

KAMAN Corp
Form 10-Q
October 26, 2017

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 29, 2017

Or
 TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission File Number: 001-35419

KAMAN CORPORATION

(Exact name of registrant as specified in its charter)

Connecticut 06-0613548
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

1332 Blue Hills Avenue
Bloomfield, Connecticut 06002
(Address of principal executive offices) (Zip Code)
(860) 243-7100
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

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Large accelerated filer Accelerated filer Non-accelerated filer
Smaller reporting company Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

At October 20, 2017, there were 27,815,173 shares of Common Stock outstanding.

PART I

Item 1. Financial Statements

CONDENSED CONSOLIDATED BALANCE SHEETS

KAMAN CORPORATION AND SUBSIDIARIES

(In thousands, except share and per share amounts) (Unaudited)

	September 29, 2017	December 31, 2016
Assets		
Current assets:		
Cash and cash equivalents	\$ 35,429	\$ 41,205
Accounts receivable, net	280,440	230,864
Inventories	385,654	393,814
Income tax refunds receivable	638	6,065
Other current assets	30,737	26,605
Total current assets	732,898	698,553
Property, plant and equipment, net of accumulated depreciation of \$245,292 and \$226,366, respectively	183,106	176,521
Goodwill	349,893	337,894
Other intangible assets, net	120,034	126,444
Deferred income taxes	48,658	59,373
Other assets	24,852	27,501
Total assets	\$ 1,459,441	\$ 1,426,286
Liabilities and Shareholders' Equity		
Current liabilities:		
Current portion of long-term debt, net of debt issuance costs	\$ 18,984	\$ 119,548
Accounts payable – trade	111,958	116,663
Accrued salaries and wages	47,990	43,165
Advances on contracts	14,814	13,356
Income taxes payable	5,058	1,165
Other current liabilities	58,503	59,989
Total current liabilities	257,307	353,886
Long-term debt, excluding current portion, net of debt issuance costs	394,459	296,598
Deferred income taxes	7,766	6,875
Underfunded pension	136,755	156,427
Other long-term liabilities	44,418	44,916
Commitments and contingencies (Note 11)		
Temporary equity, convertible notes	11	1,797
Shareholders' equity:		
Preferred stock, \$1 par value, 200,000 shares authorized; none outstanding	—	—
Common stock, \$1 par value, 50,000,000 shares authorized; voting; 29,071,569 and 28,162,497 shares issued, respectively	29,072	28,162
Additional paid-in capital	181,528	171,162
Retained earnings	579,648	560,200
Accumulated other comprehensive income (loss)	(125,579)	(156,393)
Less 1,238,311 and 1,054,364 shares of common stock, respectively, held in treasury, at cost	(45,944)	(37,344)
Total shareholders' equity	618,725	565,787
Total liabilities and shareholders' equity	\$ 1,459,441	\$ 1,426,286

See accompanying notes to condensed consolidated financial statements.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

KAMAN CORPORATION AND SUBSIDIARIES

(In thousands, except per share amounts) (Unaudited)

	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2017	September 30, 2016	September 29, 2017	September 30, 2016
Net sales	\$447,046	\$ 453,474	\$1,331,993	\$ 1,375,314
Cost of sales	308,111	317,984	933,279	961,628
Gross profit	138,935	135,490	398,714	413,686
Selling, general and administrative expenses	106,349	104,060	324,533	333,726
Restructuring costs	2,500	344	2,500	691
Net (gain) loss on sale of assets	(212	) 24	(217	) 10
Operating income	30,298	31,062	71,898	79,259
Interest expense, net	5,264	4,165	15,546	11,960
Other expense (income), net	(483	) (332	) (711	) 243
Earnings before income taxes	25,517	27,229	57,063	67,056
Income tax expense	9,237	9,774	21,034	23,329
Net earnings	\$16,280	\$ 17,455	\$36,029	\$ 43,727
Earnings per share:				
Basic earnings per share	\$0.58	\$ 0.64	\$1.31	\$ 1.61
Diluted earnings per share	\$0.58	\$ 0.62	\$1.27	\$ 1.56
Average shares outstanding:				
Basic	27,907	27,128	27,536	27,096
Diluted	28,219	28,080	28,319	27,943
Dividends declared per share	\$0.20	\$ 0.18	\$0.60	\$ 0.54

See accompanying notes to condensed consolidated financial statements.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

KAMAN CORPORATION AND SUBSIDIARIES

(In thousands) (Unaudited)

	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2017	September 30, 2016	September 30, 2017	September 30, 2016
Net earnings	\$16,280	\$ 17,455	\$36,029	\$ 43,727
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustments	7,731	1,050	24,105	1,085
Unrealized gain (loss) on derivative instruments, net of tax expense (benefit) of (\$43) and \$205 and \$72 and (\$227), respectively	(70	) 338	121	(374
Change in pension and post-retirement benefit plan liabilities, net of tax expense of \$1,309 and \$1,213 and \$3,979 and \$3,641, respectively	2,220	2,005	6,588	6,015
Other comprehensive income	9,881	3,393	30,814	6,726
Comprehensive income	\$26,161	\$ 20,848	\$66,843	\$ 50,453

See accompanying notes to condensed consolidated financial statements.

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS
KAMAN CORPORATION AND SUBSIDIARIES
(In thousands) (Unaudited)

	For the Nine Months Ended		
	September 29, 2017	September 30, 2016	
Cash flows from operating activities:			
Net earnings	\$36,029	\$ 43,727	
Adjustments to reconcile net earnings to net cash provided by (used in) operating activities:			
Depreciation and amortization	31,919	32,583	
Amortization of debt issuance costs	1,564	1,149	
Accretion of convertible notes discount	2,769	1,598	
Provision for doubtful accounts	743	1,021	
Net (gain) loss on sale of assets	(217	) 10
Loss on debt extinguishment	137	—	
Net (gain) loss on derivative instruments	(789	) 783
Stock compensation expense	4,917	4,711	
Excess tax benefit from share-based compensation arrangements	—	(302)
Deferred income taxes	6,450	3,993	
Changes in assets and liabilities, excluding effects of acquisitions/divestitures:			
Accounts receivable	(44,537) (12,011)
Inventories	12,317	(10,050)
Income tax refunds receivable	5,430	883	
Other current assets	(2,084	) 1,271
Accounts payable - trade	(5,373	) 967
Accrued contract losses	231	468	
Accrued restructuring costs	1,467	(673)
Advances on contracts	1,458	3,573	
Other accruals and payables	1,850	7,229	
Income taxes payable	3,830	28	
Pension liabilities	(11,531) (9,318)
Other long-term liabilities	(2,746) (1,624)
Net cash provided by operating activities	43,834	70,016	
Cash flows from investing activities:			
Proceeds from sale of assets	513	190	
Expenditures for property, plant & equipment	(19,874) (23,926)
Acquisition of businesses (net of cash acquired)	(1,365) (6,631)
Other, net	(2,375) (442)
Net cash used in investing activities	(23,101) (30,809)
Cash flows from financing activities:			
Net borrowings (repayments) under revolving credit agreements	(73,779) (12,959)
Debt repayment	(5,000) (3,750)
Proceeds from the issuance of 2024 convertible notes	200,000	—	
Repayment of 2017 convertible notes	(163,654) —	
Purchase of capped call - 2024 convertible notes	(20,500) —	
Proceeds from bond hedge settlement - 2017 convertible notes	58,564	—	
Bank overdraft	1,115	3,427	
Proceeds from exercise of employee stock awards	5,426	7,094	
Purchase of treasury shares	(6,931) (8,989)

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Dividends paid	(15,892)	(14,625)
Debt and equity issuance costs	(7,469)	—
Other	(379)	(246)
Windfall tax benefit	—	302
Net cash used in financing activities	(28,499)	(29,746)
Net (decrease) increase in cash and cash equivalents	(7,766)	9,461
Effect of exchange rate changes on cash and cash equivalents	1,990	(372)
Cash and cash equivalents at beginning of period	41,205	16,462
Cash and cash equivalents at end of period	\$35,429	\$ 25,551

Supplemental disclosure of noncash activities:

Common shares issued for partial unwind of warrant transactions \$30,279 \$ —

See accompanying notes to condensed consolidated financial statements.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016
(Unaudited)

1. BASIS OF PRESENTATION

The December 31, 2016, Condensed Consolidated Balance Sheet amounts have been derived from the previously audited Consolidated Balance Sheet of Kaman Corporation and subsidiaries (collectively, the "Company"), but do not include all disclosures required by accounting principles generally accepted in the United States of America ("US GAAP"). In the opinion of management, the condensed consolidated financial information reflects all adjustments necessary for a fair statement of the Company's financial position, results of operations and cash flows for the interim periods presented. All such adjustments are of a normal recurring nature, unless otherwise disclosed in this report. Certain amounts in prior year financial statements and notes thereto have been reclassified to conform to current year presentation. The statements should be read in conjunction with the consolidated financial statements and notes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2016. The results of operations for the interim periods presented are not necessarily indicative of trends or of results to be expected for the entire year.

The Company has a calendar year-end; however, its first three fiscal quarters follow a 13-week convention, with each quarter ending on a Friday. The third quarters for 2017 and 2016 ended on September 29, 2017, and September 30, 2016, respectively.

2. RECENT ACCOUNTING STANDARDS

In August 2017, the FASB issued Accounting Standards Update ("ASU") 2017-12, "Derivatives and Hedging (Topic 815) - Targeted Improvements to Accounting for Hedging Activities". The objective of this standard update is to improve the financial reporting of hedging relationships to better reflect the economic results of an entity's risk management activities in its financial statements. This ASU expands hedge accounting for both nonfinancial and financial risk components and refines the measurement of hedge results to better reflect an entity's hedging strategies. The standard update is effective for fiscal years, and interim periods within those years, beginning after December 15, 2018. Early adoption is permitted. The adoption of this standard update is not expected to have a material impact on the Company's consolidated financial statements.

In May 2017, the FASB issued ASU 2017-09, "Compensation - Stock Compensation (Topic 718) - Scope of Modification Accounting". The objective of this standard update is to address the diversity in practice and reduce the cost and complexity of applying guidance for a change to the terms or conditions of a share-based payment award. This ASU provides guidance on when an entity should apply modification accounting for stock compensation. The standard update is effective for fiscal years, and interim periods within those years, beginning after December 15, 2017. Early adoption is permitted. The adoption of this standard update is not expected to have a material impact on the Company's consolidated financial statements.

In March 2017, the FASB issued ASU 2017-08, "Receivables - Nonrefundable Fees and Other Costs (Subtopic 310-20) - Premium Amortization on Purchased Callable Debt Securities". Under this ASU, the amortization period for certain callable debt securities held at a premium is shortened to more closely align the amortization period with expectations incorporated in market pricing on the underlying securities. The standard update is effective for fiscal years, and interim periods within those years, beginning after December 15, 2018. Early adoption is permitted. The Company is currently assessing the potential impact this standard update might have on its consolidated financial statements.

In March 2017, the FASB issued ASU 2017-07, "Compensation - Retirement Benefits (Topic 715) - Improving the Net Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost". The objective of this standard update is to improve the presentation of net periodic pension cost and net periodic postretirement benefit cost. This standard update requires employers to disaggregate the service cost component from the other components of net benefit cost. This ASU also provides guidance on how to present the service cost component and the other

components of net benefit cost in the income statement and allows only the service cost component of net benefit cost to be eligible for capitalization. The other components of net benefit cost, which are expected to more than offset the service cost component, are required to be presented in the income statement separately from the service cost component and outside of operating profit. The standard update is effective for fiscal years, and interim periods within those years, beginning after December 15, 2017. The Company currently estimates that the service cost component to be included in operating profit will be approximately \$4.9 million in 2018.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016
(Unaudited)

2. RECENT ACCOUNTING STANDARDS (CONTINUED)

In February 2017, the FASB issued ASU 2017-05, "Other Income - Gains and Losses from the Derecognition of Nonfinancial Assets (Subtopic 610-20)". The objective of this standard update is to clarify the scope of asset derecognition guidance and to provide new guidance for partial sales of nonfinancial assets. The standard update is effective for fiscal years, and interim periods within those years, beginning after December 15, 2017. Early adoption is permitted, however, an entity is required to apply the amendments in this ASU in the same period that it applies the amendments for ASU 2014-09. The adoption of this standard update is not expected to have a material impact on the Company's consolidated financial statements.

In January 2017, the FASB issued ASU 2017-04, "Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment". The objective of this standard update is to simplify the subsequent measurement of goodwill, eliminating Step 2 from the goodwill impairment test. Under this ASU, an entity should perform its annual goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An entity would recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit's fair value, assuming the loss recognized does not exceed the total amount of goodwill for the reporting unit. The standard update is effective for fiscal years beginning after December 15, 2019. Early adoption is permitted. The impact of the adoption of this standard update is dependent on the Company's goodwill impairment assessment.

In November 2016, the FASB issued ASU 2016-18, "Statement of Cash Flows (Topic 230) - Restricted Cash". The objective of this standard update is to address the diversity in classification and presentation of changes in restricted cash on the statement of cash flows. Under this ASU, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The standard update is effective for fiscal years, and interim periods within those years, beginning after December 15, 2017. Early adoption is permitted. The adoption of this standard update is not expected to have a material impact on the Company's consolidated financial statements.

In October 2016, the FASB issued ASU 2016-16, "Income Taxes (Topic 740) - Intra-Entity Transfers of Assets Other Than Inventory". Under this ASU, income tax consequences of an intra-entity transfer of an asset other than inventory will be recognized when the transfer occurs. The standard update is effective for fiscal years, and interim periods within those years, beginning after December 15, 2017. Early adoption is permitted. The adoption of this standard update is not expected to have a material impact on the Company's consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, "Statement of Cash Flows (Topic 230) - Classification of Certain Cash Receipts and Cash Payments". This standard update was issued to address diversity in practice in how certain cash receipts and cash payments are presented and classified. The provisions of ASU 2016-15 will be effective for interim and annual periods beginning after December 15, 2017. Early adoption is permitted. The adoption of this standard update is not expected to have a material impact on the Company's consolidated financial statements.

In March 2016, the FASB issued ASU 2016-07, "Investments - Equity Method and Joint Ventures (Topic 323) - Simplifying the Transition to the Equity Method of Accounting". This standard update eliminates the requirement to retroactively adopt the equity method of accounting when an investment qualifies for use of the equity method. The standard update is effective for fiscal years, and interim periods within those years, beginning after December 15, 2016. The adoption of this standard update did not have a material impact on the Company's consolidated financial statements.

In March 2016, the FASB issued ASU 2016-06, "Derivatives and Hedging (Topic 815) - Contingent Put and Call Options in Debt Instruments". The objective of this standard update is to eliminate inconsistent practices with regards to assessing embedded contingent put and call options in debt instruments. The standard update is effective for fiscal years, and interim periods within those years, beginning after December 15, 2016. The adoption of this standard

update did not have a material impact on the Company's consolidated financial statements.

In March 2016, the FASB issued ASU 2016-05, "Derivatives and Hedging (Topic 815) - Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships". The objective of this standard update is to clarify whether a change in the counterparty to a derivative instrument results in a requirement to dedesignate that hedging relationship and discontinue the application of hedge accounting. The standard update is effective for fiscal years, and interim periods within those years, beginning after December 15, 2016. The adoption of this standard update did not have a material impact on the Company's consolidated financial statements.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016
(Unaudited)

2. RECENT ACCOUNTING STANDARDS (CONTINUED)

In February 2016, the FASB issued ASU 2016-02, "Leases (Topic 842)". Under this ASU as amended, lessees will be required to recognize the following for all leases (with the exception of short-term leases) at the commencement date: (i) a lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and (ii) a right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. Lessor accounting is largely unchanged under this ASU as amended. This standard update is effective for fiscal years, and interim periods within those years, beginning after December 15, 2018. Early adoption is permitted. The Company is developing a project plan to implement this standard update and is currently assessing the potential impact this standard update might have on its consolidated financial statements. The Company anticipates the ASU will have a material impact on its assets and liabilities due to the addition of right-of-use assets and lease liabilities to the balance sheet, however it does not expect the ASU to have a material impact on the Company's cash flows or results of operations.

In January 2016, the FASB issued ASU 2016-01, "Financial Instruments - Overall (Subtopic 825-10) - Recognition and Measurement of Financial Assets and Financial Liabilities". The objective of this standard update is to remove inconsistent practices with regards to the accounting for financial instruments between US GAAP and International Financial Reporting Standards ("IFRS"). The standard update intends to improve the reporting model for financial instruments to provide users of financial statements with more decision-useful information. The provisions of this standard update are effective for interim and annual periods beginning after December 15, 2017. The Company does not expect these changes to have a material impact on its consolidated financial statements.

In July 2015, the FASB issued ASU 2015-11, "Inventory (Topic 330) - Simplifying the Measurement of Inventory". ASU 2015-11 requires an entity to measure inventory within the scope of the standard at the lower of cost and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation. The standard update is effective for fiscal years beginning after December 15, 2016, including interim periods within those years. The adoption of this standard update did not have a material impact on the Company's consolidated financial statements.

Revenue Recognition

In May 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers (Topic 606)". The objective of this standard update is to remove inconsistent practices with regard to revenue recognition between US GAAP and IFRS. The standard intends to improve comparability of revenue recognition practices across entities, industries, jurisdictions and capital markets. The provisions of ASU No. 2014-09 will be effective for interim and annual periods beginning after December 15, 2017, with early adoption permitted for annual periods beginning after December 15, 2016. The Company has developed a project plan that includes a three-phase approach to implementing this standard update. Phase one, the assessment phase, was completed in early 2016. The Company concluded the second phase of the project, which included conversion activities such as establishing policies, identifying system impacts and developing a basic understanding of the impact this standard update will have on the Company's consolidated financial statements, during the fourth quarter of 2016. Phase three, which began during the first quarter of 2017, includes the integration of the standard update into financial reporting processes and systems, and developing a more robust understanding of the financial impact of this standard update on the Company's consolidated financial statements. The Company anticipates the transition to the new standard could have a material impact on the Company's consolidated financial statements but will be unable to quantify that impact until the third phase of the project has been completed. The Company expects the cost of the activities it is undertaking to transition to the new standard will result in an increase in selling, general and administrative expenses in 2017 and beyond.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016
(Unaudited)

2. RECENT ACCOUNTING STANDARDS (CONTINUED)

Revenue Recognition - continued

The Company intends to transition using the modified retrospective method upon adoption of this standard update. The Distribution segment currently recognizes the majority of its revenue at a point in time, whereas the new standard will result in certain revenue streams moving to an over time revenue recognition model. The majority of our long-term contracts in the Aerospace segment are currently accounted for under the percentage-of-completion method using units-of-delivery as a measurement basis. For these programs, early-contract unit costs in excess of the average expected cost over the life of the contract are capitalized and amortized over the number of units in the contract. With the adoption of this standard update, some deferred unit costs in excess of the contract average will be eliminated through retained earnings and will not be amortized into future earnings. The Company anticipates that many of these contracts will move to an over time revenue model under the percentage-of-completion method. For example, revenue for the Company's Joint Programmable Fuze ("JPF") program with the U.S. Government ("USG") will move from percentage-of-completion using units-of-delivery as the measurement basis to the over time revenue recognition model using input costs as the basis for recognizing progress to completion. Conversely, revenue for the K-MAX® program will move from cost-to-cost revenue recognition to point in time, with revenue on these aircraft being recognized upon delivery to the end customer. The Company is currently working to quantify the impact these changes will have on the financial statements; however, the ultimate impact cannot currently be determined as it will be dependent upon the terms of contracts with customers at such time and the Company's progress to completion as of December 31, 2017.

Subsequent to the issuance of ASU 2014-09, the FASB has issued the following updates: ASU 2015-14, "Revenue from Contracts with Customers (Topic 606) - Deferral of the Effective Date"; ASU 2016-08, "Revenue from Contracts with Customers (Topic 606) - Principal versus Agent Considerations (Reporting Revenue Gross versus Net)"; ASU 2016-10, "Revenue from Contracts with Customers (Topic 606) - Identifying Performance Obligations and Licensing"; ASU 2016-12, "Revenue from Contracts with Customers (Topic 606) - Narrow-Scope Improvements and Practical Expedients"; and ASU 2016-20, "Technical Corrections and Improvements to Topic 606". The amendments in these updates affect the guidance contained within ASU 2014-09 and are being assessed as part of the Company's revenue recognition project plan.

3. RESTRUCTURING COSTS

During the third quarter of 2017, the Company initiated restructuring activities at its Aerospace segment to support the ongoing effort of improving capacity utilization and operating efficiency to better position the Company for increased profitability and growth. Such actions include workforce reductions and the consolidation of operations, beginning in the third quarter of 2017 through the planned completion of restructuring activities in the fourth quarter of 2018. The Company currently expects these actions to result in approximately \$8.0 million to \$10.0 million in pre-tax restructuring charges, with approximately \$4.0 million expected to be recorded in 2017. Of these charges, \$5.5 million to \$6.5 million are expected to result from cash outlays for employee separation and other closure-related expenses. The Company anticipates these actions will result in total cost savings of approximately \$4.0 million annually beginning in 2019.

The following table summarizes the accrual balances by cost type for the restructuring actions:

Severance	Other (1)	Total
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In thousands

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Restructuring accrual balance at December 31, 2016	\$ —	\$—	\$—
Provision	1,292	178	1,470
Cash payments	—	—	—
Restructuring accrual balance at September 29, 2017	\$ 1,292	\$ 178	\$ 1,470

⁽¹⁾ Includes costs associated with consolidation of facilities.

The above accrual balance was included in other current liabilities on the Company's Consolidated Balance Sheets. For the three-month fiscal period ended September 29, 2017, restructuring expense, totaling \$2.5 million, was included in restructuring costs on the Company's Consolidated Statements of Operations. Included in this expense is approximately \$1.0 million of cost that primarily relates to the write-off of inventory for various small order programs that the Company will no longer continue to manufacture as a result of the consolidation of operations.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued
 For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016
 (Unaudited)

4. ACCOUNTS RECEIVABLE, NET

Accounts receivable, net consists of the following:

	September 29, 2017	December 31, 2016
In thousands		
Trade receivables	\$ 151,946	\$ 143,471
U.S. Government contracts:		
Billed	13,762	17,244
Costs and accrued profit – not billed	1,381	1,478
Commercial and other government contracts:		
Billed	84,519	50,560
Costs and accrued profit – not billed	32,992	22,234
Less allowance for doubtful accounts	(4,160)	(4,123)
Accounts receivable, net	\$ 280,440	\$ 230,864

The increase in commercial and other governments contracts billed was primarily related to receivables under the JPF program.

At December 31, 2016, \$3.7 million of unbilled receivables and accrued profit for the K-MAX® program were included in other assets on the Company's Condensed Consolidated Balance Sheet, as the amounts due were expected to be collected more than one year after the balance sheet date. At September 29, 2017, all receivables for the K-MAX® program were included in accounts receivable, net, as the amounts due are expected to be collected within one year of the balance sheet date.

Accounts receivable, net includes amounts for matters such as contract changes, negotiated settlements and claims for unanticipated contract costs. These amounts are as follows:

	September 29, 2017	December 31, 2016
In thousands		
Contract changes, negotiated settlements and claims for unanticipated contract costs	\$ 900	\$ 900

5. FAIR VALUE MEASUREMENTS

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date.

The Company uses a three-level fair value hierarchy that prioritizes the inputs used to measure fair value. This hierarchy requires the Company to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair value are as follows:

- Level 1 — Quoted prices in active markets for identical assets or liabilities.
- Level 2 — Observable inputs other than quoted prices included in Level 1, such as quoted prices in markets that are not active or other inputs that are observable or can be corroborated by observable market data.
- Level 3 — Unobservable inputs that are supported by little or no market activity and are significant to the fair value of the assets or liabilities. This includes certain pricing models, discounted cash flow methodologies and similar

techniques that use significant unobservable inputs.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016
(Unaudited)

5. FAIR VALUE MEASUREMENTS (CONTINUED)

The following table presents the carrying value and fair value of financial instruments that are not carried at fair value:

	September 29, 2017		December 31, 2016	
	Carrying Value	Fair Value	Carrying Value	Fair Value
In thousands				
Debt:				
Level 1	\$—	\$—	\$113,203	\$170,935
Level 2	420,127	446,490	303,855	279,582
Total	\$420,127	\$446,490	\$417,058	\$450,517

The above fair values were computed based on quoted market prices (Level 1 and 2) and discounted future cash flows (Level 2 observable inputs), as applicable. Differences from carrying values are attributable to interest rate changes subsequent to when the transactions occurred.

The fair values of cash and cash equivalents, accounts receivable, net and accounts payable - trade approximate their carrying amounts due to the short-term maturities of these instruments.

Recurring Fair Value Measurements

The Company holds derivative instruments for foreign exchange contracts and interest rate swaps that are measured at fair value using observable market inputs such as forward rates and our counterparties' credit risks. Based on these inputs, the derivative instruments are classified within Level 2 of the valuation hierarchy. At September 29, 2017, the derivative instruments have been included in other current assets on the Condensed Consolidated Balance Sheets. At December 31, 2016, the derivative instruments were included in other current liabilities and other long-term liabilities on the Condensed Consolidated Balance Sheets. Based on the Company's continued ability to trade and enter into forward contracts and interest rate swaps, we consider the markets for our fair value instruments to be active.

The Company evaluated the credit risk associated with the counterparties to these derivative instruments and determined that as of September 29, 2017, such credit risks have not had an adverse impact on the fair value of these instruments.

6. DERIVATIVE FINANCIAL INSTRUMENTS

The Company is exposed to certain risks relating to its ongoing business operations, including market risks relating to fluctuations in foreign currency exchange rates and interest rates. Derivative financial instruments are recognized on the Condensed Consolidated Balance Sheets as either assets or liabilities and are measured at fair value. Changes in the fair values of derivatives are recorded each period in earnings or accumulated other comprehensive income, depending on whether a derivative is effective as part of a hedged transaction. Gains and losses on derivative instruments reported in accumulated other comprehensive income are subsequently included in earnings in the periods in which earnings are affected by the hedged item. The Company does not use derivative instruments for speculative purposes.

Forward Exchange Contracts

The Company holds forward exchange contracts designed to hedge forecasted transactions denominated in foreign currencies and to minimize the impact of foreign currency fluctuations on the Company's earnings and cash flows. Some of these contracts are designated as cash flow hedges. The Company will include in earnings amounts currently included in accumulated other comprehensive income upon recognition of cost of sales related to the underlying transaction. These contracts were not material to the Company's Condensed Consolidated Balance Sheets as of September 29, 2017 and December 31, 2016. The activity related to these contracts was not material to the Company's Condensed Consolidated Financial Statements for the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016
(Unaudited)

6. DERIVATIVE FINANCIAL INSTRUMENTS (CONTINUED)

Interest Rate Swaps

The Term Loan Facility of the Company's Credit Agreement ("Term Loan") contains floating rate obligations and is subject to interest rate fluctuations. During 2015, the Company entered into interest rate swap agreements for the purposes of hedging the eight quarterly variable-rate Term Loan interest payments due in 2016 and 2017. Additionally, the Company entered into interest rate swap agreements to effectively convert \$83.8 million of its variable rate revolving credit facility debt to a fixed interest rate. These interest rate swap agreements were designated as cash flow hedges and intended to manage interest rate risk associated with the Company's variable-rate borrowings and minimize the impact on its earnings and cash flows of interest rate fluctuations attributable to changes in LIBOR rates. These agreements were not material to the Company's Condensed Consolidated Balance Sheets for the three-month and nine-month fiscal periods ended September 29, 2017 and December 31, 2016.

The activity related to these contracts was not material to the Company's Condensed Consolidated Financial Statements for the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016. Over the next twelve months, the income related to cash flow hedges expected to be reclassified from other comprehensive income is \$0.1 million.

7. INVENTORIES

Inventories consist of the following:

	September 29, 2017	December 31, 2016
In thousands		
Merchandise for resale	\$ 149,529	\$ 158,618
Raw materials	18,335	20,592
Contracts and other work in process (including certain general stock materials)	191,142	189,295
Finished goods	26,648	25,309
Total	\$ 385,654	\$ 393,814

Inventories include amounts associated with matters such as contract changes, negotiated settlements and claims for unanticipated contract costs. These amounts are as follows:

	September 29, 2017	December 31, 2016
In thousands		
Contract changes, negotiated settlements and claims for unanticipated contract costs	\$ 3,029	\$ 3,629

At September 29, 2017, and December 31, 2016, \$22.8 million and \$32.0 million, respectively, of K-MAX® inventory, including inventory associated with the new build aircraft, was included in contracts and other work in process inventory and finished goods on the Company's Condensed Consolidated Balance Sheets. Management believes that approximately \$14.9 million of the K-MAX® inventory will be sold after September 29, 2018, based upon the anticipation of additional aircraft manufacturing and supporting the fleet for the foreseeable future.

At September 29, 2017, and December 31, 2016, \$6.5 million and \$7.2 million, respectively, of SH-2G(I) inventory was included in contracts and other work in process inventory on the Company's Condensed Consolidated Balance Sheets. Management believes that approximately \$3.4 million of the SH-2G(I) inventory will be sold after September

29, 2018. This balance represents spares requirements and inventory to be used on SH-2G programs.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016
(Unaudited)

7. INVENTORIES (CONTINUED)

At September 29, 2017, backlog for the A-10 program with Boeing was \$1.4 million, representing 3 shipsets, and total program inventory was \$9.4 million, of which \$8.0 million is associated with nonrecurring costs. Through September 29, 2017, the Company has delivered 170 shipsets over the life of the program. During 2016, the U.S. Air Force ("USAF") indicated that they would delay the retirement of the A-10 fleet due to its vital close air support, search and rescue capabilities and the lack of a suitable replacement. The Company continues to monitor the defense budget and understands that despite this positive indication, the future of this program could be at risk without the continued support of Congress. The Company has not received any orders for additional shipsets in 2017, and as such, expects a break in production as it completes the units currently on order and waits for follow-on orders from the customer. The customer has not given any indication that this program will be terminated. Final production and deliveries of existing orders under this contract are anticipated to be completed during the fourth quarter of 2017. Tooling and nonrecurring costs on this program are being amortized over 242 shipsets, the number of shipsets under the program of record. These nonrecurring costs may not be recoverable in the event of an extended break in production or program termination.

Long-term Contracts

For long-term aerospace contracts, the Company generally recognizes revenue and cost of sales using the percentage-of-completion method of accounting, which allows for recognition of revenue as work on a contract progresses. The Company recognizes revenues and cost of sales based on either (1) the cost-to-cost method, in which case sales and profit are recorded based upon the ratio of costs incurred to estimated total costs to complete the contract, or (2) the units-of-delivery method, in which case sales are recognized as deliveries are made and cost of sales is computed on the basis of the estimated ratio of total cost to total sales.

Revenue and cost estimates for all significant long-term contracts for which revenue is recognized using the percentage-of-completion method of accounting are reviewed and reassessed quarterly. Based upon these reviews, the Company records the effects of adjustments in profit estimates each period. If at any time the Company determines that in the case of a particular contract total costs will exceed total contract revenue, the Company will record a provision for the entire anticipated contract loss at that time. For the three-month and nine-month fiscal periods ended September 29, 2017, there were net increases in the Company's operating income attributable to changes in contract estimates of \$1.1 million and \$3.2 million, respectively. These increases were primarily a result of improved performance on the AH-1Z program, JPF program and the SH-2G program with Peru. These improvements were partially offset by cost growth on the K-MAX® and A-10 programs. There were net decreases in the Company's operating income from changes in contract estimates of \$1.3 million and \$3.9 million, respectively, for the three-month and nine-month fiscal periods ended September 30, 2016. These decreases were primarily a result of cost growth on various programs, including the Boeing 767/777 program, the A-10 program and a composites assembly program. For the nine-month fiscal period, these decreases were partially offset by improved performance on the JPF program.

8. GOODWILL AND OTHER INTANGIBLE ASSETS, NET

Goodwill

The following table sets forth the change in the carrying amount of goodwill for each reportable segment and for the Company:

Distribution Aerospace Total

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In thousands

Gross balance at December 31, 2016	\$ 149,204	\$ 204,942	\$ 354,146
Accumulated impairment	—	(16,252)	(16,252)
Net balance at December 31, 2016	149,204	188,690	337,894
Additions	—	—	—
Impairments	—	—	—
Foreign currency translation	—	11,999	11,999
Ending balance at September 29, 2017	\$ 149,204	\$ 200,689	\$ 349,893

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016
(Unaudited)

8. GOODWILL AND OTHER INTANGIBLE ASSETS, NET (CONTINUED)

In accordance with ASC 350, Intangibles - Goodwill and Other ("ASC 350"), the Company evaluates goodwill for possible impairment on at least an annual basis. The Company is currently in the process of preparing its forecast, which it will use to complete its annual evaluation during the fourth quarter. Based upon information obtained at this point in the forecast process, management has determined that the Company will perform a quantitative assessment, rather than a qualitative assessment, for the Aerosystems reporting unit. The quantitative assessment could result in the determination that there has been an impairment of some or all of the goodwill associated with this reporting unit. The goodwill associated with the Aerosystems reporting unit is \$51.7 million.

Other intangible assets consisted of:

	Amortization Period	At September 29, 2017		At December 31, 2016	
		Gross Amount	Accumulated Amortization	Gross Amount	Accumulated Amortization
In thousands					
Customer lists / relationships	6-26 years	\$ 158,986	\$ (61,842)	\$ 154,745	\$ (51,800)
Developed technologies	10-20 years	19,998	(2,443)	19,049	(1,394)
Trademarks / trade names	3-15 years	8,906	(3,770)	8,344	(3,250)
Non-compete agreements and other	1-9 years	8,312	(8,203)	8,096	(7,444)
Patents	17 years	523	(433)	523	(425)
Total		\$ 196,725	\$ (76,691)	\$ 190,757	\$ (64,313)

The changes in other intangible assets are due to changes in foreign currency exchange rates.

In accordance with ASC 360 - Property, Plant, and Equipment ("ASC 360"), the Company is required to evaluate long-lived intangible assets for possible impairment whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. We are continuing to monitor the ongoing operating performance of our U.K. and Engineering Services facilities, including an ongoing assessment for potential triggering events that would require further evaluation. The total amount of intangible assets at our U.K. and Engineering Services businesses at September 29, 2017 was \$11.4 million and \$1.3 million, respectively.

9. DEBT

Convertible Notes

Overview

During the fiscal quarter ending June 30, 2017, the Company issued \$200.0 million aggregate principal amount of convertible senior unsecured notes due May 2024 (the "2024 Notes") pursuant to an indenture (the "Indenture"), dated May 12, 2017, between the Company and U.S. Bank National Association, as trustee. In connection therewith, the Company entered into certain capped call transactions that cover, collectively, the number of shares of the Company's common stock underlying the 2024 Notes. In a separate transaction, the Company repurchased \$103.5 million aggregate principal amount of its existing convertible senior unsecured notes due November 15, 2017 (the "2017 Notes"). In connection with the repurchase of the 2017 Notes, the Company settled a portion of the associated outstanding bond hedge transactions and warrant transactions it entered into in 2010 in connection with their issuance. See below for further discussion on the issuance of the 2024 Notes, the repurchase of the 2017 Notes and the related

transactions.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued
 For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016
 (Unaudited)

9. DEBT (CONTINUED)

Convertible Notes - continued

2024 Notes

On May 12, 2017, the Company issued \$175.0 million in principal amount of 2024 Notes, in a private placement offering. On May 24, 2017, the Company issued an additional \$25.0 million in principal amount of 2024 Notes pursuant to the initial purchasers' exercise of their overallotment option, resulting in the issuance of an aggregate \$200.0 million principal amount of 2024 Notes. The 2024 Notes bear 3.25% interest per annum on the principal amount, payable semiannually in arrears on May 1 and November 1 of each year, beginning on November 1, 2017. The 2024 Notes will mature on May 1, 2024, unless earlier repurchased by the Company or converted. The Company will settle any conversions of the 2024 Notes in cash, shares of the Company's common stock or a combination of cash and shares of common stock, at the Company's election.

Use of proceeds from the issuance of the 2024 Notes was as follows:

in thousands

Proceeds:

Gross proceeds	\$200,000
Commission fees and other expenses ⁽¹⁾	(7,348)
Net proceeds	\$192,652

Use of Proceeds:

Cost to repurchase \$103.5 million aggregate principal amount of 2017 Notes ⁽²⁾	\$(165,308)
Cost for capped call transaction related to 2024 Notes	(20,500)
Payment made to reduce revolving credit facility ⁽³⁾	(6,844)
Total use of proceeds	\$(192,652)

⁽¹⁾ Debt issuance fees paid to the counterparties and other expenses (i.e. legal and accounting fees) related to the issuance of the 2024 Notes were capitalized.

⁽²⁾ Included in this balance is \$1.7 million of related accrued interest payments.

⁽³⁾ Additional payments to the revolving credit facility were made from proceeds received as part of the bond hedge settlement related to the repurchase of the 2017 Notes. See the 2017 Notes section below for further discussion.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016
(Unaudited)

9. DEBT (CONTINUED)

Convertible Notes - continued

2024 Notes - continued

The following table illustrates the conversion rate at the date of transaction:

2024 Notes

Conversion Rate per \$1,000 principal amount ⁽¹⁾	15.3227
Conversion Price ⁽²⁾	\$65.2626
Contingent Conversion Price ⁽³⁾	\$84.84
Aggregate shares to be issued upon conversion ⁽⁴⁾	3,064,540

⁽¹⁾ Represents the number of shares of Common Stock hypothetically issuable per each \$1,000 principal amount of 2024 Notes, subject to adjustments upon the occurrence of certain specified events in accordance with the terms of the Indenture.

⁽²⁾ Represents \$1,000 divided by the conversion rate as of such date. The conversion price reflects the strike price of the embedded option within the 2024 Notes. If the Company's share price exceeds the conversion price at conversion, the noteholders would be entitled to receive additional consideration either in cash, shares or a combination thereof, the form of which is at the sole discretion of the Company.

⁽³⁾ Prior to November 1, 2023, the notes are convertible only in the following circumstances: (1) during any fiscal quarter commencing after July 1, 2017, and only during any such fiscal quarter, if the last reported sale price of the Company's common stock was greater than or equal to 130% of the applicable conversion price for at least 20 trading days (whether or not consecutive) during the 30 consecutive trading days ending on, and including, the last trading day of the immediately preceding fiscal quarter, (2) during the five consecutive business day period following any ten consecutive trading day period (the "measurement period") in which the trading price per \$1,000 principal amount of 2024 Notes for each trading day of the measurement period was less than 98% of the product of the last reported sale price of the Company's common stock and the conversion rate on each such trading day or (3) upon the occurrence of specified corporate events. On or after November 1, 2023, until the close of business on the second scheduled trading day immediately preceding the maturity date, holders may convert their notes at any time, regardless of the foregoing circumstances. If the Company undergoes a fundamental change (as defined in the Indenture), holders of the notes may require the Company to repurchase all or a portion of their notes for cash at a repurchase price equal to 100% of the principal amount to be repurchased, plus any accrued and unpaid interest. As of September 29, 2017, none of the conditions permitting the holders of the 2024 Notes to convert had been met. Therefore, the 2024 Notes are classified as long-term debt.

⁽⁴⁾ This represents the number of shares hypothetically issuable upon conversion of 100% of the outstanding aggregate principal amount of the 2024 Notes at each date; however, the terms of the 2024 Notes state that the Company may pay or deliver, as the case may be, cash, shares of the Company's common stock or a combination of cash and shares of common stock, at the Company's election. The Company currently intends to settle the aggregate principal amount in cash. Amounts due in excess of the principal, if any, also may be settled in cash, shares of the Company's common stock or a combination of cash and shares of common stock, at the Company's election.

In connection with the 2024 Notes offering, the Company entered into capped call transactions with certain of the initial purchasers or their respective affiliates. These transactions are intended to reduce the potential dilution to the Company's shareholders and/or offset the cash payments the Company is required to make in excess of the principal amount upon any future conversion of the notes in the event that the market price per share of the Company's common stock is greater than the strike price of the capped call transactions, with such reduction and/or offset subject to a cap

based on the cap price of the capped call transactions. Under the terms of the capped call transactions, the strike price (\$65.2626) and the cap price (\$88.7570) are each subject to adjustment in certain circumstances. In connection with establishing their initial hedges of the capped call transactions, the option counterparties or their respective affiliates entered into various derivative transactions with respect to the Company's common stock concurrently with or shortly after the pricing of the notes. The capped call transactions, which cost an aggregate \$20.5 million, were recorded as a reduction of additional paid-in capital.

Accounting Standards Codification ("ASC") Topic 815 - Derivatives and Hedging ("ASC 815") provides that contracts are initially classified as equity if (1) the contract requires physical settlement or net-share settlement, or (2) the contract gives the company a choice of net-cash settlement or settlement in its own shares (physical settlement or net-share settlement). The settlement terms of our capped call transactions require net-share settlement. Based on the guidance in ASC 815, the capped call transactions were recorded as a reduction of equity as of the trade date. ASC 815 states that a reporting entity shall not consider contracts to be derivative instruments if the contract issued or held by the reporting entity is both indexed to its own stock and classified in shareholders' equity in its balance sheet. The Company concluded the capped call transactions should be accounted for in shareholders' equity and are, therefore, not to be considered a derivative instrument.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued
 For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016
 (Unaudited)

9. DEBT (CONTINUED)

Convertible Notes - continued

2024 Notes - continued

ASC 470-20 "Debt with Conversion and Other Options" ("ASC 470-20"), clarifies the accounting for convertible debt instruments that may be settled in cash upon conversion, including partial cash settlement. ASC 470-20 specifies that an issuer of such instruments should separately account for the liability and equity components of the instruments in a manner that reflects the issuer's non-convertible debt borrowing rate which interest costs are to be recognized in subsequent periods. The note payable principal balance for the 2024 Notes at the date of issuance of \$200.0 million was bifurcated into the debt component of \$179.5 million and the equity component of \$20.5 million. The difference between the note payable principal balance and the fair value of the debt component representing the debt discount is being accreted to interest expense over the term of the 2024 Notes. The fair value of the debt component was recognized using a 5.0% discount rate, representing the Company's borrowing rate at the date of issuance for a similar debt instrument without a conversion feature with an expected life of seven years.

The Company incurred \$7.4 million of debt issuance costs in connection with the sale of the 2024 Notes, which was allocated between the debt and equity components of the instrument. Of the total amount, \$0.7 million was recorded as an offset to additional paid-in capital. The balance, \$6.7 million, was recorded as a contra-debt balance and is being amortized over the term of the 2024 Notes. Total amortization expense for the three-month and nine-month fiscal periods ended September 29, 2017 was \$0.2 million and \$0.3 million.

The carrying amount of the equity component and the principal amount of the liability component, the unamortized discount and the net carrying value of the liability are as follows:

	2024 Notes	
	September 29, 2017	December 31, 2016
In thousands		
Principal amount of liability	\$ 200,000	\$ —
Unamortized discount	19,476	—
Carrying value of liability	\$ 180,524	\$ —
Equity component	\$ 20,459	\$ —

Because the embedded conversion option is indexed to the Company's own stock and would be classified in shareholders' equity, it does not meet the criterion under ASC 815 that would require separate accounting as a derivative instrument.

As of September 29, 2017, the "if converted value" did not exceed the principal amount of the 2024 Notes since the closing sales price of the Company's common stock was less than the conversion price of the 2024 Notes.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued
 For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016
 (Unaudited)

9. DEBT (CONTINUED)

Convertible Notes - continued

2017 Notes

	2017 Notes	
	September 29, 2017	December 31, 2016
In thousands		
Principal amount of liability	\$ 11,500	\$ 115,000
Unamortized discount	11	1,797
Carrying value of liability	\$ 11,489	\$ 113,203

In November 2010, the Company issued convertible senior unsecured notes due on November 15, 2017, in the aggregate principal amount of \$115.0 million in a private placement offering. These notes bear 3.25% interest per annum on the principal amount, payable semiannually in arrears on May 15 and November 15 of each year, beginning in 2011. In May 2017, the Company used a portion of the net proceeds from the issuance of the 2024 Notes, along with cash received from the counterparties in connection with the termination of the existing convertible note hedge transactions referred to below, to repurchase \$103.5 million principal amount of the 2017 Notes from a limited number of holders in an arm's length transaction. This repurchase represented approximately 90% of the aggregate principal amount of 2017 Notes. The repurchases were accounted for as an extinguishment of the outstanding instrument. Of the total aggregate cost of \$165.3 million, \$60.0 million was allocated to the equity component of the 2017 Notes and was recorded as a reduction to additional paid-in capital. The remainder of the cost was attributed to the outstanding principal repurchased and accrued interest. As of September 29, 2017, \$11.5 million principal amount remains outstanding under the 2017 Notes.

The repayment of a portion of the 2017 Notes was not contingent upon the issuance of the 2024 Notes. As such, the repurchase of the 2017 Notes was accounted for as a debt extinguishment.

See below for further details on the loss on extinguishment:

in thousands

Carrying value of 2017 Notes	\$ 113,943
Carrying value of Redeemed Debt	\$ 102,548
Fair value of consideration transferred allocated to debt component ⁽¹⁾	103,637
Loss on extinguishment of 2017 Notes ⁽²⁾	\$(1,089)
Acceleration of the related portion of debt issuance cost ⁽³⁾	(297)
Total loss on extinguishment of 2017 Notes ⁽⁴⁾	\$(1,386)

⁽¹⁾ The fair value of consideration transferred was calculated using a discount rate of 3%, representing the Company's borrowing rate at the date of issuance for a similar debt instrument with a remaining expected life of six months (for the 2017 Notes).

⁽²⁾ The majority of this balance relates to the write-off of approximately \$1.0 million, 90% of the unamortized debt discount.

⁽³⁾ The Company determined that in connection with the repurchase of the 2017 Notes, 90% of the unamortized debt issuance costs should be written off, representing the approximate outstanding portion of these costs related to the

notes repurchased.

(4) This loss is included in interest expense, net on the Company's Consolidated Statement of Operations.

In connection with the 2017 Notes, the Company had entered into convertible note hedge transactions and warrant transactions ("existing call spread transactions") with certain financial institutions. These transactions were accounted for as equity instruments at the time of issuance in 2010. With the intention of repurchasing the 2017 Notes, the Company entered into agreements with these financial institutions to terminate a portion of the existing call spread transactions concurrently with the offering. In connection with these transactions, the Company received \$58.6 million in payments related to the unwind of 90% of the convertible note hedge transactions and made deliveries of 624,044 shares of the Company's common stock in connection with the partial unwind of the warrant transactions. The Company used a portion of the proceeds from the bond hedge settlement to repurchase the 2017 Notes as described above and to make a payment to the revolving credit facility. The cash proceeds received were recorded as an increase of additional paid-in-capital which was partially offset by the delivery of shares.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016
(Unaudited)

9. DEBT (CONTINUED)

Convertible Notes - continued

2017 Notes - continued

The remaining portion of the 2017 Notes are convertible at the option of the noteholders until the close of business on the second Scheduled Trading Day (as defined in the 2017 Notes indenture) immediately preceding the maturity date. Accordingly, the remaining carrying amount of the 2017 Notes was recorded in current liabilities and a portion of the equity component, representing the unamortized debt discount, was reclassified from additional paid-in-capital to temporary equity on the Company's Condensed Consolidated Balance Sheet as of September 29, 2017.

10. PENSION PLANS

Components of net pension cost for the Qualified Pension Plan and Supplemental Employees' Retirement Plan ("SERP") are as follows:

	For the Three Months Ended			
	Qualified Pension Plan		SERP	
In thousands	September 29, 2017	September 30, 2016	September 29, 2017	September 30, 2016
Service cost	\$1,198	\$ 1,149	\$ —	\$ —
Interest cost on projected benefit obligation	6,089	6,122	70	64
Expected return on plan assets	(10,512)	(10,192)	—	—
Amortization of net loss	3,486	3,173	43	45
Additional amount recognized due to curtailment/settlement	—	—	206	—
Net pension cost	\$261	\$ 252	\$ 319	\$ 109
	For the Nine Months Ended			
	Qualified Pension Plan		SERP	
In thousands	September 29, 2017	September 30, 2016	September 29, 2017	September 30, 2016
Service cost	\$3,595	\$ 3,447	\$ —	\$ —
Interest cost on projected benefit obligation	18,268	18,366	193	192
Expected return on plan assets	(31,536)	(30,576)	—	—
Amortization of net loss	10,458	9,520	109	136
Additional amount recognized due to curtailment/settlement	—	—	305	—
Net pension cost	\$785	\$ 757	\$ 607	\$ 328

The Company contributed \$10.0 million to the qualified pension plan and \$2.9 million to the SERP through the end of the third quarter of 2017. No further contributions are expected to be made to the qualified pension plan during 2017. The Company plans to contribute an additional \$0.2 million to the SERP in 2017. For the 2016 plan year, the Company contributed \$10.0 million to the qualified pension plan and \$0.5 million to the SERP.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016
(Unaudited)

11. COMMITMENTS AND CONTINGENCIES

Pension Freeze

Effective December 31, 2015, the Company's qualified pension plan was frozen with respect to future benefit accruals. Under USG Cost Accounting Standard ("CAS") 413 the Company must determine the USG's share of any pension curtailment adjustment calculated in accordance with CAS. Such adjustments can result in an amount due to the USG for pension plans that are in a surplus position or an amount due to the contractor for plans that are in a deficit position. During the fourth quarter of 2016, the Company accrued a \$0.3 million liability representing our estimate of the amount due to the USG based on our pension curtailment adjustment calculation, which was submitted to the USG for review in December 2016. Through the date of this filing, there has been no response from the USG on this matter. There can be no assurance that the ultimate resolution of this matter will not have a material adverse effect on the Company's results of operations, financial position and cash flows.

New Hartford Property

In connection with the sale of the Company's Music segment in 2007, the Company assumed responsibility for meeting certain requirements of the Connecticut Transfer Act (the "Transfer Act") that applied to the transfer of the New Hartford, Connecticut, facility leased by that segment for guitar manufacturing purposes ("Ovation"). Under the Transfer Act, those responsibilities essentially consist of assessing the site's environmental conditions and remediating environmental impairments, if any, caused by Ovation's operations prior to the sale. The site is a multi-tenant industrial park, in which Ovation and other unrelated entities lease space. The environmental assessment process, which began in 2008, has been completed and site remediation is in process.

The Company's estimate of its portion of the cost to assess the environmental conditions and remediate this site is \$2.3 million, all of which has been accrued. The total amount paid to date in connection with these environmental remediation activities is \$1.6 million. At September 29, 2017, the Company had \$0.7 million accrued for these environmental remediation activities. A portion (\$0.1 million) of the accrual related to this property is included in other current liabilities and the balance is included in other long-term liabilities. The remaining balance of the accrual reflects the total anticipated cost of completing these environmental remediation activities. Although it is reasonably possible that additional costs will be paid in connection with the resolution of this matter, the Company is unable to estimate the amount of such additional costs, if any, at this time.

Bloomfield Property

In connection with the Company's 2008 purchase of the portion of the Bloomfield campus that Kaman Aerospace Corporation had leased from NAVAIR, the Company assumed responsibility for environmental remediation at the facility as may be required under the Transfer Act and is currently remediating the property under the guidance of the Connecticut Department of Environmental Protection ("CTDEP"). The assumed environmental liability of \$10.3 million was determined by taking the undiscounted estimated remediation liability of \$20.8 million and discounting it at a rate of 8%. This remediation process will take many years to complete. The total amount paid to date in connection with these environmental remediation activities is \$12.9 million. At September 29, 2017, the Company had \$2.5 million accrued for these environmental remediation activities. A portion (\$0.7 million) of the accrual related to this property is included in other current liabilities, and the balance is included in other long-term liabilities. Although it is reasonably possible that additional costs will be paid in connection with the resolution of this matter, the Company is unable to estimate the amount of such additional costs, if any, at this time.

Rimpar Property

In connection with the Company's purchase of GRW, the Company assumed responsibility for the environmental remediation at the Rimpar, Germany facility. As part of the purchase price allocation, the Company initially accrued approximately \$4.2 million during the year ended December 31, 2015. In 2016, the Company completed a Phase II assessment in order to better understand the extent of the environmental effort necessary to remediate the facility. Based on this assessment, the Company adjusted the accrual to \$0.5 million, as results of the assessment indicated a lower level of remediation effort will be required. The total amount paid to date in connection with these environmental remediation activities is \$0.2 million. The balance (\$0.3 million) of the accrual related to this property is included in other current liabilities. Although it is reasonably possible that additional costs will be paid in connection with the resolution of this matter, the Company is unable to estimate the amount of such additional costs, if any, at this time.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016
(Unaudited)

11. COMMITMENTS AND CONTINGENCIES (CONTINUED)

Aerospace Claim Matter

On June 29, 2016, the Company received notification from a customer of their intent to file a claim for recovery of costs and expenses related to rework on certain aerostructure components previously delivered by the Company to the customer. The notification did not indicate the extent of the rework undertaken by the customer, the cost or expenses incurred by the customer or the time frame in which the customer anticipated filing its formal claim. On October 17, 2017, the Company received a letter from the customer seeking to recover \$12.4 million associated with the rework of these components and related costs incurred by the customer. The Company estimates the cost to rework the aerostructure components delivered to the customer over the time period in question is approximately \$0.2 million. Based on this analysis, the Company has accrued \$0.2 million, the estimated cost to rework the aerostructure components, as of September 29, 2017; however, there can be no assurance that the ultimate resolution of this matter will not have a material adverse effect on the Company's results of operations, financial position and cash flows.

12. COMPUTATION OF EARNINGS PER SHARE

The computation of basic earnings per share is based on net earnings divided by the weighted average number of shares of common stock outstanding for each period. The computation of diluted earnings per share reflects the common stock equivalency of dilutive options granted to employees under the Company's stock incentive plan, shares issuable on redemption of its convertible notes and shares issuable upon redemption of outstanding warrants.

	For the Three Months Ended September 29, 2017		For the Nine Months Ended September 30, 2016	
In thousands, except per share amounts				
Net earnings	\$ 16,280	\$ 17,455	\$ 36,029	\$ 43,727
Basic:				
Weighted average number of shares outstanding	27,907	27,128	27,536	27,096
Basic earnings per share	\$0.58	\$ 0.64	\$1.31	\$ 1.61
Diluted:				
Weighted average number of shares outstanding	27,907	27,128	27,536	27,096
Weighted average shares issuable on exercise of dilutive stock options	148	140	152	138
Weighted average shares issuable on redemption of 2017 Notes	117	810	457	708
Weighted average shares issuable on redemption of warrants related to the 2017 Notes	47	2	174	1
Total	28,219	28,080	28,319	27,943
Diluted earnings per share	\$0.58	\$ 0.62	\$1.27	\$ 1.56

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016
(Unaudited)

12. COMPUTATION OF EARNINGS PER SHARE (CONTINUED)

Equity awards

For the three-month and nine-month fiscal periods ended September 29, 2017, respectively, 230,272 and 267,653 shares issuable under equity awards granted to employees were excluded from the calculation of diluted earnings per share as they were anti-dilutive based on the average stock price during the period. For the three-month and nine-month fiscal periods ended September 30, 2016, respectively, 483,556 and 561,297 shares issuable under equity awards granted to employees were excluded from the calculation of diluted earnings per share as they were anti-dilutive based on the average stock price during the period.

2017 Convertible Notes

For the three-month and nine-month fiscal periods ended September 29, 2017, and September 30, 2016, respectively, shares issuable under the 2017 Notes that were dilutive during the period were included in the calculation of earnings per share as the conversion price for the 2017 Notes was less than the average share price of the Company's stock.

2024 Convertible Notes

For the three-month and nine-month fiscal periods ended September 29, 2017, shares issuable under the 2024 Notes were excluded from the diluted earnings per share calculation because the conversion price was greater than the average market price of our stock during the periods.

Warrants

Excluded from the diluted earnings per share calculation for the three-month and nine-month fiscal periods ended September 29, 2017, were 298,264 and 1,204,410, respectively, shares issuable under the warrants sold in connection with the Company's 2017 Notes as they would be anti-dilutive. Excluded from the diluted earnings per share calculation for the three-month and nine-month fiscal periods ended September 30, 2016, were 3,435,712 and 3,433,632, respectively, shares issuable under the warrants sold in connection with the Company's 2017 Notes as they would be anti-dilutive.

13. SHARE-BASED ARRANGEMENTS

General

The Company accounts for stock options, restricted stock awards, restricted stock units and performance shares as equity awards and measures the cost of all share-based payments, including stock options, at fair value on the grant date and recognizes this cost in the statement of operations. The Company also has an employee stock purchase plan which is accounted for as a liability award.

Compensation expense for stock options, restricted stock awards and restricted stock units is recognized on a straight-line basis over the vesting period of the awards. Share-based compensation expense recorded for the three-month and nine-month fiscal periods ended September 29, 2017, was \$1.2 million and \$4.9 million, respectively. Share-based compensation expense recorded for the three-month and nine-month fiscal periods ended September 30, 2016, was \$1.1 million and \$4.7 million, respectively.

From time-to-time, the Company has issued stock awards with market and performance based conditions. The total of these shares is 8,979, assuming a 100% achievement level. The Company measures the cost of these awards based on their grant date fair value to the extent of the probable number of shares to be earned upon vesting. Amortization of this cost is recorded on a straight-line basis over the requisite service period. Throughout the course of the requisite service period, the Company monitors the level of achievement compared to the target and adjusts the number of shares expected to be earned, and the related compensation expense recorded thereafter, to reflect the updated most probable outcome. Compensation expense for these awards for the three-month and nine-month fiscal periods ended September 29, 2017, and September 30, 2016, was not material.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued
 For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016
 (Unaudited)

13. SHARE-BASED ARRANGEMENTS (CONTINUED)

Stock option activity was as follows:

	For the Three Months Ended September 29, 2017		For the Nine Months Ended September 29, 2017	
	Options	Weighted - average exercise price	Options	Weighted - average exercise price
Options outstanding at beginning of period	992,779	\$ 39.89	958,679	\$ 36.18
Granted	—	\$ —	226,315	\$ 51.97
Exercised	(3,983)	\$ 39.68	(150,727)	\$ 33.36
Forfeited or expired	(9,981)	\$ 42.48	(55,452)	\$ 43.34
Options outstanding at September 29, 2017	978,815	\$ 39.86	978,815	\$ 39.86

The fair value of each option award is estimated on the date of grant using the Black-Scholes option valuation model. The following table indicates the weighted-average assumptions used in estimating fair value:

	For the Nine Months Ended September 29, 2017			
	2017		2016	
Expected option term (years)	5.0		5.2	
Expected volatility	19.9 %	26.0 %		
Risk-free interest rate	1.9 %	1.2 %		
Expected dividend yield	1.6 %	1.8 %		
Per share fair value of options granted	\$8.61	\$8.63		

Restricted Stock Award and Restricted Stock Unit activity was as follows:

	For the Three Months Ended September 29, 2017		For the Nine Months Ended September 29, 2017	
	Restricted Stock	Weighted- average grant date fair value	Restricted Stock	Weighted- average grant date fair value
Restricted Stock outstanding at beginning of period	160,481	\$ 44.13	167,674	\$ 40.27
Granted	1,000	\$ 50.85	76,008	\$ 50.01
Vested	(2,269)	\$ 43.85	(73,611)	\$ 41.56
Forfeited or expired	(2,550)	\$ 41.97	(13,409)	\$ 42.32
Restricted Stock outstanding at September 29, 2017	156,662	\$ 44.21	156,662	\$ 44.21

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016

(Unaudited)

14. SEGMENT AND GEOGRAPHIC INFORMATION

The Company is organized based upon the nature of its products and services, and is composed of two operating segments each overseen by a segment manager. These segments are reflective of how the Company's Chief Executive Officer, who is its Chief Operating Decision Maker ("CODM"), reviews operating results for the purposes of allocating resources and assessing performance. The Company has not aggregated operating segments for purposes of identifying reportable segments.

The Distribution segment is a leading power transmission, automation and fluid power industrial distributor with operations throughout the United States. The segment provides electro-mechanical products, bearings, power transmission, motion control and electrical and fluid power components to a broad spectrum of industrial markets serving both maintenance, repair and overhaul ("MRO") and original equipment manufacturer ("OEM") customers.

The Aerospace segment produces and markets proprietary aircraft bearings and components; super precision, miniature ball bearings; complex metallic and composite aerostructures for commercial, military and general aviation fixed and rotary wing aircraft; and safe and arming solutions for missile and bomb systems for the U.S. and allied militaries. The segment also markets the design and supply of aftermarket parts to businesses performing MRO in aerospace markets; performs helicopter subcontract work; restores, modifies and supports the Company's SH-2G Super Seasprite maritime helicopters; manufactures and supports the Company's K-MAX® manned and unmanned medium-to-heavy lift helicopters; and provides engineering design, analysis and certification services.

Summarized financial information by business segment is as follows:

In thousands	For the Three Months Ended		For the Nine Months Ended	
	September 29, 2017	September 30, 2016	September 29, 2017	September 30, 2016
Net sales:				
Distribution	\$267,641	\$ 274,388	\$817,965	\$ 849,104
Aerospace	179,405	179,086	514,028	526,210
Net sales	\$447,046	\$ 453,474	\$1,331,993	\$ 1,375,314
Operating income:				
Distribution	\$13,369	\$ 11,872	\$40,997	\$ 36,148
Aerospace	31,877	29,616	74,736	81,374
Net gain (loss) on sale of assets	212	(24	) 217	(10
Corporate expense	(15,160	) (10,402	) (44,052	) (38,253
Operating income	30,298	31,062	71,898	79,259
Interest expense, net	5,264	4,165	15,546	11,960
Other expense (income), net	(483	) (332	) (711	) 243
Earnings before income taxes	25,517	27,229	57,063	67,056
Income tax expense	9,237	9,774	21,034	23,329
Net earnings	\$16,280	\$ 17,455	\$36,029	\$ 43,727

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016

(Unaudited)

15. SHAREHOLDERS' EQUITY AND ACCUMULATED OTHER COMPREHENSIVE INCOME

Changes in shareholders' equity for the nine-month fiscal periods ended September 29, 2017, and September 30, 2016, were as follows:

	For the Nine Months	
	Ended	
	September 29, 2017	September 30, 2016
In thousands		
Beginning balance	\$565,787	\$ 543,077
Comprehensive income	66,843	50,453
Dividends declared	(16,581)	(14,640)
Employee stock plans and related tax benefit	5,426	7,094
Purchase of treasury shares	(6,931)	(8,989)
Share-based compensation expense	4,917	4,711
Amounts reclassified to temporary equity	1,786	(2,344)
Changes due to convertible notes transactions	(2,522)	—
Ending balance	\$618,725	\$ 579,362

The components of accumulated other comprehensive income (loss) are shown below:

	For the Three Months	
	Ended	
	September 29, 2017	September 30, 2016
In thousands		
Foreign currency translation:		
Beginning balance	\$(18,522)	\$(22,590)
Net gain/(loss) on foreign currency translation	7,731	1,050
Reclassification to net income	—	—
Other comprehensive income/(loss), net of tax	7,731	1,050
Ending balance	\$(10,791)	\$(21,540)
Pension and other post-retirement benefits ⁽¹⁾ :		
Beginning balance	\$(117,080)	\$(113,445)
Reclassifications to net income:		
Amortization of net loss, net of tax expense of \$1,309 and \$1,213, respectively	2,220	2,005
Other comprehensive income/(loss), net of tax	2,220	2,005
Ending balance	\$(114,860)	\$(111,440)
Derivative instruments ⁽²⁾ :		
Beginning balance	\$142	\$(770)
Net loss on derivative instruments, net of tax (benefit) expense of (\$4) and \$118, respectively	(6 )	) 195
Reclassification to net income, net of tax (benefit) expense of (\$39) and \$87, respectively	(64 )	) 143
Other comprehensive income/(loss), net of tax	(70 )	) 338
Ending balance	\$72	\$(432)

Total accumulated other comprehensive income (loss)	\$(125,579) \$ (133,412)
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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016

(Unaudited)

15. SHAREHOLDERS' EQUITY AND ACCUMULATED OTHER COMPREHENSIVE INCOME (CONTINUED)

	For the Nine Months Ended	
	September 29, 2017	September 30, 2016
In thousands		
Foreign currency translation:		
Beginning balance	\$(34,896)	\$(22,625)
Net gain/(loss) on foreign currency translation	24,105	1,085
Reclassification to net income	—	—
Other comprehensive income/(loss), net of tax	24,105	1,085
Ending balance	\$(10,791)	\$(21,540)
Pension and other post-retirement benefits ⁽¹⁾ :		
Beginning balance	\$(121,448)	\$(117,455)
Reclassifications to net income:		
Amortization of net loss, net of tax expense of \$3,979 and \$3,641, respectively	6,588	6,015
Other comprehensive income/(loss), net of tax	6,588	6,015
Ending balance	\$(114,860)	\$(111,440)
Derivative instruments ⁽²⁾ :		
Beginning balance	\$(49)	\$(58)
Net loss on derivative instruments, net of tax expense of \$74 and \$512, respectively	124	(845)
Reclassification to net income, net of tax (benefit) expense of (\$2) and \$285, respectively	(3)	471
Other comprehensive income/(loss), net of tax	121	(374)
Ending balance	\$72	\$(432)
Total accumulated other comprehensive income (loss)	\$(125,579)	\$(133,412)

(1) These accumulated other comprehensive income components are included in the computation of net periodic pension cost.

(See Note 10, Pension Plans for additional information.)

(2) See Note 6, Derivative Financial Instruments, for additional information regarding our derivative instruments.

16. INCOME TAXES

	For the Three Months Ended			For the Nine Months Ended		
	September 29, 2017	September 30, 2016	%	September 29, 2017	September 30, 2016	
Effective Income Tax Rate	36.2%	35.9	%	36.9%	34.8	%

The effective income tax rate represents the combined federal, state and foreign tax effects attributable to pretax earnings for the period. The increase in the effective tax rate for the three-month and nine-month fiscal periods ended September 29, 2017, compared to the statutory rate of 35%, was primarily due to a projected foreign loss in the

current periods for which no tax benefit has been provided. The effective tax rate for the three-month fiscal period ended September 30, 2016 exceeds the statutory rate of 35%, primarily due to certain discrete items, most notably unfavorable differences between foreign provisions for taxes and actual foreign returns filed.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

For the three-month and nine-month fiscal periods ended September 29, 2017 and September 30, 2016

(Unaudited)

16. INCOME TAXES (CONTINUED)

A valuation allowance for deferred tax assets, including those associated with net operating loss carryforwards, is recognized when it is more likely than not that some or all of the benefit from the deferred tax asset will not be realized. To assess that likelihood, the Company uses estimates and judgment regarding future taxable income, and considers the tax consequences in the jurisdiction where such taxable income is generated, to determine whether a valuation allowance is required. Such evidence can include current financial position, results of operations, both actual and forecasted, the reversal of deferred tax liabilities, and tax planning strategies, as well as the current and forecasted business economics.

The Company has assessed both positive and negative evidence to estimate whether sufficient future taxable income will be generated to utilize operating loss carryforwards associated with certain foreign operations that will permit the Company to use \$3.1 million of deferred tax assets associated with these foreign operations as of September 29, 2017. Through the end of the third quarter of 2017, the Company believes it is more likely than not that only \$1.2 million of these deferred tax assets will be realized and, as such, has recorded a valuation allowance of \$1.9 million. Going forward, management will continue to assess the available positive and negative evidence to determine whether it is likely sufficient future taxable income will be generated to permit the use of these deferred tax assets. The amount of the deferred tax asset considered realizable could be adjusted if estimates of future taxable income are reduced or increased, or if additional weight is given to subjective evidence such as future expected growth because objective negative evidence in the form of cumulative losses is no longer present.

17. SUBSEQUENT EVENTS

The Company has evaluated subsequent events through the issuance date of these financial statements. No material subsequent events were identified that require disclosure.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") is intended to provide readers of our condensed consolidated financial statements with the perspectives of management. It presents, in narrative and tabular form, information regarding our financial condition, results of operations, liquidity and certain other factors that may affect our future results, and is designed to enable the readers of this report to obtain an understanding of our businesses, strategies, current trends and future prospects. It should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2016 ("2016 Form 10-K") and the condensed consolidated financial statements included in Item 1 of this Form 10-Q.

OVERVIEW OF BUSINESS

Kaman Corporation (the "Company") is comprised of two business segments:

The Distribution segment is a leading power transmission, automation and fluid power industrial distributor with operations throughout the United States. The segment provides electro-mechanical products, bearings, power transmission, motion control and electrical and fluid power components to a broad spectrum of industrial markets serving both maintenance, repair and overhaul ("MRO") and original equipment manufacturer ("OEM") customers. The Aerospace segment produces and markets proprietary aircraft bearings and components; super precision, miniature ball bearings; complex metallic and composite aerostructures for commercial, military and general aviation fixed and rotary wing aircraft; and safe and arming solutions for missile and bomb systems for the U.S. and allied militaries. The segment also markets the design and supply of aftermarket parts to businesses performing MRO in aerospace markets; performs helicopter subcontract work; restores, modifies and supports our SH-2G Super Seasprite maritime helicopters; manufactures and supports our K-MAX® manned and unmanned medium-to-heavy lift helicopters; and provides engineering design, analysis and certification services.

Financial performance

Net sales decreased 1.4% and 3.1% for the three-month and nine-month fiscal periods ended September 29, 2017, compared to the comparable fiscal periods in the prior year.

Net earnings decreased 6.7% and 17.6% for the three-month and nine-month fiscal periods ended September 29, 2017, compared to the comparable fiscal periods in the prior year.

Diluted earnings per share decreased to \$0.58 for the three-month fiscal period ended September 29, 2017, compared to \$0.62 in the comparable fiscal period in the prior year. For the nine-month fiscal period ended September 29, 2017, diluted earnings per share decreased to \$1.27, compared to \$1.56 in the comparable fiscal period in the prior year.

- Cash provided by operating activities during the nine-month fiscal period ended September 29, 2017, was \$43.8 million, \$26.2 million less than the comparable fiscal period in the prior year.

Recent events

- On October 3, 2017, our Aerospace segment announced that it had signed a contract with Columbia Basin Helicopters for the purchase of a K-MAX® helicopter to be delivered in 2018.

On October 1, 2017, Mr. Richard R. Barnhart became the President of Kaman Aerospace Group, succeeding Mr. Gregory L. Steiner, who is expected to retire as of January 2, 2018.

In September 2017, Rotex Helicopter accepted the third K-MAX® helicopter from the newly reopened commercial production line. This delivery followed Lectern Aviation of China's acceptance of the first two K-MAX® helicopters in July 2017.

On September 7, 2017, the Company announced a restructuring plan resulting from its ongoing effort to improve capacity utilization and operating efficiency to better position our Aerospace segment for increased profitability and growth. These actions are expected to result in approximately \$8.0 million to \$10.0 million in pre-tax restructuring charges, beginning in the third quarter of 2017 through the planned completion of restructuring activities in the fourth

quarter of 2018. The Company anticipates these actions will result in total cost savings of approximately \$4.0 million annually beginning in 2019.

On July 17, 2017, our Aerospace segment announced it had entered into a new multi-year contract with Sikorsky to manufacture H-60 cockpits under the Department of Defense MY IX H-60 procurement authorization. The term of the agreement will be for five years, beginning in 2018 and ending in 2022.

RESULTS OF OPERATIONS

Consolidated Results

Net Sales

	For the Three Months Ended		For the Nine Months Ended		
	September 29, 2017	September 30, 2016	September 29, 2017	September 30, 2016	
	(in thousands)				
Net sales	\$ 447,046	\$ 453,474	\$ 1,331,993	\$ 1,375,314	
\$ change	(6,428)	19,732	(43,321)	52,466	
% change	(1.4)%	4.5	(3.1)%	4.0	%

Net sales decreased for the three-month and nine-month fiscal periods ended September 29, 2017, as compared to the corresponding periods in 2016, mainly due to a decrease in net sales at our Distribution segment. Net sales for the quarter remained relatively flat at our Aerospace segment when compared to the corresponding period in 2016. Foreign currency exchange rates relative to the U.S. dollar had a favorable impact of \$1.2 million for the three-month fiscal period ended September 29, 2017. For the nine-month fiscal period, there were lower net sales at our Aerospace segment and an unfavorable impact of foreign currency exchange rates relative to the U.S. dollar of \$2.7 million. (See segment discussion below for additional information.)

Gross Profit

	For the Three Months Ended		For the Nine Months Ended		
	September 29, 2017	September 30, 2016	September 29, 2017	September 30, 2016	
	(in thousands)				
Gross profit	\$ 138,935	\$ 135,490	\$ 398,714	\$ 413,686	
\$ change	3,445	5,564	(14,972)	23,897	
% change	2.5	% 4.3	(3.6)%	6.1	%
% of net sales	31.1	% 29.9	% 29.9	% 30.1	%

Gross profit increased for the three-month fiscal period ended September 29, 2017, as compared to the corresponding period in 2016. This was a result of higher gross profit at our Aerospace segment, primarily related to our JPF program customer mix. For the three-month fiscal period ended September 29, 2017, JPF deliveries consisted of mostly higher margin direct commercial sales to foreign militaries compared to deliveries of mainly USG fuzes in the corresponding period in 2016. Additionally, there were higher sales and associated gross profit under our AH-1Z program. Partially offsetting these increases in gross profit was lower gross profit at our Distribution segment, primarily attributable to lower sales under our bearings and power transmission and automation, control and energy product lines.

Gross profit decreased for the nine-month fiscal period ended September 29, 2017, as compared to the corresponding period in 2016. This was a result of lower gross profit at both our Distribution and Aerospace segments. The decrease in gross profit at our Distribution segment was primarily attributable to lower sales under our bearings and power transmission and automation, control and energy product lines. The decrease in gross profit at our Aerospace segment was primarily associated with our JPF program customer mix. For the nine-month fiscal period ended September 29, 2017, there were lower direct commercial sales to foreign militaries compared to the corresponding period in 2016. Additionally, JPF deliveries in the current nine-month period consisted mostly of USG fuzes under Option 12, which were negotiated at a lower selling price than Option 11 sold in the corresponding period in 2016.

Gross profit as a percentage of net sales increased for the three-month fiscal period ended September 29, 2017, as compared to the corresponding period in 2016, primarily due to the customer mix under our JPF program described above. Additionally, gross profit as a percentage of net sales increased during the three-month fiscal period due to improvements in various metallic and composite structures programs. Gross profit as a percentage of net sales remained relatively flat for the nine-month fiscal period ended September 29, 2017, as compared to the corresponding period in 2016.

Selling, General & Administrative Expenses (S,G&A)

	For the Three Months Ended		For the Nine Months Ended		
	September 29, 2017	September 30, 2016	September 29, 2017	September 30, 2016	
	(in thousands)				
S,G&A	\$ 106,349	\$ 104,060	\$ 324,533	\$ 333,726	
\$ change	2,289	3,907	(9,193)	26,914	
% change	2.2	% 3.9	% (2.8)	% 8.8	%
% of net sales	23.8	% 22.9	% 24.4	% 24.3	%

The increase in S,G&A for the three-month fiscal period ended September 29, 2017, compared to the corresponding period in 2016, resulted from higher corporate expenses and an increase in expenses at our Aerospace segment. The increase in corporate expenses was primarily driven by \$2.1 million in costs associated with the retirement of a senior executive and higher employee and employee-related costs, partially offset by lower consulting costs. The increase in expenses at our Aerospace segment primarily related to higher salary and wage expenses. The higher corporate expenses and increase in expenses at our Aerospace segment were partially offset by lower expenses at our Distribution segment, primarily related to lower expenses of \$2.3 million associated with our productivity and efficiency initiatives.

The decrease in S,G&A for the nine-month fiscal period ended September 29, 2017, compared to the corresponding period in 2016, resulted from lower expenses at both our Distribution and Aerospace segments, partially offset by an increase in corporate expenses. The decrease in expenses at our Distribution segment primarily related to the absence of \$6.5 million in costs associated with our 2016 productivity and efficiency initiatives and lower salary and benefit expenses. The decrease in expenses at our Aerospace segment was primarily attributable to lower costs associated with the sale of government contract program inventory (see segment discussion below for additional information), partially offset by higher salary and wage expenses. These decreases were partially offset by an increase in corporate expenses. This was a result of higher employee and employee-related costs and \$2.1 million in costs associated with the retirement of a senior executive, partially offset by lower consulting costs.

Restructuring Costs

	For the Three Months Ended		For the Nine Months Ended	
	September 29, 2017	September 30, 2016	September 29, 2017	September 30, 2016
	(in thousands)			
Restructuring costs	\$ 2,500	\$ 344	\$ 2,500	\$ 691

During the third quarter of 2017, we recorded \$2.5 million in costs for restructuring activities at our Aerospace segment to support the ongoing effort of improving capacity utilization and operating efficiency to better position the Company for increased profitability and growth. Such actions include workforce reductions and the consolidation of operations, which we expect to continue through the planned completion in the fourth quarter of 2018. Additionally, included in this expense is approximately \$1.0 million of cost that primarily relates to the write-off of inventory for various small order programs that we will no longer continue to manufacture as a result of the consolidation of operations.

Operating Income

	For the Three Months Ended	For the Nine Months Ended
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	September 29, 2017	September 30, 2016	September 29, 2017	September 30, 2016
	(in thousands)			
Operating income	\$30,298	\$ 31,062	\$71,898	\$ 79,259
\$ change	(764)	1,279	(7,361)	(3,285)
% change	(2.5)%	4.3 %	(9.3)%	(4.0)%
% of net sales	6.8 %	6.8 %	5.4 %	5.8 %

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Operating income remained relatively flat for the three-month fiscal period ended September 29, 2017, versus the comparable period in 2016, primarily due to higher operating income at both our Aerospace and Distribution segments, offset by higher corporate expenses, as discussed above. The decrease in operating income for the nine-month fiscal period ended September 29, 2017, compared to the corresponding period in 2016, was attributable to lower operating income at our Aerospace segment and higher corporate expenses, partially offset by higher operating income at our Distribution segment. (See segment discussion below for additional information.)

Interest Expense, Net

	For the Three Months Ended September 29, 2017		For the Nine Months Ended September 30, 2017	
	2016		2016	2016
Interest expense, net	\$5,264	\$ 4,165	\$15,546	\$ 11,960

(in thousands)

Interest expense, net, generally consists of interest charged on our Credit Agreement, which includes a revolving credit facility and a term loan facility, and our convertible notes and the amortization of debt issuance costs, offset by interest income. The increase in interest expense, net for both periods ended September 29, 2017, compared to the corresponding periods in 2016, was primarily attributable to higher interest expense under our convertible notes and a higher interest rate for outstanding amounts under the Credit Agreement. At September 29, 2017, the interest rate for outstanding amounts under the Credit Agreement was 2.56% compared to 2.13% at September 30, 2016. Additionally, for the nine-month fiscal period, the increase in interest expense was attributable to the write-off of unamortized debt issuance costs and the unamortized debt discount associated with the redemption of our 2017 notes, for \$0.3 million and \$1.0 million, respectively. These increases were partially offset by lower average borrowings, as compared to the corresponding periods ended September 30, 2016. (See Liquidity and Capital Resources section below for information on our borrowings.)

Effective Income Tax Rate

	For the Three Months Ended September 29, 2017		For the Nine Months Ended September 30, 2017	
	2016		2016	2016
Effective income tax rate	36.2%	35.9 %	36.9%	34.8 %

The effective income tax rate represents the combined federal, state and foreign tax effects attributable to pretax earnings for the period. The increase in the effective tax rate for the three-month and nine-month fiscal periods ended September 29, 2017, compared to the statutory rate of 35%, is primarily due to a projected foreign loss in the current periods for which no tax benefit has been provided. The effective rate for the three-month fiscal period ended September 30, 2016 exceeds the statutory rate of 35%, primarily due to certain discrete items, most notably unfavorable differences between foreign provisions for taxes and actual foreign returns filed.

Distribution Segment

Results of Operations

	For the Three Months Ended		For the Nine Months Ended	
	September 29, 2017	September 30, 2016	September 29, 2017	September 30, 2016
	(in thousands)			
Net sales	\$267,641	\$274,388	\$817,965	\$849,104
\$ change	(6,747)	(21,924)	(31,139)	(62,728)
% change	(2.5)%	(7.4)%	(3.7)%	(6.9)%
Operating income	\$13,369	\$11,872	\$40,997	\$36,148
\$ change	1,497	(2,550)	4,849	(6,641)
% change	12.6 %	(17.7)%	13.4 %	(15.5)%
% of net sales	5.0 %	4.3 %	5.0 %	4.3 %

Net sales

Net sales for the three-month and nine-month fiscal periods ended September 29, 2017 decreased when compared to the corresponding period in 2016, primarily due to decreases in sales of \$6.1 and \$27.8 million, respectively, associated with our bearings and power transmission and automation, control and energy product lines and less significant decreases in our fluid power product line. The decreases in sales in our product lines for the three-month and nine-month fiscal periods ended September 29, 2017, were mostly attributable to lower sales volume to our MRO customers of \$13.1 million and \$34.9 million, respectively, partially offset by higher sales volume to our OEM customers.

Additionally, contributing to the decrease in sales for the three-month fiscal period when compared to the corresponding period in the prior year was one fewer sales day in the current quarter. Looking at the markets we serve, sales were lower in the paper manufacturing, nonmetallic mineral product manufacturing and chemical manufacturing markets. Partially offsetting these decreases, were higher sales in the machinery manufacturing and mining markets.

Further contributing to the decrease in sales for the nine-month fiscal period was two fewer sales days in the first nine months of 2017 when compared to the corresponding period in 2016. Looking at the markets we serve, sales were lower in the food manufacturing, paper manufacturing and merchant wholesalers durable goods markets. Partially offsetting these decreases, were higher sales in the fabricated metal product and mining markets.

"Organic Sales per Sales Day" is a metric management uses to evaluate performance trends at our Distribution segment and is calculated by taking Organic Sales divided by the number of Sales Days in the period. The following table illustrates the calculation of Organic Sales per Sales Day.

	For the Three Months Ended		For the Nine Months Ended	
	September 29, 2017	September 30, 2016	September 29, 2017	September 30, 2016
(in thousands)				
Current period				
Net sales	\$267,641	\$274,388	\$817,965	\$849,104
Acquisition sales ⁽¹⁾	—	1,128	—	4,681
Organic sales	267,641	273,260	817,965	844,423
Sales days	62	63	190	192
Organic Sales per Sales Day for the current period a	\$4,317	\$4,337	\$4,305	\$4,398
Prior period				
Net sales from the prior year	\$274,388	\$296,312	\$849,104	\$911,832
Sales days from the prior year	63	64	192	193
Sales per sales day from the prior year b	\$4,355	\$4,630	\$4,422	\$4,725
% change	(a-b)÷b(0.9	)%(6.3	)%(2.6	)%(6.9

⁽¹⁾ Sales contributed by an acquisition are included in Organic Sales beginning with the thirteenth month following the date of acquisition. Prior period information is adjusted to reflect acquisition sales for that period as Organic Sales when calculating the change in Organic Sales per Sales Day for the current period.

Operating income

The increase in operating income for the three-month and nine-month fiscal periods ended September 29, 2017, when compared to the corresponding periods in the prior year, was primarily attributable to the benefits received from the productivity initiatives implemented in 2016 and lower expenses of \$2.3 million and \$6.5 million, respectively, for the cost incurred related to the implementation of these productivity and efficiency initiatives. The initiatives included operational process improvements and data analytics, primarily focused on expanding operating margins. Additionally, we experienced lower incentive compensation costs in both periods. For the nine-month fiscal period, we also experienced lower salary and benefit costs. These savings were partially offset by a decrease in sales and related gross profit.

Other Matters

Enterprise Resource Planning System

In July 2012, we announced a decision to invest in a new ERP business system for our Distribution segment with an estimated total cost of \$45.0 million. Since our announcement in 2012, Distribution has acquired nine businesses. To date, we have implemented the new ERP system at four acquired entities, of which two were not included in the original project scope. Additionally, an upgraded version of the software was released during the early stages of our initial implementation plan and Distribution elected to install this major upgrade because of the increased functionality, enhanced features and new user interface it offered. Recently, our software vendor responsible for the ERP system notified us that another upgrade is available, which is designed to improve overall performance and further enhance the capabilities of the system. Management has assessed this upgrade against the current version of the ERP system and the requirements of the business. This upgrade is expected to leverage the existing work completed to date and we are currently working closely with the software vendor to revise the project plan and

implementation timeline. As a result of the unplanned implementations at the acquired businesses and the software upgrades, our implementation timeline has been extended and the total project cost is currently estimated between \$51.0 million and \$54.0 million.

For the three-month fiscal periods ended September 29, 2017, and September 30, 2016, ERP system expenses incurred totaled \$0.4 million and \$0.3 million, respectively, and ERP system capital expenditures totaled \$0.8 million and \$1.0 million, respectively. For the nine-month fiscal periods ended September 29, 2017, and September 30, 2016, ERP system expenses incurred totaled \$1.1 million and \$0.8 million, respectively, and ERP system capital expenditures totaled \$2.7 million and \$2.9 million, respectively. Total to date ERP system capital expenditures as of September 29, 2017, were \$37.2 million. Depreciation expense for the ERP system for the three-month fiscal periods ended September 29, 2017, and September 30, 2016, totaled \$0.6 million and \$0.7 million, respectively. Depreciation expense for the ERP system for the nine-month fiscal periods ended September 29, 2017, and September 30, 2016, totaled \$1.9 million and \$2.1 million, respectively.

Aerospace Segment

Results of Operations

	For the Three Months Ended		For the Nine Months Ended		
	September 29, 2017	September 30, 2016	September 29, 2017	September 30, 2016	
	(in thousands)				
Net sales	\$ 179,405	\$ 179,086	\$ 514,028	\$ 526,210	
\$ change	319	41,656	(12,182)	115,194	
% change	0.2	% 30.3	% (2.3)	% 28.0	%
Operating income	\$ 31,877	\$ 29,616	\$ 74,736	\$ 81,374	
\$ change	2,261	1,815	(6,638)	2,599	
% change	7.6	% 6.5	% (8.2)	% 3.3	%
% of net sales	17.8	% 16.5	% 14.5	% 15.5	%

Net sales

Sales remained relatively flat for the three-month fiscal period ended September 29, 2017, as compared to the corresponding period in 2016. This was a result of an increase in sales of \$8.5 million generated by our commercial product programs, mostly offset by a decrease in sales generated by our military product programs of \$8.2 million. The increase in sales under our commercial product programs was primarily attributable to higher sales on our K-MAX® program and higher sales volume under our commercial bearings products. The decrease in military sales for the three-month fiscal period ended September 29, 2017, was primarily attributable to lower sales under our JPF program with the USG, lower sales on the Boeing A-10 program and a decrease in sales on our Sikorsky BLACK HAWK helicopter program. These decreases, totaling \$37.8 million, were partially offset by higher direct sales of our JPF to foreign militaries.

Foreign currency exchange rates relative to the U.S. dollar had a favorable impact of \$1.2 million on net sales for the three-month fiscal period ended September 29, 2017.

Sales decreased for the nine-month fiscal period ended September 29, 2017, as compared to the corresponding period in 2016, primarily due to a decrease in sales generated by our military product programs of \$27.5 million. The decrease was primarily attributable to lower direct sales of our JPF to foreign militaries, lower sales volume for our fabricated products from foreign operations, a decrease in sales under certain composite structures programs and lower sales under our Boeing A-10 program and SH-2G(I) contract with New Zealand. These decreases, totaling \$37.4 million, were partially offset by higher sales under our SH-2G program with Peru and the AH-1Z program.

Partially offsetting the decrease in military sales for the nine-month fiscal period ended September 29, 2017, was a \$15.3 million increase in sales generated by our commercial product programs. The increase was primarily attributable to higher sales under the K-MAX® program, higher sales volume under our commercial bearings products and an increase in sales under our composite structure products from foreign operations. These increases, totaling \$22.7 million, were partially offset by lower sales under our Bell Helicopter composite blade program and the Boeing 767/777 program.

Foreign currency exchange rates relative to the U.S. dollar had an unfavorable impact of \$2.7 million on net sales for the nine-month fiscal period ended September 29, 2017.

Operating income

Operating income increased for the three-month fiscal period ended September 29, 2017, compared to the corresponding period in 2016. The increase was primarily attributable to higher sales and associated gross profit under our JPF program with foreign militaries and our AH-1Z program. These increases, totaling \$15.6 million, were partially offset by lower sales volume and associated gross profit under our JPF program with the USG. Additionally, USG fuzes under Option 12 sold in the current period were negotiated at a lower selling price than Option 11 sold in the corresponding period in 2016. Further offsetting some of the increase in operating income for three-month fiscal period was \$2.5 million in costs related to restructuring activities.

Operating income decreased for the nine-month fiscal period ended September 29, 2017, compared to the corresponding periods in 2016. The decrease was primarily attributable to a decrease in sales and lower gross profit under our JPF program. In addition, operating income decreased, to a lesser extent, due to \$2.5 million in costs related to restructuring activities. These decreases were partially offset by increases of \$11.5 million, primarily attributable to higher sales and associated gross profit under our commercial bearings products, the SH-2G program with Peru and our AH-1Z program.

Further offsetting some of the decrease in operating income for the nine-month fiscal period were lower S,G&A expenses associated with the sale of government contract program inventory. For certain USG contracts, S,G&A expenses are capitalized in inventory until revenue is recognized, to the extent that gross profit is available to offset the S,G&A expenses. See the table below for the expense or benefit received from S,G&A expenses capitalized in inventory for certain government contracts.

	For the Three Months Ended		For the Nine Months Ended	
	September 29, 2017	September 30, 2016	September 29, 2017	September 30, 2016
S,G&A expensed (capitalized in inventory), net	\$ (252)	\$ (47)	\$ 52	\$ 3,056

(in thousands)

Long-Term Contracts

For long-term aerospace contracts, we generally recognize sales and cost of sales based on the percentage-of-completion method of accounting, which allows for recognition of revenue as work on a contract progresses. We recognize sales and profit based on either (1) the cost-to-cost method, in which case sales and profit are recorded based upon the ratio of costs incurred to estimated total costs to complete the contract, or (2) the units-of-delivery method, in which case sales are recognized as deliveries are made and cost of sales is computed on the basis of the estimated ratio of total cost to total sales.

Revenue and cost estimates for all significant long-term contracts for which revenue is recognized using the percentage-of-completion method of accounting are reviewed and reassessed quarterly. Based upon these reviews, we record the effects of adjustments in profit estimates each period. If at any time we determine that for a particular contract total costs will exceed total contract revenue, we will record a provision for the entire anticipated contract loss at that time. For the three-month and nine-month fiscal periods ended September 29, 2017, there were net increases in the Company's operating income attributable to changes in contract estimates of \$1.1 million and \$3.2 million, respectively. These increases were primarily a result of improved performance on the AH-1Z program, JPF program and the SH-2G program with Peru. These improvements were partially offset by cost growth on the K-MAX® and A-10 programs. There were net decreases in the Company's operating income from changes in contract estimates of \$1.3 million and \$3.9 million, respectively, for the three-month and nine-month fiscal periods ended September 30, 2016. These decreases were primarily a result of cost growth on various programs, including the

Boeing 767/777 program, the A-10 program and a composites assembly program. For the nine-month fiscal period, these decreases were partially offset by improved performance on the JPF program.

Backlog

September 2017 December 31, 2016

(in thousands)

Backlog \$556,937 \$ 581,619

Backlog decreased during the first nine months of 2017 primarily due to deliveries under our JPF program to the USG and foreign militaries and work performed on the SH-2G program with Peru. This decrease was partially offset by orders under the Sikorsky BLACK HAWK helicopter program.

Major Programs/Product Lines

Below is a discussion of significant changes in the Aerospace segment's major programs during the first nine months of 2017. See our 2016 Form 10-K for a complete discussion of our Aerospace segment's programs.

A-10

The segment has contracted with Boeing to produce the wing control surfaces (inboard and outboard flaps, slats and deceleron assemblies) for the USAF's A-10 fleet. This contract has a potential value of over \$110.0 million; however, annual quantities will vary, as they are dependent upon the orders Boeing receives from the USAF. Initial deliveries under this program began in the third quarter of 2010 and full rate production began during the fourth quarter of 2012. Through September 29, 2017, 170 shipsets have been delivered over the life of the program, and approximately 3 shipsets remain in backlog. In 2016, the USAF indicated that they would delay the retirement of the A-10 fleet due to its vital close air support, search and rescue capabilities and the lack of a suitable replacement. We continue to monitor the defense budget and understand that despite this positive indication, the future of this program could be at risk without the continued support of Congress. We have not received any orders for additional shipsets in 2017, and as such, we expect a break in production as we complete the units we currently have on order and wait for follow-on orders from our customer. We have not received any indication from our customer that this program will be terminated. Final production and deliveries of existing orders under this contract are anticipated to be completed during the fourth quarter of 2017. Tooling and nonrecurring costs on this program are being amortized over 242 shipsets, the number of shipsets under the USG program of record. At September 29, 2017 and December 31, 2016, our program backlog was \$1.4 million and \$5.3 million, respectively, and total program inventory was \$9.4 million and \$12.8 million, respectively. The current total program inventory includes nonrecurring costs of \$8.0 million, which may not be recoverable in the event of an extended break in production or program termination.

FMU-152 A/B – Joint Programmable Fuze (“JPF”)

We manufacture the JPF, an electro-mechanical bomb safe and arming device, which allows the settings of a weapon to be programmed in flight. We occasionally experience lot acceptance test failures due to the complexity of the product and the extreme parameters of the acceptance test. Given the maturity of the product, we now generally experience isolated failures, rather than systemic ones. As a result, identifying a root cause can take longer and result in inconsistent delivery quantities from quarter to quarter.

Sales of these fuzes can be direct to the USG, Foreign Military Sales ("FMS") through the USG and direct commercial sales ("DCS") to foreign militaries that, although not funded by the USG, require regulatory approvals from the USG. During 2016, we were awarded DCS contracts totaling \$93.0 million.

A total of 6,773 fuzes were delivered to our customers during the third quarter of 2017, which consisted of 1,216 fuzes delivered to the USG and 5,557 fuzes delivered as direct commercial sales to foreign governments. A total of 22,838 fuzes have been delivered during the first nine months of 2017. We expect to deliver 33,000 to 37,000 fuzes in 2017. A significant portion of these deliveries will be under Option 12 of our JPF program with the USG. Fuzes under Option 12 were negotiated at a lower selling price than Option 11 and the transition to Option 12 is expected to have an unfavorable margin impact of approximately \$6.5 million in 2017.

The Company currently provides the FMU-152 A/B to the USAF and twenty-eight other nations, but the U.S. Navy currently utilizes a different fuze - the FMU-139. In 2015, NAVAIR solicited proposals for a firm fixed price production contract to implement improvements to the performance characteristics of the FMU-139 (such improved fuze having been designated the FMU-139 D/B), and, the USAF had stated that, if and when a contract is awarded and production begins, the funds associated with the FMU-152 A/B will be redirected to the FMU-139 D/B. During the third quarter of 2015, the U.S. Navy announced that a competitor was awarded the contract for the FMU-139 D/B. In

the event the FMU-139 D/B program proceeds as planned and the USAF redirects the funds associated with the FMU-152 A/B to the FMU-139 D/B, our business, financial condition, results of operations and cash flows may be materially adversely impacted. The timing of the impact on our financial statements is dependent on the ability of our competitor to complete the design and qualification phase of the program and other factors. Our competitor has publicly stated that this program is expected to have a 32-month qualification phase, preceding production. Therefore, the earliest the Company may see an impact on its financial statements is 2019; however, due to the complexity of this program, the uncertainty associated with the successful completion of each phase in accordance with the planned schedule and the pending status of the USAF's final decision to redirect funds to the FMU-139 D/B, the timing and magnitude of the impact on the Company's financial statements is not certain.

The Company continues to see strong demand for the FMU-152 A/B. We are finalizing Options 13 and 14 with the USG and we have been authorized to begin the procurement of long lead materials for Option 13. Combined, the USG and DCS demand provides near term opportunities of more than \$100.0 million. Total JPF backlog at September 29, 2017 and December 31, 2016, was \$84.6 million and \$175.0 million, respectively, consisting of orders for delivery into 2018.

K-MAX®

During the second quarter of 2015, we announced that our Aerospace segment was resuming production of commercial K-MAX® aircraft. The aircraft are being manufactured at our Jacksonville, Florida and Bloomfield, Connecticut facilities. In the third quarter of 2017, the first three helicopters from the newly reopened commercial production line were accepted by our customers, Lectern Aviation of China and Rotex Helicopter. As of September 29, 2017 and December 31, 2016, our backlog for this program was \$6.4 million and \$13.7 million, respectively. During the second quarter, we announced that we will continue production of the commercial K-MAX® aircraft into 2019 at a minimum due to continued interest in the capabilities of the K-MAX®.

BLACK HAWK

The Sikorsky BLACK HAWK helicopter cockpit program involves the manufacture of cockpits, including the installation of all wiring harnesses, hydraulic assemblies, control pedals and sticks, seat tracks, pneumatic lines and the composite structure that holds the windscreen for most models of the BLACK HAWK helicopter. In July 2017, we announced that our Aerospace segment had entered into a new multi-year contract with Sikorsky to manufacture H-60 cockpits under the Department of Defense MY IX H-60 procurement authorization. The term of the agreement will be for five years, beginning in 2018 and ending in 2022. As of September 29, 2017 and December 31, 2016, our backlog for this program was \$103.1 million and \$45.6 million, respectively.

LIQUIDITY AND CAPITAL RESOURCES

Discussion and Analysis of Cash Flows

We assess liquidity in terms of our ability to generate cash to fund working capital requirements and investing and financing activities. Significant factors affecting liquidity include: cash flows generated from or used by operating activities, capital expenditures, investments in our business segments and their programs, acquisitions, divestitures, dividends, availability of future credit, adequacy of available bank lines of credit, and factors that might otherwise affect the company's business and operations generally, as described under the heading "Risk Factors" and "Forward-Looking Statements" in Item 1A of Part I of our 2016 Form 10-K.

We continue to rely upon bank financing as an important source of liquidity for our business activities including acquisitions. We believe this, when combined with cash generated from operating activities, will be sufficient to support our anticipated cash requirements for the foreseeable future; however, we may decide to borrow additional funds or raise additional equity capital to support other business activities including potential future acquisitions.

We anticipate a variety of items will have an impact on our liquidity during the next 12 months, in addition to our working capital requirements. These could include one or more of the following:

- the matters described in Note 11, Commitments and Contingencies, in the Notes to Condensed Consolidated Financial Statements, in addition to the cost of existing environmental remediation matters and deposits required to be made to the environmental escrow for our former Moosup facility;
- deferred compensation payments to former directors and officers;
- contributions to our qualified pension plan and Supplemental Employees' Retirement Plan ("SERP");

repurchase of common stock under the 2015 Share Repurchase Program;
payment of dividends;
costs associated with the start-up of new aerospace programs; and
the extension of payment terms by our customers and delays in letter of credit funding.

In addition, we have an aggregate principal balance of \$11.5 million of our 2017 Notes remaining as of September 29, 2017. These notes will remain convertible until the close of business on the second Scheduled Trading Day (as defined in the 2017 Notes indenture) immediately preceding the scheduled maturity date of November 15, 2017, unless earlier redeemed, repurchased or converted. We do not believe any of these matters will lead to a shortage of capital resources or liquidity that would adversely impact our business or results of operations.

We regularly monitor credit market conditions to identify potential issues that may adversely affect, or provide opportunities for, the securing and/or advantageous pricing of additional financing, if any, that may be necessary to continue with our growth strategy and finance working capital requirements.

Management regularly monitors pension plan asset performance and the assumptions used in the determination of our benefit obligation, comparing them to actual performance. We continue to believe the assumptions selected are valid due to the long-term nature of our benefit obligation.

Effective December 31, 2015, our qualified pension plan was frozen with respect to future benefit accruals. Under U.S. Government Cost Accounting Standard (“CAS”) 413 we must calculate the USG’s share of any pension curtailment adjustment calculated resulting from the freeze. Such adjustments can result in an amount due to the USG for pension plans that are in a surplus position or an amount due to the contractor for plans that are in a deficit position. During the fourth quarter of 2016, the Company accrued a \$0.3 million liability representing our estimate of the amount due to the USG based on our pension curtailment calculation which was submitted to the USG for review in December. Through the date of this filing there has been no response from the USG on this matter. There can be no assurance that the ultimate settlement of this matter will not have a material adverse effect on our results of operations, financial position and cash flows.

A summary of our consolidated cash flows is as follows:

	For the Nine Months Ended		
	September 29,		2017 vs. 2016
	2017	2016	
	(in thousands)		
Total cash provided by (used in):			
Operating activities	\$43,834	\$ 70,016	\$ (26,182)
Investing activities	(23,101)	(30,809 )	) 7,708
Financing activities	(28,499)	(29,746 )	) 1,247
Free Cash Flow (a):			
Net cash provided by operating activities	\$43,834	\$ 70,016	\$ (26,182)
Expenditures for property, plant and equipment	(19,874)	(23,926 )	) 4,052
Free cash flow	\$23,960	\$ 46,090	\$ (22,130)

(a) Free Cash Flow, a non-GAAP financial measure, is defined as net cash provided by operating activities less expenditures for property, plant and equipment, both of which are presented in our Condensed Consolidated Statements of Cash Flows. See Management’s Discussion and Analysis of Financial Condition and Results of Operations—Non-GAAP Financial Measures for more information regarding Free Cash Flow.

Net cash provided by operating activities decreased for the nine-month fiscal period ended September 29, 2017, versus the comparable period in 2016, primarily due to higher accounts receivables under our JPF program resulting from the timing of deliveries, the timing of payments associated with the 2016 implementation of the productivity and efficiency initiative at our Distribution segment and lower net earnings, partially offset by lower inventory related to our K-MAX® program.

Net cash used in investing activities decreased for the nine-month fiscal period ended September 29, 2017, versus the comparable period in 2016, primarily due to a lower earnout payment associated with a previous acquisition in the current period.

Net cash used in financing activities decreased for the nine-month fiscal period ended September 29, 2017, versus the comparable period in 2016, primarily due to the cost to repurchase a portion of the 2017 Notes, repayments under our

revolving credit facility, the purchase of the capped call transactions related to our 2024 Notes and higher debt issuance costs associated with the issuance of our 2024 Notes. These changes were partially offset by \$200.0 million in proceeds received from the issuance of our 2024 Notes and \$58.6 million in proceeds received related to the unwind a portion of the convertible note hedge transactions related to the 2017 Notes.

Financing Arrangements

Convertible Notes

During the fiscal quarter ending June 30, 2017, we issued \$200.0 million aggregate principal amount of convertible senior unsecured notes due May 2024 (the "2024 Notes") pursuant to an indenture (the "Indenture"), dated May 12, 2017, between the Company and U.S. Bank National Association, as trustee. In connection therewith, we entered into certain capped call transactions that cover, collectively, the number of shares of the Company's common stock underlying the 2024 Notes. In a separate transaction, we repurchased \$103.5 million aggregate principal amount of its existing convertible senior unsecured notes due November 15, 2017 (the "2017 Notes"). In connection with the repurchase of the 2017 Notes, we settled a portion of the associated bond hedge transactions and warrant transactions we entered into in 2010 in connection with their issuance. See below for further discussion on the issuance of the 2024 Notes, the repurchase of the 2017 Notes and the related transactions.

2024 Notes

On May 12, 2017, we issued \$175.0 million in principal amount of 2024 Notes, in a private placement offering. On May 24, 2017, we issued an additional \$25.0 million in principal amount of 2024 Notes pursuant to the initial purchasers' exercise of their overallotment option, resulting in the issuance of an aggregate \$200.0 million principal amount of 2024 Notes. The 2024 Notes bear 3.25% interest per annum on the principal amount, payable semiannually in arrears on May 1 and November 1 of each year, beginning on November 1, 2017. The 2024 Notes will mature on May 1, 2024, unless earlier repurchased by the Company or converted. We will settle any conversions of the 2024 Notes in cash, shares of the Company's common stock or a combination of cash and shares of common stock, at our election.

Use of proceeds from the issuance of the 2024 Notes was as follows:
in thousands

Proceeds:

Gross proceeds	\$ 200,000
Commission fees and other expenses ⁽¹⁾	(7,348)
Net proceeds	\$ 192,652

Use of Proceeds:

Cost to repurchase \$103.5 million aggregate principal amount of 2017 Notes ⁽²⁾	\$(165,308)
Cost for capped call transaction related to 2024 Notes	(20,500)
Payment made to reduce revolving credit facility ⁽³⁾	(6,844)
Total use of proceeds	\$(192,652)

⁽¹⁾ Debt issuance fees paid to the counterparties and other expenses (i.e. legal and accounting fees) related to the issuance of the 2024 Notes were capitalized.

⁽²⁾ Included in this balance is \$1.7 million of related accrued interest payments.

⁽³⁾ Additional payments to the revolving credit facility were made from proceeds received as part of the bond hedge settlement related to the repurchase of the 2017 Notes. See the 2017 Notes section below for further discussion.

The following table illustrates the conversion rate at the date of transaction:

	May 12, 2017
2024 Notes	
Conversion Rate per \$1,000 principal amount ⁽¹⁾	15.3227
Conversion Price ⁽²⁾	\$65.2626
Contingent Conversion Price ⁽³⁾	\$84.84
Aggregate shares to be issued upon conversion ⁽⁴⁾	3,064,540

(1) Represents the number of shares of Common Stock hypothetically issuable per each \$1,000 principal amount of 2024 Notes, subject to adjustments upon the occurrence of certain specified events in accordance with the terms of the Indenture.

(2) Represents \$1,000 divided by the conversion rate as of such date. The conversion price reflects the strike price of the embedded option within the 2024 Notes. If the Company's share price exceeds the conversion price at conversion, the noteholders would be entitled to receive additional consideration either in cash, shares or a combination thereof, the form of which is at the sole discretion of the Company.

(3) Prior to November 1, 2023, the notes are convertible only in the following circumstances: (1) during any fiscal quarter commencing after July 1, 2017, and only during any such fiscal quarter, if the last reported sale price of the Company's common stock was greater than or

equal to 130% of the applicable conversion price for at least 20 trading days (whether or not consecutive) during the 30 consecutive trading days ending on, and including, the last trading day of the immediately preceding fiscal quarter, (2) during the five consecutive business day period following any ten consecutive trading day period (the "measurement period") in which the trading price per \$1,000 principal amount of 2024 Notes for each trading day of the measurement period was less than 98% of the product of the last reported sale price of the Company's common stock and the conversion rate on each such trading day or (3) upon the occurrence of specified corporate events. On or after November 1, 2023, until the close of business on the second scheduled trading day immediately preceding the maturity date, holders may convert their notes at any time, regardless of the foregoing circumstances. If the Company undergoes a fundamental change (as defined in the Indenture), holders of the notes may require the Company to repurchase all or a portion of their notes for cash at a repurchase price equal to 100% of the principal amount to be repurchased, plus any accrued and unpaid interest. As of September 29, 2017, none of the conditions permitting the holders of the 2024 Notes to convert had been met. Therefore, the 2024 Notes are classified as long-term debt.

⁽⁴⁾ This represents the number of shares hypothetically issuable upon conversion of 100% of the outstanding aggregate principal amount of the 2024 Notes at each date; however, the terms of the 2024 Notes state that the Company may pay or deliver, as the case may be, cash, shares of the Company's common stock or a combination of cash and shares of common stock, at the Company's election. The Company currently intends to settle the aggregate principal amount in cash. Amounts due in excess of the principal, if any, also may be settled in cash, shares of the Company's common stock or a combination of cash and shares of common stock, at the Company's election.

In connection with the 2024 Notes offering, we entered into capped call transactions with certain of the initial purchasers or their respective affiliates. These transactions are intended to reduce the potential dilution to the Company's shareholders and/or offset the cash payments we are required to make in excess of the principal amount upon any future conversion of the notes in the event that the market price per share of the Company's common stock is greater than the strike price of the capped call transactions, with such reduction and/or offset subject to a cap based on the cap price of the capped call transactions. Under the terms of the capped call transactions, the strike price (\$65.2626) and the cap price (\$88.7570) are each subject to adjustment in certain circumstances. In connection with establishing their initial hedges of the capped call transactions, the option counterparties or their respective affiliates entered into various derivative transactions with respect to the Company's common stock concurrently with or shortly after the pricing of the notes. The capped call transactions, which cost an aggregate \$20.5 million, were recorded as a reduction of additional paid-in capital.

The note payable principal balance for the 2024 Notes at the date of issuance of \$200.0 million was bifurcated into the debt component of \$179.5 million and the equity component of \$20.5 million. The difference between the note payable principal balance and the fair value of the debt component representing the debt discount is being accreted to interest expense over the term of the 2024 Notes. The fair value of the debt component was recognized using a 5.0% discount rate, representing the Company's borrowing rate at the date of issuance for a similar debt instrument without a conversion feature with an expected life of seven years.

We incurred \$7.4 million of debt issuance costs in connection with the sale of the 2024 Notes, which was allocated between the debt and equity components of the instrument. Of the total amount, \$0.7 million was recorded as an offset to additional paid-in capital. The balance, \$6.7 million, was recorded as a contra-debt balance and is being amortized over the term of the 2024 Notes. Total amortization expense for the three-month and nine-month fiscal periods ended September 29, 2017 was \$0.2 million and \$0.3 million.

2017 Notes

In November 2010, we issued convertible senior unsecured notes due on November 15, 2017, in the aggregate principal amount of \$115.0 million in a private placement offering. These notes bear 3.25% interest per annum on the principal amount, payable semiannually in arrears on May 15 and November 15 of each year, beginning in 2011. In May 2017, we used a portion of the net proceeds from the issuance of the 2024 Notes, along with cash received from

the counterparties in connection with the termination of the existing convertible note hedge transactions referred to below, to repurchase \$103.5 million principal amount of the 2017 Notes from a limited number of holders in an arm's length transaction. This repurchase represented approximately 90% of the aggregate principal amount of 2017 Notes. The repurchases were accounted for as an extinguishment of the outstanding instrument. Of the total aggregate cost of \$165.3 million, \$60.0 million was allocated to the equity component of the 2017 notes and was recorded as a reduction to additional paid-in capital. The remainder of the cost was attributed to the outstanding principal repurchased and accrued interest. As of September 29, 2017, \$11.5 million principal amount remains outstanding under the 2017 Notes.

The repayment of a portion of the 2017 Notes was not contingent upon the issuance of the 2024 Notes. As such, the repurchase of the 2017 Notes was accounted for as a debt extinguishment.

See below for further details on the loss on extinguishment:

in thousands

Carrying value of 2017 Notes	\$ 113,943
Carrying value of Redeemed Debt	\$ 102,548
Fair value of Consideration Transferred ⁽¹⁾	103,637
Loss on extinguishment of 2017 Notes ⁽²⁾	\$(1,089)
Acceleration of debt issuance cost @ 90% ⁽³⁾	(297)
Total loss on extinguishment of 2017 Notes ⁽⁴⁾	\$(1,386)

⁽¹⁾ The fair value of consideration transferred was calculated using a discount rate of 3%, representing the Company's borrowing rate at the date of issuance for a similar debt instrument with a remaining expected life of six months (for the 2017 Notes).

⁽²⁾ The majority of this balance relates to the write-off of approximately \$1.0 million, 90% of the unamortized debt discount.

⁽³⁾ The Company determined that in connection with the repurchase of the 2017 Notes, 90% of the unamortized debt issuance costs should be written off, representing the approximate outstanding portion of these costs related to the notes purchased.

⁽⁴⁾ This loss is included in interest expense, net on the Company's Consolidated Statement of Operations.

In connection with the 2017 Notes, we had entered into convertible note hedge transactions and warrant transactions ("existing call spread transactions") with certain financial institutions. These transactions were accounted for as equity instruments at the time of issuance in 2010. With the intention of repurchasing the 2017 Notes, we entered into agreements with these financial institutions to terminate a portion of the existing call spread transactions concurrently with the offering. In connection with these transactions, we received \$58.6 million in payments related to the unwind of 90% of the convertible note hedge transactions and made deliveries of 624,044 shares of the Company's common stock in connection with the partial unwind of the warrant transactions. We used a portion of the proceeds from the bond hedge settlement to repurchase the 2017 Notes as described above and to make a payment to the revolving credit facility. The cash proceeds received were recorded as an increase of additional paid-in-capital which was partially offset by the delivery of shares.

The remaining portion of the 2017 Notes are convertible at the option of the noteholders until the close of business on the second Scheduled Trading Day (as defined in the 2017 Notes indenture) immediately preceding the maturity date. Accordingly, the remaining carrying amount of the 2017 Notes was recorded in current liabilities and a portion of the equity component, representing the unamortized debt discount, was reclassified from additional paid-in capital to temporary equity on the Company's Condensed Consolidated Balance Sheet as of September 29, 2017.

Credit Agreement

On May 6, 2015, we closed on an amended and restated \$700.0 million Credit Agreement. Capitalized terms used in this discussion of the Credit Agreement but not defined herein have the meanings ascribed thereto in the Credit Agreement, as amended. The Credit Agreement amends and restates our previously existing credit facility to, among other things: (i) extend the maturity date to May 6, 2020; (ii) increase the aggregate amount of revolving commitments from \$400.0 million to \$600.0 million; (iii) reinstate the aggregate amount of outstanding Term Loans to \$100.0 million; (iv) modify the affirmative and negative covenants set forth in the facility; and (v) effectuate a number of additional modifications to the terms and provisions of the facility, including its pricing. On May 8, 2017, we entered into Amendment No. 1 to the Credit Agreement to permit the offering of the 2024 Notes and the entering into of the related capped call transactions.

The term loan commitment requires quarterly payments of principal (which commenced on June 30, 2015) at the rate of \$1.25 million, increasing to \$1.875 million on June 30, 2017, and then to \$2.5 million on June 30, 2019, with \$65.0 million payable in the final quarter of the facility's term. The facility includes an accordion feature that allows us to increase the aggregate amount available to up to \$900.0 million with additional commitments from the Lenders.

Interest rates on amounts outstanding under the Credit Agreement are variable, and are determined based on the Consolidated Senior Secured Leverage Ratio. At September 29, 2017, the interest rate for the outstanding amounts on both the revolving credit facility and term loan commitment was 2.56%. In addition, we are required to pay a quarterly commitment fee on the unused revolving loan commitment amount at a rate ranging from 0.175% to 0.300% per annum, based on the Consolidated

Senior Secured Leverage Ratio. Fees for outstanding letters of credit range from 1.25% to 2.00%, based on the Consolidated Senior Secured Leverage Ratio.

The financial covenants associated with the Credit Agreement include a requirement that (i) the Consolidated Senior Secured Leverage Ratio cannot be greater than 3.50 to 1.00, with an available election to increase the maximum to 3.75 to 1.00 for four consecutive quarters in connection with a Permitted Acquisition with consideration in excess of \$125.0 million; (ii) the Consolidated Total Leverage Ratio cannot be greater than 4.00 to 1.00, with an available election to increase the maximum to 4.25 to 1.00 for four consecutive quarters in connection with a Permitted Acquisition with consideration in excess of \$125.0 million; (iii) the Consolidated Interest Coverage Ratio cannot be less than 4.00 to 1.00; and (iv) Liquidity: (a) as of the last day of the fiscal quarter of the Company ending two full fiscal quarters prior to the stated maturity of the 2017 Notes, cannot be less than an amount equal to 50% of the outstanding principal amount of the 2017 Notes, and (b) as of the last day of each fiscal quarter of the Company ending thereafter, cannot be less than an amount equal to the outstanding principal amount of the Specified Convertible Notes as of such day. We were in compliance with the financial covenants as of and for the quarter ended September 29, 2017, and do not anticipate noncompliance in the foreseeable future.

Total average bank borrowings during the quarter ended September 29, 2017, were \$269.7 million compared to \$315.6 million for the year ended December 31, 2016. As of September 29, 2017 and December 31, 2016, there was \$451.5 million and \$381.7 million available for borrowing, respectively, under the Revolving Credit Facility, net of letters of credit. However, based on EBITDA levels at September 29, 2017 and December 31, 2016, amounts available for borrowing were limited to \$165.2 million and \$209.5 million, respectively. Letters of credit are generally considered borrowings for purposes of the Revolving Credit Facility. A total of \$6.7 million and \$5.9 million in letters of credit was outstanding under the Revolving Credit Facility as of September 29, 2017 and December 31, 2016, respectively.

Other Sources/Uses of Capital

We contributed \$10.0 million to the qualified pension plan and \$2.9 million to the SERP through the end of the third quarter. We do not expect to make any further contributions to the qualified pension plan during 2017. We plan to contribute an additional \$0.2 million to the SERP in 2017. For the 2016 plan year, we contributed \$10.0 million to the qualified pension plan and \$0.5 million to the SERP.

On April 29, 2015, we announced that our Board of Directors approved a share repurchase program ("2015 Share Repurchase Program") authorizing the repurchase of up to \$100.0 million of the common stock, par value \$1.00 per share, of the Company. This new program replaced our 2000 Stock Repurchase Program. We currently intend to repurchase shares to offset the annual issuance of shares under our employee stock plans, but the timing and actual number of shares repurchased will depend on a variety of factors including stock price, market conditions, corporate and regulatory requirements, capital availability and other factors, including acquisition opportunities. As of September 29, 2017, we had repurchased 722,000 shares under the 2015 Share Repurchase Program and approximately \$68.7 million remained available for repurchases under this authorization.

NON-GAAP FINANCIAL MEASURES

Management believes the non-GAAP (Generally Accepted Accounting Principles) measures used in this report provide investors with important perspectives into our ongoing business performance. We do not intend for the information to be considered in isolation or as a substitute for the related GAAP measures. Other companies may define the measures differently. We define the non-GAAP measures used in this report and other disclosures as follows:

Organic Sales

Organic Sales is defined as "Net Sales" less sales derived from acquisitions completed during the preceding twelve months. We believe that this measure provides management and investors with a more complete understanding of underlying operating results and trends of established, ongoing operations by excluding the effect of acquisitions, which can obscure underlying trends. We also believe that presenting Organic Sales separately for our segments provides management and investors with useful information about the trends impacting our segments and enables a more direct comparison to other businesses and companies in similar industries. Management recognizes that the term "Organic Sales" may be interpreted differently by other companies and under different circumstances. The following table illustrates the calculation of Organic Sales using the GAAP measure, "Net Sales".

Organic Sales (in thousands)

	For the Three Months Ended September 30		For the Nine Months Ended September 30	
	2017	2016	2017	2016
Distribution				
Net sales	\$267,641	\$ 274,388	\$817,965	\$ 849,104
Acquisition Sales	—	1,128	—	4,681
Organic Sales	\$267,641	\$ 273,260	\$817,965	\$ 844,423
Aerospace				
Net sales	\$ 179,405	\$ 179,086	\$514,028	\$ 526,210
Acquisition Sales	—	18,037	—	53,418
Organic Sales	\$ 179,405	\$ 161,049	\$514,028	\$ 472,792
Consolidated				
Net sales	\$447,046	\$ 453,474	\$1,331,993	\$ 1,375,314
Acquisition Sales	—	19,165	—	58,099
Organic Sales	\$447,046	\$ 434,309	\$1,331,993	\$ 1,317,215

Organic Sales per Sales Day

Organic Sales per Sales Day is defined as GAAP "Net sales of the Distribution segment" less sales derived from acquisitions completed during the preceding twelve months divided by the number of Sales Days in a given period. Sales Days are the days that the Distribution segment's branch locations were open for business and exclude weekends and holidays. Management believes Organic Sales per Sales Day provides an important perspective on how net sales may be impacted by the number of days the segment is open for business and provides a basis for comparing periods in which the number of sales days differs.

Free Cash Flow

Free Cash Flow is defined as GAAP "Net cash provided by (used in) operating activities" in a period less "Expenditures for property, plant & equipment" in the same period. Management believes Free Cash Flow provides an important perspective on our ability to generate cash from our business operations and, as such, that it is an important financial

measure for use in evaluating the Company's financial performance. Free Cash Flow should not be viewed as representing the residual cash flow available for discretionary expenditures such as dividends to shareholders or acquisitions, as it may exclude certain mandatory expenditures such as repayment of maturing debt and other contractual obligations. Management uses Free Cash Flow internally to assess overall liquidity.

CONTRACTUAL OBLIGATIONS AND OFF-BALANCE SHEET ARRANGEMENTS

There have been no material changes outside the ordinary course of business in our contractual obligations or off-balance sheet arrangements during the first nine months of 2017. See our 2016 Form 10-K for a discussion of our contractual obligations and off-balance sheet arrangements.

CRITICAL ACCOUNTING ESTIMATES

Preparation of the Company's financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Management believes the most complex and sensitive judgments, because of their significance to the Consolidated Financial Statements, result primarily from the need to make estimates about the effects of matters that are inherently uncertain. Management's Discussion and Analysis and the Notes to Consolidated Financial Statements in the Company's 2016 Form 10-K describe the critical accounting estimates and significant accounting policies used in preparing the Consolidated Financial Statements. Actual results in these areas could differ from management's estimates. There have been no significant changes in the Company's critical accounting estimates and significant accounting policies in 2017.

RECENT ACCOUNTING STANDARDS

Information regarding recent changes in accounting standards is included in Note 2, Recent Accounting Standards, of the Notes to Condensed Consolidated Financial Statements in this report.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

There have been no significant changes in the Company's exposure to market risk during the first nine months of 2017. See the Company's 2016 Form 10-K for a discussion of the Company's exposure to market risk.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

We have carried out an evaluation, under the supervision and with the participation of our management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of September 29, 2017. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives. Based upon our evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that, as of September 29, 2017, our disclosure controls and procedures were effective.

Changes in Internal Controls

There was no change in our internal control over financial reporting that occurred during our most recently completed fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting. We are in the process of implementing a new enterprise-wide business system for our Distribution segment. In order to minimize disruptions to our ongoing operations we have developed a project plan that takes a phased approach to implementation and includes appropriate contingency plans. The implementation of the new ERP system will likely affect the processes that constitute our internal control over financial reporting for the Distribution segment.

PART II

Item 1. Legal Proceedings

General

From time to time, as a normal incident of the nature and kinds of businesses in which the Company and its subsidiaries are, and were, engaged, various claims or charges are asserted and legal proceedings are commenced by or against the Company and/or one or more of its subsidiaries. Claimed amounts may be substantial but may not bear any reasonable relationship to the merits of the claim or the extent of any real risk of court or arbitral awards. We record accruals for losses related to those matters that we consider to be probable and that can be reasonably estimated. Gain contingencies, if any, are recognized when they are realized and legal costs generally are expensed when incurred.

We evaluate, on a quarterly basis, developments in legal proceedings that could affect the amount of any accrual and developments that would make a loss contingency both probable and reasonably estimable. Our loss contingencies are subject to substantial uncertainties, however, including for each such contingency the following, among other factors: (i) the procedural status of the case; (ii) whether the case has or may be certified as a class action suit; (iii) the outcome of preliminary motions; (iv) the impact of discovery; (v) whether there are significant factual issues to be determined or resolved; (vi) whether the proceedings involve a large number of parties and/or claims in multiple jurisdictions or jurisdictions in which the relevant laws are complex or unclear; (vii) the extent of potential damages, which are often unspecified or indeterminate; and (viii) the status of settlement discussions, if any, and the settlement postures of the parties. Because of these uncertainties, management has determined that, except as otherwise noted below, the amount of loss or range of loss that is reasonably possible in respect of each matter described below (including any reasonably possible losses in excess of amounts already accrued), is not reasonably estimable.

While it is not possible to predict the outcome of these matters with certainty, based upon available information, management believes that all settlements, arbitration awards and final judgments, if any, which are considered probable of being rendered against us in legal proceedings and that can be reasonably estimated are accrued for at September 29, 2017. Despite this analysis, there can be no assurance that the final outcome of these matters will not have a material adverse effect on our business, financial condition, results of operations or cash flows.

As of September 29, 2017, neither the Company nor any of its subsidiaries is a party, nor is any of its or their property subject, to any material pending legal proceedings, other than ordinary routine litigation incidental to the business of the Company and its subsidiaries. Additional information relating to certain of these matters is set forth in Note 11, Commitments and Contingencies of the Notes to Condensed Consolidated Financial Statements.

Environmental Matters

The Company and its subsidiaries are subject to numerous U.S. Federal, state and international environmental laws and regulatory requirements and are involved from time to time in investigations or litigation of various potential environmental issues concerning activities at our facilities or former facilities or remediation as a result of past activities (including past activities of companies we have acquired). From time to time, we receive notices from the U.S. Environmental Protection Agency or equivalent state or international environmental agencies that we are a potentially responsible party under the Comprehensive Environmental Response, Compensation and Liability Act (commonly known as the "Superfund Act") and/or equivalent laws. Such notices assert potential liability for cleanup costs at various sites, which may include sites owned by us, sites we previously owned and treatment or disposal sites not owned by us, allegedly containing hazardous substances attributable to us from past operations. While it is not possible to predict the outcome of these proceedings, in the opinion of management, any payments we may be required to make as a result of all such claims in existence at September 29, 2017, will not have a material adverse effect on our business, financial condition and results of operations or cash flows.

Asbestos Litigation

Like many other industrial companies, the Company and/or one of its subsidiaries may be named as a defendant in lawsuits alleging personal injury as a result of exposure to asbestos integrated into certain products sold or distributed by the Company and/or the named subsidiary. A substantial majority of these asbestos-related claims have been covered by insurance or other forms of indemnity or have been dismissed without payment. The rest have been resolved for amounts that are not material to the Company, either individually or in the aggregate. Based on information currently available, we do not believe that the resolution of any currently pending asbestos-related matters will have a material adverse effect on our business, financial condition, results of operations or cash flows.

Item 1A. Risk Factors

Investors should carefully review and consider the information regarding certain factors that could materially affect our business, results of operations, financial condition and cash flows as set forth under Item 1A. "Risk Factors" in our 2016 Form 10-K. From time to time we disclose changes to risk factors that have been previously disclosed. See below for information regarding changes to our risk factors since the filing of our 2016 Form 10-K. Other than the information presented below, we do not believe there have been any material changes to the risk factors previously disclosed in our 2016 Form 10-K. Additional risks and uncertainties not presently known to us or that we currently believe not to be material may also adversely impact our business, results of operations, financial position and cash flows.

Certain of our operations are conducted through joint ventures, which entail special risks.

The Company has a 49% equity interest in Kineco-Kaman Composites - India Private Limited, a composites manufacturing joint venture located in Goa, India. The Company relies significantly on the services and skills of its joint venture partner to manage and conduct the local business operations of the joint venture and ensure compliance with all applicable laws and regulations. If our joint venture partner fails to perform these functions adequately, it may adversely affect our business, financial condition, results of operations and cash flows. Moreover, if our joint venture partner fails to honor its financial obligations to commit capital, equity or credit support to the joint venture as a result of financial or other difficulties or for any other reason, the joint venture may be unable to perform contracted services or deliver contracted products unless we provide the necessary capital, equity or credit support.

Economic conditions and regulatory changes leading up to and following the United Kingdom's ("UK") likely exit from the European Union ("EU") could have a material adverse effect on our business, financial condition and results of operations.

We have business operations in both the UK and the broader EU. In June 2016, a majority of voters in the UK elected to withdraw from the EU in a national referendum, and in March 2017, the UK gave notice to the EU that it was formally initiating the withdrawal process. The terms of any withdrawal are subject to a negotiation period that could last up to two years from that date, unless the time period is extended. The referendum and withdrawal process have created significant uncertainty about the future relationship between the UK and the EU, and have given rise to calls for the governments of other EU member states to consider withdrawal.

These developments, or the perception that any of them could occur, may have a material adverse effect on global economic conditions and the stability of global financial markets, and could significantly reduce global market liquidity and restrict the ability of key market participants to operate in certain financial markets. Asset valuations, currency exchange rates and credit ratings may be especially subject to increased market volatility. Lack of clarity about future UK laws and regulations as the UK determines which EU laws to replace or replicate in the course of its withdrawal, including financial laws and regulations, tax and free trade agreements, intellectual property rights, supply chain logistics, environmental, health and safety laws and regulations, immigration laws and employment laws, could decrease foreign direct investment in the UK, increase costs, depress economic activity and restrict our access to capital. If the UK and the EU are unable to negotiate acceptable withdrawal terms or if other EU member states pursue withdrawal, barrier-free access between the UK and other EU member states or among the European economic area overall could be diminished or eliminated. Any of these factors could have a direct or indirect impact on our business in the UK and EU, our customers and suppliers in the UK and EU and our business outside the UK and EU. Any of these factors could have a material adverse effect on our business, financial condition and results of operations and reduce the price of our common stock.

Exports of certain of our products are subject to various export control regulations and authorizations, and we may not be successful in obtaining the necessary U.S. Government approvals and resultant export licenses for proposed sales

to certain foreign customers.

We must comply with various laws and regulations relating to the export of our products and technology, including a requirement to obtain the necessary export approvals and/or other licenses or authorizations from the U.S. Government before we are permitted to sell certain products and technologies outside of the United States. We can give no assurance that we will be successful in obtaining the necessary licenses or authorizations in a timely manner or at all. Any significant delay in, or impairment of, our ability to sell products or technologies outside of the United States could have a material adverse effect on our business, financial condition and results of operations.

FORWARD-LOOKING STATEMENTS

This report contains "forward-looking statements" within the meaning of the safe harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. Forward-looking statements also may be included in other publicly available documents issued by the Company and in oral statements made by our officers and representatives from time to time. These forward-looking statements are intended to provide management's current expectations or plans for our future operating and financial performance, based on assumptions currently believed to be valid. They can be identified by the use of words such as "anticipate," "intend," "plan," "goal," "seek," "believe," "project," "estimate," "expect," "strategy," "future," "likely," "may," "should," "would," "could," "will" and other words of similar meaning in connection with a discussion of future operating or financial performance. Examples of forward looking statements include, among others, statements relating to future sales, earnings, cash flows, results of operations, uses of cash and other measures of financial performance.

Because forward-looking statements relate to the future, they are subject to inherent risks, uncertainties and other factors that may cause the Company's actual results and financial condition to differ materially from those expressed or implied in the forward-looking statements. Such risks, uncertainties and other factors include, among others: (i) changes in domestic and foreign economic and competitive conditions in markets served by the Company, particularly the defense, commercial aviation and industrial production markets; (ii) changes in government and customer priorities and requirements (including cost-cutting initiatives, government and customer shut-downs, the potential deferral of awards, terminations or reductions of expenditures to respond to the priorities of Congress and the Administration, or budgetary cuts resulting from Congressional actions or automatic sequestration); (iii) changes in geopolitical conditions in countries where the Company does or intends to do business; (iv) the successful conclusion of competitions for government programs (including new, follow-on and successor programs) and thereafter successful contract negotiations with government authorities (both foreign and domestic) for the terms and conditions of the programs; (v) the timely receipt of any necessary export approvals and/or other licenses or authorizations from the U.S. Government; (vi) timely satisfaction or fulfillment of material contractual conditions precedents in customer purchase orders, contracts, or similar arrangements; (vii) the existence of standard government contract provisions permitting renegotiation of terms and termination for the convenience of the government; (viii) the successful resolution of government inquiries or investigations relating to our businesses and programs; (ix) risks and uncertainties associated with the successful implementation and ramp up of significant new programs, including the ability to manufacture the products to the detailed specifications required and recover start-up costs and other investments in the programs; (x) potential difficulties associated with variable acceptance test results, given sensitive production materials and extreme test parameters; (xi) the receipt and successful execution of production orders under the Company's existing U.S. government JPF contract, including the exercise of all contract options and receipt of orders from allied militaries, but excluding any next generation programmable fuze programs, as all have been assumed in connection with goodwill impairment evaluations; (xii) the continued support of the existing K-MAX® helicopter fleet, including sale of existing K-MAX® spare parts inventory and the receipt of orders for new aircraft sufficient to recover our investment in the restart of the K-MAX® production line; (xiii) the accuracy of current cost estimates associated with environmental remediation activities; (xiv) the profitable integration of acquired businesses into the Company's operations; (xv) the ability to implement our ERP systems in a cost-effective and efficient manner, limiting disruption to our business, and allowing us to capture their planned benefits while maintaining an adequate internal control environment; (xvi) changes in supplier sales or vendor incentive policies; (xvii) the effects of price increases or decreases; (xviii) the effects of pension regulations, pension plan assumptions, pension plan asset performance, future contributions and the pension freeze, including the ultimate determination of the U.S. Government's share of any pension curtailment adjustment calculated in accordance with CAS 413; (xix) future levels of indebtedness and capital expenditures; (xx) the continued availability of raw materials and other commodities in adequate supplies and the effect of increased costs for such items; (xxi) the effects of currency exchange rates and foreign competition on future operations; (xxii) changes in laws and regulations, taxes, interest rates, inflation rates and general business conditions; (xxiii) the effects, if any, of the UK's exit from the EU; (xxiv) future repurchases and/or issuances of common stock; (xxv) the incurrence of unanticipated restructuring costs or the failure to realize

anticipated savings or benefits from past or future expense reduction actions; and (xxvi) other risks and uncertainties set forth herein, in our 2016 Form 10-K and in our Form 10-Q for the fiscal quarter ended June 30, 2017.

Any forward-looking information provided in this report should be considered with these factors in mind. We assume no obligation to update any forward-looking statements contained in this report.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

The following table provides information about purchases of Common Stock by the Company during the three-month fiscal period ended September 29, 2017:

Period	Total Number of Shares Purchased (a)	Average Price Paid per Share	Total Number of Shares Purchased as Part of a Publicly Announced Plan (b)	Approximate Dollar Value of Shares That May Yet Be Purchased Under the Plan (in thousands)
July 1, 2017 – July 28, 2017	—	\$ —	—	\$73,113
July 29, 2017 – August 25, 2017	8,937	\$ 50.85	8,937	\$72,658
August 26, 2017 – September 29, 2017	78,448	\$ 51.00	78,063	\$68,676
Total	87,385		87,000	

(a) During the quarter the Company purchased 385 shares in connection with employee tax withholding obligations as permitted by our equity compensation plans, which are SEC Rule 16b-3 qualified compensation plans. These were not purchases under our publicly announced program.

(b) On April 29, 2015, the Company announced that its Board of Directors approved a \$100.0 million share repurchase program.

Item 4. Mine Safety Disclosure

Information concerning mine safety violations required by Section 1503(a) of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") and Item 104 of Regulation S-K was not required for this quarterly report on Form 10-Q as there were no reportable violations during the quarter.

Item 6. Index To Exhibits

<u>10.1</u>	Offer Letter between Kaman Corporation and Richard R. Barnhart effective as of September 24, 2017 (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K dated September 21, 2017, File No. 001-35419)	Previously Filed
<u>10.2</u>	Transition and Retirement Agreement between Kaman Corporation and Gregory L. Steiner dated September 21, 2017 (incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K dated September 21, 2017, File No. 001-35419)	Previously Filed
<u>31.1</u>	Certification of Chief Executive Officer Pursuant to Rule 13a-14 under the Securities Exchange Act of 1934	Filed Herewith
<u>31.2</u>	Certification of Chief Financial Officer Pursuant to Rule 13a-14 under the Securities Exchange Act of 1934	Filed Herewith
<u>32.1</u>	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	Filed Herewith
<u>32.2</u>	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	Filed Herewith
101.INS	XBRL Instance Document	
101.SCH	XBRL Taxonomy Extension Schema Document	
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document	
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document	
101.LAB	XBRL Taxonomy Extension Label Linkbase Document	
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document	

SIGNATURES

Kaman Corporation and Subsidiaries

Signatures

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

KAMAN CORPORATION

Registrant

Date: October 26, 2017 /s/ Neal J. Keating

By: Neal J. Keating
Chairman, President and
Chief Executive Officer

Date: October 26, 2017 /s/ Robert D. Starr

By: Robert D. Starr
Executive Vice President and
Chief Financial Officer

KAMAN CORPORATION
INDEX TO EXHIBITS

<u>10.1</u>	Offer Letter between Kaman Corporation and Richard R. Barnhart effective as of September 24, 2017 (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K dated September 21, 2017, File No. 001-35419)	Previously Filed
<u>10.2</u>	Transition and Retirement Agreement between Kaman Corporation and Gregory L. Steiner dated September 21, 2017 (incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K dated September 21, 2017, File No. 001-35419)	Previously Filed
<u>31.1</u>	Certification of Chief Executive Officer Pursuant to Rule 13a-14 under the Securities Exchange Act of 1934	Filed Herewith
<u>31.2</u>	Certification of Chief Financial Officer Pursuant to Rule 13a-14 under the Securities Exchange Act of 1934	Filed Herewith
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