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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Huntington Ingalls Industries Second Quarter 2017 Earnings Conference Call. (Operator Instructions) As a reminder, this conference is being recorded.

I would like to introduce your host for today's conference, Mr. Dwayne Blake, Vice President of Investor Relations. Sir, you may begin.

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

Thanks, Terrence. Good morning, and welcome to the Huntington Ingalls Industries Second Quarter 2017 Earnings Conference Call. With us today are Mike Petters, President and Chief Executive Officer; and Chris Kastner, Executive Vice President, Business Management and Chief Financial Officer.

As a reminder, statements made in today's call that are not historical facts 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 Chris 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'll turn the call over to our President and CEO, Mike Petters. Mike?

C. Michael Petters - *Huntington Ingalls Industries, Inc. - CEO, President & Director*

Thanks, Dwayne. Good morning, everyone, and thanks for joining us on today's call. We released our second quarter results this morning that reflects solid performance across the enterprise.

So let me share some highlights from the quarter, starting on Page 3 of the presentation. Sales of $1.86 billion were up 9.3% from last year. Diluted EPS was $3.21, and operating cash was 161 -- $186 million for the quarter. Additionally, we received $3.4 billion of new contracts, including $3 billion for detailed design and construction of LHA 8 Bougainville and $218 million for long-lead material and advanced construction activities for LPD 29. As a result, backlog was approximately $21.1 billion at the end of the quarter, of which $14 billion is funded.

Regarding activities in Washington, we were honored to participate in the shipbuilding hearing before the Senate Armed Services Committee's Seapower Subcommittee this past May, where we advocated for stable and predictable funding for shipbuilding as well as an end to sequestration. The hearing also afforded an opportunity to highlight the inherent efficiencies and cost savings of leveraging hot production lines and multi-ship procurement strategies for Ford-class aircraft carriers, LPD 17-class amphibious ships and DDG 51-class destroyers.

We are pleased with the progress being made by the defense authorizing and appropriating committees in Congress with regard to the fiscal year 2018 budget and are encouraged by the support for Navy shipbuilding in various bills. As the administration completes its national defense strategy review this summer, we look forward to seeing how the results will shape the fiscal year 2019 President's budget as well as the Future Years Defense Program.

However, looming over all of this is the Budget Control Act, which remains the law of the land, as well as the need to determine how Columbia-class submarines will be funded without impacting other critically important shipbuilding priorities.

Now I'll provide a few points of interest on our business segments. Ingalls launched LHA 7 Tripoli in May and conducted very successful builder's trials on LPD 27 Portland at the end of June, with plans to complete acceptance trials and deliver the ship to the Navy by the end of the year. The team also recently completed builder's trials on DDG-114 Ralph Johnson and plans to complete acceptance trials and deliver the ship to the Navy by the end of this year. In addition, the team received the modification to the 2013 DDG multiyear contract that incorporates the Flight III radar system upgrades on DDG 125.

At Newport News, this was a very busy quarter as the team successfully delivered CVN 78 Ford and SSN 787 Washington and redelivered CVN 72 Lincoln to the Navy within a 19-day span. CVN 79 Kennedy achieved 50% structural completion, a significant milestone in the construction of this ship. In addition, SSN 789 Indiana was launched and is preparing for its planned delivery to the Navy early next year. And in July, the team reached agreement on a 52-month contract with United Steelworkers of America, its largest bargaining unit.

Turning to Technical Solutions. Its nuclear and environmental group is the part of the team that won the competition to provide management and operating services at the Nevada National Security Site. In addition, its fleet support group was awarded a task order to perform a special selected restricted availability on CG 65 USS Chosin and is also teaming with Boeing to pursue design and production of the Navy's Extra Large Unmanned Undersea Vehicle.

In closing, I am pleased with the program execution and financial performance for the first half of the year, and we remain confident in the long-term outlook for our business. The shipbuilding segments continue to invest in capital projects to increase efficiency and affordability, while Technical Solutions segment focuses on the integration process and securing key contract awards that strengthen its book of business. All of these actions support the framework for long-term sustainable value-creation for our customers, our employees and our shareholders.

So that concludes my remarks, and I will now turn the call over to Chris Kastner for some remarks on the financials. Chris?

Christopher D. Kastner - *Huntington Ingalls Industries, Inc. - CFO and EVP of Business Management*

Thanks, Mike, and good morning. Today, I will review our second quarter consolidated and segment results as well as provide you with a few updates for the second half of the year, starting with our consolidated results on Slide 4 of the presentation. Revenues in the quarter of $1.86 billion increased 9.3% over second quarter 2016 due to higher volumes at Ingalls and the acquisition of Camber, which contributed approximately $85 million.

Operating income for the quarter of $237 million increased $20 million or 9.2% from second quarter of 2016, primarily driven by the FAS/CAS adjustment. Operating margin of 12.8% was similar to second quarter 2016.

Turning to Slide 5 of the presentation. Cash from operations was $1.86 million in the quarter, and free cash flow was $107 million. Capital expenditures in the quarter were $79 million or 4.3% of revenues compared to $48 million in the second quarter of 2016. We continue to expect capital expenditures for the year to be between 4.5% and 5.5% of revenues.

Additionally, year-to-date, we've made $91 million of discretionary contributions to our qualified pension plan, and we plan to contribute the remaining discretionary balance in the third quarter. We also repurchased approximately 708,000 shares in the quarter at a cost of $138 million, bringing the balance remaining in our share repurchase program to approximately $306 million; and paid dividends of $0.60 per share or $27 million, bringing our quarter-end cash balance to $553 million. We remain committed to returning substantially all our free cash flow to shareholders through 2020.

Before I go into the segment results, let me briefly discuss our credit rating. During the quarter, Fitch affirmed its BB+ corporate credit rating of HII and raised its outlook from stable to positive, following Moody's affirmation of its Ba1 corporate credit rating and positive outlook position published in the first quarter. We believe that these developments are a natural evolution for the business as we have maintained investment-grade credit metrics for the past 2 years, driven by strong operational performance, cash generation and a measured deleveraging. We intend to continue to manage the business with a financial policy that is consistent with an investment-grade credit rating.

Turning to segment [results] on Slide 6 of the presentation. Ingalls revenues in the quarter of $639 million increased 9.2% from the same period last year, driven by higher volumes on the LHA and NSC programs, partially offset by lower volume on the LPD program. Ingalls segment operating income of $98 million and margin of 15.3% [in the] quarter were up $10 million and 11% year-over-year respectively, primarily due to higher risk retirement on the LHA and NSC programs, partially offset by lower risk retirement on the LPD program.

On Slide 7 of the presentation. Newport News revenues of $1 billion in the quarter were similar to revenues in the second quarter of 2016. Newport News operating income was $80 million in the quarter, with operating margin of 8%. Operating income was down $18 million and operating margin down 18% year-over-year, primarily due to lower risk retirement on the VCS program.

Now to Technical Solutions on Slide 8 of the presentation. Revenues of $244 million in the quarter increased 71% from the same period last year, primarily due to the acquisition of Camber and improvement in the oil and gas services business. Technical Solutions operating income of $9 million in the quarter increased $11 million from second quarter 2016, primarily due to improved performance in the oil and gas services business and the acquisition of Camber.

Additionally, regarding the Westinghouse bankruptcy, we received cash for a portion of the pre-bankruptcy cost incurred and made an adjustment to the first quarter reserve, resulting in a net margin benefit of approximately $3 million. As you recall, we took a $29 million reserve in the first quarter for costs incurred due March 29, 2017, the bankruptcy filing date. We've been operating under interim assessment agreements with Georgia and South Carolina facility owners and have been paid for all post-bankruptcy cost incurred through the end of June. We also expect to be paid for the costs incurred in July. As you may be aware, the South Carolina utility owners decided to cease construction on both new nuclear units.

While we are disappointed in this decision, we expect cost incurred for the termination date to be paid under the provisions of the Westinghouse interim assessment agreement. Other liabilities that we have incurred for the South Carolina facility will be subject to bankruptcy proceedings. Additionally, the bankruptcy court has approved an agreement on pre-bankruptcy cost for the Georgia plant. And we expect to receive payment for the remaining Georgia pre-bankruptcy cost incurred in the third quarter.

In addition, let me give you an update on Avondale. We signed a purchase and sale agreement for the sale of the property. While this is a positive step towards an eventual sale, a comprehensive due diligence process will now be initiated before the potential buyer is obligated to close.

Now for some below-the-line items for '17. We continue to expect a favorable FAS/CAS adjustment for 2017 of $198 million, a noncurrent state income tax expense to be in the $5 million to $10 million range. We still expect interest expense of $70 million for the year and the effective income tax rate to be in the 30% to 32% range.

That concludes my remarks. I'll turn the call back over to Dwayne for Q&A.

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

Thanks, Chris. (Operator Instructions) Terrence, I'll turn the call over to you to manage the Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question comes from Robert Spingarn from Crédit Suisse.

Robert Michael Spingarn - *Crédit Suisse AG, Research Division - Aerospace and Defense Analyst*

A quick follow-up on what you just said on Avondale. Is there a particular cash impact we should expect if and when that closes? And then I have a question, Mike, for you on LCS.

Christopher D. Kastner - *Huntington Ingalls Industries, Inc. - CFO and EVP of Business Management*

So regarding Avondale, the terms of that deal, that purchase and sale agreement are not disclosed at this point. We have a long way to go in the due diligence process. It could take a few months here. So that's going to take a bit of time to resolve. It's a positive first step. But we really won't know -- that will be done until it's done. From a cash standpoint, as you know, the Avondale sale is part of the restructuring proposal that we have going on with the Navy. So while there could be some initial cash pickup before the end of the year based on the terms of the deal, we would be obligated to provide some of that back to our overhead rates.

Robert Michael Spingarn - *Crédit Suisse AG, Research Division - Aerospace and Defense Analyst*

Right. Okay. Mike, on LCS, it looks like there's going to be a follow-up program here, FFG(X), that it sounds like it will be a single winner 2020 time frame for the award. Is this something that you guys are interested in? And how should we think about that opportunity?

C. Michael Petters - *Huntington Ingalls Industries, Inc. - CEO, President & Director*

In a word, yes, we're very interested in that program. We participated in the industry discussions that had been going on so far. We have advocated that the National Security Cutter could be a good small frigate. That's a possibility. We'll have to see if that's how the requirements shake out, if that even makes sense. The Navy program looks like it's going to be driven by how quickly you can get a ship to the fleet. And so we're actually pretty good at getting ships to the fleet, and so we think we have a fighter's chance, and we're really interested in the program.

Robert Michael Spingarn - *Crédit Suisse AG, Research Division - Aerospace and Defense Analyst*

Okay. And then just lastly, Chris, one other thing. On Ford, was there a profit pickup in Q2 or is that Q3? Or is there just wasn't one, just given the margins at Newport News?

Christopher D. Kastner - *Huntington Ingalls Industries, Inc. - CFO and EVP of Business Management*

There's no material adjustment within the quarter related to the Ford.

Robert Michael Spingarn - *Crédit Suisse AG, Research Division - Aerospace and Defense Analyst*

Okay. And you don't expect one?

Christopher D. Kastner - *Huntington Ingalls Industries, Inc. - CFO and EVP of Business Management*

No, I don't.

Operator

And our next question comes from David Strauss from UBS.

David Egon Strauss - *UBS Investment Bank, Research Division - MD and Senior Research Analyst*

Mike, could you give us a bit -- more of an update on Kennedy? You talked about being 50% structurally complete, but some stuff out there in the news this quarter around cost progression on it, just an update there?

C. Michael Petters - *Huntington Ingalls Industries, Inc. - CEO, President & Director*

Sure. We are 50% structurally complete. If you look in the dry dock, you can make out kind of the whole bottom keyhole area of the ship. It's looking like a ship now. We'll start building skyline here before too long. The -- in the quarter, you referenced some news. I mean, what happened during the quarter is that the GAO put out a report, which really compared 79 Kennedy to the Ford in terms of the way the cost was allocated in the shipyard. And I think that's a pretty useful report from the standpoint of saying here are -- here's a way to look at what's happening on Ford -- between what happens on Ford and what happens on Kennedy. The fact is that when we went to contract on Kennedy, we took a pretty significant reduction in the man hours between Kennedy and Ford. And we can go and kind of quibble about which hours are in their report or not. But I think it's useful to think, in the main, they got that right. There's a pretty significant reduction of man hours between Ford and Kennedy. And I think their perspective was that this is bigger than anything we've ever seen in carriers. And we agree in the main. We agree with all of that. It is bigger than anything we've ever seen before. We did take that reduction in the target. And now let's talk about why we took that reduction and why we have confidence in what we're doing. As we went into Ford, we were operating, for the first time, we're operating with a digital design and a 3D product model. But it was not complete when we started that ship. As we started the Kennedy, the model was complete. When we started the Ford, as we went through that project, the building material, because the design wasn't complete, the building material wasn't complete. And so as we go into Kennedy, not only is the design complete, but the building material is complete. Those 2 factors alone will drive reductions in the cost of the program that we think are fairly significant. Beyond that, what's happening on the ship is that as you went through the first ship of a class is a prototype. And we talked about how the first production unit is the prototype and how that's different than a lot of folks who build prototypes and then go to production after they build their prototypes. In this particular case, from the very first day of cutting the very first purchase order for equipment on the Ford, we began the process of saying, how can we do this better? And we collected, whether it was in purchasing or in engineering or in manufacturing or in assembly down on the ship, we collected those lessons learned, and we brought those back and we basically tested our labor plan, our production plan, our sourcing plan and our engineering plan. And where we felt we could make improvements, we incorporated those into the master schedule for the 79. So as you're going through this and you're going through testing the prototype, the computer tells you as an example of what -- the difference that pops up, the computer will tell you, you need to put a hole in this plate in this spot. So the craftsman will look at that and say, well, okay, but I want to go check that. And they're going to go verify it, and they're going to validate it and they're going to look at it 3 ways to Sunday and say, okay, now I believe that the hole goes in that spot. That's the kind of stuff that happens on Ford. When you go to Kennedy, the craftsman says, the computer said to put the hole in that spot, I'm going to go put the hole in that sport. I know it's right because it was right on Ford. So we think that there is a lot of that kind of prototype cost that can be shed between in terms of the labor and the man hours that go into the program. We felt confident enough about that not only to capture it and build the ship that way, but to contract Ford. So where do we stand? So far, so good. We're 50% erect on the ship. We are beginning the -- really cutting the loose -- the man hours now. We've got a lot of man hours in front of us, but so far, so good. We are basically on track with our plan. And we are very confident that we have -- that we're going to make a very, very significant labor cost reduction between Kennedy and Ford. And we'll be talking about that, I'm sure, every quarter for the next 5 or 6 years.

David Egon Strauss - *UBS Investment Bank, Research Division - MD and Senior Research Analyst*

Right, right. That's terrific color. As a follow-up, just wanted to ask about how you're thinking about growth in the shipbuilding business going forward as a whole. I think this quarter, you did about 4% growth in the shipbuilding businesses. As I look at the SCN account, it's grown by 25-or-so percent over the last couple of years. I think last I heard from you guys, you were still talking flattish. Just how you're thinking about the revenue profile from here.

C. Michael Petters - *Huntington Ingalls Industries, Inc. - CEO, President & Director*

Yes. I think if you buy into the 355-ship Navy, you can talk yourself into a pretty aggressive growth profile. We're at the place where we're saying until sequestration is taken care of and we -- it's kind of a show-us-the-money sort of perspective. And without that and without that getting sorted out, we're going to stick to our guns and say the history of the SCN account is that it's reasonably flat. My concern is that if you find another way to pay for the Columbia class, then it won't be flat. There will be growth in the profile. But if you don't find a way to pay for the Columbia class, you're going to take it out of [HII] and you're going to take it out of other ships. And so our view is that we're making pretty significant capital investment in our business, and we've talked about how generational that is. That capital investment is to support the flat plan. If we see a break loose on heading up towards the 355 ships and we get some confidence in that, we'll be talking about more capital investment. So our view is that we're optimistic, we're hopeful. Everybody is saying all the right stuff. But we got some real tough things to get over. The Budget Control Act is a big deal that we've got to get over before everybody can go about and do this the right way. So that's -- we're going to stick to our guns and say plan on flat, hope for the best.

Operator

And our next question comes from George Shapiro from Shapiro Research.

George D. Shapiro - *Shapiro Research - CEO and Managing Partner*

First, a quick one for you, Chris. The Ingalls margin seems abnormally high. I mean, it was about last year, and last year, you got a big benefit from LPD delivery. So is this -- can you give us what the EACs were or -- and/or if there is something unique in the EAC for Ingalls this quarter?

Christopher D. Kastner - *Huntington Ingalls Industries, Inc. - CFO and EVP of Business Management*

Yes, George, thanks for the question. The unique thing that happened at Ingalls this quarter, and it's becoming less unique and more run rate, is they had a very high-quality launch related to LHA 7. It's actually ahead of schedule, and they were able to retire about $30 million of risk. So it was driven by a high-quality LHA 7 launch.

George D. Shapiro - *Shapiro Research - CEO and Managing Partner*

Okay. And can you just tell us how much -- what the favorable and unfavorable EACs were? I guess we'll see it in the Q in a little while.

Christopher D. Kastner - *Huntington Ingalls Industries, Inc. - CFO and EVP of Business Management*

Well, I'll just tell you. It's positive $88 million, it's negative $28 million for a net of $60 million. And about 85% of that net is driven by Ingalls.

George D. Shapiro - *Shapiro Research - CEO and Managing Partner*

Okay. And then one for you, Mike. Can you tell us where you think we are in terms of -- you had talked about as being Newport News best hub for this year?

C. Michael Petters - *Huntington Ingalls Industries, Inc. - CEO, President & Director*

Well, I don't think that -- I mean, I think Newport News is in a phase right now that's more than a year. I think Newport News is at the beginning of CVN-79, and we go to launch that ship in 2020. So that's really the first big major milestone on 79 that affects the way that we rationalize our risk registers. We're just now going to be -- this quarter, we're going to be beginning the next refueling overhaul. We are beginning construction on the Block IV. We're going to be heading into negotiations on Block V for the Virginia class. And we're beginning Columbia. So if you look across Newport News, I mean, they've got -- those are all really, really good, solid, great programs with long runs ahead of them. But this next time period at Newport News is going to be starting up. And in the middle of that, we're going to be digitizing the shipyard and so -- to give us a chance to really be successful on these long, long runs that we have in front of us and take some significant cost out. So this is not just a 1-year event at Newport News. This is going to be a phase that they're going to go through. And I'm really happy with the team that's there, the way they're working on the programs. They're executing exceptionally well in all of their programs. And 3 deliveries in 19 days is pretty phenomenal. So I'm pretty excited about where that business is going to go, and it's going to be set up for a very, very bright future. But we got to go through some -- through a little phase of time here that's going to be a grind.

Operator

And our next question comes from Sam Pearlstein from Wells Fargo.

Samuel Joel Pearlstein - *Wells Fargo Securities, LLC, Research Division - MD, Co-Head of Equity Research & Senior Analyst*

You recently got the DDG contract for the Flight III upgrade. And I guess, just trying to think about what do you do differently? Does it make you think differently about the starting margin on that ship versus other DDG starts?

Christopher D. Kastner - *Huntington Ingalls Industries, Inc. - CFO and EVP of Business Management*

Sam, this is Chris. We assess the risk on each ship when we start out. And the risk on that is a bit different, obviously, from the Flight II. So the beginning margin rate could be less. But that's an assessment we make on each ship when we start the program.

Samuel Joel Pearlstein - *Wells Fargo Securities, LLC, Research Division - MD, Co-Head of Equity Research & Senior Analyst*

Okay. And now with the LPD-29 advanced construction, does that get you the bridge to LXR? Or do you still need anything more in order to fill that gap?

C. Michael Petters - *Huntington Ingalls Industries, Inc. - CEO, President & Director*

You know that depends on when LXR happens. If the assumption is that it's going to happen in 2019, then we're probably getting pretty close. If you take LXR and you build it right off of LPD-29 and it's the next one, the optimum time would be sooner than that. But I think to me, this is part of the discussion around how do you fund Columbia because I think, unfortunately, I think LXR becomes one of those things that could be affected by the failure to figure out how to fund Columbia. And that's why we keep bringing that up as -- you can't just go and throw all these programs out there. They're going to start bumping into each other unless you figure out how to get through sequestration.

Operator

And our next question comes from Pete Skibitski from Drexel Hamilton.

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

Mike, I wondered if you could weigh in to the D.C. debate a little bit and just discuss in terms of your discussions there, how you'd handicap the likelihood of getting a BCA workaround deal because it seems like some of the Senate democrats have kind of pulled up a flag to say, "Hey, here's one potential workaround." So is that a positive thing? Do you put your handicap at better than 50%, that we do get a workaround?

C. Michael Petters - *Huntington Ingalls Industries, Inc. - CEO, President & Director*

Yes, I -- my -- this is just one man's opinion here. I think, first of all, the discussion that's going on around the BCA of what's the real requirement for security, what are the things we need to be able to do, what's the world look like? All of those things are driving folks to recognize that the Budget Control Act is not helpful. And you kind of look any dimension, you look at it through any lens you look at, you kind of come to that conclusion. And just about everybody I talk to says, we really shouldn't be operating this way. But now how do you get it changed and how do you get it undone? My guess is it probably looks a little bit like what we've done in the past, that there will be some kind of another Ryan-Murray deal or something like that. I don't think that's the right answer. Let me be clear about that. When you only do these 2-year fixes, you are not able to do the strategic decision-making that this country needs to make on behalf of any dimension, whether it's security or some other dimension that you're looking at. You can't think strategically when you have basically a 2-year deal. Having said that, a 2-year deal is better than no deal. And so -- and I would say right now, if I had to lay a wager that as we get to the end game, there's going to be some discussion of some way to put together a deal that's going to make some of this happen. And we'll be -- and we'll see and we'll stay engaged.

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

Okay, got it. And then can you give us some details on this Nevada test site win, just in terms of what's your participation in the JV and what kind of margin or even just the level we should model in?

Christopher D. Kastner - *Huntington Ingalls Industries, Inc. - CFO and EVP of Business Management*

Well, it's 23%. It could be -- it's a 10-year program, $500 million, we're 23 -- or excuse me, $5 billion, and we're 23% of that. So on an annualized basis, it's probably south of $10 million a year.

Operator

And our next question comes from Jason Gursky from Citi.

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

Mike, I was wondering if you could spend a few minutes talking about unmanned undersea, where your capabilities are at this point, and then kind of what you view the future to be in unmanned undersea, kind of the -- its potential size of the opportunity there and maybe talk a little bit about some of the key milestones that you're looking for, either from your technical capabilities or from the customer, and when we might begin seeing this become a bit more of a meaningful portion of your revenue stream?

C. Michael Petters - *Huntington Ingalls Industries, Inc. - CEO, President & Director*

Yes, good question. Conceptually, we've had a view towards this space for a while now. And a couple of years ago, we acquired the undersea group from Columbia that had a working manned and unmanned undersea vehicle called Proteus. And we've shopped that around and we showed folks that. That was a very small acquisition, but that opened up a whole lot of doors to customers that we really didn't have great access to before that. And it's created an opportunity to partner in ways that maybe we couldn't have partnered before. We have tremendous undersea capability in our submarine construction program, and I would say that's second to none. But building submarines, where you're going to take people into the environment of the sea, is different than building an unmanned vehicle. They're just a very -- it's a very different thing. The physics are all the same, but the difference between carrying a person and not carrying a person is dramatic. And it really creates a whole different set of customers and a whole different set of requirements. So we felt like we needed to get some more knowledge in there. And so bringing those guys on from Panama City was a huge -- even though it's a small acquisition, on our part, it was a huge change in our company because it gave us a chance to go and really engage in that space. And so we've been engaging in that space as the programs have come through. The first go-around on the LDUUV, we were very involved in that when that program moved to the side. And now the Navy has gone forward with this XLUUV program. We've actually been -- we've actually teamed with Boeing to participate in that program. And we're very, very excited about the chance to work with a company like Boeing that's got a long history in this space. And I think they're excited that they have access to some of our technical capability as well. So we're excited about that, and we're excited about where that could lead, where that might go for the future. As far as the size of this market, you can -- it's kind of hard to size it. But you could go back and take the UAV marketplace back to 20, 25 years ago. And I've seen the curves that say, here's what happened with UAV. It was kind of flat for a while and then it turned and went up. And I don't know where we are on the curve around UUVs. I was a submarine guy. I can tell you for sure that the thing about being underwater is very different than being in the air. It's a different set of engineering and engineering challenges to solve. I can't say for sure that the curve is going to go up in the way that the UAV curve did. But we're staking out a position in the front end of this program, and it's been a strategic emphasis for us for the last 3 or 4 years to go figure out how to get in on the front end of this thing. We're excited about our position now. And when that curve does hit the knee and start to accelerate up, we expect to be a pretty big player in it. As far as trying to size it, I think I'm not sure I know how to size that yet. It's a really big strategic thrust for us.

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

I think that's great. And then as the follow-up question here on the -- back on the Technical Solutions side of things. Over the past couple of years, you've talked about some of the growth opportunities there. Can you maybe just provide us a quick update on the various initiatives that you had going on there from a growth perspective?

C. Michael Petters - *Huntington Ingalls Industries, Inc. - CEO, President & Director*

Sure. The first thing to understand about Technical Solutions is that when we acquired Camber, we actually then felt we had the critical mass worthy of separating this business away from the shipbuilding business and creating a third business unit. The reason we wanted to do that was because the way those -- everybody that's in the Technical Solutions division, the way that they compete is fundamentally different than the way we compete in shipbuilding. The style of competition is very different. The magnitude and the quantity of the customers that are out there are very different. And so how you go to the market is very different. It's consistent across that division now. They fundamentally go to market the same way. But their slate of customers is tremendously large compared to the customers that we have in shipbuilding. And the style of contracts and the style of competitions are very different. Behind that, though, is there's a fundamental reliance on the shipbuilding business to support the Technical Solutions team. We believe that there is great -- we've had a historic relationship between our fleet support group, the folks at AMSEC, historically, and the folks at Continental Maritime, their relationship back to shipbuilding kind of made sense, I mean, the big Navy customer, big Navy support around the world, and that continues. But then you turn to our effort in the DOE space, and we've talked about being -- we've been working with Fluor at the Savannah River site for over a decade now, but we've never really been able to kind of grow that business in any way. And we've now moved this to a place where we've been part of a winning team at the Nevada test site. And we see the Department of Energy has a lot of those kinds of programs in front of it over the next 10 years, and we expect to be a bigger player. We're certainly going to be a bigger player in that than we have been in the past. And we expect that the ability now to connect the tremendous technical capability at the shipyard to those customers at the Department of Energy is going to be something that we're going to get better and better at. And that's going to give us a chance to grow that piece of the business. Camber comes in with a whole set of customers that we have very little -- a whole lot of government customers that we, without Camber, had very little experience with. And in the main, though, Camber also had a pretty substantial Navy business. And Camber and AMSEC found themselves in places now where they're able to bid stuff that neither one of them could bid before. And so we're excited about that opportunity. And we've kind of gone through the -- all of the pain of the oil and gas space. We have another business in -- at UniversalPegasus that competes and goes to market the same way as those other folks do. Their customers are not in the government typically, and that's healthy for my business as well. And they've kind of gone through the pain, and they're starting to really capture their share of the work now and move ahead. So we believe that Technical Solutions is really well-positioned to take advantage of the growth in both government services and the potential for growth over in the oil and gas space. And we're excited about that. Our businesses are leaning back and forth between Technical Solutions and our shipbuilding business to make sure that we're able to present those tremendous capabilities that we have to the vast amount of customers that we have now compared to what we had 6 years ago.

Operator

(Operator Instructions) And our next question comes from Myles Walton from Deutsche Bank.

Myles Alexander Walton - *Deutsche Bank AG, Research Division - Director and Senior Research Analyst*

I was hoping to follow up, I mean, maybe a clarification on TS first. I think, Chris, you said that there was a $3 million reversal. And I'm just kind of thinking sequentially, the margins in TS or the EBIT contribution in TS looks like clean extra charge. In 1Q, it'd have been $11 million. Clean [ex] reversal, I guess, would have been $6 million sequentially despite a higher volume. Can you talk to the mix there and also where you are relative to the 5% to 7% long-range margin target?

Christopher D. Kastner - *Huntington Ingalls Industries, Inc. - CFO and EVP of Business Management*

Yes. So notwithstanding what's going on with the Westinghouse bankruptcy and how that eventually shakes out. We still think 2017 could be low single digits subject to that bankruptcy and how that flows through, and then we believe we're on pace to get to 5% to 7% by 2020.

Myles Alexander Walton - *Deutsche Bank AG, Research Division - Director and Senior Research Analyst*

Okay. And then, Mike or Chris, I don't know which -- in terms of the Avondale restructuring and shut down and the claim, I know that you're going through the DoD side of contracts claims at this point. How key is this P&L to that process and kind of a pathway to recovering that $300 million or so in the restructuring and shutdown?

Christopher D. Kastner - *Huntington Ingalls Industries, Inc. - CFO and EVP of Business Management*

It really isn't. There's an assumption made within the restructuring proposal for an ultimate disposition. So while it may modify the ultimate value of debt, it doesn't really impact it.

Myles Alexander Walton - *Deutsche Bank AG, Research Division - Director and Senior Research Analyst*

What's the time line of your current claim?

Christopher D. Kastner - *Huntington Ingalls Industries, Inc. - CFO and EVP of Business Management*

That could carry on 12 to 24 months. We are still negotiating informally with the Navy to try to get to resolution, but that could take a year to 1.5 years, 2 years.

Operator

And our next question comes from Doug Harned from Bernstein.

Douglas Stuart Harned - *Sanford C. Bernstein & Co., LLC., Research Division - SVP and Senior Analyst*

If we go back to CVN-79, Kennedy. Let's -- if you think about most of your mature programs on fixed-price contracts, these tend to be double-digit margins, and this is obviously the first fixed-price contract of this class. But if you look at it and think about if you stay on plan, is this a ship that you could do a double-digit margin on?

C. Michael Petters - *Huntington Ingalls Industries, Inc. - CEO, President & Director*

Well, let me just say, Doug, we're talking about a program that's going to play out over the next 6 years or so, 5 years anyway. And could we? Sure. Are we targeting that? You bet. Is there a lot of work to do between now and then? Absolutely. So we're watching it. We're working it. We're engaged in it. We certainly are pushing hard for that outcome.

Douglas Stuart Harned - *Sanford C. Bernstein & Co., LLC., Research Division - SVP and Senior Analyst*

And this is so -- that's good to hear. So this is something that you're going to see how this evolves over time as you reduce risk, and hopefully, you can get there on this one...

C. Michael Petters - *Huntington Ingalls Industries, Inc. - CEO, President & Director*

Yes, just like we do on every other program.

Douglas Stuart Harned - *Sanford C. Bernstein & Co., LLC., Research Division - SVP and Senior Analyst*

I just also wanted to ask, on the budget, we've obviously, as you described, have a whole range of scenarios here with some pretty attractive budgets, I would say, from a shipbuilding standpoint, if you look at what's in the House committees down to what if we have no debt ceiling relief, what if you can't do anything about BCA. When we look forward to the investments that you would need to make, should we ramp up the shipbuilding outlook? What do you look for as the trigger for when you can start to make some of those investments looking at some possible growth?

C. Michael Petters - *Huntington Ingalls Industries, Inc. - CEO, President & Director*

Yes, I'm not -- Doug, that's a really good question. I'm not sure there's a single light switch that I'm going to say if they fix that, then we're off and running. I would tell you that if they were to, and in the best of all universes, if somebody decided to just figure out how to make sequestration go away, that will be a pretty big indicator because the driver for that would be the requirements are just getting to be so loud that we got to go do something different than we're doing. But that's probably the biggest indicator, watching how the -- how do we maneuver our way through that. If we do another 2-year deal, that's probably -- that's not as good as making it go away, but that's better than not doing it. How this discussion goes on the debt ceiling, we'll be watching that. And all of that goes into the soup as we start to make our decisions. The advantage we have is that we can actually start to deploy our capital ahead of the Navy's decision to buy ships, and so -- because we get to watch and see how these other things happen in the appropriations process. And we'll be able to stay ahead of that, and we can throttle that and measure that based on our assessment of the terrain at that point in time. Our assessment right now is it's too early for us to get out in front of our headlights and start investing against the 355-ship Navy. It's not too early to continue the investment that we're making to support the 300-ship Navy.

Christopher D. Kastner - *Huntington Ingalls Industries, Inc. - CFO and EVP of Business Management*

Doug, I could -- I'd like to add that, tactically, the RFP for DDG 51, the quantity and the pace of those and then the Block V [ECS] RFP should show up later this year, and that will give us some indication of how quickly they want to buy those ships.

C. Michael Petters - *Huntington Ingalls Industries, Inc. - CEO, President & Director*

Yes, and if -- and that's true. And if the Congress gave the Navy to the authority to procure more than one aircraft carrier, we'd see that as a really big signal. I don't believe the Congress could do that without having some solution to the BCA. But if -- certainly, if we sit down and start negotiating with the Navy, the -- instead of the CVN-80 contract we're negotiating 2 carriers or 3 carriers, we're going to be a whole lot more inclined to go and invest against the 355 ship Navy. And I would tell you, Doug, that our suppliers would be a whole lot more inclined to it then, too.

Operator

And our next question comes from Noah Poponak from Goldman Sachs.

Matthew Porat - *Goldman Sachs Group Inc., Research Division - Research Analyst*

It's Matt Porat on for Noah. So I wanted to sort of go back to TS for a moment. You've talked about sort of some of the synergies from a sales standpoint, and I was looking to get a bit of a better sense for some of the levers you're looking to pull to sort of see those margins track a little higher?

Christopher D. Kastner - *Huntington Ingalls Industries, Inc. - CFO and EVP of Business Management*

Actually, there'll be a natural growth in those margins based upon getting some result in the nuclear sector. And winning deal, we were to -- you saw the first win with the Nevada test site. So the investments we're making within TS, if those yield some wins. And then really getting the cost structure squared away in oil and gas, they had a fairly good first quarter where they essentially broke even. And if there's a lift in that market, that could potentially show us some growth as well.

Matthew Porat - *Goldman Sachs Group Inc., Research Division - Research Analyst*

And what kind of growth are you kind of looking at from UniversalPegasus going forward here?

Christopher D. Kastner - *Huntington Ingalls Industries, Inc. - CFO and EVP of Business Management*

Well, we're talking about low single digits for the entire TS space.

Operator

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

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

Great results at Ingalls. So you mentioned Ingalls has been kind of outperforming for a while now, which is obvious. I guess, the question is, are there any other kind of major risk retirement events as you move through the rest of this year and into 2018 that we can look for as potential risk retirement events that could be as significant as what we saw in Q2?

Christopher D. Kastner - *Huntington Ingalls Industries, Inc. - CFO and EVP of Business Management*

That's a good question. I'd indicated previously I thought margin would be a bit back-end loaded for this year. Fortunately, Ingalls had a very good Q2 related to that quality launch on LHA 7. So I really think the best way to think about shipbuilding is 9% to 10% return on sales for the balance of the year.

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

Okay. And then when we look into next -- you previously -- [you guided] -- you talked about CVN-79 that there's no major risk retirement opportunities through 2020, I believe. I just want -- do you have updated view on that? Is that still...

Christopher D. Kastner - *Huntington Ingalls Industries, Inc. - CFO and EVP of Business Management*

No, the launch for CVN-79 is 2020, and there's really no risk significant risk retirement milestone until then for 79.

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

Okay. And then just any comments on where we stand with the icebreaker competition in [RFD]. If that's out, you have an -- what your expectations are for that program?

C. Michael Petters - *Huntington Ingalls Industries, Inc. - CEO, President & Director*

Well, I mean, we're very interested in the program, and we're engaged in the studies that are going on right now to -- as the program begins to take shape. I think it's going to take a little bit to work its way through. Obviously, the more complex the platform needs to be, the more likely we are to be a major player and trying to sort through it. We think icebreakers tend to be really complex platforms, and so we're excited to be part of the program, and we're putting our best foot forward.

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

Do you have a sense of the timing of that program?

C. Michael Petters - *Huntington Ingalls Industries, Inc. - CEO, President & Director*

It's moved -- at this point, it's moved a little bit faster than I would've thought. But I think that program is also going to be driven by -- from a timing perspective, it's going to be driven by all of the other budget discussions that are going on. There's a lot of stuff that could move faster if we can get the budget stuff out of the way. This would certainly be one of them.

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

Okay. And last one for me. Chris, any preliminary view on cash pension for 2018?

Christopher D. Kastner - *Huntington Ingalls Industries, Inc. - CFO and EVP of Business Management*

No, Gautam, thanks for the question. It's a bit too early from contributions or cash pension in 2018. I'll be able to provide you more color as we get towards the end of the year.

Operator

And at this time, I am showing no further questions.

C. Michael Petters - *Huntington Ingalls Industries, Inc. - CEO, President & Director*

Okay. Well, thanks to everybody for joining us on today's call. We're excited about what's happening in our business, and we're looking forward to creating more and more value, doing hard stuff and getting it done right for a lot of customers. Thank you all very much.

Operator

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