L3HARRIS TECHNOLOGIES
Fourth Quarter Fiscal Year 2019 Earnings Call
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Operator: Greetings, and welcome to the L3Harris Technologies Fourth Quarter Fiscal Year 2019 Earnings Calls. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. If anyone should require operator assistance during the conference, please press *0 on your telephone keypad. As a reminder, this conference is being recorded.

I would now like to turn the conference over to your host for today, Anurag Maheshwari, Vice President of Investor Relations. Thank you. You may begin.

Anurag Maheshwari: Thank you, Dana (sp). Good morning, everyone, and welcome to our fourth quarter fiscal 2019 earnings call. On the call with me today is Bill Brown, CEO; Chris Kubasik, CEO; and Jay Malave, CFO.

First, a few words on forward-looking statements. Discussions today will include forward-looking statements and non-GAAP financial measures. Forward-looking statements involve assumption, risks, and uncertainties that could cause actual results to differ materially from those statements. For more information, please see the press release, the presentation, and our SEC filings. A reconciliation of non-GAAP financial measures to comparable GAAP measures is included in the quarterly materials on the Investor Relations section of our website, where a replay of this call also will be available.

As supplemental information for investors, discussions only will include selected L3 and Harris combined financial information, which combines the historical operating results as the businesses have been operating together on the basis of a newly-announced four-segment structure during prior period but excluding the operating results of Harris' Night Vision business and (INAUDIBLE) businesses.

With that, Bill, I'll turn it over to you.

Bill Brown: So, thank you, Anurag. Good morning, everybody. I'm excited to welcome you to our first-ever L3Harris Technologies Earnings Call. I'm also pleased to welcome our new Chief Financial Officer, Jay Malave, who joined us on July 1st from United Technologies, where he most recently was CFO of carrier. Prior to that, Jay spent more than 20 years in the aerospace businesses, including as CFO of United Technologies Aerospace Systems and working the integration of the Goodrich acquisition.

Many of you know Jay from his time leading the Investor Relations function at United Technologies, and I'm thrilled to have him onboard and confident he will be a strong business partner to me, Chris, and the rest of the management team.

As you're aware on June 29th, in fact in minutes after we ended Harris' fiscal '19, we successfully completed the transformative merger, establishing L3Harris Technologies, and we really hit the ground running. On the first working day after closing, we consolidated headquarter activities between Harris and L3 and announced our new organizational model, creating four mission-focused segments that combine the top talent of both companies.

In the first week, we completed 115 townhalls with senior leadership, touching 80% of all employees, and then in the second week, we held a multi-big leadership meeting, where Chris and I shared our joint vision, the values, and operating philosophy with nearly 100 executives and set our initial game plan. And I have to say that the level of energy and excitement across the company is extraordinary.

So, we're off to a good start as a combined company. We'll talk more about that in a few minutes, but let me first begin by providing an update on Harris' four quarter in fiscal '19 results followed by Chris with L3's Q2 and first-half results and then Jay with combined L3 and Harris financials and guidance.

So, starting with Harris on slide three, we ended fiscal '19 on a high note with fourth quarter at non-GAAP earnings per share up 39% on revenue growth of 12%, the highest top line growth we've seen in eight years. Overall, the company margin in the fourth quarter expanded 80 basis points to a record 20.2%.

These results cap an exceptional year, in which we accelerated revenue growth and had margin expansion in all three segments. We outperformed on all guidance metrics, and we delivered a record earnings per share of $8.29, up 30%, and free cash flow of $1.055 billion. Total company book to bill was 1.1, driving funded backlog growth of 12% and setting us up for continued top line growth. All three segments contributed to our strong performance, driven by their top line growth, which continued to exceed expectations.

Let me take a few minutes to recap some of the highlights of the year on slide four and five with additional segment detail in the Appendix. Communications Systems had a terrific year with revenue up 14% from solid growth in DoD Tactical and Public Safety. DoD Tactical ended the year with revenue up 31% from last year and up 80% from fiscal ’17. This strong growth was driven by nearly $300 million of modernization demands from the Army, Marine Corps and SOCOM, as they embark a multi-year upgrade cycle.

Modernization order momentum continued in the quarter, with the Army awarding us a second HMS manpack LRIP order followed in July with the release of the two-channel leader radio RFP. We also continued to execute well on our strategy to penetrate adjacent airborne markets and were awarded the initial prototype phase of the Air Force’s airborne high-frequency radio modernization program, expanding our leadership in HF from ground to airborne.

International Tactical performed as expected, and revenue was up 3% for the year, driven by the ramp of the Australia modernization program, early adoption of multichannel products in Canada and Western Europe, and ongoing counterterrorism support in the Africa. Overall, Tactical ended the year stronger than initially expected with revenue up 14%, book to bill of 1.1, and backlog up 17% to $1.1 billion. This combined with the well-supported DoD budget request, increasing international demand for two-channel radios, and executing on expansion into adjacent sea gives us confidence in the continued growth trajectory and tactical for the second half of the year and the medium term.

In Electronic Systems, revenue increased 14%, the ninth consecutive quarter of revenue growth, ending the year up 9%. This strong performance was driven by sustained growth in long-term platforms F35, F18, and F16, and more recently by growth on B52 and SOCOM rotary aircraft; all of which collectively grew double digits, as we leveraged technology upgrades and ramped production.

Orders were strong in ES, ending the year at nearly $3 billion in bookings with two-thirds from the avionics and electronic warfare franchises, as we continue to leverage our longstanding customer relationships to solidify our position on new and long-term platforms.

In April, we received a $340 million award for F35 release systems, supporting the LRIP 12 through 14, which means all of our F35 production content across avionics and release systems is now under multi-year contracts, which increases medium-term visibility. We also received a $72 million production order to deliver upgraded countermeasure electronic warfare systems for the B52 platform, bringing that program's current value to over $430 million against a $1.3 billion total opportunity. This order momentum, along with our investments in innovation, increased content on existing platforms, and expansion of the next gen platforms, will drive a multi-year growth cycle in avionics and electronic warfare.

In Space and Intel, revenue was up 8% for the quarter and the year, well above our initial expectation of 4 to 5%, driven by mid-teens growth in our classified business. Order momentum was even stronger, as we saw continued success in strengthening incumbent positions and expanding the addressable market of our classified business by providing end-to-end mission solutions and penetrating new adjacencies.

I'm also pleased with our relentless focus on operational excellence, which drove margin expansion across each of our segments, despite the mixed challenges that come with new program starts. Our operational excellence program called HBX has driven net productivity savings that have more than off-set the dilutive margin impact of DoD tactical modernization and revenue growth on long-term platforms in classified space, resulting in total company margin of 20.2% for the fourth quarter and 19.8% for the year, 90 basis points of margin expansion.

Similarly, our multi-year focus on working capital has delivered terrific results. We ended the year with working capital of 41 days, a four-day improvement over last year and a 37-day improvement since the Exelis acquisition. Our working capital reduction combined with earnings growth resulted in record free cash flow of $1.055 billion, exceeding the post-Exelis acquisition goal of 1 billion by 2019.

Overall, we had an outstanding year of accelerated revenue growth, margin expansion, and record EPS and free cash flow, exceeding the targets we set for ourselves. And we'll continue building on this momentum as we go forward as L3Harris to drive continued above-market growth, margin expansion, and cash generation, creating long-term value for our shareholders.

Let me now turn it over to Chris to discuss L3 results for the quarter and the first half. Chris?

Chris Kubasik: Okay. Thank you, Bill, and good morning, everyone. Let me take a moment to thank and congratulate the L3 and Harris teams for their hard work this past quarter. Today's results from both companies are due to everyone's focus in the uncertain times leading up to the close of historic merger.

As Bill mentioned, day one was seamless. We rolled out new email addresses to all L3Harris employees, launched the new website and portal that connected the 50,000 employees across the globe, and installed new signage at our 50 largest sites. On the operational side in the first week, we issued nearly 40 RFPs to our supplier base, totaling 900 million in annual spend to start leveraging the purchasing power of the combined enterprise and to work towards our cost synergies goal.

Shifting now to L3 results, we had a solid second quarter, highlighted by our consolidated margin and free cash flow, both out-performing the second quarter guidance we discussed on our May earnings call. Margins expanded 160 basis points to 12.2%, and free cash flow was up 38% to $220 million. Non-GAAP EPS was up 18% to $2.91 on 2% revenue growth. These results capped a strong first half with EPS up 21% on 8% revenue growth.

Total company margins expanded 130 basis points to 11.9%, and free cash flow was $365 million or five times last year's first half, as we executed on working capital improvements that resulted in a 12-day reduction over the past 12 months. Orders were up 8%, resulting in a book to bill of 1.11, and funded backlog increased 16%.

Turning to the segments on slide six, ISR revenue grew 2%, driven by a ramp up in WESCAM turret systems and the strength of our ISR missionization business, as several key programs accelerated, including the Australian Peregrine and the Presidential aircraft recapitalization programs. This growth was partially off-set by lower deliveries of Night Vision products due to export timing, and operating income was up 50%r, resulting in margin expansion of 460 basis points to 14.3%. This was due to higher volume, improved contract performance, and L3 65 savings. In the first half, ISR revenue was up 12%, and operating income grew 45% with margin expansion of 280 basis points to 12.3%.

In the Communication segment, revenue was flat in the quarter with higher production volume for UAV communication systems, off-set by lower volume in the integrated maritime and microwave product sectors. Margins declined by 130 basis points to 7.9% from the dilutive mix impact of the maritime developmental programs and the continued investment in unmanned under-sea vehicles. For the first half, segment revenue was up 5% with margin expansion of 20 basis points to 9.3%.

Lastly, the Electronics segment second quarter revenue was up 3% with strong growth in precision engagement systems, which includes diffusing an ordinance business at 35 display systems and airport security equipment, more than off-setting the expected headwinds in the defense training solutions due to last year's competitive loss of the C17 training contract and lower volume from commercial flight simulator sales. Margin expanded 10 basis points to 13.6%, and in the first half, segment revenue was up 3% with margin expansion of 10 basis points to 14.1.

Overall, L3 had a strong first half, tracking above the guidance set at the beginning of the year and ahead of the amounts disclosed in the S4. Looking forward, as we announced on July 1 and detailed in the Appendix to the webcast slides, we have organized L3Harris into four segments that group technologies and capabilities to allow us to compete across multiple missions and domains. Cutting across theses segments, we have business development, operations, and program excellence functions to drive further growth while achieving greater cost and operational and programmatic efficiencies.

We have worked on the structure since we announced the merger in October and have assembled an outstanding, seasoned, and collaborative team to lead the new organization. I'm excited to be part of it and look forward to the work ahead.

With that, I will turn it over to Jay.

Jay Malave, Jr.: Thank you, Chris, and good morning, everyone. It's an honor to join the L3Harris team, and I look forward to working with the analysts and investor community once again. In a moment, I will discuss L3Harris guidance for the second half of calendar year 2019, and as a reminder, we have transitioned to calendar year reporting.

But beforehand in order to provide context and support for the guidance, I will walk through the L3 and Harris combined financials for the first half of calendar year 2019, which we prepared on the basis Anurag described at the start of the call, and I will also note various drivers in (INAUDIBLE) comparisons in those results. Similarly, all comparisons included in the guidance discussion are to the comparable prior-year period L3 and Harris combined financials.

Okay, starting with results. In the second quarter, revenue was up 7%, and EBIT increased 16% on higher volume and operational efficiencies, resulting in margin expansion of 140 basis points to 16.3%. EPS grew by 27% to $2.42, and free cash flow was $487 million for the quarter. For the first half, revenue was up 10%, and EBIT increased to 17% also on higher volume and operational efficiencies, resulting in margin expansion of 90 basis points to 15.8%. EPS grew 27% to $4.65, and free cash flow was slightly above $1 billion, up more than 50% from last year. First-half book to bill was 1.07.

Turning to our new segment structure on slide eight, integrated mission systems revenue for the quarter was $1.25 billion, up 3%, driven by strong growth in electro-optical airborne imaging systems and continued strength in the ISR aircraft missionization business, including the Australian Peregrine program. Operating income for the segment was up 14% to $158 million from higher volume and improved program performance. Operating margin expanded 110 basis points to 12.6%. For the first half, segment revenue was up 12%, and operating income increased 17% with margin expansion of 50 basis points to 12.1%. First-half book to bill was 1.16.

Next in Space and Airborne Systems on slide nine, revenue for the quarter was $1.2 billion, up 17%, driven by double-digit growth in avionics and electronic warfare from a production ramp and new contact on long-term aircraft platforms as well as continued strength in classified space. Segment operating income increased 25% to $225 million, and margin expanded 120 basis points to 18.8% from higher volume, strong program performance, and operational efficiencies. For the first half, segment revenue was up 16%, and operating income increased 19% with margin of 18.2%. First-half book to bill was 1.13.

Switching to Communication Systems on slide 10, revenue for the quarter was up 6% from strong growth in DoD tactical and public safety, partially off-set by lower deliveries of L3 Night Vision products due to timing and the transitional impact to full operational capability of the UAE land tactical system program. Segment operating income was up 10%, and margin expanded 80 basis points to 21.6%. A strong program execution off-set the mixed impact from the ramp in tactical radio modernization programs. For the first half, segment revenue was up 12%, and operating income increased 18% with margin expansion of 100 basis points to 21.5%. First-half book to bill was 0.96, and that's coming off a book to bill of 1.27 in the last six months of 2018.

And lastly in Aviation Systems on slide 11, revenue for the quarter was up 2%, as growth and precision engagement, airport security equipment, and FAA programs was partially off-set by the expected headwind in defense training solutions due to last year's loss of a C17 training contract and lower volume for commercial flight simulators. Segment operating income was up 11%, and margin expanded 90 basis points from better cost management. For the first half, segment revenue was up 1%, and operating income increased 9% with margin expansion of 90 basis points to 10.5%. First-half book to bill was 0.99.

Okay, now turning to guidance for the second half on slide 12. The strong year-to-date performance gives us confidence that we will continue to outperform markets in the back half of the year. Starting with the top line, we expect second-half revenue to be up in the range of 9.5 to 10.5% with strong growth across all segments. This is supported by high visibility sales coverage from our backlog and high probability follow-on opportunities.

Second-half total company EBIT margin is expected to be up approximately 170 basis points to 16.7% from higher volume, operational efficiencies, and cost synergies. EPS is expected to be in the range of $4.95 to $5.05, which reflects higher profit and share repurchases, which we will initiate over the next few days. As announced on July 1st, the board has approved a 10% dividend increase and a $4 billion share repurchase authorization program, of which we will utilize $2.5 billion over the next 12 months.

In the second half, we expect to generate free cash flow in a range of 1.3 to $1.35 billion, reflecting higher earnings and a one-to-two-day reduction in working capital from June 2019. Capital expenditures are expected to be $190 million or 2% of revenue in the second half. For the full year, revenue is expected to be up in the range of 9.5 to 10.5% with EBIT margin of approximately 16.2% and EPS in the range of $9.60 to $9.70. Full-year free cash flow is expected to be in the range of 2.3 to $2.35 billion.

Turning to the EPS bridges on slides 14 and 15, expected second-half EPS at the midpoint of $5 reflects an increase of $0.94, driven by higher volume across the four segments, operational efficiencies, and cost synergies, partially off-set by the impact of a higher tax rate of about 18%. Expected full-year EPS at the midpoint of $9.65 reflects a total increase of $1.65 with $1.70 driven by operational improvement and cost synergies and additional $0.17 coming from the elimination of L3 intangible and pension amortization and lower interest and shared health, partially off-set by $0.22 tax headwinds.

Switching to the segment outlook, in Integrated Mission Systems, we expect revenue to be up approximately 10.5% in the second half, driven by continued strength in airborne imaging systems and growth in ISR aircraft missionization and maritime platforms with operating margin of approximately 12.5%. Full-year segment revenue is expected to up approximately 11.2% with operating margin of approximately 12.3%.

Space and Airborne Systems revenue is expected to be up approximately 11.5% in the second half, driven by continued double-digit growth in avionics and electronic warfare and strong growth in classified space. Segment operating margin is expected to be approximately 18.7%.

Full-year segment revenue is expected to grow approximately 13.9% with operating margin of approximately 18.4%.

Communication Systems revenue is expected to be up approximately 9.5% in the second half, driven by strong growth across all sectors with operating margin in the range of 22.1%. Full-year segment revenue is expected to be up approximately 10.7% with operating margin of approximately 21.8%.

Lastly, Aviation Systems revenue is expected to be up approximately 7% in the second half, driven largely by continued double-digit growth in precision engagement. Operating margin is expected to be approximately 14% from improvements in EDD and productivity initiatives across the segment. Full-year segment revenue is expected to grow approximately 4% with operating margin of about 12.3%.

So to summarize, we expect the first-half momentum to carry over to the second half in addition to the benefit from cost synergies, resulting in a strong 2019. I'll stop here and turn it back over to Bill for closing remarks.

Bill Brown: Well, thank you, Jay. I know that's a lot to take in. So, let me wrap up with a few comments on the budget and our strategic priorities going forward. In regard to the budget, I'm very encouraged by the recent bipartisan deal raising the BCA caps over the next two years and removing a threat of sequestration. We continue to believe the House and Senate will support increased funding to meet national security demands, which are well-aligned with our core franchises, and with budget outlays continuing to lag budget appropriations, we expect growth momentum to continue in the medium term.

A few weeks ago, Chris and I aligned with our leadership team on our top strategic priorities, first and foremost being integration and accelerating in the capture of cost synergies. We now expect to hit a gross run rate of $150 million by the end of calendar '19, putting us on track to meet or exceed 40% or $200 million of gross savings in calendar 2020. We're off to a great start on segment and headquarter consolidations and supply chain activities, and we're growing increasingly confident of exceeding $500 million gross cost synergies in calendar '22.

Other priorities include driving operational excellence through our new program called E3, Excellence Everywhere Everyday, establishing a new performance culture building on the strengths of both companies, investing smartly and aggressively in technology to grow revenue and increase share, reshaping our portfolio to focus on high-margin, high-growth technology differentiated businesses, and maximizing cash flow that will be returned to shareholders through repurchases and dividends. Overall, the progress and alignment in the first 30 days has exceeded our expectations, and we feel even more confident in the strategic combination and our ability to deliver shareowner value.

So with that, let me turn to the operator to open the line for questions.

Operator: Thank you. At this time, we will be conducting a question-and-answer session. If you would like to ask a question, please press *1 on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press *2 if you would like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the * keys.

Our first question comes from Robert Stallard of Vertical Research Partners. Caller, you may proceed.

Robert Stallard: Maybe a quick first question for Bill. There was some commentary at the Paris Air Show that the combined company might be looking at some post-merger disposals, and I wonder if there'd been any further thought or development on that front.

Bill Brown: Well, Rob, thanks for the question. Yeah, it's definitely a key priority, as I mentioned in my closing remarks in terms of top priority for the management team. Certainly, as we've talked about before in this call and other venues, a broader mix of businesses gives us an opportunity to take a fresh look at the combined company portfolio and really think about what fits, what doesn't fit. It certainly gives an optionality to do some things with businesses that we no longer consider strategic.

We continue to look at this through a couple of different lenses. Certainly, one is does the business have technology that's required by differentiation. Can we deliver good returns? Can we grow and win green share, etc.? And we're going to evaluate what businesses were based in those metrics. We continue to have this dialogue. Chris and I are working very hard on this. We're engaging our new board on this as well. We're not going to deliberate decisions and discussions in public, but it's certainly top of mind to us, Rob.

Robert Stallard: Thanks, and then maybe a follow-on for Jay, and welcome back. In the free cash flow guidance, there's around $400 million worth of adjustments, and I was wondering how many of these are one-off items of 2019 and won't be repeating themselves in 2020 and beyond.

Jay Malave, Jr.: So, you're talking in the back half, Rob?

Robert Stallard: Yeah, it's in the release. There is a reconciliation of the guidance for the full-year, where you've got 1875 to 1925, and then, there are a number of adjustments to get you to 2.3 to 2.35 adjusted free cash flow for the year.

Jay Malave, Jr.: Right. So, when you look at that, we will continue to expect some of the integration costs we'll still see going into next year from a cash basis. But let me just take you back to the second half of free cash flow because we expected an uptick in net income. There will be a little bit of an outflow related to working capital with one-to-two day's improvement, but we're going to try to hold that flat and we'll see a little bit of a benefit in cash taxes.

So, we feel good about the second half, and specific to your question in terms of what we see going next year, as I mentioned, there will be some continued costs related to the integration restructuring-type level of cost and those type of items, but beyond that, I don't expect there to be other significant items that will repeat going forward.

Unknown Speaker: Just in a nutshell, I think for the year we're at 260 million of free cash impact from deal with integration costs. We had about 25 million or so in the first half. The 235 will be in the back half. About 100 million of that 95 are going to be deal costs. That's going to be behind us by Q3. The balance is integration costs, and we'll see some little drag forward into calendar '20 on integration costs as well.

Robert Stallard: That's very helpful. Thank you.

Operator: Our next question comes from Sheila Kahayaoglu of Jeffries. Caller, you may proceed.

Sheila Kahayaoglu: Thanks. Good morning Bill and Chris and welcome, Jay. On the deal closing, you guys increased share repurchases and your dividends. How are you maybe thinking about your overall free cash flow target and targeting return to shareholders?

Unknown Speaker: Well, I think, as Jay was alluding to, we feel good about this year in terms of cash generation. We're still targeting $3 billion three years out. That's calendar '22. We'll certainly ramp to that. So, I think we're off to a really good start in terms of the cash we generate in the first half. LTM cash, what we're going to do with it this year, so all that's looking pretty good.

We ended June on a pro forma basis with $1.7 billion on the balance sheet. We're going to generate about $2.5 billion more or less in the next 12 months. So, that puts us at about 4.2 billion more or less of cash available for deployment. Our dividends are about 700 million 680.

That's including the 10% increase we announced on July 1st. That will be in act this year in August.

We'll reevaluate that in January, 700 million in dividends. We have about $300 million worth of deal and integration costs. We just spoke about that over the next 12 months. We had to fund (INAUDIBLE) deferred compensation programs, but what that means is it leaves you about $3 billion over that period of time for things to do, $2.5 billion on buyback and about a half a billion dollars, Sheila, that's going to be held on the balance sheet, just because it's what we require for normal working capital needs.

Sheila Kahayaoglu: On the margins, the pro forma margin guidance for the total company implies second half margins are up 80 basis points over the first half but these in acceleration. Can you maybe talk about the moving pieces, how much of that is coming from synergies versus the underlying business profitability?

Unknown Speaker: So you're right, Sheila. The first half on a pro forma basis is up 90 basis points, the second half up 170. So, it's up sequentially as well as 167. Through the year, about 130 basis points of margin expansion. So, 16 to a little bit better than we had thought when we put the deal together in S4. So, we feel good about the trajectory. As you mentioned on the call, about $40 million in the back half is coming from net cost synergies.

There's a road map in the back on the EPS bridge which indicates the absence of L3 intangibles and pension amortization. That's about another $40, 43 million We see an operational improvement year-over-year in a couple of businesses from L3 including EDD. We see operational excellence savings, which will off-set some mix growth, some investment in the back half; all of which gets us to about the 170 in the back half, and we feel it's pretty well calibrated.

Operator: Our next question comes from Carter Copeland of Melius Research. Caller, you may proceed.

Carter Copeland: Just a couple quick ones. One, I realize it's hard because we didn't have a Harris guide for the next fiscal year out there, but it looks like on a pro forma basis the top line that you've put forth for the second half is a little bit ahead of where we may have been on a pro forma basis coming in. Could you just verify that and maybe help us size it?

And then, as a follow-on, I wonder as part of the many decisions you made in getting the deal closed and whatnot, where you shook out on things like incentive compensation, not necessarily for the executive team but as you go a layer down in terms of driving the sort of behavior that you want, if there was anything useful or notable to speak about there that will help us understand where your points of emphasis are. Thanks, guys.

Unknown Speaker: Yeah, sure, Carter. Thanks. So really on the first point--first of all, Harris is trailing a little bit, backtracking a bit better on calendar '19 in terms of versus the S4, and combined company basis for calendar '19, we're about a half a billion dollars better. So, it's quite a bit stronger than we envisioned late last year when we put out the S4. But again, as mentioned at that time, the S4 was related to strategic plans, which were put together earlier in the year over the summer.

The market has gotten a bit better. We want some strategic opportunities, so we feel good about where we'll at in calendar '19, a bit better than we started. 20's looking pretty good as well certainly with the budget backdrop. Strong-funded backlog at the mid-point of the year is up 15%. So, a lot of it's tracking I think for really good top line progress.

On the comp program, we're still in discussions with our board in terms of what we do going forward, but Chris and I--obviously, there's a short-term plan and a longer-term plan. On the short-term basis, it'll be some combination of revenue (INAUDIBLE) free cash, and since we all know the importance of cash generation, the importance of driving working capital improvements, there's probably a slight tilt towards free cash, much like we did a number of years ago at Harris.

You'll know Chris mentioned about the big stuff up in the first half and free cash generation up 5X over the first half of last year. I think 50% of the short-term comp for the L3 executives came on free cash, and we all know when you incentivize for something you get results. So, that's kind of where we're thinking on the short-term basis. Longer-term, it'll be performance-based equity. That will be tied to the targets we're discussing with shareowners.

Carter Copeland: Thanks.

Operator: Our next question comes from Peter Arment of Baird. Caller, you may proceed.

Peter Arment: Thanks. Question, Jay, I guess on CapEx. You mentioned 190 million for the second half of the year, about 2% of revenues. Just thinking about longer-term, as we think over the forecast period and thinking about your integration period, is that still a good number to go off of, about 2% of sales?

Jay Malave, Jr.: Yeah, I believe it is, Peter. 2% on a full-year basis, that's $380 million, 190 in the first half and 190 in the second half. I think going forward it feels like that's the right place to be to fund and be prepared for the growth, and yeah, I think 2% is where you should go with it.

Peter Arment: Just as a quick follow-up. Now, I know you're not talking about quarterly guidance here, but just thinking about the second half guidance that you put out, is there anything you'd call out regarding 3Q versus 4Q, either on the EPS or free cash flow, just thinking from a modeling perspective (INAUDIBLE).

Unknown Speaker: Nothing material, Peter. There'll be additional non-GAAP charges in Q3 because some of the deal and integration expenses, but on a non-GAAP reported earnings per share revenue growth should all look pretty stable Q3 versus Q4.

Operator: Our next question comes from David Strauss of Barclay's. Caller, you may proceed.

David Strauss: Thanks. Bill, in the Harris deck, you had a slide that showed the medium-term outlook by segment. I wanted to see if you might offer--since we're new to the combined company segment, I wanted to see you if you would offer your thoughts on kind of how the growth rates relative to each other among the segments might look going forward and also from a margin opportunity beyond what we're looking at for the second half of '19.

Bill Brown: Well, David, it's still a little bit early. Obviously, we just put the company together. It took enormous work to put together a pro forma guidance in the back half. So, it's a little bit premature to get out beyond that, but maybe, just some high-level comments without getting into the segment-by-segment looks here.

For us, looking at 10% growth in a calendar year in the industry that we happen to be in is pretty special. You follow us. You follow others in the space. Looking at 10% at back half feels pretty good as well. So, I mentioned the S4 is a little dated. We're doing a lot better than the S4, about half a billion dollars' stronger this year.

So, we're coming off a stronger starting point in the S4. I think L3's numbers were growing at 5 to 6%, in that range. We were a little bit higher than that. I see us continuing to grow in that mid-to-high single-digit range into '20 and maybe a little bit beyond that. It comes from a good bipartisan budget deal. The top line's budget is not growing that much, 3% and then basically flat the year after, but the certainty that provides, the funding line that we see tactical, F35, other places that affect the business are very, very good and very positive.

I think it's $122 billion worth of appropriations that are out there that are exceeding the outlays. So, those outlays have to catch up. There's just a lot of dry powder in this system that should keep all of the boats moving in the water, and we feel pretty good about the medium-term outlook. On the margin side, look, anything ending at 162 this year would be a great result. We're at the front-end of our ramp-on synergies, only 40 million this year and getting to 300 million several years' out. That's another 170, 180 basis points.

So, you can kind of run the math and get to 18% pretty quickly a few years out, and we'll ramp to that as quickly as we can. So, as we look out at the back-end of the year, we feel great, and I think the outlook in calendar '20 also looks pretty good too.

David Strauss: As a follow-up, I wanted to ask about the free cash flow cadence beyond this year. So, you're guiding to the full-year adjusted free cash flow number around 2, 3. You've got this $3 billion target for calendar 2022. Apply a little less than a 10% cater between here and there, which just seems a little like, given what you're talking about from a working capital, upside opportunity and synergies. Can you just help square that, why it's not a higher growth rate between here and there?

Bill Brown: Look, we feel really good about where ended on an LTM basis on cash and just for referencing a couple of data point. Harris over the last 12 months was better than by four days of working capital. So, it went from 45 to 41, a day or two better than we thought a couple of months ago. L3's results were 12 days better year-over-year in the June ending quarter.

So, we're making good progress. Over the balance of the year, we're only looking at getting another day or two between June and the back-end of the year, but we're starting from about 75 days pro forma at the end of June. Harris is sitting at 41. I think we got a lot of opportunity ahead of us. Let's get through the next couple of quarters. We'll give you guidance on calendar '20, and certainly to look at Chris and Jay, we're all over trying to figure out a way to make sure that the cash gets accelerated. That's certainly what we're trying to do.

Unknown Speaker: And keep in mind, the working capital is going to want to grow with the increase in volume. So, our challenge is going to be to take out the productivity in working capital and hold it flat over that period of time.

Unknown Speaker: And I'll chime in. We're clearly focused on this, Dave. You've seen the progress, as Bill mentioned, to 12 days. The good news is a lot of that is coming out of inventory, a little bit out of day sales outstanding. So, we haven't even really focused on the payable lever. So, the teams are working it hard, and we're allocating targets right down to the program manager level. Everybody knows what they need to do to achieve these targets.

Operator: Our next question comes from Gautam Khanna of Cowan. Caller, you may proceed.

Gautam Khanna: Yes, thank you. I may have missed this, but Bill, can you talk about maybe some sort of ballpark what we would expect in divestments now that the deal is closed in terms of size (INAUDIBLE) and then I have a follow-up.

Bill Brown: No, I don't think we're going to size it today, only because those decisions aren't yet made, and we're at the front-end of the process. It's going to take some time to get alignment, work the process. And what I'll do--Gautam knows I've done before, I know Chris has done before, is rather than talking about something that we're going to do, I'll talk about what we have done when that is done.

So, we don't have a predetermined target of what we're trying to do. Again, what we're looking at is we want to make sure the management team is focused on the businesses that are strategic, ones that are technology-driven, have great returns, and we can win, and Chris and I spent a lot of time in the last few months on this. We worked with our boards. We've got a meeting coming up in a couple of weeks on this. So, we're on it, but I'm not going to size how much the divestiture might be until we really get around to making some decisions around that.

Gautam Khanna: I appreciate that. Just a quick follow-up. Tactical Comms book to bill looked pretty strong. I was wondering if you could give us some flavor on the 12- to 18-month outlook pipeline for international, domestic, and just any kind of commentary you can give around (INAUDIBLE).

Bill Brown: The international pipeline remains pretty good at around 2.5 billion, and the shape of it has not changed a lot. So, we had a good finish on international, a good basically flattish in Q4, but we had a good year, about 3%. DoD pipeline is around 1.7 billion, so it's up a little bit. What's interesting is the mix.

It's about 50/50 now between base and modernization. As we would've expected, modernization has started to grow. We see that over the course of fiscal '19, it basically tripled in size in terms of modernization. The pipeline is now half modernization. That's back-stopped by what is a pretty good budget outlook. I got to tell you, we had a good year in tactical. The guys just did a great job. We were up about 13% this year in calendar '19. It's going to be about 10%, 12% or so, low double-digit in the back half. DoD's going to continue to grow pretty well, and see international in the low-to-mid single-digit range.

DoD is gonna continue to grow pretty well. You will see international the low to mid-single digit range. So, we see continue momentum in this business, you know, and it goes beyond the backend of the year based on what I'm seeing in the budget. So, you know, the tactical business is performing--performing very well as expected.

Gautam Khanna: And Last one for me, you know, any major recompetes monitoring over the next 12 months, thank you.

Chris Kubasik: Any major recompetes? Any recompetes, that was the question? Okay. If I can go with major recompetes, we'll be able to see a lot over the next 12 months. I mean there's always places that we're bidding and there's opportunities out there. You know, but there's--there's nothing that's really significant. The one that--that's really coming into mind is what we call our sensor program, it's where we do maintenance for ground based telescopes, it's 12 sites around the world, the legacy Excellus program to $150, 100, $200 million of year of revenue. It's under a recompete. But, it's one of those programs that I feel very strong about from way back when we bought Excellus there were 35, 30 percent on time delivery. We're closed the quarter at around 94, 95 percent, very, very good reputation with the customers.
So, that's the only one that's jumping off my mind is a recompete that certainly I got my eye on. But, there's nothing more than that. So, thanks for the question.

Gautam Khanna: Thank you.

Chris Kubasik: You bet.

Operator: Our next question comes from Michael C.R. Molli (PH) of Sun Trust. Caller, you may proceed.

Michael C.R. Molli: Hey, good morning, guys, thanks for taking questions and nice results. Just on the second half margins, specifically the aviation segment, I think you've got, you know, pretty strong margin expansion in the second half of the year there looking at 14 percent versus, you know, 10 and a half I think. You did some initial comments in what's driving that. But, can you be a little bit more specific there on the sharp margin expansion in that segment?

Chris Kubasik: Yeah, this is Chris. We see an up ramp from a couple main drivers. As you recall, we have the EDD business in there, which, of course, is a tough compare for '18 compared to '19. So, we talked earlier in January about a significant improvement, 40 basis points, from not having the same issues at EDD which we don't expect to have in '19 that we had in '18. We have some E3 savings that are pretty significant in the $40 million range. And we have a pretty good road path to execute upon those.

And, you know, we have some growth opportunities in the commercial aviation sector, specifically avionics that has higher margins in addition to some QV (PH) and ordinance opportunities. All that contributes to the guidance we gave.

Michael C.R. Molli: Got it. And then just a bigger picture on the defense budget. I know we've got the two-year budget deal. But, any thoughts on sort of what's taking place with the expansion of this night court process that, you know, Mark Esper looks to be implementing. Do you guys see this as a risk or opportunity as you look at the potential pipeline of business, you know, versus modernization, legacy? I know, you know, funding lines look good now but it seems like, you know, what we saw take place at the Army could be expanding now into the Navy and the Air Force and just wondering how you guys are viewing that process.

Chris Kubasik: Well, look, I think it's still very early. He was only confirmed very recently, but through what he did when he was Army secretary was actually, you know, very positive, very productive. I think it's notable that he with Ryan McCarthy, with the chief, got together and really prioritized where they wanted to spend limited Army dollars that focused on key priorities and start to move away from things that weren't, you know, all that critical.

You know, the fact is I think between what we do, what L3 does on a combined basis, you know, the fact is we're working on, you know, important programs and I think we ended up being -- doing very well through the Army process.

I'd envision the same thing over with across DoD what he's now going to work on. So, you know, the discipline of looking at where they want to spend dollars is important. And I think based on the things that we're working on, you know, we're gonna be--I think we're gonna end up being pretty, pretty strong here.

Michael C.R. Molli: Sounds good. Thanks, guys.

Chris Kubasik: You bet.

Operator: Our next question comes from George Shapiro of Shapiro Research. Caller, you may proceed.

George Shapiro: Good morning. I was wondering, Bill, if you could provide a breakdown of your revenues between the O&M budget and the investment budget because L3 had a high percentage from the O&M budget.

Bill Brown: Yeah, no, on the DoD side, so about 55, 60 percent DoD and about--so, 50/50 O&M versus procurement.

George Shapiro: Okay. and then with some of the shorter cycle businesses that you're in and the flattening of the budget, is there any concern that your growth rate can slow somewhat quickly, more quickly, than others would with longer cycle businesses might have or you think it's--you're getting enough share that we keep going on with better than industry growth rates?

Bill Brown: Yeah, I mean the short cycle business that we really have talked about in the past, George, is really around the tactical radio business. And that, that has become, you know, when we merged with Excellus it became a smaller piece of the overall company. Certainly as we've proved in the other segments, you know, so it's like 35, 36 percent of the legacy Harris Company. It's not even smaller as part of L3 Harris.

You know, but the fact is it is a relatively quick turn business, but it's a little bit different today it would have been a few years ago. With today a lot more of the business is driven by modernization. And modernization has a lot more visibility to it than these quick turn O&M funded orders that we would have gotten in the past. So, you know, I'm not terribly concerned. We had a very, very strong count of fiscal '19. We had a really extraordinary first half of calendar '19 in DoD tactical. That would naturally mitigate itself or slow down a little bit in the back half. But, it's still very healthy growth, north of 20 percent.

So, look, it's a great business. We're across all of the different platforms, different contract vehicles, all the services that weren't on the front end and what we believe is a multi-year range here, George.

George Shapiro: Okay, very good. Thanks very much.

Bill Brown: You bet.

Operator: Our next question comes from Rob Spingarn of Credit Suisse. Caller, you may proceed.

Robert Spingarn: Hi, good morning and congrats on the deal. I just wanted to go back to the guidance and this really can be for anybody, but Jay, this is the guidance you gave. If I look at the second half revenues it looks like in everything but AS we have a slight decrease in growth. Is that just comps or there anything else going on there?

Jay Malavo: Yeah, Rob, some of it is comps. We had, you know, up in the last half of the last year was some pretty significant growth rates. But, you're talking--you're kind of splitting hairs. In the integration mission systems business it was 12 percent growth in the first half and we're expecting around 10 and a half growth. So, a real slight reduction there. In communications systems we're nearly 12 percent. We're gonna be nine and a half there, close to 10. And so, yeah, I'd say the more compares up than anything else. But, the growth rates are still pretty substantial and pretty significant to support the 10 percent in the back half.

As I said in my comments, high visibility with the backlog. We have 90 percent visibility in the backlog to the back half. And so, we feel really good about going into this next six months.

Robert Spingarn: And then I guess for the increase growth in AS does this go back to the comments that Chris just made about some new programs or are there things ramping there?

Jay Malavo: What we're seeing we're seeing, you know, what Chris called the precision engagement systems business ramps a bit more in the back half than the front half? It grew really nicely the first half, you know, even stronger in the back. And it's just a lot of classified work that Chris and his team have solidified themselves on. Plus a lot of fusing business for munitions. And that up temple (PH) there is pretty high. We're also getting, you know, a little bit better comps on the commercial training business, the defense training business looks a little bit better. The C17 carriers for the full year, but there's F-16 wins that have happened that's gonna help mitigate the C17 loss in the back half.

So, really across, across all the pieces of AS it just gets better. And that's why we're seeing, you know, better growth in the back half than the front half.

Robert Spingarn: Okay and then just a clarification, just on the proceeds from the night vision sale, the L3 pension pre-funding that I think you were gonna direct those proceeds toward, has that happened? Is that in the op cash flow guidance for this year?

Jay Malavo: No, what's gonna happen is--so we're still on track for that. The net proceeds will be about $325 million. We expect to get through the process in Q3. It's deep in the (INAUDIBLE) review. You know, and that will be used to pre-fund the pension. You know, that'll basically mitigate any cash contributions on the L3 side for the pensions through the next couple of years. I think through calendar, into calendar '22. You know, so that's like a $70 million improvement, if you will, in cash.

But, you know, remember night vision generated some cash, so there's a bit of an offset. On an annualized basis that's sort of a 50, $60 million net benefit to us in the pre-cash side. And that is in our guidance.

Robert Spingarn: But the timing is in the guidance for this year.

Jay Malavo: Not in the back half. It's in the outlook as we get into 20 and beyond.

Robert Spingarn: Okay. Thank you.

Jay Malavo: You bet.

Operator: Our next question comes from Richard Saffron of Buckingham (PH) Research Group. Caller, you may proceed.

Richard Saffron: Thanks. Bill, Chris, Jay. Good morning, how are you?

Unknown: Good, Richard, good morning.

Richard Saffron: First I had a bit of a top level kind of philosophy question here. You know, for lack of a better term, you know, commercial business model has really been at the core of Harris. So, what I wanted to ask was how you--how long you might think it might take to apply that model to the new combined company. How long you think it might be before we see tangible results? Just interested in any color you can provide there on how you're thinking about implementing that?

Bill Brown: Well, again, it's a great question. And it's a, you know, less philosophical, more financial, in a sense of what we've tried to do. And I relate back to where we were three ago with Excellus. Excellus manufactured radios in Fort Wayne (PH) it was under a sort of normal model and with cost disclosures and we moved that up to (inaudible). It took some time but that's now a full commercial model business.

At L3 West Can (PH), the West Can business they had a very profitable, nice sized business growing very well, great positions around the world. That's a commercial model business much like what we do in the tactical side. There's a possibility to take the Saxsun (PH) business that L3 has that is very strong and over time migrate back to a commercial model. It's something that we'll work on. It may not be a needle mover in the next couple of years. It's something that, obviously, we're focused on. But, we can say that that's gonna be the key driver to the margin expansion. It's gonna come through, you know, operational excellence. It'll come through synergies. It's gonna come through basic better performance in our company.

So, I mean, we're certainly on it, Richard.

Richard Saffron: Okay, thanks for that. Now, just quickly then, on the F-35 program, you know, just following up on your opening remarks. You know, just generally we seen a lot of changes among suppliers on the F-35 program. So, I just wanted to know, you know, are there still incremental opportunities out there for you on that program. And, if possible, in your answer could you just discuss how your content on that platform has evolved?

Bill Brown: Yeah, sure. We, you know, now I'm gonna quote a number and I--this is probably just legacy (inaudible) I'm gonna look at (inaudible) to confirm this; there's $2.2 million for shipset today. So, we do the common components. We do the battle system. We do the release systems. So, about $2.2 million. That we know is gonna grow to about 2.7 over the next several years. You know, we won three different pieces of what they call TAC refresh three. So, one is the mission computer called the ICP, you know it as the aircraft memory system, as well as the electronic unit, the panoramic cockpit display, PCEU (PH) and all of those things add together over time to give us another half a billion dollars of content for F-35.

So, that's gonna grow in terms of content per shipset, you know, and then it's gonna also grow with the ramp, which is why it's an important one for us to keep talking about. As the number of the shipset continue to grow, plus our content continues to grow, it's gonna continue to be a growth driver for the company.

Chris Kubasik: And, Richard, on the Legacy L3's, you know, we have the crypto. We have the display. So, you know, I think another 500 or 600 per shipset as well. And when we put the merger together we talked about the benefit of scale. I think Lockheed martin would acknowledge we're one of the top suppliers. It gives you better access to the management team to be a part of the strategy. We've put effective bid on other components in the years ahead, given our scale and investments.

Richard Saffron: Thanks very much. I appreciate that.

Chris Kubasik: You bet.

Operator: Our next question comes from Noah Poponak of Goldman Sachs. Caller, you may proceed.

Noah Poponak: Hey, good morning, everybody.

Chris Kubasik: Good morning.

Bill Brown: Good morning, Noah.

Noah Poponak: In the (inaudible), the 3 billion, three year free cash flow target, what is the, you know, underlying organic business segment; so, you know, before--you know, putting aside anything below the line, putting aside the working capital opportunity and the synergy, just the core, newly combined business segment EBITDA growth rate on that three-year basis that you were assuming in the 3 billion.

Bill Brown: Yeah, I think top line is around 5, 6 percent, you know, a little bit higher than our EBITDA growth. You know, when we--you know, it yields about half a billion dollars of incremental net income incremental cash coming from growth over the three-year period.

Noah Poponak: Okay. the five--I guess 500 on the new--shall I be thinking about that relative to the two, three to two three and a halves, so it'd be kind of 20 percent of that on a--but over three years, so call it a 6 percent (inaudible)?

Bill Brown: Yeah, it only--it was off like a 2--2-0 to 2.1 billion dollar pre-cash basis. So, it's gonna be maybe a little bit less than that. But, yeah, it's about that range, 6, 7 percent.

Noah Poponak: Okay. And then just to make sure I have the bridge correct working off of this year, in the 2, 3 to 2, 3, 5 how much working capital and synergy is in that? It sounded like the one to two days of working capital is maybe 50 million bucks. And then I thought I saw 40 million synergy in the deck, but then I, Bill, I heard you say in 150, I didn't know if maybe that was a run rate number. Can you just clarify those for me?

Bill Brown: Yeah, sure. So, there's $40 million of net synergies at the back half. So, it's net synergy to the full year as well. And that cross through to generating cash on an (inaudible) basis. The 150 is the run rate will be added to the cost synergies by the calendar year. So, that's a run rate will be averaged. It gives us confidence that we can be at $200 million so in calendar ’20 growth savings dropping through. So, that’s how we talked about it.

Over the course of the back end of the year we were, I think we were around 75 days at--on a pro forma basis in June. And, as Jay pointed out, we're expecting one to two days of improvement sequentially through the back end of the year on working capital. So, anything around 74, 73 days.

Noah Poponak: Okay, so I should be kind of in the zone of maybe call it 100 million bucks of the 500 that you have for the--in that free cash flow bridge of net after tax synergy, plus capital efficiency, maybe 100 of the 500 is happening in 2019?

Bill Brown: I’m not sure and we’re looking at each other here, not sure--

Noah Poponak: --Well, it’s 40 to 50 of synergy and then one to two days of working capital, I guess--.

Bill Brown: --Well, once we work capital on a full year basis it’s probably on the order of 30, $60 million in that range. So, it’ll be half of that over the course of the back end of the year.

Noah Poponak: Okay. And then just, you know, bigger picture on the margins. You know, clearly the margins will expand if you achieve the synergy plans.

Should we be giving consideration for margin expansion in the underlying business before synergies. Harris kind of had incremental margins from the partially commercial model. Legacy L3 had plans to continue to improve the operations of the margins in the business before the deal. Is it fair to assume the margins are expanding independent of the synergies and then synergies in addition to that?

Unknown Speaker: It's fair to assume that. Yeah, both independent businesses had talked about margin expansion. In both pieces, it was (INAUDIBLE) of 100 basis points, and certainly, the synergy that we had talked about would be incremental to that, which is going back when we first talked about the deal on a pro forma basis, the even margin was around 14.

We said that we'd get to around 17 through 100 basis points organic growth on margins, another 200 basis points on synergy to get to 17. Obviously, (INAUDIBLE) into calendar 16, we're doing a bit better than that, as starting off here. So yeah, it is incremental to the benefits of synergies, Noah.

Operator: Our next question comes from Seth Seifman of JPMorgan. Caller, you may proceed.

Seth Seifman: Thanks very much. I apologize if I missed it in the prepared remarks. I know there was a lot going on, but the profitability in the Communications business at L3 in the quarter, nearly 8%, maybe if you can address that, and it kind of seemed like we were moving past last year's issues and what kind of risks that presents going forward.

Chris Kubasik: Yeah, Seth. This is Chris. That was driven, as we put in the prepared comments, mainly by the maritime sector. We have a pretty strong international focus in maritime. We have some steady cornerstone programs, as I call them focused on sensors and control systems, but there are some new developments going on, one in the unmanned arena, both surface and under sea and that requires investments.

And then, we have some new programs for the Columbia and the Destroyer and some laser weapons. Those were slowed in the quarter by some additional costs to get those development programs on track, and those will have long 10- to 20-year (INAUDIBLE) once we get going. So, it was focused on maritime development, to answer your question.

Seth Seifman: Bill, in legacy Harris, the Space and Intelligence segment, it seems like the book to bill for fiscal '19 was probably around 1.0, which is pretty solid. Obviously, there's some good growth there, but there's also a ton of growth in the Space budget. So, maybe, if you could talk a little bit about the visibility you have there and the confidence you have that you guys are taking a fair share on the Space side.

Bill Brown: Yeah, look, Seth, we feel very good about the Space business. You're right. In the year, the book to bill was a little over 1. Backlog came up a little bit, so there's a good trend there, and we've talked about that pretty consistently over the course of fiscal '19 with the classified business being up mid-teens. Order is looking pretty good, and that comes in a couple of different areas.

When we talk about our classified business, it's not just space. So, there's opportunities in space in both exquisite as well as moving to small (INAUDIBLE), and the team has just done a great job maintaining a strong position on exquisite components while at the same time taking the lead on full-ended mission solutions with small (INAUDIBLE). But our classified business in that area also relates to other domains, and that business continues to go well.

Again, some philosophy, moving from providing components to subsystems to now full mission solutions, whether they be terrestrial systems, near-shore systems, deep water systems. And that business has gone very well and is really this philosophy, the budgets are coming up, and we're expanding our ability to compete on more full-ended mission solutions. And you can see the trajectory happening in the back-end of the year. We continue to see strong growth in the classified business.

Chris Kubasik: I'll just say that Bill and I spent a fair amount of time last week reviewing the classified business, and I was thoroughly impressed with the technology and the opportunities. So, we're excited about the Space business going forward and other classified work.

Operator: Our next question comes from Jon Raviv of Citi. Caller, you may proceed.

Jon Raviv: Now, that we've had some more time pass, any sort of additional perspective on industry M&A would be appreciated by you guys, as others talk up more scaled investments to increase their probability of wins, and by definition taking some market share. What do you consider the impact to be on LHX going forward besides bagging you a nice CFO?

Bill Brown: Yeah, we bagged a nice CFO, exactly. So, let me start in with that one, Jon, since you led with that. So, Chris and I started this conversation quite a long time ago with a goal of creating a very large-scaled mission solutions prime, and that's exactly what we've done. We continue to assess implications of what other people in the space do, but when I look at just the company that we have created and the opportunities ahead of us, I think we're very well-positioned.

When you talk about scale, I think we are scale in places where we need to be scale. We're scale in tactical radios. We're becoming scale in the space business. We're scale in lots of different areas of the company, and we feel great. The company is a technology leader. Our strategy is to continue to invest significantly and aggressively in innovation.

We've been running about 4% of our revenue in IRAD, and we continue to see that continue to go up. We've got a great set of people who are great technologists and business leaders to drive our business. What's going to require for us to win is continuing to accelerate the deployment of technologies into the marketplace, into the field (INAUDIBLE) and continue to execute well on our programs.

That's what we can do, and no matter what happens in the market and the changes in the structure, we're going to keep focus on what we do well, the things that we can control, and the technology in the way we execute. So, I think we're in a good spot here, Jon.

Operator: Our final question comes from Josh Sullivan of Seaport Global Securities. Caller, you may proceed.

John Sullivan: Just given the success with the Exelis combination and maybe using that as a benchmark, can you talk about how the experience so far with L3 has been maybe similar to that integration and then maybe where it's been a little more dynamic?

Bill Brown: It's a much bigger scale, clearly, and there's a lot of complexity within L3. It was a company built over 20 years so a lot of M&A, and Chris has talked about the desire to move from a holding company to an operating company, and we're sort of on that journey. So, getting information, getting it consistently across businesses is a bit of a challenge, but the reality is we're out of the gates very, very quickly.

We've got a great seasoned integration team, people that are very experienced. They've done this before. There are a lot of people from the Exelis integration. We're getting data very quickly. The enthusiasm and energy across the company is very good. It's gone, from my vantage point, certainly better than we would've imagined and better than we did with Exelis.

We're going faster on supply chain. That was an area that took us a little time to ramp up to on Exelis, so we're at that a lot faster this time. Obviously, with the segments and the headquarters, we made those decisions. We executed on that on day one here, which is very important. The revenue opportunities ahead of us are quite significant, something that Chris is spending a lot of time, and we're very encouraged.

So, we're going to get on that probably a lot faster this time than we did with Exelis. Keep in mind, we're in a different market space with different part of the cycle. Back with Exelis, we're still coming out of sequestration. The visibility and the budgets weren't very strong. So, we focused much more on cost side. This time is different.

And Chris and the team are really putting a lot of time and effort into making sure we understand where the revenue opportunities are and then making sure that we fund them. So, I'm optimistic about the trajectory that we're on here, and clearly, we're on a great path to deliver half a billion of gross cost synergies and hopefully a big more than that over time, Josh.

So, that wraps up our call. So, thank you very, very much. Chris and I are very excited about the company that we've created and getting to the closure of this historic merger on exactly the minute that we thought we would be in mid-October of last year. There's a lot of precision in that, as you'd expect from us and this team. We're very excited. We're confident. We've created a lot of value for owners, but importantly, and Chris mentioned this in his comments, we have 50,000 employees at this company who are working very, very hard to deliver results, keep their focus on the customer, and we want to thank them for all their efforts.

And we look forward to updating you again on the merger and the progress we're having at the end of October for next earnings release. So, thank you very much.

Operator: This concludes today's conference. You may disconnect your lines at this time. Thank you for your participation and have a wonderful day.