Ladies and gentlemen, thank you, for standing by, and welcome to the Lockheed Martin Third Quarter 2018 Earnings Results Conference Call. [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 third quarter 2018 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 welcome to our call today. As today's release illustrates, we continue to outperform the goals we set at the beginning of 2018, with another quarter of strong operational accomplishments, important new business awards and outstanding financial results. We've seen strong financial performance across the entire corporation. And this performance, coupled with our improved outlook for the remainder of the year, has resulted in us updating our guidance again this quarter.

I'm especially pleased to see our earnings and cash expectations continue to grow as we remain focused on operational performance and delivering long-term value to shareholders. Our third quarter and year-to-date financial performance and improved full year projections are the result of the strength provided by our broad portfolio of offerings as each of our 4 business areas contributed to our updated 2018 financial outlook.

We will discuss the financials in detail a little later in the call, but I do want to highlight two key actions that our Board of Directors took this quarter in the area of cash deployment. First, we increased the quarterly dividend by 10% to $2.20 per share or $8.80 annually, maintaining our long-standing commitment to a strong dividend. Second, we also increased our share repurchase authority by $1 billion, bringing total repurchase authority to $3.7 billion. This level of authority provides additional flexibility to continue to return cash to stockholders through share repurchases if market conditions and our fiduciary duties permit.

Together, these two actions demonstrate our continued strategy of balanced cash deployment and long-term commitment to delivering returns for our stockholders.

I'll cover performance highlights in just a moment, but I want to begin by noting several strategic new business awards that we received this quarter, which position us for long-term growth in our existing portfolio, as well as affording us exciting new opportunities.

In August, our Lockheed Martin Space team received an initial $2.9 billion reward from U.S. Air Force for 3 next-generation missile warning satellites. These overhead persistent infrared, or OPIR, satellites build upon our legacy SBIRS spacecraft with a modernized bus and increased survivability, delivering advanced early warning and improved resiliency. We look forward to delivering these next-gen capabilities with this new opportunity. [Technical Difficulty] competitor contract of over $1.3 billion for the first two GPS follow-on satellites, with a total estimated contract value of up to $7.2 billion for 22 new GPS-IIIF spacecraft. These new GPS space vehicles are designed to provide greater accuracy and improved anti-jamming capabilities, providing the technology upgrades to ensure GPS-III remains the gold standard in navigation, positioning and timing.

Moving to our Aeronautics business area. We secured approximately $1.7 billion in orders for 22 additional C-130J transport planes. The results of the increases included in 2017 and 2018 fiscal year omnibus appropriations legislation. These awards bring our C-130J backlog to 70 aircraft, another example of the enduring demand for this legendary platform.

In Missiles and Fire Control, we were very excited to be awarded the $480 million Air-launched Rapid Response Weapon, or ARRW program, to provide critical design review and production readiness support for new hypersonic weapon. The ARRW contract marks our third 2018 award in this emerging technological area, and when combined with the previously announced Tactical Boost Glide and Hypersonic Conventional Strike Weapon, or HCSW programs, brings the aggregate value of our 2018 hypersonic awards to over $1.5 billion.

We were disappointed, though, at not being selected for 3 large competitive bids this quarter. We believe our proposals represented outstanding technical offerings at our lowest possible pricing. Had we matched the winning prices and been awarded the contracts, we estimate that we would have incurred cumulative losses across all three programs in excess of $5 billion, an outcome that we do not feel would have been in the best interest of our stockholders or our customers.

As we conduct our lessons learned process, we will seek to discover any root cause issues which may lead us to alter our future capture strategies. However, our objective will always be to position the corporation to perform with excellence for our customers while delivering outstanding value to our stockholders.

Our new business pipeline remains robust and our win rates remain strong. The strategic awards I noted earlier contributed to the corporation recording over $18 billion in awards during the third quarter and allowed our backlog to climb to over $109 billion, a new high watermark.

Turning briefly to the Department of Defense budgets. The President signed into law the DoD 2019 fiscal year appropriations act last month, the first time in a decade that an appropriations bill has been enacted prior to the start of the fiscal year. The act provides approximately $670 billion of base budget funding for the nation's security and defense programs. The legislation aligns with the Bipartisan Budget Act of 2018, which provided with an additional $80 billion for national defense over 2 years in fiscal 2018 and fiscal 2019.

The final FY '19 appropriations also reflect continued support for our broad portfolio as funding was increased from the Presidential budget request for some of our key programs, including 16 additional F-35 jets; 14 additional THAAD interceptors, 8 additional C-130J aircraft; 8 additional BLACK HAWK helicopters and 2 additional Littoral Combat Ships. These increases were supported by both House and Senate appropriations committees and reflects strong bipartisan support for these platforms.

Moving on, I'd like to highlight several significant milestones we achieved across the corporation during the past quarter, beginning with an update on our F-35 program. We saw 4 significant events take place this quarter. In September, we finalized an $11.5 billion Low-Rate Initial Production, or LRIP, 11 contract with the Department of Defense for the production and delivery of 141 F-35 aircraft. Notably, we came to agreement on unit prices, which are the lowest in program history, with the F-35A, our conventional takeoff and landing, or CTOL variant, achieving an $89.2 million price, a 5.4% reduction from the LRIP 10 per unit amount. We remain focused on delivering the best value to our U.S. services, international partner nations and Foreign Military Sales customers as we continue to pursue achieving an $80 million CTOL target price.

The F-35 program also continued its maturation process as it was approved to transition into the operational test and evaluation, or OTE phase, in November. The Defense Department had certified the programs readiness to enter the OTE phase, one of the final steps being approved for full rate production.

Also in September, F-35 aircraft participated in their first U.S. combat mission as the U.S. Marine Corps F-35Bs successfully conducted an air strike in support of Operation Freedom's Sentinel ground clearance operations in Afghanistan.

The Marine Corps was the first service to declare the F-35 ready for initial operational capability in 2017, and the aircraft has been deployed as part of the Essex Amphibious Ready Group, enabling enhanced stability and security from international waters and demonstrating the remarkable capabilities of this fifth-generation fighter.

Lastly, on the F-35. We were all extremely proud to see our U.K. Ministry of Defense partner celebrate an F-35B performing its first carrier landing as British pilots touched down on the HMS Queen Elizabeth in the Atlantic Ocean, laying the foundation for the future of fixed-wing aviation aboard the U.K. carrier fleet. The F-35 subsequently took flight using the ship's ski ramp platform and later performed successful night landings on the carrier, both with and without the use of night vision technology. The F-35 and the HMS Queen Elizabeth are at the beginning of the 2-month developmental test process to establish the envelope for the F-35 to operate from the deck of the ship, and we are very happy to be part of these landmark events.

Moving to our Missiles and Fire Control business area. We saw strong domestic and international demand for our tactical missile products this quarter, as well as continued international PAC-3 support in our air and missile defense organization.

In our tactical missiles organization, we were awarded an FMS contract totaling over $630 million to provide Hellfire missiles to the Netherlands and Japan.

Our tactical missiles team also received a pair of awards totaling over $0.5 billion for 42 High Mobility Artillery Rocket Systems, or HIMARS, launchers and associated hardware to be delivered to the U.S. Army and international customers.

Earlier this quarter, U.S. and Swedish officials formalized an agreement to provide PAC-3 MSE missiles to the government of Sweden, helping to increase the country's defensive capabilities and support interoperability with U.S. and NATO forces. Sweden will become the sixth international customer to sign an agreement for PAC-3 MSE missiles, and we look forward to providing our leading-edge missile defense products in support of their national security objectives.

I'll close with our Rotary and Mission Systems business area and discuss several noteworthy achievements from our Sikorsky team. First, the Sikorsky S-97 Raider prototype helicopter demonstrated the ability to fly at speeds exceeding 200 knots during recent flight testing at our Sikorsky development flight center. The Raider aircraft incorporates our Collier award-winning X2 Technology, a suite of capabilities, which include our innovative counter-rotating blade design, fly-by-wire flight controls and advanced vehicle management systems to provide a critical speed and handling quality needed by today's warfighter.

The X2 technology allows for speeds twice that of conventional helicopters, and we look forward to offering this unique solution to the U.S. Army as it begins to revolutionize its aircraft fleet as part of the upcoming Future Vertical Lift program.

I would also like to congratulate the Sikorsky team on an upcoming milestone as October 31 will mark the 40th anniversary of the first BLACK HAWK delivery to the U.S. Army in 1978. The iconic BLACK HAWK helicopter has more than 10 million flight hours, supporting our army customers' brave missions and has played a key role in humanitarian efforts, aerial firefighting and border patrols as well. Over 4,000 BLACK HAWKs of all types are in service worldwide. And I would like to thank the Sikorsky organization for their dedication in delivering this remarkable aircraft to our customers for the past 40 years. And we look forward to continuing this partnership for years to come.

These two significant accomplishments come at a time when we will be recognizing another key milestone. This November, we will mark the third anniversary of Sikorsky aircraft joining the Lockheed Martin family. The Sikorsky organization has expanded and strengthened our corporation's portfolio over the short time, and I would like to thank the entire team for their efforts as we celebrate this important occasion.

With that, I'll turn the call over to Bruce.

Bruce 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 begin with Chart 3 and an overview of our results for the quarter. Once again, we exceeded our expectations for every financial metric in the quarter as we did through the first half of this year. Sales, segment operating profit and cash from operations before making our final pension contribution for the year continued to be strong. The $1.5 billion pension contributions we made in the third quarter completes the $5 billion of pension outlays that we've been discussing all year.

We continued our cash deployment actions in the quarter, returning around $800 million of cash to our shareholders through a combination of dividends and share repurchases. And we grew our backlog to a record $109 billion in the quarter, with all 4 business areas contributing to that growth. Based on our performance in the quarter, we expect strong results for sales, segment operating profit, earnings per share and cash from operations for the full year, as we'll show in a few charts.

We were pleased with how our financial results are shaping up thus far in 2018, and we'll be discussing how our performance this year is carrying over into next year when we get to our charts showing preliminary trends for 2019 later in the presentation.

Turning to Chart 4. We compare our sales and segment operating profit in the third quarter of this year with last year's results. I'll note for comparison purposes that the third quarter of this year has 14 weeks in the accounting period while last year's third quarter had 13 weeks in the accounting period, and this situation will reverse itself in the fourth quarter when we have 13 weeks this year and will compare to 14 weeks in the fourth quarter of last year. Even without the extra week in the quarter, our results exceeded our expectations. With that background, sales grew 16% compared with the same quarter last year to $14.3 billion, continuing the momentum we had in the first two quarters, while segment operating profit increased 23% over last year's level to nearly $1.6 billion.

And all four business areas contributed to the significant increases in both sales and profit in the quarter, while the margin increases in the quarter were driven primarily by RMS due to improved performance in our Sikorsky and integrated warfare systems and sensors lines of businesses and by Space due to improved performance in our government satellites line of business. On Chart 5, we'll discuss our earnings per share in the quarter. Our EPS of $5.14 was $1.82 or 55% higher than our results last year, driven by higher sales volume, the margin improvements that I just discussed and a lower tax rate in the quarter compared to last year.

Moving on to Chart 6. We provide our revised outlook for the year. With only the fourth quarter left in the year, we are providing our best point estimate of results for the entire year rather than the ranges we have provided in previous quarters. We expect sales to be around $53 billion for the year, near the top of the guidance range we provided last quarter and 6% higher than our results in 2017. At $5.8 billion, our forecasted segment operating profit will exceed the top end of our guidance range last quarter, resulting in a 10.9% margin, about 70 basis points higher than last year's results.

Our FAS/CAS pension adjustment remains unchanged at a little more than $1 billion. Our earnings per share is expected to be around $17.50, also above the high end of our previous guidance range, recognizing the strong performance in our business segment operating profit as well as a lower tax rate in our lower estimates, which I'll discuss further in a moment. And we're increasing our outlook for cash from operations by $100 million to be equal to or greater than $3.4 billion as we expect a large portion of our earnings increase to be billed and collected before year-end.

Chart 7 provides a reconciliation of our earnings per share outlook this quarter compared to last quarter. Operational performance is expected to drive a $0.40 increase in EPS, driven by higher segment operating profit as a result of higher sales volume and margins in our business areas. Taxes and other are expected to add another $0.20 in EPS, with most of that increase coming from a lower tax rate as we continue to reflect the latest understanding of the tax legislation passed last year. We now expect our full year effective tax rate to be between 13.5% and 14%. Together, these changes represent an expected $0.60 improvement from the midpoint of the EPS range we provided last quarter to a new outlook of $17.50 per share.

Chart 8 shows our new outlook for sales by business area for the year, also with point estimates for each of the business areas rather than the ranges we provided in the prior outlook. We are increasing our sales outlook by $650 million compared to the midpoint of our last guidance. We expect it to be near or slightly above the high end of the guidance range from last quarter, continuing the strong results we've seen so far this year.

On Chart 9, we provide a similar view of our new outlook for segment operating profit by business area for the year. We're increasing our segment operating profit outlook by $150 million from the midpoint of the range we provided last quarter, and our point estimate is above the high end of that range. Three of the 4 business areas are expected to exceed the high end of their prior range, showing the broad-based nature of our performance improvements.

On Chart 10, we provide our preliminary look at our 2019 trends. We expect our 2019 sales level will grow 5% to [Technical Difficulty] '18 sales, which equates to approximately a 6% to 7% increase over the midpoint in the 2018 guidance range we provided in July. We expect our segment operating margin will remain strong at between 10.5% and 10.8%. This margin level assumes similar performance in our legacy programs in all business areas with some dilution resulting from the growing number of new start programs, as the increases in our backlog levels would indicate.

We also expect to have lower equity earnings associated with the ULA business as a result of the number and mix of launches expected in 2019 compared with 2018. We estimate that our cash from operations will be at least $7 billion, as we've noted in previous calls, and we have no planned pension contributions next year.

We also plan to have at least $1 billion in share repurchases, about the same levels we expect to have in 2018, more than offsetting any planned share issuances in the year. And similar to 2018, we have a debt maturity coming due next year worth $900 million.

Moving to our FAS/CAS outlook. We expect our 2019 FAS/CAS adjustment will be approximately $1.5 billion or about $500 million higher than the adjustment for 2018. This estimate assumes a discount rate at the end of the year of 4.125% or 50 basis points above the 2018 rate. Based on our performance to-date, we are assuming a 1% return on our assets for the full year. And going forward, we are reducing our long-term asset return assumption by 50 basis points to 7% per year.

All told, we expect to see continued strong growth in the 2019 based on the mix of follow-on extensions of our legacy programs and a number of quality, new and exciting orders that demonstrate the long-term strength of our portfolio.

And finally, on Chart 11, we have our summary. We've seen strong performance from all of our business areas this year, and I'm especially pleased with our year-to-date orders, both in quantity and quality. Our full year outlook has improved in all financial metrics, and we look forward to continued growth in 2019.

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

Question-and-Answer Session

Operator

[Operator Instructions]. And first, we'll go to the line of Myles Walton with UBS.

Myles Walton

So a quick question for you, first on the margin side. So the implied mix that you're talking about, can you give us maybe quantification of how much the growth in cost versus fixed price and also maybe by segments, a bit more color on where the 10 to 50 basis points of headwind is coming from?

Bruce Tanner

Yes, thanks, Myles. I'll take that one on. I think the simplest way to understand it is we are seeing pretty much new starts in all of our business areas, and you've seen some of that in prior orders that were released. And frankly, some of that you haven't seen because some of that has occurred on some classified contracts and actually multiple business areas. So I won't be able to get into probably as much detail as you would like in that discussion, but suffice to say that that's actually causing some of that margin pressure that we're seeing going forward as well. The largest single item that is driving the margin reduction next year, though, is actually our ULA equity earnings. Those are actually going -- we expect those to be down nearly $150 million or so from this year's estimate of the equity earnings from ULA. And you should think of that as a pretty significant reduction in both the launch quantity in terms of the number of vehicles launched, but probably more importantly, a pretty significant change in the mix of those launch vehicles. So we have more, for instance, Delta IV launches in 2018 than we expect to have in 2019. Those are obviously the most profitable launch vehicles in all of ULA's portfolio.

So that's the biggest driver. But as I said, without going into all the various pieces, maybe I'll tell you what. I'll try to hit just a couple of the business areas maybe very quickly going into next year. I'll give you more detail on this, Myles, when we talk to you in January. But as far as the margins in aeronautics, we actually expect those to be fairly similar next year to what they are this year. And that kind of goes to the comment I think I made in my prepared remarks, where we actually do expect to have legacy programs, as we're calling them, have increases in margins year-over-year. But start-up activities, including by the way, I'll count the F-16 production program as a restart there. We've been out of production for some 3 years, so that's one example of where I would cite we have production I can talk about. Other programs in some of the classified, in the Skunk Works areas, the contract activity that's driving us to have kind of a flat margin going forward. Our Missiles and Fire Control margins, probably maybe slightly lower, comparable to slightly lower than it is this year.

And again, the same story is within aeronautics. Legacy programs are actually expected to have margin improvement. We're actually seeing pretty good growth in our SOF GLSS contracts, higher than we expected, quite honestly. And you recall that contract brings lower margin than in the overall portfolio of Missiles and Fire Control. Probably the biggest single driver, though, at Missiles and Fire Control is a whole bunch of new starts. And you should think of those as hypersonic programs, new starts, as well as a number of other programs, including classified activity that's going on there that we've talked about orders being received previously on this call. RMS, right now, we're looking at actually pretty comparable margin going forward. So really, you should think of the first 3 business areas that I've talked about, ARRW, Missiles and Fire Control and RMS all having comparable -- maybe slightly less in Missiles and Fire Control. The biggest driver, as I said, earlier, is Space Systems or Space, and that's primarily because of the ULA equity earnings there. The rest of the portfolio is actually performing about as expected next year compared to this year.

Operator

Our next question is from David Strauss with Barclays.

David Strauss

I wanted to ask a multiple-part question on F-35. It looks like F-35 in the quarter grew fairly significantly well above kind of the delivery rate growth. Can you talk about kind of how far in terms of the revenue growth we're seeing, how that breaks out between production and sustainment? Kind of how far ahead we are based on going from 91 deliveries this year to 130? And then last one, on your cost curve, obviously, the price per LRIP is coming down like 5%, 6%. Can you talk about your cost curve? What kind of learning you're seeing from a cost perspective?

Bruce Tanner

David, I'll take that one on as well. So you had a lot of parts in that question. I'm just going to try to keep up with them. Relative to revenue growth on F-35, I think what you surmise is pretty accurate. And we did have some pretty significant growth in the quarter. I think we were double-digit, actually a little more than double-digit on F-35 in the quarter. As we look, and maybe that's the heart of your question, what does that look like next year, I think, you said relative to the ramp-up from 91 to about 130 aircraft. We would expect F-35 next year to also grow probably at the double-digit, maybe a little bit higher than that. And that's for both production and sustainment activity, David. And the one wildcard that I'll mention that really did surprise me as well as we were getting ready for this call is that actually the development activity on F-35 is going to grow at double-digit rate next year. So part of that is we had a pretty significant reduction in the older SDD contract from 2017 to 2018, but we're starting to see more and more sort of new noncore SDD development activities being added to the contract. And that's actually growing, as I said earlier. That's growing, the development portfolio, higher than double-digit from 2018 to 2019, so that's kind of a pleasant surprise for us.

Cost curve, I don't have the learning. Maybe Marillyn does at the top of her head. I want to say we were at the mid-80s to maybe a little bit higher percent learning curve on F-35. I think that's about right that we've been running about that level, almost since the LRIP 1, David. So we're still maintaining that. At some point in time, that will start to level out as we've kind of branched all we can out of our learning curve, and that's where we need to have some potential investments to get some sort of step improvements going forward there. But at least, right now sort of year-to-date and we're still -- or Q-to-date and we're still seeing that trend. Think of it as mid- to higher 80% learning curve is what we're experiencing on F-35. by the way, very much in line with what we've seen on other legacy production programs, if not slightly better.

Operator

The next question is from Rob Stallard with Vertical Research.

Robert Stallard

Marillyn, I just wanted to follow up on your comments regarding those programs you've lost in the quarter and the potential $5 billion hit. Are you concerned that this is changing the landscape for defense contracting, and the sort of low ball bids could make your future profitability less attractive?

Marillyn Hewson

No, not for us. I mean, that's not the kind -- that's not what you would expect from Lockheed Martin, and that was the point in my opening remarks is that we're going to pursue good business for this company and being able to perform at what we say we can perform, too, for our customers. So that's the key for us. How other competitors behave in this environment, I really can't speak to you. You'll have to ask them.

Robert Stallard

That was more from the other direction. Is this potentially what the customers are now expecting as they see these prices out there?

Marillyn Hewson

Well, we have seen -- we've talked about this in the past call, so that -- we obviously made a clarification on what you're asking. We do see that the affordability is a very important element for them, and a lot of these best value procurements, when we know that we've got a good technology solution when it comes down to lowest cost technically acceptable -- lowest price technically acceptable, LPTA-type decision, we are seeing -- we are assuming that's happening because if you come in with a technical solution that's good and comparable, and you meet all of those elements, but then they just go for lowest price and ultimately, that could be the opportunity that the government is taking on affordability. And they cite that. We've seen in the media that they would cite that they've gotten things at much lower than they anticipated. Bruce, anything you want to add?

Bruce Tanner

The one thing I want to add, Marillyn, is -- Rob, I think I wouldn't necessarily draw a long conclusion from 3 awards. I'll tell you, those were disappointing for a lot of reasons. But the fact that they were really decided, all 3 of them, on sort of a LPTA basis didn't help the situation. It's not getting -- I would argue, the best capabilities for the warfighter in the hands of the warfighter. What else? I don't think that's entirely universal amongst all the competitions that we've seen this year. And we frankly won some competitions where we weren't the highest price. So I do know that you can automatically, as I said, draw a conclusion that, that's necessarily a change from on every program that's going to be competed going forward. So it's not a one-size-fits-all, if you will.

Operator

And our next question is from Jon Raviv with Citi.

Jonathan Raviv

Bruce, some of the commentary you provided on the margin, I was wondering if you can give us some perspective on sales growth, including on some of the single aisles, which impacted 2018. How [indiscernible] what the prospect is for growth to accelerate in '19?

Bruce Tanner

Yes, so as we said, we experienced growth all throughout 2018. And we talked about that on previous calls as far as how we came out with roughly a 2% expectation, we ended up actually having 6% growth over 2017. And I think in the past, I attributed that to the significant plus-up in terms of the omnibus increases. Many -- higher rate of awards, and especially in the first half of the year than what we were expecting to have and an earlier turn-on for a lot of those awards than what was historically we've seen. This, I think, speaks to the speed concept that Secretary Mattis always talks about now, is getting things to the warfighter's hands quicker. So I think that was part of the reason we're seeing in 2018 as high as we are. 2019, I'll try to do the same, if you will. I think the highest growing business area is going to be Missiles and Fire Control. I think they're going to grow probably a little bit north of double-digit, maybe not much more than that. Next up is aeronautics, which collectively, I think, is probably going to grow probably in the high single digits, not quite the double-digit level but that's still good growth there.

RMS and right now, both RMS and Space are expected to be sort of comparable to where our results were for 2018 or where they're expected to be for 2018. I think that there's a business area or two that I could point to, where there may be some opportunity to get some growth beyond that. The comparable level is probably in both of those. I think we had some potentially good news, for instance, on the Canadian Surface Combatant competition and depending on when that gets fully awarded. I won't go through the entire process. That has the potential, I think, to create some growth going forward. So I'm watching those faces, but you should think of it, Jon, as really the Aeronautics and Missiles and Fire Control sort of carrying the heavy load in terms of sales growth, with Space and RMS somewhat comparable expectation to where they are this year, with hopefully some upside to that level.

Operator

Next question is from Rich Safran with Buckingham Research.

Richard Safran

Bruce, I think this is going to be for you. And I'm going to ask you a bit of a forward-looking question here. And if you feel you can't answer it, just tell me and I'll ask something else. The long-term 2018 to 2020 cash from ops guide was not in the slides. So I thought I'd ask you about that. Would you comment on your 2018 to 2020 cash from operations trends? And would you care to comment on 2021? And if you can't answer it, would you include in your answer just a general discussion of major programs, about what's baked into your guidance and what's not?

Bruce Tanner

Yes. Thanks, Rich. Let me figure out how to better navigate through your question there. So we've given sort of 3-year numbers in the past. We're actually going to talk about that probably more in the January call, but I'll give it a shot here as well. So in the past, we've said that we had expected about $3 billion in 2018. We're ending up at about $3.4 billion, so a pretty good beat relative to our expectations there. We still see in 2000 -- I would say, 2019 we're providing a trend information of at least $7 billion. We still see $7 billion, which we teed up in one of those charts that we briefed previously in 2020. And you should think of that, Rich, as we're actually seeing some pretty good-sized working capital growth in both 2019 and 2020 associated with a lot of our new start programs. It so happened that it happens on a time when it's sort of fortunate for us because it happens in 2 years where we don't have pension contribution, so we're kind of able to have nice, robust cash in both '19 and '20, even while we're growing working capital. The fortunate thing about 2021 is that working capital starts to actually reverse itself, so we actually start to recover a lot of the working capital growth we're actually seeing in '18, '19 and '20.

And at least as we sit here today, Rich, and I'm not trying to give a 3-year guidance number for you, but I would think that the 2021 cash ought to be fairly comparable to our cash from operations in 2019 and 2020. And that's despite the fact that we start making pension contributions at a pretty good magnitude in 2021, somewhere north of $1.5 billion or so. So you should think of that as we're recovering working capital in that time frame. We're also starting to have higher depreciation recovery in terms of cash recovered versus the capital expenditure increases we've seen in the last couple of years, and we expect to see next year as well. And then lastly, the profit growth we're getting from the sales growth that we talked about earlier. So sort of those three things is what's giving us a pretty -- as we sit here today, at least, I'll say a fairly good expectation that we can hold at the $7 billion level, at least as we're looking out for the next 3 years or so.

Operator

Our next question from Sam Pearlstein with Wells Fargo.

Samuel Pearlstein

I just want to follow up on that comment you just made about capital spending. And I guess I'm trying to just think about that as we project forward, how much does it increase and when does that increase stop? And is this new facility, that go with a lot of the wins that you've seen to-date? I mean, can you just characterize where that money is going?

Bruce Tanner

So Sam, I'll take that. It seems like I get this question every year, and every year it seems like I'm saying next year is sort of the peak of capital expenditures. And unfortunately, that's not the case now. But I would argue this is all good news. Capital expenditures next year, probably going to be $1.5 billion or more than that, slightly, so a pretty good increase from this year. At least, in our 3-year planning, the 2020 capital expenditures are actually higher than 2019. And then, they come down actually fairly dramatically in the 2021 time frame. So our free cash flow will start to look better in 2021 because of that. And most of it -- you kind of nailed it, Sam. Think of this as the continuing ramp-up of both buildings and tooling at Missiles and Fire Control to support capacity increases for weapons and air missile defense programs. So I think I've talked about in previous calls that we're seeing significant demand to increase production rates on a number of our programs, particularly the weapons but not exclusively weapons, also air missile defense. And I like to use the example of Hellfire. I think we're building similar -- I think the capacity numbers we're being asked to support, we're going to go up to like 11,000 per year or more. PAC-3, we've got a request that could potentially go up to 500 missiles per year.

So we're seeing some fairly good-sized requests in terms of additional capacity. That's the good news. And the good news, I guess, also is that it takes capital to support those requirements in order to support those increases that will result in growth in the out years once that capacity comes online. So that's what's going on at Missiles and Fire Control. At Space, we're completing sort of a fairly large infrastructure support to have a brand-new sort of manufacturing facility for larger satellites that will actually result in a more efficient build of those satellites as well. And that sort of starts to finalize, I think in 2019. And then finally, we actually are seeing a ramp-up of both buildings and the tooling in those buildings at Aeronautics, primarily to support our Skunk Works or ADP programs out in the West Coast. So this is where a lot of the stuff that we can't necessarily talk about is going on. But it does take added infrastructure to support that going forward. So the three big chunks, that's the reason for the capital increases over the next couple year. Marillyn, I don't know if there anything else I left out.

Marillyn Hewson

I think you covered it, Bruce. Thank you.

Operator

And next, we'll go to Doug Harned with Bernstein.

Douglas Harned

A question that I think -- I feel like just has to be asked right now is given the political situation with Saudi Arabia, can you give us a sense of what your backlog exposure is to Saudi and to UAE? And how are you thinking about the current political environment and the relationship with Saudi? How do you work with that with your portfolio?

Marillyn Hewson

Yes, thanks for the question, Doug. I'll just first remind you and the rest of the folks on the call that most of these agreements that we have are government to government purchases, so anything that we do has to do with following strictly the regulations of the U.S. government. In a way, that includes sales to Saudi Arabia. And we do business in more than 70 countries, so this is just the way we do business, generally speaking, is through government to government procurements. And they certainly are the ones that we've been talking about, the weapons sales we've been talking about to Saudi Arabia. We continue to make progress on the programs that we had talked about from the May of 2017 announcement way back then. For example, we announced this quarter that our Multi-Mission Surface Combatant program with Saudi Arabia has moved forward with some additional -- an additional $450 million contract for detailed planning and design for their multi-mission combatant. That was already on the contract. And then beyond that, we'll just work with the U.S. government as they're continuing their relationship with Saudi. In terms of the outlook, Bruce, do you want to take that?

Bruce Tanner

Yes, I'll take a shot at that, Doug. So I look at this. And really, we were thinking we possibly could get a question on this during the call. But we've really just had, as Marillyn said, the one significant order so far, which was for the MMSC. So think of that as a next-generation LCS, if you will, but more capable ship. The largest order that we've been waiting on obviously, is THAAD, and that has not taken place yet, not sure when that will take place. But the interesting thing about the THAAD order is while it brings a significant increase in the backlog, the resulting sales, profit and cash flow with that order are very much pushed to the right. And you should think of that, Doug, as it's because there's a dependency on the radar that has to have a technology refresh, that is actually some years out into the future. So even with the large orders, we would not have significant sales in the near term because those missiles would be arriving too soon to be supported by the actual radar that needs to be refreshed, as I said. So I think the initial operating capability in Saudi is like 2023, if I'm not mistaken. And just to give you some idea of the level, I don't have -- your question was on backlog. I don't have the exact level of backlog, but I did take a look at sales projections going forward for KSA, and I think we have in 2019 about less than $0.5 billion of sales plan. And I looked out into 2020, it's just less than $900 million of sales. So not a huge amount of dependency on the activity even though the opportunities we've described are much larger than that, obviously.

Operator

The next question is from Peter Arment with Baird.

Peter Arment

Maybe, Bruce, just following on to that. Maybe you could just update us on some of the outstanding international contracts that you're expecting maybe before the end of the year and just any levels of backlog, where you sit, that you're finishing up?

Bruce Tanner

Yes. Probably not so much international orders as fourth quarter is always the quarter where we get quite a bit of domestic orders from the U.S. government. It's the first quarter of the fiscal year, and that tends to have quite a bit going on, with new funds being left there. The biggest order, obviously, by far is -- and I should have said that does include international orders as well. And there is the F-35 economic order quantity or block buy. You should think of that as about 219 aircraft comprising lots 12, 13 and 14, both for U.S. aircraft, all 3 variants, as well as a significant amount of international aircraft as well. So that's, obviously, the biggest single order. You should think of that as approaching $30.5 billion or so. We also expect to get the added FY '18 20 aircraft that came on the FY '18 appropriations in the fourth quarter as well. And then, we'll get quite a few -- I'll say the normal, as I said, first quarter, the fiscal year orders for things like the PAC-3 fiscal year '19, probably another block buy of THAAD missiles. All the normal orders have sort of come up with that fiscal year.

We're looking at actually growing backlog in large part because of the -- we actually have a record backlog, as Marillyn said and as I've said, in the third quarter, but we expect that number will exceed $120 billion by the end of the year, primarily because of what we just talked about on the F-35 block buy but not obviously exclusive to that. Going forward, in the 2019, I won't go too forward into the year, but we would expect to hopefully get -- at U.S. international, we'd expect to see an F-16 Slovakia order next year. I think we have next year out of the 24 C-130s, that we expect to get probably about 11 will be international aircraft and 6 of those hopefully for Germany in that category. Let's see, what else, I'm thinking out loud. That's probably enough for right now. Like I said, a lot of the other orders in our business areas are really coming from domestic sources, like some Orion orders. We're going to get 2 -- we'll, I can't think what the E stands for. It's the flight of the Orion.

Marillyn Hewson

Exploration.

Bruce Tanner

Exploration something. We already got 2 of those orders on Orion next year, so it's a pretty good-sized order within our Space business. And again, as I've mentioned earlier, Peter, we have the potential for closing on the Canadian Surface Combatant, which is a huge program. I think that's probably the largest shipbuilding program in the world once it starts, and we will be the integrator and combat system provider for that. I think the total content potentially that comes out of that is north of $7 billion. So wouldn't expect to get that all in one fell swoop in an order in 2019, but that will be the initial start of something that large.

Operator

Our next question is from Rajeev Lalwani with Morgan Stanley.

Rajeev Lalwani

Marillyn, I wanted to come back to you, I guess ask you another political question. There's been some discussion recently about lower defense budgets for fiscal '20. I think it's like 5% or so of the decline. How do you interpret that? And do you have any insight as to what the base that may be using to step down from? And if it is some sort of contraction, how do you think Lockheed is positioned? What are the risks and opportunities we should be thinking about?

Marillyn Hewson

Thanks for the question, Rajeev. I guess as we look at fiscal year '20, right now the President -- that future year defense program input that came out earlier this year was showing an increase -- a modest increase in FY '20 funding levels, and we'll just have to see what's actually submitted in the presidential budget. That doesn't come in until early next year. We'll wait to see. But I'll just remind you, it was very healthy in FY '18 and '19 with -- giving not only us, but our industry counterparts, a lot more visibility. And as you know, we have long-cycle business, and so we've got a lot of things in motion now as we would be looking into 2020. We're always mindful of the BCA caps because they come back into play in 2020 and 2021. And we're always [indiscernible] with our lawmakers to [indiscernible] and they need to address that. And they have been addressing that for these two year bipartisan budget cap agreements that they put in place. So hopefully, they will continue to do that because Secretary Mattis and the Trump administration have highlighted that we've got to continue to modernize our military. Now I do know that the President did come out and asked all the departments across the government to look at a reduction of 5% in their spending, and that's just a way to try to focus on affordability and reducing cost, but we'll see how they come back with DoD because they have also been very strong about the need to focus on defense spending and modernizing our military. So we'll see how that plays out. But back to my point earlier, right now we're seeing a modest increase for FY '20. Who knows, it could be even higher because of the modernization that needs to happen.

Operator

Next, we'll go to Seth Seifman with JPMorgan.

Seth Seifman

Bruce, I wanted to follow up on some of the comments you made about cash and working capital. And so first of all, if we think about bridging the cash from, if we thought about kind of $3.5 billion or so of operating cash flow this year and then not having to -- no pension contributions would probably get you pretty close to 7. And then, your underlying operating profit growth is probably another 200 or so after tax. And then, the working capital kind of takes that -- takes a little bit of chunk out of that. Is that, at least for your initial guidance, which I assume is probably -- you want to take account of -- be a little bit conservative. But is that kind of a -- are those the big pieces in terms of how we get from last year to -- or this year to next year?

Bruce Tanner

Yes, I think you've got it pretty well nailed, Seth. And the only thing I might throw out there is we'll get, obviously, a little bit lower tax -- cash taxes paid because of deductibility of future pension contributions that we'll be making in that time frame as well.

Operator

The next question is from Rob Spingarn with Crédit Suisse.

Robert Spingarn

So a couple of questions, Bruce, for you. Just on the F-35, I know you talked about the learning curve and Marillyn did as well, but you did have this tremendous incremental margin in the quarter, best in 3 years. And if you could just talk to how that changes as that learning curve flattens, I think you were about 24%. I'm sure there were some maybe unusual things in there. But if you talk a little bit about that margin trend and how we see that going forward. And then separately, is there -- with the volatility in equity markets, is there a return on assets level or underperformance that would require return to ERISA contributions in '19 and '20?

Bruce Tanner

Yes, let me take the -- well, I'll think about your second. Let me take your first one there. So we did have some pretty good step-ups, or risk retirements as we call them, on F-35 in the quarter. You should think of that as mostly, I'll say getting to sort of an annual review of older production contracts that took place in the third quarter. So I think the step-ups we have, the biggest ones were actually on LRIP 8 and LRIP 9. And that's just sort of taking both of those programs, I think -- that's just sort of taking both of those programs from where we had booked profit up to date to sort of where we expect to be at contract closeout. And that happened to be in this quarter. And just given the size of those contracts and the size of the difference we had and where we were booking versus where we expect to be at completion, that ended up being a pretty good-sized risk requirement.

Trend going forward, as I said and maybe it wasn't clear, but this is one of those legacy programs that I would think we'd have the ability to do a little bit of margin improvement, and we actually did cross the 10% ROS level in 2018 for the entire program, which we've been talking about for a long, long time that, that was sort of the year we were targeting, and we actually got there this year. I think there might be some potential for incremental improvement going forward. But I think more of the story of F-35 is just going to be the volume of the -- or sort of similar to maybe slightly improving margins going forward trend-wise, as we would characterize it. As far as the pension funding and the return on assets it could drive, I think at the 1% level, I think, Rob, that would probably drive maybe a couple of hundred million dollars of funding in the 2020 time frame. We've talked previously about having 0 contributions in both '19 and '20. I think we're now seeing probably a little bit of a required contribution in 2020, which by the way, we did not have when we first came out with the $7 billion in both of those years. So I think we'll be able to offset -- more than offset that going forward and still maintain the $7 billion we said even with the now $200 million or so of contribution.

Operator

The next question is from Joe DeNardi with Stifel.

Joseph DeNardi

Marillyn, just a question from a corporate risk standpoint. I think if we were to go back several years, the expectation was that F-35 would maybe get to 20%, 25% of total sales. It seems like it's marching higher than that. I'm just wondering at what point in terms of its contribution to revenue or earnings it would become unacceptably big just in terms of contribution to the total company?

Marillyn Hewson

Well, first of all, I don't think it growing in sales is unacceptably big to the corporation, but we like to see it continue to sell all around the world as we've said. We like to see it go the way of the F-16, which, as you know, we've sold over 4,500 aircraft around the world. And today the F-35 program of record is around 3,200, so we hope to see it to continue to grow at that level. I understand your question, though, it being a large element of the corporation. And it really is a program that has -- if you look at it, it's not a single customer and has broad-based support. It's a global product, so not only do we have the domestic customers across fleet services, but we have today with 9 international -- 8 international partners and the 3 FMS customers and many more. They're making the decision on their fighter aircraft procurements that I think they will find the best choice is the F-35, hopefully. It's going to continue to sell and it's broad-based. So even though it is a big program relatively speaking, when you consider the customer base, it's -- I think that helps mitigate the risk. In addition to that, we're seeing a lot of -- yes, as I said in my opening remarks, we're seeing a lot of growth in all elements of our business. So every business area contributed to the growth for this quarter and for our outlook for the year, and we'll continue to see growth. We've got a lot of new programs across the business, and they will help to likewise mitigate the risk of one single program. So I feel very comfortable, and I'd like to see the F-35 sales continue to grow.

Greg Gardner

Well, John, thank you very much. We're actually a little bit past the hour. With that, I'll turn it over to Marillyn for some final thoughts.

Marillyn Hewson

Sure. I'll conclude the call today. And I want to conclude just by reiterating that the corporation had another strong quarter, and we consider ourselves very well positioned to deliver growth and substantial value to our customers and our stockholders as we progress towards the successful closure of 2018 and as we look ahead into 2019. So I want to thank you all again for joining us on the call today, and we look forward to speaking with you on our next earnings call in January. John, that concludes the call for today.