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HRS - Q3 2017 Harris Corp Earnings Call

EVENT DATE/TIME: MAY 03, 2017 / 12:30PM GMT

OVERVIEW:

Co. reported 3Q17 non-GAAP EPS of $1.38. Expects FY17 revenue to decline about 1% and non-GAAP EPS to be $5.50-5.55.

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Harris Corporation's Third Quarter 2017 Earnings Conference Call. (Operator Instructions) I would now like to introduce your host for today's conference, Mr. Anurag Maheshwari, Vice President of Investor Relations. Sir, you may begin.

Anurag Maheshwari

Thanks, Channel. Good morning, everyone, and welcome to our third quarter fiscal 2017 earnings call. I'm Anurag Maheshwari. On the call today is Bill Brown, Chairman and Chief Executive Officer; and Rahul Ghai, Senior Vice President and Chief Financial Officer.

First, a few words on forward-looking statements. Forward-looking statements made today involve assumptions, risks and uncertainties that could cause actual results to differ materially from those statements. For more information and related discussion, please see the press release, the presentation and Harris' SEC filings.

In addition, a reconciliation of non-GAAP financial measures discussed today to comparable GAAP measures is included in the quarterly material on the Investor Relations section of our website which is www.harris.com where a replay of this call also will be available. With that, Bill, I will turn it over to you.

William M. Brown - *Harris Corporation - Chairman, CEO and President*

Okay. Well, thank you, Anurag, and welcome to your very first earnings call. And good morning, everyone. Anurag has recently taken over as Head of Investor Relations from Pam who retired from Harris after 20 terrific years. Anurag has been with Harris for about 3 years, leading business development in the Asia Pacific region and previously worked in private equity in Singapore for about 7 years. He and I also worked together at United Technologies in Singapore about a decade ago, and we're very pleased to have him here at the corporate office.

So earlier today, we reported third quarter results that extend our strong year-to-date performance as we continue to deliver on our strategy. Our key priorities for the year have been the focus to portfolio on our core technology differentiated businesses, deploy capital in a balanced and shareholder-friendly way, drive operational excellence including flawless integration of Exelis, and continued investments to position the company for a long-term growth. Last week, we achieved an important milestone with the completion of the sale of IT Services that we announced in late January. This transaction marks the fifth asset sale in the last 4 years as we've shaped the company around our core franchises where technology differentiates our solutions.

The sale of CapRock and IT Services, along with year-to-date free cash flow, has generated $1.5 billion that we are using to buy back stock, deleverage, pay dividends and pre-fund pension. We remain on track to execute $700 million of share repurchases in fiscal '17, a record for Harris in a single year. Between share repurchases and dividends, we've returned about $950 million in cash to shareholders this fiscal year. We still plan to use $400 million in proceeds from IT Services to pre-fund the pension, freeing up future cash flow. And we continue to deleverage as planned, paying down $575 million in term loans and other debt through April, and bringing debt repayment since the Exelis acquisition, to $1.3 billion of our $2 billion goal. Exelis' integration continues to progress well through the third quarter with all projects near completion as we generated an incremental $50 million of synergies in fiscal '17. We expect to exit the year at $145 million of run rate synergies, higher than our initial estimate of $100 million to $120 million and a full year ahead of our original plan. Moving forward, we'll continue to drive productivity, lower cost and improve program execution as we extend operational excellence and best practices throughout Harris.

Our progress on these strategic objectives is reflected in third -- in solid third quarter and year-to-date results. Despite organic revenue down about 3% in the quarter, operating margin was a strong 19% and non-GAAP earnings per share was up 2% to $1.38. Year-to-date organic revenue was down about 1%, operating margin up 50 basis points and non-GAAP EPS, up 5%.

Free cash flow was $164 million in the quarter and $410 million year-to-date as we enter what is typically our strongest cash quarter. Total company book-to-bill was 1.0 for the quarter and greater than 1 year-to-date. As a result of our strong year-to-date performance, we're tightening our guidance for fiscal '17 and now expect revenue down about 1%, the midpoint of prior guidance and earnings per share of $5.50 to $5.55, slightly above the previous midpoint. Free cash flow remains unchanged at about $800 million.

And before turning the call over to Rahul to go through the details by segment, let me provide some high-level color. Legacy tactical revenue continues to trend better, up 1% in the quarter with international up 8%, driven by strong growth in Europe and Latin America. Europe remains a solid growth area following a record fiscal '16 driven by a broad-based modernization effort across Eastern Europe, in particular in Poland and Romania in the quarter and Ukraine earlier this year. In Latin America, we continue to build on a momentum from the first half with an even stronger third quarter resulting in significant double-digit year-to-date growth from modernizations and counter narcotics programs. International tactical continues to trend to the upside with a revenue down about 10% year-to-date versus down 19% in the first half, and we now expect international tactical revenue to be down mid-single digits for the year versus the prior high single-digits guidance. We expect a strong fourth quarter on an easy compare to prior year with solid backlog coverage and the line of sight to the remainder.

DoD tactical revenue, as expected, was down about 20%, driven by an extension of the CR through April and cautious buying behavior. With revenue up 1% year-to-date, we continue to see DoD about flat for the year which implies Q4 being about flat as well with a large part in backlog or funded with fiscal '16 budget. Overall, we're now seeing legacy tactical to be down low to mid-single-digits, an improvement from down mid- to high single digits in the prior guidance. Army and SOCOM modernization programs are progressing and are well supported. In the pending omnibus package, the HMS program is fully funded at $274 million in GFY '17, up significantly from the prior year and matching the House Defense Appropriations bill that was passed in March, indicating strong continued support for Army modernization. On SOCOM, we submitted the Manpack proposal in February with the decision expected this summer, and we remain on track to complete the development of a 2-channel handheld and begin product deliveries in the second half of our fiscal '18.

Electronic Systems was flat for the quarter and up 3% year-to-date, driven by the ramp of the UAE battlefield management system program and strong double-digit growth in electronic warfare. Our outlook in electronic warfare remains positive with a solid and growing pipeline of upgrade opportunities on international F-16s where the installed base is over 500 aircraft plus upgrades and new builds on U.S. and the international F-18s. We also see strong growth in the avionics business with 2 consecutive quarters of strong orders through long-term platforms like the F-35, F-18 and P-8.

In Space and Intel, we were down 3% in the quarter but still up 2% year-to-date with growth largely driven by classified customers where we continue to expand into new adjacencies. Although we had good growth in the first half, it's being offset by a few program transitions moving from development into sustainment in the second half and more recently by a few task orders and commercial opportunities slipping into fiscal '18. As a result, we now expect revenue for Space and Intel to be about flat in the year. With a pipeline that had grown by 8% to more than $11 billion over the past year and our continued high win rate, we remain confident in the long-term outlook for the business.

We're now in the final innings of fiscal '17 and we're encouraged by our year-to-date results and confident in our expectations for the balance of the year. Congress will be voting on our omnibus package later this week and I'm hopeful for a positive outcome. As we look at fiscal '18, all of the components for top line growth are coming together, forming an inflection point for Harris. Fiscal '17's share repurchases will offset much of fiscal '18's dilutive effects from divestitures, and our operational excellence agenda will continue to lower cost and contribute to earnings growth in '18 and beyond. So let me now turn the call over to Rahul to walk through our financial results. Rahul?

Rahul Ghai - *Harris Corporation - CFO and SVP*

Thank you, Bill, and good morning, everyone. As a reminder, discussions today are on a non-GAAP basis and exclude Exelis integration and other costs. This quarter, we transitioned to a 3-segment reporting structure and results and guidance exclude both CapRock and IT Services which are reported as discontinued operations.

Turning now to segment details on Slide 5. Communication Systems revenue in the quarter was $461 million, down 5% versus prior year. Tactical Communications revenue was also down 5%, but legacy tactical was up 1% driven by international which grew at 8%. Year-to-date backlog for legacy tactical is up 5% to $421 million. Operating income for the segment was $140 million compared to $151 million in the prior year due to lower volume. Year-to-date segment revenue is down 9% with operating income down 10%. Year-to-date operating margin of 29% is down 60 basis points versus prior year due to lower volume partially offset by synergy savings. However, operating margins have trended sequentially higher for 3 consecutive quarters.

Book-to-bill was slightly below 1 for the quarter with strong bookings in Public Safety and airborne radios. This quarter, we received a $36 million order for Small Tactical Terminal airborne radios which will be integrated onto a growing number of diversified air platforms across an expanding customer base. And following the close of the quarter, Public Safety was awarded a $75 million contract from a utility company to upgrade a legacy analog system to a P25 digital network.

Space and Intelligence Systems on Slide 6. Segment operating income in the quarter was up 1% on a revenue down 3% compared to prior year as higher revenue from intelligence community was more than offset by few environmental and space programs that have transitioned from development to sustainment. Year-to-date revenue is up 2% with operating income up 11%, resulting in margin expansion of 130 basis points from 15.2% to 16.5%, driven by solid program execution and higher pension income.

Book-to-bill was more than 1 for the quarter driven by strong bookings from our classified customers. This quarter, the classified business received a $500 million single-award IDIQ contract from National Geospatial Intelligence Agency with an initial task order of $15 million to perform search and retrieval services for geospatial products. We also received $28 million and $18 million in follow-on contracts to support U.S. missile warning, missile defense and space surveillance missions under the SENSOR program.

Electronic Systems on Slide 7. Electronic Systems now includes the financial results of the air traffic management business that remains with Harris after the IT Services divestiture. Segment operating income in the quarter was up 4% on flat organic revenue compared to prior year as higher revenue from electronic warfare solutions on the continued ramp of UAE integrated battle management system was offset by lower revenue from wireless products and the ADS-B program transition from buildout to sustainment. Year-to-date revenue is up 3% with operating income up 12%, resulting in margin expansion of 170 basis points from 20% to 21.7%, driven by solid program execution, a contract adjustment in the second quarter and higher pension income. Book-to-bill was slightly below 1 for the quarter with strong bookings in avionics and air traffic management including a $72 million follow-on contract to provide engineering services for Next Generation Air Traffic Management weather initiatives and a $72 million follow-on contract for Sonobuoy Launching Systems for the U.S. Navy's P-8 antisubmarine aircraft. Additionally, we've received a $25 million follow-on contract from the U.S. Air Force for electronic warfare demonstrations.

Moving to Slide 8 and 9 for fiscal '17 guidance. Given our year-to-date performance, we now expect organic revenue down about 1% for the year at the midpoint of the previous guidance excluding prior year revenue from the Aerostructures business. Full year non-GAAP EPS guidance which excludes Exelis acquisition-related integration and other charges as we narrowed from a range of $5.40 to $5.60 to a range of $5.50 to $5.55. As previously communicated, full year EPS guidance reflects about $700 million in share repurchases for the year as well as an effective non-GAAP tax rate of 28.5%.

In segment guidance, margins now reflect the reallocation of FAS pension income, stranded cost and the accounting of discontinued operations related to the CapRock and IT Services divestitures. These reallocations differ by segment resulting in modest impact to segment margins. In Communication Systems, we now expect revenue to be down about 7% versus down 7% to 9% in the previous guidance, with Harris legacy tactical now down low to mid-single digits. Segment operating margins are now expected to be about 30%.

In Space and Intelligence Systems, we now expect revenue to be about flat versus up 1% to 3% in the previous guidance. While classified business remains strong, it is offset by some task orders and commercial awards that have shifted to the right. Segment operating margins are now expected to be about 16.5%.

In Electronic Systems, we now expect revenue to be up about 3% at the midpoint of the previous guidance. We continue to see strong growth in electronic warfare, F-35 UAE battle management programs, partially offset by softness in wireless products and the ADS-B program. Segment operating margins are now expected to be about 20.5%.

Free cash flow guidance of approximately $800 million is unchanged. This guidance excludes pension pre-funding which will be reported in operating cash flow. This pre-funding is in addition to our annual contribution of approximately $188 million for a total pension contribution of approximately $588 million for fiscal 2017. As I mentioned last quarter, this contribution fully fund the pension on an IRS basis and eliminates mandatory contributions of about $200 million for the next few years.

During the third quarter, we launched a $350 million accelerated share repurchase or ASR program, and will initiate an additional $250 million ASR program in the fourth quarter. We remain on track to repurchase about $700 million of shares this fiscal year.

On Slide 10, we have provided historical financials of the business on a continuing operations basis that reflect reallocations of stranded costs and FAS pensions to the 3-segment structure. We will also be filing an 8-K with restated total company financials. And with that, let me turn to the operator to open the line for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question comes from the line of Jason Gursky.

Jason Michael Gursky - *Citigroup Inc, Research Division - Director and Senior Analyst*

I was wondering if you could spend a few minutes discussing with a little bit more detail on the comment that you made about the Space Systems pipeline of $11 billion. Can you just talk a little bit about where that pipeline is from an end market perspective, and the cadence that you expect on those awards over the next couple of years? And when that revenue stream might actually begin to accrue to the company?

William M. Brown - *Harris Corporation - Chairman, CEO and President*

Sure, Jason. Thanks for that question. Yes, so we're very pleased with where the pipeline happens to be. It's pretty significant. Again, it's up about 8% year-over-year. Keep in mind that Space and Intel business is about 2/3 in the classified space and those budgets are just becoming revealed as we see what's coming through the Omnibus. So we know that there's been strong support for the program that we happen to be on. These will -- opportunity will come to fruition over the next several years. Our win rate in that segment is very, very high. It's north to 70%. So we feel good when we see this sort of size of the pipeline growing with us, entering new missionaries. And the high level of our successive win rates, we feel pretty confident, those opportunity to materialize over the next several years. I really can't characterize exactly when that might happen but we do know that those will happen over the next several years. They come into bunch of different areas. There's a number of classified programs on the ground side and we talked about winning a pretty significant ground adjacency very recently. There's been a lot of attention and a lot of focus on Space Superiority, significant investments in protecting our overhead architecture and Harris is in the middle of that. We've also have -- had some substantial wins in our ground sustaining program, we call SENSOR. That's coming through performing exceptionally well on the task orders. When we bought Exelis as a program that was legacy Exelis, the delivery rate was something like around 30%. Unless past quarter, it was about 100%, so we feel very, very good about that. So there's been lots of really good performance. And I think we're executing very, very well. And on the commercial side, we've seen a couple of the reflectors that had slipped out of the year going into fiscal '18 but our commercial space, the reflector business, also looks pretty robust. We see at least 10 different opportunities over the next 24 months coming to fruition. Our win rate there is actually quite high as well. So that's maybe a little bit more color, Jason.

Jason Michael Gursky - *Citigroup Inc, Research Division - Director and Senior Analyst*

Yes, that's great. And then maybe just one number related question, it's when you get poised to return to growth here over the next year or so. Can you talk a little bit about the impacts of that growth on working capital and whether we should expect working capital to become a source or a use of cash as you return to growth?

William M. Brown - *Harris Corporation - Chairman, CEO and President*

Sure. Well, thank you for that. In fact, we've seen so far year-to-date, we've seen working capital build. Even though our revenue is down a little bit, we do expect in our fourth quarter fiscal '17 for that to reverse, which would give us to our $800 million target for the year in free cash flow. And we -- and that's with about -- in the high 40s in terms of data network and capital, so pretty good step-down from where we were at the end of Q3 but in line with or maybe a little bit better than where we were ending in fiscal '16. And we do see a little bit more opportunity with that, so it will be important for us to keep managing our working capital levels very, very aggressively as we return to growth over the next 3 years.

Operator

And our next question comes from the line of Carter Copeland of Barclays.

Phillip Carter Copeland - *Barclays PLC, Research Division - Associate Director and Senior Analyst*

Congrats on getting all these transactions done.

William M. Brown - *Harris Corporation - Chairman, CEO and President*

Carter, thank you.

Phillip Carter Copeland - *Barclays PLC, Research Division - Associate Director and Senior Analyst*

Bill, I wanted to just ask a clarification to start off. You may have commented about fiscal '18 being an inflection point and the repo is offsetting the -- with divestiture dilution and cost savings. But I just want to clarify, you still expect it to organically grow EBIT as we transition to next year and that's part of that inflection. And the other thing I wanted to ask about was just in terms of the order momentum in legacy tactical, I know the revenues have been strong in Europe, but maybe if you could speak to the -- what the book-to-bill looks like there and maybe also hit international, the kind of the latest color on Australia which I know is still sitting out there.

William M. Brown - *Harris Corporation - Chairman, CEO and President*

Carter, I think you covered quite the gamut on that one. So let me start with the first one. Yes, we do expect to return to top line organic growth next year, and there's a number of contributors to earnings per share next year. Certainly, revenue's going to be one. We continue to drive hard on our OpEx agenda. We typically take out 2% to 3% net of cost every year in terms of normal operational excellence and that will be a contributor -- in the terms of the share repo that we're doing now will be a contributor going into next year. We don't see as much pension tailwind. We don't see as much synergy tailwind as we saw this year. So lots of puts and takes but we do expect to grow earnings per share into fiscal '18. Now on -- maybe I'll start and maybe Rahul can jump in a little bit on the tactical side. We saw at that very good momentum through the year in our legacy tactical business. Europe has been a very, very strong performer for us this year and it keeps getting incrementally better. A lot of it is in Eastern Europe. I mentioned a few countries that were important in the quarter. Poland, Romania, they remain important. Ukraine was in the early part of this year. So we feel very good about that. The Central American and Latin American region also remains very, very strong for us. The offsetting areas are -- remains Central Asia where it's in a transition period. It's very low. It's a lot of headwind for us this year. Not seeing that, that's (inaudible) going to turn around into next year. The Middle East has been soft but we're starting to see some glimpses of some orders flow through there, we saw some even in early April, some movement and some good support on what it seems so far in the Omnibus. So we're seeing good support for our international business, and I'm encouraged with the trends. We do expect for a company to end with a book-to-bill about 1 as well as in CS as well as in within the tactical business. And an important part of that is Australia. We do see -- as Australia comes through at the back end of the year, we will be well above 1 in the tactical business. We still think we get about 1 even when Australia doesn't book. So in Australia, the opportunity is just under $300 million. So that $250 million to $300 million range is part of the $1 billion-plus multi-year opportunity in Australia. We're deep in contract negotiations with them. It's going to happen right at the back end of our fiscal year, so the end of June, and we're tracking towards that. We'll be given any big international opportunity. It could slip into July or August but we're right on the edge of that. We're in deep negotiations. It's going to come to us. We know the size. The scope has been now well defined, so we feel very good about the progress now in Australia. So I think I fit on the points.

Rahul Ghai - *Harris Corporation - CFO and SVP*

Yes, you did. And I'll say those Communication Systems, Carter, we -- the other part of the growth next year would be in the Electronic Systems space. Bill mentioned the opportunities on the EW platform with F-16s and F-18s. So we expect electronic warfare to continue to grow and the C4 -- the battle management system win in UAE is going to drive growth in our C4i businesses, so those will be the other 2 contributors for growth in fiscal '18.

Operator

And our next question comes from the line of Pete Skibitski of Drexel Hamilton.

Peter John Skibitski - *Drexel Hamilton, LLC, Research Division - Senior Equity Research Analyst*

Bill, one top level type of question. I'm just curious as to your thinking as you kind of finish up fiscal '17 here as a more focused defense electronics company. And it seems like the budget is starting to improve your visibility. Why is it so? I'm just trying to get a sense from you in terms of how you think about the company growth-wise, just notionally over the next few years, whether or not we'll get the DoD budget outlook? And then do you think you can kind of outgrow the DoD budget growth kind of more in line, or for whatever reason below that? I'm just curious as to how you think about the company at this point.

William M. Brown - *Harris Corporation - Chairman, CEO and President*

Well, I think I would say once we see where the President is going over the next 5 years, all we've seen so far is a '17 Omnibus that's apparently going to go to his desk at the end of this week. And some indicators, some high-level indicators for the shape of a budget in '18 which certainly shows the DoD with substantial growth, DHS with substantial growth. We think the Intel budget is going to comp alot, at the offset of some other parts of the government. So there's a lot of room between now and then and really understanding the '18 budget, how it's shaped and then beyond that. But I would say, Pete, given everything that I've seen, in fact, anyone's view of the budget even under this cluster, we'll see the DoD budgets getting better. So we're at a great point. We've worked very, very hard as a team to streamline our portfolio on to businesses where technology can differentiate where we have good strong positions in businesses that are aligned very clearly with where the DoD and our customers are moving with key mission needs. So we feel very good about where we happen to be. I mentioned this last time. I think the fact that the portfolio is more streamlined allows the management team to focus more on businesses where we know we can drive shareholder value. And I don't want to understate that. I think that's a very, very important part of this whole dynamic of shaping our portfolio. So we all feel good. We feel good we're set up to grow in '18 and beyond. We still have opportunity to do better on productivity. That's an everyday event, but I'm pleased with how we've executed on the portfolio of transformation. I'm pleased with how we've executed on the Exelis integration, the investments we made in R&D to position ourselves for growth at the time when the budgets are inflecting. So I think all things are looking very positive for the company.

Peter John Skibitski - *Drexel Hamilton, LLC, Research Division - Senior Equity Research Analyst*

I'll just ask one quick program question. I'm not sure if you mentioned about this. This new one, the SOCOM Wideband HF Manpack, do you have kind of a sense of the schedule for that program?

William M. Brown - *Harris Corporation - Chairman, CEO and President*

It's going to follow the SOCOM Manpack program which we are now in -- we put in our final offer very, very recently. We expected award on that, this summer. The HF program will come behind that. It's part of 3 different programs for SOCOM, handheld demand pack and the HF radio that it's been estimated will be $900 million of opportunity. Obviously, we won the sole source single -- 2-channel handheld. We're in the mix on the Manpack. And frankly, on the HF side, that's a position where we've launched some products recently with NSA certification. We have a very, very high share of the global market on HF, so we feel very good about our prospects on that radio as well. More to come as we get to the Manpack.

Operator

And our next question comes from the line of Howard Rubel of Jefferies.

Howard Alan Rubel - *Jefferies LLC, Research Division - MD and Senior Equity Research Analyst of Aerospace and Defense Electronics*

Bill, now that you've finished with -- or you've largely finished with Exelis, I recognize you don't rest and you're going to do something next. How do you end this other reshaping of the enterprise. So how do you think about some of the operating targets that you won? And where do you expect you might be able to find some incremental synergies or other operational efficiencies in the enterprise?

William M. Brown - *Harris Corporation - Chairman, CEO and President*

Well, look, I mean in terms of just our focus right now is delivering against guidance here in '17 and making sure that we're set up to deliver growth in top line and bottom line in cash next year and capture all of the opportunities that we think we can capture within the budget as they're being shaped. I really like where the portfolio happens to be. Going back 5 years, they think the step we took to invest more in IRAD, when most people were pulling back, if you just go back 5 years, we're up about $100 million a year incrementally in IRAD , in this company and that is in all the different franchise programs that we're now set up to perform on. In fact, a lot of the wins we're seeing come from some of the investments we've made over the last 3 to 5 years. So I feel very good about where we happen to be. There is always more to do on the cost side, as I mentioned a minute ago. Our operational excellence agenda is maturing. We're sort of 4, 5 years into it with a decade-long journey. There's lots of more things that we can do including streamlining and simplifying a lot of our systems across the company. So there's a lot more that we can do. I think we're set up to continue to perform into the future.

Rahul Ghai - *Harris Corporation - CFO and SVP*

And just to add to that Howard, where we're focused on the Exelis side is driving integration. I think the next part of this journey would be taking this HBX culture that builds in driving on the legacy Harris side now into Exelis, and we see some really good opportunities to continue to simplify operations and streamline the business there on the Exelis side. So that's the some (inaudible) opportunity from the Exelis side going forward as well.

Howard Alan Rubel - *Jefferies LLC, Research Division - MD and Senior Equity Research Analyst of Aerospace and Defense Electronics*

I mean -- I think the SENSOR program is probably one of the best examples of that whole process, and my guess also is moving Fort Wayne to Rochester is similar. Just as a follow-up on -- now that you're -- just on 2 products, one on FAA. As you transition to ADS-B to maintenance, I mean I believe you have the opportunity to sell the data, and then also could you just talk for a moment about the evolution of GPS III and the opportunities there?

William M. Brown - *Harris Corporation - Chairman, CEO and President*

Yes, sure. Let me start with on the FAA side. So you're right. I mean the ADS-B system that we owned about 640, 650 towers. It was built by the Exelis team. That buildout is complete. It's now in a sustainment mode and we do own the data rights on ADS-B. The equipage today and I think it's just over 2000 aircraft right now, so it's not -- and all the aircraft have to be fully equipped by early 2020, so we're still on the front end of the evolution of that business and that marketplace. I think where there's an opportunity going forward is now trying to use those -- that broad array of towers to enable the UAS into -- UAVs into the North American airspace system. That I think could be an important and distinctive technology for allowing UAVs into NAS. I think there's some encouragement on that piece. On GPS III, as you know, Howard, we're under contract for space vehicles 1 through 10. 9 and 10 were awarded late last year. For long lead materials, we see some other opportunities for 9 and 10 coming up very shortly maybe this quarter. 11 through 32 is being competed. It's a 2-phase process. There's 3 different bidders on that. We partnered up with Lockheed who will provide the payload today on GPS III. So again, it's in 2 phases. There's a first phase, the production readiness with some small amount of money and then it goes to a more substantial competition. I think the award is some time out in the spring of 2019 and it's likely to be of those 20 space vehicles, 10 award, maybe 10 auctioned. We are developing a fully digital payload for that, so it's not -- we'll provide today to GPS III not fully digital but we're investing in that and we expect it to be a player and supporter for Lockheed on 11 through 32.

Operator

And our next question comes from the line of Gautam Khanna of Cowen and Company.

Gautam J. Khanna - *Cowen and Company, LLC, Research Division - MD and Senior Analyst*

I was wondering if you could talk a little bit more about the Australia award and how quickly you expect it to convert to revenue, a. B, given you now have more color on the scope, what the anticipated margin profile of that program's going to be relative to the rest of the legacy tactical comps?

William M. Brown - *Harris Corporation - Chairman, CEO and President*

Look, the Australia program, first of all, is we've been into some very detailed negotiations with them. For some period of time, we're in the Phase 3 of a multi-year phase. It's a broader systems offering. We have a number of people on our team. I mean again, we're expecting an award on this, an order booking towards the end of our fiscal year. It'll be again $250 million to $300 million. We'll see revenue flowing off on that program over the next, probably, 3 years or so. The margins are, I think pretty strong. So I don't really want to say specifically where we happen to be, but they remain pretty strong in that program and really any of the systems programs that we have to have inside the company. So I don't see any sort of the pressure on the CS segment going forward because of the Australia margins.

Gautam J. Khanna - *Cowen and Company, LLC, Research Division - MD and Senior Analyst*

Okay. And so to your point, though, it will deliver over 3 years. It's not like a quick turn type of order.

Rahul Ghai - *Harris Corporation - CFO and SVP*

It would be. Gautam, it's something that -- the pieces, there are 2 pieces, the system integration and then providing the radios as well in that order. So yes, I think we should be able to get revenue from that in 2018.

Gautam J. Khanna - *Cowen and Company, LLC, Research Division - MD and Senior Analyst*

Okay. Secondly, could you give us -- in prior periods, you've sometimes given your pipeline figures for DoD and the international RF tactical. Do you have those numbers?

Rahul Ghai - *Harris Corporation - CFO and SVP*

Yes. So on the international side, Gautam, our pipeline is pretty steady. I mean it's around the same $2.4 billion-ish where it has been. It kind of keeps moving in and out with opportunities coming, so there's really not a lot of change to the international pipeline and the typical areas that it comes from is also kind of the same -- it all continues to be one of our bigger opportunities and then Australia, we're still tracking that. As we mentioned before, that's a -- long term that's about $1 billion opportunity obviously, the upfront award. So the geographical distribution has not changed much. The size overall has not changed much. And I think on the DoD, the pipeline is up slightly over where we were. I think -- and it's now kind of north about $1.2 billion, $1.3 billion, and so that's where I think -- that's up where we were last time.

Gautam J. Khanna - *Cowen and Company, LLC, Research Division - MD and Senior Analyst*

Okay. And on Iraq, in prior years, I remember I think it was a December quarter, a couple or a year ago, you had a $66 million order. Could you frame for us how big the Iraq opportunity still remains to be and what you anticipate booking in the next 12 months with Iraq?

William M. Brown - *Harris Corporation - Chairman, CEO and President*

We do see a couple of opportunities moving down the path in Iraq, Gautam. I mean I'm not sure, we'll give you specific to a country in the next couple of months. I mean I think just to step back a little bit, Iraq is still a very big opportunity in our large pipeline. Rahul just went through about $2.4 billion. Iraq is on the order of about $0.5 billion, so it's a very big opportunity. Those -- they're starting to move through the pipeline. I was very encouraged to see in the Omnibus, the continued support for, they call it now, counter ISIL train and equip but there's also an Iraq Train and Equip Fund that was set aside with substantial amount of money that expires at the end of this fiscal year. So by September, it was something like $300 million. So that remains good support by the U.S. government for equipping in Iraq. So we still see that to be a big opportunity and it's going to materialize over the next probably, couple of years, that's really the shape of our pipeline. I don't think I want to call it anytime in the next couple of months.

Gautam J. Khanna - *Cowen and Company, LLC, Research Division - MD and Senior Analyst*

And just last one, do you have any preliminary view on how much legacy or a tactical could grow in fiscal '18?

William M. Brown - *Harris Corporation - Chairman, CEO and President*

I don't think we're going to comment on '18 as a whole or even a specific subsegment of the company. As we said before, we do expect that '18 will be a growth year and -- for the company and I'll leave it at that. I think you can see the trends in what's happening in the DoD budgets and where we happen to be as a DoD tactical business, but I don't think we'll comment on a specific business until we get out and close on '17 and shape the whole company.

Operator

And our next question comes from the line of Seth Seifman of JP Morgan.

Seth Michael Seifman - *JP Morgan Chase & Co, Research Division - Senior Equity Research Analyst*

Bill, I heard you say that you're still expecting a selection on Manpack in this summer. You're still expecting orders and shipments by late in the calendar year?

William M. Brown - *Harris Corporation - Chairman, CEO and President*

Yes, Seth, there's 2 -- I use the word Manpack loosely, there's 2 Manpacks. One is one for SOCOM. We have put in our final proposal. The award we expected this summer, it will go into a developing phase and we see revenue coming off of that more likely in our fiscal '19, not '18. On the Army Manpack, is now into customer testing and there's 3 vendors on that. We think our offering has performed and performing very, very well. The Army has recently told us that there will be now 2 steps. They expect that they're going to have an interim field-based risk reduction step in order to verify some of those deferred threshold requirements, and we expect an order of about 150 units more or less in our fourth quarter. Same would have to the other 2 players in this space. It will get delivered at the end of the calendar year or going through some additional testing. And then what now they're expecting is that there will be an order for now up to 6 (inaudible) the BCTs versus the original 2 that will be split between 2 vendors. So it's a total of 3,800 radios, 1,900 a piece. That will be awarded sometime in the February or March of calendar '18 period which will be revenue for us as being one of the 2 vendors at the back end of our fiscal '18. So a little bit of a shift on the Army Manpack program, again, very, very encouraging that the testing goes on. We're performing very well. The money is in the budget, which is very encouraging, what we saw in the Omnibus, as well as a substantial increase in the number of BCTs that are going to be fielded by the Army from the Manpack program. So I think that's very encouraging news to us.

Seth Michael Seifman - *JP Morgan Chase & Co, Research Division - Senior Equity Research Analyst*

That's very helpful. And second question on air traffic control, how do you think about the impact of potential privatization on Harris? Or is there any impact?

William M. Brown - *Harris Corporation - Chairman, CEO and President*

Yes. Well, Seth, look -- thanks for that question. The FAA is one of our biggest customers across the company. It's more than $0.5 billion. It's a very large partnership, significant partnership that we've had with them and it's been -- for the last couple of decades. As you know, we have the base FTI program which has been very stable, it's been for a long period of time performing exceptionally well and then in a number of NextGen programs. I think -- look, there's been a lot of debate. It's not a new debate. It's been happening over the last, probably, couple of decades. I think what's different now is it appears the administration is now getting behind privatization. I think if it goes in that direction, the transition period is probably at least 5 years because of the size and complexity of the FAA system, the North American air traffic control system. So I think it's a multi-year transition. We don't think that there's going to be any near-term impact, mainly because the programs that were on are essential programs. There's very strong support for the NextGen programs including in the recent omnibus. All of the airlines even support the NextGen programs. So we feel very good that we will not be impacted certainly not anytime in the near term by any discussion on privatization, but I can tell you there's a lot of distance between now and having that finally approved. There's a lot of different voices in this including from the general aviation community, the DoD. A lot of people have airports in their backyard that won't going to be impacted. And so a lot of room between now and something being definitized on privatization. So we'll watch and see how it plays out and we'll keep you posted on it.

Operator

And our next question comes from the line of Robert Stallard of Vertical Research.

Robert Alan Stallard - *Vertical Research Partners, LLC - Partner*

Bill, you mentioned that there have been some impact of the CR in the quarter. It might be tough, but can you sort of size what you think the impact could have been across your various businesses over the last 3 months? And then perhaps, more importantly, when you think you could be called back up?

William M. Brown - *Harris Corporation - Chairman, CEO and President*

We calibrated pretty well in the year based on the CR, so we felt our tactical business was well calibrated and coming in today keeping the DoD about flat for the year sort of a testament of that, it was recently well calibrated. In our Electronic Systems business, we have our wireless products. It's more of a short-term product type business, has seen a little bit of the impact but not enough to take us off our game in Electronic Systems. So we feel that our business and where we happen to be, has been well calibrated. We originally guided at the beginning of the year flat to down 2 as a company and now we're down about 1. So we're right in the middle of the range. So I think we have been well calibrated and I think that remains the same today.

Robert Alan Stallard - *Vertical Research Partners, LLC - Partner*

Okay, and then a quick follow-up on the numbers. It looks like the Exelis integration costs have moved up a little by $5 million for the full year. I was wondering if you could comment on what's behind that. And then looking into next year what sort of level of integration costs you might be expecting for the next 12 months.

William M. Brown - *Harris Corporation - Chairman, CEO and President*

Most of the integration costs are going to be behind us by the end of the year. The total for the program is about $250 million. Most of that is now spent. Net is going to be about $200 million. So it's up a little bit. It was $35 million and now it's about $40 million. It's restructuring. It's integration costs and a little bit of the other restructuring around the stranded cost reduction activities but we think we're pretty well captured in that $40 million estimate.

Rahul Ghai - *Harris Corporation - CFO and SVP*

So just to make a final point on that, Rob, the step-up is not due to Exelis integration costs going up. But we had mentioned last quarter that as we're taking some stranded costs, or there'll be some restructuring cost, that will lead to spend to get the stranded costs out, and that's what you see the change from $35 million to $40 million.

Robert Alan Stallard - *Vertical Research Partners, LLC - Partner*

Okay, and then any more of this activity still to go on next fiscal year?

Rahul Ghai - *Harris Corporation - CFO and SVP*

We should be pretty much done by the end of this fiscal year, so we do not expect any integration costs too for next year.

Operator

And our next question comes from the line of Josh Sullivan of Seaport Global.

Joshua Ward Sullivan - *Seaport Global Securities LLC, Research Division - Director of Aerospace and Defense and Engineered Materials and Senior Industrials Analyst*

Just on international radios, I guess particularly in Europe. I know you mentioned Eastern Europe is a source of strength, but are you seeing any increased fly activity from other core NATO allies, maybe as they look to increase defense spending?

Rahul Ghai - *Harris Corporation - CFO and SVP*

A little bit. It's not a lot we do. I think that directionally, it's -- the words from the administration are good as this pressure on NATO to spend more. We do see some incremental opportunities coming from our allies in Western Europe. We have a few small orders, nothing big at this point coming from Western Europe. And that market is fairly stable year-over-year, so not a lot of change on the Western Europe side.

William M. Brown - *Harris Corporation - Chairman, CEO and President*

But over time, we know that there will be a substantial upgrade in the U.K., this Morpheus program, and we're going to be right in the middle of that. There's been some recent progress on that. That is going to move forward. It's probably not in the next 2 years but certainly in the next 3 or 4, where we'll be able to start to be some meaningful revenue for Harris and that now will happen, that's going to be a big opportunity. It was estimated at GBP 3.5 billion total upgrade. About 20%, 25% is going to be radio. So we think, we've got a good position on that because of 50 -- 40,000 radio there today, legacy radios, so good opportunity for us. Over time, it's probably not the back end of the 3-year period that we're thinking about when it's going to start to hit us.

Joshua Ward Sullivan - *Seaport Global Securities LLC, Research Division - Director of Aerospace and Defense and Engineered Materials and Senior Industrials Analyst*

And then just on electronic warfare. You mentioned some expectations for growth, but how do you balance between maybe some of the legacy programs and the F-35? If there were any changes to production volumes on either legacy programs or the F-35, are you more exposed one way or the other?

William M. Brown - *Harris Corporation - Chairman, CEO and President*

I think more broadly sort of electronic warfare we do have substantial content on F-35. It's not EW system, it's on F-35, so very substantial content with opportunities to grow that content over time because we're performing very, very well. As there's a broad multi-year drive in the DoD towards open systems, we do have some opportunities to perhaps get a little more content there. We also have significant content with the F-18. So if there is a contemplation certainly in the omnibus of additional F-18 aircraft, that works for us. We do have the IDECM system for the defense electronic countermeasure system before the F-18, so that will be good news for us. And then what we're seeing is across all of the legacy platforms, because of new threats, all of the legacy platforms both fixed wing and rotary need to be upgraded, and we've got strong positions on many of those platforms, and that's really what's behind a lot of the strong order growth in revenue growth now in electronic warfare.

Operator

I'm showing no further questions at this time.

Anurag Maheshwari

Thank you again for joining us on the call today, everyone. If any additional questions, I'm available at 321-727-9383. Thank you again and have a great day.

William M. Brown - *Harris Corporation - Chairman, CEO and President*

Thank you, everybody.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This concludes today's program. You may all disconnect. Everyone have a great day.
