Good day, and welcome, everyone, to the Lockheed Martin Third Quarter 2012 Earnings Results Conference Call. Today's call is being recorded. At this time, for opening remarks and introductions, I would like to turn the call over to Mr. Jerry Kircher, Vice President of Investor Relations. Please go ahead, sir.

**Jerry F. Kircher**

Thank you, Ally, and good afternoon, everyone. I'd like to welcome you to our third quarter 2012 earnings conference call. Joining me today on the call are Bob Stevens, our Chairman and Chief Executive Officer; Chris Kubasik, our Vice Chairman, President and Chief Operating 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. Please see today's press release and our SEC filings for a description of some of the factors that may cause actual results to vary materially from anticipated results. We have posted charts on our website today that we plan to address during the call to supplement our comments. Please access our website at www.lockheedmartin.com, and click on the Investor Relations link to view and follow the charts.

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

**Robert J. Stevens**

Thanks, Jerry, and good afternoon, everyone. Thanks for joining the call today. We know most of you are having a really busy day, and we appreciate you being with us.

I want to begin with a brief summary of the third quarter, which I see as a continuation of the strong momentum and focus on execution we've been achieving throughout this year. In the third quarter, segment operating margin increased to 12.1%, a solid improvement over the prior year level of 11.2%. Cash generation was strong at $1.6 billion, and earnings per share from continuing operations expanded by 11%.

Our financial strength enabled a 15% increase in our quarterly dividend to $1.15 a share or $4.60 annually. This is the 10th consecutive year that we've raised the dividend by a double-digit percentage increase. We continue to implement our cash deployment strategy and returned over $600 million to shareholders in the quarter through dividend payments and share repurchases.

Strong year-to-date performance and execution also enabled us to increase our 2012 full year outlook for sales, operating profit, earnings per share and cash from operations. These results reflect the strength of our corporation and the focus we all have on delivering value to customers and shareholders. Thanks to everyone in the company for their many contributions in driving these strong results.

Turning to the external environment and budget status. Congress passed the continuing resolution to fund government fiscal year 2013 activities for 6 months through March 27, 2013. Under this continuing resolution, our key programs continue to be supported and funded at levels consistent with prior fiscal year appropriations.

Beyond the continuing resolution that's in place, the possibility of sequestration continues to be of great concern to us. As currently written, this law that requires approximately $55 billion in reductions to defense accounts and a like amount to non-defense discretionary accounts will take effect on January 2. We have petitioned Congress and the administration to stop sequestration and replace it with a more constructive process, a position we continue to support.

In parallel, we've also been asking the government for additional planning information so we can responsibly and properly prepare to act. On September 28, the Department of Defense provided additional planning guidance, indicating that no contract actions associated with sequestration would occur on January 2, the date sequestration is to be effective, and that no contract action would likely occur for several months beyond January 2.

On that same day, the Office of Management and Budget assured that any of our employees who would potentially be affected by a reduction in force necessitated by sequestration would be eligible for full coverage under the provisions of the WARN Act and that our company would be able to recover associated costs. With this new information, we adjusted the timing of our actions as it would have been improper for us to issue WARN notices in October or November when the timing of any potential sequestration-related events would likely not occur for at least 6 months or more.

Some reporting about our decision to move the timing of the release of WARN notices has been inaccurate, concluding that we either no longer intend to issue WARN notices if a sequestration-driven reduction in force is necessary or that employees potentially affected by reduction in force would not have the full coverage of the WARN Act, or that our actions may have been taken to achieve some political objectives. These conclusions are not only inaccurate, they are absolutely wrong.

The additional planning guidance we received from the Department of Defense on September 28 moved the likely timing of sequestration-related actions by the government by about 3 months into 2013, and we adjusted our schedule accordingly. So let me be very clear. We will issue WARN notices at the appropriate time if sequestration actions meet the required conditions in full compliance with the law, as we always have. We will work to assure that our employees are treated fully and fairly under the law, receiving protection under the WARN Act which, for us, has been and remains a high and nonnegotiable priority. And our sole interest and motivation throughout all the discussions about sequestration has been to understand the complex issues arising from this unprecedented circumstance, to be fully compliant with law and regulation and to take actions in the best interest of our company and our employees. We have done so, and we will continue to work to stop sequestration.

So while I can't precisely forecast the impacts of sequestration or events that will unfold in a dynamic global security environment, there is one thing I know for certain. Every one of our 120,000 employees stands ready to take on whatever challenges will emerge. We worked hard over many years to build a culture based on ethics and integrity and high performance.

We have a strategy that is tuned to the complex global security environment we face. We have extraordinary talent and dedicated employees who have fashioned an all-weather portfolio of global solutions for global customers, and we continue on our drive to reduce costs and meet affordability goals.

We'll be happy to talk to you about these subjects and any other you may wish, but first, let's turn to Chris for an outline of our operational highlights. Chris?

**Christopher Eugene Kubasik**

Thanks, Bob. As you noted, from an operating perspective, we had a very strong quarter and maintained our positive momentum in an uncertain and challenging environment. We also continue to implement strategic actions to increase our customer alignment and drive affordability throughout the enterprise.

We recently announced the de-layering and reorganization of our Electronic Systems business, resulting in 2 new business areas effective December 31. The businesses are Missiles and Fire Control, which focuses mainly on the mission of the Army and Special Operations Forces; and Mission Systems and Training, which supports the Navy and the Missile Defense Agency. This new structure will streamline management, reduce cost by $50 million a year and better position us to grow integrated services and support for our products.

I'm also proud of our continuous efforts to improve affordability, and I would like to highlight 3 areas: First, we're leveraging engineering processes in advanced technology; second, we've improved supply chain integration; and finally, we've reduced our overhead cost. One of the best opportunities to drive affordability is in the design and technology insertion phase, where we make decisions in concert with our customers about how mission success will be achieved.

We've developed Engineering for Affordability principles that center around rapid, transparent and collaborative decision-making to achieve mission success with the most affordable designs. Advanced technology is foundational to this approach. Application of advanced manufacturing processes and materials allows us to perform more rapid prototyping, reduce component costs, speed up the development process and shorten design cycles.

We are training our engineering work force to bring cost to the forefront in all of our development programs. The supply chain is another focus area. About 50% of our program content is provided by our suppliers and teammates. As systems become increasingly complex, tight integration of this network of companies is key to maintaining affordability.

To respond to this complexity, we have launched a focused effort to meet with our top suppliers and subcontractors to assure plans are in place to continuously improve their program execution, affordability and quality. We also have instituted corporate-wide agreements, which have generated more than $300 million in annual savings.

Reducing overhead cost is another element of our approach to affordability. Our significant successes in this area include reduction of $1.2 billion in annual cost over the past 2 years, while remaining on target for an additional $1.1 billion this year. We've reduced 1.5 million square feet of facilities over the past 2 years and have additional planned reductions of 2.9 million square feet for 2012 through 2014. With the future uncertain, we will continue with our initiatives, remain agile and take further actions should sequestration occur.

Turning to the F-35 Joint Strike Fighter program. Overall, the program continues to progress in development flight testing, solving technical challenges, increasing production deliveries and expanding international activities. Total flight test on the program have now been ahead of plan for the last 21 months.

Year-to-date through September, test flights are ahead of plan by 181 flights or 25%, and test points are also ahead of plan by over 1,100 points or 17%. We currently have 15 aircraft executing this plan. With our IAM partners back to work, production activities also continue to expand as we delivered 12 aircraft in the third quarter, up significantly from second quarter deliveries of 3 aircraft.

This brings year-to-date production deliveries to 17 aircraft, illustrating the program's maturity and progress. Internationally, the F-35 is maintaining strong partner support. This quarter, we delivered the first international aircraft to the United Kingdom with the acceptance of their initial STOVL aircraft. And Italy became the eighth international customer to formally fund procurement for aircraft.

We continue to receive significant interest and inquiries from other international countries as they evaluate the F-35 for their next-generation fighter requirements. We recognize that the key to the long-term success of the F-35 program is delivering fifth-generation capability while driving down the cost of the aircraft as quickly as possible, and it is happening.

Our later cost curve for assembling aircraft is improving faster than any previous fighter program dating back over 40 years. As volume increases, we believe this has us positioned to achieve the unit recurring flyaway cost objective of $67 million in FY '12 dollars by 2018. We are achieving these results by implementing various cost-cutting programs such as streamlining aircraft assembly, reducing time between building jets and improving material flow.

At Fort Worth earlier this week, I saw firsthand the improved aircraft processing flow and upgraded tooling that is helping to drive down the cost below the government's baseline estimates. In summary, the program is demonstrating increasing maturity, tempo and affordability, and the JSF team looks forward to providing this critical asset to our nation and our allies.

Now I'll turn the call over to Bruce to review our financial performance.

**Bruce L. Tanner**

Thanks, Chris, and good afternoon, 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 the third quarter. Sales for the quarter were $11.9 billion, similar to what we generated in the second quarter this year. Our segment operating profit margin was strong at 12.1%, and I'll discuss that in more detail in a couple of charts.

Earnings per share grew 11% to $2.21. Our cash from operations was a robust $1.6 billion, and we increased our quarterly dividend by 15% to $1.15 per share while also increasing our outlook for sales, earnings, EPS and operating cash for the full year. Lastly, in our release today, we provided preliminary 2013 financial trends and pension information, and I'll discuss those in a little more detail in later charts as well.

On Chart 4, we'll look at sales by the 4 business areas. Aeronautic sales were 7% lower than in the third quarter of last year, driven primarily by lower C-130 deliveries and F-22 production volume. Electronic Systems sales grew 4% in the quarter as all 3 lines of business had growth over the same period last year. As expected, IS&GS had lower sales than last year, but the decline was only 1% as we experienced continued growth in our Intelligence line of business, driven by federal cyber activities. Space Systems sales were 5% lower than the same period last year as we had one commercial satellite delivery last year and none this quarter. So overall, a 2% decline in sales driven by lower aircraft quantities in the quarter and the timing of satellite deliveries.

On a year-to-date basis, on Chart 5, you can see that 3 of the 4 business areas have experienced growth over the 2011 period with total sales up 2%. This strong performance led to the increase in our full year sales outlook.

On Chart 6, we'll discuss our segment operating profit margins for the quarter. The primary reason for the 90 basis point margin increase to 12.1% was due to improvements in Electronic Systems and Space Systems. In Electronic Systems, the margin improved by 110 basis points to 13.3%. The improvement came from Missiles and Fire Control, primarily in air and missile defense programs and MS2 from our ship and aviation systems programs.

The increased margin for Space Systems was primarily due to higher equity earnings from the United Launch Alliance and wind down activities associated with the United Space Alliance. The margins for Aeronautics and IS&GS were relatively comparable to last year.

Turning to Chart 7 and our earnings per share in the quarter. EPS from continuing operations grew 11% over the amount reported last year, driven mostly by the higher margins in the quarter. And adjusting our reported EPS for the effects of the FAS/CAS adjustment, increases our EPS to $2.60 per share.

If you'll turn to Chart 8, you can see our operating cash flow performance in the quarter compared with last year. Operating cash was just under $1.6 billion this quarter compared to $551 million last year. But last year included nearly $1 billion in pension contributions. And considering the strong performance so far this year, we again increased our guidance for operating cash flow by $100 million to greater than, or equal to, $4 billion for the year.

On Chart 9, we'll discuss the dividend increase in the quarter, our 10th consecutive year of double-digit increases. You can see the dramatic increase in dividend levels and yield over the past 5 years with the current yield in 2012 more than twice what it was in 2008. And the increase brings our annualized dividend yield to just about 5% based on recent prices.

On Chart 10, we'll discuss our updated guidance. Due to the year-to-date sales performance, we increased our sales outlook by $500 million. We increased segment operating profit by $175 million. We also increased earnings per share by $0.30, as I'll detail on the next chart. And again, we increased our cash from operations by $100 million.

Chart 11 shows our earnings per share outlook reconciliation. You can see that the segment margin -- segment operating profit increase was the primary reason for adding $0.30 to our guidance, reflecting the increased earnings outlook by each of the 4 business areas.

Chart 12 shows our increased sales guidance, with all 4 business areas increasing guidance for the year, resulting in the $500 million increase in total. Space Systems has the largest increase, $250 million, reflecting strong government satellite activity. And Electronic Systems increased by $150 million with growth coming from both MS2 and Missiles and Fire Control.

Chart 13 shows our new segment operating profit guidance. Here again, all 4 business areas are increasing their outlook for the year with the largest increases also coming from Electronic Systems and Space Systems, and the total increase for the year equaling $175 million.

On Chart 14, we'll discuss the preliminary trends we see for 2013. First, our trend data does not assume the impacts of sequestration as there are still many unknowns remaining as to how sequestration would be implemented if enacted. With that caveat, we expect a low single-digit decline in our total sales volume. Aeronautics and Electronic Systems are expected to be roughly comparable with 2012 levels. Space is expected to be down slightly due to the absence of any commercial satellite deliveries in 2013. And for IS&GS, we are expecting to decline in the mid single-digit range resulting primarily from the continued downturn in federal IT budgets. IS&GS also is expected to have the greatest impact from the continuing resolution due to the short-cycle nature of the business. We expect our segment operating margin will remain above 11% next year, the seventh consecutive year that our margin will exceed 11%.

And with an assumed 75 basis point reduction in the discount rate at year end down to 4% and an 8% return on assets this year, our FAS/CAS pension adjustment is expected to be $700 million, about $135 million lower than the 2012 level. Finally, we expect the level of pension contributions next year to be comparable to this year's level, although I'll remind you that we'll be considering potential discretionary contributions between now and year end, consistent with our historical practice.

And finally, we wrap up with our summary on Chart 15. The third quarter built upon the strong performance we've demonstrated this year, and our increased outlook reflects our expectation that 2012 will be a very solid year. We continue to return value to shareholders with our industry-leading dividend yield, and we'll be providing detailed guidance on the January call reflecting our new business area alignments.

With that, I'll turn the call back over to Chris for final thoughts before we open up for questions. Chris?

**Christopher Eugene Kubasik**

Well, thanks, Bruce. I just wanted to take a quick minute and remind everyone that this is Bob's last earning call as he steps down as CEO later this year and, therefore, he won't be joining us on future calls.

Despite knowing his aversion to personal praise and accolades, I want to thank him for his service and stewardship of our corporation. Bob's leadership and passion have been embedded in the DNA of our corporation. His focus on mentoring and training the next-generation leaders has created the deepest bench strength in the industry and will serve the corporation for decades to come.

On a personal note, I've had the privilege of working with Bob for over a decade in my various roles, and I've seen his passion for the mission and his drive for excellence demonstrated on a daily basis. I know many of you on the call have also had the pleasure and opportunity to interact with Bob over the years. So Bob, I'd like to speak for all of us, and thank you for your contributions, and wish you the best.

With that, I'll open up the lines for questions, Ally, and we stand by to answer.

**Question-and-Answer Session**

**Operator**

[Operator Instructions] Our first question comes from Doug Harned of Sanford Bernstein.

**Douglas S. Harned - Sanford C. Bernstein & Co., LLC., Research Division**

First, Bob, it's hard to believe it's your last earnings call, and just wanted to say it's been great working with you over the years. I mean, you've always provided some great insights regarding both the company and the industry, and so I wish you all the best going forward. But I'd like to get one more insight from you on a favorite topic here, which is the F-35. If you look back over your last several years, could you describe how the F-35 program has changed in 2 ways? First, how has Lockheed Martin's relationship with the customer evolved since negotiations always appear to be pretty tense and neither of you has much of an alternative to the other? And then second, how has Lockheed Martin's approach to performance change along with that of the program office so you can avoid some of the pitfalls that we saw farther back in the past related to cost and quality and schedule? So perhaps you could give us a sense of those 2 things.

**Robert J. Stevens**

Sure, I'll do my best, Doug. Thanks for the kind comments. Let me start with the evolution of the program and customer relations. I actually think that with respect to expectations, we've been very, very close with all our customers, and I would extend that to members of the Congress. I think everybody understands that we have an aging tactical fighter fleet, that we need to recapitalize that fleet, that we need fifth-generation capabilities. And in the most ideal circumstance, we would not do this alone, but we would do this with friends and allies so that we would have both burden sharing on the cost and flexibility and interoperability on the mission capability side of that platform, and the F-35 does all those things. Since I was here at the beginning or the inception of the F-35 program, I know full well that no one really underestimated the challenge or the complexity of bringing online a fifth-generation airplane with 3 variants that would have the performance characteristics that are embedded in the F-35. And I would tell you in my best professional judgment having done this for a long time, while there are areas of challenges that we continue to work on, there are other areas where we've done very well. And I think if you scale the size of this program, recall that many people talk about it being the biggest program or the most expensive program, but it is designed to replace more than 10 other kinds of airplanes. So that if you have an overrun of a percentage, it's a big overrun because it's a big complex program. Anytime we don't meet a performance commitment, we feel there's been a shortfall on our part, and we redouble our efforts to accomplish those goals. But I think the program has had the highest level of visibility, the most number of detailed reviews and absolutely the greatest level of transparency where you all on the call know the technical details of this program as it's unfolding almost at the same time the engineers responsible for the performance of the system know it. And I think there's some very good features of that, and I think there's some really lousy features of that because people come to the wrong conclusion because they haven't done this before as to what is a likely outcome about resolving a technical issue. So we know that it's not easy, but this program is succeeding. And I'll ask Chris to comment in a moment because it's worth the time to comment. He spent time in Fort Worth with the new Chief of Staff of the Air Force, who's deeply involved in this program. Chris will give you his own assessment. You mentioned customer relations. It's a challenging program, but I personally believe the customer wants what we want, and we will do everything that we must do to have very high quality relations and get everything about this program right because the stakes for the country and for our friends and allies are just too damn high to set the bar anywhere else. With regard to our performance, we've always been realistic. We have superb subject matter expertise here. I would put our high-speed combat tactical fighter airplane program credentials against any other company on this planet, and I believe there are those who would kill to have the capabilities we have in not only our company, but remember, the extensive supply chain that we built for the F-35 around the world. So it's a complicated program, but it is improving in its dimensions. We're happy to pick ourselves up and move ourselves forward. When we're doing well, we'll tell you. When we're not doing well, we'll redouble our efforts to get this right. Chris, you have some insight. You've been in Fort Worth just this week.

**Christopher Eugene Kubasik**

Yes, thanks, Bob. Doug, a couple things I may want to point out is, we actually have 94 aircraft in production flow between Fort Worth, Marietta and the Italian facility. So we have LRIP 3 aircraft all the way up through and including our first LRIP 7 airplane. So I'm not sure everyone appreciates the quantity and the speed at which these aircraft are, in fact, being produced. And as I look ahead to next year, we will actually deliver more F-35s in 2013 than the F-16 and the C-130J combined. So the volume is picking up. The production is going well, and the customer has been very satisfied in the deliveries that we've made. And as many of you may know, even later this year, the Marine Corps is preparing for its first operational base for the F-35 at the Marine Corps Air Station in Yuma. So there's some outside perspective to give you the volume and the progress that we're making. I guess specifically you asked about the relationship and General Bogdan was in Fort Worth recently, last week, if I recall, had very productive meetings with the team. We're very excited about him taking over, and we're looking forward to working with him. And we're both committed to 100% strong -- 100% commitment to a strong and collaborative relationship. As Bob said, I was recently, this week, down with General Welsh. He's very engaged. He was checking on the status of his aircraft, and both these gentlemen are very demanding. They hold us to the highest standards possible, and we actually prefer that. So we're looking forward to a great 2013 on F-35 and much more after that.

**Operator**

Our next question comes from Heidi Wood of Morgan Stanley.

**Heidi Rolande Wood - Morgan Stanley, Research Division**

Yes, Bob, a couple of years ago, you laid out a vision for making Lockheed a global security company. And, in a way, one can see the proposed move with EADS and BAE as some attempts to -- for others to catch up on that. Can you expand a little bit on what you see going forward in terms of pressing on, on that vision? Do you think that you would be looking -- that the company would be looking for international acquisitions or pieces of that to sort of build more of a global perspective?

**Robert J. Stevens**

Yes, thanks for the question, Heidi. When we talked years ago about a global security company, we were not necessarily focusing on international acquisitions as much as expanding international opportunities by building the core portfolio of the business that would address the emerging or evolving needs. Of course, at the time, we were talking about cyber security. When I think others weren't talking about cyber security, we were talking about moving more into services business and support and logistics for the core that we have. I will tell you, I'm really quite pleased with the portfolio that we have and how well that portfolio is maturing. Now I will certainly say in the same breath that which was embedded in Doug's question, we want to do a better job on the F-35. We know there are areas where we need to improve, and I think we're a company that realistically looks at that. But I'm very pleased with the portfolio. So as we look at the evolution of global security now, we take into account the evolution of world economic conditions that I think, generally, we would describe as showing signs of stress, and the stress may be different depending upon what region of the world we look at. But generally, we've concluded there'll be fewer resources available to our customers, wherever those customers may be, relative to meeting what is essentially a growing set of demands in the global security environment, which tells us, as we evolve this portfolio into international opportunities, we must continue to drive on affordability and cost reduction. And I think we're doing that effectively, and we have not stopped the continuous pursuit of refining that model. I think we've done a very good job of exploiting partnerships internationally, rather than making the international acquisitions as the only avenue to extend the range of our company, we've sought out very high-quality partners who bring immediate value-added credentials to enhance our offerings. And I think you should look for more of that from us. But you should also think of us relative to acquisitions in terms of extending the string-of-pearls approach of very selective, very high-quality, very easy to integrate, very specific and purposeful additions to the business. So I do expect more from Chris and the leadership team on extending the global security reach of the company.

**Christopher Eugene Kubasik**

Yes, Heidi. I'll just -- it's Chris. I'll give you a little more insight. Here in the third quarter, 25% of our orders were actually from international customers. And as you know we're -- currently about 17% of our revenue is derived from foreign military sales and direct commercial sales. I see it halfway to about 20%, and I think that's based on the strength of the portfolio, as Bob said. And when you look at Missile Defense with PAC-3 and THAAD, the precision-guided weapons and of course, the aircraft, I'd be disappointed if we're not at that 20% goal in the next couple of years.

**Operator**

Our next question comes from Bill Loomis at Stifel, Nicolaus.

**William R. Loomis - Stifel, Nicolaus & Co., Inc., Research Division**

I have a question on IS&G [ph] on the outlook. You talked about a lower, mid single-digit decline next year, yet you've won some pretty substantial contracts, the DISA/GSM-O and DoD/DC3 are just 2 of them. What's going away as some of these bigger wins you've had are ramping up over the next year?

**Bruce L. Tanner**

Yes, Bill, this is Bruce. I'll take that one on. I think -- when I think about IS&GS going to next year, there's really sort of 2 pressures that we see occurring kind of simultaneously. One is, as you're well aware of, there is a 6-month continuing resolution at least for the first 6 months of the fiscal year. I'll remind you that IS&GS is the shorter cycle business of our -- of all of our business areas, and therefore, it converts the most sales from the current fiscal year of any of our business areas. So that continuing resolution period caused us to have some pause from some increases that might otherwise have happened had that not been in place. And the second element that's causing some pressure in '13 is simply the overall federal IT budget. And if you take a look at where the federal IT budget is planned for 2013 and beyond, it has some significant reductions from the previous year's level, and being that we're the largest provider of IT services for 18 straight years, it's hard to overcome that sort of budget reduction when you're as big a player in that marketplace as we are. So those are really the 2 biggest drivers going into next year. And I wouldn't want to split it up and say, which one's the bigger contributor. But I'd say that probably, if I was, it would be the overall IT budget reductions.

**Operator**

Our next question comes from Joe Nadol with JPMorgan.

**Joseph B. Nadol - JP Morgan Chase & Co, Research Division**

First off, Bob, great working with you over a very long period of time, and best wishes to you. I have a more mundane question, just on the change in Electronic Systems and the restructuring there or the realignment there. Just on the surface, it doesn't seem like breaking one segment into 2 would save money. And, obviously, that's what you guys are in the business are doing these days. So maybe if you could help elaborate on why that saves money. And if it's just a matter of taking a layer out, why wasn't it done previously? Just finally, on the same point, does this -- can we read anything into this in terms of potential portfolio moves next year?

**Christopher Eugene Kubasik**

Joe, this is Chris. I'll take an attempt at that. The way we eliminate cost in this is that we've eliminated a layer between the businesses, and then ultimately, the executive office. If you go back in history, maybe a decade ago or so, we had probably 12 individual entities, maybe all in the $0.5 billion to $1 billion range in the Electronic Systems business area oversaw and managed that broad portfolio. Over time, we've consolidated and combined each of those entities, most recently with the Owego being combined into our MS2 business. Prior to that, I think the Eagan facility as well. So when we looked at the current alignment, we had about 4 businesses reporting in, and we thought they'd gotten to the scale and the size that we could consolidate them. Each of these will themselves eliminate some cost, and we're looking at probably close to 200 of our employees will be laid off as part of this process here in the coming months. And I think it was the right thing to do, and it was the right time to do it.

**Joseph B. Nadol - JP Morgan Chase & Co, Research Division**

In terms of portfolio moves, anything we can read into it, Chris?

**Christopher Eugene Kubasik**

No, no. It was just too -- like I said, to eliminate the cost, get closer to the customer and better align our training and services business with the underlying core product. So that's all there was to it.

**Operator**

Our next question comes from Michael Lewis from Lazard Capital Markets.

**Michael S. Lewis - Lazard Capital Markets LLC, Research Division**

My question is how do you see the book to bill ending out Q4? And I think the more important question is, have you noted any momentum from the POs on getting awards out the door quicker following the year end and now moving into the next fiscal year?

**Bruce L. Tanner**

Yes, Michael, this is Bruce. I'll take that one on. Book to bill wise, let me just -- maybe just address it with sort of a backlog perspective. I think we're at $75.6 billion or something like that through the end of the third quarter. That's basically tracking where we thought we'd be at this time. We're actually probably a little bit ahead of where we thought we'd be otherwise. I've said on previous calls, and I'll say on this one, I still think we will end the year fairly close to where we began the year at close to $80 billion of backlog. And the orders that need to happen in the fourth quarter, there's very few of them that are, I'll say, competitive orders. Most of them are sort of just fiscal year orders that happen every year. And they're not the sort of orders that are subject to the sequestration limits because they're not necessarily large orders that are increasing over the prior fiscal year's last year same time frame. The one big item that we're watching is in order to get to that level that I talked about again close to where we started the year and from a backlog perspective, we need to close on the F-35 LRIP 5 contract and get the additional fundings from an undefinitized [ph] contractual action for Lot 6 on that. We stand here today thinking that can be done in the fourth quarter, and that's the basis of the planning that we have for the end of the year for that backlog number. As far as your second question, some acceleration, I think we saw some of that throughout the year. That's again one of the reasons are why I think we were ahead of where we thought we might otherwise be at the end of the third quarter. And I think people that -- I can't remember, Chris or whoever said it earlier but some comments about unfunded obligations and trying to get funds put on contract as we head into a sequestration environment. I think we saw some customer actions doing that. It's hard to put a figure on that, if you will, but I think we did see some or experience some that earlier this year as well.

**Operator**

Our next question comes from Jason Gursky of Citi.

**Jason M. Gursky - Citigroup Inc, Research Division**

Bob, best of luck with the next chapter. A quick question just as a bit of a follow on kind of taking the last questioner's topic one step further and talk about '13 as it relates to the opportunity set. Assuming that sequester, there's some sort of resolution there, what are the things that are going to drive backlog and book to bill next year? And given the pipeline and the visibility that you have, is it possible for us to continue to maintain a book to bill around 1?

**Christopher Eugene Kubasik**

So Jason, this is Chris. Let me give you a couple of the larger opportunities and orders that we're looking at. We have F-16 in Iraq. We have a multiyear potential for the C-130J with the U.S. government. We have the next tranche of C-5 aircraft. And while it probably wouldn't be an order, but there is a decision for the F-35 in South Korea. I think that might actually hit the books when we're successful in 2014, but the decision should be announced later this year in 2013. So we see those opportunities in Aeronautics, in the Space business. Of course, Orion, we're looking at 2 more Cerberus satellites, and there's actually a couple commercial satellites internationally that we're in current discussions with. So I see opportunities there as well. The former Electronic Systems, a couple more Littoral Combat Ships, as I mentioned in my upfront comments, missile defense between Egypt and PAC-3 and THAAD we see lots of opportunities, not only here but around the globe. And then within IS&GS, there's several opportunities including a couple international, specifically in Australia and working with the Missile Defense Agency here. So it's a pretty broad portfolio. Some of these are competitive. Some are follow-on, but we're pretty optimistic about the 2013 opportunities to grow this enterprise.

**Robert J. Stevens**

Yes, and Jason you asked the question could we kind of hold -- I think if I understood your question right, could we kind of hold to the level of backlog that we end this year. Now we still think we'll end the year 2013 assuming the orders that Chris just described come through at about, again, for another year have about the $80 billion level as well.

**Operator**

Our next question comes from Rob Stallard of Royal Bank of Canada.

**Robert Stallard - RBC Capital Markets, LLC, Research Division**

First of all, best of luck for the future, Bob. It's been quite a ride.

**Robert J. Stevens**

Thank you.

**Robert Stallard - RBC Capital Markets, LLC, Research Division**

The question I have is regarding the dividend. You highlighted that you've raised dividend again quite recently, another double-digit increase. You're now paying it over 50% of earnings, over 50% of free cash flow. How much longer can these double-digit increases continue until they start to get a little bit unsustainable?

**Christopher Eugene Kubasik**

Yes, Rob. I'll take that one on. We -- I think we've been very pleased with the dividend increases and what we think this brought in terms of, I'll say, at least from my perspective, a little bit of price stability, and I think a little bit of price floor to the stock price since we've increased the dividend here recently to the levels that we have now. Several years back under Bob and Chris' leadership, we committed to providing 50% or more of free cash flow in the form of either dividends or share repurchases. I'm pleased to say with the increases we've given in dividends, we now do that strictly by the dividends that we do provide. If we just stop there with dividends, you're already at the 50% of free cash flow. As I look this year and next year, I mean, the first thing that I tend to do when I look at the dividend and payouts and the like is I do adjust for the FAS/CAS. So if I was to do that this year, for instance, I think we'd add back $1.60 or so for the FAS/CAS impact to our numbers and therefore, the earnings per share gets close to a $10 per share number. So when you kind of get on the cash-on-cash basis, the dividends are less than 50% as I would view it today. And I think going forward, the question is how much cash do we need to invest in the company to support the growth rate of the company. We're generating far more cash today than we need to support the growth rate, particularly when that growth rate starts to slow going forward. And so going forward, I still believe we will be generating more cash than we need to support the growth of the company, and we will have the opportunity when CAS Harmonization kicks in, in particular the next 2 years to recover a lot of the discretionary, and not just discretionary but that's a big piece of it, pension payments that we've paid in the last few years. And that will have the effect of increasing cash over what you might ordinarily think as sort of an average run rate. I'll remind you that we have some $4 billion of advanced funding in our pension plan that is yet to be recovered under our government contracts. So as CAS Harmonization plays out over the next few years, that will be added to sort of this the average run rate, if you will, of cash generation. And I think that's where the opportunity to continue with dividends and other cash deployment actions, not just dividends, will come from.

**Operator**

Our next question comes from Cai Von Rumohr of Cowen and Company.

**Cai Von Rumohr - Cowen and Company, LLC, Research Division**

Yes, and Bob, let me join the other folks in congratulating you on a job extraordinarily well done.

**Robert J. Stevens**

Thanks, Cai.

**Cai Von Rumohr - Cowen and Company, LLC, Research Division**

So pension, $700 million, walk us through some of the assumptions, I guess, you talked a little bit about the discount rate that's like where is your return, what are you assuming for return on assets and where are you year-to-date? What should we look for CAS to do next year? What should we look for your contributions to be next year?

**Bruce L. Tanner**

Cai, I'll take that one also. So pensions were -- we changed our long-term rate, I'd say the start of this year, I guess, end of last year to 8% per year. We're tracking very nicely to that as we sit here today. I think the overall global markets are above that, and we're tracking, I'll say, nicely with what a little less than 2 months to go on the year, but I feel good about what our returns are for this year. Next year's numbers were also premised -- well, I'll back up. Next year's numbers were premised on us achieving 8% this year. So that's the starting point. And as far as the CAS cost next year by itself, I'm trying to recall that, but I think the CAS cost itself goes up to like 1 point -- think of it $1.4-ish billion or so. Think of a FAS number, if we stop today somewhere around $2.1 billion, and that's how you get to the $700 million

FAS/CAS adjustment. And the contributions that we're expecting to make next year are essentially the same as this year, you should think as $1.1-ish billion range.

**Operator**

Our next question comes from Sam Pearlstein of Wells Fargo.

**Samuel J. Pearlstein - Wells Fargo Securities, LLC, Research Division**

Chris, I wanted to go back to something you had said earlier in the call. You talked about $1.2 billion of overhead reduction in the last few years and on the docket for another $1.1 billion this year. I guess I'm trying to just understand, how much does it cost for you to actually accomplish that? What kind of returns do you get, and then how much of that do you actually get to keep as opposed to it ultimately going back to the customer?

**Christopher Eugene Kubasik**

Yes, Sam. That's a great question. It varies by business area. This is pretty much the overhead reduction. A lot of this ties to some of the facility. I gave you some numbers on the facility square footage that were taken out. We do a business case and a payback for all these affordability projects that we have. And generally, they pay back within the 12- to 18-month cycle. So when we do something like facility consolidation, we'll be moving the cost of moving the cost of consolidating as it relates to that. Right now, we're about 50% cost plus 50% fixed price. So half goes in back to the government, if you will. The other half generally is built into our forward pricing to some degree. It really depends on the backlog mix. But the investment to get these overhead savings are not that significant and generally results in both people and capital assets as the main driver. Of course, we're focused on processes and new systems and such, but it's a pretty quick payback.

**Robert J. Stevens**

And Sam, I'll -- let me add to that. The conversation that we have internally here has placed a greater emphasis on this general subject of affordability and cost reduction because with or without sequestration, we know that we're facing a long cycle where the demands of our security customers are going to go up relative to their missions, and they're not going to have the economic resources available to meet those growing demands. And we've got to get out in front of this. So we're pushing ourselves, and Chris is absolutely right, and embedded in your question is the notion. You certainly want to pick the highest payoff opportunities and do them the soonest, and we are. But I'm not and we've not been reluctant to look at all sorts of cost-reduction opportunities even if they have a longer payback, as long as they payback because it's going to be a longer cycle process that we're involved with where it's going to take continuous refinement, continuous refocusing. And one of the benefits that we think we achieved from some of these reorganizations is not necessarily measured in the economic return but in our ability to have greater levels of agility and more refined resource allocation. So we can move with the increasing rate of the volatility in our markets. One of the characteristics we've seen out on the marketing horizon is this shorter cycle, much more highly volatile environment where change is occurring more quickly, and you have to be able to respond to that change. And so there's sort of this proportionality between the size and structure of the organization and the ability to move quick at the edge. And we're getting better at moving quick to the edge, and with that, we can take cost out of the business.

**Bruce L. Tanner**

Sam, you might get a triple out of this one because I'll speak to this one also, and I think I'm going to go back to something Chris said in his opening remarks. I think we're all good -- we've all demonstrated, we've all done this throughout our careers of taking the kind of actions to reduce facilities' headcount when it's required. And I don't think that's necessarily all that newsworthy or all that new and innovative. What Chris mentioned in his opening remarks that I'm talking about taking into account affordability into the design of products and sort of getting that upfront view of affordability, that's something I'm actually very excited about. And I think we've really just sort of scratched the surface on that. And as we see the chance to bid and win new products with that concept in mind, I think you will see some really interesting characteristics coming out of that because we are changing the nature of maybe how we've done that in years past in a manner and in a process that I think is going to pay off significantly to both ourselves and our customer.

**Operator**

Our next question comes from Carter Copeland of Barclays.

**Carter Copeland - Barclays Capital, Research Division**

Bob, let me join everyone in congratulating you on all your successes. I think, Chris, he's left you with a pretty high bar for stock price performance, and I think as a shareholder, he'll hold you to it. So best of luck on that.

**Robert J. Stevens**

Thank you. He's up to it, Carter. He's up to it.

**Carter Copeland - Barclays Capital, Research Division**

I want to expand on the last question, if you will. Obviously, your peers are sort of chasing down the cost curve as well to remain competitive, and I wondered if you might tell us how it is that you benchmark yourself against the peer group to see how well of a job you're actually doing and getting cost out. I mean, obviously, there's a lot of overhead that's going to need to come out of the industrial base, given the budget forecast that we're looking at even out without sequestration. And so I wondered if you might share with us how it is that you benchmark yourself, and then give us kind of an assessment of where you are relative to your peers and your efforts so far.

**Robert J. Stevens**

Yes, I'll be very blunt about this. We started to take cost out before our peers, and we had no reservation about being the first mover here as there are an extraordinary number of metrics that we can benchmark ourselves to. We think one of the most meaningful ones is examining our win rate when we get our feedback from our customer. How many competitions are we losing because we were not cost competitive because that brings at home more clearly than anything else. I think what will give us the competitive advantage as we move forward with a competitive group that is also attempting to remove cost is we've made significant new investments in new products, where others have older product lines that will require new investments. For example, we have the Littoral Combat Ship. We have the F-35 Joint Strike Fighter which is a fifth-generation capability. We've refreshed Aegis to an open architecture. We evolved PAC-3, and we're evolving the THAAD missile system. These are all new and fresh technologies. We have a similar portfolio in Space Systems. The vitality and the vibrancy and the recent investment in these new next-generation systems I think has a lot more legs in a competitive climate, particularly in a climate where we'll be taking cost out. So our goal here is to focus on the benchmarks in the industry. We're entirely comfortable of front running the industry when we have confidence in knowing what we have to do and how we have to do it, and we have that confidence. We think we have a relevant portfolio that's proven. And as we drive higher levels of affordability, we think we'll pass that metric of cost competitiveness in competitive awards as we look forward.

**Christopher Eugene Kubasik**

Yes, Carter, and I'm glad you asked the follow-up question because we do spend a lot of time talking about affordability. And the point I was trying to get across is it's more than the cost cutting. We talked about the supply chain, and Bruce reemphasized the importance of the engineering and design. We can go on all day, but another very, very important element is the volume. And the executive leadership team spends a fair amount of their time traveling the globe, building relationships, meeting with customers because we all know whatever product it is, if we can get some of our allies and friends around the globe to also purchase airplanes or missiles, not only does the U.S. government benefit but they benefit as well just from a financial perspective. There's obviously a strategic, operational and other benefits of a coalition warfare. But that's another leg of the affordability, and we spend a lot of time trying to grow this business. And that's one of the benefits that all of our customers realize.

**Jerry F. Kircher**

Ally, this is Jerry. Just to be sure, I've got a note here that there's 7 people in the queue. We have some ability to go longer today, so we'd like to catch the people that are still in the queue. So we're going to extend the call, if that's all right. So let's do the next caller.

**Operator**

Our next question comes from Rich Safran of Buckingham Research.

**Richard Tobie Safran - The Buckingham Research Group Incorporated**

Bob, once again, best wishes. I wanted to just ask about, if I might, about build rates at Aeronautics, C-130J, C-5 and F-16. I think you're delivering 34 C-130Js this year, 37 F-16s if I got my numbers right. Just wanted to know if you could comment if you're anticipating similar run rates next year, or could this moderate some? Also, I know you're tracking a bunch of new orders and I just wanted to know if any of them you think might impact '13 deliveries.

**Bruce L. Tanner**

Rich, this is Bruce. I'll take that one on. Chris made an interesting observation relative to our expectations next year with the F-35 deliveries surpassing both C-130 line and the F-16 line. I think that's kind of the new era that we're facing in the corporation, an era where obviously the F-35 is going to become the dominant production line in the corporation. And it started this quarter, the third quarter with more deliveries for the F-35 in this quarter than any of the other 2 aircraft as well. As we look into 2013, and I look at Aeronautics in general, there's a lot of mix that's going on within Aeronautics. In my prepared remarks, I said that Aeronautics is going to be relatively comparable next year from a revenue perspective to where they are this year, but there's a lot of moving pieces in that number. So you're spot on with the aircraft quantities that you gave for 2012. You should expect somewhere on the order of 20 to 25 fewer F16s next year than this year, and that's predominantly because we're building in 2012 some 24 aircraft for the government of Turkey, and they're actually being built off the Turkish line. So while we hate to lose the aircraft, I guess the good news of that discussion is that, really, the aircraft build rate at Fort Worth won't change from 2012 and 2013. So there's an element of stability there that might not be apparent, given the quantity changes. We're also looking to lower the C-130 build rate. You're right, the numbers, we should do 33, 34 this year or so. We're going to ramp back down to about a 24 per month -- or I wish it's a month, 24 aircraft per year build rate on the C-130 beginning next year, and we think that, that level allows us to have again sort of a stable build line for a number of years going into the future. And then offsetting those 2 reductions, which may not be all that apparent, I don't think you mentioned C-5 but we're going to deliver 3 or 4 of the C-5 in the RERP aircraft or Re-engining and Reliability Improvement Program for C-5s. And those 3 or 4 will grow to probably close to 10 or so next year. We're getting very close to the sort of the maximum rate on the C-5 program, which I think it's about 11 aircraft per year to modify those 49 C-5 into the RERP configuration. So between the lower F-16s, the fewer C-130s, higher C-5 and then the missing piece is higher F-35 volume next year, Aeronautics is going to stay relatively comparable. But again, as I just indicated, a lot of moving pieces in that discussion.

**Christopher Eugene Kubasik**

And Rich, you asked us, while we'll be working hard to get new orders over the next several months, none of those would impact 2013 deliveries, it would be beyond the calendar year.

**Operator**

Our next question comes from David Strauss of UBS.

**David E. Strauss - UBS Investment Bank, Research Division**

I think this one's probably for Bruce. In terms of your guidance for 2013, not exactly sure what above 11% means, but in terms of the margins, but if you could help us a little bit with the big pieces that would impact margin next year, obviously a little bit lower volume. I think USA is going away, level of cume adjustments and whatever else you want to throw in there.

**Bruce L. Tanner**

Yes, I'm not sure I'm going to get at this point, David, any more specific than what we provided in the press release relative to the margins that we did say. I do think we're going to be above 11%. I think as I said in my remarks seventh consecutive year where we have been above 11%. As we look at 2013, maybe what I ought to do is just kind of go around by the business areas and talk a little bit of that. I spent a lot of time just talking to Aeronautics, I think Aeronautics revenue I should say. If I think of the earnings around the margin of Aeronautics, because of all the mix changes that I just described, I think we'll have slightly lower margins at Aeronautics primarily because of the mix changes that I just described. We're losing some F-16s and losing some C-130s at higher margins and replacing that with C-5 and F-35 at lower margins. I still think we'll be in the 11-ish percent range for Aeronautics. So not a huge drop-off but probably not as high as this year. If I go over to Electronic Systems, I think Electronic Systems is probably the one business area I can look at and say even with the numbers I'm seeing now, I'm hopeful at least that there will be some potential for some modest growth there above even what I'm thinking of for 2013. And relative to the margins, I think the margins will stay at the 13-plus percent range. I'll qualify that though by saying that we're going to give you in January a new configuration with 2 new business areas. So I'll say I'll hold that thought till January, but I'll give you the data in the current configuration. And I would say we're going to stay fairly close to where we are today from a margin perspective in all of Electronic Systems. Space Systems is likely going to be down slightly, primarily because we will have slightly lower equity earnings because of the USA closure. For all intents and purpose that, that joint venture is coming to a close this year. Despite that, I think with some of the production satellite programs that are now going through the production phase and are well out of the developmental phase, we're seeing some higher margins on those contracts, and I think that we'll probably see margins a little bit lower. But I would guess in the mid-11 for Space Systems going next year, they've had a benefit this year from a couple of the closeouts that we talked about the wind down of the USA that won't replicate next year. And then I guess the last, IS&GS, I would think it will follow very closely to where we are now, somewhere in the 9-ish percent margin range. I think I covered all 4 of them, David, probably more detail than you care to hear, but I think that covers it.

**Operator**

Our next question comes from Robert Spingarn of Credit Suisse.

**Robert Spingarn - Crédit Suisse AG, Research Division**

Bob, again, congratulations, and best wishes.

**Robert J. Stevens**

Thanks, Rob.

**Robert Spingarn - Crédit Suisse AG, Research Division**

Two -- I'll try to make them quick. One for Chris, one for Bruce. Bruce, I'll just start with you. On your color on '13, are you assuming full obligation of CR funds to spending authority limits, or do you embed some kind of cushion for this half-paralyzed environment we've seen at times this year because unless we assume full resolution of sequester by early '13, I would think -- and formal adoption of the fiscal '13 president's request, might we think of this as a best case scenario at least for revenues?

**Bruce L. Tanner**

Rob, I thought about that quite a bit, and I don't think so. I don't think it's the best case scenario. I mean, obviously the worst case would be a sequester, but is this a best case? I'm not sure of that. We have very...

**Robert Spingarn - Crédit Suisse AG, Research Division**

Negotiated outcome would be something between what I think your assumptions are and full sequester.

**Robert J. Stevens**

Rob, let me -- so when we paid this, they're -- now we're talking about some combinatorial -- some possibilities here. But it is possible we'll have a CR through March 27, and it's possible that a CR will be extended. There are also appropriation bills that have been marked, and a fair amount of effort has been gone into, let me say, preparing those bills to move. So it is possible the bill could move even without a resolution to sequester because part of these interesting combinations that make any detailed planning on our part impossible as to what the outcomes could be would be a movement of the appropriation bills and some deferral sequestration while a more thoughtful process to achieve what's called the larger or the big transaction, the full scope resolution that includes tax policy, entitlement reform and defense and nondefense discretionary spending. That could occur too. Thereby, lifting the opportunity in 2013 with regard to appropriated levels of funding rather than CR levels of funding. So there are interesting combinations here that could either put a little pressure on '13 or actually relieve some pressure on '13. Sorry to interrupt you, Bruce.

**Bruce L. Tanner**

No, I was -- Bob is talking in much more detail and thorough answer probably than I was going to do. Rob, the other thing I was going to say is

I'll just remind you of our portfolio as you go around the 4 business areas, really Aeronautics and Space Systems for a large intent and purposes don't have much impact to the CR because most of their sales are coming from fiscal year '13 budgets. So very -- I'm not sure I used the word insulated but very little impact from there. IS&GS, as I've said many times, short-cycle business would be the most subject to CR. But frankly, we weren't expecting a whole lot of growth year-over-year, fiscal year over fiscal year in that business to begin with. And then Electronic Systems is somewhere in between. I think you had a question for Chris that you didn't get to ask, Rob.

**Operator**

Our next question comes from Myles Walton of Deutsche Bank.

**Myles A. Walton - Deutsche Bank AG, Research Division**

Best wishes, Bob. A couple of follow-ups and clarifications. You didn't mention when you're talking about bookings the larger Space contract that I think was a 2012 opportunity, and I don't think you mentioned it within the realm of the '13 opportunities either. Is that still on the table? And I guess, Bruce, it's not implied to get to $80 billion, you need this to happen.

**Bruce L. Tanner**

Rob, I'll just say our government satellite -- or I'm sorry, Myles. That's 2 calls in a row. I called you the wrong name, Myles. I'll just leave it and say that our government satellite business is very healthy, strong and well supported. The $80 billion achievement if we're able to get that this year, I didn't mention that re-alliance [ph] on government satellites because I'm not concerned about that relative to our ability to achieve that number.

**Myles A. Walton - Deutsche Bank AG, Research Division**

Just to clarify. So you don't need it to achieve the number?

**Bruce L. Tanner**

We do not.

**Myles A. Walton - Deutsche Bank AG, Research Division**

Okay. And then the other question was really more around the F-35 and the overall life cycle opportunity, which has always been a key part of that program. It sounds like the customer wants to, not surprisingly, insert some competition to maintain pricing discipline. Has your view changed on Lockheed Martin's ability to capture that tail of the program and really make it into the bigger opportunity that's always been if you could capture that aftermarket strength?

**Robert J. Stevens**

Well, Myles, we, one, know the program pretty well, know the demands. Nobody wants to lower the total cost of operation of this airplane more than we do along with our customers. We see competition in every aspect of this business every day, and we certainly not only don't fear the competition, it actually makes us better. I think our customers realize that. So if there are competitive opportunities here that also lower the total cost of operation, we are certainly going to pursue them and pursue them aggressively. I think we have the insight that one would have from being the design agent and the prime contractor overseeing the supply chain. I think we are as able as anybody to provide very high-quality, very low-cost support service throughout the life cycle of this airplane. So we'll look forward to these discussions.

**Operator**

Our next question comes from Peter Arment of Sterne Agee.

**Peter J. Arment - Sterne Agee & Leach Inc., Research Division**

Congratulations, Bob. Chris, a question regarding -- I guess when you were talking about the reorganization and taking cost out, and I can appreciate stripping out some of the management. But I'm surprised you're not seeing -- doing more I guess in IS&GS, given that, that's where you're seeing the most delay awards or scope reductions, and the customers have been focused on price. Is there opportunity there to continue to take cost out, or is it just not businesses that you want to break out for competitive reasons?

**Christopher Eugene Kubasik**

Yes, Peter. We think we've been very aggressive in taking out cost. I think back a couple of years, I think we had over 145,000 employees. We're currently at 120,000. We don't announce but we're happy to talk about the layoffs. There've been significant layoffs probably every quarter for the last 8 quarters. We highlighted this because of the reorganization, but we've streamlined over the years, I recall when IS&GS had about 11 different companies, if you will, or components, we're now down to 3, civil and defense and Intel line of business. We're very competitive. Bob mentioned, we look at our win rates on occasion when we lose competition. I'm not aware of any competition in IS&GS where we've lost as a result of cost. So again, we've done a fair amount. We'll continue to look at it. And of the $1.1

billion, I'm sure a couple of hundred million of that is coming out of the IS&GS. I just didn't differentiate it or highlight it for you.

**Operator**

The last question comes from Noah Poponak of Goldman Sachs.

**Noah Poponak - Goldman Sachs Group Inc., Research Division**

Congrats, Bob, on your last call.

**Robert J. Stevens**

Thanks, Noah.

**Noah Poponak - Goldman Sachs Group Inc., Research Division**

Since I'm last, I'm going to try to sneak in 2 follow-ups to some of the other conversations you had. So the first one is with regard to the potential strategies with which sequestration could be avoided, Bob, I wonder, are there 1 or 2 kind of bigger things that are being discussed on the Hill that are floating to the top? And what are the high points of them, if there are? And then secondarily and separately, on the margin topic, you mentioned in your remarks you've had 6 or 7 years in a row with the segment operating margin above 11%. I basically wonder if you think you can repeat that. You've talked about the cost reductions and productivity improvements. On the other hand, you have a generally tougher customer, presumably these EAC adjustments wind down and become a headwind. Is that 11% kind of a reasonable longer-term margin, or does it need to come down?

**Robert J. Stevens**

Yes, I'll start with the discussion about strategies for sequestration. Of course, on the hill now, there is no discussion because we're in the recess prior to the election. To perhaps oversimplify this but maybe a little over simplification is good because it is really a complex set of scenarios right now. Three things -- one of 3 things will likely happen. We'll get a resolution or the grand bargain outcome, which tends to have value ranges of $4 trillion to $5 trillion, which is a significant amount of work that would go in, looking at tax, looking at entitlement, looking at spending. The onset of sequestration could be delayed beyond January 2 maybe to be coterminal with the CR in March or maybe beyond that or sequestration will take effect. My sense is the latter 2 are a little bit more likely than the first one. It would seem to be hard to get a grand bargain in a lame-duck session of the Congress. So my guess is we'll either see a delay of the onset or sequestration will take place. When you think about sequestration taking place, we already received from the Department of Defense additional planning guidance that we received on September 28 that said, they don't anticipate taking any contract actions on January 2. And they thought it was unlikely that they would take contract actions for several months beyond that, which puts us through our first fiscal quarter and puts the government into its second fiscal half before any impacts might be realized at least on the defense side. Civil government agencies are going to be different, and they don't have the large acquisition accounts, and a lot of their expenses are associated with people. So it's just not clear. I know every one of us wants to be in a position of doing better at predicting what will happen with respect to sequestration. But I can tell you, I don't know, and I don't know anybody who does know. There's a lot of speculation, but there's not greater clarity. So inside our company, we're preparing for the prospect of sequestration. As I said, we will issue WARN notices if that's required, if sequestration has reductions in force. We're working every day to try to avoid that. In the interim, we're asking our employees to stay very focused on the tasks at hand. And I think you see in the third quarter and in the year-to-date performance an exceptional quality by the talent in this company and their professionalism and staying focused on the goal, on the mission, on execution, and they are not being distracted by this. And for that, we are all so enormously proud of them for remaining focused like that. So the best we can do is try to keep you posted on how sequestration unfolds. Obviously, the next event would be what happens in the lame-duck session of Congress. Relative to margins, I do think that it is possible to sustain these margins over the long run, and we haven't given up on attempting to improve these margins. It has a lot to do with your portfolio. It has a lot to do with your business mix, and it has a lot to do with how well you're able to execute. And we make investments every day on building this portfolio to have real legs and real durability in a complex global security environment. We do focus every day on execution, and we're taking this business more broadly internationally and expect to have pretty robust opportunities to perform.

**Bruce L. Tanner**

So I'll just add, I think we are structurally different today and going forward than we were maybe a few years back, that has helped our situation as well. And Bob mentioned the international contact growing. I think that's one thing that contributes to the ability to maintain the 11%. We've talked a lot about our equity earnings. Those are companies that we did not have, I'll say, the margin boost from recognizing those equity earnings in years past, and that had -- sort of in the case of United Launch Alliance, that's sort of a double benefit because you lost the sales associated with that activity. So the margin improvement was pretty substantial. The last thing I'll point to sort of a structural change is if you just think of all the combinations that led to the current Lockheed Martin, a number of those brought with them intangible amortizations associated with those acquisitions. And those were a drag on margins in the early years of this corporation as well that no longer exist as we sit here today. Bob?

**Robert J. Stevens**

Thanks. First, let me thank everybody for being on the call. We had a long day. You had a longer day. So we appreciate you being here with us. I certainly appreciate your kind words and all the good wishes you offered me. I was thinking that since I became our company's Chief Financial Officer in 1999, we've had about 52 quarters together to have these exchanges, and I have really enjoyed the interaction that we've all shared over the years. I want to wish each of you well in your professional pursuits and certainly in your personal lives. At this end, I'm certain our company is in great hands with Chris and Marillyn and Bruce and Jerry and the other members of the executive team. I'm really grateful for having the privilege of working on this management team and having had the opportunity to work with my fellow employees here who are simply exceptional people who do extraordinary work in the nation's interest. I will miss them, and I will miss you, but I will be listening to these calls. So I'm sure that Chris and Bruce look forward to talking with all of us in January. We'll sign off from this end. Thank you.