those have got to sort out and again the timing event, Peter is what we're watching very, very closely to see whether or not those orders come in this year, the early part of next year. But we're hopeful they can sort of butt up against the multi-year nine deliveries we're talking about.

Greg Gardner

John, this is Greg. I think we have time for one more question.

Operator

And that will be from Jason Gursky with Citi. Please go ahead.

Jason Gursky

Good morning. I wanted to - Marillyn, I want to ask you about the Company's supply chain, your strategy there. You've spoken in the past about the need for Lockheed and its suppliers to focus on two things, affordability and cybersecurity, essentially to ensure continuity. Can you provide us a bit of an update on the Company's effort to drive affordability out of the supply chain and is your strategy continuing to evolve there? Are you looking to maybe vertically integrate a little bit more than where you've been in the past and as you look out at things, how far along do you think you are in accomplishing your near to medium term goals on affordability? And then on the cybersecurity front, how do you view the health of the industry overall at this point? And what's Lockheed and the rest of the industry currently doing to improve the cybersecurity health of the supply chain? Thanks.

Marillyn Hewson

Thanks, Jason. Those are great questions. If you look at our supply chain, it represents 60, sometimes 70% of the revenue on many of our programs. It’s a very important element of our business in terms of our execution on programs, performance on programs as well as what we're able to financially accomplish with those programs. So that's great question. On the affordability front, I would just start with our largest program, which is the F-35 and representing last year about 23% of our sales. We put a lot of effort into that piece of it. And collectively with our team mates, major team mates, with Northrop Grumman and BAE Systems, we worked together on something we call - that the government calls a blueprint for affordability, where we actually put funding upfront working, not just with the three team mates, Lockheed Martin, BAE and Northrop Grumman, but all the way through our supply chain and identifying areas where we can invest, continue to drive cost down on the F-35 beyond what you would normally get through a ramp up of production and the volume. And we'll continue to do that. We’re also doing that on the sustainment side. So look at where are there cost reduction initiatives that we can put in place there that would continue to drive the cost down. But we are - we work with supply chain affordability every day on all of our programs. I feel really good about our affordability initiatives in that regard. Our teams that work directly with our sub-contractors, with our suppliers, that is one of their primary efforts and ones that working alongside them, they’re constantly focused on.

The other thing I would say is where we have a big opportunity on F-35 is through the block buy because that's where we can get the volume reduction. That’s where we can get suppliers, if they know they're going to get three lots worth of work, 450 airplanes and plus, then they can invest in driving the cost down. They can commit to a lower price to us on their element of the system. But bottom line is, we work all the way across our supply chain on ongoing basis and are constantly driving. In terms of vertical integration, I think it really just is driven on a case by case basis where it makes sense. I mean if we're assuming that we think we have the capability inside Lockheed Martin, that we could do at less cost and more - and better technology, then we might look at some vertical integration there or through an acquisition that gives us the opportunity to do that. But generally speaking, we're mainly focused on the affordability and the performance of our supply chain on an ongoing basis.

You asked a question about cybersecurity and sort of the health of the industry and what are we doing on that front. I will just speak from a Lockheed Martin standpoint. We recognize that the supply chain is - it's critically important that they have in place appropriate cyber defenses in their business. And so we have worked with the Department of Commerce and the National Institute of Standards to help put in place voluntary initiatives that - and frameworks that work with supply chain on how they can get employees the appropriate defenses. We then audit and monitor what our supply chain, our suppliers have in the way of cybersecurity defenses on an ongoing basis. And we actually work with our customer. Our customer often looks to us for the depth and capability we have in cybersecurity. It is a line of business for us. We do it for many customers and supporting them, and we likewise take that same capability and try to work it back through the supply chain as well.

In terms of health of the industry, I think it's an ongoing effort that we've got to constantly stay focused on as a nation. The threats are constantly changing or there's always an unpredictability in that sense. But we've been a thought leader and an industry leader in cybersecurity for many years. In fact we have the national cyber range where we develop that and where our government customers and others can bring their solutions and test them on those national cyber range and determine whether it brings the kind of defenses that we're looking for, that they expect. And so I would say across the board, cyber has been an area for us that, as in everything that we do across the system, it runs through all of our programs. It is - we have a robust capability that we provide to customers and we work hard with our supply chain to make sure that they get the right defenses in their own networks on ongoing basis. Thank you.

So I think that that was the last question. Greg, let me just wrap back and conclude the call today. I want to conclude by restating that our second quarter results and our increased 2017 outlook reflect that we have an ongoing commitment to our strategy for growth, strong cash generation and we continue to deliver innovative solutions for our customers and long term value creation for our stockholders. We’re very pleased with the solid results that we had for the quarter. I want to thank you all for joining us on the call today and we look forward to speaking with you on the next earnings call in October. So John, that concludes our call today.