Woodward, Inc.
Form 10-Q
July 21, 2016
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 June 30, 2016

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 000-08408
WOODWARD, INC.
(Exact name of registrant as specified in its charter)

Delaware	36-1984010
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1081 Woodward Way, Fort Collins, Colorado	80524
(Address of principal executive offices)	(Zip Code)

(970) 482-5811

(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, or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

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

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

Yes No

As of July 19, 2016, 61,481,213 shares of the registrant's common stock with a par value of $0.001455 per share were outstanding.

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PART I – FINANCIAL INFORMATION

Item 1.Financial Statements

WOODWARD, INC.

CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS

(In thousands, except per share amounts)

(Unaudited)

	Three-Months Ended June 30,		Nine-Months Ended June 30,	
	2016	2015	2016	2015
Net sales	$ 507,664	$ 494,810	$ 1,432,156	$ 1,475,678
Costs and expenses:				
Cost of goods sold	370,722	351,421	1,050,238	1,050,783
Selling, general and administrative expenses	36,415	39,305	114,020	117,598
Research and development costs	29,928	33,555	93,287	97,912
Amortization of intangible assets	6,887	7,224	20,759	22,026
Interest expense	6,522	6,077	19,664	17,355
Interest income	(610)	(219)	(1,498)	(567)
Other (income) expense, net (Note 16)	(5,608)	(112)	(10,044)	(1,651)
Total costs and expenses	444,256	437,251	1,286,426	1,303,456
Earnings before income taxes	63,408	57,559	145,730	172,222
Income tax expense	12,361	13,806	28,039	40,830
Net earnings	$ 51,047	$ 43,753	$ 117,691	$ 131,392
Earnings per share (Note 3):				
Basic earnings per share	$ 0.83	$ 0.68	$ 1.90	$ 2.02
Diluted earnings per share	$ 0.81	$ 0.66	$ 1.85	$ 1.98
Weighted Average Common Shares Outstanding (Note 3):				
Basic	61,341	64,781	62,015	65,088
Diluted	63,109	66,227	63,560	66,504
Cash dividends per share paid to Woodward common stockholders	$ 0.11	$ 0.10	$ 0.32	$ 0.28

See accompanying Notes to Condensed Consolidated Financial Statements

WOODWARD, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE EARNINGS

(In thousands)

(Unaudited)

	Three-Months Ended June 30,		Nine-Months Ended June 30,	
	2016	2015	2016	2015
Net earnings	$ 51,047	$ 43,753	$ 117,691	$ 131,392
Other comprehensive earnings:				
Foreign currency translation adjustments	(9,359)	6,979	(9,488)	(27,966)
Gain (loss) on foreign currency transaction designated as a hedge of a net investment in a foreign subsidiary (Note 6)	395	11	912	11
Taxes on changes in foreign currency translation adjustments	444	240	149	1,500
	(8,520)	7,230	(8,427)	(26,455)

Reclassification of net realized (gains) losses on derivatives to earnings (Note 6)	(18)	25	39	74
Taxes on changes in derivative transactions	7	(10)	(14)	(28)
	(11)	15	25	46
Minimum retirement benefit liability adjustments (Note 18)				
Amortization of:				
Net prior service cost (benefit)	56	56	169	169
Net loss	424	128	1,276	385
Foreign currency exchange rate changes on minimum retirement benefit liabilities	657	(604)	1,228	454
Taxes on changes in minimum retirement liability adjustments, net of foreign currency exchange rate changes	(421)	141	(997)	(368)
	716	(279)	1,676	640
Total comprehensive earnings	$ 43,232	$ 50,719	$ 110,965	$ 105,623

See accompanying Notes to Condensed Consolidated Financial Statements

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WOODWARD, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except per share amounts)

(Unaudited)

	June 30, 2016	September 30, 2015 (a)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 118,119	$ 82,202
Accounts receivable, less allowance for uncollectible amounts of $2,798 and $3,841, respectively	291,181	322,215
Inventories	500,043	447,664
Income taxes receivable	4,740	21,838
Other current assets	36,433	43,791
Total current assets	950,516	917,710
Property, plant and equipment, net	844,455	756,100
Goodwill	555,530	556,977
Intangible assets, net	204,310	225,138
Deferred income tax assets	43,934	13,105
Other assets	47,321	44,886
Total assets	$ 2,646,066	$ 2,513,916
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Short-term borrowings and current portion of long-term debt	$ 100,000	$ 2,430
Accounts payable	178,095	173,287
Income taxes payable	47,921	6,555
Accrued liabilities	125,760	155,936
Total current liabilities	451,776	338,208
Long-term debt, less current portion	685,000	850,000
Deferred income tax liabilities	1,081	56,414
Other liabilities	349,685	116,190
Total liabilities	1,487,542	1,360,812
Commitments and contingencies (Note 20)		
Stockholders' equity:		
Preferred stock, par value $0.003 per share, 10,000 shares authorized, no shares issued	-	-
Common stock, par value $0.001455 per share, 150,000 shares authorized, 72,960 shares issued	106	106
Additional paid-in capital	141,895	131,231
Accumulated other comprehensive losses	(58,184)	(51,458)
Deferred compensation	5,061	4,322
Retained earnings	1,593,124	1,495,274
	1,682,002	1,579,475

Treasury stock at cost, 11,501 shares and 9,763 shares, respectively	(518,417)	(422,049)
Treasury stock held for deferred compensation, at cost, 157 shares and 173 shares, respectively	(5,061)	(4,322)
Total stockholders' equity	1,158,524	1,153,104
Total liabilities and stockholders' equity	$ 2,646,066	$ 2,513,916

(a) Retrospectively adjusted as discussed in Note 2, Recent accounting pronouncements

See accompanying Notes to Condensed Consolidated Financial Statements.

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WOODWARD, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Nine-Months Ended June 30,	
	2016	2015
Cash flows from operating activities:		(a)
Net earnings	$ 117,691	$ 131,392
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	49,921	55,754
Net gain on sales of assets	(4,188)	(766)
Stock-based compensation	13,267	11,086
Deferred income taxes	(87,338)	1,623
Loss on derivatives reclassified from accumulated comprehensive earnings into earnings	39	74
Proceeds from formation of joint venture (Note 4)	250,000	-
Changes in operating assets and liabilities:		
Accounts receivable	40,012	65,345
Inventories	(56,187)	(44,630)
Accounts payable and accrued liabilities	(6,548)	(41,868)
Current income taxes	58,184	(10,897)
Retirement benefit obligations	(2,903)	(3,365)
Other	(9,469)	7,742
Net cash provided by operating activities	362,481	171,490
Cash flows from investing activities:		
Payments for purchase of property, plant, and equipment	(128,628)	(190,865)
Proceeds from sale of assets	5,747	2,486
Net cash used in investing activities	(122,881)	(188,379)
Cash flows from financing activities:		
Cash dividends paid	(19,841)	(18,285)
Proceeds from sales of treasury stock	12,532	7,936
Payments for repurchases of common stock	(125,542)	(157,118)
Borrowings on revolving lines of credit and short-term borrowings	560,000	869,970
Payments on revolving lines of credit and short-term borrowings	(520,596)	(701,610)
Payments of long-term debt and capital lease obligations	(107,188)	-
Payments of debt financing costs	-	(2,359)
Net cash used in financing activities	(200,635)	(1,466)
Effect of exchange rate changes on cash and cash equivalents	(3,048)	(9,548)
Net change in cash and cash equivalents	35,917	(27,903)

Cash and cash equivalents at beginning of period	82,202	115,287
Cash and cash equivalents at end of period	$ 118,119	$ 87,384

(a) Retrospectively adjusted as discussed in Note 2, Recent accounting pronouncements

See accompanying Notes to Condensed Consolidated Financial Statements.

WOODWARD, INC.

CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(In thousands)

(Unaudited)

	Number of shares				Stockholders' equity					
							Accumulated other comprehensive (loss earnings			
	Preferred stock	Common stock	Treasury stock	Treasury stock held for deferred compensation	Common stock	Additional paid-in capital	Foreign currency translation adjustments	Unrealized derivative gains (losses)	Minimum retirement benefit liability adjustments	Total accum other compr (loss) earnin
Balances as of October 1, 2014	-	72,960	(7,397)	(198)	$ 106	$ 112,491	$ 10,819	$ 105	$ (14,457)	$ (3,5
Net earnings	-	-	-	-	-	-	-	-	-	-
Other comprehensive income (loss), net of tax	-	-	-	-	-	-	(26,455)	46	640	(25,
Cash dividends paid	-	-	-	-	-	-	-	-	-	-
Purchases of treasury stock	-	-	(2,670)	-	-	-	-	-	-	-
Sales of treasury stock	-	-	428	-	-	(4,841)	-	-	-	-
Common shares issued from treasury stock for benefit plans	-	-	259	-	-	4,490	-	-	-	-
Tax benefit attributable to stock-based compensation	-	-	-	-	-	4,511	-	-	-	-
Stock-based compensation	-	-	-	-	-	11,086	-	-	-	-
Purchases of stock by deferred	-	-	-	(18)	-	-	-	-	-	-

compensation plan										
Distribution of stock from deferred compensation plan	-	-	-	43	-	-	-	-	-	-
Balances as of June 30, 2015	-	72,960	(9,380)	(173)	$ 106	$ 127,737	$ (15,636)	$ 151	$ (13,817)	$ (29,
Balances as of October 1, 2015	-	72,960	(9,763)	(173)	$ 106	$ 131,231	$ (21,610)	$ 166	$ (30,014)	$ (51,
Net earnings	-	-	-	-	-	-	-	-	-	-
Other comprehensive income (loss), net of tax	-	-	-	-	-	-	(8,427)	25	1,676	(6,7
Cash dividends paid	-	-	-	-	-	-	-	-	-	-
Purchases of treasury stock	-	-	(2,660)	-	-	-	-	-	-	-
Sales of treasury stock	-	-	605	-	-	(7,961)	-	-	-	-
Common shares issued from treasury stock for benefit plans	-	-	317	-	-	5,319	-	-	-	-
Tax benefit attributable to stock-based compensation	-	-	-	-	-	39	-	-	-	-
Stock-based compensation	-	-	-	-	-	13,267	-	-	-	-
Purchases of stock by deferred compensation plan	-	-	-	(25)	-	-	-	-	-	-
Distribution of stock from deferred compensation plan	-	-	-	41	-	-	-	-	-	-
Balances as of June 30, 2016	-	72,960	(11,501)	(157)	$ 106	$ 141,895	$ (30,037)	$ 191	$ (28,338)	$ (58,

See accompanying Notes to Condensed Consolidated Financial Statements

WOODWARD, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

Note 1. Basis of Presentation

The Condensed Consolidated Financial Statements of Woodward, Inc. ("Woodward" or the "Company") as of June 30, 2016 and for the three and nine-months ended June 30, 2016 and June 30, 2015, included herein, have not been audited by an independent registered public accounting firm. These Condensed Consolidated Financial Statements reflect all normal recurring adjustments that, in the opinion of management, are necessary to present fairly Woodward's financial position as of June 30, 2016, and the statements of earnings, comprehensive earnings, cash flows, and changes in stockholders' equity for the periods presented herein. The results of operations for the three and nine-months ended June 30, 2016 are not necessarily indicative of the operating results to be expected for other interim periods or for the full fiscal year. Dollar and share amounts contained in these Condensed Consolidated Financial Statements are in thousands, except per share amounts.

The Condensed Consolidated Balance Sheet as of September 30, 2015 was derived from Woodward's Annual Report on Form 10-K for the fiscal year then ended. During the three-months ended March 31, 2016, Woodward adopted Accounting Standards Update ("ASU") 2015-17, "Balance Sheet Classification of Deferred Taxes," and retrospectively applied the guidance to its deferred tax assets and liabilities as of September 30, 2015. For further discussion of the impact of adopting this new accounting guidance, see Note 2, Recent accounting pronouncements.

The Condensed Consolidated Financial Statements included herein have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC") for interim reporting. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") have been condensed or omitted pursuant to such rules and regulations.

These unaudited Condensed Consolidated Financial Statements should be read in conjunction with the audited Consolidated Financial Statements and Notes thereto included in Woodward's most recent Annual Report on Form 10-K filed with the SEC and other financial information filed with the SEC.

Management is required to use estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements, the reported revenues and expenses recognized during the reporting period, and certain financial statement disclosures, in the preparation of the Condensed Consolidated Financial Statements included herein. Significant estimates in these Condensed Consolidated Financial Statements include allowances for uncollectible amounts, net realizable value of inventories, customer rebates earned and payable, warranty reserves, useful lives of property and identifiable intangible assets, the evaluation of impairments of property, the provision for income tax and related valuation reserves, the valuation of assets and liabilities acquired in business combinations, including identifiable intangible assets and goodwill, assumptions used in the determination of the funded status and annual expense of pension and postretirement employee benefit plans, the valuation of stock compensation instruments granted to employees and board members, and contingencies. Actual results could vary from Woodward's estimates.

In the first quarter of fiscal year 2016, Woodward changed the name of its Energy segment to Industrial. The term "energy" is largely viewed as "oil and gas" and therefore was not representative of the broader markets Woodward serves in this segment.

Note 2. Recent accounting pronouncements

From time to time, the Financial Accounting Standards Board ("FASB") or other standards setting bodies issue new accounting pronouncements. Updates to the FASB Accounting Standards Codification ("ASC") are communicated through issuance of an Accounting Standards Update ("ASU").

In June 2016, the FASB issued ASU 2016-13, "Measurement of Credit Losses on Financial Instruments." ASU 2016-13 adds a current expected credit loss ("CECL") impairment model to U.S. GAAP that is based on expected losses rather than incurred losses. ASU 2016-13 is effective for fiscal years beginning after December 15, 2019 (fiscal year 2021 for Woodward), including interim periods within the year of adoption. Early adoption is permitted for fiscal years beginning after December 15, 2018 (fiscal year 2020 for Woodward), including interim periods within those fiscal years. Woodward has not determined in which period it will adopt the new guidance but does not expect the application of the CECL impairment model to have a significant impact on Woodward's allowance for uncollectible amounts for accounts receivable and notes receivable from municipalities.

In March 2016, the FASB issued ASU 2016-09, "Improvements to Employee Share-Based Payment Accounting," to simplify financial reporting of the income tax impacts of share-based compensation arrangements. As early adoption is allowed, Woodward adopted ASU 2016-09 during the second quarter of fiscal year 2016. Under ASU 2016-09 Woodward classifies the excess income tax benefits from stock-based compensation arrangements as a discrete item within income tax expense, rather than recognizing such excess income tax benefits in additional paid-in capital. As required by ASU 2016-09, Woodward applied this classification guidance effective as of October 1, 2015.

Under ASU 2016-09, excess income tax benefits from stock-based compensation arrangements are classified as cash flow from operations, rather than as cash flow from financing activities. In addition, when Woodward withholds shares from an employee's exercise of stock options to fund payment by Woodward of the employee's taxes, the payment is classified as a financing activity. Woodward has elected to apply the cash flow classification guidance of ASU 2016-09 retrospectively to any prior periods presented.

Woodward has elected to continue to estimate the number of stock-based awards expected to vest, as permitted by ASU 2016-09, rather than electing to account for forfeitures as they occur.

The following table shows the impact of retrospectively applying this guidance to the Condensed Consolidated Statement of Earnings and Condensed Consolidated Statement of Cash Flows for the three-months ended December 31, 2015.

	Three-Months Ended December 31, 2015		
	As previously reported	Adjustment	As recast
Statement of Earnings:			
Earnings before income taxes	$ 27,956	$ -	$ 27,956
Income tax expense	2,345	(209)	2,136
Net earnings	$ 25,611	$ 209	$ 25,820
Earnings per share:			
Basic earnings per share	$ 0.41	$ -	$ 0.41
Diluted earnings per share	$ 0.40	$ -	$ 0.40
Weighted average common shares outstanding:			
Basic	63,054	-	63,054
Diluted	64,373	79	64,452
Statement of Cash Flows:			
Net cash provided by operating activities	$ 37,112	$ 248	$ 37,360
Net cash used in investing activities	(31,279)	-	(31,279)
Net cash used in financing activities	(1,131)	(248)	(1,379)
Effect of exchange rate changes on cash and cash equivalents	(2,482)	-	(2,482)
Net change in cash and cash equivalents	$ 2,220	$ -	$ 2,220

The following table shows the impact of retrospectively applying this guidance to the Condensed Consolidated Statement of Cash Flows for the nine-months ended June 30, 2015.

	Nine-Months Ended June 30, 2015		
	As previously reported	Adjustment	As recast
Statement of Cash Flows:			
Net cash provided by operating activities	$ 167,320	$ 4,170	$ 171,490
Net cash used in investing activities	(188,379)	-	(188,379)
Net cash provided by (used in) financing activities	2,704	(4,170)	(1,466)
Effect of exchange rate changes on cash and cash equivalents	(9,548)	-	(9,548)
Net change in cash and cash equivalents	$ (27,903)	$ -	$ (27,903)

In February 2016, the FASB issued ASU 2016-02, "Leases (Topic 842)." The purpose of ASU 2016-02 is to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018 (fiscal year 2020 for Woodward), including interim periods within the year of adoption. In transition, Woodward will be required to recognize and measure leases beginning in the earliest period presented using a modified retrospective approach; therefore, Woodward anticipates restating its Consolidated Financial Statements for the two fiscal years prior to the year of adoption. Early adoption is permitted. Woodward has not determined in which period it will adopt the new guidance and is currently assessing the impact this guidance may have on its Consolidated Financial Statements, including which of its existing operating leases will be impacted by the new guidance. Rent expense for all operating leases in fiscal year 2015, none of which was recognized on the balance sheet, was $7,299. As of September 30, 2015, future minimum rental payments required under operating leases, none of which were recognized on the balance sheet, were $19,546.

In November 2015, the FASB issued ASU 2015-17, "Balance Sheet Classification of Deferred Taxes," to simplify financial reporting and more closely conform U.S. GAAP with International Financial Reporting Standards ("IFRS"). Under ASU 2015-17, Woodward will classify all deferred tax assets and liabilities by taxing jurisdiction, along with any related valuation allowances, as either a single non-current asset or liability on the balance sheet. ASU 2015-17 is effective for fiscal years – and interim periods within those fiscal years – beginning after December 15, 2016 (fiscal year 2018 for Woodward). As early adoption is allowed, Woodward adopted ASU 2015-17 during its second quarter of fiscal year 2016, and retrospectively applied the guidance to its deferred tax assets and liabilities as of September 30, 2015. The following table shows the impact of retrospectively applying this guidance to the Condensed Consolidated Balance Sheet deferred tax assets and liabilities as of September 30, 2015.

	September 30, 2015		
	As previously reported	Adjustment	As recast
Current deferred income tax assets	$ 29,766	$ (29,766)	$ -
Total current assets	947,476	(29,766)	917,710
Noncurrent deferred income tax assets	9,388	3,717	13,105
Total assets	2,539,965	(26,049)	2,513,916

Current deferred income tax liabilities	14	(14)	-
Total current liabilities	338,222	(14)	338,208
Noncurrent deferred income tax liabilities	82,449	(26,035)	56,414
Total liabilities	1,386,861	(26,049)	1,360,812
Total liabilities and stockholders' equity	2,539,965	(26,049)	2,513,916
Net deferred tax liabilities	43,309	-	43,309

In April 2015, the FASB issued ASU 2015-03, "Simplifying the Presentation of Debt Issuance Costs." Under ASU 2015-03, Woodward will present debt issuance costs in the balance sheet as a reduction from the related debt liability rather than as an asset. Amortization of such costs will continue to be reported as interest expense. ASU 2015-03 is effective for fiscal years – and interim periods within those fiscal years – beginning after December 15, 2015 (fiscal year 2017 for

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Woodward). Early adoption is allowed. In August 2015, the FASB issued ASU 2015-15, "Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements." ASU 2015-15 supplements the requirements of ASU 2015-03 by allowing an entity to defer and present debt issuance costs related to a line of credit arrangement as an asset and subsequently amortize the deferred costs ratably over the term of the line of credit arrangement. Woodward has not determined in which period it will adopt the new guidance. Retrospective adoption is required. Woodward had unamortized debt issuance costs of $4,638 as of June 30, 2016 and $5,521 as of September 30, 2015. Long-term debt issuance costs will be reclassified from other assets to long-term debt upon adoption.

In April 2015, the FASB issued ASU 2015-02, "Consolidation (Topic 810): Amendments to the Consolidation Analysis" in response to stakeholders' concerns about current accounting for consolidation of certain legal entities and changes the analysis that a reporting entity must perform to determine whether it should consolidate such legal entities. ASU 2015-02 is effective for public business entities for fiscal years – and interim periods within those fiscal years – beginning after December 15, 2015, but early adoption is allowed. Woodward adopted ASU 2015-02 on January 1, 2016, concurrent with the consummation of the joint venture formation described in Note 4, "Joint ventures." The adoption of ASU 2015-02 had no impact on Woodward's conclusion that the joint venture described in Note 4 should not be consolidated following the guidance of ASC 810, Consolidation.

In May 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers" and has subsequently issued several supplemental and/or clarifying ASUs (collectively "ASC 606"). ASC 606 prescribes a single common revenue standard that replaces most existing U.S. GAAP revenue recognition guidance. ASC 606 outlines a five-step model, under which Woodward will recognize revenue as performance obligations within a customer contract are satisfied. ASC 606 is intended to provide more consistent interpretation and application of the principles outlined in the standard across filers in multiple industries and within the same industries compared to current practices, which should improve comparability. Adoption of ASC 606 is required for annual reporting periods beginning after December 15, 2017 (fiscal year 2019 for Woodward), including interim periods within the reporting period. Woodward may elect to adopt ASC 606 in fiscal year 2018, but does not expect to do so. Upon adoption, Woodward must elect to adopt either retrospectively to each prior reporting period presented or using the cumulative effect transition method with the cumulative effect of initial adoption recognized at the date of initial application. Woodward has not determined what transition method it will use. Woodward is currently assessing the impact that the future adoption of ASC 606 may have on its Condensed Consolidated Financial Statements by analyzing its current portfolio of customer contracts, including a review of historical accounting policies and practices to identify potential differences in applying the guidance of ASC 606.

Note 3. Earnings per share

Basic earnings per share is computed by dividing net earnings available to common stockholders by the weighted-average number of shares of common stock outstanding for the period.

Diluted earnings per share reflects the weighted-average number of shares outstanding after consideration of the dilutive effect of stock options and restricted stock.

The following is a reconciliation of net earnings to basic earnings per share and diluted earnings per share:

	Three-Months Ended	Nine-Months Ended

	June 30,		June 30,	
	2016	2015	2016	2015
Numerator:				
Net earnings	$ 51,047	$ 43,753	$ 117,691	$ 131,392
Denominator:				
Basic shares outstanding	61,341	64,781	62,015	65,088
Dilutive effect of stock options and restricted stock	1,768	1,446	1,545	1,416
Diluted shares outstanding	63,109	66,227	63,560	66,504
Income per common share:				
Basic earnings per share	$ 0.83	$ 0.68	$ 1.90	$ 2.02
Diluted earnings per share	$ 0.81	$ 0.66	$ 1.85	$ 1.98

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The following stock option grants were outstanding during the three and nine-months ended June 30, 2016 and 2015, but were excluded from the computation of diluted earnings per share because their inclusion would have been anti-dilutive:

	Three-Months Ended June 30,		Nine-Months Ended June 30,	
	2016	2015	2016	2015
Options	-	-	731	699
Weighted-average option price	$ n/a	$ n/a	$ 46.55	$ 46.55

The weighted-average shares of common stock outstanding for basic and diluted earnings per share included the weighted-average treasury stock shares held for deferred compensation obligations of the following:

	Three-Months Ended June 30,		Nine-Months Ended June 30,	
	2016	2015	2016	2015
Weighted-average treasury stock shares held for deferred compensation obligations	166	182	175	194

Note 4. Joint ventures

On January 4, 2016, Woodward and General Electric Company (“GE”), acting through its GE Aviation business unit, consummated the formation of a strategic joint venture between Woodward and GE (the “JV”). The JV designs, develops and sources the fuel system for specified existing and all future GE commercial aircraft engines that produce thrust in excess of fifty thousand pounds.

As part of the JV formation, Woodward contributed to the JV certain contractual rights and intellectual property applicable to the existing GE commercial aircraft engine programs within the scope of the JV. Woodward has no initial cost basis in the JV because Woodward had no cost basis in the contractual rights and intellectual property contributed to the JV. GE purchased from Woodward a 50% ownership interest in the JV for a $250,000 cash payment to Woodward. In addition, GE will pay contingent consideration to Woodward consisting of fifteen annual payments of $4,894 each per year beginning January 4, 2017 subject to certain claw-back conditions. Neither Woodward nor GE contributed any tangible assets to the JV.

Woodward determined that the JV formation was not the culmination of an earnings event because Woodward has significant performance obligations to support the future operations of the JV. Therefore, Woodward recorded the $250,000 consideration received from GE for its purchase of a 50% equity interest in the JV as deferred income. The $250,000 deferred income will be recognized as an increase to net sales in proportion to revenue realized on sales of applicable fuel systems within the scope of the JV in a particular period as a percentage of total revenue expected to be realized by Woodward over the estimated remaining lives of the underlying commercial aircraft engine programs assigned to the JV. As of June 30, 2016, accrued liabilities include $6,176 and other liabilities include $240,129 of unamortized deferred income realized upon the JV formation. Amortization of the deferred income recognized as an increase to sales was $1,733 for the three-months and $3,695 for the six-months ended June 30, 2016.

The $250,000 cash consideration received from GE on January 4, 2016 is taxable upon receipt for income tax purposes but not currently recognized in earnings for book purposes. Therefore, during the three month period ended March 31, 2016, Woodward recorded estimated incremental current income taxes payable of $94,125 and a related noncurrent deferred tax asset of $94,125. As of June 30, 2016, current income taxes payable includes $46,520 related to the receipt of $250,000 from GE on January 4, 2016.

Woodward and GE jointly manage the JV and any significant decisions and/or actions of the JV require the mutual consent of both parties. Neither Woodward nor GE has a controlling financial interest in the JV, but Woodward does have the ability to significantly influence the operating and financial decisions of the JV. Therefore, Woodward is accounting for its 50% ownership interest in the JV using the equity method of accounting. Other income includes $2,728 for the three-months and $4,886 for the six-months ended June 30, 2016 related to Woodward's equity interest in the earnings of the JV.

During the six-months ended June 30, 2016, Woodward received no cash distributions from the JV and therefore, Woodward's net investment in the JV was $4,886 as of June 30, 2016.

During the three and six-months ended June 30, 2016, Woodward net sales include $15,136 and $30,151, respectively, of sales to the JV and a reduction to sales of $7,643 and $14,659, respectively, related to royalties paid to the JV by Woodward on sales by Woodward directly to third party aftermarket customers. At June 30, 2016, the JV owed Woodward $4,426 and Woodward owed the JV $3,908.

Note 5. Financial instruments and fair value measurements

Financial assets and liabilities recorded at fair value in the Condensed Consolidated Balance Sheets are categorized based upon a fair value hierarchy established by U.S. GAAP, which prioritizes the inputs used to measure fair value into the following levels:

Level 1: Inputs based on quoted market prices in active markets for identical assets or liabilities at the measurement date.

Level 2: Quoted prices included in Level 1, such as quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable and can be corroborated by observable market data.

Level 3: Inputs reflect management's best estimates and assumptions of what market participants would use in pricing the asset or liability at the measurement date. The inputs are unobservable in the market and significant to the valuation of the instruments.

The table below presents information about Woodward's financial assets that are measured at fair value on a recurring basis and indicates the fair value hierarchy of the valuation techniques Woodward utilized to determine such fair value. Woodward had no financial liabilities required to be measured at fair value on a recurring basis as of June 30, 2016 or September 30, 2015.

	At June 30, 2016				At September 30, 2015			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Financial assets:								
Cash	$ 117,339	$ -	$ -	$ 117,339	$ 79,517	$ -	$ -	$ 79,517
Investments in money market funds	41	-	-	41	20	-	-	20
Investments in reverse repurchase agreements	739	-	-	739	2,665	-	-	2,665
Equity securities	11,964	-	-	11,964	9,883	-	-	9,883
Total financial assets	$ 130,083	$ -	$ -	$ 130,083	$ 92,085	$ -	$ -	$ 92,085

Investments in money market funds: Woodward sometimes invests excess cash in money market funds not insured by the Federal Depository Insurance Corporation ("FDIC"). Woodward believes that the investments in money market funds are on deposit with creditworthy financial institutions and that the funds are highly liquid. The investments in money market funds are reported at fair value, with realized gains from interest income realized in earnings and are included in “Cash and cash equivalents.” The fair values of Woodward’s investments in money market funds are based on the quoted market prices for the net asset value of the various money market funds.

Investments in reverse repurchase agreements: Woodward sometimes invests excess cash in reverse repurchase agreements. Under the terms of Woodward’s reverse repurchase agreements, Woodward purchases an interest in a pool of securities and is granted a security interest in those securities by the counterparty to the reverse repurchase agreement. At an agreed upon date, generally the next business day, the counterparty repurchases Woodward’s interest in the pool of securities at a price equal to what Woodward paid to the counterparty plus a rate of return determined daily per the terms of the reverse repurchase agreement. Woodward believes that the investments in these reverse repurchase agreements are with creditworthy financial institutions and that the funds invested are highly liquid. The investments in reverse repurchase agreements are reported at fair value, with realized gains from interest income realized in earnings, and are included in “Cash and cash equivalents.” Since the investments are generally overnight, the carrying value is considered to be equal to the fair value as the amount is deemed to be a cash deposit with no risk of change in value as of the end of each fiscal quarter.

Equity securities: Woodward holds marketable equity securities, through investments in various mutual funds, related to its deferred compensation program. Based on Woodward’s intentions regarding these instruments, marketable equity securities are classified as trading securities. The trading securities are reported at fair value, with realized gains and losses recognized in "Other (income) expense, net." The trading securities are included in "Other assets." The fair values of Woodward's trading securities are based on the quoted market prices for the net asset value of the various mutual funds.

Accounts receivable, accounts payable, the current portion of long-term debt, and short-term debt are not remeasured to fair value, as the carrying cost of each approximates its respective fair value. The estimated fair values and carrying costs of other financial instruments that are not required to be remeasured at fair value in the Condensed Consolidated Balance Sheets were as follows:

		At June 30, 2016		At September 30, 2015	
	Fair Value Hierarchy Level	Estimated Fair Value	Carrying Cost	Estimated Fair Value	Carrying Cost
Assets:					
Notes receivable from municipalities	2	$ 17,774	$ 16,165	$ 16,112	$ 15,638
Liabilities:					
Long-term debt, excluding current portion	2	$ (725,891)	$ (685,000)	$ (873,734)	$ (850,000)

In fiscal years 2014 and 2013, Woodward received long-term notes from a municipality within the state of Illinois in connection with certain economic incentives related to Woodward's development of a second campus in the greater-Rockford, Illinois area for its Aerospace segment. The fair value of the long-term notes was estimated based on a model that discounted future principal and interest payments received at an interest rate available to the Company at the end of the period for similarly rated municipal notes of similar maturity, which is a level 2 input as defined by the U.S. GAAP fair value hierarchy. The interest rates used to estimate the fair value of the long-term notes were 2.0% at June 30, 2016 and 3.0% at September 30, 2015.

In fiscal year 2013, Woodward received a long-term note from a municipality within the state of Colorado in connection with certain economic incentives related to Woodward's development of a new campus at its corporate headquarters in Fort Collins, Colorado. The fair value of the long-term note was estimated based on a model that discounted future principal and interest payments received at an interest rate available to the Company at the end of the period for similarly rated municipal notes of similar maturity, which is a level 2 input as defined by the U.S. GAAP fair value hierarchy. The interest rates used to estimate the fair value of the long-term note were 2.0% at June 30, 2016 and 3.0% at September 30, 2015.

The fair value of long-term debt was estimated based on a model that discounted future principal and interest payments at interest rates available to the Company at the end of the period for similar debt of the same maturity, which is a level 2 input as defined by the U.S. GAAP fair value hierarchy. The weighted-average interest rates used to estimate the fair value of long-term debt were 2.4% at June 30, 2016 and 2.8% at September 30, 2015.

Note 6. Derivative instruments and hedging activities

Woodward has exposures related to global market risks, including the effect of changes in interest rates, foreign currency exchange rates, changes in certain commodity prices and fluctuations in various producer indices. From time to time, Woodward enters into derivative instruments for risk management purposes only, including derivatives designated as accounting hedges and/or those utilized as economic hedges. Woodward uses interest rate related derivative instruments to manage its exposure to fluctuations of interest rates. Woodward does not enter into or issue derivatives for trading or speculative purposes.

By using derivative and/or hedging instruments to manage its risk exposure, Woodward is subject, from time to time, to credit risk and market risk on those derivative instruments. Credit risk arises from the potential failure of the counterparty to perform under the terms of the derivative and/or hedging instrument. When the fair value of a derivative contract is positive, the counterparty owes Woodward, which creates credit risk for Woodward. Woodward mitigates this credit risk by entering into transactions with only creditworthy counterparties. Market risk arises from the potential adverse effects on the value of derivative and/or hedging instruments that result from a change in interest rates, commodity prices, or foreign currency exchange rates. Woodward minimizes this market risk by establishing and monitoring parameters that limit the types and degree of market risk that may be undertaken.

In June 2015, Woodward designated an intercompany loan of 160,000 RMB between two wholly owned subsidiaries as a hedge of a foreign currency exposure of the net investment of the borrower in the lender. Foreign exchange gains on the loan of $912 for the nine-months ended June 30, 2016 and $11 for the nine-months ended June 30, 2015 are included in foreign currency translation adjustments within total comprehensive earnings. In June 2016, the intercompany loan was repaid, resulting in a realized gain of $1,484 that was recognized within total comprehensive earnings, of which $912 was recognized in fiscal year 2016 and $572 was recognized in fiscal year 2015.

In July 2016, Woodward designated a new intercompany loan of 160,000 RMB between two wholly owned subsidiaries as a hedge of a foreign currency exposure of the net investment of the borrower in the lender. Foreign exchange gains or losses on the loan will be recognized in foreign currency translation adjustments within total comprehensive earnings.

Woodward did not enter into any derivatives or hedging transactions during any of the three or nine-months ended June 30, 2016.

The remaining unrecognized gains and losses in Woodward's Condensed Consolidated Balance Sheets associated with derivative instruments that were previously entered into by Woodward, which are classified in accumulated other comprehensive losses ("accumulated OCI"), were net gains of $308 as of June 30, 2016 and $269 as of September 30, 2015.

The following table discloses the impact of derivative instruments in cash flow hedging relationships on Woodward's Condensed Consolidated Statements of Earnings, recognized in interest expense:

	Three-Months Ended June 30,		Nine-Months Ended June 30,	
	2016	2015	2016	2015
Amount of (income) expense recognized in earnings on derivative	$ (18)	$ 25	$ 39	$ 74
Amount of (gain) loss recognized in accumulated OCI on derivative	-	-	-	-
Amount of (gain) loss reclassified from accumulated OCI into earnings	(18)	25	39	74

Based on the carrying value of the realized but unrecognized gains and losses on terminated derivative instruments designated as cash flow hedges as of June 30, 2016, Woodward expects to reclassify $72 of net unrecognized gains on terminated derivative instruments from accumulated other comprehensive earnings to earnings during the next twelve months.

Note 7. Supplemental statement of cash flows information

	Nine-Months Ended June 30,	
	2016	2015
Interest paid, net of amounts capitalized	$ 31,764	$ 30,090
Income taxes paid	59,431	48,801
Income tax refunds received	1,715	426

Non-cash activities:		
Purchases of property, plant and equipment on account	13,656	39,122
Property, plant and equipment acquired by capital lease	1,626	-
Common shares issued from treasury to settle benefit plan obligations (Note 18)	13,999	12,574
Cashless exercise of stock options	753	-

Note 8. Accounts Receivable

Almost all of Woodward's sales are made on credit and result in accounts receivable, which are recorded at the amount invoiced. In the normal course of business, not all accounts receivable are collected and, therefore, an allowance for losses of accounts receivable is provided equal to the amount that Woodward believes ultimately will not be collected. In establishing the amount of the allowance, customer-specific information is considered related to delinquent accounts, past loss experience, bankruptcy filings, deterioration in the customer's operating results or financial position, and current economic conditions. Accounts receivable losses are deducted from the allowance, and the related accounts receivable balances are written off when the receivables are deemed uncollectible. Recoveries of accounts receivable previously written off are recognized when received.

Consistent with business practice common in China, Woodward's Chinese subsidiary accepts from Chinese customers, in settlement of certain customer accounts receivable, bankers' acceptance notes issued by creditworthy Chinese banks. Bankers' acceptance notes are financial instruments issued by Chinese financial institutions as part of financing arrangements between the financial institution and a customer of the financial institution. Bankers' acceptance notes represent a commitment by the issuing financial institution to pay a certain amount of money at a specified future maturity date to the legal owner of the banker's acceptance note as of the maturity date. The maturity date of bankers' acceptance notes varies, but it is Woodward's policy to accept only bankers' acceptance notes with maturity dates no more than 180 days from the date of Woodward's receipt of such draft. The issuing financial institution is the obligor, not Woodward's customers. Upon Woodward's acceptance of a banker's acceptance note from a customer, such customer has no further obligation to pay Woodward for the related accounts receivable balance. Woodward only accepts bankers' acceptance notes issued by creditworthy banks as to which the credit risk associated with the bankers' acceptance notes is assessed to be minimal.

The composition of Woodward's accounts receivable at June 30, 2016 and September 30, 2015 follows:

	June 30, 2016	September 30, 2015
Accounts receivable from:		
Customers	$ 285,091	$ 323,137
Other (Chinese financial institutions)	8,888	2,919
Allowance for uncollectible customer amounts	(2,798)	(3,841)
	$ 291,181	$ 322,215

Note 9. Inventories

	June 30, 2016	September 30, 2015
Raw materials	$ 62,208	$ 63,896
Work in progress	116,748	91,501
Component parts (1)	266,124	248,047

Finished goods	54,963	44,220
	$ 500,043	$ 447,664

(1) Component parts include items that can be sold separately as finished goods or included in the manufacture of other products.

Note 10. Property, plant, and equipment

	June 30, 2016	September 30, 2015
Land and land improvements	$ 87,466	$ 79,311
Buildings and building improvements	523,238	372,160
Leasehold improvements	14,018	16,907
Machinery and production equipment	417,435	365,040
Computer equipment and software	112,273	118,154
Office furniture and equipment	25,517	20,939
Other	18,371	18,325
Construction in progress	138,798	252,763
	1,337,116	1,243,599
Less accumulated depreciation	(492,661)	(487,499)
Property, plant and equipment, net	$ 844,455	$ 756,100

Included in "Land and land improvements" and "Buildings and improvements" are assets held for sale of $681 at September 30, 2015 related to Woodward's Industrial segment. The sale of these assets was completed on April 15, 2016.

Included in "Office furniture and equipment" and "Other" is $1,626 of gross assets acquired on capital leases.

In fiscal year 2015, Woodward completed and placed into service a manufacturing and office building on a second campus in the greater-Rockford, Illinois area and has occupied the new facility in anticipation of beginning serial production of new narrow-body product lines beginning in fiscal year 2017 for its Aerospace segment. This campus is intended to support Woodward's expected growth in its Aerospace segment over the next ten years and beyond, required as a result of Woodward being awarded a substantial number of new system platforms, particularly on narrow-body aircraft. Included in "Construction in progress" are costs of $66,695 at June 30, 2016 and $47,629 at September 30, 2015, associated with new equipment purchases for the second campus including capitalized interest of $1,469 at June 30, 2016 and $499 at September 30, 2015.

During the first nine-months of fiscal year 2016, Woodward completed and placed into service a new campus at its corporate headquarters in Fort Collins, Colorado to support the future growth of its Industrial segment by supplementing its existing Colorado manufacturing facilities and corporate headquarters. Woodward began occupying the new campus during its second quarter of fiscal year 2016. Approximately $158,000 of assets were placed in service during the six-months ended June 30, 2016, and were recorded to "Buildings and building improvements." Included in "Construction in progress" are $4,554 at June 30, 2016 and $151,669 at September 30, 2015, associated with the construction of the new campus and related new equipment purchases, including capitalized interest of $284 at June 30, 2016 and $5,205 at September 30, 2015.

Concurrent with and in relation to Woodward's significant investment in three new campuses and related equipment in the greater-Rockford, Illinois area, its corporate headquarters in Fort Collins, Colorado (both discussed above), and a new campus in Niles, Illinois (that was completed in fiscal year 2015), Woodward initiated a comprehensive review of its depreciation lives as required by U.S. GAAP to evaluate the estimates of the useful lives of Woodward assets. This review resulted in estimates of the useful lives of both existing and new assets generally in excess of those utilized prior to fiscal year 2016. The revised estimates will be used in fiscal year 2016 and going forward and result in a downward adjustment of depreciation on existing assets of approximately $12,000 for fiscal year 2016.

For the three and nine-months ended June 30, 2016 and June 30, 2015, Woodward had depreciation expense as follows:

	Three-Months Ended June 30,		Nine-Months Ended June 30,	
	2016	2015	2016	2015
Depreciation expense	$ 10,413	$ 11,280	$ 29,162	$ 33,727

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For the three and nine-months ended June 30, 2016 and June 30, 2015, Woodward capitalized interest that would have otherwise been included in interest expense of the following:

	Three-Months Ended June 30,		Nine-Months Ended June 30,	
	2016	2015	2016	2015
Capitalized interest	$ 914	$ 2,544	$ 5,054	$ 7,310

Note 11. Goodwill

	September 30, 2015	Effects of Foreign Currency Translation	June 30, 2016
Aerospace	$ 455,423	$ -	$ 455,423
Industrial	101,554	(1,447)	100,107
Consolidated	$ 556,977	$ (1,447)	$ 555,530

Woodward tests goodwill for impairment at the reporting unit level on an annual basis and more often if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. Woodward completed its annual goodwill impairment test as of July 31, 2015 during the quarter ended September 30, 2015. At that date, Woodward determined it was appropriate to aggregate certain components of the same operating segment into a single reporting unit. The fair value of each of Woodward's reporting units was determined using a discounted cash flow method. This method represents a level 3 input and incorporates various estimates and assumptions, the most significant being projected revenue growth rates, earnings margins, future tax rates, and the present value, based on an estimated weighted-average cost of capital (or the discount rate) and terminal growth rate, of forecasted cash flows. Management projects revenue growth rates, earnings margins and cash flows based on each reporting unit's current operational results, expected performance and operational strategies over a ten-year period. These projections are adjusted to reflect current economic conditions and demand for certain products, and require considerable management judgment.

Forecasted cash flows used in the July 31, 2015 impairment test were discounted using weighted-average cost of capital assumptions ranging from 9.49% to 12.83%. The terminal values of the forecasted cash flows were calculated using the Gordon Growth Model and assumed an annual compound growth rate after ten years of 4.03%. These inputs, which are unobservable in the market, represent management's best estimate of what market participants would use in determining the present value of the Company's forecasted cash flows. Changes in these estimates and assumptions can have a significant impact on the fair value of forecasted cash flows. Woodward evaluated the reasonableness of the reporting units' resulting fair values utilizing a market multiple method.

The results of Woodward's goodwill impairment tests performed as of July 31, 2015 did not indicate impairment of any of Woodward's reporting units.

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Note 12. Intangible assets, net

	June 30, 2016			September 30, 2015		
	Gross Carrying Value	Accumulated Amortization	Net Carrying Amount	Gross Carrying Value	Accumulated Amortization	Net Carrying Amount
Customer relationships and contracts:						
Aerospace	$ 282,225	$ (129,675)	$ 152,550	$ 282,225	$ (116,232)	$ 165,993
Industrial	40,906	(33,200)	7,706	41,409	(32,891)	8,518
Total	$ 323,131	$ (162,875)	$ 160,256	$ 323,634	$ (149,123)	$ 174,511
Intellectual property:						
Aerospace	$ -	$ -	$ -	$ -	$ -	$ -
Industrial	19,314	(17,644)	1,670	19,445	(16,921)	2,524
Total	$ 19,314	$ (17,644)	$ 1,670	$ 19,445	$ (16,921)	$ 2,524
Process technology:						
Aerospace	$ 76,605	$ (41,775)	$ 34,830	$ 76,605	$ (37,411)	$ 39,194
Industrial	22,864	(15,748)	7,116	22,924	(14,621)	8,303
Total	$ 99,469	$ (57,523)	$ 41,946	$ 99,529	$ (52,032)	$ 47,497
Other intangibles:						
Aerospace	$ -	$ -	$ -	$ 1,400	$ (1,300)	$ 100
Industrial	1,233	(795)	438	1,248	(742)	506
Total	$ 1,233	$ (795)	$ 438	$ 2,648	$ (2,042)	$ 606
Total intangibles:						
Aerospace	$ 358,830	$ (171,450)	$ 187,380	$ 360,230	$ (154,943)	$ 205,287
Industrial	84,317	(67,387)	16,930	85,026	(65,175)	19,851
Consolidated Total	$ 443,147	$ (238,837)	$ 204,310	$ 445,256	$ (220,118)	$ 225,138

For the three and nine-months ended June 30, 2016 and June 30, 2015, Woodward recorded amortization expense associated with intangibles of the following:

	Three-Months Ended June 30,		Nine-Months Ended June 30,	
	2016	2015	2016	2015
Amortization expense	$ 6,887	$ 7,224	$ 20,759	$ 22,026

Future amortization expense associated with intangibles is expected to be:

Year Ending September 30:	
2016 (remaining)	$ 6,725
2017	25,788
2018	24,965
2019	23,129
2020	20,354
Thereafter	103,349