

LEIDOS 4Q FY14

# Earnings Conference Call

March 27, 2014



# Forward-Looking Statements

Certain statements in this presentation contain or are based on "forward-looking" information within the meaning of the Private Litigation Reform Act of 1995. In some cases, you can identify forward-looking statements by words such as "expects," "intends," "plans," "anticipates," "believes," "estimates" and similar words or phrases. Forward-looking statements in this presentation include, among others: estimates of future revenues, operating income, cash flow, growth and profitability as well as statements about future regular or special dividends, stock repurchases and other anticipated uses of capital. These statements reflect our belief and assumptions as to future events that may not prove to be accurate.

Actual performance and results may differ materially from the forward-looking statements made in these slides depending on a variety of factors, including: developments in the U.S. Government defense budget, including budget reductions, implementation of spending cuts (sequestration) or changes in budgetary priorities; delays in the U.S. Government budget process or approval to raise the U.S. debt ceiling; delays in the U.S. Government contract procurement process or the award of contracts; delays or loss of contracts as a result of competitor protests; changes in U.S. Government procurement rules, regulations and practices; our compliance with various U.S. Government and other government procurement rules and regulations; governmental reviews, audits and investigations of our company; our ability to effectively compete and win contracts with the U.S. Government and other customers; our ability to attract, train and retain skilled employees, including our management team, and to obtain security clearances for our employees; our ability to accurately estimate costs associated with our firm-fixed-price and other contracts; our ability to comply with certain agreements entered into in connection with the CityTime matter; cybersecurity, data security or other security threats, systems failures or other disruptions of our business; resolution of legal and other disputes with our customers and others or legal or regulatory compliance issues; our ability to effectively acquire businesses and make investments; our ability to maintain relationships with prime contractors, subcontractors and joint venture partners; our ability to manage performance and other risks related to customer contracts, including complex engineering or design build projects; our ability to profitably operate and recover our investment in the Plainfield Renewable Energy Project; the failure of our inspection or detection systems to detect threats; the adequacy of our insurance programs designed to protect us from significant product or other liability claims; our ability to manage risks associated with our international business; our ability to declare future dividends based on our earnings, financial condition, capital requirements and other factors, including compliance with applicable laws and contractual agreements; risks associated with the recently completed spin-off of our technical, engineering and enterprise information technology services business, such as disruption to business operations or a failure to realize the expected benefits of the spin-off; our ability to execute our business plan and long-term management initiatives effectively; and to overcome these and other known and unknown risks that we face. These are only some of the factors that may affect the forward-looking statements contained in these slides. For further information concerning risks and uncertainties associated with our business, please refer to the filings we make from time to time with the U.S. Securities and Exchange Commission.

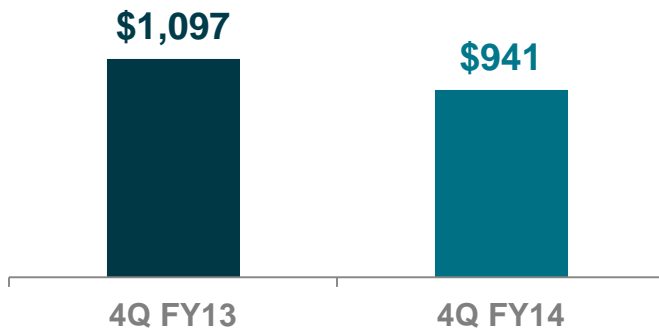
All information in this presentation is as of March 27, 2014. The Company expressly disclaims any duty to update the forward-looking statements provided in this presentation to reflect subsequent events, actual results or changes in the Company's expectations. The Company also disclaims any duty to comment upon or correct information that may be contained in reports published by investment analysts or others.

# Executive Summary

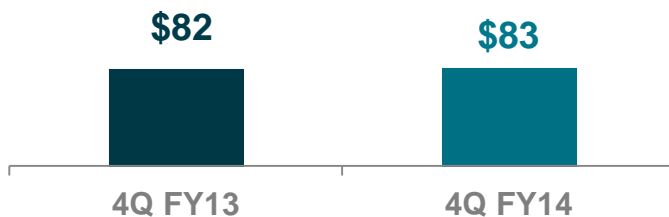
- ▶ Sequestration, delayed decisions, and the high level of protest activity continues to weigh on our results
- ▶ Despite these pressures, we remain positive on Leidos prospects:
  - Focused on organic growth
  - Capitalizing on new markets / no longer limited by OCI conflicts
  - Portfolio shaping
  - Low capital intensity, low pension obligations & strong cash generation
  - Continuous improvement to drive down costs
- ▶ Serve three markets National Security, Health & Engineering
- ▶ Management transition
- ▶ Leidos returned ~ 20% of equity market capitalization through dividend, special dividend and share repurchase in FY14
- ▶ Our commitment to capital deployment remains steadfast

# National Security Solutions – Overview

## Revenue (\$M)



## Operating Income (\$M)



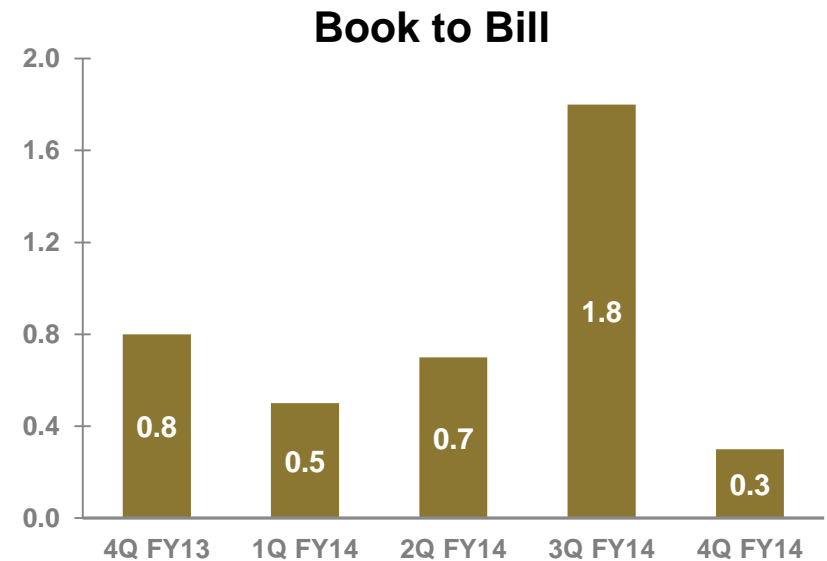
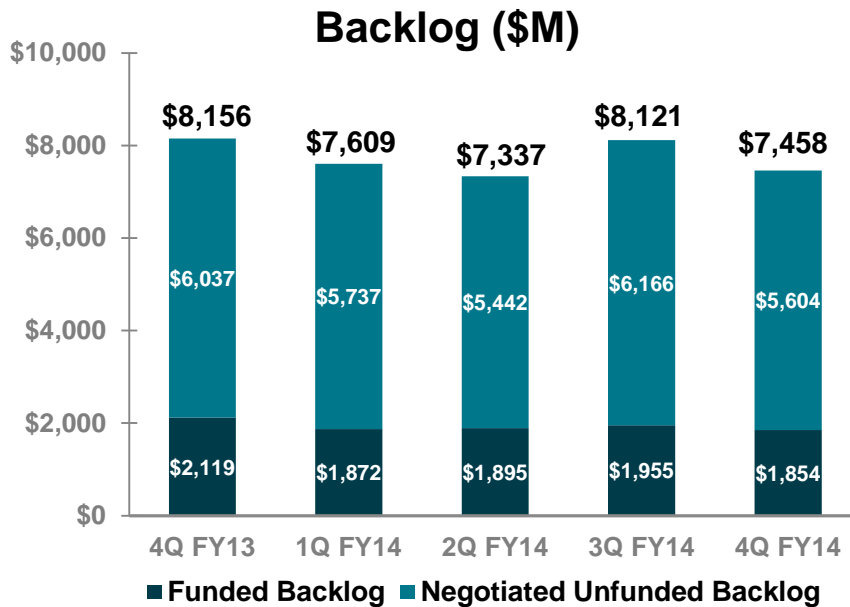
Revenue decline of \$156M, or 14%, driven by:

- ▶ Overseas drawdown (\$65M), including completion of JLI contract
- ▶ The completion of several intelligence contracts (\$21M)
- ▶ Funding reductions, partially offset by program wins

Operating income increase of \$1M

- ▶ Cost reductions effort
- ▶ Portfolio shaping initiatives
- ▶ Improved profit performance on existing contracts

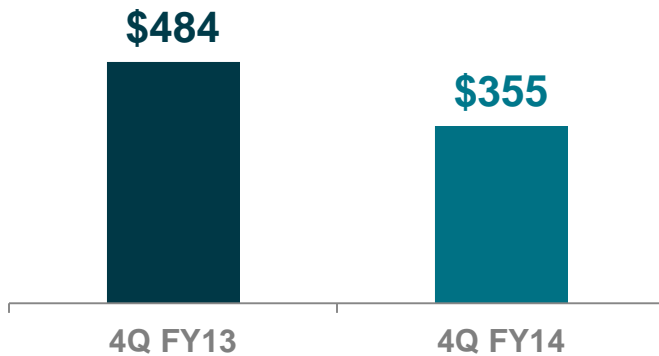
# National Security Solutions – Awards & Backlog



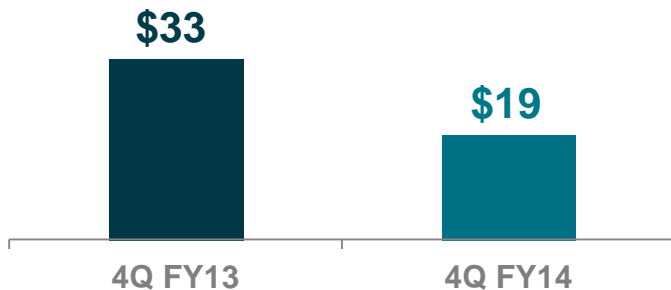
- ▶ Book to bill 0.3x for 4Q14 and 0.8x for FY14: 4Q historically low book-to-bill
  - \$4B C2 WMD R&D IDIQ (expected Leidos value \$800M)
  - Unconstrained/non-OCI markets now constitute half of qualified pipeline
  - Win Rate for FY14 – 59%

# Health and Engineering – Overview

## Revenue (\$M)



## Operating Income (\$M)



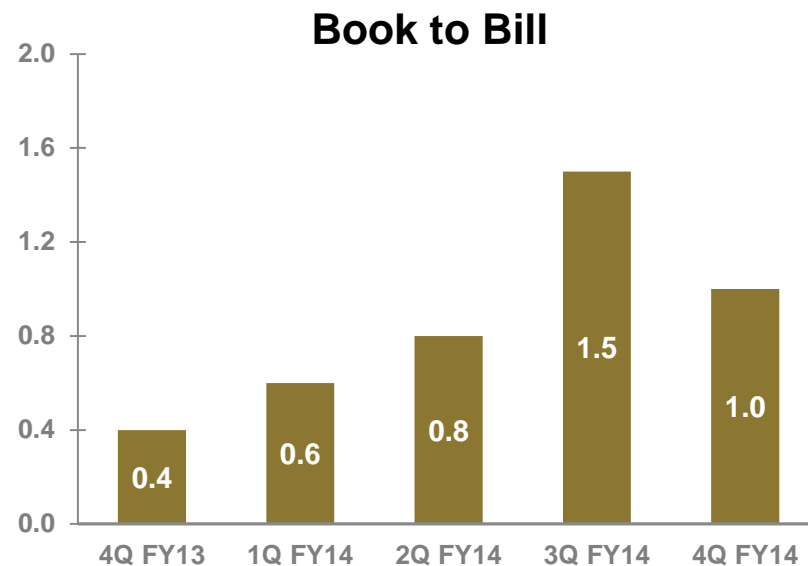
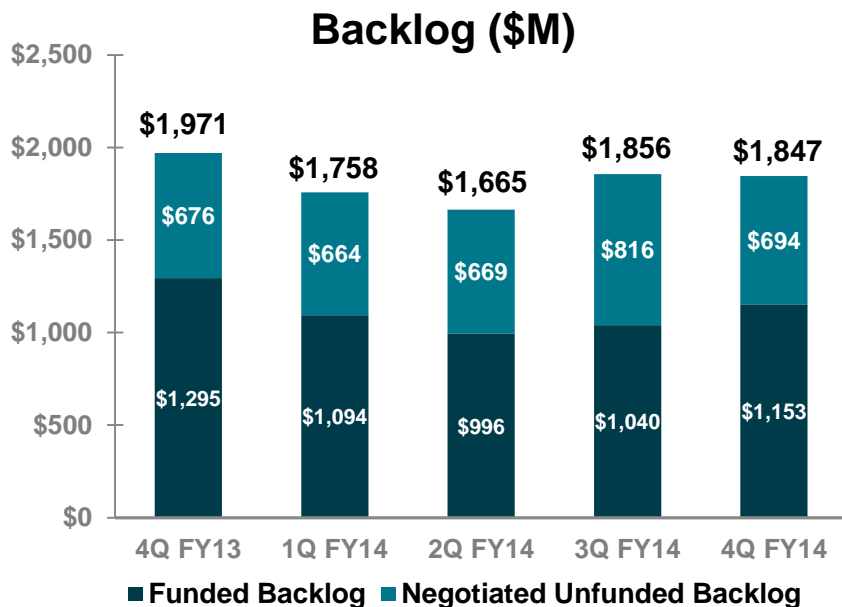
Revenue decline of \$129M, or 27%, driven by:

- ▶ Completion of energy design-build construction projects (\$52M)
- ▶ Sequestration impact on commercial health (\$23M)
- ▶ Timing of secure commerce product deliveries (\$19M)
- ▶ Engineering (\$8M) and design build (\$18M)

Operating income declined \$14M driven by:

- ▶ Lower revenue volumes
- ▶ Plainfield start-up costs (\$4M)
- ▶ Legal settlement (\$4M)

# Health and Engineering – Awards & Backlog



► **Book to bill 1.0x for 4Q14 and 0.9x for FY14:**

- \$243M multiple-award IDIQ for the National Guard Bureau
- \$83M three additional contracts for LSB Industries Ammonia Plant Relocation (Commercial Engineering)
- \$16M three contracts for Department of Veterans Affairs

# Profit and Loss

*\$ in millions, except for EPS*

	4Q14	4Q13	% chg.
<b>Revenues</b>	1,295	1,580	-18%
Cost of revenues	1,110	1,351	-18%
Selling, general and administrative expenses	97	125	-22%
Bad debt expense	(1)	2	
Separation transaction and restructuring expenses	7	11	
<b>Operating income</b>	82	91	-10%
<i>As a % of sales</i>	6.3%	5.8%	
Net interest	(24)	(16)	
Other income, net	(11)	0	
Income from continuing operations before income taxes	47	75	-37%
Income tax benefit (expense)	0	73	
<b>Income from continuing operations</b>	47	148	-68%
<b>Diluted EPS from continuing operations</b>	\$ 0.56	\$ 1.73	-68%



# Leidos Fiscal Year 2015 Guidance

	<b>FY15 Guidance</b>
Revenue	\$4.9B to \$5.1B
Non-GAAP Diluted EPS*	\$2.35 to \$2.55
Cash Flow from Continuing Operations	At or above \$350M

\* For a definition of Non-GAAP Diluted EPS please see slide 18

# Appendix

# Working Days per Quarter

	Q1	Q2	Q3	Q4	Year Total
FY15	64	63	64	60	251
FY14	65	63	64	60	252
Increase / (Decrease)	(1)	0	0	0	(1)

# Non-GAAP Reconciliations

This presentation includes certain non-GAAP financial measures, such as operating income, operating margin, and earnings per share. These non-GAAP financial measures are not meant to be considered in isolation or as a substitute for results prepared in accordance with generally accepted accounting principles in the United States (GAAP). A reconciliation of non-GAAP financial measures included in this presentation to the most directly comparable financial measure calculated and presented in accordance with GAAP accompanies this presentation and is on our website at [www.Leidos.com](http://www.Leidos.com). Leidos management believes that these non-GAAP financial measures provide useful information to investors regarding the Company's financial condition and results of operations as they provide another measure of the Company's profitability, and are considered important measures by financial analysts covering Leidos and its peers.

# Revised Historical Financials – Income Statement

	1Q13	2Q13	3Q13	4Q13	FY13	1Q14	2Q14	3Q14	4Q14	FY14
<b>Revenue</b>	<b>\$ 1,598</b>	<b>\$ 1,623</b>	<b>\$ 1,668</b>	<b>\$ 1,580</b>	<b>\$ 6,469</b>	<b>\$ 1,597</b>	<b>\$ 1,462</b>	<b>\$ 1,418</b>	<b>\$ 1,295</b>	<b>\$ 5,772</b>
Cost of revenue	1,387	1,394	1,432	1,351	5,564	1,377	1,296	1,223	1,110	5,006
Selling, general and administrative expenses	95	118	131	125	469	126	106	113	97	442
Bad debt expense	-	-	-	2	2	2	-	43	(1)	44
Intangible asset impairment charges	-	-	-	-	-	2	30	19	-	51
Separation transaction and restructuring expenses	-	-	-	11	11	14	19	25	7	65
<b>Operating income (loss)</b>	<b>\$ 116</b>	<b>\$ 111</b>	<b>\$ 105</b>	<b>\$ 91</b>	<b>\$ 423</b>	<b>\$ 76</b>	<b>\$ 11</b>	<b>\$ (5)</b>	<b>\$ 82</b>	<b>\$ 164</b>
Non-Operating income (expense):										
Interest income	2	2	1	4	9	4	6	5	-	15
Interest expense	(28)	(25)	(20)	(20)	(93)	(20)	(18)	(21)	(24)	(83)
Other income (expense), net	1	5	2	-	8	1	-	2	(11)	(8)
Income (loss) from continuing operations before income taxes	91	93	88	75	347	61	(1)	(19)	47	88
Income tax (expense) benefit	(34)	(32)	(30)	73	(23)	(21)	6	11	-	(4)
<b>Income (loss) from continuing operations</b>	<b>\$ 57</b>	<b>\$ 61</b>	<b>\$ 58</b>	<b>\$ 148</b>	<b>\$ 324</b>	<b>\$ 40</b>	<b>\$ 5</b>	<b>\$ (8)</b>	<b>\$ 47</b>	<b>\$ 84</b>
<b>Diluted earnings (losses) per share from continuing operations</b>	<b>\$ 0.67</b>	<b>\$ 0.72</b>	<b>\$ 0.70</b>	<b>\$ 1.73</b>	<b>\$ 3.82</b>	<b>\$ 0.43</b>	<b>\$ 0.06</b>	<b>\$ (0.10)</b>	<b>\$ 0.56</b>	<b>\$ 0.98</b>
<b>Diluted weighted average number of share outstanding</b>	<b>83</b>	<b>83</b>	<b>83</b>	<b>84</b>	<b>83</b>	<b>84</b>	<b>84</b>	<b>84</b>	<b>84</b>	<b>83</b>

# Historical Financials – Segment Income Statement

	1Q13	2Q13	3Q13	4Q13	FY13	1Q14	2Q14	3Q14	4Q14	FY14
<b>Health &amp; Engineering Segment</b>										
Revenue	\$ 416	\$ 417	\$ 508	\$ 484	\$ 1,825	\$ 521	\$ 451	\$ 408	\$ 355	\$ 1,735
Operating Income	\$ 31	\$ 29	\$ 47	\$ 33	\$ 140	\$ 35	\$ (3)	\$ (30)	\$ 19	\$ 21
<b>National Security Segment</b>										
Revenue	\$ 1,184	\$ 1,208	\$ 1,161	\$ 1,097	\$ 4,650	\$ 1,077	\$ 1,019	\$ 1,012	\$ 941	\$ 4,049
Operating Income	\$ 93	\$ 102	\$ 83	\$ 82	\$ 360	\$ 71	\$ 72	\$ 66	\$ 83	\$ 292
<b>Corporate</b>										
Revenue	\$ (1)	\$ -	\$ -	\$ -	\$ (1)	\$ -	\$ (7)	\$ (1)	\$ (1)	\$ (9)
Operating Income	\$ (8)	\$ (20)	\$ (25)	\$ (24)	\$ (77)	\$ (30)	\$ (58)	\$ (41)	\$ (20)	\$ (149)
<b>Elimination</b>										
Revenue	\$ (1)	\$ (2)	\$ (1)	\$ (1)	\$ (5)	\$ (1)	\$ (1)	\$ (1)	\$ -	\$ (3)
Operating Income	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
<b>Total Continuing Operations</b>										
Revenue	\$ 1,598	\$ 1,623	\$ 1,668	\$ 1,580	\$ 6,469	\$ 1,597	\$ 1,462	\$ 1,418	\$ 1,295	\$ 5,772
Operating Income	\$ 116	\$ 111	\$ 105	\$ 91	\$ 423	\$ 76	\$ 11	\$ (5)	\$ 82	\$ 164

# Non-GAAP Operating Income Reconciliation

	1Q13	2Q13	3Q13	4Q13	FY13	1Q14	2Q14	3Q14	4Q14	FY14
Revenue	\$ 1,598	\$ 1,623	\$ 1,668	\$ 1,580	\$ 6,469	\$ 1,597	\$ 1,462	\$ 1,418	\$ 1,295	\$ 5,772
<b>Operating income (loss) from continuing operations</b>	<b>\$ 116</b>	<b>\$ 111</b>	<b>\$ 105</b>	<b>\$ 91</b>	<b>\$ 423</b>	<b>\$ 76</b>	<b>\$ 11</b>	<b>\$ (5)</b>	<b>\$ 82</b>	<b>\$ 164</b>
Intangible asset impairment charges	-	-	-	-	-	2	30	19	-	51
Separation transaction and restructuring expense	-	-	-	11	11	14	19	25	7	65
Impact of Plainfield	-	-	6	4	10	3	14	32	-	49
<b>Non-GAAP operating income from continuing operations</b>	<b>\$ 116</b>	<b>\$ 111</b>	<b>\$ 111</b>	<b>\$ 106</b>	<b>\$ 444</b>	<b>\$ 95</b>	<b>\$ 74</b>	<b>\$ 71</b>	<b>\$ 89</b>	<b>\$ 329</b>

Note: Please see description of non-GAAP Operating Income on slide 17

# Revised Non-GAAP EPS Reconciliation

	1Q13	2Q13	3Q13	4Q13	FY13	1Q14	2Q14	3Q14	4Q14	FY14
<b>GAAP income (loss) from continuing operations</b>	\$ 57	\$ 61	\$ 58	\$ 148	\$ 324	\$ 40	\$ 5	\$ (8)	\$ 47	\$ 84
Intangible asset impairment charges	-	-	-	-	-	2	30	19	-	51
Separation transaction and restructuring expenses	-	-	-	11	11	14	19	25	7	65
Impact of Plainfield	-	-	6	4	10	3	14	32	12	61
<b>Total non-GAAP adjustments</b>	\$ -	\$ -	\$ 6	\$ 15	\$ 21	\$ 19	\$ 63	\$ 76	\$ 19	\$ 177
Adjustment to the income tax provision to reflect non-GAAP adjustments*	-	-	(2)	(5)	(7)	(7)	(22)	(26)	(7)	(62)
Significant tax adjustment for CityTime settlement	-	-	-	(96)	(96)	-	-	-	-	-
<b>Non-GAAP net income from continuing operations</b>	\$ 57	\$ 61	\$ 62	\$ 62	\$ 242	\$ 52	\$ 46	\$ 42	\$ 59	\$ 199
<b>GAAP diluted earnings (losses) per share from continuing operations</b>	\$ 0.67	\$ 0.72	\$ 0.70	\$ 1.73	\$ 3.82	\$ 0.43	\$ 0.06	\$ (0.10)	\$ 0.56	\$ 0.98
Total adjustments from non-GAAP net income, above**	\$ -	\$ -	\$ 0.05	\$ (1.03)	\$ (0.98)	\$ 0.14	\$ 0.49	\$ 0.60	\$ 0.14	\$ 1.39
<b>Non-GAAP diluted earnings per share from continuing operations</b>	\$ 0.67	\$ 0.72	\$ 0.75	\$ 0.70	\$ 2.84	\$ 0.57	\$ 0.55	\$ 0.50	\$ 0.70	\$ 2.37
<b>Diluted Shares</b>	83	83	83	84	83	84	84	84	84	83

\* Calculation uses an effective tax rate of 35% on non-GAAP adjustments.

\*\* Adjustments calculated by dividing non-GAAP net income from continuing operations by weighted average diluted shares. This calculation excludes the impact of the allocation of distributed and undistributed earnings to participating securities.

Note: Please see description of non-GAAP EPS on slide 18





# Non-GAAP Reconciliations

**Non-GAAP Operating Income** is a non-GAAP financial measure that is reconciled to the most directly comparable GAAP financial measure, operating income. Non-GAAP operating income adjusts operating income for the following discrete items:

- ▶ **Separation transaction and restructuring expenses** – This adjustment represents costs for strategic advisory services, legal and accounting services, lease termination and facility consolidation and severance costs associated with our recent spin-off and headquarter relocation.
- ▶ **Plainfield** – This adjustment represents the write-down of \$32 million taken as part of cancelling our outstanding accounts receivable in exchange for the assets of the Plainfield Plant in 3Q14, and estimate-at-completion adjustments related to the Plainfield project taken in 3Q13, 4Q13, 1Q14 and 2Q14.
- ▶ **Impairments** – This adjustment represents impairments of long-lived assets due to changes in actual performance against performance projected when the long lived assets were acquired.

# Non-GAAP Reconciliations (continued)

**Non-GAAP Earnings Per Share** is a non-GAAP financial measure that is reconciled to the most directly comparable GAAP financial measure, earnings per share. Non-GAAP earnings per share adjusts earnings per share for the following discrete items:

- ▶ **Separation transaction and restructuring expenses** – This adjustment represents costs for strategic advisory services, legal and accounting services, lease termination and facility consolidation and severance costs associated with our recent spin-off and headquarter relocation.
- ▶ **Plainfield** – This adjustment represents the write-down taken as part of cancelling our outstanding accounts receivable in exchange for the assets of the Plainfield Plant, and estimate-at-completion adjustments related to the Plainfield project. Plainfield refinancing charges of \$12 million incurred in 4Q14 are included in this amount.
- ▶ **Impairments** – This adjustment represents impairments of long-lived assets due to changes in actual performance against performance projected when the long lived assets were acquired.
- ▶ **Reversal of Tax Reserve** – This adjustment represents a \$96 million reversal of the tax reserve taken in 4Q13 for uncertain tax positions related to the CityTime settlement.



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