

THOMSON REUTERS STREETEVENTS

EDITED TRANSCRIPT

HRS - Q3 2013 Harris Earnings Conference Call

EVENT DATE/TIME: APRIL 30, 2013 / 12:30PM GMT

OVERVIEW:

HRS reported 3Q13 EPS of \$1.12. Expects FY13 revenues to be down 6-7% and EPS to be \$4.60-4.70.



APRIL 30, 2013 / 12:30PM, HRS - Q3 2013 Harris Earnings Conference Call

CORPORATE PARTICIPANTS

Pamela Padgett *Harris Corporation - VP IR*

Bill Brown *Harris Corporation - President & CEO*

Gary McArthur *Harris Corporation - SVP & CFO*

CONFERENCE CALL PARTICIPANTS

Carter Copeland *Barclays - Analyst*

Yair Reiner *Oppenheimer - Analyst*

Pete Skibitski *Drexel Hamilton - Analyst*

Joe Nadol *JPMorgan - Analyst*

Gautam Khanna *Cowen and Company - Analyst*

Arnin Thrustolavern *Sterne Agee - Analyst*

Chris Quilty *Raymond James - Analyst*

PRESENTATION

Operator

Good day ladies and gentlemen and welcome to the quarter three 2013 Harris earnings conference call. My name is Matthew and I will be your operator for today. At this time, all participants are in listen-only mode. We will conduct a question-and-answer session toward the end of this conference.

(Operator Instructions)

As a reminder, this call is being recorded to replay purposes. And now, I would like to turn the call over to Pamela Padgett, Vice President of Investor Relations. Please proceed, ma'am.

Pamela Padgett - *Harris Corporation - VP IR*

Thank you. Good morning everyone and welcome to Harris's third quarter fiscal 2013 earnings call. I'm Pamela Padgett and on the call today is Bill Brown, President and CEO and Gary McArthur, Senior Vice President and Chief Financial Officer. Before we get started, a few words on forward-looking statements.

In the course of this teleconference, Management may make forward-looking statements. Forward-looking statements involve assumptions, risks and uncertainties that could cause actual results to differ materially from those statements. For more information and discussion of such assumptions, risks and uncertainties, please see the press release and filings made by Harris with the SEC. In addition, in our press release and on this teleconference and the related presentation, we will discuss certain financial measures and information that are non-GAAP financial measures.

A reconciliation to the comparable GAAP measures is included in the tables of the press release and on the Investor Relations section of our website, which is www.Harris.com. A replay of this call will also be available on the Investor Relations section of our website. Now with that, Bill, I'll turn the call over to you.



APRIL 30, 2013 / 12:30PM, HRS - Q3 2013 Harris Earnings Conference Call

Bill Brown - *Harris Corporation - President & CEO*

Okay. Well thank you, Pam, and welcome to our third-quarter fiscal 2013 earnings call. Our third-quarter results were in line with our preliminary release issued April 11 and significantly weaker than previously expected primarily due to US and international tactical radio procurement delays.

Since our second-quarter earnings call, US Government funding constraints experienced under the continuing resolution were magnified when sequestration was triggered. The resulting slowdown in spending was felt across all of our government businesses, but most significantly in Tactical Communications, where the softness in our DoD business was exacerbated by the delay of key international awards that slipped into the fourth quarter, or possibly early next fiscal year. Additionally, operating performance in Integrated Network Solutions did not meet our expectations as a result of the delay in an important software release in commercial healthcare and slower revenue growth in CapRock Communications.

Now turning to slides 3 and 4 in the presentation, earnings per share was \$1.12, down 21% from the prior year, non-GAAP EPS of \$1.42. Revenue was down 12% compared to the prior year, with book-to-bill of 0.94, and funded backlog was down 2% sequentially and up 3% over the prior year. We expect the fiscal environment to remain challenging and we are implementing further Company-wide restructuring and cost reduction actions in the fourth quarter. These actions are anticipated to generate annualized savings of \$40 million to \$50 million net of what we expect to pass along to our government customers.

We are reducing our workforce by about 3%, including a 7% reduction in indirect employment and about a 10% reduction in our executive population. We also plan to reduce our facility footprint by about 200,000 square feet and have announced an early redemption of \$300 million in debt. These reductions are in addition to previous actions taken to address the slower government spending environment. Following these actions, employment will be down by about 6% since the end of calendar 2011, including a 20% reduction in our executive population.

We also continue to advance our operational excellence agenda to improve efficiency, streamline processes and lower cost, with productivity savings this year tracking well above our previously announced target of \$75 million. Free cash flow was solid in the quarter at \$185 million, bringing us to \$382 million for the first three quarters of fiscal 2013, up 24% versus prior year and 96% of net income. We continue to tighten down on capital spending and now estimate a range of \$185 million to \$195 million versus \$234 million spent last year. We continued to return cash to shareholders, repurchasing \$160 million of stock in the quarter, with plans to repurchase an additional \$140 million of stock by the end of our fiscal year.

Based on third-quarter results, we've recalibrated our full-year guidance to reflect the current environment as we now see it. The passing of the appropriations bill has been meaningful, triggering the process for government fiscal 2013 funding to work its way down to individual programs. And the release of the President's 2014 budget has provided insight into spending priorities, which appear to align well with our capabilities. However, we've yet to see how sequestration will impact specific line items, and the political horse trading behind the scenes to get a budget passed, if it happens, has just begun.

As a result, we've decided to provide fiscal 2014 guidance when we report our full-year results in July when we hope to have a little more clarity around government spending. I'll come back with a few comments before we open the call to questions. So, now, let me turn it over to Gary to discuss segment results. Gary?

Gary McArthur - *Harris Corporation - SVP & CFO*

Thank you, Bill, and good morning. Moving to segment results on slide 5, revenue for RF Communications was \$418 million and declined 22% compared to \$538 million in the prior year. Orders for the segment totaled \$486 million and book-to-bill was 1.16. In Tactical Communications, revenue was \$276 million and declined 31%. Tactical Communication orders were \$297 million, backlog was \$582 million and book-to-bill was 1.08. While orders in both DoD and international were down from the prior year, both DoD and international book-to-bills were greater than 1.

In the quarter, we received a \$26 million order from the US Marine Corps and a \$19 million order from the US Navy for Falcon III radios, as well as a \$10 million order from the Department of Defense, the first order for a new ISR product that combines wideband tactical communications and signals intelligence. Combining these capabilities results in a more powerful solution and a multifunctional device. It also reduces the overall weight a soldier carries. In the third quarter Harris was awarded a \$500 million increase in the ceiling value of our IDIQ contract with US Army



APRIL 30, 2013 / 12:30PM, HRS - Q3 2013 Harris Earnings Conference Call

Communications-Electronics Command, or CECOM. The contract supports our foreign military sales and is encouraging as we have already booked orders against it.

Significant international tactical radio orders highlighted in our earnings release included \$40 million from Brunei; \$29 million from a country in Asia; \$23 million from Australia; and \$14 million from a country in Africa. Several international opportunities have taken longer to book than expected, pushing into later this fiscal year, or some possibly into next fiscal year, including Iraq, Saudi Arabia, the Philippines and Brazil, all of which are excellent opportunities in the \$10s of millions. In addition, the next \$50 million award from a country in central Asia, which is part of a longer -- excuse me, a larger \$400 million total opportunity mentioned last quarter, is winding its way through the FMS process and nearing completion.

The 12- to 18-month international opportunity pipeline is \$2.4 billion, with over \$1 billion in the proposal or closure phases. This compares to \$2.4 billion total pipeline with \$800 million in the proposal or closure phases at the end of the second quarter. While slower than we would have liked, a number of the opportunities are very mature and nearing completion, like those just mentioned, as well as others such as Poland and the country in Africa.

The US pipeline is \$1 billion with \$500 million in the proposal or closure phases. The pipeline is smaller than the second quarter \$1.2 billion with \$600 million in the proposal or closure phases. The reduction reflects the slowdown in spending and in particular the schedule delays in awarding the JTRS Manpack Rifleman Radio and MNVR modernization opportunities. These have been reduced from \$400 million in the second quarter pipeline to a total of about \$200 million in our current pipeline, only one-third of which relates to HMS Manpack and Rifleman Radios.

In Public Safety and Professional Communications revenue growth increased 2% to \$142 million. Orders almost doubled and book-to-bill was 1.3. Public Safety orders in the quarter included \$42 million from Chester County, Pennsylvania; \$19 million from Spotsylvania County, Virginia to deploy P25 emergency communication systems; \$23 million from the Commonwealth of Pennsylvania for a 2-year maintenance agreement extension to support the statewide radio system and manage their network operations center; and a \$6 million order under newly awarded \$17 million contract from the US Marine Corps to replace the existing land mobile radio infrastructure at all seven installations in the Eastern United States.

This is the third land radio -- land mobile radio delivery order the company has received in the last year from the Marine Corps and provides interoperability with civilian agencies, which is critical in disaster relief and in other Homeland Security events. Operating income for the RF Communications segment was \$116 million. Cost reductions, a focus on operational excellence and reduced discretionary spending allowed us to achieve 27.8% operating margin in the quarter, despite a 22% revenue decline. Year-over-year margin decline was driven by volume-related factory absorption and investment in higher R&D, which was up 6% for the segment and up 9% in Tactical.

Turning now to slide 6 and Integrated Network Solutions, the third quarter revenue decreased 6% to \$365 million. Revenue growth in CapRock of 4% and in Healthcare Solutions at 6% was more than offset by a decline in IT Services revenue, up 10%. In CapRock revenue was flat in the government market, up slightly in Energy, with the majority of the revenue growth coming from maritime.

In Healthcare Solutions, revenue in the government market increased while commercial revenue lagged as a result of the software release delay. The software is currently being tested in the hospital environment and the new expected release date is now first quarter of fiscal 2014. We said last quarter that the profitability for Healthcare and 2013 hinged on this software release. This pushes our target for reaching full-year profitability into early fiscal 2014. We're still making good progress, reducing losses each quarter with the year-to-date down about 50%, compared to last year. Segment orders were down 34% as a result of delayed government awards in IT Services and CapRock.

In the Healthcare market the joint effort between the DoD and VA, called iEHR, to provide a single electronic healthcare record is being reconsidered and is causing some procurement delays. This effort will eventually provide new opportunities and our credentials in this area are strong. For example, we've been executing well on a major interoperability contract that we won last year and have started two initial DoD medical center deployments in Texas and Virginia. Under this multi-year, \$80 million healthcare innovation contract, we developed and are now deploying a service-oriented architecture suite that will support information sharing and enable new types of clinical collaboration and integration of legacy data. This will be the largest healthcare interoperability system of its kind ever built.



APRIL 30, 2013 / 12:30PM, HRS - Q3 2013 Harris Earnings Conference Call

In addition, Healthcare Solutions was awarded in the quarter a 4-year contract with a potential value of \$38 million from the VA to supply Enterprise Data Warehouse services. With this contract, we have leveraged our strong competitive position in providing interoperability solutions and moved upstream giving us the opportunity to provide business intelligence capabilities and predictive analytics. Key orders at CapRock included \$24 million from several US Government customers under the DISA Future Commercial Satellite Communications Services Acquisition program and \$17 million follow-on order in maritime from CSnet International for the continued operation and maintenance of a subsea ocean observatory in the Mediterranean sea.

In IT services, we received a \$24 million order from the Canadian Department of National Defense for the Avionics Optimized Weapons System Support program for the CF-18 Hornet fleet. In Integrated Network Solutions segment operating income was \$30 million, compared with prior year GAAP operating income of \$22 million and non-GAAP of \$33 million. Operating performance improvement in Healthcare Solutions was more than offset by an operating income decline in IT Services as a result of lower sales volume. In CapRock operating performance improved somewhat after excluding expenses associated with third-quarter cost reductions.

Moving to slide 7, revenue in Government Communications was \$442 million, decreasing 6% from the prior year. Slightly higher revenue from civil customers and flat revenue from national customers was more than offset by a mid-teen decrease in revenue from Department of Defense. Operating income was \$67 million compared with \$64 million in the prior year, and operating margin was 15.2% as a result of strong program performance on fixed-price contracts, including excellent performance on satellite programs. As previously announced, we completed the sale of the Broadcast Communications business in early February.

Turning to slide 8, free cash flow was \$185 million versus \$152 million last year. Capital expenditures were \$49 million compared to \$53 million in the prior year. During the quarter we repurchased about 3.4 million shares of our common stock for a total cash outlay of \$160 million. Year-to-date repurchases totaled \$260 million. Our effective tax rate for the quarter was 26.9% and was favorably impacted by the re-enacted R&D investment tax credit as well as favorable tax settlements.

Moving to slide 9, as previously announced we updated guidance to reflect budget uncertainty and delays in international tactical radio awards. For total Harris, revenue is now expected to be down 6% to 7% and EPS in the range of \$4.60 to \$4.70. In RF Communications our previous guidance of 7% to 9% lower is now 12% to 14% lower. Operating margin is now expected to be around 29%, including 70 to 80 basis points impact of higher R&D expense. In Integrated Network Solutions we've lowered our revenue guidance from a decline of 0% to 1% to a decline of 4% to 5% to reflect further weakness in government markets and slower than expected growth in commercial markets. Operating margin is now expected to be about 8% for the segment.

In Government Communications Systems we expect revenue to be flat to slightly down compared to previous expectations of 1% to 2% growth. As a result of continued excellent program execution and continued favorable program product mix, we expect margin to remain around 14.5%. We now expect our tax rate for the fiscal year to be approximately 31%. We continue to scrutinize capital spending. Our revised guidance for CapEx is now \$185 million to \$195 million and we now expect to generate free cash flow in the range of \$500 million to \$550 million, lower than our previous guidance of \$590 million to \$650 million as a result of lower income, slower pay by the US Government and cash restructuring charges. Based on revised guidance, free cash flow to non-GAAP net income will still be around 100%. With that, let me turn it back to, Bill.

Bill Brown - Harris Corporation - President & CEO

Okay. Well, thank you, Gary. During this time of transition in the US Government market, we are focused on the things that we control. We're implementing further cost reduction actions to position our Company for success and will continue to adapt as the market dictates, adjusting our cost structure accordingly while investing in long-term growth. Our focus is also on execution.

Our initiatives in Healthcare Solutions and CapRock are not producing the revenue growth and improved margins as quickly as expected. The integration has been difficult and progress has been choppy as the businesses still lack maturity in systems and processes. We have new leadership at Healthcare and at the INS segment level. We've mobilized the best talent from across the Company and we're focused on rapidly addressing these issues. The healthcare market and the energy and maritime market addressed by CapRock, are strong and growing and we're committed to

APRIL 30, 2013 / 12:30PM, HRS - Q3 2013 Harris Earnings Conference Call

building the talent and the skill set to support these businesses as part of a broader, multi-year strategy of accessing growing commercial markets and creating a larger international footprint.

A transformation of this scale will have its challenges like we are currently experiencing, but we remain confident about our ultimate success in executing our strategy. We are committed throughout our Company to operational excellence, continuous improvement and increasing customer value. In doing these things well, we drive superior shareholder returns. And now with that, I'd like to ask the operator to open the line for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Carter Copeland, Barclays.

Carter Copeland - Barclays - Analyst

Good morning, guys. I wondered if you might characterize what the guidance for RF in tactical implies for the mix between international and domestic revenues for the year and how you see that business exiting domestic versus international in the fourth quarter?

Bill Brown - Harris Corporation - President & CEO

Well we knew that coming into the year that international would be higher than the DoD business on orders, on sales, and that remains to be the case throughout the full-year.

Carter Copeland - Barclays - Analyst

Is it materially -- is it materially different in the fourth quarter because of the order delays? I mean, I think a little bit better than 50% -- I'm just trying to figure out is there a difference in the trends of domestic versus international, specifically in the fourth quarter due to the slippage of the international orders? I think you're talking about for the remainder of the year.

Bill Brown - Harris Corporation - President & CEO

We expect the fourth quarter is going to be pretty strong on the international business. And I think consistent in the fourth quarter as like for the full year, probably 8 to 10 points higher in international than it is on the DoD side.

Carter Copeland - Barclays - Analyst

And, how do you think about the risk around some of these -- some of these slippages to the right? Obviously, the budget has a lot of pressures. How are you thinking about the risk that these orders may not slide and just slide to the right, but may not materialize in the amounts that you were previously thinking, and I know you highlighted a little bit of degradation in the pipeline. But, how are you thinking about the risk that maybe these don't just slide, they come in at much lower amounts than what you were thinking originally?



APRIL 30, 2013 / 12:30PM, HRS - Q3 2013 Harris Earnings Conference Call

Bill Brown - *Harris Corporation - President & CEO*

Well, look, our forecast and our guidance as we see it today is based on a bottoms-up approach. We've spoken with all of our customers. We do this as we normally do, program by program, opportunity by opportunity. We -- obviously we scrubbed this pretty closely and carefully as best as we can, knowing the information that's at our fingertips. You know, on the DoD side the team is quite confident that with the appropriations bill that's been signed the procurement freeze that we've seen so far over the course of the last several months is starting to thaw. In fact, the dialogue that we are seeing with DoD customers is showing a little more confidence and optimism today than really just a month or two ago.

On the international side, we are seeing good progress, really good movement on some opportunities. Gary talked about a number of them in Iraq, particular the MOD, Saudi Arabia, Philippines, Poland, a country in central Asia. Not all of those, Carter, have to book and ship in order to hit our guidance. I think the \$500 million increase in the CECOM IDIQ is a very positive sign for us, overall, in the support of US government for certain international markets. So, we believe our forecast, our guidance here for the fourth quarter is appropriately calibrated and hedged. We feel comfortable that we can hit the guidance range that we set for the full year.

Carter Copeland - *Barclays - Analyst*

Great. Thanks for the color. Just as a follow-up, briefly, on INS. There's a lot of moving pieces here. I know you had talked about expecting some margin pressure and hits due to the NMCI contract. But also as you look through the rest of the businesses in Healthcare and that breakeven target moving a little bit and CapRock growing a little bit slower and just in general your commentary across those businesses, how do you think about the long-term margin target for that business? And the ability and timing to get to double-digit margins there?

Bill Brown - *Harris Corporation - President & CEO*

You know, our long-term target for INS hasn't changed from before. We still see ourselves getting into the low teens overall. We do know that in the IT services business margins will come down. They've been very solid for the year. We've been pleasantly surprised with the performance of the team and taking out cost as revenue changes. Margins have stayed in the pretty solid double-digit rate through the course of Fiscal 2013 and we feel pretty good about that.

That being said, it's not materialized as strongly as we had hoped in both Healthcare and CapRock. Instead of the several hundred basis point improvement in CapRock margins for the year, it's quite a bit lower than that. Were not pleased with that, but that doesn't change our long-term perspective that CapRock should be a low to mid-teen types margin business comparable with other people in the space. And Healthcare should also be a low- to mid-teens, maybe in the high teens, ROS business over time. I wouldn't knock myself into today, in terms of the timeframe to get to that, but I don't change my perspective today that INS as a whole can get to the low teens over time.

Carter Copeland - *Barclays - Analyst*

The targets are unchanged?

Bill Brown - *Harris Corporation - President & CEO*

No.

Carter Copeland - *Barclays - Analyst*

Great. Thank you very much.



APRIL 30, 2013 / 12:30PM, HRS - Q3 2013 Harris Earnings Conference Call

Operator

Yair Reiner, Oppenheimer.

Yair Reiner - Oppenheimer - Analyst

Thank you, just a couple questions for me. First, just to build on the last question. For tactical, how much business do you need to book and turn in the quarter to hit your guidance for the fourth quarter?

Gary McArthur - Harris Corporation - SVP & CFO

To hit our guidance for the fourth quarter, we need to turn a significant amount of orders here in the months of May and June. We have a significant amount of the business already in backlog. As Bill had mentioned, we're expecting a bigger increase in orders and revenue coming from international than we are from the domestic side.

Yair Reiner - Oppenheimer - Analyst

Okay. Then, in GCS, you mentioned that the civil business is holding up pretty well. We've all heard about the cuts, the FAA -- have you seen any change in your civil business since sequestration began to kick in? I guess, the effects of the sequestration began to bite a bit harder, or do you think you are kind of at a steady state right now?

Bill Brown - Harris Corporation - President & CEO

Interestingly we've both -- and what we see in fiscal 2013 and also what we see in the President's budget for Fiscal 2014, we feel pretty good about both our weather programs and the FAA. In fact, on the weather side it looks like the weather systems in general is well-supported. Those are funding for next year is up 19%. Now, the FAA programs are well-supported. FTI, which is the backbone we provide for the FAA is well-funded. There is a \$1 billion in the budget for next Gen programs. So, we've seen no impact in fiscal 2013 and we are not expecting any impact going into fiscal 2014.

Yair Reiner - Oppenheimer - Analyst

Got it. And then one last question about the restructuring. Clearly you are taking a lot of costs out. I imagine a part of that is you found areas where maybe you had necessary cost. A part of that is, I imagine, taking out some capacity. So, to what extent can we read into this that you see lower potential business going forward, as well, that you need to resize the overall business for that. How should we think about that? Thank you.

Bill Brown - Harris Corporation - President & CEO

Well, I think we are taking out cost in order to address what we know is a declining revenue environment. It's reflected in our fiscal 2013 guidance that we provided today. We see opportunities across lots of areas in the company, including in our executive population, our indirects. We've taken a harder look at our facilities. Some offices around the DC, Virginia area, but also a few larger facilities. We're taking action to address the cost structure that we happen to have. I think it's going to position us very, very well for success going forward. And it will allow us to reinvest and continue to invest in long-term growth of the company as we've been doing so far year-to-date on growth initiatives and R&D spending.

Yair Reiner - Oppenheimer - Analyst

Thank you.



APRIL 30, 2013 / 12:30PM, HRS - Q3 2013 Harris Earnings Conference Call

Operator

Pete Skibitski, Drexel Hamilton.

Pete Skibitski - Drexel Hamilton - Analyst

Good morning. I guess on RF, on tactical Coms, I'm just wondering, I guess the nature of that business is pretty quick turnaround. But, I wonder if you could characterize the revenue decline? Was it across-the-board in US DoD? Was it service specific? Any more color that you could add on the revenue decline?

Bill Brown - Harris Corporation - President & CEO

Across the DoD business, I think it would be fair to say that most of the decline occurred in the US Army over the course of year-to-date as well as what we expect for the full-year.

Pete Skibitski - Drexel Hamilton - Analyst

Okay. Understood. And then can you -- I guess at this point some of these upcoming competitions are fairly critical. I wonder if you could update us on the timing of some of the big ones, the JTRS Manpack, the MNVR, and whatever else you want to mention, Applique or Rifleman radio?

Bill Brown - Harris Corporation - President & CEO

Sure. On the Manpack and the Rifleman, it appears that both of those programs are getting delayed by about six months. That's the latest information that I have. It looks like the RFP is going to come out sometime in the August/September timeframe depending upon the Manpack or the Rifleman. The award will be early next year in the February/March timeframe and delivery will be sort of late spring, early summer in the May, June, July timeframe for both the rifleman and the Manpack. The MNVR does appear to be tracking closer to the current schedule that we last talked about. Delayed by about a month, we still expect an award in June, certainly before the end of our fiscal year. I understand deliveries on that program will occur early in calendar 2014, like around February timeframe.

Pete Skibitski - Drexel Hamilton - Analyst

Okay. Got it. I'll just take one more, I guess, on capital deployment, guys. You're retiring \$300 million in debt. Should we expect share repurchase to slow going forward for a while as a result of that deployment? And also wondering about acquisitions, divestitures, kind of how you're thinking about that right now?

Bill Brown - Harris Corporation - President & CEO

What we said during the prepared remarks is that we do intend to continue to buy back stock owing through the fourth quarter. Another \$140 million is our currently target. That would put us to \$400 million total for the year, exactly in line with what we had committed before. \$200 million of ours is quote-unquote regular buyback, \$200 million from the proceeds of selling BCD -- the broadcast business, and going into next fiscal year we don't see our capital deployment strategy to be deviating substantially from where we are at today.

Pete Skibitski - Drexel Hamilton - Analyst

Got it. Thanks very much.



APRIL 30, 2013 / 12:30PM, HRS - Q3 2013 Harris Earnings Conference Call

Operator

Joe Nadol, JPMorgan.

Joe Nadol - JPMorgan - Analyst

Thanks. Good morning. On the Tactical Communications margins, you guys don't disclose them discreetly but it looks like they were probably in the 37% range. Just was wondering, either Bill or Gary, if you could comment, help provide some color around the different moving parts that drive that. How important is volume? What's going on with pricing? And then, mix -- I know it's an open-ended question, but margins were down, not surprisingly given the volume, but were down quite a bit year-on-year. I'm just trying to gauge what the moving parts look like.

Bill Brown - Harris Corporation - President & CEO

Yes. I think a couple of things. One, in everything that we do in today's environment, we always get price pressure and we push on that very hard. We continue to sell value in the value of our products. I think we've been successful in holding the line on pricing. What we have seen, in our margins overall in RF and importantly in the tactical business, are two things. One is, because of the volume deterioration, we are starting to run into factory absorption problems. That's the one thing that did ding us in the quarter. The other is continued investment in R&D. For the full year we see that that's probably 70, 80 basis points of impact at the RF segment level. We continue to invest, importantly, in the tactical business. Those are the two principal factors that are impacting our margins in Tactical Communications.

Joe Nadol - JPMorgan - Analyst

Okay. So, as you look at the profile rather than year-on-year if you look sequentially, I mean, there's nothing about -- considering that your book-to-bill is a little over 1 here and it looks like your volume in Q4 should be in line with Q3, you are better and you're looking for orders to pick back up. You wouldn't expect really anymore adverse reaction to your margins, unless volume were to again deteriorate?

Bill Brown - Harris Corporation - President & CEO

No, we don't. We guided for the year 29%. That certainly has an implication, but what the ROS is for the segment is in Q4, it does hit (inaudible) volume, as you just pointed out. We know the investment that we are making, and making in Q4 as well. So at the moment we don't think it has any further downside.

Joe Nadol - JPMorgan - Analyst

Okay. And then just over on government Coms, your margin there continued to be better and better, hitting 15% here. Could you just give a little more context around EAC or [key-in] catch up adjustments and how those have been performing? Maybe -- I know you're not giving guidance for next year yet, but a little more color as to how you're thinking about that margin performance going into -- going forward?

Bill Brown - Harris Corporation - President & CEO

Well, we're thrilled with the performance of the GCS team and they've done a fantastic job. They are executing very, very well on a number of different dimensions and we are thrilled with the margin performance in the quarter. That being said, I think we've pointed out to you before, that that high level of ROS is not sustainable. It's going to come down and we'll probably be adjusting as we go into fiscal 2014.

APRIL 30, 2013 / 12:30PM, HRS - Q3 2013 Harris Earnings Conference Call

It probably won't be any different than what we've talked about in June of last year. But that is a very special margin rate that we happened to hit. On the EACs, we'll be showing in the queue that our EAC's this year about \$16 million in the quarter. It's pretty consistent with EAC adjustments in the quarter at last year. So year over year, not a big driver of margin performance. I think it's truly just very good execution by the team at JCF.

Joe Nadol - *JPMorgan - Analyst*

Very good. And then Bill, if you don't mind just one more. Back to RF and the international on tactical. You know, it seems like there's been -- there's a number of things that have slipped and it seems like it's getting a little better here. I know it's a lot of different countries and you named and a whole bunch of the important ones. But is there anything bigger picture, whether it's Department of State, Department of Defense, Afghanistan, what's going on with the conflict, that's really underpinning a lot of the movement in the order stream? Or, is this really all just sort of one-off different moving pieces? And, give us the latest, I guess, on -- if there are any larger factors at play, how you are thinking about them?

Bill Brown - *Harris Corporation - President & CEO*

There's really not -- I wouldn't say a lot of larger factors. Obviously, as we spoke last time for the country in central Asia, that is supported by the FMS process. There had been some sand in the gears in that process. We see that starting to break up a little bit and more progress being made. I'm pretty confident that we are not losing share. We're confident that market opportunities we've talked about before remain. The pipeline is still very robust at \$2.4 billion.

Joe, it's really just the timing that's very, very difficult to predict. Keep in mind we're coming off of a very strong 2012. Orders and revenue were very strong last year, up double digits into record levels. In February of this year, I was in the Middle East at the trade show. I met with the dealers and customers of -- all of the customers that we've just spoken about, Iraq, Saudi, UAE, Jordan, Afghanistan, Pakistan. And look, I think we are very well-positioned with excellent products and a very strong reputation in all of those markets. Wideband still is a very, very large untapped opportunity in the international markets.

What I observed when I was there through direct conversation is some of the competitors we play against in the international markets have pulled back a little bit on investment in new products. And in fact we're throttling up investing in new products, new capabilities to expand the addressable market. I think we are very, very well-positioned. It's really just a matter of timing. I do hope that you will see some good announcements coming forth from us in the fourth quarter, based on the pipeline that we see maturing in international.

Joe Nadol - *JPMorgan - Analyst*

Okay. Thank you.

Operator

Gautam Khanna, Cowen and Company.

Gautam Khanna - *Cowen and Company - Analyst*

Bill, you mentioned, I think, in your opening remarks, being somewhat pleased with the DoD's priorities as they were expressed in the 2014 request. I'm just wondering if you could elaborate on this? When we look at some of the radio line items nearly all were kind of revised downward from the fiscal 2013 request. So where do you see kind of the alignment shaping out well?



APRIL 30, 2013 / 12:30PM, HRS - Q3 2013 Harris Earnings Conference Call

Bill Brown - *Harris Corporation - President & CEO*

Thanks for the question, Gautam. Look, my comment was really more around the overall budget that the President put forth. I think that's very encouraging. We did give a lot of insights on priorities. I think that has aligned pretty well with our capabilities. I referenced a bit about some of the positives on weather systems and the impact on GOES-R. The FAA programs which we feel very, very good about.

We do a lot of work with the VA and IT services for the VA is up double-digit rates. I think on -- perhaps on the other side of the coin, maybe a little bit more balance on tactical radios. You are right, it's a bit mixed. SOCOM, Air Force, Marine Corps funding is down. All the modernization is supported, although it really is at a slower rate. But I'm pleased to see the commitment to modernization.

I'm pleased to see the commitment to open competition. I'm thrilled that the Manpack RDT&E has been brought down from \$120 million last year to \$5 million. I think these all very, very important steps that have been taken and I think work in our favor in many ways over the long term. I do see national intelligence programs funding coming down a little bit. So, I think there are some things that are positive in President's budget. There's also some things that, I guess, provide a bit more balance. So, for us, like all other Americans, there's something for everyone to not like in what came out in the President's budget.

But, we recognize as everyone else does that it's pre-sequestration. It's pre-negotiation on entitlements and on revenue. So, I think there's a lot of ground to cover between now and a fiscal 2014 budget, if that happens over the course of the summer. We are just being -- we're being prudent in where we speak today.

Gautam Khanna - *Cowen and Company - Analyst*

Thanks. And just a follow-up, if I may. Can you comment on sort of the duration of the backlog and how that's evolved over the last year? Because, obviously you had north of 560 in backlog entering the quarter which would have covered, you know, kind of flat sequential sales these things. So I'm just curious, how do we think about the delivery and timing on some of those orders already?

Gary McArthur - *Harris Corporation - SVP & CFO*

Hi Gautam, this is Gary. I don't know if the duration of the backlog has changed materially. Obviously, in the backlog, had included some products and services for Australia that were expected over time. A country in northern Africa as well, is an ongoing program, we're into different phases of that. So, some of that is expected over time. You know, the backlog did come in slightly higher in tactical, compared sequentially to where it was. So, overall, I wouldn't say the duration of the backlog changed materially from what we had expected.

Gautam Khanna - *Cowen and Company - Analyst*

Okay. If I might ask one more, I'm sorry. Last year, I think you had an Investor Day and it doesn't sound like you had one this year, where you offered at least a preliminary view on the September quarter. I just wondered if you could give us -- given the restructuring and all the moving pieces, should we expect that to be kind of the lightest of the year and sequentially down from Q4? Or, how do you directionally think of the profile in 2014?

Bill Brown - *Harris Corporation - President & CEO*

We're not -- as I mentioned in the remarks, we're not going to provide any fiscal 2014 guidance today. There's a budget, there is some visibility we'd still like to see from US government funding. We will provide some guidance toward the end of July when we publish our full-year 2013 results. Look, for us and everybody else, I think our first-quarter, which is the last quarter of the government fiscal year 2013, is likely to be challenging for everybody. We are moving fast on the restructuring. Much of the things that we're doing will occur in the course of the fourth quarter. I hope that we will get this tailwind going into the fiscal year, but a lot hinges on the behavior of the government customers and we'll shed some more light on the full-year as well as the balance over the course of the year when we speak at the end of July.



APRIL 30, 2013 / 12:30PM, HRS - Q3 2013 Harris Earnings Conference Call

Gautam Khanna - *Cowen and Company - Analyst*

Thanks and good luck.

Operator

[Arnin Thrustolavern], *Sterne Agee*.

Arnin Thrustolavern - *Sterne Agee - Analyst*

Through the CapRock business, can you expand on the slower than expected revenue growth? The Gulf rig count activity appears to do a little better than expected. Was the weakness coming from land-based government communications? Or has there been any sort of technological shift in off-shore use of SATCOM versus say, laying fiber-optic cable?

Bill Brown - *Harris Corporation - President & CEO*

No. Look, in CapRock the maritime business performed, we think, very, very well. Royal Caribbean was a key driver of that. We're performing very, very well. All 33, 34 boats that we are doing for Royal Caribbean are done and operating and I think that customer is very, very pleased. So we've seen good growth on the maritime side.

The government side was relatively weak. We think that that is market related. On energy, it was weak. It was disappointing. From my perspective, it was due principally to execution. I think in some ways we stubbed our toe a little bit on the energy side in our responsiveness to our customers. I want to reassure you we've got people focused on that, we are going to get that fixed.

Arnin Thrustolavern - *Sterne Agee - Analyst*

Great. And then just on the Healthcare Solution business, how is the right sizing of the commercial business progressing? I know you have this delay here, but are you still investing in that vertical for growth? Or are you looking at more at harvesting at this point?

Bill Brown - *Harris Corporation - President & CEO*

No. We are not doing any harvesting. I think this is not an issue of cost take-out, it's about getting a piece of software right. We've got a good set-up team that's pushing on this. We will launch it in the first quarter fiscal 2014. From what I have seen and heard with large commercial healthcare operators who have seen the software that we are going to be releasing, they are enthusiastic about it, they are excited about it.

I have to say it's a very complicated piece of software, which is what has caused us some difficulties. But, this is an investment. We are going to move forward with it and I think, ultimately, we are going to be very successful in the commercial healthcare side.

Arnin Thrustolavern - *Sterne Agee - Analyst*

Great. Thanks.

Operator

Chris Quilty, Raymond James.



APRIL 30, 2013 / 12:30PM, HRS - Q3 2013 Harris Earnings Conference Call

Chris Quilty - Raymond James - Analyst

I wanted to follow-up on your comment about the R&D investments in the RF business. Can you clarify, is that a stepped-up level of investment from what you had planned, perhaps a year ago? If so, is it being driven by the tactical radio or the first responder side of the business? And is it primarily new product or is it push into new product areas?

Gary McArthur - Harris Corporation - SVP & CFO

Chris, this is Gary. We definitely have stepped up the R&D investment as we've talked about doing a year over year compare. A lot of the investment is in the Tactical Communications area. It has to do with building the two channel Manpack, making sure the waveforms are where they need to be on WNW. So, a lot of investment is going in there. As well as -- we have increased investment in public safety where we're continuing to invest in LTE. We expect that market to take longer to come to fruition. But it is an important area for us and we're investing there as well.

Chris Quilty - Raymond James - Analyst

Speaking of waveforms, have you ever made progress on the ANW2 and getting that accepted into the repository?

Bill Brown - Harris Corporation - President & CEO

We continue to work on that. We do know that that is very important for the US Army and really the services general, but particularly the US Army to have nonproprietary waveforms in their fielding requirements. We continue to push on this and we'll update you as we make progress.

Chris Quilty - Raymond James - Analyst

Okay. And a follow-up on the Public Safety business. Can you just give us sort of an update on where you think you stand with that business? Both in terms of your product offering, your geographical presence and the overall spending environment for the local municipal government market relative to the federal?

Gary McArthur - Harris Corporation - SVP & CFO

Okay, Chris, this is Gary again. In the public safety market, looking across our product line, we think we have quality products. We think there's additional room for taking out cost of those products, but we expect to be more competitive over time in the terminal piece. I think on the systems and the open architecture, I think we're extremely competitive with Motorola in that space. And then, looking at the government market, right now we're seeing that state and local growing mid-single digits. So, we're seeing opportunities there to continue to increase our revenue with the market growth as well as taking share from Motorola.

Pamela Padgett - Harris Corporation - VP IR

Operator, I think we have one more question in the queue? If you're finished, Chris.

Operator

Pete Skibitski, Drexel Hamilton.



APRIL 30, 2013 / 12:30PM, HRS - Q3 2013 Harris Earnings Conference Call

Pete Skibitski - *Drexel Hamilton - Analyst*

I guess to follow-up on the last one, Public Safety. It seemed like you had a fantastic first half of the year and it seemed like revenue kind of slowed in the quarter. And I think you have a really tough comp in the fourth quarter this year. So, I'm just wondering, overall, do you still expect the type of growth for the full year in Public Safety that you were thinking earlier in the year? Or is the market slowing there?

Bill Brown - *Harris Corporation - President & CEO*

We still see very good growth for the year in Public Safety. We think it's going to be up mid-single digits. The orders in Q3 were very strong. As Gary pointed out it was up more than double in the quarter, 1.33 book-to-bill. I think the outlook for that business continues to be very, very positive. We will see a slightly weaker second half than we saw in the first half. We saw a very strong first half result.

But, the backlog is solid, the pipeline is large, it's healthy. I think we are doing a very, very good job winning large program opportunities in the marketplace. Those, as you know, can be lumpy. We went for a number of quarters with book-to-bill less than 1. We need to and will do better on the flow business, which is the terminal side of the business. In general, I think we feel still pretty good about growth this year as well as long-term growth possibilities in Public Safety. I think there's lots of opportunities to grow and improve margins in that business.

Pete Skibitski - *Drexel Hamilton - Analyst*

Okay. Just one last one, if I could. I apologize if you spoke to this already. On the cost reductions and the \$40 million to \$50 million in annual savings, is that company-wide or is it focused on RF in particular? And then, as a corollary, the previously announced charges, \$65 million to \$115 million, have you narrowed those? Are there going to be all booked at the corporate level?

Bill Brown - *Harris Corporation - President & CEO*

Well, that is company-wide. And it's across all the businesses as well as at corporate. The charges will likely be booked, I think, Gary, at the corporate level. The delta between the low end and the high end is just potential impairments that we might have to take, including in the Healthcare business in the fourth quarter. That is yet to be determined and that's the delta between the low-end and the high-end of the cost range.

Pete Skibitski - *Drexel Hamilton - Analyst*

Great. Thank you.

Pamela Padgett - *Harris Corporation - VP IR*

I think that wraps us up. Thank you everyone for joining us and we will see you next quarter.

Operator

Thank you. Thanks for joining, ladies and gentlemen. This concludes your presentation. You may now disconnect. Good day.

APRIL 30, 2013 / 12:30PM, HRS - Q3 2013 Harris Earnings Conference Call

DISCLAIMER

Thomson Reuters reserves the right to make changes to documents, content, or other information on this web site without obligation to notify any person of such changes.

In the conference calls upon which Event Transcripts are based, companies may make projections or other forward-looking statements regarding a variety of items. Such forward-looking statements are based upon current expectations and involve risks and uncertainties. Actual results may differ materially from those stated in any forward-looking statement based on a number of important factors and risks, which are more specifically identified in the companies' most recent SEC filings. Although the companies may indicate and believe that the assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate or incorrect and, therefore, there can be no assurance that the results contemplated in the forward-looking statements will be realized.

THE INFORMATION CONTAINED IN EVENT TRANSCRIPTS IS A TEXTUAL REPRESENTATION OF THE APPLICABLE COMPANY'S CONFERENCE CALL AND WHILE EFFORTS ARE MADE TO PROVIDE AN ACCURATE TRANSCRIPTION, THERE MAY BE MATERIAL ERRORS, OMISSIONS, OR INACCURACIES IN THE REPORTING OF THE SUBSTANCE OF THE CONFERENCE CALLS. IN NO WAY DOES THOMSON REUTERS OR THE APPLICABLE COMPANY ASSUME ANY RESPONSIBILITY FOR ANY INVESTMENT OR OTHER DECISIONS MADE BASED UPON THE INFORMATION PROVIDED ON THIS WEB SITE OR IN ANY EVENT TRANSCRIPT. USERS ARE ADVISED TO REVIEW THE APPLICABLE COMPANY'S CONFERENCE CALL ITSELF AND THE APPLICABLE COMPANY'S SEC FILINGS BEFORE MAKING ANY INVESTMENT OR OTHER DECISIONS.

©2013, Thomson Reuters. All Rights Reserved.