Good day and welcome, everyone, to the Lockheed Martin First Quarter 2017 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. Greg Gardner, Vice President of Investor Relations. Please go ahead, sir.

Greg M. Gardner - Lockheed Martin Corp.

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

Statements made in today's call that are not historical fact are considered forward-looking statements and are made pursuant to the safe harbor provisions of federal securities law. Actual results may differ materially from those projected in the forward-looking statements. Please see today's press release and our SEC filings for a description of some of the factors that may cause actual results to differ materially from those in the forward-looking statements.

We have posted charts on our website today that we plan to address during the call to supplement our comments. Please access our website at www.lockheedmartin.com and click on the Investor Relations link to view and follow the charts.

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

Marillyn A. Hewson - Lockheed Martin Corp.

Thanks, Greg. Good morning, everyone, and thank you for joining us on the call today. We are pleased to have you with us to review our first quarter results.

As today's release detailed, we had a solid quarter operationally and financially with strong top-line growth and outstanding cash generation. I would like to take this opportunity to thank our team for their continuing efforts, as we focus the corporation on growth, successfully delivering solutions to customers and value to stockholders.

While Bruce will cover the financial results in detail a little later, I wanted to touch on several highlights for this quarter. First, our operating profit and earnings per share were negatively impacted by two earnings adjustments that I will comment on in a minute. Our EPS of $2.61 equaled that of last year; however, our EPS would have been $3 per share without these adjustments. Second, our cash from operations was strong in the quarter and we increased our outlook for the year. And lastly, we returned over $1 billion to stockholders in the form of dividends and stock repurchases.

I'd like to take a moment to comment on the two earnings adjustments that occurred this quarter, which caused an unanticipated negative impact to operating profit and EPS. The first was a charge associated with an international C4I contract to produce the world's first end-to-end integrated air and missile defense system. Our solution to date has proven to be less mature than needed for this highly complex effort and we are working with the customer to fulfill their requirements. We do believe, however, that once completed, this system has the potential to bring these uniquely integrated capabilities to other customers around the world.

The second item is a non-cash impairment charge related to an international joint venture in which we participate. During the first quarter, the venture in which we own a minority interest, determined that reduced business prospects required it to impair certain assets. As a consequence, we recorded our proportionate share and this resulted in the other charge you saw in our earnings release today.

Finally, I am pleased to report that during the first quarter, we were able to arrive at an overall economic agreement for F-35 LRIPs 9 through 11, that allowed us to accept the unilateral pricing for LRIP 9, complete negotiations for LRIP 10 and establish cash payment terms for all three lots that were improvements over previous positions. It was the overall bundling of economic considerations and resulting improved cash terms that enabled us to increase our cash outlook for the year that you saw in our earnings release.

We will continue our strong emphasis on growth, cash generation and shareholder-friendly actions as our business areas continue to provide products and services that are in great demand by our customers.

Before discussing operational highlights from our business areas this quarter, I'd like to outline the status of DOD budgets. At this time, government spending remains limited by the continuing resolution that is set to expire on April 28. As you know, the continuing resolution, or CR, limits funding to prior year's levels and prohibits new programs from starting.

Discussions are underway to extend the CR as Congress continues to debate the regular appropriations bills. We are hopeful that these discussions result in an approved FY 2017 Defense Appropriations Act as we feel a further lack of budget clarity could have longer-term consequences for our armed forces and our industry. And we continue to urge our country's leadership to reach an agreement.

There are however, several encouraging indications that our nation's leaders are aligned with the need for a focus on defense spending. First, the House recently passed the FY 2017 appropriations bill, and it is currently residing with the Senate. This bill, which is in compliance with the Bipartisan Budget Act of 2015, also supports vital equipment procurement, with increased spending called out for BLACK HAWK helicopters, as well as additional F-35s. Similarly, we are pleased to see President Trump's 2017 supplemental defense appropriations submission and the administration's initial FY 2018 budget outline, or skinny budget; both request funds in excess of the Budget Control Act caps.

Last month, I attended the Munich Security Conference, where well-respected leaders from the U.S. and participating countries echoed the theme that the international security environment has become increasingly more volatile. Recent events around the world have only served to confirm this sentiment. We, as a nation, need to recognize these threats and provide our military leaders relief from current budgetary constraints and allow them to address the challenges they face in defense of our country and our citizens. We remain hopeful that progress will continue to be made in this area, and upcoming legislation will include the increases necessary to continue to equip and maintain our fighting forces.

Moving to operations, the quarter contained multiple mission success events, and I'd like to feature one each from our Aeronautics, Missiles and Fire Control, and Rotary and Mission Systems business areas. As some of you may know, this past February, the U.S. Air Force held their premier air combat exercise, Red Flag, at Nellis Air Force Base outside Las Vegas, Nevada.

This year's training event featured, for the first time, the F-35A conventional takeoff and landing, or CTOL, variant, which was placed into service following its successful initial operating capability declaration in August of 2016.

After flying over 207 sorties, the fleet of 13 F-35A jets posted an impressive success rate of 20 to 1 against the highest level threats known in the simulated contested environment. Just as importantly, the aircraft's stealth capability and electronic warfare suite allowed it to eliminate ground-based surface-to-air missile installations, effectively securing the battle space and providing unparalleled situational awareness.

In addition, the F-35 flew alongside the F-22 Raptor and joint and coalition forces, including participants from the Royal Australian Air Force and the United Kingdom's RAF, demonstrating the important interoperability this generation platform provides.

Lastly, and just as significantly, the CTOL jet excelled in the maintenance aspect of the exercise. The F-35 and its Autonomic Logistics Information System, or ALIS, proved to be a highly reliable weapon system, achieving a mission capable rate well above 90%, and far surpassing legacy aircraft averages of 70% to 85% availability during the high ops tempo environment of Red Flag, a design quality that has been recognized by users as a true differentiator of this product. We believe the success of this event continues to highlight the unprecedented abilities of the F-35, and we are proud to produce the most capable and reliable aircraft in the world.

Turning to our Missiles and Fire Control business area, I'd like to highlight a noteworthy milestone that occurred this quarter. Last month, we were honored to have our long range anti-ship missile, or LRASM, selected as the Aviation Week Laureate Award winner in the Defense category for its technical achievements in meeting an urgent operational need of our warfighters. LRASM is a precision-guided, anti-ship standoff missile based on the Extended Range version of our Joint Air-to-Surface Standoff Missile, or JASSM-ER variant. LRASM is currently being developed and integrated for operational capability on Navy and Air Force platforms.

Also, in collaboration with our Rotary and Mission Systems business area and their vertical launch system technology, our Missiles and Fire Control team initiated development with our own investment funding of an innovative surface launch solution that can be deployed from ships at sea, providing the U.S. Navy with new anti-surface warfare capability as part of their distributed lethality concept. We were pleased with this award recognition and with our ability to continue to bring our company's capabilities and collaboration to bear for our customers and warfighters.

Finally, just a few weeks ago, in our Rotary and Mission Systems business area, our Sikorsky CH-53K King Stallion heavy lift helicopter, received an affirmative Milestone C decision from the Defense Acquisition Board and will now enter the low rate initial production phase of the program. This Milestone C decision comes less than 18 months after the CH-53K made its first flight, a remarkable accomplishment for this aircraft, with its unmatched payload capability and modern avionics.

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

Bruce L. Tanner - Lockheed Martin Corp.

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. We had mixed results as we begin 2017. As expected, we had strong sales growth across the portfolio, along with outstanding cash generation in the quarter, and we continue to implement the cash deployment actions that our stockholders are used to seeing.

On the other hand, our operating profit in the quarter was impacted by two negative events that detracted from what otherwise would have been a strong earnings quarter. Based on these results, we've updated our outlook for the year to reflect higher sales and cash from operations, and slightly lower segment operating profit and earnings per share. We'll elaborate on all of these items as we progress through the next few charts.

On chart 4, we compare our sales and earnings per share in the first quarter of this year with last year's results. Sales were about 7% higher this quarter, compared with last year, with each of the four business areas showing growth over last year's results. Aeronautics and Space Systems led the growth, with Aeronautics driven by F-35 production and sustainment, which more than offset one fewer aircraft delivery in the quarter for the both C-130 and C-5 programs.

Space Systems growth was driven by the inclusion of AWE sales this quarter, compared with none in the first quarter of last year. Both Rotary and Mission Systems and Missiles and Fire Control grew at low single-digit rates in the quarter.

Earnings per share of $2.61 was consistent with our results from a year ago, but this quarter's results included $0.39 of charges associated with our revised estimate to complete the C4I contract and the joint venture impairment. These two items offset strong performance by Space Systems in the quarter, along with higher earnings in Aeronautics due to the continued increase in F-35 activity.

Turning to chart 5, we'll discuss the cash return to our shareholders in the quarter. Subtracting our capital expenditure level from the $1.7 billion of cash from operations in the quarter, our free cash flow was $1.5 billion. We've returned just over $1 billion of cash to our stockholders in the quarter or 70% of our free cash flow. And this was fairly evenly split between share repurchases and dividends. So we're right on track for the full year cash deployment goals we discussed last quarter.

On chart 6, we'll provide our updated outlook for 2017. We're increasing our sales outlook by $100 million based on higher expectations for Space Systems for the rest of this year. Our segment operating profit outlook has several moving pieces that net to a $30 million reduction from our previous guidance.

We are lowering our RMS's outlook by $90 million, with a $120 million C4I charge, partially offset by $30 million of improved performance in other parts of the portfolio. We're increasing our outlook for Aeronautics by $35 million and Space Systems by $25 million for the year with the Aeronautics increase driven by performance improvements in a number of programs and the Space Systems increase driven mostly by higher expected equity earnings from ULA.

Our other unallocated expense increased by $50 million, mostly driven by the joint venture impairment we discussed. We'll show how all these changes impacted our earnings per share outlook on the next chart and finally, we are increasing our cash from operations by $300 million to now be greater than or equal to $6 billion.

Chart 7 provides a reconciliation of our current and prior earnings per share outlook. As we've already discussed, the C4I charge and the JV impairment are $0.25 and $0.14 negative impacts to our January EPS outlook range of $12.25 to $12.55. Combined, the increased outlooks from Aeronautics and Space Systems, along with the partial offset within RMS add $90 million to our segment operating profit outlook or about $0.20 to our previous EPS guidance. And a lower tax expense forecast, along with several other minor improvements in our expense outlook, adds another $0.09 to our prior outlook. Netting all of these items results in a reduction of $0.10 in our EPS outlook or a new guidance range of $12.15 to $12.45.

On chart 8, we show our revised sales outlook by business area. The $100 million increase in sales is due to the improved outlook we have for Space Systems for the rest of the year. We're maintaining the sales ranges for the other three business areas at this time.

Chart 9 provides the updated segment operating profit outlook by business area. We decreased our operating profit outlook in total by $30 million. RMS is down $90 million for the C4I contract charge, net of other improvements. Aeronautics is $35 million higher and Space Systems is higher by $25 million.

And finally, on chart 10, we have our summary. Our first quarter performance was mixed with a couple of earnings charges detracting from strong performance elsewhere in the business. Our cash performance was strong in the quarter and we expect that performance to carry over to a higher full year outlook than we provided last quarter. We continue to provide significant cash returns to our stockholders and we're not giving up on trying to overcome our early setbacks and making 2017 a year we can be proud of.

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

Question-and-Answer Session

Operator

Thank you. In the interest of time, we are limiting you to one question. Please return to the queue for any follow-up questions. And our first question for today comes from the line of Doug Harned from Bernstein Research.

Douglas Stuart Harned - Sanford C. Bernstein & Co. LLC

Yes. Good morning.

Bruce L. Tanner - Lockheed Martin Corp.

Hey, Doug.

Marillyn A. Hewson - Lockheed Martin Corp.

Good morning.

Douglas Stuart Harned - Sanford C. Bernstein & Co. LLC

On F-35, two things. If you look at the situation, if we should end up in a continuing resolution, could you talk a little bit about what that might mean for F-35? And then, also you've talked about getting the CTOL version, the price down to about, maybe, under $80 million by 2021. Can you talk about what that means for the margin trajectory for the program?

Marillyn A. Hewson - Lockheed Martin Corp.

So, Doug, just on a continuing resolution, we wouldn't expect any impact on F-35. That, as you know, is a long-cycled business. The contracts that we're performing on were some time ago. So with – the CR effects are not being able to add new contracts at this point. So the program that we're producing on today is not impacted by the CR. I'll let Bruce pick up the question on margins.

Bruce L. Tanner - Lockheed Martin Corp.

Yeah. I don't think I've got a whole lot off from the CR issue, Doug, other than – as you well know the F-35, I mean the work that we're performing today was from several fiscal years ago. It takes about three years or so to go through the F-35 lifecycle from sort of the initial dollar award to the first aircraft delivery. So, as Marillyn said, I wouldn't expect to see, especially in 2017, much of an impact, if anything, even should CR be extended.

On the CTOL question, getting price below $80 million and its impact on margin, the only way that would impact our margin negatively, Doug, is if we price those contracts assuming that we can get there and obviously don't achieve that but that's not our expectation. Our expectation is that we'll bring – be able to bring the cost down to support that price with both the U.S. government customer as well as our international customers and make the profit levels that we've talked about before that we should be making, when we get to kind of full rate production on this contract around this program. So, I would say, arguably no impact unless we have performance that we're not expecting to have in that timeframe.

Operator

Thank you. And our next question comes from the line of George Shapiro from Shapiro Research.

George D. Shapiro - Shapiro Research LLC

Yes, Bruce, just a follow-up on that F-35. The sales increase seeing a little low to me, given I thought we're going to get up about $2.5 billion for the year, if you just comment on that. And then in return for getting better cash terms on the program, did you give up anything in potential margin, or if not, what did you give up? And then, incremental margin in the quarter was about 17%, would imply that there were some pickups in margin rates, if you could talk about which blocks. Thanks.

Bruce L. Tanner - Lockheed Martin Corp.

Yeah. Thanks, George. Good questions. So, yeah, sales in the first quarter probably were a little lighter than we'd expected. I think it's important that we did say we're going to hold the guidance for the other business areas besides Space Systems that includes Aeronautics. We still think that the F-35 program is going to have the kind of volume growth throughout the rest of the year that we saw – that we forecasted in the guidance that we provided to you last quarter.

And just to put it in some perspective, I think I looked at the F-35 program. I think the first quarter is up like 15% over the first quarter of last year. So we're still seeing some pretty significant volume increases, even though we expect the full year to actually be higher than that. So I still think we're going to track to the outlook we provided in first quarter and I think we'll catch up between now and the end of the year to where we expected to be when we talked last quarter.

The better cash terms that we got there, you should think of that impacting the LRIP 9 contract, LRIP 10 and LRIP 11. And I think your question specifically, George, was, did we give up margins associated with that. You should think of this as sort of bundling of a lot of things that got together the – I'll say the biggest thing that – and this was in Marillyn's comments. The biggest thing that we gave up during this bundling of activities or economic opportunities was we dropped the claim on the LRIP 9 unilateral and we feel good about that. Frankly, we're glad to have that behind us. And we think that the economic benefits of what we got collectively justified dropping that claim going forward. So we're good and we're glad to get that behind us.

And then lastly, as you usually do, George, you did a good analysis on sort of the incremental margin in the quarter and it is higher. I think you said 17%, I think that's about right. Couple of things happened there and I think it's all good news as you might expect there. One of the bigger things that happened is we actually had some step ups associated with our international final assembly and checkout facilities. I think of this as both the Italian facility as well as the Japanese facility where we're doing the – as by definition, the final assembly and checkout of F-35s at those two locations.

As you might expect, we started those efforts fairly low. It's not easy to sort of establish from essentially nowhere, a program of record and the ability to deliver aircraft at an international location. So we started looking those – both those locations and the work that we're doing to support those establishments pretty conservatively. It turns out, we're doing pretty good on those contracts and we're actually delivering aircraft out of the Italian FACO and expect to soon on the Japanese FACO as well. So, because of that, we were actually able to step up from our previous conservative numbers there and we feel good about where we are as we sit here today. So, thanks.

Operator

Thank you. And our next question comes from the line of Peter Arment from Baird.

Peter J. Arment - Robert W. Baird & Co., Inc.

Yes. Good morning, Marillyn and Bruce.

Bruce L. Tanner - Lockheed Martin Corp.

Hey, Peter.

Marillyn A. Hewson - Lockheed Martin Corp.

Good morning.

Peter J. Arment - Robert W. Baird & Co., Inc.

Bruce, maybe just it's kind of a quick one on first, just clarification. What should we expect for kind of overall helicopter deliveries , Bruce, (25:40) for the year? I understand, commercial, obviously, is way down, but just kind of expectations around kind of the government deliveries. And then just also just related to, I guess, LRIP 11 was kind of key for your overall bookings guidance for the year for 2017. Are you still kind of targeting a book-to-bill of near 1 for 2017? Thanks.

Bruce L. Tanner - Lockheed Martin Corp.

Yeah. Thanks, Peter. So, helo deliveries for the year, in total, were down in the first quarter. As you saw from the earnings release we provided, I think we're down 14 in total between our commercial and military aircraft in the first quarter. We actually expect that to pick up in the next three quarters of the year, and actually finish the year just about at the exact same spot that we ended 2016 with in terms of deliveries; you should think of that as 180-plus helos in total.

We did not deliver – I don't remember if you asked this question or not, Peter, but just to comment on it, we did not deliver any commercial helos in the first quarter. However, if you look at the outlook for the rest of the year, we do expect to deliver about the same number of commercial helos in 2017 as we did in 2016. Those helos are in the backlog as we sit here today, they're just phased differently in the year than they were last year. And then I think your – let's see, I think that just bakes into what's the – the military helicopters are the difference between the total in that 10 aircraft that I just talked about there.

And I think your last question was on the LRIP 11 and booking guidelines and our booking guidance that we provided. We still expect to see – it's probably going to come in two tranches, Peter. Second quarter, we expect to get an undefinitized contractual action, very large one, associated with LRIP 11. So that will be a pretty significant order, pretty significant increase in book-to-bill in the quarter. And then we're hoping, and I think the government is hoping as well, to finalize and definitize the LRIP 11 contract by the third quarter of this year. We'll get another little bump associated with that definitization. And we do expect, as you said in the question, we do expect to finish the year at a greater than 1:1 – or 1.0, excuse me, book-to-bill ratio.

Operator

Thank you. And our next question comes from the line of Joseph DeNardi from Stifel.

Joseph DeNardi - Stifel, Nicolaus & Co., Inc.

Yeah. Thank you very much.

Bruce L. Tanner - Lockheed Martin Corp.

Hey, Joe.

Joseph DeNardi - Stifel, Nicolaus & Co., Inc.

Bruce, I'm wondering if you could just talk about, over the past five or six months, just at a very high level, on F-35, has anything changed on that program? Clearly, there's been a lot of discussion around pricing and contracting. Has anything changed on that program at all over the past few months that would kind of affect your view on margins on that program longer term?

Bruce L. Tanner - Lockheed Martin Corp.

No, Joe, I'm trying to think. The only thing that's happened over the last six months sort of negatively on the program, we did have this tube issue, which we refer to as the PAO tube issue, that we had to essentially make some modifications into some delivered aircraft to remove that – remove and replace that tubing, as well as change the process going forward. That had a slight hit to the overall performance on the program, but other than that, there's not – I'm thinking and I'm looking at Marillyn when I'm saying this, Joe, there's nothing structural that I would point to that's different than what we've been saying for the last couple years about our ability to sort of structurally grow the program's margins as we head into full rate production. So, I think the short answer to your question is no.

Marillyn A. Hewson - Lockheed Martin Corp.

And the PAO tubes issue is behind us now. We have modified all the aircraft.

Joseph DeNardi - Stifel, Nicolaus & Co., Inc.

Yeah. Good point. PAO is – we're done. I think it was done actually at very beginning of the first quarter.

Operator

Thank you. And our next question comes from the line of Carter Copeland from Barclays.

Carter Copeland - Barclays Capital, Inc.

Hey. Good morning, Bruce and Marillyn.

Marillyn A. Hewson - Lockheed Martin Corp.

Good morning.

Carter Copeland - Barclays Capital, Inc.

Just a clarification on the cash, and then I wondered if you could give us just a little bit more color on the booking rate adjustments. I think you called out there were several. Did the LRIP finalization 9 through 11 have any impact, upwardly, on the multi-year cash profile that you had talked about previously ,or did it impact the phasing?

And then on the booking rates, I noticed that you were down, clearly, a C-5 delivery, and you called out the revenues, but no mention of the profits there. Was there a booking rate adjustment there? And you called out a couple of negative booking rate adjustments on various programs. I wondered if you could just give us some color on that.

Bruce L. Tanner - Lockheed Martin Corp.

Okay. Carter, I'll take a shot at those. So, I think just the overall booking rate adjustments, I think you're asking about the F-35 in particular, and we mentioned a couple. The biggest change in F-35 were for those two international...

Carter Copeland - Barclays Capital, Inc.

FACOs, yeah.

Bruce L. Tanner - Lockheed Martin Corp.

...final assembly and checkout, yeah, final assembly and checkout facilities that I talked about before in Italy and Japan. And as I said, this is a good example where we perform – we had a couple of setbacks with some international programs. Here is some good news on the international side, where we actually did a very good job of establishing those facilities and are doing a good job at those facilities, and that resulted in the (31:28) that you saw in the first quarter.

LRIP 9 through 11, I think your question relates to the three-year $15 billion or more objective that we established our goal that we established last, I guess, it was fourth quarter or first quarter of this year. I think it gives us an opportunity, Carter. It surely gives us greater clarity, because we've got better insight into established terms and conditions for the next three significant LRIP contracts in a row. So we won't have to, if you will, haggle over terms and conditions associated with cash collections. So, I'd like to think that gave us greater clarity, and I think it gives us some potential to have some better performance, F-35 related, relative to what we had expectation wise in that $15 billion as well. So, I think there is the possibility there that you were hinting at in your question.

And then on the C-5, we did mention the profit being down, for the one aircraft being down. There was no really change in margins whatsoever, and there was – and I'll say an associated earnings reduction associated with the lower sales volume, but margin is exactly the same as it was a year ago, so no change there whatsoever.

Operator

Thank you. And our next question comes from the line of Seth Seifman from JPMorgan.

Seth M. Seifman - JPMorgan Securities LLC

Thanks very much, and good morning. I wonder if you could talk a little bit more about Sikorsky and whether you expect to get to a positive contribution on the EBIT line from Sikorsky this year. And then whether next year promises to see kind of more meaningful EBIT contribution and if you could size that at all?

Bruce L. Tanner - Lockheed Martin Corp.

Seth, can you go through that one more time, I'm not sure I followed that entirely.

Seth M. Seifman - JPMorgan Securities LLC

Sure. Yeah. On Sikorsky, I wonder if you could tell us, if you expect to get to a positive EBIT contribution from Sikorsky in 2017 and then if we should think about a much more meaningful contribution in 2018 on the EBIT line and maybe if you could size that.

Bruce L. Tanner - Lockheed Martin Corp.

Yeah. Sorry. So, the Sikorsky, I think, we're really close, well let's back up. Sikorsky is always going to have, at least for a long period of time, the intangible amortization associated with the purchase accounting, if you will, for that acquisition. So you should think of Sikorsky getting $230 million or so a year, at least for the next few years and then I think it sort of gradually gets smaller than that. But we'll have that with us for – I think the period of amortization is something like 15 years. So, it's going to be with us a long time. That's going to be a drag there.

As we look at kind of 2017, I think Sikorsky is actually going to be a positive for us in terms of absolute EBIT dollars, even with that drag. It's going to get a little, I'll say, messier going forward, because we've actually combined some things in with Sikorsky from the heritage Lockheed Martin performance. So, for instance, several of you have been to our facilities in Owego, New York, where we do or have done historically a lot of helicopter modification programs and helicopter enhancement programs, including the U.S. Navy's Romeo and Sierra, sort of submarine hunting helicopter and the mission packages that go with that. We've combined that together with what we are now referring to as Sikorsky, at least internally. And if you add that together with the piece that came from Owego, it's a strong positive to us in the year.

But just focusing on Sikorsky going forward into 2018, we should see an uptick there, as we continue to sort of wean our way from the restructuring charges and some of the implementation cost that we have, in order to attain the savings that we expect to see. And we do expect to see those savings start to materialize in pretty good fashion starting in 2018. So that'll be our expectation.

I think more importantly, as we've talked about in the past, 2018's cash flow is where we're expecting to see some pretty good sized increases and that's predominantly because of working off a lot of the development programs and especially things like the Canadian Maritime Helicopter program, where we're actually at a loss position when we acquire that business. And as we start to get out of the CMH – or not the CHMP, the CH-53K developments and the presidential helicopters and actually started converting these into production contracts. We should start seeing much stronger cash flows starting in 2018 to accompany the increase in earnings that I just talked about.

Operator

Thank you. And our next question comes from the line of Pete Skibitski from Drexel Hamilton.

Peter John Skibitski - Drexel Hamilton LLC

Hey, good morning guys. Not sure how to pronounce this, but EDGE-T may be. Can you give us a sense of how much risk remains on that program and maybe also that the timing of some of the key risk retirement milestones?

Bruce L. Tanner - Lockheed Martin Corp.

Yeah. Pete, I'll take a shot at that. So it's EDGE-T, I know it well. Let me just give you a little bit of background, maybe just I think it'd be helpful in not just with where we got to go in the future, but maybe how we got here. I think as I look at this, what's sort of unusual about this is this is a firm fixed priced contract that includes a pretty substantial amount of developmental work. That's not something that we generally sign up for. I mean, typically in a perfect world, we'd like to deliver sort of products off our production lines internationally.

On this one, we actually chose to do some development and almost by definition, when you do that at an international environment, you're going to do it on a fixed price basis. Frankly, that's one of the reasons why we like to do most of the development with U.S. government under a cost-reimbursable type contract as opposed to development contract – as opposed to fixed price, excuse me.

We knew, going in, this would be a challenge to perform this work, but we had developed capabilities under our own IRAD dollars that we thought would make this essentially an off-the-shelf solution and we sort of priced it accordingly. And as it turns out, as we got into the implementation of this, the solution ended up being far less robust than what was needed. And I'll say the implementation environment was more complex than we expected.

And there was also some evolving customer requirements and sort of some give and take that occurred, the longer the implementation took to deploy. So, all of those things led us to where we are today. Where we sit today, we think we have this sized appropriately. The milestones that you talked about going forward and probably what we won't talk about those milestones, because they're not necessarily large enough in the total scheme of things of Lockheed Martin to mention. But amongst them is finalizing this off-the-shelf system and putting it in place in country. We think we're about there. We're doing that and we think it's now has the capabilities that were promised in the contract. Now, it gets down to sort of the implementing and connecting a whole bunch of systems in country to this sort of command and control structure and making sure they all talk to each other and work each other.

There's probably another two years, I'm going to guess, Pete, worth of the work to do. And we'll surely keep you apprised as we go through the next few quarters, if there's any issues there. But, we think we have this thing sized about right as we said – as I said earlier. I mean this is unfortunately not the first charge that we've taken on this contract. We took some charges throughout, I think, the last – the biggest one was in 2015. But, we sort of took some incremental changes in 2016, but we think we've sized this thing about right.

The reason this was important to us, Pete, was – and the reason we took the chance to do an international program with fixed price development is, as Marillyn said in our opening remarks, no one's ever done this before. I mean, this – "some people, this is hard work." But the good news is if we do this hard work, there's a lot of international customers who would like to have this capability for their own integrated air missile defense systems. And we think there's even potentially a play to come back within the U.S. government for this capability as well. So it's pretty unique in its capabilities, but it was pretty difficult to do and we're hoping there's a tail of business that comes along with our successful completion of this contract.

Operator

Thank you. And our next question comes from the line of David Strauss from UBS.

David E. Strauss - UBS Securities LLC

Thanks. Good morning.

Bruce L. Tanner - Lockheed Martin Corp.

Hey, David.

David E. Strauss - UBS Securities LLC

Hey. Bruce, Missiles and Fire Control, can you touch on the program mix and margin profile there? I think the margins have been coming down in that business for several years now, I think that you've primarily cited the mix of business within that. Can you talk about when you see that mix kind of bottoming out in the margin profile from here? Thanks.

Bruce L. Tanner - Lockheed Martin Corp.

Sure, David. So, Missile and Fire Control (sic) [Missiles and Fire Control] (41:26), I probably have sounded like a broken record on this, but there is a lot of things going on, and we've talked about them in the past, but I'll probably repeat myself here a little bit. We had a number of some larger programs, especially, sort of the consumable OCO type contracts where we had HELLFIREs and guided multiple launch rocket systems, ATACMS missiles and the like, where we did – time after time would get continual orders on top of previous orders and we did well on those contracts. Sort of the volume aspects of that helped us a lot because there was quick need for those products and they did well for us.

We also completed a couple of larger programs relative to PAC-3s, couple larger contracts that we also performed better than what we negotiated on. And all of this sort of culminated at the end of 2015, middle of 2016 where we had to start renegotiating those contracts over and basically, you snap a new line in the sand and you start off with your historical good performance and you've got to sort of achieve that again to make those sorts of margins.

So, we had a bit of a reset, if you will, on the new business where we've done previously better than negotiated; and on the new business, we started off booking essentially at the negotiated amount, so that's part of it.

The other part is, we have made some strategic bids in Missiles and Fire Control, and fortunately, we have been successful on a couple of those bids. Primary amongst that was the JAGM missile, the Joint Air-to-Ground missile, which is essentially the replacement long-term for the HELLFIRE missile. We did go into that, as you might expect, pricing it as this – if it was a strategic opportunity. We won that but what that says is during the development, parts of that program, its margin is much, much lower than what we would historically see at Missiles and Fire Control.

There is a couple of other opportunities and development programs, not all of which we can talk about, that we either are performing on or we expect to and hope to win on, that also sort of drags to our historical level of higher margins on Missiles and Fire Control. And frankly, if we win those and perform on them as we expect, I would not expect to see huge improvements in the Missiles and Fire Control margins over the next couple of years.

And that would be a good thing because the volume that we would have on that new business will be the type of business that will support us for literally decades to come. So it's worth sort of the strategic investments and the strategic bids that we put forward. But it does come at the expense of historically high margins.

Having said that, I'm very pleased with Missile and Fire Control, it's not like they are our problem child whatsoever, we are still looking at just south of, what, 15% margins, so it's a highly, highly performing business, highest margin within the corporation still and we would expect that to be the case going forward.

Operator

Thank you. And our next question comes from the line of Jason Gursky from Citi.

Jason Gursky - Citigroup Global Markets, Inc.

Hey, good morning, everyone. Thanks.

Bruce L. Tanner - Lockheed Martin Corp.

Hi, Jason.

Marillyn A. Hewson - Lockheed Martin Corp.

Good morning.

Jason Gursky - Citigroup Global Markets, Inc.

Marillyn, I wonder if you would – hey, good morning. Wonder if you would spend a few minutes on talking about the opportunity set in front of you here over the next 12 to say 18 months, I know we've got things like T-X trainer and JSTARS and a little bit further out there is maybe Future Vertical Lift here on the domestic side, and then maybe some of the international opportunities, MEADS, THAAD, Aegis in the European, Middle East and Asian areas?

Marillyn A. Hewson - Lockheed Martin Corp.

Sure, Jason. Thanks for the question. Just starting off with F-35, if you just look at the ramp-up on that program, it's very significant over the next few years. And when we get to full rate production, we'll probably be delivering roughly 200 aircraft a year.

So, that's a big opportunity. The next five years, we think about 50% of the orders will be in the international marketplace. We're continuing to see additional interest from a lot of countries around the F-35 that are currently not in the program of record, so we expect that over the next few to several years, that we'll continue to see additional countries that will become buyers of the F-35.

In the area of missile defense, that continues to be a great demand for us internationally. You mentioned Aegis and PAC-3, also THAAD is another one that we expect. Areas like in the Middle East, we expect that there we will continue to see opportunities. You've probably seen that there was a notification on Qatar and we think some other countries in that region will also be considering THAAD as we go forward.

And then beyond that, Aegis, as we've sold some systems on Aegis, we'll continue to see opportunities for, potentially, for Aegis Ashore, which is the land-based Aegis and we continue to sell PAC-3s. So, in the missile defense arena, PAC-3 MSE, the extended range, we expect we'll continue to see strong demand.

And then there is MEADS. Germany has already selected MEADS, the Medium Extended Air Defense System, and we're moving forward on that. We expect to get underway this year with a contract with them – or late this year, and we'll see other countries; watch that space. We've had interest from Poland and others.

And then, continuing on the international front, F-16, as you've probably seen, there has been an informal Congressional notification for selling F-16s to Bahrain, up to 19 or 20 aircraft. And we continue to be looking at the opportunity for selling F-16s to India, which could be a much bigger buy by India over time, as they move through their process.

So, and then F-16 upgrades, we were doing from South Korea, Taiwan, Singapore, and others that have made a selection on that. We think, with that large fleet that's out there, that we'll continue to see other countries that will look at F-16 upgrades.

So on the aircraft front and the missile defense front, continuing opportunities. And beyond that, I mentioned LRASM in my discussion on the front end with my opening remarks. We think there is a big opportunity for LRASM for the U.S. government as we move forward. We've sold JASSMs to other countries, so LRASM even could be a potential for international opportunities.

T-X and JSTARS are two bids that, this year, that we are participating in. We think we have a very strong offering on T-X, the next trainer replacing the T-38, that capability we're offering is a T-50A, It's a very mature program that has low risk, and we can accelerate the schedule and meet the needs of the Air Force up to two years earlier than probably a clean sheet design could do, or maybe more. So, we're very much ready with our offering on that; we expect to be very competitive in that opportunity.

JSTARS, we've got a great team pulled together on JSTARS as well, and we're bidding on that opportunity.

Future Vertical Lift is a little further out, but of course, we're in the demonstration phase, in the technical demonstration on that, and are teaming on that capability. So, we expect to be in a good position for Future Vertical Lift as we go forward.

And then the Ground Based Strategic Deterrent, we will participate in that competition, and we think we have a strong offering and LRSO. So, we are engaged in, not only our current portfolio that we believe is very strong and there is a strong demand for, but we are pursuing some big opportunities in other areas.

And I didn't mention our Space Systems area, but commercial satellites and the satellites for the military, as we continue to grow that portfolio as well.

So, I think I've kind of walked around the system. I did mention C-130, I mean, there continues to be interest in the C-130 in countries like India and Saudi Arabia and France and Germany, and we hope to – we are currently on a multi-year with the U.S. government, we would expect them to continue to purchase C-130s going forward.

And I think that – Bruce, any others, maybe, you can add to that? I've kind of tried to walk around the portfolio. We have a very broad portfolio, as you all know, and a very strong portfolio. So, we're really pleased with how well it's supported in the current budget, and what's in the budget deliberations going forward for the U.S. government. But around the world, we've got great opportunities internationally.

Bruce L. Tanner - Lockheed Martin Corp.

No, I think you covered it.

Marillyn A. Hewson - Lockheed Martin Corp.

Okay.

Operator

Thank you. And our next question comes from the line of Rich Safran from Buckingham Research.

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

Hi, Marillyn, Bruce, Greg, good morning.

Marillyn A. Hewson - Lockheed Martin Corp.

Good morning.

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

Marillyn, maybe I'll follow up a little bit more on that F-16 comments you were just making here. Just a couple of items here, or a few items here on that. So, I saw you moving the line out of Forth Worth to Greenville. I thought that was interesting decision, considering you're only having a few remaining in backlog. So, what does it mean that you're moving the line?

You mentioned Bahrain as a possible order here, is that something you could see happen this year, because I think you'll – you don't have enough in backlog, I think, to finish the year, if I'm correct about that?

And then, also, it seems that the Air Force is interested in extending the life of the F-16, some kind of SLEP program, and maybe you could discuss the implications of that, and what you're expectations are there?

Marillyn A. Hewson - Lockheed Martin Corp.

Sure. Thanks, Rich. Well, first off, yes, we are moving the line to Greenville, and let me just give a little background on that. I think we've let you all know that we will be delivering our last F-16s off the line in Fort Worth later this year, and then actually, the line will stop for a period of time. It was important for us to continue to look at restarting that line. We know how to do that, we have a robust supply chain that has been able to increase and decrease over the life of the F-16, and deal with changes in quantities, and we're ready to restart that line.

The reason we're moving to Greenville is, we're ramping up production on the F-35 in Forth Worth, we need the facilities there for what we're doing. Greenville is a great operation that has a strong talent and good facilities there. So, it will be a final assembly and check-out facility for the F-16 there, it's just – we basically produce the aircraft through our supply chain elements of it, and we will assemble it there and deliver it from Greenville.

And we're excited about that, it's a – we've also selected Greenville as our site for producing the final assembly of the T-X, of our trainer opportunity as well, the T-50A, so – and we have demonstrated the capability for doing fighters in that facility, so we're excited about it being the place for the future F-16s.

In terms of it being this year, for Bahrain, getting an order this year, we feel good about it, but it's really government to government, so we'll have to go through the finishing up on the formal congressional notification and get an order underway. And we look forward to that opportunity. We're very encouraged by that, and we would produce those in Greenville for that reason.

In terms of the F-16 SLEP, the Service Life Extension Program, we were pleased to see that the F-16 was designated to have an extended useful life. It has been a strong program for us, and so we continue, as I said, to do upgrades around the world, so that airframe and its capability, it has demonstrated it can fly many more hours and that will open the opportunity for putting new systems on it, new weapons systems, new mission systems and radars and things of that nature. So we see that as a very positive for that fleet, for it to continue to serve our customers, not only U.S. Air Force, but customers around the world for many, many years to come.

Operator

Thank you. And our next question comes from the line of Cai von Rumohr from Cowen and Company.

Cai von Rumohr - Cowen and Company, LLC

Thanks so much. Maybe if you could give us a little more color on the JV adjustments you took. And then ULA, I guess was strong in the quarter; my understanding was, it was expected to be down about $150 million from the 3.25 (54:59) last year. What's changed there? And then maybe on the revenue recognition accounting changes expected to come next year, just a quick thought on what that should do. I assume that would be a big plus for the CH-53? Thanks.

Marillyn A. Hewson - Lockheed Martin Corp.

So, Cai, maybe I'll take the JV, and then let Bruce pickup on the AWE and Bruce you can fill anything more on that. The JV itself, as I mentioned in my opening remarks, this is a non-cash impairment charge. And we are actually a minority interest in this JV.

Back in the mid to late 2000s, the UAE was looking for U.S. partners that would help them to develop their fixed wing and rotary wing sustainment capabilities so that they could support their aircraft in-country and look at broadly supporting beyond the UAE, other countries' aircraft. And we entered in this joint venture in 2010. At the time, we were a 20% owner in it from a Lockheed Martin standpoint, Sikorsky was a 20% owner, and the UAE entity had 60%. Of course, when we acquired Sikorsky in 2015, that increased our position. So, we are a 40% owner in the joint venture.

The joint venture has been successful. It's been a good joint venture, it's got about 4,000 employees, sales of about $1.5 billion a year. It's been very profitable every year with equity earnings that come back to us through Sikorsky and now to us, both our share and Sikorsky's share. And it's generated to offset credits for us that have satisfied a lot of obligations for us for the programs that we have in country. So from that standpoint, it's successful.

The ambition, though, for that entity is for it to grow regionally and become a sustainment center for the region. And so facilities were built and machinery and equipment procured in order to prepare for growing beyond just the UAE market. And unfortunately those projections haven't materialized.

The fact that oil prices have been lower has not helped matters, but it's been a damper on what the outlook was for it. So, the charge basically recognizes the diminished value of those assets and the lower demand environment. We still have aspirations for that entity, and hopefully, we will see longer term that outlook. But as we looked at it today, the reduced business prospects, the entity determined that they needed to impair certain assets, and so that's what we dealt with.

Bruce L. Tanner - Lockheed Martin Corp.

And Kyle, I'll take a shot at your other two questions. ULA, I think your analysis is right on. And you should think about it's really just the phasing in the year.

We're still expecting that ULA will be about two thirds or so of the equity earnings that we'll get from that entity this year versus what we received last year. It just so happens the first quarter was disproportionately higher than it was compared to the first quarter of last year.

But we would expect that to come back down to the levels we talked about other than the upper that we mentioned in the first quarter. They're going to come down to levels we talked about in the January call, that's still our expectation for ULA.

And then lastly you asked around rev rec, revenue recognition standard that becomes effective January 1, 2018. I'll speak for myself here, Kyle, I'm starting to get insight into sort of rev rec the old way, if you will, and rev rec the new way. Our expectation and what we've disclosed in the Ks and the Qs is that we wouldn't expect to see a large change relative to our sales and/or earnings even though we are going to be changing some contracts that are currently on a delivery-based or what we call units-of-delivery-based method of sales recognition to a cost-to-cost methodology.

So that will have some impacts on sort of our opening balance sheet under the new rev rec approach, as well as sort of our opening backlog position, but I wouldn't think the sort of the run rate if you will, of sales and earnings going forward would be a material difference at all and that's sort of what I'm seeing as I look at the data so far.

We'll give you a whole lot more insight into that in the second quarter. And when we give you our third quarter trend information for 2018, my expectation is that we'll be able to give you a better insight as to exactly what we're expecting to see 2018's impact as a result of rev rec change, but again I wouldn't expect it to be very large.

Greg M. Gardner - Lockheed Martin Corp.

Karen, we're coming up on the hour, we have time for one more question please.

Operator

Thank you. Our final question for today comes from the line of Myles Walton from Deutsche Bank.

Myles Alexander Walton - Deutsche Bank Securities, Inc.

Thanks for squeezing me in. Good afternoon. Bruce, I was hoping you could touch on cash flow and the couple of things you brought up on the call, one was the Sikorsky cash flow growth expectation into 2018, and the second is the resolution of the F-35, kind of with the trajectory there? And I want to put in context, so you have a $1 billion after-tax pension headwind to operating cash flow in 2018 that we know about; are the two things you mentioned, the F-35 and the Sikorsky, enough to give you confidence that you can grow operating cash flow exclusive of the pension after-tax?

Bruce L. Tanner - Lockheed Martin Corp.

Exclusive of the pension after-tax; I think the answer is pretty close. If you take out the planned pension contribution for next year, I think the short answer is yes to that question. We are doing the outlook right now, $6 billion for the year, 2017, we sort of teed up when we gave the $15 billion three-year goal of every year at or around $5 billion or so. With that $5 billion, I think it's pretty close; it's close enough that that'd probably be a good challenge for us to try to figure out how to make that happen.

Marillyn A. Hewson - Lockheed Martin Corp.

So, let me wrap up. Since that was our last question, I want to conclude the call today. And I'll end by reinforcing our commitment to our strategy of growth in top-line sales and strong cash generation while at the same time providing our customers with world-class solutions to their continuous challenges and delivering our stockholders long-term value creation.

Thank you again for joining us on the call today. We look forward to speaking to you on the next earnings call in July. Karen, that concludes our call today.