

MOOG INC.  
Form 10-Q  
August 01, 2016  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

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FORM 10-Q

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(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended July 2, 2016

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 1-05129

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INC.  
(Exact name of registrant as specified in its charter)

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New York State (State or other jurisdiction of incorporation or organization)	16-0757636 (I.R.S. Employer Identification No.)
East Aurora, New York (Address of principal executive offices) (716) 652-2000 (Telephone number including area code)	14052-0018 (Zip Code)

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Former name, former address and former fiscal year, if changed since last report.

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).  
Yes  No

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

The number of shares outstanding of each class of common stock as of July 26, 2016 was:

Class A common stock, \$1.00 par value, 32,538,249 shares

Class B common stock, \$1.00 par value, 3,337,934 shares

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## PART I FINANCIAL INFORMATION

## Item 1. Financial Statements

Moog Inc.

Consolidated Condensed Balance Sheets  
(Unaudited)

(dollars in thousands)	July 2, 2016	October 3, 2015
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$394,429	\$309,853
Receivables	647,987	698,419
Inventories	500,734	493,360
Deferred income taxes	93,121	91,210
Prepaid expenses and other current assets	36,415	34,653
Total current assets	1,672,686	1,627,495
Property, plant and equipment, net of accumulated depreciation of \$713,435 and \$677,168, respectively	518,233	536,756
Goodwill	746,590	737,212
Intangible assets, net	119,284	143,723
Other assets	43,932	41,285
Total assets	\$3,100,725	\$3,086,471
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current liabilities		
Short-term borrowings	\$1,377	\$83
Current installments of long-term debt	184	34
Accounts payable	150,091	165,973
Accrued salaries, wages and commissions	124,898	125,270
Customer advances	174,700	167,423
Contract loss reserves	31,413	30,422
Other accrued liabilities	102,432	116,300
Total current liabilities	585,095	605,505
Long-term debt, excluding current installments	1,108,438	1,075,067
Long-term pension and retirement obligations	288,732	348,239
Deferred income taxes	77,803	60,209
Other long-term liabilities	3,107	2,919
Total liabilities	2,063,175	2,091,939
Commitments and contingencies (Note 17)	—	—
Redeemable noncontrolling interest	7,875	—
Shareholders' equity		
Common stock	51,280	51,280
Other shareholders' equity	978,395	943,252
Total shareholders' equity	1,029,675	994,532
Total liabilities and shareholders' equity	\$3,100,725	\$3,086,471
See accompanying Notes to Consolidated Condensed Financial Statements.		

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Moog Inc.

Consolidated Condensed Statements of Earnings  
(Unaudited)

(dollars in thousands, except per share data)	Three Months Ended		Nine Months Ended	
	July 2, 2016	July 4, 2015	July 2, 2016	July 4, 2015
Net sales	\$613,260	\$ 634,539	\$1,792,859	\$1,902,308
Cost of sales	429,598	443,963	1,268,550	1,354,264
Gross profit	183,662	190,576	524,309	548,044
Research and development	36,006	34,157	110,535	96,882
Selling, general and administrative	88,553	90,733	254,318	280,718
Interest	8,662	7,916	25,919	20,953
Restructuring	(39	) 6,604	8,303	6,604
Other	(1,082	) 442	(2,600	) 1,327
Earnings before income taxes	51,562	50,724	127,834	141,560
Income taxes	15,916	14,393	35,121	37,871
Net earnings attributable to common shareholders and noncontrolling interest	\$35,646	\$ 36,331	\$92,713	\$ 103,689
Net earnings (loss) attributable to noncontrolling interest	(665	) —	(889	) —
Net earnings attributable to common shareholders	\$36,311	\$ 36,331	\$93,602	\$ 103,689
Net earnings per share attributable to common shareholders				
Basic	\$1.01	\$ 0.95	\$2.57	\$2.62
Diluted	\$1.00	\$ 0.94	\$2.55	\$2.59
Average common shares outstanding				
Basic	36,038,340	38,389,629	36,411,428	39,555,423
Diluted	36,267,975	38,744,620	36,663,165	39,963,142
See accompanying Notes to Consolidated Condensed Financial Statements.				

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Moog Inc.

Consolidated Condensed Statements of Comprehensive Income  
(Unaudited)

	Three Months Ended		Nine Months Ended	
	July 2, 2016	July 4, 2015	July 2, 2016	July 4, 2015
(dollars in thousands)				
Net earnings attributable to common shareholders and noncontrolling interest	\$35,646	\$36,331	\$92,713	\$103,689
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustment	(25,439 )	12,067	(33,683 )	(68,212 )
Retirement liability adjustment	5,313	3,498	14,396	14,988
Change in accumulated income (loss) on derivatives	(2,327 )	465	(1,396 )	392
Other comprehensive income (loss), net of tax	(22,453 )	16,030	(20,683 )	(52,832 )
Comprehensive income	\$13,193	\$52,361	\$72,030	\$50,857
Comprehensive income (loss) attributable to noncontrolling interest	(665 )	—	(889 )	—
Comprehensive income attributable to common shareholders	\$13,858	\$52,361	\$72,919	\$50,857
See accompanying Notes to Consolidated Condensed Financial Statements.				

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Moog Inc.  
Consolidated Condensed Statements of Cash Flows  
(Unaudited)

	Nine Months Ended	
(dollars in thousands)	July 2, 2016	July 4, 2015
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net earnings attributable to common shareholders and noncontrolling interest	\$92,713	\$103,689
Adjustments to reconcile net earnings to net cash provided (used) by operating activities:		
Depreciation	58,674	59,468
Amortization	16,485	19,010
Deferred income taxes	7,765	14,569
Equity-based compensation expense	2,794	4,569
Other	6,967	4,212
Changes in assets and liabilities providing (using) cash:		
Receivables	43,214	51,547
Inventories	(9,959)	(4,763)
Accounts payable	(16,456)	7,332
Customer advances	9,689	(5,008)
Accrued expenses	(7,106)	(21,182)
Accrued income taxes	686	(8,205)
Net pension and post retirement liabilities	(38,828)	(23,817)
Other assets and liabilities	(5,858)	5,407
Net cash provided by operating activities	160,780	206,828
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Acquisitions of businesses, net of cash acquired	(11,016)	—
Purchase of property, plant and equipment	(42,605)	(57,712)
Other investing transactions	1,164	12,597
Net cash used by investing activities	(52,457)	(45,115)
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Net short-term repayments	—	(3,337)
Proceeds from revolving lines of credit	274,670	335,185
Payments on revolving lines of credit	(261,570)	(425,185)
Proceeds from long-term debt	20,000	—
Payments on long-term debt	(10,047)	(5,250)
Proceeds from senior notes, net of issuance costs	—	294,430
Proceeds from sale of treasury stock	2,229	11,437
Purchase of outstanding shares for treasury	(42,203)	(297,417)
Proceeds from sale of stock held by SECT	2,897	7,328
Purchase of stock held by SECT	(1,634)	(12,121)
Purchase of stock held by SERP Trust	(2,300)	(7,328)
Excess tax benefits from equity-based payment arrangements	442	5,973
Other financing transactions	(1,909)	—
Net cash used by financing activities	(19,425)	(96,285)
Effect of exchange rate changes on cash	(4,322)	(19,276)
Increase in cash and cash equivalents	84,576	46,152
Cash and cash equivalents at beginning of period	309,853	231,292

Cash and cash equivalents at end of period	\$394,429	\$277,444
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See accompanying Notes to Consolidated Condensed Financial Statements.

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Moog Inc.

Notes to Consolidated Condensed Financial Statements

Nine Months Ended July 2, 2016

(Unaudited)

(dollars in thousands, except per share data)

Note 1 - Basis of Presentation

The accompanying unaudited consolidated condensed financial statements have been prepared by management in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, all adjustments consisting of normal recurring adjustments considered necessary for the fair presentation of results for the interim period have been included. The results of operations for the three and nine months ended July 2, 2016 are not necessarily indicative of the results expected for the full year. The accompanying unaudited consolidated condensed financial statements should be read in conjunction with the financial statements and notes thereto included in our Form 10-K for the fiscal year ended October 3, 2015. All references to years in these financial statements are to fiscal years.

Recent Accounting Pronouncements

In April 2014, the Financial Accounting Standards Board ("FASB") issued ASU No. 2014-08, "Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity." This ASU is intended to change the criteria for reporting discontinued operations and enhance convergence of the FASB's and the International Accounting Standard Board's (IASB) reporting requirements for discontinued operations. The provisions of this ASU are effective for fiscal years beginning after December 15, 2014 and interim periods within those fiscal years. We adopted this amendment in the first quarter of 2016. The adoption of this standard did not have any impact on our financial statements.

Note 2 - Acquisition and Divestiture

In 2016, we acquired a 70% ownership in Linear Mold and Engineering, a Livonia, Michigan-based company specializing in metal additive manufacturing that provides engineering, manufacturing and production consulting services to customers across a wide range of industries, including aerospace, defense, energy and industrial. The purchase price, net of acquired cash, was \$22,765 consisting of \$11,016 in cash, issuance of a \$1,280 unsecured note and assumption of \$10,469 of debt. The acquisition also includes a redeemable noncontrolling interest in the remaining 30%, which is exercisable beginning three years from the date of acquisition. This acquisition is included in our Aircraft Controls segment. The purchase price allocation is subject to adjustments as we obtain additional information for our estimates during the measurement period.

In 2015, we sold the Rochester, New York and Erie, Pennsylvania life sciences operations of our Medical Devices segment for \$2,988 in cash.

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## Note 3 - Receivables

Receivables consist of:

	July 2, 2016	October 3, 2015
Accounts receivable	\$273,918	\$291,188
Long-term contract receivables:		
Amounts billed	122,219	113,565
Unbilled recoverable costs and accrued profits	243,071	286,395
Total long-term contract receivables	365,290	399,960
Other	12,923	12,557
Total receivables	652,131	703,705
Less allowance for doubtful accounts	(4,144 )	(5,286 )
Receivables	\$647,987	\$698,419

We securitize certain trade receivables in transactions that are accounted for as secured borrowings (Securitization Program). We maintain a subordinated interest in a portion of the pool of trade receivables that are securitized. The retained interest, which is included in Receivables in the consolidated condensed balance sheets, is recorded at fair value, which approximates the total amount of the designated pool of accounts receivable. Refer to Note 6, Indebtedness, for additional disclosures related to the Securitization Program.

## Note 4 - Inventories

Inventories, net of reserves, consist of:

	July 2, 2016	October 3, 2015
Raw materials and purchased parts	\$192,187	\$188,843
Work in progress	240,123	243,373
Finished goods	68,424	61,144
Inventories	\$500,734	\$493,360

There are no material inventoried costs relating to long-term contracts where revenue is accounted for using the percentage of completion, cost-to-cost method of accounting as of July 2, 2016 or October 3, 2015.

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## Note 5 - Goodwill and Intangible Assets

The changes in the carrying amount of goodwill are as follows:

	Aircraft Controls	Space and Defense Controls	Industrial Systems	Components	Medical Devices	Total
Balance at October 3, 2015	\$188,525	\$158,213	\$110,843	\$217,763	\$61,868	\$737,212
Acquisitions	21,076	—	—	—	—	21,076
Foreign currency translation	(7,637)	(73)	(4,512)	591	(67)	(11,698)
Balance at July 2, 2016	\$201,964	\$158,140	\$106,331	\$218,354	\$61,801	\$746,590

Goodwill at July 2, 2016, in our Medical Devices reporting unit, is net of a \$38,200 accumulated impairment loss.

The components of intangible assets are as follows:

		July 2, 2016		October 3, 2015	
	Weighted- Average Life (years)	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Customer-related	11	\$165,598	\$(114,990)	\$171,779	\$(110,697)
Program-related	19	65,971	(25,586)	75,720	(27,463)
Technology-related	9	70,304	(51,056)	73,299	(49,723)
Marketing-related	9	25,116	(17,322)	25,997	(16,648)
Other	9	4,729	(3,480)	4,772	(3,313)
Intangible assets	12	\$331,718	\$(212,434)	\$351,567	\$(207,844)

Substantially all acquired intangible assets other than goodwill are being amortized. Customer-related intangible assets primarily consist of customer relationships. Program-related intangible assets consist of long-term programs represented by current contracts and probable follow on work. Technology-related intangible assets primarily consist of technology, patents, intellectual property and software. Marketing-related intangible assets primarily consist of trademarks, trade names and non-compete agreements.

Amortization of acquired intangible assets was \$4,989 and \$16,285 for the three and nine months ended July 2, 2016 and \$5,994 and \$18,788 for the three and nine months ended July 4, 2015. Based on acquired intangible assets recorded at July 2, 2016, amortization is expected to be approximately \$21,000 in 2016, \$17,500 in 2017, \$16,800 in 2018, \$15,200 in 2019 and \$13,400 in 2020.

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## Note 6 - Indebtedness

Short-term borrowings consist of:

	July 2, 2016	October 3, 2015
Lines of credit	\$97	\$ 83
Other short-term debt	1,280	—
Short-term borrowings	\$1,377	\$ 83

We maintain short-term line of credit facilities with banks throughout the world that are principally demand lines subject to revision by the banks.

Long-term debt consists of:

	July 2, 2016	October 3, 2015
U.S. revolving credit facility	\$688,100	\$675,000
Senior notes	300,000	300,000
Securitization program	120,000	100,000
Obligations under capital leases	522	101
Senior debt	1,108,622	1,075,101
Less current installments	(184 )	(34 )
Long-term debt	\$1,108,438	\$1,075,067

On June 28, 2016, we amended our U.S. revolving credit facility. The amendment extended the maturity of the credit facility to June 28, 2021. Our U.S. revolving credit facility has a capacity of \$1,100,000 and provides an expansion option, which permits us to request an increase of up to \$200,000 to the credit facility upon satisfaction of certain conditions. The credit facility is secured by substantially all of our U.S. assets.

On November 21, 2014, we completed the sale of \$300,000 aggregate principal amount of 5.25% senior notes due December 1, 2022 at par with interest paid semiannually on June 1 and December 1 of each year. The aggregate net proceeds of \$294,430 were used to repay indebtedness under our U.S. bank credit facility, thereby increasing the unused portion of our revolving credit facility.

On April 15, 2016, we amended the Securitization Program. The amendment increased our borrowing capacity to \$120,000 and extended the maturity to April 13, 2018. Under the Securitization Program, we sell certain trade receivables and related rights to an affiliate, which in turn sells an undivided variable percentage ownership interest in the trade receivables to a financial institution, while maintaining a subordinated interest in a portion of the pool of trade receivables. Interest for the Securitization Program is based on 30-day LIBOR plus an applicable margin. A commitment fee is also charged based on a percentage of the unused amounts available and is not material. The agreement governing the Securitization Program contains restrictions and covenants which include limitations on the making of certain restricted payments, creation of certain liens, and certain corporate acts such as mergers, consolidations and sale of substantially all assets. The Securitization Program has a minimum borrowing requirement equal to the lesser of either 80% of our borrowing capacity or 100% of our borrowing base, which is a subset of the trade receivables sold under this agreement. As of July 2, 2016, our minimum borrowing requirement was \$96,000.

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## Note 7 - Product Warranties

In the ordinary course of business, we warrant our products against defects in design, materials and workmanship typically over periods ranging from twelve to sixty months. We determine warranty reserves needed by product line based on historical experience and current facts and circumstances. Activity in the warranty accrual is summarized as follows:

	Three Months		Nine Months	
	Ended July 2, 2016	July 4, 2015	Ended July 2, 2016	July 4, 2015
Warranty accrual at beginning of period	\$20,398	\$17,618	\$18,660	\$19,953
Warranties issued during current year	2,609	2,358	7,952	6,057
Adjustments to pre-existing warranties	(879 )	(391 )	(1,227 )	(1,976 )
Reductions for settling warranties	(1,898 )	(2,306 )	(4,946 )	(5,462 )
Foreign currency translation	(350 )	322	(559 )	(971 )
Warranty accrual at end of period	\$19,880	\$17,601	\$19,880	\$17,601

## Note 8 - Derivative Financial Instruments

We principally use derivative financial instruments to manage interest rate risk associated with long-term debt and foreign exchange risk related to foreign operations and foreign currency transactions. We enter into derivative financial instruments with a number of major financial institutions to minimize counterparty credit risk.

## Derivatives designated as hedging instruments

Interest rate swaps are used to adjust the proportion of total debt that is subject to variable and fixed interest rates. The interest rate swaps are designated as hedges of the amount of future cash flows related to interest payments on variable-rate debt that, in combination with the interest payments on the debt, convert a portion of the variable-rate debt to fixed-rate debt. At July 2, 2016, we had interest rate swaps with notional amounts totaling \$125,000. The interest rate swaps effectively convert this amount of variable-rate debt to fixed-rate debt at 2.49%, including the applicable margin of 1.63% as of July 2, 2016. The interest will revert back to variable rates based on LIBOR plus the applicable margin upon the maturity of the interest rate swaps. These interest rate swaps mature at various times between December 5, 2016 and June 5, 2017.

We use foreign currency contracts as cash flow hedges to effectively fix the exchange rates on future payments and revenue. To mitigate exposure in movements between various currencies, including the Philippine peso and the British pound, we had outstanding foreign currency forwards with notional amounts of \$67,045 at July 2, 2016. These contracts mature at various times through March 2, 2018.

These interest rate swaps and foreign currency contracts are recorded in the consolidated condensed balance sheets at fair value and the related gains or losses are deferred in shareholders' equity as a component of Accumulated Other Comprehensive Income (Loss) (AOCI). These deferred gains and losses are reclassified into the consolidated condensed statements of earnings during the periods in which the related payments or receipts affect earnings. However, to the extent the interest rate swaps and foreign currency contracts are not perfectly effective in offsetting the change in the value of the payments and revenue being hedged, the ineffective portion of these contracts is recognized in earnings immediately. Ineffectiveness was not material in the first nine months of 2016 or 2015.

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## Derivatives not designated as hedging instruments

We also have foreign currency exposure on balances, primarily intercompany, that are denominated in foreign currencies and are adjusted to current values using period-end exchange rates. The resulting gains or losses are recorded in the consolidated condensed statements of earnings. To minimize foreign currency exposure, we had foreign currency contracts with notional amounts of \$115,916 at July 2, 2016. The foreign currency contracts are recorded in the consolidated condensed balance sheets at fair value and resulting gains or losses are recorded in the consolidated condensed statements of earnings. We recorded the following gains or losses on foreign currency contracts which are included in other income or expense and generally offset the gains or losses from the foreign currency adjustments on the intercompany balances that are also included in other income or expense:

Three Months Ended	July 2, 2016	July 4, 2015	Nine Months Ended	July 2, 2016	July 4, 2015
Net	\$1,942	\$(1,246)	\$5,901	\$(2,661)	

## Summary of derivatives

The fair value and classification of derivatives is summarized as follows:

		July 2, 2016	October 3, 2015
Derivatives designated as hedging instruments:			
Foreign currency contracts	Other current assets	\$ 328	\$ 12
Foreign currency contracts	Other assets	119	39
	Total asset derivatives	\$ 447	\$ 51
Foreign currency contracts	Other accrued liabilities	\$ 4,068	\$ 1,755
Foreign currency contracts	Other long-term liabilities	116	572
Interest rate swaps	Other accrued liabilities	402	756
Interest rate swaps	Other long-term liabilities	—	268
	Total liability derivatives	\$ 4,586	\$ 3,351
Derivatives not designated as hedging instruments:			
Foreign currency contracts	Other current assets	\$ 2,823	\$ 115
Foreign currency contracts	Other accrued liabilities	\$ 241	\$ 429

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## Note 9 - Fair Value

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Depending on the nature of the asset or liability, various techniques and assumptions can be used to estimate fair value. The definition of the fair value hierarchy is as follows:

Level 1 – Quoted prices in active markets for identical assets and liabilities.

Level 2 – Observable inputs other than quoted prices in active markets for similar assets and liabilities.

Level 3 – Inputs for which significant valuation assumptions are unobservable in a market and therefore value is based on the best available data, some of which is internally developed and considers risk premiums that a market participant would require.

Our derivatives are valued using various pricing models or discounted cash flow analyses that incorporate observable market data, such as interest rate yield curves and currency rates, and are classified as Level 2 within the valuation hierarchy. Our Level 3 fair value liabilities typically represent contingent consideration recorded for acquisitions to be paid if various financial targets are met.

The following table presents the fair values and classification of our financial assets and liabilities measured on a recurring basis, all of which are classified as Level 2.

	Classification	July 2, October 3, 2016 2015	
Foreign currency contracts	Other current assets	\$3,151	\$ 127
Foreign currency contracts	Other assets	119	39
	Total assets	\$3,270	\$ 166
Foreign currency contracts	Other accrued liabilities	\$4,309	\$ 2,184
Foreign currency contracts	Other long-term liabilities	116	572
Interest rate swaps	Other accrued liabilities	402	756
Interest rate swaps	Other long-term liabilities	—	268
	Total liabilities	\$4,827	\$ 3,780

Our only financial instrument for which the carrying value differs from its fair value is long-term debt. At July 2, 2016, the fair value of long-term debt was \$1,111,810 compared to its carrying value of \$1,108,622. The fair value of long-term debt is classified as Level 2 within the fair value hierarchy and was estimated based on quoted market prices.

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## Note 10 - Employee Benefit Plans

Net periodic benefit costs for U.S. defined benefit pension plans consist of:

	Three Months Ended July 2, 2016		Nine Months Ended July 2, 2015	
Service cost	\$5,909	\$5,909	\$17,728	\$17,726
Interest cost	9,415	8,508	28,244	25,523
Expected return on plan assets	(12,595)	(11,784)	(37,787)	(35,352)
Amortization of prior service cost (credit)	46	37	140	112
Amortization of actuarial loss	6,542	5,588	19,626	16,766
Pension expense for defined benefit plans	\$9,317	\$8,258	\$27,951	\$24,775

Net periodic benefit costs for foreign defined benefit pension plans consist of:

	Three Months Ended July 2, 2016		Nine Months Ended July 2, 2015	
Service cost	\$1,357	\$1,553	\$3,995	\$4,529
Interest cost	1,245	1,271	3,711	3,640
Expected return on plan assets	(1,229)	(1,364)	(3,669)	(3,908)
Amortization of prior service cost (credit)	(20)	(12)	(58)	(37)
Amortization of actuarial loss	660	574	1,957	1,645
Pension expense for defined benefit plans	\$2,013	\$2,022	\$5,936	\$5,869

Net periodic benefit costs for the post-retirement health care benefit plan consists of:

	Three Months Ended July 2, 2016		Nine Months Ended July 2, 2015	
Service cost	\$40	\$56	\$121	\$169
Interest cost	117	144	351	432
Amortization of actuarial gain	(143)	(26)	(429)	(79)
Net periodic postretirement benefit cost	\$14	\$174	\$43	\$522

Pension expense for the defined contribution plans consists of:

	Three Months Ended July 2, 2016		Nine Months Ended July 2, 2015	
U.S. defined contribution plans	\$3,832	\$3,483	\$10,632	\$10,426
Foreign defined contribution plans	1,496	1,819	4,605	5,118
Total pension expense for defined contribution plans	\$5,328	\$5,302	\$15,237	\$15,544

Actual contributions for the nine months ended July 2, 2016 and anticipated additional 2016 contributions to our defined benefit pension plans are as follows:

	U.S. Plans	Foreign Plans	Total
Actual	\$67,002	\$5,711	\$72,713
Anticipated	959	1,359	2,318
Total expected contributions	\$67,961	\$7,070	\$75,031



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## Note 11 - Restructuring

In 2016, we initiated further restructuring actions in conjunction with exiting a product line within Aircraft Controls in the U.S. We have also taken actions as a result of the business outlook in specific markets and locations in Components and Industrial Systems that resulted in workforce reductions in Canada, Europe and the U.S. The expense for all of these actions consists of \$4,581 of non-cash charges, primarily for writing off intangible assets, \$3,242 for severance and \$480 for facility closure.

In 2015, we initiated additional restructuring plans as a result of ongoing reviews of our lines of business and operations. The restructuring actions taken resulted in workforce reductions, primarily in the U.S., Europe and Asia. In 2014, we initiated restructuring plans in response to the business outlook, which includes a change in the mix of sales and delays and cancellations of orders for certain product lines. The restructuring actions taken resulted in workforce reductions, primarily in the U.S. and Europe.

Restructuring activity for severance and other costs by segment is as follows:

	Space Aircraft and Controls Defense		Industrial Systems	Components	Medical Devices	Total
Balance at October 3, 2015	\$ 3,047	\$ 7,237	\$ 4,003	\$ 117	\$ 142	\$ 14,546
Charged to expense - 2016 plan	5,923	—	1,165	1,215	—	8,303
Adjustments to provision	(275 )	(289 )	79	—	—	(485 )
Cash payments - 2014 plan	(11 )	(604 )	—	—	—	(615 )
Cash payments - 2015 plan	(2,568 )	(5,443 )	(3,404 )	(117 )	(72 )	(11,604 )
Cash payments - 2016 plan	(939 )	—	(998 )	(1,173 )	—	(3,110 )
Non-cash charges - 2016 plan	(4,581 )	—	—	—	—	(4,581 )
Foreign currency translation	(31 )	(18 )	98	—	1	50
Balance at July 2, 2016	\$ 565	\$ 883	\$ 943	\$ 42	\$ 71	\$ 2,504

As of July 2, 2016, the restructuring accrual consists of \$750 for the 2014 plan, \$1,000 for the 2015 plan and \$754 for the 2016 plan. Restructuring for all plans is expected to be paid by April 1, 2017, except portions classified as long-term liabilities based on payment arrangements.

## Note 12 - Income Taxes

The effective tax rates for the three and nine months ended July 2, 2016 were 30.9% and 27.5%, respectively. The effective tax rates for the three and nine months ended July 4, 2015 were 28.4% and 26.8%, respectively. The effective tax rates for these periods are lower than the U.S. federal statutory tax rate primarily due to a significant portion of our earnings that come from foreign operations with lower tax rates and the recognition and timing of U.S. research and development tax credits. In addition, we also benefited from the reversal of accruals for certain tax exposures outside the U.S. whose statutes of limitations expired during these periods.

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## Note 13 - Shareholders' Equity

The changes in shareholders' equity for the nine months ended July 2, 2016 are summarized as follows:

	Amount	Number of Shares	
		Class A Common Stock	Class B Common Stock
<b>COMMON STOCK</b>			
Beginning of period	\$51,280	43,638,618	7,641,095
Conversion of Class B to Class A	—	28,183	(28,183 )
End of Period	51,280	43,666,801	7,612,912
<b>ADDITIONAL PAID-IN CAPITAL</b>			
Beginning of period	456,512		
Equity-based compensation expense	2,794		
Issuance of treasury shares	(349 )		
Adjustment to market - SECT, SERP and other	539		
End of period	459,496		
<b>RETAINED EARNINGS</b>			
Beginning of period	1,579,794		
Net earnings attributable to common shareholders	93,602		
End of period	1,673,396		
<b>TREASURY STOCK</b>			
Beginning of period	(701,771 )	(10,318,431 )	(3,323,926)
Issuance of treasury shares	2,578	87,915	—
Purchase of treasury shares	(42,203 )	(898,036 )	—
End of period	(741,396 )	(11,128,552 )	(3,323,926)
<b>STOCK EMPLOYEE COMPENSATION TRUST (SECT)</b>			
Beginning of period	(44,211 )		(828,381 )
Issuance of shares	2,897		64,676
Purchase of shares	(1,634 )		(29,234 )
Adjustment to market	328		—
End of period	(42,620 )	—	(792,939 )
<b>SUPPLEMENTAL RETIREMENT PLAN (SERP) TRUST</b>			
Beginning of period	(5,337 )		(100,000 )
Purchase of shares	(2,300 )		(50,000 )
Adjustment to market	(426 )		—
End of period	(8,063 )	—	(150,000 )
<b>ACCUMULATED OTHER COMPREHENSIVE LOSS</b>			
Beginning of period	(341,735 )		
Other comprehensive income (loss)	(20,683 )		
End of period	(362,418 )		
<b>TOTAL SHAREHOLDERS' EQUITY</b>	<b>\$1,029,675</b>	<b>32,538,249</b>	<b>3,346,047</b>



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The changes in AOCI, net of tax, by component for the nine months ended July 2, 2016 are as follows:

	Accumulated foreign currency translation	Accumulated retirement liability	Accumulated gain (loss) on derivatives	Total
AOCI at October 3, 2015	\$ (72,788 )	\$ (266,910 )	\$ (2,037 )	\$ (341,735 )
Other comprehensive income (loss) before reclassifications	(33,683 )	958	(3,130 )	(35,855 )
Amounts reclassified from AOCI	—	13,438	1,734	15,172
Other comprehensive income (loss)	(33,683 )	14,396	(1,396 )	(20,683 )
AOCI at July 2, 2016	\$ (106,471 )	\$ (252,514 )	\$ (3,433 )	\$ (362,418 )

The amounts reclassified from AOCI into earnings are as follows:

Statement of earnings classification	Three Months Ended		Nine Months Ended	
	July 2, 2016	July 4, 2015	July 2, 2016	July 4, 2015
Retirement liability:				
Prior service cost	\$26	\$25	\$82	\$73
Actuarial losses	7,098	6,093	21,154	18,362
Reclassification from AOCI into earnings	7,124	6,118	21,236	18,435
Tax effect	(2,610 )	(2,254 )	(7,798 )	(6,795 )
Net reclassification from AOCI into earnings	\$4,514	\$3,864	\$13,438	\$11,640
Derivatives:				
Foreign currency contracts Sales	\$206	\$(33 )	\$480	\$3
Foreign currency contracts Cost of sales	323	93	1,393	1,011
Interest rate swaps Interest	154	322	624	1,062
Reclassification from AOCI into earnings	683	382	2,497	2,076
Tax effect	(181 )	(157 )	(763 )	(784 )
Net reclassification from AOCI into earnings	\$502	\$225	\$1,734	\$1,292

The amounts deferred in AOCI are as follows:

Statement of earnings classification	Net deferral in AOCI - effective portion			
	Three Months Ended		Nine Months Ended	
	July 2, 2016	July 4, 2015	July 2, 2016	July 4, 2015
Foreign currency contracts Sales	\$(2,946)	\$677	\$(3,461)	\$276
Foreign currency contracts Cost of sales	(664 )	(641 )	(407 )	(68 )
Interest rate swaps Interest	(140 )	(62 )	(52 )	(1,823)
Net loss	(3,750 )	(26 )	(3,920 )	(1,615)
Tax effect	921	266	790	715
Net deferral in AOCI of derivatives	\$(2,829)	\$240	\$(3,130)	\$(900)

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## Note 14 - Stock Employee Compensation Trust and Supplemental Retirement Plan Trust

The Stock Employee Compensation Trust (SECT) assists in administering and provides funding for equity-based compensation plans and benefit programs, including the Moog Inc. Retirement Savings Plan (RSP). The Supplemental Retirement Plan (SERP) Trust provides funding for benefits under the Moog Inc. SERP. Both the SECT and the SERP Trust hold shares as investments. The shares in the SECT and SERP Trust are not considered outstanding for purposes of calculating earnings per share. However, in accordance with the trust agreements governing the SECT and SERP Trust, the trustees vote all shares held by the SECT and SERP Trust on all matters submitted to shareholders.

## Note 15 - Earnings per Share

Basic and diluted weighted-average shares outstanding are as follows:

	Three Months Ended		Nine Months Ended	
	July 2, 2016	July 4, 2015	July 2, 2016	July 4, 2015
Basic weighted-average shares outstanding	36,038,340	38,389,629	36,411,428	39,555,423
Dilutive effect of equity-based awards	229,635	354,991	251,737	407,719
Diluted weighted-average shares outstanding	36,267,975	38,744,620	36,663,165	39,963,142

For the three and nine months ended July 2, 2016, there were 91,175 and 72,293 common shares subject to equity-based awards, respectively, excluded from the calculation of diluted earning per share as they would be anti-dilutive. There were no material anti-dilutive equity-based awards outstanding for the three and nine months ended July 4, 2015.

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## Note 16 - Segment Information

During 2015, we made a change to our segment reporting. Our Components segment now includes our sensors and handpieces product line, which we previously included in the Medical Devices segment. This product line consists of manufactured ultrasonic and optical sensors as well as surgical handpieces distributed to medical OEMs. Since the customer base is different from the sale of medical pumps directly to end users, the chief operating decision maker is now reviewing performance and assessing the allocation of resources of this product line as part of the Components segment. All historical amounts have been restated to conform to this new organization.

Below are sales and operating profit by segment for the three and nine months ended July 2, 2016 and July 4, 2015 and a reconciliation of segment operating profit to earnings before income taxes. Operating profit is net sales less cost of sales and other operating expenses, excluding interest expense, equity-based compensation expense and other corporate expenses. Cost of sales and other operating expenses are directly identifiable to the respective segment or allocated on the basis of sales, number of employees or profit.

	Three Months Ended		Nine Months Ended	
	July 2, 2016	July 4, 2015	July 2, 2016	July 4, 2015
Net sales:				
Aircraft Controls	\$274,175	\$270,339	\$804,779	\$811,103
Space and Defense Controls	90,764	95,266	262,579	288,477
Industrial Systems	130,103	130,581	383,526	393,092
Components	92,285	112,630	265,673	335,396
Medical Devices	25,933	25,723	76,302	74,240
Net sales	\$613,260	\$634,539	\$1,792,859	\$1,902,308
Operating profit:				
Aircraft Controls	\$30,532	\$28,401	\$67,705	\$75,195
Space and Defense Controls	13,747	6,149	38,920	19,784
Industrial Systems	11,534	13,068	38,437	38,972
Components	10,754	14,966	23,839	47,828
Medical Devices	2,182	3,506	8,015	6,558
Total operating profit	68,749	66,090	176,916	188,337
Deductions from operating profit:				
Interest expense	8,662	7,916	25,919	20,953
Equity-based compensation expense	875	603	2,794	4,569
Corporate and other expenses, net	7,650	6,847	20,369	21,255
Earnings before income taxes	\$51,562	\$50,724	\$127,834	\$141,560

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Note 17 - Commitments and Contingencies

From time to time, we are involved in legal proceedings. We are not a party to any pending legal proceedings which management believes will result in a material adverse effect on our financial condition, results of operations or cash flows.

We are engaged in administrative proceedings with governmental agencies and legal proceedings with governmental agencies and other third parties in the normal course of our business, including litigation under Superfund laws, regarding environmental matters. We believe that adequate reserves have been established for our share of the estimated cost for all currently pending environmental administrative or legal proceedings and do not expect that these environmental matters will have a material adverse effect on our financial condition, results of operations or cash flows.

In the ordinary course of business we could be subject to ongoing claims or disputes from our customers, the ultimate settlement of which could have a material adverse impact on our consolidated results of operations. While the receivables and any loss provisions recorded to date reflect management's best estimate of the projected costs to complete a given project, there is still significant effort required to complete the ultimate deliverable. Future variability in internal cost and as well as future profitability is dependent upon a number of factors including deliveries, performance and government budgetary pressures. The inability to achieve a satisfactory contractual solution, further unplanned delays, additional developmental cost growth or variations in any of the estimates used in the existing contract analysis could lead to further loss provisions. Additional losses could have a material adverse impact on our financial condition, results of operations or cash flows in the period in which the loss may be recognized.

We are contingently liable for \$19,735 of standby letters of credit issued by a bank to third parties on our behalf at July 2, 2016.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations contained in the Company's Annual Report filed on Form 10-K for the fiscal year ended October 3, 2015. All references to years in this Management's Discussion and Analysis of Financial Condition and Results of Operations are to fiscal years and amounts may differ from reported values due to rounding.

OVERVIEW

We are a worldwide designer, manufacturer and systems integrator of high performance precision motion and fluid controls and control systems for a broad range of applications in aerospace and defense and industrial markets.

Within the aerospace and defense market, our products and systems include:

• Defense market - primary and secondary flight controls for military aircraft, stabilization and automatic ammunition loading controls for armored combat vehicles, tactical and strategic missile steering controls and gun aiming controls.

• Commercial aircraft market - primary and secondary flight controls for commercial aircraft.

• Commercial space market - satellite positioning controls and thrust vector controls for launch vehicles.

In the industrial market, our products are used in a wide range of applications including:

• Industrial automation market - injection molding, metal forming, heavy industry, material and automotive testing, pilot training simulators and surveillance systems.

• Energy market - oil and gas exploration, wind energy and power generation.

• Medical market - sleep apnea devices, surgical handpieces, CT scanners, as well as enteral clinical nutrition and infusion therapy solutions.

We operate under five segments, Aircraft Controls, Space and Defense Controls, Industrial Systems, Components and Medical Devices. Our principal manufacturing facilities are located in the United States, United Kingdom, Philippines, Germany, Italy, Netherlands, China, Costa Rica, Japan, Luxembourg, India, Canada and Ireland.

We have long-term contracts with some of our customers. These contracts are predominantly within Aircraft Controls and Space and Defense Controls and represent 33%, 34% and 33% of our sales in 2015, 2014 and 2013, respectively.

We recognize revenue on these contracts using the percentage of completion, cost-to-cost method of accounting as work progresses toward completion. The remainder of our sales are recognized when the risks and rewards of ownership and title to the product are transferred to the customer, principally as units are delivered or as service obligations are satisfied. This method of revenue recognition is predominantly used within the Industrial Systems, Components and Medical Devices segments, as well as with aftermarket activity.

We concentrate on providing our customers with products designed and manufactured to the highest quality standards. Our products are applied in demanding applications, "When Performance Really Matters®." We believe we have achieved a leadership position in the high performance, precision controls market, by capitalizing on our strengths, which include:

• superior technical competence in delivering mission-critical solutions,

• an innovative customer-intimacy approach,

• a diverse base of customers and end markets served by a broad product portfolio,

• well-established international presence serving customers worldwide, and

• a proven ability to successfully undertake investments designed to enhance our control systems product franchise and drive continued growth.

These strengths have afforded us the ability to expand our current solutions into new, complimentary technologies, which provide us with the opportunity to develop our product scope supply from one market to another and from component to systems supplier, as well as achieve substantial content positions on the platforms on which we currently participate. As we seek to be the dominant supplier in the current niche markets we serve, we will also look for innovation in all aspects of our business, employing new technologies to improve productivity and to develop

progressive business models.

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Our financial objectives include increasing our revenue base and improving our long term profitability and cash flow from operations while continuously focusing on internal cost improvement initiatives. In doing so, we expect to maintain a balanced, diversified portfolio in terms of markets served, product applications, customer base and geographic presence. Our fundamental strategies to achieve our objectives include:

- maintaining our technological excellence by building upon our systems integration capabilities while solving our customers' most demanding technical problems in applications "When Performance Really Matter®,"
- utilizing our global capabilities and strong engineering heritage to innovate new solutions,
- maximizing customer value by implementing lean enterprise principles, and
- investing in talent development to accelerate our leadership capability and employee performance.

We focus on improving shareholder value through strategic revenue growth, both acquired and organic, through improving operating efficiencies and manufacturing initiatives and through utilizing low cost manufacturing facilities without compromising quality. Additionally, we take a balanced approach to capital deployment, which may include strategic acquisitions or further share buyback activity in order to maximize shareholder returns over the long-term. We face numerous challenges to improving shareholder value. These include, but are not limited to, adjusting to dynamic global economic conditions that are influenced by governmental, industrial and commercial factors, pricing pressures from customers, strong competition, foreign currency fluctuations and increases in employee benefit costs. Based on periodic strategy reviews, including the financial outlook of our business, we may also engage in restructuring activities, including reducing overhead, consolidating facilities, exiting some product lines and divesting operations.

### Acquisition and Divestiture

All of our acquisitions are accounted for under the purchase method and, accordingly, the operating results for the acquired companies are included in the consolidated statements of earnings from the respective dates of acquisition. Under purchase accounting, we record assets and liabilities at fair value on the consolidated balance sheet. The purchase price described for each acquisition below is net of any cash acquired and includes debt issued or assumed.

In 2016, we acquired a 70% ownership in Linear Mold and Engineering, a Livonia, Michigan-based company specializing in metal additive manufacturing that provides engineering, manufacturing and production consulting services to customers across a wide range of industries, including aerospace, defense, energy and industrial. We acquired Linear Mold and Engineering for \$23 million. The acquisition also includes a redeemable noncontrolling interest in the remaining 30%, which is exercisable beginning three years from the date of acquisition. This acquisition is included in of our Aircraft Controls segment.

In 2015, we sold the Rochester, New York and Erie, Pennsylvania life sciences operations of our Medical Devices segment for \$3 million.

### CRITICAL ACCOUNTING POLICIES

On a regular basis, we evaluate the critical accounting policies used to prepare our consolidated financial statements, including, but not limited to, revenue recognition on long-term contracts, contract loss reserves, reserves for inventory valuation, reviews for impairment of goodwill, purchase price allocations for business combinations, pension assumptions and deferred tax asset valuation allowances.

There have been no material changes in critical accounting policies in the current year from those disclosed in our 2015 Annual Report on Form 10-K. However, we have expanded our disclosure for reviews for impairment of goodwill. The disclosure below includes key assumptions and circumstances that, if changed, could negatively impact

our assessment of goodwill in reporting units for which the fair value is not significantly in excess of carrying value.

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## Reviews for Impairment of Goodwill

During the fourth quarter of 2015, we transferred the management of our sensors and handpieces business from Medical Devices to Components. Accordingly, we performed an interim test on goodwill for impairment for our Medical Devices reporting unit. This reporting unit had \$62 million of goodwill at October 3, 2015. The fair value of the Medical Devices reporting unit exceeded its carrying amount by 18%. Had we used a discount rate that was 100 basis points higher or a terminal growth rate that was 100 basis points lower than those we assumed, the fair value of this reporting unit would have exceeded its carrying amount by 4% and 10%, respectively.

The primary factor causing the fair value of this reporting unit to not be substantially greater than the carrying value is that the Medical Devices segment was created through a series of acquisitions between 2006 and 2009. The creation of this reporting unit resulted in recording substantial goodwill, which increased the carrying value. The key assumptions that drive the estimated fair value are the projected revenue and operating margins, which are used to project future cash flows. Our expectation for this reporting unit is for revenue growth over the five year projection period to be driven by the overall market growth of the home healthcare segment of the infusion therapy market and by capturing market share due to new product offerings. Additionally, our expectation is that operating margins improve throughout the five year projection period, driven by improved sales, as well as continued cost containment activities. If cash flows generated by our Medical Devices reporting unit were to decline in the future, or if there were adverse revisions to key assumptions, we may be required to record impairment charges. There are specific circumstances that would pose risk to the fair value of this reporting unit. Lower than projected growth rates of the home healthcare segment of the infusion therapy market, changes in provider capital purchase cycles, changes in healthcare legislation, changes in private insurance plans, as well as changes in treatment therapies may negatively affect the fair value of this reporting unit. Also, our projected market share capture rates may be lower due to delayed or unsuccessful new product offerings, which would negatively affect the fair value of this reporting unit. In addition, the fair value of this reporting unit may be negatively impacted based on the results of strategic reviews and courses of action that we may decide to pursue.

## RECENT ACCOUNTING PRONOUNCEMENTS

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers (Topic 606)," which supersedes the revenue recognition requirements in ASC 605, Revenue Recognition. This ASU requires revenue recognition to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This ASU also requires additional disclosures about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and assets recognized from costs incurred to obtain or fulfill a contract. This ASU can be adopted using either a full retrospective or modified retrospective approach. In March 2016, the FASB issued ASU No. 2016-08, "Revenue from Contracts with Customers (Topic 606): Principal Versus Agent Considerations." This ASU clarifies implementation guidance on principal versus agent considerations. In April 2016, the FASB issued ASU No. 2016-10, "Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing." This ASU clarifies implementation guidance on licensing arrangements as well as the process of identifying performance obligations. In May 2016, the FASB issued ASU No. 2016-11, "Revenue Recognition (Topic 605) and Derivatives and Hedging (Topic 815): Rescission of SEC Guidance Because of Accounting Standards Updates 2014-09 and 2014-16 pursuant to Staff announcements at the March 3, 2016 EITF Meeting." This ASU rescinds certain SEC paragraphs within ASC 605 and supersedes it with updated guidance found within Topic 606. Also, in May 2016, the FASB issued ASU No. 2016-12, "Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients." This ASU is intended to clarify certain narrow aspects of the guidance found within the new revenue recognition standard. The provisions of each ASU are effective for fiscal years beginning after December 15, 2017 and interim periods within those fiscal years, pursuant to the issuance of ASU No. 2015-14, "Revenue from Contracts with Customers (Topic 606): Deferral of Effective Date," in August 2015. These amendments are applicable to us beginning in the first quarter of 2019. We are currently evaluating the adoption of these standards on our financial statements.

In August 2014, the FASB issued ASU No. 2014-13, "Consolidation (Topic 810): Measuring the Financial Assets and Financial Liabilities of a Consolidated Collateralized Financing Entity." This ASU allows a reporting entity to elect to measure the financial assets and the financial liabilities of a consolidated collateralized financing entity using either the measurement alternative included in the ASU or Topic 820. The provisions of this ASU are effective for fiscal years beginning after December 15, 2015 and interim periods within those fiscal years. Early adoption is permitted as of the beginning of an annual period. This amendment is applicable to us beginning in the first quarter of 2017. The adoption of this standard is not expected to have a material impact on our financial statements.

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In August 2014, the FASB issued ASU No. 2014-15, "Presentation of Financial Statements - Going Concern (Subtopic 205-40): Disclosures of Uncertainties about an Entity's Ability to Continue as a Going Concern." This ASU requires management to evaluate whether there are conditions or events that raise substantial doubt about the entity's ability to continue as a going concern within one year after the date that the financial statements are issued or are available to be issued. This ASU also requires management to disclose certain information depending on the results of the going concern evaluation. The provisions of this ASU are effective for fiscal years ending after December 15, 2016 and for interim periods within those fiscal years thereafter. Early adoption is permitted. This amendment is applicable to us beginning in the first quarter of 2017. The adoption of this standard is not expected to have a material impact on our financial statements.

In January 2015, the FASB issued ASU No. 2015-01, "Income Statement - Extraordinary and Unusual Items (Subtopic 225-20): Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items." This ASU eliminates from GAAP the concept of extraordinary items. The ASU retains and expands the existing presentation and disclosure guidance for items that are unusual in nature or occur infrequently to also include items that are both unusual in nature and infrequently occurring. The provisions of this ASU are effective for fiscal years beginning after December 15, 2015 and interim periods within those fiscal years. Early adoption is permitted, provided that presentation applied to the beginning of the fiscal year of adoption. This amendment is applicable to us beginning in the first quarter of 2017. The adoption of this standard is not expected to have a material impact on our financial statements.

In April 2015, the FASB issued ASU No. 2015-03, "Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs." This ASU requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. In August 2015, the FASB issued ASU No. 2015-15, "Interest - Imputation of Interest (Subtopic 835-30): Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements." This ASU provides additional guidance on ASU No. 2015-03, specific to debt issuance costs arising from line-of-credit arrangements. This ASU provides an option to either apply the provisions of ASU No. 2015-03 to line-of-credit arrangements or to defer and instead present debt issuance costs as an asset and subsequently amortize the deferred debt issuance costs ratably over the term of the line-of-credit arrangement. The provisions of each ASU are effective for fiscal years beginning after December 15, 2015 and interim periods within those fiscal years. Early adoption is permitted, and retrospective application is required. These amendments are applicable to us beginning in the first quarter of 2017. The adoption of these standards are not expected to have a material impact on our financial statements.

In May 2015, the FASB issued ASU No. 2015-07, "Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities that Calculate Net Asset Value per Share (or Its Equivalent)." This ASU removes the requirement to make certain disclosures as well as categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share practical expedient. The provisions of this ASU are effective for fiscal years beginning after December 15, 2015 and interim periods within those fiscal years. Early adoption is permitted, and retrospective application is required. This amendment is applicable to us beginning in the first quarter of 2017. Other than requiring a change to our disclosures, the adoption of this standard is not expected to have a material impact on our financial statements.

In July 2015, the FASB issued ASU No. 2015-11, "Inventory (Topic 330): Simplifying the Measurement of Inventory." This ASU requires inventory to be measured at the lower of cost or net realizable value. The provisions of this ASU are effective for fiscal years beginning after December 15, 2016 and interim periods within those fiscal years. Early adoption is permitted, and the amendment is required to be applied prospectively. This amendment is applicable to us beginning in the first quarter of 2018. The adoption of this standard is not expected to have a material impact on our financial statements.

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In September 2015, the FASB issued ASU No. 2015-16, "Business Combinations (Topic 805): Simplifying the Accounting for Measurement-Period Adjustments." This ASU eliminates the requirement to retrospectively account for changes to provisional amounts initially recorded in a business acquisition opening balance sheet. The provisions of this ASU are effective for fiscal years beginning after December 15, 2015 and interim periods within those fiscal years. Early adoption is permitted as of the effective date for financial statements that have not yet been made available for issuance. This amendment is applicable to us beginning in the first quarter of 2017. The adoption of this standard is not expected to have a material impact on our financial statements.

In November 2015, the FASB issued ASU No. 2015-17, "Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes." This ASU amends existing guidance to require presentation of deferred tax assets and liabilities as noncurrent within the balance sheet. The provisions of the ASU are effective for fiscal years beginning after December 15, 2016 and interim periods within those fiscal years. Early adoption is permitted, and may be applied either prospectively or retrospectively. This amendment is applicable to us beginning in the first quarter of 2018. We are currently evaluating the adoption of this standard on our financial statements.

In January 2016, the FASB issued ASU No. 2016-01, "Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities." This ASU requires most equity investments be measured at fair value, with subsequent changes in fair value recognized in net income. The amendment also impacts the measurement of financial liabilities under the fair value option as well as certain presentation and disclosure requirements for financial instruments. The provisions of this ASU are effective for fiscal years beginning after December 15, 2017 and interim periods within those fiscal years. Early adoption is permitted for some, but not all, provisions. The amendment requires certain provisions to be applied prospectively and others to be applied by means of a cumulative-effect adjustment. This amendment is applicable to us beginning in the first quarter of 2019. We are currently evaluating the adoption of this standard on our financial statements.

In February 2016, the FASB issued ASU No. 2016-02, "Leases (Topic 842)." This ASU requires most lease arrangements to be recognized in the balance sheet as lease assets and lease liabilities. The ASU also requires additional disclosures about the leasing arrangements. The provisions of this ASU are effective for fiscal years beginning after December 15, 2018 and interim periods within those years. Early adoption is permitted. This amendment is applicable to us beginning in the first quarter of 2020. We are currently evaluating the adoption of this standard on our financial statements.

In March 2016, the FASB issued ASU No. 2019-09, "Compensation - Stock Compensation (Topic 718): Improvements to Employee Share Based Payment Accounting." This ASU simplifies several aspects of the accounting for share-based payment transactions, including income tax consequences, classification of awards and classification on the statement of cash flows. The provisions of this ASU are effective for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years. Early adoption is permitted. This amendment is applicable to us beginning in the first quarter of 2018. We are currently evaluating the adoption of this standard on our financial statements.

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## CONSOLIDATED RESULTS OF OPERATIONS AND OUTLOOK

(dollars and shares in millions, except per share data)	Three Months Ended				Nine Months Ended			
	July 2, 2016	July 4, 2015	\$ Variance	% Variance	July 2, 2016	July 4, 2015	\$ Variance	% Variance
Net sales	\$613	\$635	\$ (21)	(3) %	\$1,793	\$1,902	\$ (109)	(6) %
Gross margin	29.9 %	30.0 %			29.2 %	28.8 %		
Research and development expenses	\$36	\$34	\$ 2	5 %	\$111	\$97	\$ 14	14 %
Selling, general and administrative expenses as a percentage of sales	14.4 %	14.3 %			14.2 %	14.8 %		
Interest expense	\$9	\$8	\$ 1	9 %	\$26	\$21	\$ 5	24 %
Restructuring expense	\$—	\$7	\$ (7)	(101) %	\$8	\$7	\$ 2	26 %
Effective tax rate	30.9 %	28.4 %			27.5 %	26.8 %		
Net earnings attributable to common shareholders	\$36	\$36	\$ —	— %	\$94	\$104	\$ (10)	(10) %
Diluted average common shares outstanding	36	39	(2)	(6) %	37	40	(3)	(8) %
Diluted earnings per share attributable to common shareholders	\$1.00	\$0.94	\$ 0.06	6 %	\$2.55	\$2.59	\$ (0.04)	(2) %

Net sales decreased in the third quarter of 2016 compared to the third quarter of 2015 driven by a \$20 million decline in our Components segment and a \$5 million decline in our Space and Defense segment. Aircraft Controls partly offset the declines by \$4 million, due to higher commercial aircraft sales.

Net sales decreased in the first three quarters of 2016 compared to the first three quarters of 2015. With the exception of our Medical Devices segment, the rest of our segments' sales declined. Weaker foreign currencies, in particular the British Pound and the Euro relative to the U.S. dollar, contributed approximately 20% of the sales decline in the first three quarters of 2016.

Gross margin increased in the first three quarters of 2016 compared to the same period of 2015. We benefited from the absence of last year's \$7 million correction of an out-of-period accounting adjustment in our Space and Defense Controls segment. In addition, our year-to-date restructuring benefits from actions taken in 2015 contributed \$7 million of reduced costs. Also, our sales mix improved from higher amounts of foreign military sales in Aircraft Controls. However, the improvements were partly offset by an adverse sales mix in both Components and in Industrial Systems due to lower energy and industrial market sales.

Research and development expenses increased in the first three quarters of 2016 compared to the same periods of 2015. Within Aircraft Controls, research and development expenses increased \$13 million as we had higher activity on the Embraer E-2 and the Airbus A350 programs.

In the first three quarters of 2016 compared to the first three quarters of 2015, selling, general and administrative expenses as a percentage of sales decreased. Most of the decline is attributable to an on-going focus on expense reduction across our segments. Additionally, we benefited \$9 million from our 2015 restructuring activities.

In 2015, we incurred \$15 million of restructuring expenses, primarily in Industrial Systems, Space and Defense Controls and Aircraft Controls. Through nine months of 2016, the total savings were \$16 million, or 76% of our projected benefits for the year. In the second quarter of 2016, we incurred \$8 million of restructuring expenses, primarily related to exiting a product line in Aircraft Controls. Through the third quarter of 2016, the total savings were \$2 million, or 20% of our subsequent four-quarter benefits total.

In the first three quarters of 2016 compared to the first three quarters of 2015, interest expense increased \$3 million due to higher levels of debt attributable to the funding of our share repurchase program. Additionally, interest expense increased \$2 million due to higher interest rates following the issuance of our \$300 million senior notes in November 2014.



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In comparison to the U.S. statutory tax rate, our effective tax rates in 2016 and 2015 differ as a result of earnings being taxed in foreign jurisdictions with lower statutory tax rates. Additionally, our effective tax rates reflect the timing of enactment of the U.S. research and development tax credit, as well as the reversal of accruals for certain tax exposures outside of the U.S. whose statutes of limitations have expired.

Average common shares outstanding decreased in the third quarter and in the first nine months of 2016 compared to the same periods of 2015 due to our share buyback program. Since the Board of Directors amended the program in January 2014, we have repurchased ten million shares, and have three million additional shares available for repurchase under this program.

Other comprehensive loss in the third quarter of 2016 includes \$25 million of foreign currency translation loss. In the third quarter of 2015, other comprehensive income included \$12 million of foreign currency translation income. The negative change for foreign currency translation adjustments during this period is attributable to the changes in the British Pound and the Euro, which decreased \$39 million in total. Other comprehensive loss in the first three quarters of 2016 includes \$34 million of foreign currency translation loss. In the first three quarters of 2015, other comprehensive loss includes \$68 million of foreign currency translation loss. The positive change for foreign currency translation adjustments during this period is due to changes in the the Euro, which increased \$36 million.

2016 Outlook – We expect sales in 2016 to decrease 4% from fiscal 2015 to \$2.42 billion. We expect sales declines in Components and Industrial Systems, as they are negatively impacted by global macro-economic conditions, particularly affecting our marine energy and industrial products. We also expect sales declines in Space and Defense Controls due to lower satellite sales. Partly offsetting the declines is anticipated growth in Aircraft Controls as the Airbus A350 program continues to ramp up. We expect an operating margin of 9.7%. The benefits of our 2015 and 2016 cost containment activities will drive margin expansion; however, the improvement will be offset by the effects of lower sales and an unfavorable sales mix in Components. We expect net earnings attributable to common shareholders will decrease 7% to \$122 million. Average diluted shares outstanding will decrease 7% to 37 million due to shares already repurchased under our current share buyback program. We expect diluted earnings per share will range between \$3.25 and \$3.45, with a midpoint of \$3.35, which would be flat with 2015.

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During 2015, we made a change to our segment reporting. Our Components segment now includes our sensors and handpieces product line, which we previously included in the Medical Devices segment. This product line consists of manufactured ultrasonic and optical sensors as well as surgical handpieces distributed to medical OEMs. Since the customer base is different from the sale of medical pumps directly to end users, the chief operating decision maker is now reviewing performance and assessing the allocation of resources of this product line as part of the Components segment. Sales of sensors and handpieces were \$25 million in 2015. All amounts have been restated to present sensors and handpieces within Components.

Operating profit, as presented below, is net sales less cost of sales and other operating expenses, excluding interest expense, equity-based compensation expense and other corporate expenses. Cost of sales and other operating expenses are directly identifiable to the respective segment or allocated on the basis of sales, number of employees or profit. Operating profit is reconciled to earnings before income taxes in Note 16 of the Notes to Consolidated Condensed Financial Statements included in this report.

**Aircraft Controls**

(dollars in millions)	Three Months Ended				Nine Months Ended			
	July 2, 2016	July 4, 2015	\$	%	July 2, 2016	July 4, 2015	\$	%
Net sales - military aircraft	\$134	\$141	\$ (7 )	(5 %)	\$386	\$401	\$ (15 )	(4 %)
Net sales - commercial aircraft	140	129	11	8 %	419	410	\$ 9	2 %
	\$274	\$270	\$ 4	1 %	\$805	\$811	\$ (6 )	(1 %)
Operating profit	\$31	\$28	\$ 2	8 %	\$68	\$75	\$ (7 )	(10 %)
Operating margin	11.1 %	10.5 %			8.4 %	9.3 %		
Backlog					\$590	\$691	\$ (101 )	(15 %)

Aircraft Controls' net sales were comparable in the third quarter and in the first three quarters of 2016 and 2015; however, in both periods, commercial aircraft sales increased while military aircraft sales decreased.

In the third quarter of 2016 compared to the third quarter of 2015, commercial OEM sales increased \$15 million while commercial aftermarket sales decreased \$4 million. Commercial OEM sales for the Airbus A350 program increased \$10 million due to the program's ramp and sales for Boeing programs increased \$7 million due to higher deliveries. The lower aftermarket sales were due to lower levels of Boeing 787 initial provisioning and business jet aftermarket sales. In the third quarter of 2016, military OEM sales decreased \$5 million across multiple programs due to lower levels of production. Also, military aftermarket sales declined \$2 million across several programs.

In the first three quarters of 2016 compared to the same period of 2015, commercial OEM sales increased \$14 million while commercial aftermarket sales declined \$5 million. Commercial OEM sales to Airbus increased \$18 million due to the A350 program, and sales for Boeing programs increased \$3 million. These increases were partially offset by lower sales on various business jet programs. The commercial aftermarket sales decline was driven by lower levels of Boeing 787 initial provisioning and business jet aftermarket sales. Within military aircraft, OEM sales decreased \$9 million and aftermarket decreased \$6 million. OEM sales on the V-22 program decreased \$13 million. OEM sales also decreased \$8 million across various other military programs. These declines were partially offset by \$6 million of increased sales for foreign military aircraft and by \$6 million of increased sales for the F-35 program. The decline in military aftermarket sales in the first three quarters of 2016 is largely due to work on the C-5 program winding down, partially offset by increased activity on F-35 aftermarket.

Operating margin increased in the third quarter of 2016 compared to the third quarter of 2015. We benefited from \$3 million of restructuring benefits, with approximately one-half of the benefits associated with our 2015 restructuring actions and the other half associated with the benefits of exiting a product line earlier in 2016.

Operating margin declined in the first three quarters of 2016 compared to the first three quarters of 2015. Research and development expenses increased \$13 million, largely associated with the Embraer E-2 and the Airbus A350 programs. Additionally, we incurred \$6 million of restructuring charges related to exiting a product line in the second quarter of 2016. Partially offsetting the margin declines were savings related to our restructuring activities in both

2015 and 2016, which contributed \$5 million of incremental operating profit. Additionally, an improved sales mix, due to higher amounts of foreign military sales, as well as lower operating costs also helped to offset the margin pressures.

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The year-to-date savings related to our restructuring activities of 2015 are \$3 million, or approximately 60% of our total expected annual benefits. Our current expected annual benefits are 90% of our original annual expected benefits, as we have revised our workforce planning. The year-to-date savings related to our restructuring actions of 2016 are \$1 million and are in line with our total expected return.

The decrease of twelve-month backlog for Aircraft Controls at July 2, 2016 compared to July 4, 2015 is primarily due to changes in commercial OEM order patterns.

2016 Outlook for Aircraft Controls – We expect sales in Aircraft Controls to remain at \$1.09 billion in 2016.

Commercial OEM aircraft sales are expected to increase 5%, due primarily to the continued ramp up of the Airbus A350 program. We expect that commercial aftermarket sales will decline due to the lower levels of Boeing 787 initial provisioning sales. We expect military sales will decline 4% in 2016, as lower V-22 and military aftermarket sales will be partially offset by higher F-35 production sales. We expect our operating margin will decrease to 8.5% in 2016 from 9.2% in 2015. Our operating margin will be negatively affected by our second quarter restructuring expenses, as well as increased research and development costs due to the continued spend on the A350 and the Embraer E-2 programs. However, we expect that lower costs, including the benefits from our recent restructuring actions, will offset some of the margin pressures.

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## Space and Defense Controls

(dollars in millions)	Three Months Ended				Nine Months Ended			
	July 2, July 4, \$		%		July 2, July 4, \$		%	
	2016	2015	Variance	Variance	2016	2015	Variance	Variance
Net sales	\$91	\$95	\$ (5 )	(5 %)	\$263	\$288	\$ (26 )	(9 %)
Operating profit	\$14	\$6	\$ 8	124 %	\$39	\$20	\$ 19	97 %
Operating margin	15.1%	6.5 %			14.8 %	6.9 %		
Backlog					\$238	\$234	\$ 4	2 %

Space and Defense Controls' net sales decreased in the third quarter and in the first three quarters of 2016 compared to the same periods of 2015 as a result of declining sales in our space market.

Sales in our space market decreased \$4 million in the third quarter of 2016 compared to the third quarter of 2015, due in part to the completion of prior year satellite contracts. For the first three quarters of 2016 compared to the first three quarters of 2015, sales in our space market decreased \$23 million, due primarily to satellite and launch vehicle contracts winding down. Within our defense market, sales decreased \$3 million in the first three quarters of 2016, driven primarily by lower sales volumes on missile systems.

Operating margin increased in the third quarter of 2016 compared to the third quarter of 2015. The absence of last year's \$6 million of restructuring charges contributed to higher operating profit. In addition, we had lower costs in our security business. Also, the restructuring benefits resulting from last year's actions increased operating profit by \$2 million.

Operating margin increased in the first three quarters of 2016 compared to the first three quarters of 2015. The absence of last year's \$8 million out-of-period adjustment, as well as the prior year's \$6 million restructuring expense contributed to the increase in operating profit. Additionally, the restructuring benefits associated with the prior year's expense increased operating profit by \$5 million. These year-to-date savings match our original total expected annual benefits. Also, improved sales mix, primarily in our satellite business, contributed incremental profit.

The higher level of twelve-month backlog for Space and Defense Controls at July 2, 2016 compared to July 4, 2015 is due to higher orders for launch vehicles and naval and defense controls programs, partially offset by lower levels for missile systems.

2016 Outlook for Space and Defense Controls – We expect sales in Space and Defense Controls to decrease 6% to \$360 million in 2016. We expect sales declines in our space market due to lower than anticipated sales for satellite programs. We expect our operating margin will increase to 14.0% in 2016 from 8.7% in 2015, due to the absence of the 2015 accounting correction and the benefit from our 2015 restructuring actions.

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## Industrial Systems

(dollars in millions)	Three Months Ended				Nine Months Ended			
	July 2, 2016		July 4, 2015		July 2, 2016		July 4, 2015	
	\$	%	\$	%	\$	%	\$	%
Net sales	\$130	\$131	\$ —	— %	\$384	\$393	\$ (10)	(2 %)
Operating profit	\$12	\$13	\$ (2)	(12 %)	\$38	\$39	\$ (1)	(1 %)
Operating margin	8.9 %	10.0 %			10.0 %	9.9 %		
Backlog					\$155	\$185	\$ (30)	(16 %)

Industrial Systems' net sales were comparable in the third quarters of 2016 and 2015.

Industrial Systems' net sales decreased in the first nine months of 2016 compared to the first nine months of 2015.

Weaker foreign currencies, in particular the Euro and the Brazilian Real relative to the U.S. dollar, resulted in a \$13 million sales decline. Excluding the currency effects, Industrial Systems' sales increased \$4 million, as simulation programs increased \$9 million, but were partially offset by \$5 million of lower industrial automation sales. Simulation programs increased due to higher sales volumes to flight simulation customers. Sales decreased in our industrial automation market due to the continuing economic weakness in our markets resulting in lower demand for our products.

Operating margin decreased in the third quarter of 2016 compared to the third quarter of 2015. We were negatively affected in the quarter by an unfavorable sales mix due to lower sales in our non-renewable energy and industrial automation markets. Also, research and development expenses increased \$1 million due to work on our next generation wind products. Partly offsetting the declines was \$2 million of benefits from our 2015 restructuring activities.

Operating margin increased slightly in the first nine months of 2016 compared to the same period of 2015. Operating profit included \$5 million of benefits from our 2015 restructuring activities. These year-to-date savings are approximately 70% of our original total expected annual benefits and are in line with our expectations. However, higher research and development expenses decreased operating profit by \$3 million. Additionally, an unfavorable sales mix in our energy and industrial automation markets in the first nine months of 2016 negatively affected operating profit. We also incurred \$1 million of additional restructuring expense in the second quarter of 2016.

The lower level of twelve-month backlog in Industrial Systems at July 2, 2016 compared to July 4, 2015 is due to the completion of simulation orders as well as lower energy orders related to the decline in the energy market.

2016 Outlook for Industrial Systems – We expect sales in Industrial Systems to decrease 3% to \$505 million in 2016. We expect that the impacts of the weaker foreign currencies relative to the U.S. dollar, as well as the evolving global economic conditions, will continue to negatively impact our sales. We expect our operating margin will increase to 9.8% in 2016 from 8.6% in 2015, as we benefit from both our recent restructuring actions and our cost containment activities.

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## Components

(dollars in millions)	Three Months Ended				Nine Months Ended			
	July 2, 2016	July 4, 2015	\$	%	July 2, 2016	July 4, 2015	\$	%
Net sales	\$92	\$113	\$ (20 )	(18 %)	\$266	\$335	\$ (70 )	(21 %)
Operating profit	\$11	\$15	\$ (4 )	(28 %)	\$24	\$48	\$ (24 )	(50 %)
Operating margin	11.7%	13.3 %			9.0 %	14.3 %		
Backlog					\$165	\$165	\$ —	— %

Components' net sales decreased across all of our markets in the third quarter and in the first three quarters of 2016 compared to the same periods of 2015.

Within our non-aerospace and defense market, sales in our energy, our industrial and our medical markets decreased in total by \$14 million in the third quarter of 2016 and \$50 million in the first nine months of 2016 compared to the same periods of 2015. Within our energy market, sales declined \$8 million and \$28 million, respectively, due to the macro-economic conditions centered around the significant decline in the price of crude oil and the resulting lower demand for our marine products. Also, sales declined \$4 million and \$11 million, respectively, in our industrial market due to unfavorable order timing and due to macro-economic industrial conditions. Additionally, sales declined \$1 million and \$11 million, respectively, in our medical market due in part to a lower price point for a key customer's next generation sleep apnea product. Within our aerospace and defense market, sales decreased \$7 million and \$20 million, respectively, due primarily to lower demand for aftermarket products and lower orders for our space and defense products.

Operating margin declined in the third quarter and in the first three quarters of 2016 compared to the same periods of 2015. The decreases are due, in part, to lower demand for our marine energy products resulting from the significant decline in the price of crude oil. Operating margin in the first nine months of 2016 was also negatively affected by lower sales in our medical and our military markets.

The twelve-month backlog at July 2, 2016 is comparable to the level at July 4, 2015, as higher orders for our defense market are offset by lower orders in our marine energy market.

2016 Outlook for Components – We expect sales to decrease 17% to \$365 million in 2016 across all of our markets. We expect our operating margin will decrease to 10.0% in 2016 from 13.4% in 2015. We will continue to be negatively impacted by macro-economic conditions reducing the demand for products in our energy and industrial markets in 2016.

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Medical Devices

(dollars in millions)	Three Months Ended				Nine Months Ended			
	July 2, 2016	July 4, 2015	\$ Variance	% Variance	July 2, 2016	July 4, 2015	\$ Variance	% Variance
Net sales	\$26	\$26	\$ —	1 %	\$76	\$74	\$ 2	3 %
Operating profit	\$2	\$4	\$ (1 )	(38 %)	\$8	\$7	\$ 1	22 %
Operating margin	8.4 %	13.6%						