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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Huntington Ingalls Industries fourth-quarter earnings conference call.

(Operator Instructions)

As a reminder, this call is being recorded. I would now like to introduce your host for today's conference, Mr. Dwayne Blake, Vice President of Investor Relations. You may begin, sir.

Dwayne Blake - *Huntington Ingalls Industries Inc. - VP of IR*

Thanks, Ronya. Good morning, and welcome to the Huntington Ingalls Industries fourth quarter 2015 earnings conference call. With us today are Mike Petters, President and Chief Executive Officer; Barb Niland, Corporate Vice President of Business Management and Chief Financial Officer; and Chris Kastner, Corporate Vice President and General Manager of Corporate Development.

As a reminder, statements made in today's call that are not historical fact are considered forward-looking statements, and are made pursuant to the Safe Harbor provisions of federal securities law. Actual results may differ. Please refer to our SEC filings for a description of some of the factors that may cause actual results to vary materially from anticipated results.

Also in their remarks today, Mike and Barb will refer to certain non-GAAP measures, including certain segment and adjusted financial measures. Reconciliations of these metrics to the comparable GAAP measures are included in the Appendix of our earnings presentation that is posted on our website.

We plan to address the posted presentation slides during the call to supplement our comments. Please access our website at HuntingtonIngalls.com, and click on the Investor Relations link to view the presentation, as well as our earnings release. With that, I will turn the call over to our President and CEO Mike Petters. Mike?

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Thanks, Dwayne. Good morning, everyone, and thanks for joining us on today's call. This morning we released fourth quarter and full-year 2015 financial results that reflects solid operating margin performance and cash generation at Ingalls and Newport News, while our UniversalPegasus operations continue to be negatively impacted by extremely unfavorable market conditions.

2015 was a year of inflection, marking achievement of our goal of 9%-plus operating margin in the shipbuilding business, and the end of the first five years of operations since the spin-off. I want to thank each one of the 36,000 employees of Huntington Ingalls for their hard work and dedication that produced these results, and for the continuous commitment to safety, quality, cost, and schedule.

Now during the quarter, we had two events that reduced our GAAP earnings. First, we absorbed the $40- million, one-time cost to refinance our 10-year notes, which will significantly reduce our interest costs going forward. Second, we recorded a $16-million, non-cash goodwill impairment charge, and a $27-million, non-cash intangible asset impairment charge in our Other segment.

The impairments were driven by continued low crude oil prices, and a deterioration of market fundamentals in the oil and gas services industry. Note that fourth quarter 2014 results included similar impacts of $37 million to refinance our seven-year notes, and a $47-million, non-cash goodwill impairment charge.

2015 full-year results also included costs from early payment of our term loan in the third quarter, and a non-cash goodwill impairment charge in our Other segment, and favorable resolution of an insurance litigation matter at Ingalls in the second quarter. All comparative data that I discuss today are adjusted for these items, as well as the FAS/CAS adjustment.

For the quarter, sales of $1.9 billion were consistent with last year, and segment operating margin was 8.8%, down from 9.4% last year. For the full year, sales of $7 billion were 1% higher than 2014. Segment operating margin of 9% was consistently with 2014. Diluted EPS was $1.95 for the quarter, compared to $2.19 last year. Diluted EPS for the full year was $7.33, up from $7.14 last year.

Additionally, we received $700 million in new contract awards during the quarter, resulting in backlog of $22 billion at the end of the year, of which $11 billion is funded. Cash generation was particular strong again in the fourth quarter, with $309 million of free cash flow, which was down slightly from last year. We ended the year with approximately $900 million of cash on the balance sheet.

Since our third-quarter earnings call in November, the FY16 budget has been authorized and appropriated, and the president's FY17 budget request has been released. Within the 2016 budget, I want to point out a few highlights.

The final portion of funding was authorized and appropriated to support construction of the 12th LPD, LPD-28; and accelerate by two years' construction of the next-generation amphibious warship, LXR, that will be based upon the LPD. Funding was also authorized and appropriated for a ninth national security cutter. All of these actions are reflective of the broad support for the capabilities that these ships provide, and our ability to execute within the cost and schedule expectations of our customers.

The president's FY17 budget request marks the beginning of the process for Congress to consider shipbuilding priorities and investment for the next fiscal year. We were very pleased to see that the president requested funding for all key shipbuilding programs of record, including advanced procurement for the Ohio-class replacement program, continuation of CVN-79 Kennedy, and advanced procurement for CVN-80, Enterprise, which is the third Ford-class aircraft carrier.

The president also requested investment for the refueling overhaul of CVN-73 George Washington, and advanced procurement for the refueling overhaul of CVN-74 John C. Stennis; as well as two Virginia-class submarines, two DDG-51-class destroyers; LHA-8, which is the next big-deck amphibious warship; and TAOX, the next-generation fleet oiler.

We were also pleased to see substantial investment requested for a new Coast Guard icebreaker. We look forward to Congress considering all of these requests over the next several months. Now I will provide a few points of interest on our business segments.

At Ingalls, the LPD and NSC programs continue to perform very well, and are reaping the benefits of serial production, while the DDG and LHA programs remain on track. We expect contract awards for LPD-28 and NSC-9 later this year, and we look forward to continuing our outstanding track record of performance on these very important programs.

At Newport News, CVN-78 Ford achieved the milestone recognizing installation of over 14 million feet of electrical and fiber optic cable in January. This team is working through the test program in preparations for builders' trials in the second quarter, with delivery to follow. The Virginia-class submarine program continues to perform at a high level, while CVN-72 Lincoln and CVN-65 Enterprise continue on their paths to re-delivery to the customer expected at the end of this year and in the first half of next year, respectively.

As I mentioned earlier, UniversalPegasus recognized non-cash goodwill and purchased intangible asset impairment charges in the quarter. As you know, this is a tough time for the oil and gas industry, but we are continuing to take specific actions to right-size our operations for this dynamic environment, to position UPI for long-term success when the market turns.

In closing, I want to recap some of the accomplishments by our team in 2015. We delivered NSC-5 James at Ingalls, and SSN-785 John Warner at Newport News. Ingalls and Newport News generated segment operating margin above 9% for the second year in a row. Operating and free cash flow were the highest since the spin-off in 2011, and we were awarded $8 billion in new contracts, including detailed design and construction for CVN-79 John F. Kennedy, and construction of NSC-8 midget.

Looking ahead, we laid out the path to 2020 at our first Investor Day this past November. The path includes investing $1.5 billion in capital to strengthen and protect our core shipbuilding business, returning substantially all of our free cash flow to shareholders via dividend increases of at least 10% annually, and share repurchases; and leveraging our deep technical services competencies and nuclear operations expertise to optimize and expand our services portfolio.

I am excited about the possibilities these strategic initiatives provide for our employees, our customers, and our shareholders as we continue to create long-term sustainable value. I am confident that we have the right team in place to provide the leadership and focus necessary to execute these initiatives.

Now I have one other important duty to perform as part of this call, that of formally recognizing Barb's contribution to Huntington Ingalls, as she leaves us for retirement. Barb has been a full partner in all that we have accomplished, and someone I have had the pleasure of working directly with for the past 12 years. Her professionalism and pragmatism have been at the heart of our planning and execution. While we have great confidence in Chris, we will definitely miss Barb.

That concludes my remarks, and I will now turn the call over to Barb Niland for some remarks on the financials. Barb?

Barb Niland - *Huntington Ingalls Industries Inc. - Corporate VP of Business Management & CFO*

Thanks, Mike, for the kind words. It's been a privilege working for you, and representing the 36,000 employees of Huntington Ingalls Industries. Good morning, everyone on the call. Today I'm going to review our consolidated and segment results for the fourth quarter and full year. Then I will hand the call over to Chris Kastner, who will be taking the reins as the new CFO on March 1 to wrap up with some information on 2016.

As Mike mentioned, all of the numbers that I discussed today will be adjusted for the insurance litigation settlement, the non-cash goodwill and purchased intangible asset impairment charges, and the one-time expenses related to early extinguishment of debt. Please refer to the presentation on our website, or the earnings release from this morning, for more information and the detailed reconciliations.

Turning to the consolidated results on slides 4 and 5 of the presentation, and starting with the quarter, total revenues of $1.9 billion decreased 1.1% from the same period last year, due to lower volumes at UPI and Ingalls, partially offset by higher volumes at Newport News. Segment operating income of $167 million decreased $14 million from the fourth-quarter 2014, and segment operating margin of 8.8% decreased 63 basis points, due to lower risk retirement at Ingalls and lower performance at UPI.

Total operating income of $187 million decreased $4 million from the fourth quarter 2014, and total operating margin of 9.8% was down 10 basis points, as favorable FAS/CAS adjustment was offset by the lower segment margin at Ingalls and UPI.

For the full year, revenue increased 1.1% to just over $7 billion, driven by higher volumes at Newport News. Segment operating income of $633 million and segment operating margin of 9% were in line with 2014, as improved performance at Ingalls and Newport News was offset by the continued pressures at UPI.

Total operating income of $735 million increased $33 million, primarily due to favorable FAS/CAS adjustment. Total operating margin was 10.5%.

Moving on to cash flow, cash from operations was $411 million in the quarter, and free cash flow was $309 million. For the full year, cash from operations increased $112 million to $828 million, and free cash flow of $640 million increased $80 million over 2014. The increase was primarily due to the after-tax effect of the insurance litigation settlement in the second quarter and lower pension contributions.

Capital expenditures in the quarter increased $28 million to $102 million from the same period last year. For the full year, capital expenditures increased $23 million to $188 million from 2014.

Cash contributions to our pension and post-retirement benefits plans were $136 million in the year, of which $99 million were discretionary contributions to our qualified pension plans. Asset returns for the year was a negative 1%, and pension discount rates increased almost 40 basis points to 4.73% at the end of the year.

During the quarter, we re-purchased over 332,000 shares at a cost of $38 million, bringing the total number of shares re-purchased in the year to over 1.9 million, and at a cost of $234 million. In addition, we paid dividends in the quarter of $0.50 per share, or $24 million, bringing the total dividend paid for the year to $81 million.

Interest expense in the quarter was $64 million, and $137 million for the full year, and included $40 million and $44 million, respectively, of one-time expenses related to the early extinguishment of debt. This compares to interest expense in the fourth quarter of 2014 of $66 million, and $149 million for the full year, which also included $37 million of one-time expense for the early extinguishment of debt in both the quarter and the full year.

Our effective income tax rate in the quarter was 37.5%, compared to 34.2% in the fourth quarter of 2014. The increase was primarily driven by lower domestic manufacturing deductions year over year. For the full year, the tax rate was 36.1%, compared to 33.3% in 2014. The year-over-year increase was driven by the lower domestic manufacturing deductions and higher portions of goodwill impairment that were not amortizable for tax purposes.

Moving on to segment results, and starting with Ingalls on slides 6 and 7, revenues at Ingalls of $580 million in the quarter declined 4.6% from fourth quarter 2014, due to the deliveries of NSC-4 and NSC-5, and lower volumes on LPD-26. The decline in revenue was partially offset by higher volumes on the DDG program.

Operating margin of 10.2% in the quarter decreased 167 basis points from the fourth quarter of 2014, driven by lower risk retirement on the LPD program. For the full year, Ingalls generated revenues of $2.2 billion, which decreased 4.3% from 2014. Operating margin of 11% for the year increased 102 basis points from 2014, driven by higher performance on both the LHA-6 America class and NSC programs, as well as the favorable resolution of outstanding contract changes.

Turning to slide 8, revenues at Newport News of approximately $1.3 billion in the quarter increased 2.6% from the fourth quarter 2014, due to increased volumes on the VCS program, and in-fleet support services. Operating margin in the quarter of 9.3% was in line with the fourth quarter of 2014. For the full year, Newport News revenues of $4.7 billion increased 3.6%, and operating margin of 9% was similar to 2014.

Turning to the Other segment on slides 9 and 10, UPI generated an operating loss of $12 million on revenues of $29 million in the quarter, compared to an operating loss of $7 million on revenues of $56 million in the fourth quarter of 2014. The decreases were driven by the prolonged decline in oil and gas services, and the effect of restructuring costs during the quarter. For the full year, UPI generated an operating loss of $32 million on revenues of $134 million.

Overall, it was another good quarter and good year. As Mike said earlier, we are proud of what our employees have accomplished since the spin. That wraps up my remarks for the quarter and the full year. I will now turn the call over to Chris Kastner to provide you with some information on 2016. Chris?

Chris Kastner - *Huntington Ingalls Industries Inc. - Corporate VP & Manager of Corporate Development*

Thanks, Barb, and good morning. Turning to slides 11 and 12 and starting with the income statement, for the full year we expect revenues to be relatively similar to 2015, segment operating margin in our shipbuilding business to be in the 9%-plus range. As a reminder, there can be variation in margins between the quarters, but for the full year, we expect to achieve the 9%-plus margin.

We're expecting a favorable net FAS/CAS adjustment of $137 million for the year, and we expect deferred state income tax expense to be in the range of $10 million to $15 million. We expect interest expense of approximately $75 million for the year, and the income tax rate to be in the range of 33.5% to 34.5%.

Now to a couple of items that will impact cash flow. We plan to contribute $210 million in cash to our pension and post-retirement benefit plans, of which $167 million is discretionary contribution to our qualified pension plans. We also expect capital expenditures to be in the range of 3.5% to 4.5% of revenues for the year.

That concludes my remarks on 2016. I will turn the call back over to Dwayne for Q&A.

Dwayne Blake - *Huntington Ingalls Industries Inc. - VP of IR*

Thanks, Chris. As a reminder to everyone on the call, please limit yourself to one initial question and one follow-up, so we can get as many people through the queue as possible. Ronya, I'll turn it back over to you to manage the Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Gautam Khanna, Cowen.

Gautam Khanna - *Cowen and Company - Analyst*

That was great. Gautam Khanna, Cowen.

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Good morning.

Gautam Khanna - *Cowen and Company - Analyst*

Pretty well. Good, doing well. Guys, I was wondering if you could elaborate on the budget comments, the budget request comments you made in the opening remarks. With respect to the icebreaker, can you give us a sense for how that might be procured, and when that might actually be awarded? Also, any color on the LXR program, and maybe some updated milestones on the Ohio class?

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Okay.

Barb Niland - *Huntington Ingalls Industries Inc. - Corporate VP of Business Management & CFO*

That's about everything, right?

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Yes, so how much time do we have here? We'll start with -- let's start with the LXR program because I think that's center line of good news here. The Navy wants to -- in their budget request, they've identified LXR as a program that stays inside the fit-up, and they've actually -- I think they've got it set for the first ship procurement in 2020, I think.

The main thing there is last year we went through a decision process. The Navy made a critical decision to say that the LXR program is going to be based on the LPD hull. Then last year we had the first round of funding for LPD-28. We've now gone through and completely funded LPD-28, which is sort of a transition, if you will, from the production run of LPDs on a path to the LXR.

From my standpoint, this is all really good news, because we have a very efficient path to keep the amphibs moving. I've said for five years now that the amphibs are in the scrum, really, when it comes to some of this funding. I think the Navy and the Marine Corps have shown their commitment to the program, and we're excited about that.

When it shows up in the President's request, that's a further validation of the importance of the program. It's consistent with the Navy's plans for making it proceed in an efficient way, and it aligns with the way that we're thinking about the business in terms of that production line. We're excited about that, and we have the opportunity to really capture the efficiencies of serial production, which we've been trying to do across all of our programs.

On the Ohio replacement program, I've been pretty vocal about we've got to find a separate source of money. We've got to find more money for the shipbuilding budget to handle the Ohio replacement program, because it could -- it's big enough so it would crowd out other shipbuilding.

I think this is going to be a discussion that we're going to have for the next five to 10 years, really, is how are we going to pay for the program, and how comfortable can we do it inside of the Navy's budget. But this first go-round is a great indication that it's going to happen, and that the other programs are going to stay on track. We are very pleased with the way that came out.

There's a lot of discussion about different kinds of mechanisms to fund this, and from our standpoint, we're somewhat agnostic about whatever the mechanism is. What we really need to see is that the funding is there without affecting other programs. That's what happens in this budget, and that's what looks like is happening in the Navy's plan, by and large.

With regard to the icebreaker, we're on the front end of that program. We're still at the point of our customers are out there trying to set their requirements. Setting the requirements and setting the pace for the program are things that are always in flux right now.

It's clear there's a commitment to the program. It's a program that we're very interested in, and we've been in dialogue to understand what those requirements are and to position ourselves to be able to participate in that program and support the Coast Guard's plans when they go forward. All of that is good news for us.

Gautam Khanna - *Cowen and Company - Analyst*

Thanks, and congratulations Barb and Chris. I'll turn it over.

Operator

Pete Skibitski, Drexel Hamilton.

Pete Skibitski - *Drexel Hamilton - Analyst*

Yes, a couple questions I've got. Guys, on the pension contributing the pretty large discretionary amount, can you help walk us through the calculus on that? You talked about returning most of free cash to the shareholders, but you're making the decision here to make a pretty large discretion contribution to the plan. What led you down that path to putting that kind of money into the plan?

Chris Kastner - *Huntington Ingalls Industries Inc. - Corporate VP & Manager of Corporate Development*

Yes. Thanks for the question. This is Chris. Our practice is to fund 90% of our plans on a pre-mat basis. In order to maximize our cash recovery across our multiple plans, it calls for that contribution. It's simply maximizing our cash recovery.

Pete Skibitski - *Drexel Hamilton - Analyst*

Okay, understood. One more. Excluding the impairments at UPI, the ongoing operating losses is sharp still. Do you guys -- how are you guys thinking about 2016? Do you feel like the business is sized right to at least break even in 2016, or is that a quarter-by-quarter issue you're going to have to manage?

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Yes, it's going to be quarter by quarter. The dynamics in that market place have been pretty volatile just in the past 30 days. Our commitment here is to maintain the relationships we have with those critical customers out there that are in that space. That means that we've got to preserve capabilities that those customers are going to need.

We are winning our share of the work that is out there; but it's not going to be work that's going to kick in until the end of this year or next year. The time-phasing of that is something that we've got to fight our way through quarter by quarter.

I wish it were different. I wish it were a different way, but our commitment here is to those customer relationships. We're going to do what we have to do to make sure we get that right.

Barb Niland - *Huntington Ingalls Industries Inc. - Corporate VP of Business Management & CFO*

Pete, in Q4 slightly over half of the UPI loss adjusted for the PI and the goodwill was related to restructuring costs associated with leases and severance.

Pete Skibitski - *Drexel Hamilton - Analyst*

Okay, so the ongoing operating loss was in the single-digit millions, is that maybe what should we run out for next year?

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

That's just about right.

Barb Niland - *Huntington Ingalls Industries Inc. - Corporate VP of Business Management & CFO*

There's still pressure in that range.

Pete Skibitski - *Drexel Hamilton - Analyst*

Okay. Thanks, guys.

Operator

Jason Gursky, Citi.

Jason Gursky - *Citigroup - Analyst*

Hi, good morning, everyone. Barb, congrats once again.

Barb Niland - *Huntington Ingalls Industries Inc. - Corporate VP of Business Management & CFO*

Thanks, Jason. Good morning.

Jason Gursky - *Citigroup - Analyst*

Barb, one last question for you on the way out on Avondale. Can you update us on the progress of recovery at Avondale, given all of the moving parts, and what's being handed over to Chris at this point to take care of?

Barb Niland - *Huntington Ingalls Industries Inc. - Corporate VP of Business Management & CFO*

Yes, Chris started this. Now he's going to go finish it here. We continue to evaluate opportunities, including sales. We did competitively bid, and selected a brokerage service to assist in the potential sale of real estate and other assets while we continued to pursue restructuring.

We have had a few interested parties. That continues to move along. In addition to that, we've been in discussions on a regular basis with our customer regarding our proposal, and those discussions continue.

Jason Gursky - *Citigroup - Analyst*

Okay, great. Maybe a couple of quick comments about the pipeline of business that you are bidding on outside of the core shipbuilding business. What kinds of things might we look forward to hear in the next -- call it 8.5, 9 months, 10 months -- here in calendar 2016. What are the key programs that you're out there bidding that we all ought to be paying attention to, as to who are going to be the winners and losers, and what that will help us understand about future growth opportunities?

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Sure. We talked in November about both the commercial nuclear space, as well as the government services space. In government services, there's both support of the fleet around the world, as well as participating in the Department of Energy areas.

Commercial nuke, let's start with that. We're supporting the project that Southern Company and Westinghouse are constructing down at the Vogtle Plant. We're proud of the performance that we have there.

Our hope is that as that market starts to expand, we have an opportunity to do some more in that space. We're navigating our way through the creation of the design and the regulatory oversight of the NRC to make sure we get all that right. We've done great work there so far, and we're hoping that we can turn that into something bigger than what we've got today.

In the Department of Energy space, I think the biggest thing that's on the horizon right now is out at Hanford. But the Nevada National Security Site is coming up. We've made a bid on that, and we're partnered with Honeywell and Jacobs.

Of course, in the DoE space, there's always a lot of those things going on and a lot of different teams being formed and moving around. It's a little bit tricky to try to handicap the timing of some of these things in the way that they get awarded. But we are very happy with the way that SN3 has stepped into that market space now, and is creating the alliances we need to be successful in that space.

Then supporting the Navy around the world, we're watching and participating as the Navy continues to be on call. Longer deployment cycles are putting pressure on maintenance cycles and support, from both an engineering and planning perspective that our folks at AMSEC are very deeply involved in.

Especially as the Navy continues to be forward deployed, we are forward deployed with them. Today we have 100 people supporting the Navy in Japan, for instance. We're around the world there doing those kinds of things to support them. That's really on a services as the need comes up kind of business.

Our expectation is that the demand for that is going to go up. I'm not sure I can put a specific target out there in terms of a date on that space or a specific program in that space, but I am a believer that the demand for the Navy is going to drive that market.

Jason Gursky - *Citigroup - Analyst*

Okay, that's great. Thank you.

Operator

Doug Harned, Bernstein.

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Doug Harned - *Sanford C. Bernstein & Co. - Analyst*

Thank you, good morning.

Barb Niland - *Huntington Ingalls Industries Inc. - Corporate VP of Business Management & CFO*

Good morning, Doug.

Doug Harned - *Sanford C. Bernstein & Co. - Analyst*

First, Secretary Carter in his pre-budget statement, he made some comments about CVN-78 construction, and that it was undisciplined, and that there would not be another carrier like that, or a construction process like that. How do you interpret those remarks, and what implications do they have for the approach to CVN-79 and future carriers?

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Well, I'm not sure I would use the word undisciplined, but I would say that the next carrier will not be from a cost and scheduled performance perspective, will not be like Ford. Ford was a lead ship. We've talked many times about the challenges that lead ships have.

This was a particularly challenging project, because of the major insertion of technology into the platform. We basically kept the hull and redesigned everything else in that ship. And so, today, what we have is we have a ship that's built.

The ship is completed. We are in a test program now that's going to drive us through the first half of this year. What we've done though, when you build a lead ship is, as we talked about that lead ship is, it's your first production unit, but it's also your first prototype.

That is the prototype, and that's where you, in prototypes you test out your build plans. You test out training plans for your employees. You test out the tooling that you have.

You test out your supply chain. You're basically testing everything. In the course of that testing, you learn things.

And what we have is a very extensive process for capturing those lessons learned, and applying them to CVN-79. And Doug as you know, we signed a contract for CVN-79 in the middle of last year which reflected frankly, reflected a lot of that learning. Some of that learning is the capital that we need to invest, to drive the efficiencies.

And so, that's part of our capital plan going forward, is to invest in support that program. But there will be a substantially fewer man-hours required to build CVN-79, than what we took on CVN-78. The other thing I would say, is that in -- there's a broader discussion going on about, capability and capacity, which was really interesting to see part of.

In the Navy's parlance, this isn't a light switch, where you go from one to the other. It's really -- these things take a long time. If you go back a decade ago, CVN-78 was not the only lead ship program out there.

The carrier was a new design program. We had -- at 10 years ago, we were coming through the first new submarine at Newport News. Texas was our first delivery of a submarine in 10 years, so we were kind of on -- just at the very beginning of clearing up the lead ship kinds of issues in the submarine program.

The LHD program was a new design program. The LHA was a new design program. The DDG-1000 was a new design program.

The LPD program was a new design program. So 10 years ago, the Navy was basically redesigning all of the ships in its fleet. Every one of those programs on the front-end went through the first ship of a class kind of perturbations that you've got to work through, when your first ship is a -- your first production unit is also your prototype.

Ford actually is the biggest of those ships, and has taken the longest to come through that. But now, if you go and look at the sequence of things that are in the Navy's budget today, the carrier is not a new design ship any more. The Virginia Class program is the gold standard for serial production, and technology insertion into a mature platform.

The DDG-51 program has been restarted, and we're back into serial production on that program. We are now coming through the -- we're in the second ship of the LHA class, have come through all of the design challenges that LHA-6 had, and LHA-7 is performing fine. LHA-8 is in the budget.

And you can just tick down, every one of the programs the Navy has today, are all mature programs that are basically in serial production. And the most important thing we have to do, is keep that moving.

And so, from my standpoint, the capability versus capacity discussion is a really interesting one. But it's different for the Navy, because the horizon is so much further away in shipbuilding, than it is in anything else. And that's why I'm so happy about where we are with the budget, because it definitely shows the Navy's commitment to preserving these production lines and keeping -- not just the capacity out there, but the capability out there as well.

Doug Harned - *Sanford C. Bernstein & Co. - Analyst*

But if I can just follow up on this on the capital plan, because if I look at capital spending for involving the CVN-79, CVN-80. And then also, you mentioned before that the LXR plan, it is being built off of LPD-17. But you also have the TAO-205 plan, which seems to be building off T-AKE and T-AO-187. So if I look at -- you've got investment for CVN-79.

The Navy is trying to make both of those two other programs competitive. Yet one seems to just totally tied to NASSCO, and one seems totally tied to Ingalls. How do you think about the investment across those programs? It looks hard to compete on TAO-205.

Do you invest in that? What does this mean for the CapEx profile over the next year?

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

That's a great question, Doug, and pretty insightful. Without commenting on the competition, what I would say is that, it reminds you that in our shipyards, we build multiple classes of ships. And so, when we think about putting capital investment in the shipyards, most of the capital investment that we put in, is designed for multiple classes of ships. And so we're focused on those processes and those things that are going to become be common across different classes.

It's not uncommon, but it's lesser -- it's the lesser investment for us to turn around and say, we're going to invest in a facility that can only be used for a platform or a class of ship. And so, given that, we step back, and we don't look at necessarily -- we are investing in improving the performance in LPD program, and we're investing in those kinds of facilities that would help us be successful in the TAO program, should that be our program.

But it's not -- we're not looking at making a specific investment to chase a specific program at this point. So that's kind of the way we think about it. And that's why we talk about this investment over the next five years, this $1.5 billion.

This is a generational reset for the our businesses, and we're going to end up building classes of ships in these capital facilities that are not even on the drawing board right now.

Doug Harned - *Sanford C. Bernstein & Co. - Analyst*

Okay, thank you.

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

You bet.

Operator

Sam Pearlstein, Wells Fargo.

Sam Pearlstein - *Wells Fargo Securities, LLC - Analyst*

Good morning.

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Good morning.

Barb Niland - *Huntington Ingalls Industries Inc. - Corporate VP of Business Management & CFO*

Good morning, Sam.

Sam Pearlstein - *Wells Fargo Securities, LLC - Analyst*

Mike, I just wanted to follow up. You mentioned the builder trials for CVN-78 in Q2, and delivery to follow shortly thereafter. Does that mean that delivery has slipped out of the first half? And then, I'm just trying to think about is there a impact to P&L like Ingalls ships, like a reserve release or anything like that upon delivery?

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Well, on the second issue, it's a cost type contract, and so it's a little -- it's going to be -- in terms of reserve release it's going to be pretty insignificant. As far as the schedule goes, I don't even want to put any sort of a stake on the ground in terms of saying, this is what we're going to go do.

The bottom line is that we're testing the ship. And the ship, as I was told 20 years ago when I was doing carrier construction, the ship will leave when it's ready. We're doing everything we can to get the ship out.

We expect that to happen in the middle of the year. There is a sequence from builder trials to delivery that we go through. And so, the team down there is committed to getting it done as quickly as possible.

As I said earlier, the ship is complete. We're testing systems right now that have been installed. And not only are we testing the systems themselves, kind of is system working the way that it was designed to work?

We're also testing, does it work with the other systems the way it's supposed to work to? And as a lead ship, all of this integration is a big challenge for us. And the Navy and the Company are working through this with -- one of the -- probably the best team in the business to get it done.

And so, I don't -- like I said, I don't want to commit to any specific date on the schedule. What I am going to tell you, it's going to go, as quick as we can get it out.

Doug Harned - *Sanford C. Bernstein & Co. - Analyst*

Okay. Thank you. And then just to follow up, the employment reductions you had announced last year were effective in February. So I'm just trying to think about, how did that affect the P&L?

Are there period expenses in Q1? Is it then recoverable? Just trying to think about how to -- how it's going to impact the first quarter?

Barb Niland - *Huntington Ingalls Industries Inc. - Corporate VP of Business Management & CFO*

Yes, it was -- for last year, the reserve was booked for that, and it's all recoverable because it's part of our normal benefit package.

Sam Pearlstein - *Wells Fargo Securities, LLC - Analyst*

Okay. Thank you.

Operator

George Shapiro, Shapiro Research.

George Shapiro - *Shapiro Research - Analyst*

Yes, Barb, good luck.

Barb Niland - *Huntington Ingalls Industries Inc. - Corporate VP of Business Management & CFO*

Good morning, George.

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Good morning, George.

George Shapiro - *Shapiro Research - Analyst*

And welcome, Chris.

Chris Kastner - *Huntington Ingalls Industries Inc. - Corporate VP & Manager of Corporate Development*

Thank you.

George Shapiro - *Shapiro Research - Analyst*

My question is on -- trying to get a little more hands-on free cash flow for 2016. So the way I rough it out -- and tell me where I may be wrong. CapEx could be $100 million higher than what it was in 2015.

You had the $150 million insurance payment in Q2, which I assume you don't get something like that in 2016. And then, it looks like the pension payment -- maybe is $110 million higher than 2015. I don't know whether you made a payment in the fourth quarter or not.

So I kind of put all that together, and net income after FAS/CAS is probably comparable. I figure that maybe free cash flow is going to turn out to be somewhere around $300 million in 2016, versus 2015. I was just wondering if that's -- what might -- if that's correct, or what might be wrong with it?

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Yes, I think you have all the elements there, George. Those are the large drivers. I don't see much movement in working capital.

It's fairly balanced through the year. So I think you have it. We don't provide guidance, of course, and payments could move beyond the quarter ends or year-end, which would drive it a bit, on some of our larger contracts. But I think you have the essential elements.

George Shapiro - *Shapiro Research - Analyst*

Okay, thanks. I'll stick with my one question.

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Okay.

Operator

Joseph DeNardi, Stifel.

Joseph DeNardi - *Stifel Nicolaus - Analyst*

Yes, thanks, good morning.

Barb Niland - *Huntington Ingalls Industries Inc. - Corporate VP of Business Management & CFO*

Good morning.

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Good morning.

Joseph DeNardi - *Stifel Nicolaus - Analyst*

Mike, I wonder if you could just talk about the relative revenue contribution from 78 and 79 this year? And kind of what your assumptions around the margin impact of that, just on the 9%-plus guidance you gave for the year? Just any help with that.

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Well, we don't break anything out by program. And so, probably not going to do much help you with the trade off between 78 and 79. But our commitment is, that our core shipbuilding business is going to -- for the year is going to perform at 9%-plus.

As Chris pointed out in his comments, there is going to be some lumpiness there, and the Ford in the first half of the year is going to have pressure in it. There's no other way to say it. But across the whole business, for the whole year, we're going to be at 9%-plus.

Joseph DeNardi - *Stifel Nicolaus - Analyst*

Okay. And then, just on the M&A side, I think we've talked quite a bit about this at the Investor Day, but what are you seeing there? Are you guys active in looking at other assets, to build out the other segment, or is it just a wait-and-see approach at this time?

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Well, we won't comment specifically about any particular opportunity. We've got our radar up, and we're looking around. The question is, how do you value anything, and how does it fit in with the strategic view of the organization?

As I have said from time to time, the first question we ask ourselves is, why would we be a better owner of that business? And you've got to get through that before you can do anything else.

We laid out -- at the Investors conference, we laid out some very specific filters that, or hurdles if you will, that you have to get over for any transaction. And we are insistent that we're going to stick to that.

Joseph DeNardi - *Stifel Nicolaus - Analyst*

Okay, thank you.

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

You bet.

Operator

Darryl Genovesi, UBS.

Darryl Genovesi - *UBS Securities LLC - Analyst*

Hi, guys. Thanks for the time.

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

You bet.

Barb Niland - *Huntington Ingalls Industries Inc. - Corporate VP of Business Management & CFO*

Good morning.

Darryl Genovesi - *UBS Securities LLC - Analyst*

I guess, a similar question to George, but on an accrual basis. Mike, I know you don't like to give a lot of forward guidance, but maybe perhaps ex-pension, broadly speaking, do you think you guys could grow earnings this year?

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

I'm sorry? Do I think what? (multiple speakers) to grow earnings?

Darryl Genovesi - *UBS Securities LLC - Analyst*

Maybe you can grow earnings, ex-pension?

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Yes, I mean, I think the challenge is that our core shipbuilding business is right now, even though there's good things in the budget, the things that are in the budget don't manifest themselves for a few years in our program. And I think we said for five years, that the best way to think about the core shipbuilding business that we have is, that it's flat.

And so, I think that, if you want to do the math, our commitment to buy back shares and those kinds of things are out there. But our basic business is a flat shipbuilding business, with an opportunity to do some things on the services side from time to time, and the earnings are going to be 9%-plus.

Darryl Genovesi - *UBS Securities LLC - Analyst*

Okay. Thanks for that. And then, maybe just one more on the competitive situation. I mean, in your opinion, does the decision to use a LPD hull form on LXR still leave an opportunity for a meaningful competitive bidding process? And I guess, a similar question on SSBN-X with -- another having -- kind of gotten into the meat of the next budget cycle now, has there been any clarity offered by the Navy on what your role versus GD's might be on the program?

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Well, I will let you talk to the Navy about what their acquisition strategy for LXR might be. I do think that we are in a place in shipbuilding, where there's really a lot more allocation, than there is competition. And in some cases, competition actually slows down the process and/or stifles the innovation somewhat.

So I think you have to -- kind of think our way through that a little bit. I don't exactly know how LXR will come out. We do think that decisions that have been made on LXR so far, have been very smart decisions on the part of the Navy, to take advantage of the -- all the challenges that we had to fight our way through a decade ago, to get these programs up to where they are today.

And I think it's a really key decision not to go, and start over with a clean sheet of paper and redesign that ship. And so, all of those are really good.

I want to make sure that I catch -- I think I might have said that LXR was a 2020 program, but I think it's really a 2021 program. And so, well, whatever it is, it's inside the fit up. And that's the most important thing, that's not one of those bowriders that sits right outside of fit up forever.

I mean, it's actually in the program, and the Navy is moving forward on it. So we're excited about that. If the Navy chooses to compete, we'll compete. If the Navy chooses another path, we'll partner into that path, and we'll go execute. So more to come, I guess.

Darryl Genovesi - *UBS Securities LLC - Analyst*

Great. Thanks a lot.

Operator

Ron Epstein, BofA Merrill Lynch.

Kristine Liwag - *BofA Merrill Lynch - Analyst*

Hi, good morning, everyone. It's actually Kristine Liwag calling in for Ron.

Barb Niland - *Huntington Ingalls Industries Inc. - Corporate VP of Business Management & CFO*

Good morning.

Kristine Liwag - *BofA Merrill Lynch - Analyst*

Can you guys discuss how much is lost in goodwill and intangible assets related your oil and gas business? And also what are the trigger points for possibly more impairments and write-downs?

Barb Niland - *Huntington Ingalls Industries Inc. - Corporate VP of Business Management & CFO*

Okay. So on the -- for UPI, the goodwill balance is around $29 million and the purchase intangible balance is around $4 million. When, at the end of the year, when oil prices continued to drop, we went back. It triggered another look at our forecast, and when we looked at our forecast, we decided that, hey -- this has been prolonged.

Originally, we thought we were going to see a recovery sooner, so we looked at it with a more delayed recovery. I'm not saying, it can't happen. It's possible if oil prices continue to drop, we could have a problem. But right now I think we are in a fairly reasonable place on -- as far as goodwill and purchase intangibles.

Kristine Liwag - *BofA Merrill Lynch - Analyst*

Great. And then, switching gears. It seems like the Navy's study on potential alternatives to the CVN-78 class is back on the table, and with possibly smaller carriers in the long-term. Can you discuss what this would mean for you?

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Well, I think first of all, let's talk about the analysis of alternatives. And one thing that I think is really important for folks -- and the Navy is going to go off and do their study, and I don't know how that's all going to turn out. However, the Navy works their way through that, we see ourselves as their principal partner in shipbuilding, and we will be there to help them do whatever it is that they believe that they need to go do.

Now having said that, one of the things that gets lost, when you do all of these alternatives, and you do this analysis is that there's a lot of metrics that get thrown around, like cost per ton, and things like that, to try to drive more affordable solutions to a missions set. The thing that people don't get sometimes is that the cheapest thing we do is create volume. Building volume in the ship is what actually creates -- that's the cheapest thing we do.

So making it large actually, suddenly creates a whole lot of flexibility in the platform that you didn't have before. I am not the metric guy, but I don't believe you can buy two-thirds of a carrier for two-thirds of the cost, two-thirds of the capability for two-thirds of the cost. I don't believe you can do that.

Because the first thing you do, is you start to reduce the volume, you significantly change the flexibility and the capability of the ship. And so, this has been looked at many, many times. Every time it gets looked at, we come back to this decision, that we really do need the volume at sea, so we have the flexibility to go do those missions, that we don't even know about right now, that we're going to need to perform for 50 years ago.

So I'm a strong advocate for the big deck carrier. And now having said that, if the Navy chooses to go on a different path, then we'll be right there, and we will help them be successful in that path.

Kristine Liwag - *BofA Merrill Lynch - Analyst*

Great. Thank you very much.

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

You got it.

Operator

Roman Schweizer, Guggenheim.

Roman Schweizer - *Guggenheim Securities LLC - Analyst*

Yes, good morning, everyone.

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Good morning.

Barb Niland - *Huntington Ingalls Industries Inc. - Corporate VP of Business Management & CFO*

Good morning.

Roman Schweizer - *Guggenheim Securities LLC - Analyst*

And Barb, fair winds and following seas. Wish you the best.

Barb Niland - *Huntington Ingalls Industries Inc. - Corporate VP of Business Management & CFO*

Thank you.

Roman Schweizer - *Guggenheim Securities LLC - Analyst*

So my first question just regarding Newport News, I was wondering if there was any opportunity or discussions with the Navy to pull forward possibly any work on CVN-73, or any of the projects there, to kind of help smooth that workload out in 2016?

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

There's been a lot of discussion with the Navy on how do we manage this workload valley challenge. But the real challenge that we have is, that we have these three carriers to deliver now, starting in the middle of the year, and carrying over to the first part of next year.

You can do a lot of things, and you can move a lot of work around, and the Navy has worked with us to do that. But having said all that, we still have -- this is pretty disruptive. And so, we've got to fight our way through it.

The most discouraging thing about this, and I'm sure the Navy is discouraged about it as we are, is that on the back end of this, we're going to start hiring back. Two years from now, we're going to be coming right back up towards the levels where we were, before we started laying people off.

And the Navy works with us very closely, to try to prevent those kinds of situations from happening. But this happened because of the sequester environment in Washington, and the disruption that created in long-term planning.

And until we get it out of that environment, we're all just doing the best we can, to fight through it, and preserve our skills to the best of our ability. It's no way -- it's no way for the greatest country on earth to run its business. And we've got to do better than that.

Roman Schweizer - *Guggenheim Securities LLC - Analyst*

Okay. Thank you. And just one more follow-up, related to Newport News, but on the submarine side.

You sort of talked about the impact of Ohio Class and Virginia Class -- really the submarine industrial base, and how that workload is sort of spread and shared, as those two programs go simultaneously. The Navy's fit up -- well, cut Virginia class, in 2021 the ramp would drop to one per year. And I was just wondering, when you look at that total workload available, would one Ohio Class and one Virginia Class still be sort of net additive to that industrial base?

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Well, I think you need to recognize that the Ohio class submarine is a significantly different, larger volume of work, than a Virginia class submarine. And so, it might be one and one equals two, but one Ohio class plus one Virginia class is a significantly higher level of work for the industrial base than two Virginia class submarines.

And so, I think that -- and the other thing I would point out, is that you are looking at the appropriations documents. The real question in the business is not, what happens in the years when the money gets funded. What you have to work your way through is, what's happening in the business as the ships get built?

What do the volumes look like? What do the delivery teams look like, and how do those line up? So you are really -- 2021 is only forecast of where you might be in 2026 or 2027 so -- or 2025 even.

So that's kind of the complexity of the challenge. But, I think is easily -- it's not even close, one Ohio class plus one Virginia class is significantly more work than two Virginia class.

Roman Schweizer - *Guggenheim Securities LLC - Analyst*

Great. Thank you very much.

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

You bet.

Operator

George Shapiro, Shapiro Research.

George Shapiro - *Shapiro Research - Analyst*

Yes, I just wanted to pursue -- maybe Barb or Chris, what the adjustments were in Ingalls, where you said there was lower risk retirement? Could you just quantify what they were, because we probably won't get to see them until the K comes out?

Barb Niland - *Huntington Ingalls Industries Inc. - Corporate VP of Business Management & CFO*

Right. Well, for the quarter, we had $71 million favorable risk retirement, and they were -- and that was primarily related to the Virginia class, and across the program.

And in 2014, in the fourth quarter, we had a lot of risk retirement related to the LPD programs, that we didn't have in 2015 in this quarter. So we had $51 million in the quarter of net favorable adjustments. So none of the downers were individually significant, and the uppers were primarily related to Virginia class program.

George Shapiro - *Shapiro Research - Analyst*

Okay. Thanks very much.

Barb Niland - *Huntington Ingalls Industries Inc. - Corporate VP of Business Management & CFO*

All right. Thank you.

Mike Petters - *Huntington Ingalls Industries Inc. - President & CEO*

Okay. Well, I think that's it on our call list, and so we'll wrap up here. I would like to thank everybody for joining us today.

And I again, would to like to thank Barb. I believe this is our 20th call together. So thank you for that, for all of your support and hard work over all these years.

We had a great year in 2015. That captures and culminates nearly five years of really hard work by our team. So we take -- while we'll celebrate that a little bit, but we know that we are not ever done.

We have mapped out a strategy for the next five years, that in essence positions our Company for the next 25 to 30 years. In order for those plans to become reality, our focus on program execution, risk retirement, and cash generation will not change. So thanks for your interest in HII, and we look forward to seeing you soon.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This concludes today's program. You may now all disconnect.

Everyone, have a great day.
