

TEXTRON INC
Form 10-Q
October 24, 2014
[Table of Contents](#)

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

(Mark One)

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

For the quarterly period ended September 27, 2014

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 1-5480

Textron Inc.

(Exact name of registrant as specified in its charter)

Edgar Filing: TEXTRON INC - Form 10-Q

Delaware

(State or other jurisdiction of incorporation or organization)

05-0315468

(I.R.S. Employer Identification No.)

40 Westminster Street, Providence, RI

(Address of principal executive offices)

02903

(Zip code)

(401) 421-2800

(Registrant's telephone number, including area code)

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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 definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act (Check one):

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 Act). Yes No

As of October 10, 2014, there were 276,048,870 shares of common stock outstanding.

Table of Contents

TEXTRON INC.

INDEX

	Page
<u>PART I. FINANCIAL INFORMATION</u>	
<u>Item 1. Financial Statements</u>	
<u>Consolidated Statements of Operations (Unaudited)</u>	3
<u>Consolidated Statements of Comprehensive Income (Unaudited)</u>	4
<u>Consolidated Balance Sheets (Unaudited)</u>	5
<u>Consolidated Statements of Cash Flows (Unaudited)</u>	6
<u>Notes to the Consolidated Financial Statements (Unaudited)</u>	
<u>Note 1. Basis of Presentation</u>	8
<u>Note 2. Business Acquisitions</u>	9
<u>Note 3. Retirement Plans</u>	11
<u>Note 4. Earnings per Share</u>	11
<u>Note 5. Accounts Receivable and Finance Receivables</u>	12
<u>Note 6. Inventories</u>	14
<u>Note 7. Accrued Liabilities</u>	14
<u>Note 8. Debt</u>	15
<u>Note 9. Accumulated Other Comprehensive Loss and Other Comprehensive Income</u>	15
<u>Note 10. Commitments and Contingencies</u>	17
<u>Note 11. Derivative Instruments and Fair Value Measurements</u>	17
<u>Note 12. Income Tax Expense</u>	18
<u>Note 13. Segment Information</u>	19
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	20
<u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u>	32
<u>Item 4. Controls and Procedures</u>	32
<u>PART II. OTHER INFORMATION</u>	
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	33
<u>Item 6. Exhibits</u>	34
<u>Signatures</u>	34

Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. FINANCIAL STATEMENTS****TEXTRON INC.
Consolidated Statements of Operations (Unaudited)**

	Three Months Ended		Nine Months Ended	
	September 27, 2014	September 28, 2013	September 27, 2014	September 28, 2013
<i>(In millions, except per share amounts)</i>				
Revenues				
Manufacturing revenues	\$ 3,405	\$ 2,871	\$ 9,701	\$ 8,492
Finance revenues	25	33	81	106
Total revenues	3,430	2,904	9,782	8,598
Costs and expenses				
Cost of sales	2,845	2,473	8,077	7,193
Selling and administrative expense	304	245	959	820
Interest expense	47	41	141	134
Acquisition and restructuring costs	3		39	
Total costs and expenses	3,199	2,759	9,216	8,147
Income from continuing operations before income taxes	231	145	566	451
Income tax expense	71	47	174	124
Income from continuing operations	160	98	392	327
Income (loss) from discontinued operations, net of income taxes	(1)	1	(4)	4
Net income	\$ 159	\$ 99	\$ 388	\$ 331
Basic earnings per share				
Continuing operations	\$ 0.57	\$ 0.35	\$ 1.40	\$ 1.18
Discontinued operations			(0.02)	0.01
Basic earnings per share	\$ 0.57	\$ 0.35	\$ 1.38	\$ 1.19
Diluted earnings per share				
Continuing operations	\$ 0.57	\$ 0.35	\$ 1.39	\$ 1.15
Discontinued operations			(0.02)	0.01
Diluted earnings per share	\$ 0.57	\$ 0.35	\$ 1.37	\$ 1.16
Dividends per share				
Common stock	\$ 0.02	\$ 0.02	\$ 0.06	\$ 0.06

See Notes to the consolidated financial statements.

Table of Contents**TEXTRON INC.****Consolidated Statements of Comprehensive Income (Unaudited)**

	Three Months Ended		Nine Months Ended	
	September 27, 2014	September 28, 2013	September 27, 2014	September 28, 2013
<i>(In millions)</i>				
Net income	\$ 159	\$ 99	\$ 388	\$ 331
Other comprehensive income, net of tax:				
Pension and postretirement benefits adjustments, net of reclassifications	17	64	62	127
Deferred gains/losses on hedge contracts, net of reclassifications	(5)	2	2	(11)
Foreign currency translation adjustments	(43)	12	(47)	3
Other comprehensive income (loss)	(31)	78	17	119
Comprehensive income	\$ 128	\$ 177	\$ 405	\$ 450

See Notes to the consolidated financial statements.

Table of Contents

TEXTRON INC.

Consolidated Balance Sheets (Unaudited)

<i>(Dollars in millions)</i>	September 27, 2014	December 28, 2013
Assets		
Manufacturing group		
Cash and equivalents	\$ 430	\$ 1,163
Accounts receivable, net	1,150	979
Inventories	4,081	2,963
Other current assets	539	467
Total current assets	6,200	5,572
Property, plant and equipment, less accumulated depreciation and amortization of \$3,662 and \$3,463	2,442	2,215
Goodwill	2,020	1,735
Other assets	2,509	1,697
Total Manufacturing group assets	13,171	11,219
Finance group		
Cash and equivalents	81	48
Finance receivables, net	1,308	1,493
Other assets	179	184
Total Finance group assets	1,568	1,725
Total assets	\$ 14,739	\$ 12,944
Liabilities and shareholders equity		
Liabilities		
Manufacturing group		
Short-term and current portion of long-term debt	\$ 383	\$ 8
Accounts payable	1,135	1,107
Accrued liabilities	2,375	1,888
Total current liabilities	3,893	3,003
Other liabilities	2,451	2,118
Long-term debt	2,474	1,923
Total Manufacturing group liabilities	8,818	7,044
Finance group		
Other liabilities	238	260
Debt	1,111	1,256
Total Finance group liabilities	1,349	1,516
Total liabilities	10,167	8,560
Shareholders equity		
Common stock	36	35
Capital surplus	1,432	1,331
Treasury stock	(302)	
Retained earnings	4,416	4,045
Accumulated other comprehensive loss	(1,010)	(1,027)
Total shareholders equity	4,572	4,384
Total liabilities and shareholders equity	\$ 14,739	\$ 12,944
Common shares outstanding (in thousands)	276,195	282,059

See Notes to the consolidated financial statements.

Table of Contents**TEXTRON INC.****Consolidated Statements of Cash Flows (Unaudited)**

For the Nine Months Ended September 27, 2014 and September 28, 2013, respectively

<i>(In millions)</i>	Consolidated	
	2014	2013
Cash flows from operating activities		
Net income	\$ 388	\$ 331
Less: Income (loss) from discontinued operations	(4)	4
Income from continuing operations	392	327
Adjustments to reconcile income from continuing operations to net cash provided by (used in) operating activities:		
Non-cash items:		
Depreciation and amortization	325	285
Deferred income taxes	(41)	74
Other, net	80	38
Changes in assets and liabilities:		
Accounts receivable, net	(55)	(178)
Inventories	(370)	(443)
Other assets	24	(51)
Accounts payable	(120)	(25)
Accrued and other liabilities	137	(276)
Income taxes, net	61	(96)
Pension, net	31	(17)
Captive finance receivables, net	107	257
Other operating activities, net	(2)	2
Net cash provided by (used in) operating activities of continuing operations	569	(103)
Net cash used in operating activities of discontinued operations	(3)	(5)
Net cash provided by (used in) operating activities	566	(108)
Cash flows from investing activities		
Net cash used in acquisitions	(1,580)	(53)
Capital expenditures	(255)	(300)
Finance receivables repaid	77	157
Proceeds from sales of receivables and other finance assets	37	152
Other investing activities, net	(4)	13
Net cash used in investing activities	(1,725)	(31)
Cash flows from financing activities		
Proceeds from long-term debt	1,187	412
Principal payments on long-term and nonrecourse debt	(462)	(997)
Increase in short-term debt	25	96
Purchases of Textron common stock	(302)	
Settlement of convertible notes		(215)
Proceeds from settlement of capped call		75
Dividends paid	(17)	(16)
Other financing activities, net	33	16
Net cash provided by (used in) financing activities	464	(629)
Effect of exchange rate changes on cash and equivalents	(5)	(8)
Net decrease in cash and equivalents	(700)	(776)
Cash and equivalents at beginning of period	1,211	1,413
Cash and equivalents at end of period	\$ 511	\$ 637

See Notes to the consolidated financial statements.

Table of Contents**TEXTRON INC.****Consolidated Statements of Cash Flows (Unaudited) (Continued)**

For the Nine Months Ended September 27, 2014 and September 28, 2013, respectively

<i>(In millions)</i>	Manufacturing Group		Finance Group	
	2014	2013	2014	2013
Cash flows from operating activities				
Net income	\$ 378	\$ 300	\$ 10	\$ 31
Less: Income (loss) from discontinued operations	(4)	4		
Income from continuing operations	382	296	10	31
Adjustments to reconcile income from continuing operations to net cash provided by (used in) operating activities:				
Non-cash items:				
Depreciation and amortization	315	271	10	14
Deferred income taxes	(25)	29	(16)	45
Other, net	69	69	11	(31)
Changes in assets and liabilities:				
Accounts receivable, net	(55)	(178)		
Inventories	(344)	(459)		
Other assets	38	(40)	(14)	(11)
Accounts payable	(120)	(25)		
Accrued and other liabilities	145	(262)	(8)	(24)
Income taxes, net	57	(101)	4	5
Pension, net	31	(12)		(5)
Dividends received from Finance Group		30		
Capital contributions paid to Finance Group		(1)		
Other operating activities, net	(2)	2		
Net cash provided by (used in) operating activities of continuing operations	491	(381)	(3)	24
Net cash used in operating activities of discontinued operations	(3)	(5)		
Net cash provided by (used in) operating activities	488	(386)	(3)	24
Cash flows from investing activities				
Net cash used in acquisitions	(1,580)	(53)		
Capital expenditures	(255)	(300)		
Finance receivables repaid			307	558
Finance receivables originated or purchased			(123)	(164)
Proceeds from sales of receivables and other finance assets			37	152
Other investing activities, net	(12)	19	(18)	40
Net cash provided by (used in) investing activities	(1,847)	(334)	203	586
Cash flows from financing activities				
Proceeds from long-term debt	1,093	150	94	262
Principal payments on long-term and nonrecourse debt	(201)	(312)	(261)	(685)
Increase in short-term debt	25	96		
Purchases of Textron common stock	(302)			
Settlement of convertible notes		(215)		
Proceeds from settlement of capped call		75		
Dividends paid	(17)	(16)		(30)
Capital contributions paid to Finance group				1
Other financing activities, net	33	16		
Net cash provided by (used in) financing activities	631	(206)	(167)	(452)
Effect of exchange rate changes on cash and equivalents	(5)	(8)		
Net increase (decrease) in cash and equivalents	(733)	(934)	33	158
Cash and equivalents at beginning of period	1,163	1,378	48	35
Cash and equivalents at end of period	\$ 430	\$ 444	\$ 81	\$ 193

See Notes to the consolidated financial statements.

Table of Contents

TEXTRON INC.

Notes to the Consolidated Financial Statements (Unaudited)

Note 1. Basis of Presentation

Our Consolidated Financial Statements include the accounts of Textron Inc. (Textron) and its majority-owned subsidiaries. On March 14, 2014, we completed the acquisition of all of the outstanding equity interests in Beech Holdings, LLC, which included Beechcraft Corporation and other subsidiaries, (collectively "Beechcraft"). The results of Beechcraft have been included in our consolidated financial statements only for the period subsequent to the completion of the acquisition. As a result, the consolidated financial results for the nine months ended September 27, 2014 do not reflect a full nine months of Beechcraft operations.

We have prepared these unaudited consolidated financial statements in accordance with accounting principles generally accepted in the U.S. for interim financial information. Accordingly, these interim financial statements do not include all of the information and footnotes required by accounting principles generally accepted in the U.S. for complete financial statements. The consolidated interim financial statements included in this quarterly report should be read in conjunction with the consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 28, 2013. In the opinion of management, the interim financial statements reflect all adjustments (consisting only of normal recurring adjustments) that are necessary for the fair presentation of our consolidated financial position, results of operations and cash flows for the interim periods presented. The results of operations for the interim periods are not necessarily indicative of the results to be expected for the full year.

Our financings are conducted through two separate borrowing groups. The Manufacturing group consists of Textron consolidated with its majority-owned subsidiaries that operate in the Bell, Textron Systems and Industrial segments, and the recently formed Textron Aviation segment, which includes the legacy Cessna segment and the acquired Beechcraft business. The Finance group, which also is the Finance segment, consists of Textron Financial Corporation (TFC) and its consolidated subsidiaries. We designed this framework to enhance our borrowing power by separating the Finance group. Our Manufacturing group operations include the development, production and delivery of tangible goods and services, while our Finance group provides financial services. Due to the fundamental differences between each borrowing group's activities, investors, rating agencies and analysts use different measures to evaluate each group's performance. To support those evaluations, we present balance sheet and cash flow information for each borrowing group within the Consolidated Financial Statements. All significant intercompany transactions are eliminated from the Consolidated Financial Statements, including retail and wholesale financing activities for inventory sold by our Manufacturing group and financed by our Finance group.

Use of Estimates

We prepare our financial statements in conformity with generally accepted accounting principles, which require us to make estimates and assumptions that affect the amounts reported in the financial statements. Actual results could differ from those estimates. Our estimates and assumptions are reviewed periodically, and the effects of changes, if any, are reflected in the Consolidated Statements of Operations in the period that they are determined.

During 2014 and 2013, we changed our estimates of revenues and costs on certain long-term contracts that are accounted for under the percentage-of-completion method of accounting. These changes in estimates increased income from continuing operations before income taxes

Edgar Filing: TEXTRON INC - Form 10-Q

in the third quarter of 2014 and 2013 by \$10 million and \$4 million, respectively, (\$6 million and \$2 million after tax, or \$0.02 and \$0.01 per diluted share, respectively). For the third quarter of 2014 and 2013, the gross favorable program profit adjustments totaled \$25 million and \$12 million, respectively, and the gross unfavorable program profit adjustments totaled \$15 million and \$8 million, respectively.

The changes in estimates increased income from continuing operations before income taxes in the first nine months of 2014 and 2013 by \$69 million and \$13 million, respectively, (\$43 million and \$8 million after tax, or \$0.15 and \$0.03 per diluted share, respectively). For the first nine months of 2014 and 2013, the gross favorable program profit adjustments totaled \$90 million and \$30 million, respectively, and the gross unfavorable program profit adjustments totaled \$21 million and \$17 million, respectively. Gross favorable program profit adjustments in the second quarter of 2014 included \$16 million related to the settlement of the System Development and Demonstration phase of the Armed Reconnaissance Helicopter (ARH) program which was terminated in October 2008.

New Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, Revenue from Contracts with Customers, that outlines a comprehensive five-step revenue recognition model based on the principle that an entity should recognize revenue to depict the transfer of promised 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 and services. Entities have the option of using either a full retrospective or a modified retrospective approach for the adoption. This ASU is effective for our

Table of Contents

company at the beginning of fiscal 2017; early adoption is not permitted. We are currently evaluating the new guidance to determine the impact it is expected to have on our consolidated financial statements, along with the transition method we expect to utilize.

Note 2. Business Acquisitions**2014 Beechcraft Acquisition**

On March 14, 2014, we acquired Beechcraft for an aggregate cash payment of \$1.5 billion that included a repayment of a portion of Beechcraft's working capital credit facility at closing. We financed a portion of the purchase price with the issuance of \$600 million in senior notes on January 30, 2014 and by drawing \$500 million under the five-year term loan agreement entered into on January 24, 2014. The balance was paid from cash on hand.

Beechcraft is a leading manufacturer of business, special mission, light attack and trainer aircraft, including the King Air turboprops, piston-engine Baron and Bonanza, and the T-6 trainer and AT-6 light attack military aircraft. Beechcraft also has a global network of both factory-owned and authorized service centers. The acquisition of Beechcraft and the formation of the Textron Aviation segment provide increased scale and complementary product offerings, allowing us to strengthen our position across the aviation industry and enhance our ability to support our customers.

The consideration paid for this business was allocated on a preliminary basis to the assets acquired and liabilities assumed based on their estimated fair values at the acquisition date, which have been subsequently adjusted as estimates are being finalized. Due to the size and breadth of this acquisition, additional time is necessary to complete the purchase accounting related to the fair values of certain assets and liabilities. We will finalize the purchase accounting as soon as reasonably possible during the one-year-measurement period allowed under generally accepted accounting principles. Any potential adjustments to the preliminary fair values could be material. Our allocation of the purchase price is presented below.

(In millions)

Accounts receivable	\$ 118
Inventories	770
Other current assets	175
Property, plant and equipment	258
Intangible assets	581
Goodwill	226
Other assets	171
Accounts payable	(143)
Accrued liabilities	(282)
Other liabilities	(396)
Total net assets acquired	\$ 1,478

Goodwill of \$226 million was primarily related to expected synergies from combining operations and the value of the existing workforce, and intangible assets of \$581 million included unpatented technology related to original equipment manufactured parts and designs and customer relationships valued at \$373 million and trade names valued at \$208 million. The unpatented technology and customer relationships assets have a life of 15 years, resulting in amortization expense in the range of approximately \$17 million to \$31 million annually. Substantially all of the trade names intangible asset has an indefinite life and therefore is not subject to amortization.

We acquired tax-deductible goodwill of approximately \$260 million in this transaction. We also recorded unrecognized tax benefits of approximately \$95 million at the acquisition date.

In connection with the integration of Beechcraft, we initiated a restructuring program in our Textron Aviation segment in the first quarter of 2014 to align the Cessna and Beechcraft businesses, reduce operating redundancies and maximize efficiencies. We expect to incur costs for this program related to employee terminations, facility consolidations, contract terminations and other transition-related costs, and estimate that this program will result in charges of approximately \$35 million in 2014. We expect to incur additional costs in 2015, but do not expect these costs to be material. In the third quarter and first nine months of 2014, we recorded charges of \$3 million and \$28 million, respectively, related to restructuring activities that were included in the Acquisition and restructuring costs line on the Consolidated Statements of Operations. In addition, we incurred transaction costs of \$11 million during the first quarter of 2014 related to the acquisition that were also included in the Acquisition and restructuring costs line.

Table of Contents**Other 2014 Acquisitions**

During the first nine months of 2014, we made aggregate cash payments of \$101 million for the following acquisitions:

Industrial

- Tug Technologies Corporation, a manufacturer of ground support equipment in the aviation industry, acquired on May 2, 2014.
- The assets of Dixie Chopper, a manufacturer of zero-turn radius mowers for the commercial and residential markets, acquired on February 6, 2014.

Textron Systems

- ProFlight, LLC, a pilot training operation, acquired on July 2, 2014.

Actual and Pro-Forma Impact from 2014 Acquisitions

The operating results for the 2014 acquisitions are included in the Consolidated Statement of Operations since their respective closing dates. From the closing dates through September 27, 2014, revenues related to these acquisitions totaled \$435 million and \$993 million for the three- and nine-month periods, respectively. The cost structures of Beechcraft and Cessna have been significantly integrated since the acquisition of Beechcraft, therefore, it is not possible to separately report earnings for this acquisition. The earnings related to the other 2014 acquisitions were not significant.

The unaudited supplemental pro-forma data included in the table below presents consolidated information as if our 2014 acquisitions had been completed on December 30, 2012. This pro-forma information should not be considered indicative of the results that would have occurred if the acquisition and related financing had been consummated on December 30, 2012, nor are they necessarily indicative of future results as they do not reflect the potential realization of cost savings and synergies associated with the acquisition.

	Three Months Ended		Nine Months Ended	
	September 27, 2014	September 28, 2013	September 27, 2014	September 28, 2013
<i>(In millions, except per share amounts)</i>				
Revenues	\$ 3,430	\$ 3,308	\$ 10,145	\$ 9,907
Income from continuing operations, net of income taxes	169	78	462	279
Diluted earnings per share from continuing operations	\$ 0.60	\$ 0.28	\$ 1.64	\$ 0.98

Certain pro-forma adjustments were made to reflect the allocation of the preliminary purchase price to the acquired net assets including depreciation and intangible amortization expense, resulting from the valuation of tangible and intangible assets, and amortization of inventory fair value step-up adjustments, along with the related tax effects. The pro-forma results for 2013 were also adjusted to include transaction and restructuring costs of \$3 million and \$39 million for the three- and nine-month periods, respectively, related to the Beechcraft acquisition; these costs were excluded from the 2014 pro-forma results. In addition, the pro-forma results exclude the financial impact related to Beechcraft's emergence from bankruptcy in 2013.

Table of Contents**Note 3. Retirement Plans**

We provide defined benefit pension plans and other postretirement benefits to eligible employees. The components of net periodic benefit cost for these plans are as follows:

	Pension Benefits		Postretirement Benefits Other Than Pensions	
	September 27, 2014	September 28, 2013	September 27, 2014	September 28, 2013
<i>(In millions)</i>				
Three Months Ended				
Service cost	\$ 27	\$ 33	\$ 1	\$ 1
Interest cost	86	72	5	5
Expected return on plan assets	(117)	(104)		
Amortization of prior service cost (credit)	3	4	(5)	(6)
Amortization of net actuarial loss	28	46		2
Net periodic benefit cost	\$ 27	\$ 51	\$ 1	\$ 2
Nine Months Ended				
Service cost	\$ 81	\$ 100	\$ 3	\$ 5
Interest cost	250	218	15	15
Expected return on plan assets	(345)	(314)		
Amortization of prior service cost (credit)	11	11	(16)	(11)
Amortization of net actuarial loss	84	138	1	5
Net periodic benefit cost	\$ 81	\$ 153	\$ 3	\$ 14

Note 4. Earnings Per Share

In February 2014, we entered into an Accelerated Share Repurchase agreement (ASR) with a counterparty and repurchased 4.3 million shares of our outstanding common stock from the counterparty for \$150 million. The initial delivery of shares resulted in an immediate reduction of the outstanding shares used to calculate the weighted average common shares for basic and diluted earnings per share. The ASR is scheduled to settle in December 2014. Upon final settlement of the ASR, we may receive additional shares or pay additional cash or shares, at our option, based on the daily volume weighted average market price (VWAP) of our common stock over the course of the calculation period, less a discount. We intend to settle any amount payable by us in shares. At September 27, 2014, based on the VWAP through that date, we would be required to issue to the counterparty approximately 278,000 shares to settle the ASR. For accounting purposes, the ASR is considered a treasury stock purchase for the 4.3 million shares delivered to us by the counterparty, and a forward contract indexed to our common stock for the shares to be delivered upon settlement, if any. The forward contract is not required to be separately accounted for as a derivative.

We calculate basic and diluted earnings per share (EPS) based on net income, which approximates income available to common shareholders for each period. Basic EPS is calculated using the two-class method, which includes the weighted-average number of common shares outstanding during the period and restricted stock units to be paid in stock that are deemed participating securities as they provide nonforfeitable rights to dividends. Diluted EPS considers the dilutive effect of all potential future common stock, including stock options and shares that would have been delivered if the ASR were settled at September 27, 2014. In addition, for the first nine months of 2013, prior to the maturity of our convertible notes on May 1, 2013 as disclosed in Note 7 of our 2013 Annual Report on Form 10-K, diluted EPS included the shares that could have been issued upon the conversion of the notes and upon the exercise of the related warrants.

Edgar Filing: TEXTRON INC - Form 10-Q

The weighted-average shares outstanding for basic and diluted EPS are as follows:

<i>(In thousands)</i>	Three Months Ended		Nine Months Ended	
	September 27, 2014	September 28, 2013	September 27, 2014	September 28, 2013
Basic weighted-average shares outstanding	278,860	281,525	280,096	278,296
Dilutive effect of:				
Stock options	1,892	185	2,027	221
ASR	278		301	
Convertible notes and warrants				6,226
Diluted weighted-average shares outstanding	281,030	281,710	282,424	284,743

Stock options to purchase 2 million shares of common stock outstanding are excluded from our calculation of diluted weighted-average shares outstanding for both the three and nine months ended September 27, 2014, as their effect would have been anti-dilutive. Stock options to purchase 6 million and 5 million shares of common stock outstanding are excluded from our calculation

Table of Contents

of diluted weighted-average shares outstanding for the three and nine months ended September 28, 2013, respectively, as their effect would have been anti-dilutive.

Note 5. Accounts Receivable and Finance Receivables**Accounts Receivable**

Accounts receivable is composed of the following:

<i>(In millions)</i>	September 27, 2014	December 28, 2013
Commercial	\$ 849	\$ 654
U.S. Government contracts	329	347
	1,178	1,001
Allowance for doubtful accounts	(28)	(22)
Total	\$ 1,150	\$ 979

We have unbillable receivables, primarily on U.S. Government contracts, that arise when the revenues we have appropriately recognized based on performance cannot be billed yet under terms of the contract. Unbillable receivables within accounts receivable totaled \$124 million at September 27, 2014 and \$163 million at December 28, 2013.

Finance Receivables

Finance receivables by classification are presented in the following table:

<i>(In millions)</i>	September 27, 2014	December 28, 2013
Finance receivables held for investment	\$ 1,329	\$ 1,483
Allowance for losses	(56)	(55)
Total finance receivables held for investment, net	1,273	1,428
Finance receivables held for sale	35	65
Total finance receivables, net	\$ 1,308	\$ 1,493

Credit Quality Indicators and Nonaccrual Finance Receivables

We internally assess the quality of our finance receivables based on a number of key credit quality indicators and statistics such as delinquency, loan balance to estimated collateral value and the financial strength of individual borrowers and guarantors. Because many of these indicators are difficult to apply across an entire class of receivables, we evaluate individual loans on a quarterly basis and classify these loans into three categories based on the key credit quality indicators for the individual loan. These three categories are performing, watchlist and nonaccrual.

Edgar Filing: TEXTRON INC - Form 10-Q

We classify finance receivables as nonaccrual if credit quality indicators suggest full collection of principal and interest is doubtful. In addition, we automatically classify accounts as nonaccrual once they are contractually delinquent by more than three months unless collection of principal and interest is not doubtful. Recognition of interest income is suspended for these accounts and all cash collections are used to reduce the net investment balance. We resume the accrual of interest when the loan becomes contractually current through payment according to the original terms of the loan or, if a loan has been modified, following a period of performance under the terms of the modification, provided we conclude that collection of all principal and interest is no longer doubtful. Previously suspended interest income is recognized at that time. Accounts are classified as watchlist when credit quality indicators have deteriorated as compared with typical underwriting criteria, and we believe collection of full principal and interest is probable but not certain. All other finance receivables that do not meet the watchlist or nonaccrual categories are classified as performing.

A summary of finance receivables categorized based on the credit quality indicators discussed above is as follows:

<i>(In millions)</i>	September 27, 2014	December 28, 2013
Performing	\$ 1,111	\$ 1,285
Watchlist	117	93
Nonaccrual	101	105
Total	\$ 1,329	\$ 1,483
Nonaccrual as a percentage of total finance receivables	7.60%	7.08%

We measure delinquency based on the contractual payment terms of our loans and leases. In determining the delinquency aging

Table of Contents

category of an account, any/all principal and interest received is applied to the most past-due principal and/or interest amounts due. If a significant portion of the contractually due payment is delinquent, the entire finance receivable balance is reported in accordance with the most past-due delinquency aging category.

Finance receivables by delinquency aging category are summarized in the table below:

<i>(In millions)</i>	September 27, 2014	December 28, 2013
Less than 31 days past due	\$ 1,165	\$ 1,295
31-60 days past due	94	108
61-90 days past due	41	37
Over 90 days past due	29	43
Total	\$ 1,329	\$ 1,483

Accrual status loans that were greater than 90 days past due totaled \$4 million at September 27, 2014 and \$5 million at December 28, 2013. At September 27, 2014 and December 28, 2013, 60+ days contractual delinquency as a percentage of finance receivables was 5.27% and 5.39%, respectively.

Loan Modifications

Troubled debt restructurings occur when we have either modified the contract terms of finance receivables for borrowers experiencing financial difficulties or accepted a transfer of assets in full or partial satisfaction of the loan balance. The types of modifications we typically make include extensions of the original maturity date of the contract, delays in the timing of required principal payments and deferrals of interest payments. The changes effected by modifications made during the first nine months of 2014 and 2013 to finance receivables were not material.

Impaired Loans

On a quarterly basis, we evaluate individual finance receivables for impairment in non-homogeneous portfolios and larger balance accounts in homogeneous loan portfolios. A finance receivable is considered impaired when it is probable that we will be unable to collect all amounts due according to the contractual terms of the loan agreement based on our review of the credit quality indicators discussed above. Impaired finance receivables include both nonaccrual accounts and accounts for which full collection of principal and interest remains probable, but the account's original terms have been, or are expected to be, significantly modified. If the modification specifies an interest rate equal to or greater than a market rate for a finance receivable with comparable risk, the account is not considered impaired in years subsequent to the modification. Interest income recognized on impaired loans was not significant in the first nine months of 2014 or 2013.

A summary of impaired finance receivables, excluding leveraged leases, and the average recorded investment is provided below:

<i>(In millions)</i>	September 27, 2014	December 28, 2013
Recorded investment:		

Edgar Filing: TEXTRON INC - Form 10-Q

Impaired loans with related allowance for losses	\$ 78	\$ 59
Impaired loans with no related allowance for losses	53	78
Total	\$ 131	\$ 137
Unpaid principal balance	\$ 135	\$ 141
Allowance for losses on impaired loans	23	14
Average recorded investment	116	155

A summary of the allowance for losses on finance receivables that are evaluated on an individual basis and on a collective basis is provided below. The finance receivables included in the table below excludes leveraged leases in accordance with generally accepted accounting principles.

<i>(In millions)</i>	September 27, 2014	December 28, 2013
Allowance based on collective evaluation	\$ 33	\$ 41
Allowance based on individual evaluation	23	14
Finance receivables evaluated collectively	\$ 1,077	\$ 1,226
Finance receivables evaluated individually	131	137

Table of Contents

Allowance for Losses

We maintain the allowance for losses on finance receivables at a level considered adequate to cover inherent losses in the portfolio based on management's evaluation. For larger balance accounts specifically identified as impaired, a reserve is established based on comparing the expected future cash flows, discounted at the finance receivable's effective interest rate, or the fair value of the underlying collateral if the finance receivable is collateral dependent, to its carrying amount. The expected future cash flows consider collateral value; financial performance and liquidity of our borrower; existence and financial strength of guarantors; estimated recovery costs, including legal expenses; and costs associated with the repossession and eventual disposal of collateral. When there is a range of potential outcomes, we perform multiple discounted cash flow analyses and weight the potential outcomes based on their relative likelihood of occurrence. The evaluation of our portfolio is inherently subjective, as it requires estimates, including the amount and timing of future cash flows expected to be received on impaired finance receivables and the estimated fair value of the underlying collateral, which may differ from actual results. While our analysis is specific to each individual account, critical factors included in this analysis are industry valuation guides, age and physical condition of the collateral, payment history and existence and financial strength of guarantors.

We also establish an allowance for losses to cover probable but specifically unknown losses existing in the portfolio. The allowance is established as a percentage of non-recourse finance receivables, which have not been identified as requiring specific reserves. The percentage is based on a combination of factors, including historical loss experience, current delinquency and default trends, collateral values and both general economic and specific industry trends. Finance receivables are charged off at the earlier of the date the collateral is repossessed or when no payment has been received for six months, unless management deems the receivable collectible.

A rollforward of the allowance for losses on finance receivables is provided below:

	Nine Months Ended	
	September 27, 2014	September 28, 2013
<i>(In millions)</i>		
Balance at the beginning of period	\$ 55	\$ 84
Provision for losses	7	(23)
Charge-offs	(11)	(9)
Recoveries	5	11
Transfers		(1)
Balance at the end of period	\$ 56	\$ 62

Note 6. Inventories

Inventories are composed of the following:

	September 27, 2014	December 28, 2013
<i>(In millions)</i>		
Finished goods	\$ 1,646	\$ 1,276
Work in process	2,791	2,477
Raw materials and components	555	407
Progress/milestone payments	4,992	4,160
	(911)	(1,197)

Total	\$ 4,081	\$ 2,963
-------	----------	----------

Note 7. Accrued Liabilities

We provide limited warranty and product maintenance programs, including parts and labor, for certain products for periods ranging from one to five years. Changes in our warranty and product maintenance liabilities are as follows:

<i>(In millions)</i>	Nine Months Ended	
	September 27, 2014	September 28, 2013
Accrual at the beginning of period	\$ 223	\$ 222
Provision	240	203
Settlements	(240)	(210)
Acquisitions	65	
Adjustments*	(8)	(3)
Accrual at the end of period	\$ 280	\$ 212

* Adjustments include changes to prior year estimates, new issues on prior year sales and currency translation adjustments.

Table of Contents**Note 8. Debt**

On January 24, 2014, we entered into a five-year term loan agreement with a syndicate of banks in the principal amount of \$500 million. On January 30, 2014, we issued \$250 million in 3.65% notes due 2021 and \$350 million in 4.30% notes due 2024 under our shelf registration statement. Upon the closing of the Beechcraft acquisition on March 14, 2014, we fully drew down on the five-year term loan and used the cash, along with the net proceeds of the issuance of the notes, to finance a portion of the acquisition. During the third quarter of 2014, we repaid \$200 million of the five-year term loan.

Note 9. Accumulated Other Comprehensive Loss and Other Comprehensive Income

The components of Accumulated Other Comprehensive Loss are presented below:

<i>(In millions)</i>	Foreign Currency Translation Adjustments	Pension and Postretirement Benefits Adjustments	Deferred Gains/Losses on Hedge Contracts	Accumulated Other Comprehensive Loss
For the nine months ended September 27, 2014				
Beginning balance	\$ 93	\$ (1,110)	\$ (10)	\$ (1,027)
Other comprehensive income (loss) before reclassifications	(47)	9	(4)	(42)
Amounts reclassified from Accumulated Other Comprehensive Loss		53	6	59
Other comprehensive income (loss)	(47)	62	2	17
Ending balance	\$ 46	\$ (1,048)	\$ (8)	\$ (1,010)
For the nine months ended September 28, 2013				
Beginning balance	\$ 81	\$ (1,857)	\$ 6	\$ (1,770)
Other comprehensive income (loss) before reclassifications	3		(9)	(6)
Amounts reclassified from Accumulated Other Comprehensive Loss		127	(2)	125
Other comprehensive income (loss)	3	127	(11)	119
Ending balance	\$ 84	\$ (1,730)	\$ (5)	\$ (1,651)

Table of Contents

The before and after-tax components of Other Comprehensive Income are presented below:

<i>(In millions)</i>	Pre-Tax Amount	Tax (Expense) Benefit	After-Tax Amount
For the three months ended September 27, 2014			
Pension and postretirement benefits adjustments:			
Amortization of net actuarial loss*	\$ 28	\$ (10)	\$ 18
Amortization of prior service credit*	(2)	1	(1)
Pension and postretirement benefits adjustments, net	26	(9)	17
Deferred gains/losses on hedge contracts:			
Current deferrals	(9)	3	(6)
Reclassification adjustments	2	(1)	1
Deferred gains/losses on hedge contracts, net	(7)	2	(5)
Foreign currency translation adjustments	(39)	(4)	(43)
Total	\$ (20)	\$ (11)	\$ (31)
For the three months ended September 28, 2013			
Pension and postretirement benefits adjustments:			
Amortization of net actuarial loss*	\$ 48	\$ (18)	\$ 30
Amortization of prior service credit*	(2)	1	(1)
Amendment to postretirement benefit plan	55	(20)	35
Pension and postretirement benefits adjustments, net	101	(37)	64
Deferred gains/losses on hedge contracts:			
Current deferrals	3	(1)	2
Deferred gains/losses on hedge contracts, net	3	(1)	2
Foreign currency translation adjustments	8	4	12
Total	\$ 112	\$ (34)	\$ 78
For the nine months ended September 27, 2014			
Pension and postretirement benefits adjustments:			
Amortization of net actuarial loss*	\$ 85	\$ (30)	\$ 55
Amortization of prior service credit*	(5)	3	(2)
Amendment to postretirement benefit plan	15	(6)	9
Pension and postretirement benefits adjustments, net	95	(33)	62
Deferred gains/losses on hedge contracts:			
Current deferrals	(7)	3	(4)
Reclassification adjustments	9	(3)	6
Deferred gains/losses on hedge contracts, net	2		2
Foreign currency translation adjustments	(46)	(1)	(47)
Total	\$ 51	\$ (34)	\$ 17
For the nine months ended September 28, 2013			
Pension and postretirement benefits adjustments:			
Amortization of net actuarial loss*	\$ 143	\$ (51)	\$ 92
Amendment to postretirement benefit plan	55	(20)	35
Pension and postretirement benefits adjustments, net	198	(71)	127
Deferred gains/losses on hedge contracts:			
Current deferrals	(11)	2	(9)
Reclassification adjustments	(3)	1	(2)
Deferred gains/losses on hedge contracts, net	(14)	3	(11)
Foreign currency translation adjustments	6	(3)	3
Total	\$ 190	\$ (71)	\$ 119

*These components of other comprehensive income are included in the computation of net periodic pension cost. See Note 11 of our 2013 Annual Report on Form 10-K for additional information.

Table of Contents

Note 10. Commitments and Contingencies

We are subject to legal proceedings and other claims arising out of the conduct of our business, including proceedings and claims relating to commercial and financial transactions; government contracts; alleged lack of compliance with applicable laws and regulations; production partners; product liability; patent and trademark infringement; employment disputes; and environmental, safety and health matters. Some of these legal proceedings and claims seek damages, fines or penalties in substantial amounts or remediation of environmental contamination. As a government contractor, we are subject to audits, reviews and investigations to determine whether our operations are being conducted in accordance with applicable regulatory requirements. Under federal government procurement regulations, certain claims brought by the U.S. Government could result in our suspension or debarment from U.S. Government contracting for a period of time. On the basis of information presently available, we do not believe that existing proceedings and claims will have a material effect on our financial position or results of operations.

Note 11. Derivative Instruments and Fair Value Measurements

We measure fair value at 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. We prioritize the assumptions that market participants would use in pricing the asset or liability into a three-tier fair value hierarchy. This fair value hierarchy gives the highest priority (Level 1) to quoted prices in active markets for identical assets or liabilities and the lowest priority (Level 3) to unobservable inputs in which little or no market data exist, requiring companies to develop their own assumptions. Observable inputs that do not meet the criteria of Level 1, which include quoted prices for similar assets or liabilities in active markets or quoted prices for identical assets and liabilities in markets that are not active, are categorized as Level 2. Level 3 inputs are those that reflect our estimates about the assumptions market participants would use in pricing the asset or liability based on the best information available in the circumstances. Valuation techniques for assets and liabilities measured using Level 3 inputs may include methodologies such as the market approach, the income approach or the cost approach and may use unobservable inputs such as projections, estimates and management's interpretation of current market data. These unobservable inputs are utilized only to the extent that observable inputs are not available or cost effective to obtain.

Assets and Liabilities Recorded at Fair Value on a Recurring Basis

We manufacture and sell our products in a number of countries throughout the world, and, therefore, we are exposed to movements in foreign currency exchange rates. We utilize foreign currency exchange contracts to manage this volatility. Our foreign currency exchange contracts are measured at fair value using the market method valuation technique. The inputs to this technique utilize current foreign currency exchange forward market rates published by third-party leading financial news and data providers. These are observable data that represent the rates that the financial institution uses for contracts entered into at that date; however, they are not based on actual transactions so they are classified as Level 2. At September 27, 2014 and December 28, 2013, we had foreign currency exchange contracts with notional amounts upon which the contracts were based of \$753 million and \$636 million, respectively. At September 27, 2014, the fair value amounts of our foreign currency exchange contracts were a \$7 million asset and a \$15 million liability. At December 28, 2013, the fair value amounts of our foreign currency exchange contracts were a \$2 million asset and a \$15 million liability.

We primarily utilize forward exchange contracts which have maturities of no more than three years. These contracts qualify as cash flow hedges and are intended to offset the effect of exchange rate fluctuations on forecasted sales, inventory purchases and overhead expenses. At September 27, 2014, we had a net deferred loss of \$8 million in Accumulated other comprehensive loss related to these cash flow hedges. Net gains and losses recognized in earnings and Accumulated other comprehensive loss on cash flow hedges, including gains and losses related to hedge ineffectiveness, were not significant in the periods presented.

We hedge our net investment position in major currencies and generate foreign currency interest payments that offset other transactional exposures in these currencies. To accomplish this, we borrow directly in foreign currency and designate a portion of foreign currency debt as a hedge of a net investment. We record changes in the fair value of these contracts in other comprehensive income to the extent they are effective as cash flow hedges. Currency effects on the effective portion of these hedges, which are reflected in the foreign currency translation adjustments within Accumulated other comprehensive loss, were not significant in the periods presented.

Our Finance group has entered into interest rate exchange contracts to mitigate exposure to changes in the fair value of its fixed-rate receivables and debt due to fluctuations in interest rates. These interest rate exchange contracts are not exchange traded and are measured at fair value utilizing widely accepted, third-party developed valuation models. The actual terms of each individual contract are entered into a valuation model, along with interest rate data, which is based on readily observable market data published by third-party leading financial news and data providers. At September 27, 2014 and December 28, 2013, we had interest rate exchange contracts with notional amounts upon which the contracts were based of \$162 million and \$229 million, respectively. The fair value amounts of our interest rate exchange contracts were a \$1 million asset and a \$3 million liability at September 27, 2014. At December 28, 2013, the fair value amounts of our interest rate exchange contracts were a \$2 million asset and \$5 million liability.

Table of Contents

Our exposure to loss from nonperformance by the counterparties to our derivative agreements at September 27, 2014 was minimal. We do not anticipate nonperformance by counterparties in the periodic settlements of amounts due. We historically have minimized this potential for risk by entering into contracts exclusively with major, financially sound counterparties having no less than a long-term bond rating of A. The credit risk generally is limited to the amount by which the counterparties' contractual obligations exceed our obligations to the counterparty. We continuously monitor our exposures to ensure that we limit our risks.

Assets Recorded at Fair Value on a Nonrecurring Basis

During the periods ended September 27, 2014 and December 28, 2013, the Finance group's impaired nonaccrual finance receivables of \$55 million and \$45 million, respectively, were measured at fair value on a nonrecurring basis using significant unobservable inputs (Level 3). Impaired nonaccrual finance receivables represent assets recorded at fair value on a nonrecurring basis since the measurement of required reserves on our impaired finance receivables is significantly dependent on the fair value of the underlying collateral. For impaired nonaccrual finance receivables secured by aviation assets, the fair values of collateral are determined primarily based on the use of industry pricing guides. Fair value measurements recorded on impaired finance receivables resulted in charges to provision for loan losses totaling \$5 million and \$16 million for the three and nine months ended September 27, 2014, respectively, and \$3 million and \$8 million for the three and nine months ended September 27, 2013, respectively.

Assets and Liabilities Not Recorded at Fair Value

The carrying value and estimated fair values of our financial instruments that are not reflected in the financial statements at fair value are as follows:

	September 27, 2014		December 28, 2013	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
<i>(In millions)</i>				
Manufacturing group				
Long-term debt, excluding leases	\$ (2,760)	\$ (2,959)	\$ (1,854)	\$ (2,027)
Finance group				
Finance receivables held for investment, excluding leases	1,072	1,102	1,231	1,290
Debt	(1,111)	(1,112)	(1,256)	(1,244)

Fair value for the Manufacturing group debt is determined using market observable data for similar transactions (Level 2). At September 27, 2014 and December 28, 2013, approximately 76% and 70%, respectively, of the fair value of term debt for the Finance group was determined based on discounted cash flow analyses using observable market inputs from debt with similar duration, subordination and credit default expectations (Level 2). The remaining Finance group debt was determined based on observable market transactions (Level 1). Fair value estimates for finance receivables held for investment were determined based on internally developed discounted cash flow models primarily utilizing significant unobservable inputs (Level 3), which include estimates of the rate of return, financing cost, capital structure and/or discount rate expectations of current market participants combined with estimated loan cash flows based on credit losses, payment rates and expectations of borrowers' ability to make payments on a timely basis.

Note 12. Income Tax Expense

Edgar Filing: TEXTRON INC - Form 10-Q

Income tax expense equated to an effective income tax rate of 30.7% for both the three and nine months ended September 27, 2014, compared with the U.S. federal statutory income tax rate of 35.0%. The difference between the statutory and the effective income tax rate was primarily due to benefits from income attributable to international operations in countries with lower tax rates.

Income tax expense equated to an effective income tax rate of 32.4% and 27.5% for the three and nine months ended September 28, 2013, respectively, compared with the U.S. federal statutory income tax rate of 35.0%. For the nine months ended September 28, 2013, the difference between the statutory and the effective income tax rate was primarily due to benefits from income attributable to international operations in countries with lower tax rates and a favorable impact of four percentage points, resulting from the retroactive reinstatement and extension of the Federal Research and Development Tax Credit as part of the American Taxpayer Relief Act of 2012 enacted on January 2, 2013.

Table of Contents**Note 13. Segment Information**

We operate in, and report financial information for, the following five business segments: Bell, Textron Systems, Industrial, Finance and the recently formed Textron Aviation segment as discussed in Note 1.

Segment profit is an important measure used for evaluating performance and for decision-making purposes. Segment profit for the manufacturing segments excludes interest expense, certain corporate expenses and acquisition and restructuring costs related to the Beechcraft acquisition. The measurement for the Finance segment includes interest income and expense along with intercompany interest expense. Our revenues by segment and a reconciliation of segment profit to income from continuing operations before income taxes are as follows:

<i>(In millions)</i>	Three Months Ended		Nine Months Ended	
	September 27, 2014	September 28, 2013	September 27, 2014	September 28, 2013
REVENUES				
<i>Manufacturing group</i>				
Textron Aviation	\$ 1,080	\$ 593	\$ 3,048	\$ 1,861
Bell	1,182	1,162	3,174	3,136
Textron Systems	358	405	1,003	1,256
Industrial	785	711	2,476	2,239
	3,405	2,871	9,701	8,492
Finance segment	25	33	81	106
Total revenues	\$ 3,430	\$ 2,904	\$ 9,782	\$ 8,598
SEGMENT PROFIT				
<i>Manufacturing Group</i>				
Textron Aviation	\$ 62	\$ (23)	\$ 104	\$ (81)
Bell	146	131	383	395
Textron Systems	27	35	100	107
Industrial	53	52	213	188
	288	195	800	609
Finance segment	5	13	16	47
Segment profit	293	208	816	656
Corporate expenses and other, net	(22)	(34)	(103)	(109)
Interest expense, net for Manufacturing group	(37)	(29)	(108)	(96)
Acquisition and restructuring costs	(3)		(39)	
Income from continuing operations before income taxes	\$ 231	\$ 145	\$ 566	\$ 451

Table of Contents**Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS****Overview and Consolidated Results of Operations**

On March 14, 2014, we completed the acquisition of Beech Holdings, LLC, which included Beechcraft Corporation and other subsidiaries, (collectively Beechcraft). The acquired Beechcraft business and the legacy Cessna segment were combined to form a new segment named Textron Aviation. The results of Beechcraft have been included in Textron's consolidated financial statements only for the period subsequent to the completion of the acquisition. As a result, the consolidated financial results for the nine months ended September 27, 2014 do not reflect a full nine months of Beechcraft operations.

An analysis of our consolidated operating results is set forth below. A more detailed analysis of our segments' operating results is provided in the Segment Analysis section on pages 22 to 27.

Revenues

	Three Months Ended		Nine Months Ended	
	September 27, 2014	September 28, 2013	September 27, 2014	September 28, 2013
<i>(Dollars in millions)</i>				
Revenues	\$ 3,430	\$ 2,904	\$ 9,782	\$ 8,598
<i>% change compared with prior period</i>	18%		14%	

Revenues increased \$526 million, 18%, in the third quarter of 2014, compared with the corresponding period of 2013, as revenue increases in the Textron Aviation, Industrial and Bell segments were partially offset by lower revenues in the Textron Systems and Finance segments. The net revenue increase included the following factors:

- Higher Textron Aviation revenues of \$487 million, primarily due to a \$398 million impact from the Beechcraft acquisition and \$80 million in higher volume, largely resulting from higher Citation jet volume.
- Higher Industrial segment revenues of \$74 million, primarily due to a \$39 million impact from acquisitions and \$36 million in higher volume, largely in the Fuel Systems and Functional Components product line.
- Higher Bell revenues of \$20 million, primarily reflecting a \$158 million increase in V-22 program volume due to an increase in deliveries and higher product support and other volume, partially offset by lower other military and commercial volume primarily reflecting lower aircraft deliveries.
- Lower Textron Systems revenues of \$47 million, primarily due to lower volume, principally reflecting lower vehicle deliveries in the Marine and Land Systems product line.

Edgar Filing: TEXTRON INC - Form 10-Q

- Lower Finance revenues of \$8 million, primarily attributable to gains on the disposition of finance receivables held for sale during 2013.

Revenues increased \$1,184 million, 14%, in the first nine months of 2014, compared with the corresponding period of 2013, as revenue increases in the Textron Aviation, Industrial and Bell segments were partially offset by lower revenues in the Textron Systems and Finance segments. The net revenue increase included the following factors:

- Higher Textron Aviation revenues of \$1.2 billion, primarily due to a \$924 million impact from the Beechcraft acquisition and \$233 million in higher volume, largely resulting from higher Citation jet volume.
- Higher Industrial segment revenues of \$237 million, primarily due to \$113 million in higher volume, largely in the Fuel Systems and Functional Components product line, and a \$97 million impact from acquisitions.
- Higher Bell revenues of \$38 million, primarily due to a \$208 million increase related to the V-22 program reflecting product support and other volume, partially offset by lower commercial and other military volume primarily reflecting lower aircraft deliveries. The decrease in other military volume was partially offset by \$41 million related to the settlement of the System Development and Demonstration (SDD) phase of the Armed Reconnaissance Helicopter (ARH) program, which was terminated in October 2008.
- Lower Textron Systems revenues of \$253 million, largely due to lower volume in the Marine and Land Systems product line of \$172 million, reflecting lower vehicle deliveries, and in the UAS product line of \$103 million, reflecting the timing of deliveries.
- Lower Finance revenues of \$25 million, primarily attributable to gains on the disposition of finance receivables held for sale during 2013.

Table of Contents**Cost of Sales and Selling and Administrative Expense**

	Three Months Ended		Nine Months Ended	
	September 27, 2014	September 28, 2013	September 27, 2014	September 28, 2013
<i>(Dollars in millions)</i>				
Operating expenses	\$ 3,149	\$ 2,718	\$ 9,036	\$ 8,013
Cost of sales	2,845	2,473	8,077	7,193
<i>% change compared with prior period</i>	15%		12%	
<i>Gross margin percentage of Manufacturing revenues</i>	16.4%	13.9%	16.7%	15.3%
Selling and administrative expenses	\$ 304	\$ 245	\$ 959	\$ 820
<i>% change compared with prior period</i>	24%		17%	

Manufacturing cost of sales and selling and administrative expenses together comprise our operating expenses. Cost of sales increased \$372 million, 15%, in the third quarter of 2014, and \$884 million, 12%, in the first nine months of 2014, compared with the corresponding periods of 2013, largely due to the impact of acquired businesses, primarily Beechcraft. In the third quarter and first nine months of 2014, gross margin increased as a percentage of Manufacturing revenues largely due to improved leverage resulting from higher revenues primarily in the Textron Aviation segment.

Selling and administrative expense increased \$59 million, 24%, and \$139 million, 17%, in the third quarter and first nine months of 2014, respectively, compared with the corresponding periods of 2013, largely related to businesses acquired in the past year and compensation expense. In addition, the increase in the first nine months of 2014 was partially offset by \$28 million in severance costs incurred in 2013 in connection with a voluntary separation program in the legacy Cessna segment.

Acquisition and Restructuring Costs

In the third quarter and first nine months of 2014, we incurred \$3 million and \$39 million, respectively, in acquisition and restructuring costs related to the Beechcraft acquisition. These costs included severance costs of \$3 million and \$28 million, respectively, resulting from a restructuring program described below and transaction costs of \$11 million incurred during the first quarter of 2014, primarily related to advisory services. Acquisition and restructuring costs are not included in segment profit.

In connection with the integration of Beechcraft, we initiated a restructuring program in our Textron Aviation segment in the first quarter of 2014 to align the Cessna and Beechcraft businesses, reduce operating redundancies and maximize efficiencies. We expect to incur costs for this program related to employee terminations, facility consolidations, contract terminations and other transition-related costs, and estimate that this program will result in charges of approximately \$35 million in 2014. We expect to incur additional costs in 2015, but do not expect these costs to be material.

Interest Expense

	Three Months Ended		Nine Months Ended	
	September 27, 2014	September 28, 2013	September 27, 2014	September 28, 2013
<i>(Dollars in millions)</i>				
Interest expense	\$ 47	\$ 41	\$ 141	\$ 134

Edgar Filing: TEXTRON INC - Form 10-Q

% change compared with prior period

15%

5%

Interest expense on the Consolidated Statement of Operations includes interest for both the Finance and Manufacturing borrowing groups with interest related to intercompany borrowings eliminated. Interest expense for the Finance segment is included within segment profit and includes intercompany interest.

Consolidated interest expense increased \$6 million, 15%, and \$7 million, 5%, in the third quarter and first nine months of 2014, respectively, compared with the corresponding periods of 2013, primarily due to higher average debt outstanding related to the Beechcraft acquisition financing. The increase in interest expense for the first nine months of 2014 was partially offset by the maturity of our convertible notes in the second quarter of 2013.

Income Taxes

Income tax expense equated to an effective income tax rate of 30.7% for both the third quarter and first nine months of 2014 compared with the U.S. federal statutory income tax rate of 35.0%. The difference between the statutory and the effective income tax rate was primarily due to benefits from income attributable to international operations in countries with lower tax rates.

Table of Contents

Income tax expense equated to an effective income tax rate of 32.4% and 27.5% in the third quarter and first nine months of 2013, respectively, compared with the U.S. federal statutory income tax rate of 35.0%. In the first nine months of 2013, the difference between the statutory and the effective income tax rate was primarily due to benefits from income attributable to international operations in countries with lower tax rates and a favorable impact of four percentage points, resulting from the retroactive reinstatement and extension of the Federal Research and Development Tax Credit as part of the American Taxpayer Relief Act of 2012 enacted on January 2, 2013.

Backlog

<i>(In millions)</i>	September 27, 2014	December 28, 2013
Bell	\$ 5,332	\$ 6,450
Textron Systems	3,126	2,803
Textron Aviation	1,358	1,018

Backlog at the Bell segment decreased \$1.1 billion primarily due to V-22 helicopter deliveries. The increase in backlog of \$340 million at the Textron Aviation segment was primarily the result of the Beechcraft acquisition.

Segment Analysis

We operate in, and report financial information for, the following five business segments: Textron Aviation, which consists of the legacy Cessna segment combined with the newly-acquired Beechcraft business, Bell, Textron Systems, Industrial and Finance. Segment profit is an important measure used for evaluating performance and for decision-making purposes. Segment profit for the manufacturing segments excludes interest expense, certain corporate expenses and acquisition and restructuring costs related to the Beechcraft acquisition. The measurement for the Finance segment includes interest income and expense along with intercompany interest expense.

In our discussion of comparative results for the Manufacturing group, changes in revenue and segment profit typically are expressed for our commercial business in terms of volume, pricing, foreign exchange and acquisitions. Additionally, changes in segment profit may be expressed in terms of mix, inflation and cost performance. Volume changes in revenue represent increases/decreases in the number of units delivered or services provided. Pricing represents changes in unit pricing. Foreign exchange is the change resulting from translating foreign-denominated amounts into U.S. dollars at exchange rates that are different from the prior period. Acquisitions refers to the revenues generated from businesses that were acquired within the previous 12 months. For segment profit, mix represents a change due to the composition of products and/or services sold at different profit margins. Inflation represents higher material, wages, benefits, pension or other costs. Performance reflects an increase or decrease in research and development, depreciation, selling and administrative costs, warranty, product liability, quality/scrub, labor efficiency, overhead, product line profitability, start-up, ramp up and cost-reduction initiatives or other manufacturing inputs.

Approximately 30% of our 2013 full year revenues were derived from contracts with the U.S. Government. For our segments that have significant contracts with the U.S. Government, we typically express changes in segment profit related to the government business in terms of volume, changes in program performance or changes in contract mix. Changes in volume that are discussed in net sales typically drive corresponding changes in our segment profit based on the profit rate for a particular contract. Changes in program performance typically relate to profit recognition associated with revisions to total estimated costs at completion that reflect improved or deteriorated operating performance or award fee rates. Changes in contract mix refers to changes in operating margin due to a change in the relative volume of contracts with higher

Edgar Filing: TEXTRON INC - Form 10-Q

or lower fee rates such that the overall average margin rate for the segment changes.

Textron Aviation

<i>(Dollars in millions)</i>	Three Months Ended		Nine Months Ended	
	September 27, 2014	September 28, 2013	September 27, 2014	September 28, 2013
Revenues	\$ 1,080	\$ 593	\$ 3,048	\$ 1,861
Operating expenses	1,018	616	2,944	1,942
Segment profit (loss)	62	(23)	104	(81)
Profit margin	5.7%	(3.9)%	3.4%	(4.4)%

Table of Contents

Textron Aviation Revenues and Operating Expenses

The following factors contributed to the change in Textron Aviation's revenues for the periods:

<i>(In millions)</i>	Q3 2014 versus Q3 2013	YTD 2014 versus YTD 2013
Acquisition	\$ 398	\$ 924
Volume	80	233
Pricing	9	30
Total change	\$ 487	\$ 1,187

In the third quarter of 2014, Textron Aviation's revenues increased \$487 million, 82%, compared with the corresponding period of 2013, primarily due to the impact of the Beechcraft acquisition of \$398 million and higher volume of \$80 million. The higher volume was primarily the result of higher Citation jet volume of \$99 million partially offset by lower CitationAir volume of \$18 million, related to exiting our fractional share business. We delivered 33 Citation jets and 30 King Air turboprops in the third quarter of 2014, compared with 25 Citation jets in the third quarter of 2013. During the third quarter of 2014, the portion of the segment's revenues derived from aftermarket sales and services represented 35% of its total revenues, compared with 41% in the third quarter of 2013.

In the first nine months of 2014, Textron Aviation's revenues increased by \$1.2 billion, 64%, compared with the corresponding period of 2013, primarily due to the impact of the Beechcraft acquisition of \$924 million and higher volume of \$233 million. The higher volume was primarily the result of higher Citation jet volume of \$329 million, partially offset by lower CitationAir volume of \$62 million related to exiting our fractional share business and lower pre-owned aircraft volume of \$39 million. We delivered 104 Citation jets and 72 King Air turboprops in the first nine months of 2014, compared with 77 Citation jets in the first nine months of 2013. During the first nine months of 2014, the portion of the segment's revenues derived from aftermarket sales and services represented 33% of its total revenues, compared with 37% in the first nine months of 2013.

Textron Aviation's operating expenses increased by \$402 million, 65%, and by \$1.0 billion, 52%, in the third quarter and first nine months of 2014, respectively, compared with the corresponding periods of 2013, primarily due to the incremental operating costs related to the Beechcraft acquisition, and higher net sales volume as described above. Textron Aviation's operating expenses exclude acquisition and restructuring costs incurred across the segment as a result of the Beechcraft integration, which are reported separately and are discussed in the Acquisition and Restructuring Costs section above.

Textron Aviation Segment Profit

The following factors contributed to the change in Textron Aviation's segment profit for the periods:

<i>(In millions)</i>	Q3 2014 versus Q3 2013	YTD 2014 versus YTD 2013
Volume	\$ 29	\$ 73
Performance and other	39	46
Pricing and inflation	17	38

Edgar Filing: TEXTRON INC - Form 10-Q

2013 Voluntary Separation Program				28
Total change	\$	85	\$	185

Textron Aviation segment profit increased \$85 million in the third quarter and \$185 million in the first nine months of 2014, compared with the corresponding periods of 2013, primarily due to an increase in Performance and other, higher volume as described above, and favorable pricing and inflation. The increase in segment profit in the first nine months of 2014 also resulted from \$28 million in severance costs incurred in 2013 in connection with a voluntary separation program. During the second quarter of 2014 the cost structures of Beechcraft and Cessna were significantly integrated, and as a result, Performance and other reflects the net profit impact of Beechcraft, including the benefit of the integrated cost structure. Performance and other also includes amortization of \$10 million and \$55 million in the third quarter and first nine months of 2014, respectively, related to fair value step-up adjustments of acquired inventories sold during the periods.

Table of Contents**Bell**

	Three Months Ended		Nine Months Ended	
	September 27, 2014	September 28, 2013	September 27, 2014	September 28, 2013
<i>(Dollars in millions)</i>				
Revenues:				
V-22 program	\$ 600	\$ 442	\$ 1,425	\$ 1,218
Other military	164	254	647	720
Commercial	418	466	1,102	1,198
Total revenues	1,182	1,162	3,174	3,136
Operating expenses	1,036	1,031	2,791	2,741
Segment profit	146	131	383	395
Profit margin	12.4%	11.3%	12.1%	12.6%

Bell manufactures helicopters, tiltrotor aircraft, and related spare parts and provides services for military and commercial markets. Bell's major U.S. Government programs at this time are the V-22 tiltrotor aircraft and the H-1 helicopter platforms, which are both in the production stage and represent a significant portion of Bell's revenues from the U.S. Government.

Bell Revenues and Operating Expenses

The following factors contributed to the change in Bell's revenues for the periods:

	Q3 2014 versus Q3 2013	YTD 2014 versus YTD 2013
<i>(In millions)</i>		
Volume and mix	\$ 13	\$ 11
Other	7	27
Total change	\$ 20	\$ 38

Bell's revenues increased \$20 million, 2%, in the third quarter of 2014, compared with the corresponding period of 2013, primarily due to higher volume, which included the following factors:

- \$158 million increase in V-22 program volume, reflecting higher aircraft deliveries and \$79 million in higher product support and other volume. Bell delivered 12 V-22 aircraft in the third quarter of 2014, compared with 10 aircraft in the third quarter of 2013.
- \$90 million decrease in other military volume, primarily reflecting lower H-1 aircraft deliveries as we delivered 4 aircraft in the third quarter of 2014, compared with 7 aircraft in the third quarter of 2013.
- \$48 million decrease in commercial revenue, largely related to lower aircraft deliveries. Bell delivered 41 commercial aircraft in the third quarter of 2014, compared with 54 commercial aircraft in the third quarter of 2013.

Edgar Filing: TEXTRON INC - Form 10-Q

Bell's revenues increased \$38 million, 1%, in the first nine months of 2014, compared with the corresponding period 2013, primarily due to the following factors:

- \$208 million increase in V-22 program revenue, reflecting higher product support and other volume of \$107 million and higher aircraft deliveries. Bell delivered 30 V-22 aircraft in the first nine months of 2014 compared to 28 V-22 aircraft in the first nine months of 2013.
- \$96 million decrease in commercial revenue, largely related to lower volumes reflecting lower sales activity across the market. Bell delivered 121 commercial aircraft in the first nine months of 2014, compared with 138 commercial aircraft in the first nine months of 2013.
- \$73 million decrease in other military volume, primarily related to the H-1 program, largely reflecting lower aircraft deliveries. This decrease was partially offset by \$41 million recorded in the second quarter of 2014, related to the settlement of the SDD phase of the ARH program, which was terminated in October 2008. Bell delivered 17 H-1 aircraft in the first nine months of 2014, compared with 19 aircraft in the first nine months of 2013.

Bell's operating expenses increased \$5 million and \$50 million, in the third quarter and first nine months of 2014, respectively, compared with the corresponding periods of 2013, primarily due to higher net sales volume as discussed above.

Table of Contents**Bell Segment Profit**

The following factors contributed to the change in Bell's segment profit for the periods:

<i>(In millions)</i>		Q3 2014 versus Q3 2013		YTD 2014 versus YTD 2013
Volume and mix	\$	(9)	\$	(28)
Performance		24		8
Other				8
Total change	\$	15	\$	(12)

Bell's segment profit increased \$15 million, 11%, in the third quarter of 2014, compared with the corresponding period of 2013, primarily due to favorable performance. Favorable performance resulted from our cost reduction activities in 2014 as well as unfavorable performance in 2013, when we experienced manufacturing inefficiencies associated with labor disruptions resulting from negotiations with bargained employees as well as the implementation of a new enterprise resource planning system.

Bell's segment profit decreased \$12 million, 3%, in the first nine months of 2014, compared with the corresponding period of 2013. The impact of volume and mix was largely driven by lower commercial volume and an unfavorable mix of commercial aircraft deliveries, partially offset by a \$16 million favorable program profit adjustment related to the ARH program as described above. Favorable performance primarily reflected our cost reduction activities in 2014 as well as unfavorable performance in 2013 as described above.

Textron Systems

<i>(Dollars in millions)</i>	Three Months Ended		Nine Months Ended	
	September 27, 2014	September 28, 2013	September 27, 2014	September 28, 2013
Revenues	\$ 358	\$ 405	\$ 1,003	\$ 1,256
Operating expenses	331	370	903	1,149
Segment profit	27	35	100	107
Profit margin	7.5%	8.6%	10.0%	8.5%

Textron Systems Revenues and Operating Expenses

The following factors contributed to the change in Textron Systems' revenues for the periods:

<i>(In millions)</i>		Q3 2014 versus Q3 2013		YTD 2014 versus YTD 2013
Volume	\$	(66)	\$	(286)
Acquisitions		18		31
Other		1		2

Edgar Filing: TEXTRON INC - Form 10-Q

Total change	\$	(47)	\$	(253)
--------------	----	------	----	-------

Revenues at Textron Systems decreased \$47 million, 12%, in the third quarter of 2014, compared with the corresponding period of 2013, primarily due to lower volume, principally reflecting lower vehicle deliveries in the Marine and Land Systems product line.

Revenues at Textron Systems decreased \$253 million, 20%, in the first nine months of 2014, compared with the corresponding period of 2013, primarily due to lower volume in the Marine and Land Systems product line of \$172 million, reflecting lower vehicle deliveries, and the UAS product line of \$103 million, due to the timing of deliveries during the year.

Textron Systems operating expenses decreased \$39 million, 11%, and \$246 million, 21%, in the third quarter and first nine months of 2014, respectively, compared with the corresponding periods of 2013, primarily due to lower sales volume as discussed above.

Table of Contents

Textron Systems Segment Profit

The following factors contributed to the change in Textron Systems segment profit for the periods:

<i>(In millions)</i>		Q3 2014 versus Q3 2013	YTD 2014 versus YTD 2013
Performance	\$	(3)	\$ 24
Volume		(4)	(23)
Other		(1)	(8)
Total change	\$	(8)	\$ (7)

Segment profit decreased \$8 million in the third quarter of 2014, compared with the corresponding period of 2013, primarily driven by the lower volume described above.

Segment profit at Textron Systems decreased \$7 million in the first nine months of 2014, compared with the corresponding period of 2013, primarily driven by \$24 million of improved performance offset by \$23 million in lower volume described above.

Industrial

<i>(Dollars in millions)</i>	Three Months Ended		Nine Months Ended	
	September 27, 2014	September 28, 2013	September 27, 2014	September 28, 2013
Revenues:				
Fuel Systems and Functional Components	\$ 459	\$ 442	\$ 1,462	\$ 1,373
Other Industrial	326	269	1,014	866
Total revenues	785	711	2,476	2,239
Operating expenses	732	659	2,263	2,051
Segment profit	53	52	213	188
Profit margin	6.8%	7.3%	8.6%	8.4%

Industrial Revenues and Operating Expenses

The following factors contributed to the change in Industrial revenues for the periods:

<i>(In millions)</i>		Q3 2014 versus Q3 2013	YTD 2014 versus YTD 2013
Volume	\$	36	\$ 113
Acquisitions		39	97
Foreign exchange		(4)	17
Other		3	10

Edgar Filing: TEXTRON INC - Form 10-Q

Total change	\$	74	\$	237
--------------	----	----	----	-----

Industrial segment revenues increased \$74 million, 10%, in the third quarter of 2014, compared with the corresponding period of 2013, primarily due to the impact of acquisitions of \$39 million and higher volume of \$36 million. Higher volume resulted from a \$23 million increase in the Fuel Systems and Functional Components product line, principally reflecting automotive industry demand in North America, and a \$13 million increase in the Other Industrial product lines.

Industrial segment revenues increased \$237 million, 11%, in the first nine months of 2014, compared with the corresponding period of 2013, primarily due to higher volume of \$113 million and the impact of acquisitions of \$97 million. Higher volume resulted from an \$88 million increase in the Fuel Systems and Functional Components product line, principally reflecting automotive industry demand in North America and Asia, and a \$25 million increase in the Other Industrial product lines.

Operating expenses for the Industrial segment increased \$73 million, 11%, and \$212 million, 10%, in the third quarter and first nine months of 2014, respectively, compared with the corresponding periods of 2013, largely due to the impact from higher sales volume discussed above and additional operating expenses from recently acquired businesses.

Table of Contents**Industrial Segment Profit**

The following factors contributed to the change in Industrial s segment profit for the periods:

<i>(In millions)</i>	Q3 2014 versus Q3 2013	YTD 2014 versus YTD 2013
Volume and mix	\$ (1)	\$ 13
Other	2	12
Total change	\$ 1	\$ 25

Segment profit for the Industrial segment increased \$1 million, 2%, in the third quarter of 2014, compared with the corresponding period of 2013. The higher volume described above did not have an impact on segment profit, primarily due to the mix of products sold in the period.

Segment profit for the Industrial segment increased \$25 million, 13%, in the first nine months of 2014, compared with the corresponding periods of 2013, largely due to the impact from higher volume as described above.

Finance

<i>(In millions)</i>	Three Months Ended		Nine Months Ended	
	September 27, 2014	September 28, 2013	September 27, 2014	September 28, 2013
Revenues	\$ 25	\$ 33	\$ 81	\$ 106
Segment profit	5	13	16	47

Finance segment revenues decreased \$8 million and \$25 million in the third quarter and first nine months of 2014, respectively, compared with the corresponding periods of 2013, primarily attributable to a \$13 million and \$30 million impact from gains on the disposition of finance receivables held for sale during 2013. These gains resulted from the payoff of loans in amounts, and sale of loans at prices, in excess of the values established in previous periods.

Finance segment profit decreased \$8 million and \$31 million in the third quarter and first nine months of 2014, respectively, compared with the corresponding periods of 2013, primarily due to a change in provision for loan losses of \$8 million and \$30 million, respectively, reflecting reserve reversals in 2013 primarily related to the non-captive business, and the impact from gains on finance receivables held for sale as discussed above. These decreases in segment profit were partially offset by lower administrative expense of \$5 million and \$15 million in the third quarter and first nine months of 2014, respectively, primarily associated with the exit of the non-captive business.

Finance Portfolio Quality

Edgar Filing: TEXTRON INC - Form 10-Q

The following table reflects information about the Finance segment's credit performance related to finance receivables that are classified as held for investment.

<i>(Dollars in millions)</i>	September 27, 2014	December 28, 2013
Finance receivables	\$ 1,329	\$ 1,483
Nonaccrual finance receivables	101	105
Ratio of nonaccrual finance receivables to finance receivables	7.60%	7.08%
60+ days contractual delinquency	\$ 70	\$ 80
60+ days contractual delinquency as a percentage of finance receivables	5.27%	5.39%

Table of Contents**Liquidity and Capital Resources**

Our financings are conducted through two separate borrowing groups. The Manufacturing group consists of Textron consolidated with its majority-owned subsidiaries that operate in the Textron Aviation, Bell, Textron Systems and Industrial segments. The Finance group, which also is the Finance segment, consists of Textron Financial Corporation and its consolidated subsidiaries. We designed this framework to enhance our borrowing power by separating the Finance group. Our Manufacturing group operations include the development, production and delivery of tangible goods and services, while our Finance group provides financial services. Due to the fundamental differences between each borrowing group's activities, investors, rating agencies and analysts use different measures to evaluate each group's performance. To support those evaluations, we present balance sheet and cash flow information for each borrowing group within the Consolidated Financial Statements.

Key information that is utilized in assessing our liquidity is summarized below:

<i>(Dollars in millions)</i>	September 27, 2014	December 28, 2013
Manufacturing group		
Cash and equivalents	\$ 430	\$ 1,163
Debt	2,857	1,931
Shareholders' equity	4,572	4,384
Capital (debt plus shareholders' equity)	7,429	6,315
Net debt (net of cash and equivalents) to capital	35%	15%
Debt to capital	38%	31%
Finance group		
Cash and equivalents	\$ 81	\$ 48
Debt	1,111	1,256

We believe that our calculations of debt to capital and net debt to capital are useful measures as they provide a summary indication of the level of debt financing (i.e., leverage) that is in place to support our capital structure, as well as to provide an indication of the capacity to add further leverage. We believe that we will have sufficient cash to meet our future needs, based on our existing cash balances, the cash we expect to generate from our manufacturing operations and other available funding alternatives, as appropriate.

We maintain an effective shelf registration statement filed with the Securities and Exchange Commission that authorizes us to issue an unlimited amount of public debt and other securities. On January 30, 2014, we issued \$250 million in 3.65% notes due 2021 and \$350 million in 4.30% notes due 2024 under this registration statement. On January 24, 2014, we also entered into a five-year term loan agreement with a syndicate of banks in the principal amount of \$500 million. Upon the closing of the Beechcraft acquisition on March 14, 2014, we fully drew down on the five-year term loan and used the cash, along with the net proceeds of the issuance of the notes, to finance a portion of the acquisition. The balance of the Beechcraft acquisition purchase price was paid from cash on hand. During the third quarter of 2014, we repaid \$200 million of the five-year term loan.

Manufacturing Group Cash Flows

Cash flows from continuing operations for the Manufacturing group as presented in our Consolidated Statements of Cash Flows are summarized below:

<i>(In millions)</i>	Nine Months Ended	
	September 27, 2014	September 28, 2013
Operating activities	\$ 491	\$ (381)
Investing activities	(1,847)	(334)
Financing activities	631	(206)

Cash flows from operating activities increased \$872 million during the first nine months of 2014, compared with the corresponding period of 2013, largely due to a favorable change in working capital, lower contributions of \$112 million to our pension plans and higher net income of \$86 million. We made pension contributions of \$61 million and \$173 million in the first nine months of 2014 and 2013, respectively. A significant factor contributing to the working capital change was an increase of \$183 million in customer deposits, primarily at Bell resulting from higher performance-based payments on certain contracts.

Table of Contents

Working capital was also favorably impacted by a \$158 million increase related to income taxes payable due to higher income tax provision and lower net tax payments, a \$123 million increase in cash from accounts receivable, largely at Bell, and a \$115 million reduction in cash used for inventories. Net tax payments were \$136 million and \$179 million in the first nine months of 2014 and 2013, respectively.

Investing cash flows in the first nine months of 2014 included a \$1.6 billion aggregate cash payment to acquire Beechcraft and several other businesses within our Industrial and Textron Systems segments. Cash flows from investing activities also included capital expenditures of \$255 million and \$300 million in the first nine months of 2014 and 2013, respectively.

In the first nine months of 2014, financing activities included proceeds of \$1.1 billion from long-term debt, which was used to finance a portion of the Beechcraft acquisition, partially offset by the repayment of \$201 million of outstanding debt. Financing activities in the first nine months of 2013 primarily consisted of the repayment of \$527 million of outstanding debt, including the settlement of our convertible notes, which was partially offset by proceeds of \$246 million from the issuance of long-term debt and commercial paper.

Share Repurchases

In the third quarter of 2014, under a 2013 share repurchase authorization, we repurchased an aggregate of 4.1 million shares of our outstanding common stock for \$152 million. In addition, in the first quarter of 2014, we repurchased 4.3 million shares of our outstanding common stock from a counterparty for \$150 million under an accelerated share repurchase agreement as disclosed in Note 4 to the Consolidated Financial Statements.

Finance Group Cash Flows

Cash flows from continuing operations for the Finance group as presented in our Consolidated Statements of Cash Flows are summarized below:

<i>(In millions)</i>	Nine Months Ended	
	September 27, 2014	September 28, 2013
Operating activities	\$ (3)	\$ 24
Investing activities	203	586
Financing activities	(167)	(452)

Cash flows from operating activities decreased \$27 million during the first nine months of 2014, compared with the corresponding period of 2013, primarily due to changes in net taxes received/paid of \$52 million, partially offset by a decrease of \$21 million in cash used for accrued interest and other liabilities, largely associated with the exit of the non-captive business. Net tax payments were \$18 million in the first nine months of 2014, while net tax receipts were \$34 million in the first nine months of 2013.

Cash flows from investing activities primarily included finance receivables repaid and proceeds from sales of receivables and other finance assets totaling \$344 million and \$710 million in the first nine months of 2014 and 2013, respectively, partially offset by finance receivable originations of \$123 million and \$164 million, respectively.

Cash used for financing activities included \$261 million of payments on long-term and nonrecourse debt in the first nine months of 2014, compared with \$685 million of payments in the first nine months of 2013. These cash outflows were partially offset by proceeds from long-term debt of \$94 million and \$262 million in the first nine months of 2014 and 2013, respectively.

Consolidated Cash Flows

The consolidated cash flows from continuing operations, after elimination of activity between the borrowing groups, are summarized below:

<i>(In millions)</i>	Nine Months Ended	
	September 27, 2014	September 28, 2013
Operating activities	\$ 569	\$ (103)
Investing activities	(1,725)	(31)
Financing activities	464	(629)

Cash flows from operating activities increased \$672 million during the first nine months of 2014, compared with the corresponding period of 2013, largely due to a favorable change in working capital, lower contributions of \$112 million to our pension plans and higher net income of \$65 million. A significant factor contributing to the working capital change was an increase of \$183 million in customer deposits, primarily at Bell resulting from higher performance-based payments on certain contracts. Other favorable changes in working capital included a \$123 million increase in cash from accounts receivable, largely at Bell, and a \$73 million reduction in cash used for inventories.

Table of Contents

In the first nine months of 2014, investing activities primarily included a \$1.6 billion aggregate cash payment to acquire Beechcraft and several other businesses within our Industrial and Textron Systems segments, partially offset by the repayment of \$201 million of outstanding debt. Total cash provided by financing activities in the first nine months of 2014 included proceeds of \$1.2 billion from long-term debt, which was used primarily to finance a portion of the Beechcraft acquisition. In the first nine months of 2013, financing activities primarily consisted of the repayment of \$1.2 billion of outstanding debt, including the settlement of our convertible notes, partially offset by proceeds from long-term debt of \$412 million and the issuance of commercial paper.

Captive Financing and Other Intercompany Transactions

The Finance group finances retail purchases and leases for new and used aircraft and equipment manufactured by our Manufacturing group, otherwise known as captive financing. In the Consolidated Statements of Cash Flows, cash received from customers or from the sale of receivables is reflected as operating activities when received from third parties. However, in the cash flow information provided for the separate borrowing groups, cash flows related to captive financing activities are reflected based on the operations of each group. For example, when product is sold by our Manufacturing group to a customer and is financed by the Finance group, the origination of the finance receivable is recorded within investing activities as a cash outflow in the Finance group's statement of cash flows. Meanwhile, in the Manufacturing group's statement of cash flows, the cash received from the Finance group on the customer's behalf is recorded within operating cash flows as a cash inflow. Although cash is transferred between the two borrowing groups, there is no cash transaction reported in the consolidated cash flows at the time of the original financing. These captive financing activities, along with all significant intercompany transactions, are reclassified or eliminated from the Consolidated Statements of Cash Flows.

Reclassification and elimination adjustments included in the Consolidated Statement of Cash Flows are summarized below:

	Nine Months Ended	
	September 27, 2014	September 28, 2013
<i>(In millions)</i>		
Reclassifications from investing activities:		
Cash received from customers	\$ 230	\$ 401
Finance receivable originations for Manufacturing group inventory sales	(123)	(144)
Other	(26)	26
Total reclassifications from investing activities	81	283
Reclassifications from financing activities:		
Capital contribution paid by Manufacturing group to Finance group		1
Dividends received by Manufacturing group from Finance group		(30)
Total reclassifications from financing activities		(29)
Total reclassifications and adjustments to cash flow from operating activities	\$ 81	\$ 254

Critical Accounting Estimates

The accounting policies that we believe are most critical to the portrayal of our financial condition and results of operations are disclosed on pages 34 through 37 in our 2013 Annual Report on Form 10-K. The following section provides an update of the year-end disclosure for long-term contracts to include program profit adjustments made during the quarter.

Long-Term Contracts

Edgar Filing: TEXTRON INC - Form 10-Q

We make a substantial portion of our sales to government customers pursuant to long-term contracts. These contracts require development and delivery of products over multiple years and may contain fixed-price purchase options for additional products. We account for these long-term contracts under the percentage-of-completion method of accounting. Under this method, we estimate profit as the difference between total estimated revenues and cost of a contract. The percentage-of-completion method of accounting involves the use of various estimating techniques to project costs at completion and, in some cases, includes estimates of recoveries asserted against the customer for changes in specifications. Due to the size, length of time and nature of many of our contracts, the estimation of total contract costs and revenues through completion is complicated and subject to many variables relative to the outcome of future events over a period of several years. We are required to make numerous assumptions and estimates relating to items such as expected engineering requirements, complexity of design and related development costs, product performance, performance of subcontractors, availability and cost of materials, labor productivity and cost, overhead and capital costs, manufacturing efficiencies and the achievement of contract milestones, including product deliveries, technical requirements, or schedule.

At the outset of each contract, we estimate the initial profit booking rate. The initial profit booking rate of each contract considers risks surrounding the ability to achieve the technical requirements (for example, a newly-developed product versus a mature

Table of Contents

product), schedule (for example, the number and type of milestone events), and costs by contract requirements in the initial estimated costs at completion. Profit booking rates may increase during the performance of the contract if we successfully retire risks surrounding the technical, schedule, and costs aspects of the contract. Likewise, the profit booking rate may decrease if we are not successful in retiring the risks; and, as a result, our estimated costs at completion increase. All of the estimates are subject to change during the performance of the contract and, therefore, may affect the profit booking rate. When adjustments are required, any changes from prior estimates are recognized using the cumulative catch-up method with the impact of the change from inception-to-date recorded in the current period. The aggregate gross amount of all program profit adjustments that are included within segment profit are presented below.

	Three Months Ended		Nine Months Ended	
	September 27, 2014	September 28, 2013	September 27, 2014	September 28, 2013
<i>(In millions)</i>				
Gross favorable	\$ 25	\$ 12	\$ 90	\$ 30
Gross unfavorable	(15)	(8)	(21)	(17)
Net program profit adjustments	\$ 10	\$ 4	\$ 69	\$ 13

Forward-Looking Information

Certain statements in this Quarterly Report on Form 10-Q and other oral and written statements made by us from time to time are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements, which may describe strategies, goals, outlook or other non-historical matters, or project revenues, income, returns or other financial measures, often include words such as believe, expect, anticipate, intend, plan, estimate, guidance, project, target, potential, will, may and similar expressions intended to identify forward-looking statements. These statements are only predictions and involve known and unknown risks, uncertainties, and other factors that may cause our actual results to differ materially from those expressed or implied by such forward-looking statements. Given these uncertainties, you should not place undue reliance on these forward-looking statements. Forward-looking statements speak only as of the date on which they are made, and we undertake no obligation to update or revise any forward-looking statements. In addition to those factors described in our 2013 Annual Report on Form 10-K under RISK FACTORS, among the factors that could cause actual results to differ materially from past and projected future results are the following:

- Interruptions in the U.S. Government's ability to fund its activities and/or pay its obligations;
- Changing priorities or reductions in the U.S. Government defense budget, including those related to military operations in foreign countries;
- Our ability to perform as anticipated and to control costs under contracts with the U.S. Government;
- The U.S. Government's ability to unilaterally modify or terminate its contracts with us for the U.S. Government's convenience or for our failure to perform, to change applicable procurement and accounting policies, or, under certain circumstances, to withhold payment or suspend or debar us as a contractor eligible to receive future contract awards;
- Changes in foreign military funding priorities or budget constraints and determinations, or changes in government regulations or policies on the export and import of military and commercial products;
- Volatility in the global economy or changes in worldwide political conditions that adversely impact demand for our products;
- Volatility in interest rates or foreign exchange rates;
- Risks related to our international business, including establishing and maintaining facilities in locations around the world and relying on joint venture partners, subcontractors, suppliers, representatives, consultants and other business partners in connection with international business, including in emerging market countries;
- Our Finance segment's ability to maintain portfolio credit quality or to realize full value of receivables;
- Performance issues with key suppliers or subcontractors;
- Legislative or regulatory actions, both domestic and foreign, impacting our operations or demand for our products;
- Our ability to control costs and successfully implement various cost-reduction activities;
- The efficacy of research and development investments to develop new products or unanticipated expenses in connection with the launching of significant new products or programs;
- The timing of our new product launches or certifications of our new aircraft products;
-

Edgar Filing: TEXTRON INC - Form 10-Q

Our ability to keep pace with our competitors in the introduction of new products and upgrades with features and technologies desired by our customers;

- Increases in pension expense or employee and retiree medical benefits;
- Continued demand softness or volatility in the markets in which we do business;
- Difficulty or unanticipated expenses in connection with integrating acquired businesses; and
- The risk that anticipated synergies and opportunities as a result of acquisitions will not be realized or the risk that acquisitions do not perform as planned, including, for example, the risk that acquired businesses will not achieve revenue projections.

Table of Contents

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There has been no significant change in our exposure to market risk during the fiscal quarter ended September 27, 2014. For discussion of our exposure to market risk, refer to Item 7A. Quantitative and Qualitative Disclosures about Market Risk contained in Textron's 2013 Annual Report on Form 10-K.

Item 4. CONTROLS AND PROCEDURES

We have carried out an evaluation, under the supervision and with the participation of our management, including our Chairman, President and Chief Executive Officer (CEO) and our Executive Vice President and Chief Financial Officer (CFO), of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Act) as of the end of the fiscal quarter covered by this report. Based upon that evaluation, our CEO and CFO concluded that our disclosure controls and procedures are effective in providing reasonable assurance that (a) the information required to be disclosed by us in the reports that we file or submit under the Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and (b) such information is accumulated and communicated to our management, including our CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

There were no changes in our internal control over financial reporting that occurred during the fiscal quarter ended September 27, 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

During the first quarter of 2014, we completed the acquisition of Beech Holdings, LLC, which included Beechcraft Corporation and other subsidiaries. We are in the process of integrating this business into our system of internal control over financial reporting.

Table of Contents**PART II. OTHER INFORMATION****Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

The following provides information about our third quarter 2014 repurchases of equity securities that are registered pursuant to Section 12 of the Securities Exchange Act of 1934, as amended:

Period (shares in thousands)	Total Number of Shares Purchased(1)	Average Price Paid per Share (excluding commissions)	Total Number of Shares Purchased as part of Publicly Announced Plan(1)	Maximum Number of Shares that may yet be Purchased under the Plan(2)
June 29, 2014 - August 2, 2014	1,585	\$ 37.98	1,585	19,130
August 3, 2014 - August 30, 2014	1,500	36.78	1,500	17,630
August 31, 2014 - September 27, 2014	1,006	36.59	1,006	16,624
Total	4,091	\$ 37.20	4,091	

(1) These shares were purchased pursuant to a plan authorizing the repurchase of up to 25 million shares of Textron common stock that had been announced on January 23, 2013. This plan has no expiration date.

(2) Excludes 4.3 million shares repurchased from a counterparty in February 2014 under the Accelerated Share Repurchase agreement described in Note 4 to the Consolidated Financial Statements.

Table of Contents

Item 6. EXHIBITS

- 12.1 Computation of ratio of income to fixed charges of Textron Inc. Manufacturing Group
- 12.2 Computation of ratio of income to fixed charges of Textron Inc. including all majority-owned subsidiaries
- 31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 Certification of Chief Executive Officer Pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 Certification of Chief Financial Officer Pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 101 The following materials from Textron Inc. s Quarterly Report on Form 10-Q for the quarterly period ended September 27, 2014, formatted in XBRL (eXtensible Business Reporting Language): (i) the Consolidated Statements of Operations, (ii) the Consolidated Statements of Comprehensive Income, (iii) the Consolidated Balance Sheets, (iv) the Consolidated Statements of Cash Flows and (v) the Notes to the Consolidated Financial Statements.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

TEXTRON INC.

Date: October 24, 2014

/s/ Mark S. Bamford
Mark S. Bamford
Vice President and Corporate Controller
(principal accounting officer)

Table of Contents

LIST OF EXHIBITS

- 12.1 Computation of ratio of income to fixed charges of Textron Inc. Manufacturing Group
- 12.2 Computation of ratio of income to fixed charges of Textron Inc. including all majority-owned subsidiaries
- 31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 Certification of Chief Executive Officer Pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 Certification of Chief Financial Officer Pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 101 The following materials from Textron Inc.'s Quarterly Report on Form 10-Q for the quarterly period ended September 27, 2014, formatted in XBRL (eXtensible Business Reporting Language): (i) the Consolidated Statements of Operations, (ii) the Consolidated Statements of Comprehensive Income, (iii) the Consolidated Balance Sheets, (iv) the Consolidated Statements of Cash Flows and (v) the Notes to the Consolidated Financial Statements.