Good day, everyone, and welcome to the Lockheed Martin Third Quarter 2013 Earnings Results Conference Call. Today's call is being recorded.

At this time, for opening remarks and introductions, I would like to turn the call over to Mr. Jerry Kircher, Vice President of Investor Relations. Please go ahead, sir.

Jerry F. Kircher, III

Thank you, Stephanie, and good morning, everyone. I'd like to welcome you to our third quarter 2013 earnings conference call. Joining me today on the call are Marillyn Hewson, our Chief Executive Officer and President; and Bruce Tanner, our Executive Vice President and Chief Financial Officer. I like to remind you the statements made in today's call that are not historical facts are considered forward-looking and are made pursuant to the Safe Harbor provisions of Federal Securities Law. Actual results may differ. Please see today's press release and our SEC filings for a description of some of the factors that may cause actual results to vary materially from anticipated results.

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 A. Hewson

Thanks, Jerry. Good morning, everyone, and thank you for joining us on the call today. I hope you've all had a chance to review our third quarter earnings release and financial results. The results directly illustrate the continuation of our strong operational and financial momentum and enabled us to increase our financial outlook for 2013.

The focus and efforts of our Lockheed Martin team continued to position the Corporation for delivery of solutions to customers and value to shareholders. I offer my congratulations and appreciation to all of our employees and especially to those employees directly affected by the government shutdown, for their outstanding achievements and performance while operating in a challenging and dynamic environment. While there were numerous financial accomplishments in the quarter that Bruce will outline in his comments, I want to offer my thoughts on key strategic achievements this quarter.

From my perspective, beyond the program execution and financial results that remain exceptional, other accomplishments can be seen in three key strategic areas. These areas are backlog expansion, international growth and cash generation. We have continued to describe our portfolio as the best positioned in the sector with unique and direct alignment to many of the essential programs identified by customers as they satisfy their national security requirements. Many of our programs have provided these solutions to customers over several decades, because they are proven and they are cost-effective.

Addressed validation of this alignment and positioning of our programs to customers' needs is visible with our achievement of increased – increasing levels of annual backlog for the past three years ending with over $82 billion in backlog at year-end 2012, while operating in a challenging global and domestic economic environment. This quarter, our portfolio alignment and product offerings resulted in $15 billion in new orders and expansion of our backlog to nearly $79 billion. We continue to execute on the forecast we outlined to you at the beginning of the year that our backlog expansion would resume in the third quarter. Looking forward, the new business pipeline remains robust with significant domestic and international awards expected later this year on many of our legacy programs.

With the establishment of a continuing resolution for fiscal year 2014 in place through January 15, we remain on the path previously outlined to you, to further expand our backlog in the fourth quarter to a year-end estimate of at least $80 billion. Our ability to continue the expansion of our backlog is strategically important as it helps solidify our business and provide visibility into our future financial outlook. Our strong backlog consisting of multiple years of prior fiscal appropriations driven by our longer cycle production programs provides a level of financial stability and strategic differentiation in this era of potential government budget uncertainty.

Another area within which we achieved significant strategic progress this quarter was in the international business arena. As you recall, we have a stated goal to expand our international sales content to at least 20% of revenues in the next few years. To achieve this goal, we have moved aggressively to build upon our long-standing in-country presence and further strengthen relationships with international countries around the world through partnerships, in-country production, and establishment of in-country joint technology offices. All of these actions are essential to enable expansion of international work for the Corporation.

Financial benefits to the Corporation are increased sales, cash flow, and earnings contribution. Benefits to our customers are increased factory loading and our ability to improve cost through higher production throughput. Specific events furthering our international expansion were seen across multiple business areas this quarter and included finalization of a multibillion dollar award from the United Arab Emirates for our THAAD missile defense system.

This was a significant strategic event with the UAE serving as the inaugural international customer for the THAAD system. Demand for this proven system is only growing and has been expressed by numerous countries from the Asia-Pacific region to the Middle East. Additionally, finalization of our LRIP 6 and 7 contracts on the F-35 program contained a growing component of international work with inclusion of new aircraft awards for Australia, Italy, Norway, and the United Kingdom.

Looking forward into 2014, Japan and Israel are scheduled to finalize new orders, which would further expand our international backlog. Additional international award can be seen on the near horizon with the Netherlands' announcement of its first order to procure Joint Strike Fighters for its national defense. We look forward to providing these revolutionary aircraft to one of our key strategic partner countries.

Finally, we were pleased that South Korea plans to reopen the competition for their future fighter program, potentially providing us a new customer opportunity for our fifth generation F-35 Fighter and further growth in international activity. Our international work is expected to grow and help mitigate domestic pressures in 2014 with growth visible and achievable due to our backlog of existing work. Our international expansion is broad based, is happening now, and we feel increasingly confident about our achievement of our stated goal of at least 20% in the near future.

Let me turn to cash flow. Our ability to deliver consistently strong cash flows continues to be a strategic differentiator for our Corporation. The importance of cash is embedded in our corporate DNA. I was pleased that we were able to – again able to increase our 2013 cash flow outlook this quarter. Our strong and increasing cash flow enables us to invest prudently in the future of the Corporation, in areas such as capital expenditures, and research and development, while also providing the ability to pursue our cash deployment strategy for returns to shareholders in the areas of increasing dividends and share repurchases. We continue to strongly believe in the return of value to shareholders through dividends and share repurchases.

As I look forward, our future cash flows are expected to be aided by increasing levels of customer advances from growing international work and recovery of our $8 billion in prior year's pension contributions. We feel very good about our future cash and the potential for continued strong and increasing cash flows that will position the Corporation to differentiate from competitors.

Before turning the call over to Bruce to cover financials, I wanted to briefly speak about Government budgets. Last week, agreement was reached to implement a continuing resolution to fund FY14 government expenditures through January 15, 2014. This action enabled federal agencies to return to work and eliminated the partial Government shutdown. The agreement also extended the nation's debt limit authority until February 7, 2014, avoiding a default that could have occurred last week.

Additionally, Congress agreed to conduct conference committee discussions on FY14 budget levels and cost elements with a goal for completion of a budget agreement by December 13, 2013. These actions are a step forward as they enable resumption of full government and contractor operations during the periods outlined. Resumption of normal work is the best path forward to eliminate disruptions to operations, enable cost affordability and savings initiative to progress and provide critical equipment and services to our customers.

There is still much budget work to be done by Congress to address the debt ceiling before February 7 and determine the level of funding for the entire 2014 fiscal year before the continuing resolution expires next January. We continue to urge Congress and the administration to focus on long-term solutions to confront the difficult fiscal issues facing our country and avoid a repeat of the disruption that the nation recently experienced.

As part of those solutions, we also ask that they address and revise the across the board budget reduction policy required under the current sequestration law. This non-strategic allocation of budget reductions is not good for our nation or our national security strategy. With the closure of Government fiscal year 2013, we can now determine that budget reduction action implemented under sequestration will result in a limited impact to our portfolio of programs in 2013, with impacts seen primarily on our shorter cycle business.

Our original estimate of $825 million in potential reduction to revenues was significantly muted due to our large backlog of work remaining unaffected by FY13 budget cuts. This enabled us to refine our revenue outlook for calendar year 2013 to a new guidance value of approximately $45 billion, better than we projected on our July earnings call.

As we look forward into 2014, clearly there is no shortage of possible government budget outcomes. These outcomes range from full implementation of sequestration cuts required under the Budget Control Act to less severe scenarios. These multiple scenarios are challenging to predict. However, with our anticipated strong year-end backlog I spoke to earlier, aided by growing international revenues unaffected by U.S. government budget actions, we are expecting to see mitigation of financial impacts on our Corporation. Accordingly, we are providing initial trend analysis for 2014 that projects our revenues to be only slightly below 2013 levels.

I'll now ask Bruce to go through some of the details of our 2013 financial performance and 2014 trend analysis, and then we'll open up the line for your questions.

Bruce L. Tanner

Thanks, Marillyn. Good morning, everyone. As I highlight our key financial accomplishments, please follow along with the web charts that we included with our earnings release today. Let's start with Chart 3 and an overview of the quarter. Sales in the quarter were $11.3 billion, down from last year, but slightly ahead of our expectations. Segment operating margin continued to be very strong at 12.8% and this strong performance contributed to a 16% increase in earnings per share to $2.57 from continuing operations.

We generated $900 million in cash from operations after a $750 million pension contribution. We continued to reward our shareholders with almost $1 billion of cash returned to the repurchase of nearly 5 million shares along with our quarterly dividend payment. As expected, we received $15 billion in orders in the quarter, which brings our backlog to just under $79 billion, and finally due to our operating performance, we increased our 2013 outlook for segment operating profit, earnings per share, and cash from operations.

Chart 4 shows our sales and segment operating margins for the third quarter this year versus last year. Our sales were 4% lower than last year, but ahead of our expectations after sequestration was enacted. Segment operating margin increased 70 basis points over the third quarter of last year to 12.8%, continuing the strong performance we've achieved thus far this year.

We'll show the breadth of the margin improvement on Chart 5, which shows our third quarter segment operating margins for each of the 5 business areas compared with last year's results. Segment margins were higher or comparable in 4 of the 5 business areas. Improvements in Missiles and Fire Control resulted from improved performance across a number of programs, most notably in Air and Missile Defense programs such as PAC-3 and THAAD and Fire Control programs such as the LANTIRN and Sniper programs.

Improvements in Mission Systems and Training were also broad based with the largest improvement coming from our radar programs. Margins in

Aeronautics and IS&GS were slightly higher or comparable, while our margin in Space Systems remained strong and was 60 basis points lower than the third quarter of last year. Last year's results were the highest level ever experienced in Space Systems and included significantly higher earnings from our United Launch Alliance and United Space Alliance joint ventures, the latter due to wind down activities in 2012.

Turning to Chart 6, we'll discuss our earnings per share. EPS from continuing operations in the quarter was 16% higher than a year ago at $2.57 per share, driven primarily by improved margins and a lower FAS/CAS adjustment this year. On a pension-adjusted basis, our EPS grew to $2.80 per share in the quarter.

On Chart 7, we'll discuss our cash from operations in the quarter. We continue to have excellent cash generation with $900 million in the quarter, although that is lower than last year's level, we made a $750 million pension contribution this year, while no contribution was made in the third quarter of last year. We've completed our planned funding of our pension plans in 2013 and consistent with our historical practices, we will evaluate making additional contributions to our pension trusts at year-end, but only to the extent that these contributions will not impact our ability to generate $4.3 billion in cash from operations.

Turning to Chart 8, we'll discuss our cash return to shareholders in the quarter. We've returned almost $1billion to shareholders this quarter through share repurchases and dividends. The level of share repurchases was more than double what we did in the third quarter of last year and brings the total cash returned so far this year to more than $2.6 billion.

Moving to Chart 9, we'll look at our backlog and book-to-bill ratios since last year. Consistent with the quarterly backlog profile, we provided at the beginning of the year, our backlog grew to just under $79 billion this quarter, achieving a strong book-to-bill ratio of $1.3 billion. We continue to expect that backlog will increase further in the fourth quarter and end the year above the $80 billion level.

On Chart 10, we provide our updated guidance. As we said on the last call, the effects of sequestration were not as great this year as we had initially modeled them to be and we now feel comfortable in saying our sales for the year are anticipated to be around the $45 billion level.

Reflecting our strong operational performance throughout this year, we're increasing our forecasted segment operating profit by $125 million. Partially offsetting improvements in our segment operating performance is an increase in our unallocated expenses for severance charges related to reduction in force announced last week in our MST business area and a net increase in expenses for our deferred compensation plans. The net increase in operating earnings resulted in an increase to our earnings per share guidance of $0.20 to –to $9.40 to $9.70 per share. And finally, we increased our expectations for cash from operations by $100 billion to equal or better than $4.3 billion.

Chart 11 shows our updated outlook for both sales and segment profit by business area and ties the guidance updates from the previous chart. On Chart 12, we provide our initial view of our expectations for 2014. We believe sales next year will be only slightly below the 2013 level with growth in our Aeronautics business area offsetting reduction in our IS&GS and Space Systems business areas, while both Missiles and Fire Control and Mission Systems and Training are expected to be relatively comparable to their 2013 levels. And we expect our segment operating margins to be lower than this year's record level, but above the 11.5% its level in total as we experience the dilutive effect of F-35 production growth in Aeronautics, as we described for several quarters along with the absence of several non-recurring benefits in the other business areas this year.

We expect our FAS/CAS pension adjustment will provide income of $150 million in 2014 after several years of reducing our reported earnings. Our assumptions that led to the favorable adjustment, our 75 basis points increase from the discount rates to 4.75%, a low single-digit return on assets in 2013 and $1 billion in pension funding in 2014.

Finally, we have our summary on Chart 13. We've had outstanding performance all during 2013 and we expect that to continue and result in a very solid year, particularly in this dynamic environment. With our current portfolio as well as our enhanced focus on international expansion, we like our strategic positioning heading into the next few years. We've provided outstanding value to shareholders this year from both a total shareholder return perspective as well as with cash return to shareholders and while we're providing high-level trend information today, we'll provide our usual detailed guidance during the January call.

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

Question-and-Answer Session

Operator

Thank you. (Operator Instructions) Our first question comes from Jason Gursky with Citi. Your line is open.

Jason M. Gursky – Citigroup Global Markets Inc.

Good morning, everyone.

Bruce L. Tanner

Hey, Jason. Good Morning.

Marillyn A. Hewson

Good morning.

Jason M. Gursky – Citigroup Global Markets Inc.

Marillyn and Bruce, so I was wondering if you could just walk us through the assumptions on your – with your major programs that are embedded in your outlook for 2014, just so some of the building blocks and kind of track progress as we go along?

Bruce L. Tanner

Yes, Jason, I'll give you a high-level view. Marillyn has something to add, I'll throw on a couple of other or she could throw on a couple topics as well. So maybe just starting with the biggest business area Aeronautics, probably the topic that you'd be curious about is the aircraft quantity changes say from this year to next year. So think of the F-35 quantities, we're going to finish the year probably around the 36 aircraft deliveries or so, we expect that to grow somewhat next year to maybe 38, maybe a couple more than that, but somewhere in that range.

Our F-16 deliveries this year are 13 aircrafts. That is expected to grow perhaps about 15 aircraft next year. C-130Js, I think, we're going to do about 24 to 25. There is one that's kind of on the bubble of delivering this year and next year, but if it happens this year, it will be 25. Even if that happens this year, we still think we'll stay steady at about the 24 aircraft level next year. In C-5, this one is ramping up between 2013 and 2014.

We're going to deliver somewhere between, I'll say, 5 to as many as 8 this year, but in any event, we think we'll grow that number to 10 aircraft next year, and the reason we are a little hesitant on giving the numbers for 2013 is because of some of the activities that led to the de-book this quarter relative to some of the over and above works that we're experiencing in those aircraft that could cause delay in some of those deliveries this year.

If I think around the other business areas, you should think, we are seeing a slight reduction in quantities of some of our Air and Missile products associated with the PAC-3 program, but that's more than offset at Missiles and Fire Control by increases in the THAAD production quantities, think about both domestically as well as with the recently completed UAE international order.

We have no commercial satellites or commercial launches next year in our Space Systems business. We expect to have obviously no large programs that jump out on our IS&GS business area, but we expect to see a continued downward trend within IS&GS probably somewhere in the -- I think of that as the high single-digit range level between 2013 and 2014, so that probably covers a bunch of program Jason, there may be others you want to hear about, and if so, others can ask on the call when we go down to further questions.

Operator

Our next question comes from Richard Safran with Buckingham Research. Your line is open.

Richard T. Safran – The Buckingham Research Group, Inc.

Hi, good morning.

Bruce L. Tanner

Good morning Rich.

Marillyn A. Hewson

Good morning.

Richard T. Safran – The Buckingham Research Group, Inc.

I was interested – just kind of a two-part question on your comments, Marillyn, at the opening and on the 4Q bookings chart on Chart 9. One, should we kind of infer that there's very little risk from the Government shutdown on 4Q bookings in terms of what the Government is going to want to contract? and then as a second part, I found it interesting that you had enough confidence in your outlook to talk about 2014 trends. Could you discuss what's driving your confidence in your outlook, just especially given where the Congress and the Administration are? Thanks.

Bruce L. Tanner

Hey Rich. I'll give a shot at both of those and we'll see if Marillyn has some color or commentary to provide beyond that. So fourth quarter orders, we do feel very comfortable in stating what we said relative to expectations that will grow backlog between now and the end of the year. And in particular, the reason we feel that way is that there are really very few competitive awards expected to occur in the fourth quarter and we have really no reliance on sort of new start programs in the quarter either.

And just as importantly, while we're operating in a continuing resolution environment, we believe all the awards that we're expecting to receive in the quarter can be awarded under the continuing resolution. So just to maybe name a couple of them that we expect that will lead to the year-end backlog numbers we talked, the most significant awards are occurring in our Space Systems business. So think of that as the SBIRS Spacecraft 5 and 6 contract definitization by the end of the year, the annual -- in this case, the FY14 annual installment of the Fleet Ballistic Missile award.

We expect to receive a pretty significant contract extension on the Orion program within NASA, and then if I go – that's – those are probably the most significant, all of which are in Space. If I go to other business areas, we're expecting things like the normal sort of FY14 award of the C-5 modernization aircraft this year. We should close hopefully on the FY13 contract to finalize or definitize the C-130 deliveries for the U.S. Government, and then we've got just a whole slew of sorting what I would call the numerous funding from fiscal year 2014 funds becoming available for things like JASSMs, PAC-3s, sustainment contracts across multiple business areas. So again, we feel pretty good about all those happening. Again, not anything that I would say isn't a competitive award that could be pushed out or that we could lose in the fourth quarter that would diminish those numbers. So I think it's a really good visibility as we go into 2014 as well.

I think you asked about the 2014 guidance or maybe you expressed some surprise that we were at the levels we are, so maybe at a high level, I'll just talk about what we're seeing in 2014. As Marillyn said, we do expect sales to be slightly lower than 2013 and you should think of that as we are going to see growth in Aeronautics, that's primarily coming from the F-35 production program as well as the C-5M delivery growth and numbers that I've talked about earlier, and that's offsetting reductions in, as I've said, IS&GS and Space and Missiles and Fire Control and MST again are fairly comparable.

Margins, again, we expect to remain above 11.5%. and I've talked in quarters past about what I like to refer to as sort of the algebra effect of the F-35, where we get higher volume on the F-35 program at lower margins than the overall margins of Aeronautics and that has the effect of lowering margins in aero overall. Missiles and Fire Control and IS&GS, I would think are going to be relatively comparable to 2013, whereas Space and MST, probably a little lower than where we experienced this year, but still very strong relative to recent history on those – in both of those business areas and this is due to a number of non-recurring events, positive events that occurred in 2013. Space also has the lower equity earnings expectation in 2014 compared to 2013.

So Rich, maybe just to sum up, 2014, I would say from a margin perspective, looks very similar to 2013 when we began the year just without sort of performance improvements that we have experienced throughout 2013 that we've yet to obviously experience in 2014. Maybe one last note on 2014, you should see the tax rate in 2014 increase a little bit over 2013. You'll recall we actually had two tranches, if you will, of R&D tax credit in the year 2013. So, probably more than you wanted to know there, Rich, but hopefully that covers your question.

Operator

Our next question comes from Doug Harned with Sanford Bernstein. Your line is open.

Doug Stuart Harned – Sanford C. Bernstein & Co. LLC

Yes, good morning.

Bruce L. Tanner

Good morning.

Doug Stuart Harned – Sanford C. Bernstein & Co. LLC

I'm interested in understanding the trends in IS&T a little bit better**.** If you look, and I guess I would put that in conjunction with the comments you made around sequestration, and that sequestration, the impact this year was a little bit less than you had thought. What I'm trying to get at is, is this largely a timing issue or has – have some other things happened that is kind of strengthened the picture this year. And then how does that link to IS&T which you've said will be weaker next year? And does that play into the civil, the defense to the Intel portions of it?

Marillyn A. Hewson

So Doug, I would just say to that point you know when we gave some insight earlier in the year about what we expected on the impact to sequestration, it really was looking across all of businesses, we did recognize that our shorter cycle business like IS&GS would have a more significant near-term impact. But that was juts modeling that Bruce and his team did just to kind of take a look at what was the outlook for the year of things that could be impacted, we have not seen the impact and so it wasn't really just because of IS&GS.

IS&GS is – because it has a large IT infrastructure work and support and the information technology area, has been impacted because that's an area that the Government can cut back on pretty readily. We do – it is – as I said, it is a short shorter cycle business, where we see growth there, potential growth where as in the cyber security arena, but it's fairly a new area for us or we continue to see some offset of growth there. Bruce, I don't if you want to maybe add some other…

Bruce L. Tanner

Yes maybe just, I think you asked a question about where we're seeing that maybe by the LOVs, the civil, defense and intelligence. And so we're actually seeing little bit of growth in our defense business and a lot of that's because we've won – going back to Marillyn's, kind of we've won several sort of cyber activities from competitors sort of – no we refer to as playing offense if you will in that arena, so we've been successful on it. And that's one of the reasons why the defense business is growing this year over last year.

As we looked next year, there's not as many of those sorts of competitions coming up, I believe all three lines of the business civil, defense and intelligence in next year's numbers as we said here today though, we're expecting to reduce compared to 2013. And I think that's just sort of the – a combination of two things, one that is what I've always said when you're the largest provider of IT Services to the Federal Government for 18 straight years now, I believe. That when the federal government's budget goes down, you are likely to go down as well; we expect that to happen again in 2014.

And the other side of that is, I'll say we have within the numbers that I talked, within the ranges that I've talked in the trend information so that considered the growth [ph] and ongoing sequestration level impact this year as well. So the combination of those two events is what we see happening within IS&GS. I always like to close that by saying, at some point, IT spending has to increase. You cannot continually reduce IT spending for the Federal Government and expect to provide the services the population expects. In some point, it will turn the other way.

Operator

Our next question comes from Ron Epstein with Bank of America Merrill Lynch. Your line is open.

Unidentified Analyst

Hi, good morning. This is actually Elizabeth in for Ron today.

Bruce L. Tanner

Hi, Elizabeth.

Unidentified Analyst

Hi. We see – it's actually seeing Boeing really emphasize recently their Partnering for Success program, where they are trying to get 15% of their suppliers. And we were just wondering, with all the cash that you're returning to shareholders and the DoD under so much pressure, at what point do you think the DoD sort of tries to implement its own Partnering for Success and take 15% from the defense contractors?

Bruce L. Tanner

Well, I'll let Marillyn state from her perspective, Elizabeth, I don't think we've ever stopped Charles to do what we think makes sense economically and from an affordability perspective with our supply chain. And we maybe have a little different views, there has been some – and we think the real ability to have supply chain starts actually with the designs that we come up with and how we can make those more affordable to build and sustain going forward.

So it's not something that we woke up overnight and realize that we had the correct elements for our supply chain to become affordable. We are probably two-thirds of our costs to sales today are in the supply chain. If we are going to be affordable, it's going to have to include our supply chain and always has and that's the focus that we do today. We have, I would argue, very good relationships with our supply chain. We have annual sessions, where we meet with them.

Actually Marillyn has spoken to that group in mass to show the emphasis that we place on our supply chain and expectations not just of affordability, but of quality as schedule timeliness and alike. So this is something that we put in place for quite sometime that is not a new item of course.

Marillyn A. Hewson

I would add to that, Elizabeth, I think if you are asking is our customer treating us as their supplier in a fashion that they were going to put some push on us to be more affordable, they have been. I mean, that is a – they have been very clear that is a top priority for them. They are dealing with very significant budget constraints and increasing global security demand. So they are challenged and, across our industry, they have a press for us to all to be more affordable in solutions that we provide them and how we manage our business.

It’s not something that is new to us. We’ve been very proactive as leaders in the industry to drive down our cost and we have taken actions to reduce our footprint. We have had to take some painful actions in reducing our workforce at times to adjust to the business base. We are investing in technologies to provide them with a more affordable product. So we take the weight out or we make it – overall total cost lower. A lot of things that we are doing to support our customers drive for affordability, and at the same time, they offer incentive provisions to get in cost savings because it is so critically important to them. So in some of our contracts, we have those types of incentives to encourage us to continue to drive costs down.

So as Bruce said, we manage our supply chain. It’s an ongoing effort on our part to make sure that we get the best value from them in terms of costs, schedule, quality and at the same time, we want to provide our customer with the most affordable solutions and the most technically capable solutions for what their needs are.

Operator

Our next question comes from Cai von Rumohr with Cowen & Co. Your line is open.

Cai von Rumohr – Cowen & Co. LLC

Yes. Thanks so much, and great performance again.

Bruce L. Tanner

Thank you, Cai.

Marillyn A. Hewson

Thank you.

Cai von Rumohr – Cowen & Co. LLC

So I have a two-part question. First, you talked about sales being down modestly next year. Could you talk about international, if that’s growing, what sort of growth do you see in international and what are the key drivers? And secondly, DoD as it looks at the fiscal 2015 budget, had some priority programs and some bill payer programs, potential bill payer programs, included in those are C-130, C-5 and LCS. Maybe you could comment on your thoughts as to whether those programs you think are at risk in the FY15 budget? Thanks.

Marillyn A. Hewson

So on the international growth side, we certainly continue to see growth in F-35. In fact, over the next five years, close to half of the orders will be international deliveries for the F-35 as we move forward. On C-130J, there continues to be a demand for the C-130J and we continue to sell F-16s around the world. So we see growth in those areas. Missile defense is another very important element for us in our international growth, Bruce talked about that and PAC-3 and of course, we have our operations for Aegis Ashore, and then, we do see other opportunities for us as we look forward into the – in the satellite, commercial satellite arena, and cyber security and our IT arena for growth in the sale and international growth.

On the F-15 priorities, you mentioned C-130, LCS and C-5, all of those are part of our – of the strategic management review that was done by the U.S. Government. They are high priority programs and, in addition to those, I think Missile Defense continues to be a high-priority program.

Bruce L. Tanner

And the another thing I would add Cai is, I was a little surprised to hear C-130 mentioned in that comment, where one of the few problems in the DoD that's actually is being considered for a multi-year program to buy an additional 79 aircraft for a couple of the services right now. I think that's got strong support, it obviously has reduced – affordability aspect to it versus buying them on individual fiscal years that has I think been well received by our customers and we expect that to happen. So that's one that caught my ear a little bit, somewhat of a surprise when you had that to discussion there.

Operator

Our next question comes from David Strauss with UBS. Your line is open.

Bruce L. Tanner

Hi David are you on mute?

David E. Strauss – UBS Securities LLC

Hey good morning.

Bruce L. Tanner

Hey there.

Marillyn A. Hewson

Good morning.

David E. Strauss – UBS Securities LLC

Good morning Marillyn. I wanted to ask you about back on sequestration. So when you saying in the release that you assumed all impact known associated with sequestration, just so I'm clear that that you're assuming inherently in that that sequestration relates to fiscal 2014 comes through as we know announced another $15 billion to $20 billion cut off of to the total DoD budgets. And then the last part of my question, maybe if you could walk us through Bruce, I think back in January, maybe within the airport [ph] you put together that side that showed that in terms of the total revenues that would be impacted by sequestration in 2013 were in like 20%. Where does that number move to in 2014, or in other words how much of your – what proportion you think of your revenues will actually be impacted by sequestration in 2014? Thanks.

Bruce L. Tanner

Yes. Okay thank you David. It's a good question. So let me give you maybe a long windy answer on the sequestration impacts for next year. I think I'll cover hopefully both of your questions in this answers. If not again maybe you can come back on and ask the question again, but. So we still think sequestration how that impacts 2014, is broken up from our business area perspective than the sort of the long cycle businesses and short cycle. We always refer to aeronautics and space for instance as long cycle businesses. But there are also large parts of Missiles and Fire Control and Mission Systems and Training that are also really considered to be long cycle businesses, as well.

So you should think of those as, in my words being relatively insulated part of the effects to sequestration in FY 2014, because most of their calendar year 2014 sales are from prior fiscal year funded activities or prior fiscal year funded backlog. That also says there's not probably as much upside as sequestration improves over what our expectations are either in those long cycle businesses. Our short cycle businesses and primary one being the IS&GS, but also has smaller parts Missiles and Fire Control, Mission Systems and Training as well. We faced some pretty good reduction into the numbers that we're expecting relative to the guidance, assuming the trend information we provided to the slightly less than 2013 sales those reductions are planned in that outlook already.

And we think that pretty much captures what we think will happen under a sequestration environment, under a lot of different scenarios that we can think of. And the reason for that is while we say they are short cycle businesses, each one of those businesses IS&GS, the service is part of MFC, the service is part of MST and backlog from prior year funding is actually greater than one time sales in each case.

So, there was not as long or as not as significant in terms of the backlog as the long cycle business and there is definitely more current year award to current year sales going on in those business areas. It is more insulated than perhaps you might think, and I think we experienced that ourselves and we try to do the modeling at the start of this year that we actually have more insulation in my words that maybe we – maybe we would otherwise thought we had at the start of the year.

There is also the aspect next year that we don't want to lose track and back to I guess Cai's question. We do expect international growth for the next year both in terms of absolute dollar as well as on a percent of sales base. So that helps to mitigate any down side we're seeing from the sequestration impact as well, and finally at least as we've looked at it, we think there is minimal – if there is really any reliance on 2013 unobligated funds, balance that's left, the outstanding at the end of the fiscal year to become 2014 sales for Lockheed Martin.

So if, if those funds were to evaporate, if those funds were to be used to offset FY 2014 sequestration reductions, we think again, we're again insulated from that aspect as well. So hopefully that covers the two questions you had there David.

Operator

Our next question comes from Noah Poponak with Goldman Sachs. Your line is opened.

Noah Poponak – Goldman Sachs & Co.

Hi, good morning everybody.

Bruce L. Tanner

Morning Noah.

Marillyn A. Hewson

Good morning.

Noah Poponak – Goldman Sachs & Co.

I guess I'm trying to figure out how the parse – to me revenue being down slightly is a positive surprise given what the budget is doing, and that you are the Bellwether in sense. And I hear you saying and I know that you have well positioned the favorite programs and I obviously hear you saying no that it's a long cycle business. I guess, I'm trying to sort of quantify or parse out, how much of each of those two items it really is in 2014, because if it's almost entirely just favored programs, that would suggest you could move back to actually growing sooner than later if sequestration is the last cut. Whereas if it's long, if it's more being long cycle than it is favored programs, that would suggest you actually have several more years of not really being able to grow the top line even if sequestration is the last cut?

Bruce L. Tanner

Yes, so interesting question, Noah, and I'll see if I can parse my answers to the question the way you parsed your questions. as we look into 2014, I think one of the things that may surprise some folks as going forward is that we're actually probably seeing more growth in the F-35 program in next year the number that we are trending towards, the slightly less than $45 billion next year, that maybe a lot of people would have expected. So just in big numbers, the F-35 is going to be 15% or 16% of the sales of the Corporation in 2013 and F-35 jointly between the development program and the production program, but all of the growth coming from the production program is probably going to grow some 15% year-over-year from 2013 to 2014.

So that's – I think that's one of those programs, Noah that I would characterize as both long cycle and the right priority. I think the prioritization has been demonstrated continually throughout the past year, both domestically and internationally, with the support that we're getting on the program and obviously by definition, I guess, it's a long cycle program. I think we've got other programs that has same deal, the C-130, I mentioned with the multi-year, the Air and Missile Defense programs, where they're both long cycle and high priority; LCS is another one that would fall in that category.

So I'll tell you – and I'll let Marillyn opine here also on it, because I know she feels strongly about this, but we've said all along we think that we have the best portfolio in the business. We think we have the opportunity to sell that portfolio internationally, which helps to mitigate or mute the impacts of the domestic reductions. And so I don't think that the scenario you described where we would expect to see growth depending on how sequestration plays out in 2014 is unrealistic at all.

Marillyn A. Hewson

Yes, I'd just agree with what Bruce has outlined for you. And we've talked, as you said yourself, we have a well positioned portfolio of programs and as

Bruce outlined where we see the growth opportunities in 2014. If there is an impact with sequestration as we – there is a full impact with sequestration. We walked through where the impact will be on the shorter cycle businesses. If we don't see that same significant level, we should expect to have some offset there and then the longer cycle business as we move on, we do see growth, continued growth in Air and Missile Defense and the F-35 and even F-16 upgrades and the number of other opportunities on C-130Js internationally as well as the multi-year.

Operator

Our next question comes from Joe Nadol with JPMorgan. Your line is open.

Joseph B. Nadol – JPMorgan Securities LLC

Thanks. Good morning.

Bruce L. Tanner

Good Morning.

Marillyn A. Hewson

Good morning.

Joseph B. Nadol – JPMorgan Securities LLC

Couple of Green IT Tech questions for you, Bruce, just on the margins, maybe it would help us if you quantified a little bit the two items that you say might pressure segment margins next year. How much pressure do you see on the F-35 becoming a bigger part of the mix, because you're 12.8% year-to-date on segment margins just seems like a 11.5%. There is a lot of room to come in ahead of 11.5% even given some of the pressures? And the second part of that is just on MST, in particular, you highlighted radar programs as being a big driver of the upside, we can see adjustments in the quarter, are you getting into a situation there, where there is – you could for a few quarters, get some upside just given that the opportunities on those contracts or is just truly do you think not sustainable? Thanks.

Bruce L. Tanner

Yes, thanks, Joe. So let's see the F-35, is in the reference to what's happening with the F-35 growth and its impact on Aeronautics margin, and first off, I know you are looking at the 12.8%, but I think if you – that's where we ended the quarter. I think that's the highest quarter we've ever had in the history of the Corporation. If you go to the full year, I think, we're looking – if you go to mid point of guidance, probably in the 12.3% to

12.4% range. So I'm not going to debate whether that's going down or up relative to 11.5% and it obviously is, but it may not be from the 12.8% picture starting from.

The only thing I tried to emphasize was on the – on a previous question was that 11.5% that we are talking about, actually looks a lot like where we started the year 2013. I forgot what we – what our guidance was in the start of the year, but it was somewhere in the 11.6% or 11.7% as I recall, it kind of feels like a similar level to me is where we started in 2013. Most years we have had positive performance improvements throughout the year that have enabled us to have benefits. We don't count on those happening every year when we provide the initial guidance, but I think our track record for most years would say that's been where we've been successful. So as I look at Aeronautics, I would expect that reduction to occur I mean from a margin perspective 2013 versus 2014, they are going to – I think if we go to the midpoint they are probably in the 11.4-ish range. And I would think that we'll still see it somewhere in the 11% margins even with the dilutive effective of the F-35 and C-5 increases in Aeronautics.

The point I'm trying to make on the – in my prepared remarks was that in particular with an MST we had I believe in the second quarter that was the highest margin in the history of MST, and we had a few contractual resolutions there that we did described in both the press release and Q which you should think of being $75-ish million or so. On top of that, we have had very good performance, you mentioned the Radar programs, those are very good. I think that's a business that kind of stays in 11-ish range on a kind of a go-forward basis.

And then you didn't ask about it, but the one I mentioned previously, was the Space Systems Company with the joint venture in equity earnings. We had some high equity earnings this year, really associated with launch related activities. Those are expected to come down a little bit next year. Could we see the same experience with some performance out of ULA, next year as we saw this year? Yes. But are we planning on that with our guidance? Not at this point in time. So Space Systems, I'm very pleased with margins there, again this is probably the highest share in the history of space. I think that's a business that probably stays in 12% range going into next year.

So what we say here today, we are not at all just pleased with where we expect the margins to go next year and I'd say we have the same sorts of opportunities to increase those margins next year as we did this year.

Operator

Our next question comes from Rob Stallard with Royal Bank of Canada. Your line is open.

Rob Stallard – RBC Capital Markets LLC

Good morning.

Marillyn A. Hewson

Good morning.

Bruce L. Tanner

Good morning.

Rob Stallard – RBC Capital Markets LLC

On the F-35, on the most recent contract you signed; I was wondering if you can give us some color on how the contractual terms might have changed, and how your discussions with the customer have progressed, you could have a separate customer?

Bruce L. Tanner

Firstly. Rob, I guess, the first thing as we negotiated Lot 6 and 7 combined if you will, they are separate contracts, but we did do a – essentially, concurrently. And we did so in about six months time versus Lot 5 where we probably took about 18 months. So I think we are on a good path there. As for as contractually speaking, we do have essentially a fixed price contract and I'd say essentially, because there is a little bit of essential share on underrun there between the Government and ourselves, there is no share on the overrun.

So think about fixed price in that regard and I'm trying to think Rob, I think off the top of my head, I think most other terms and conditions that we negotiated with Lot 5 carried over and so I'm looking at Marillyn here, she was very engaged in Lot 5, carried over into Lot 6 and 7. I don't think we had much to speak of the change of anything there. So I'll probably leave it at that.

Marillyn A. Hewson

Yes. I agree, Bruce.

Bruce L. Tanner

Okay.

Operator

Our next question comes from Robert Spingarn with Credit Suisse. Your line is open.

Ross D. Cowley – Credit Suisse Securities (USA) LLC

Good morning, everybody. This is actually Ross Cowley in for Rob. I just wanted to touch base on the AMDR contract, specifically find out how surprised you were when the award went to Raytheon and whether how the debriefing is going, whether this is something that you could protest?

Marillyn A. Hewson

Well, I'll answer that. From an AMDR standpoint, we were disappointed on the decision by the Government. we did see a decrease last week and so we're in the midst of evaluating the information. But we've had – we've been engaged on the Aegis System for the past 42 years. So we have deep understanding of that program and of the mission. So we were certainly disappointed, but we're still on the midst of evaluation – evaluating information that came out of the debriefing.

Operator

Our next question comes from Myles Walton with Deutsche Bank. Your line is open.

Myles A. Walton – Deutsche Bank Securities, Inc.

Thanks, hi good morning. Bruce, the cash into 2014, outside of the pension tailwind and net income, how should we think about the advances, cash taxes, any of that working capital sensitivities.

Bruce L. Tanner

And so trying to look at some paper I got in front of me, Myles, in terms of the advances. typically, what we project going forward is that our advances will come down. We don't have a huge number of direct commercial contract plans in the 2014 timeframe that would sort of bring typical advance payments with them, most of our international growth next year comes in the form of foreign military sales contracts. So I wouldn't expect to see the starting sorts of advances that we've had in the past that result in our advanced balance going on the balance sheet there.

Working capital wise, I think we're going to see some improvements there, as we kind of go through the production and we obviously have some withholds associated with the business system rule for things like Earned

Value Management System that have been made pretty public that we expect to finalize and that will improve the working capital position associated with those. I think from a thinking or planning perspective, you should think of next year's number, I think being higher than the level of cash that it's going to generate in 2013. I know it's been in the either in a response to question or in my prepared remarks we talked about the potential for looking in the fourth quarter additional pension contributions. Even with that, I'd say we would stay above the $4.3 billion level in 2013 and I think we'll be north of that in 2014.

Operator

And our next question comes from George Shapiro with Shapiro Research. Your line is open.

George D. Shapiro – Shapiro Research LLC

Yes, good morning Bruce.

Bruce L. Tanner

Hey George.

Marillyn A. Hewson

Good morning.

George D. Shapiro – Shapiro Research LLC

The question I have got is two parts. Last years ending funded backlog with $55 billion versus the $82 billion that you quote. Given that the funding is less assured these days, what do you figure that funded backlog will end this year? And then my second one is, I know you've given some color to try and mitigate why sales are only down a few percent next year. But just conceptually, I mean, you'll be down 4% to 5% this year and next year, the budget is worse, the sequestration impact is worse. So maybe a little more clarity on why you think you'll actually decline less next year than this year? Thanks.

Bruce L. Tanner

So George good questions as usual. So I'm doing this a little of the top of my head. You asked funded backlog at the end of last year, funded at the end of this year and maybe embedded in your question was, don't you have more risk, the difference between funded and unfunded. I think the key distinct and there's what's obligated, versus necessarily what's funded. The real issue from a sequestration perspective is, taking those unobligated funds and those are the ones that are really at risk S-3 as I made to comments before about, again why we think we have in 2014 a pretty good handle along what our revenue is going to be. So we don't have a reliance on the unobligated funds turning into sales in 2014.

I don't particularly see an issue was funded backlog balance in the end of this year. I think it will be comparable, either percentage basis or an absolute basis to where we ended last year on a percentage basis relative to the ending backlog amount. So I don't think that's an issue that I am particularly concerned about as we sit here today. Going forward, you asked about my paraphrase, why we feel comfortable with saying we're going to be relatively comparable to the 2013 sales, even though it appears the budget is going down more. You're actually right with that.

Going back to the question, I think, Noah asked, it is a function of our portfolio as to things that I talked about when I described the sequestration impacts. We do expect international sales to grow both on a percentage basis and on absolute dollar basis. Our single largest program, the F-35, as I said, is expected to grow 15%. We have other growth, in particular, Air and Missile Defense products have – and Missiles and Fire Control. And so for all the reasons that I went around the hone earlier by each business area, we feel pretty good about that. I mean, the things that I would think could change that dramatically, George, from what we are expecting to see now as if sort of obligated, under contract programs were terminated or partially terminated. And if that were to happen, sort of all bets are off, but that's not a scenario that we're counting on or guiding towards at all when we give our trend information for 2014.

Jerry F. Kircher, III

Stephanie, I think we're maybe a minute past to the hour here. So I'm going to maybe turn it back over to Marillyn for final thoughts.

Marillyn A. Hewson

Thanks, Jerry. As we conclude today, I believe our third quarter results and increased guidance, illustrate the solid position and performance of the Corporation to provide solutions to customers and value to shareholders. In an uncertain budget environment, our strong backlog of work, our solid balance sheet, our robust cash generation and the exceptional execution of our employees, will continue to propel our Corporation forward. I am confident in our future because of the outstanding performance, innovation and integrity of our workforce, as we support our customers and their essential missions. Thanks again for joining us on the call today. We look forward to speaking with you on our next earnings call in January.

Stephanie, that concludes our call today.