

TEXTRON INC
Form 10-Q
April 28, 2016
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

(Mark One)

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

For the quarterly period ended April 2, 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 1-5480

Textron Inc.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

05-0315468

(I.R.S. Employer Identification No.)

40 Westminster Street, Providence, RI

(Address of principal executive offices)

02903

(Zip code)

Edgar Filing: TEXTRON INC - Form 10-Q

(401) 421-2800

(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 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 (Check one):

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 Act). Yes No

As of April 15, 2016, there were 268,831,736 shares of common stock outstanding.

Table of Contents

TEXTRON INC.

Index to Form 10-Q

For the Quarterly Period Ended April 2, 2016

	Page
<u>PART I. FINANCIAL INFORMATION</u>	
<u>Item 1. Financial Statements</u>	
<u>Consolidated Statements of Operations (Unaudited)</u>	3
<u>Consolidated Statements of Comprehensive Income (Unaudited)</u>	4
<u>Consolidated Balance Sheets (Unaudited)</u>	5
<u>Consolidated Statements of Cash Flows (Unaudited)</u>	6
<u>Notes to the Consolidated Financial Statements (Unaudited)</u>	
<u>Note 1. Basis of Presentation</u>	8
<u>Note 2. Business Acquisitions</u>	9
<u>Note 3. Retirement Plans</u>	9
<u>Note 4. Share-Based Compensation</u>	9
<u>Note 5. Earnings Per Share</u>	11
<u>Note 6. Accounts Receivable and Finance Receivables</u>	11
<u>Note 7. Inventories</u>	13
<u>Note 8. Accrued Liabilities</u>	13
<u>Note 9. Debt</u>	13
<u>Note 10. Derivative Instruments and Fair Value Measurements</u>	14
<u>Note 11. Accumulated Other Comprehensive Loss and Other Comprehensive Income (Loss)</u>	15
<u>Note 12. Commitments and Contingencies</u>	15
<u>Note 13. Segment Information</u>	16
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	17
<u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u>	25
<u>Item 4. Controls and Procedures</u>	25
<u>PART II. OTHER INFORMATION</u>	
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	25
<u>Item 5. Other Information</u>	26
<u>Item 6. Exhibits</u>	27
<u>Signatures</u>	27

Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. FINANCIAL STATEMENTS****TEXTRON INC.
Consolidated Statements of Operations (Unaudited)**

	Three Months Ended	
	April 2, 2016	April 4, 2015
<i>(In millions, except per share amounts)</i>		
Revenues		
Manufacturing revenues	\$ 3,181	\$ 3,051
Finance revenues	20	22
Total revenues	3,201	3,073
Costs and expenses		
Cost of sales	2,635	2,509
Selling and administrative expense	308	337
Interest expense	43	43
Total costs and expenses	2,986	2,889
Income from continuing operations before income taxes	215	184
Income tax expense	64	56
Income from continuing operations	151	128
Loss from discontinued operations, net of income taxes	(1)	
Net income	\$ 150	\$ 128
Basic earnings per share		
Continuing operations	\$ 0.55	\$ 0.46
Discontinued operations		
Basic earnings per share	\$ 0.55	\$ 0.46
Diluted earnings per share		
Continuing operations	\$ 0.55	\$ 0.46
Discontinued operations		
Diluted earnings per share	\$ 0.55	\$ 0.46
Dividends per share		
Common stock	\$ 0.02	\$ 0.02

See Notes to the Consolidated Financial Statements.

Table of Contents

TEXTRON INC.

Consolidated Statements of Comprehensive Income (Unaudited)

	Three Months Ended	
	April 2, 2016	April 4, 2015
<i>(In millions)</i>		
Net income	\$ 150	\$ 128
Other comprehensive income (loss), net of tax:		
Pension and postretirement benefits adjustments, net of reclassifications	21	24
Deferred gains (losses) on hedge contracts, net of reclassifications	21	(12)
Foreign currency translation adjustments	24	(56)
Other comprehensive income (loss)	66	(44)
Comprehensive income	\$ 216	\$ 84

See Notes to the Consolidated Financial Statements.

Table of Contents

TEXTRON INC.

Consolidated Balance Sheets (Unaudited)

<i>(Dollars in millions)</i>	April 2, 2016	January 2, 2016
Assets		
Manufacturing group		
Cash and equivalents	\$ 723	\$ 946
Accounts receivable, net	1,209	1,047
Inventories	4,477	4,144
Other current assets	328	341
Total current assets	6,737	6,478
Property, plant and equipment, less accumulated depreciation and amortization of \$4,015 and \$3,915	2,560	2,492
Goodwill	2,114	2,023
Other assets	2,397	2,399
Total Manufacturing group assets	13,808	13,392
Finance group		
Cash and equivalents	55	59
Finance receivables, net	1,066	1,087
Other assets	170	170
Total Finance group assets	1,291	1,316
Total assets	\$ 15,099	\$ 14,708
Liabilities and shareholders equity		
Liabilities		
Manufacturing group		
Short-term debt and current portion of long-term debt	\$ 309	\$ 262
Accounts payable	1,227	1,063
Accrued liabilities	2,341	2,467
Total current liabilities	3,877	3,792
Other liabilities	2,320	2,376
Long-term debt	2,800	2,435
Total Manufacturing group liabilities	8,997	8,603
Finance group		
Other liabilities	225	228
Debt	888	913
Total Finance group liabilities	1,113	1,141
Total liabilities	10,110	9,744
Shareholders equity		
Common stock	36	36
Capital surplus	1,617	1,587
Treasury stock	(774)	(559)
Retained earnings	5,442	5,298
Accumulated other comprehensive loss	(1,332)	(1,398)
Total shareholders equity	4,989	4,964
Total liabilities and shareholders equity	\$ 15,099	\$ 14,708
Common shares outstanding (in thousands)	268,721	274,228

See Notes to the Consolidated Financial Statements.

Table of Contents**TEXTRON INC.****Consolidated Statements of Cash Flows (Unaudited)**

For the Three Months Ended April 2, 2016 and April 4, 2015, respectively

<i>(In millions)</i>	Consolidated 2016	2015
Cash flows from operating activities		
Net income	\$ 150	\$ 128
Less: Loss from discontinued operations	(1)	
Income from continuing operations	151	128
Adjustments to reconcile income from continuing operations to net cash used in operating activities:		
Non-cash items:		
Depreciation and amortization	109	110
Deferred income taxes	19	(7)
Other, net	30	32
Changes in assets and liabilities:		
Accounts receivable, net	(143)	(115)
Inventories	(313)	(327)
Other assets	61	(45)
Accounts payable	147	127
Accrued and other liabilities	(230)	(63)
Income taxes, net	17	95
Pension, net	7	17
Captive finance receivables, net	(4)	31
Other operating activities, net	(1)	(2)
Net cash used in operating activities of continuing operations	(150)	(19)
Net cash used in operating activities of discontinued operations		(2)
Net cash used in operating activities	(150)	(21)
Cash flows from investing activities		
Net cash used in acquisitions	(164)	(32)
Capital expenditures	(88)	(79)
Finance receivables repaid	17	31
Other investing activities, net	10	23
Net cash used in investing activities	(225)	(57)
Cash flows from financing activities		
Proceeds from long-term debt	362	9
Increase in short-term debt	42	25
Principal payments on long-term debt and nonrecourse debt	(46)	(70)
Purchases of Textron common stock	(215)	
Dividends paid	(6)	(6)
Other financing activities, net	7	11
Net cash provided by (used in) financing activities	144	(31)
Effect of exchange rate changes on cash and equivalents	4	(5)
Net decrease in cash and equivalents	(227)	(114)
Cash and equivalents at beginning of period	1,005	822
Cash and equivalents at end of period	\$ 778	\$ 708

See Notes to the Consolidated Financial Statements.

Table of Contents**TEXTRON INC.****Consolidated Statements of Cash Flows (Unaudited) (Continued)**

For the Three Months Ended April 2, 2016 and April 4, 2015, respectively

<i>(In millions)</i>	Manufacturing Group		Finance Group	
	2016	2015	2016	2015
Cash flows from operating activities				
Net income	\$ 147	\$ 124	\$ 3	\$ 4
Less: Loss from discontinued operations	(1)			
Income from continuing operations	148	124	3	4
Adjustments to reconcile income from continuing operations to net cash provided by (used in) operating activities:				
Non-cash items:				
Depreciation and amortization	106	108	3	2
Deferred income taxes	17	(3)	2	(4)
Other, net	29	28	1	4
Changes in assets and liabilities:				
Accounts receivable, net	(143)	(115)		
Inventories	(313)	(327)		
Other assets	62	(51)	(1)	6
Accounts payable	147	127		
Accrued and other liabilities	(223)	(54)	(7)	(9)
Income taxes, net	16	81	1	14
Pension, net	7	17		
Other operating activities, net	(1)	(2)		
Net cash provided by (used in) operating activities of continuing operations	(148)	(67)	2	17
Net cash used in operating activities of discontinued operations		(2)		
Net cash provided by (used in) operating activities	(148)	(69)	2	17
Cash flows from investing activities				
Net cash used in acquisitions	(164)	(32)		
Capital expenditures	(88)	(79)		
Finance receivables repaid			68	112
Finance receivables originated			(55)	(50)
Other investing activities, net		(6)	10	29
Net cash provided by (used in) investing activities	(252)	(117)	23	91
Cash flows from financing activities				
Proceeds from long-term debt	345		17	9
Increase in short-term debt	42	25		
Principal payments on long-term debt and nonrecourse debt			(46)	(70)
Purchases of Textron common stock	(215)			
Dividends paid	(6)	(6)		
Other financing activities, net	7	2		9
Net cash provided by (used in) financing activities	173	21	(29)	(52)
Effect of exchange rate changes on cash and equivalents	4	(5)		
Net increase (decrease) in cash and equivalents	(223)	(170)	(4)	56
Cash and equivalents at beginning of period	946	731	59	91
Cash and equivalents at end of period	\$ 723	\$ 561	\$ 55	\$ 147

See Notes to the Consolidated Financial Statements.

Table of Contents

TEXTRON INC.

Notes to the Consolidated Financial Statements (Unaudited)

Note 1. Basis of Presentation

Our Consolidated Financial Statements include the accounts of Textron Inc. (Textron) and its majority-owned subsidiaries. We have prepared these unaudited consolidated financial statements in accordance with accounting principles generally accepted in the U.S. for interim financial information. Accordingly, these interim financial statements do not include all of the information and footnotes required by accounting principles generally accepted in the U.S. for complete financial statements. The consolidated interim financial statements included in this quarterly report should be read in conjunction with the consolidated financial statements included in our Annual Report on Form 10-K for the year ended January 2, 2016. In the opinion of management, the interim financial statements reflect all adjustments (consisting only of normal recurring adjustments) that are necessary for the fair presentation of our consolidated financial position, results of operations and cash flows for the interim periods presented. The results of operations for the interim periods are not necessarily indicative of the results to be expected for the full year.

Our financings are conducted through two separate borrowing groups. The Manufacturing group consists of Textron consolidated with its majority-owned subsidiaries that operate in the Textron Aviation, Bell, Textron Systems and Industrial segments. The Finance group, which also is the Finance segment, consists of Textron Financial Corporation and its consolidated subsidiaries. We designed this framework to enhance our borrowing power by separating the Finance group. Our Manufacturing group operations include the development, production and delivery of tangible goods and services, while our Finance group provides financial services. Due to the fundamental differences between each borrowing group's activities, investors, rating agencies and analysts use different measures to evaluate each group's performance. To support those evaluations, we present balance sheet and cash flow information for each borrowing group within the Consolidated Financial Statements. All significant intercompany transactions are eliminated from the Consolidated Financial Statements, including retail financing activities for inventory sold by our Manufacturing group and financed by our Finance group.

Use of Estimates

We prepare our financial statements in conformity with generally accepted accounting principles, which require us to make estimates and assumptions that affect the amounts reported in the financial statements. Actual results could differ from those estimates. Our estimates and assumptions are reviewed periodically, and the effects of changes, if any, are reflected in the Consolidated Statements of Operations in the period that they are determined.

During 2016 and 2015, we changed our estimates of revenues and costs on certain long-term contracts that are accounted for under the percentage-of-completion method of accounting. These changes in estimates increased income from continuing operations before income taxes in the first quarter of 2016 and 2015 by \$29 million and \$18 million, respectively, (\$19 million and \$11 million after tax, or \$0.07 and \$0.04 per diluted share, respectively). For the first quarter of 2016 and 2015, the gross favorable program profit adjustments totaled \$34 million and \$33 million, respectively, and the gross unfavorable program profit adjustments totaled \$5 million and \$15 million, respectively.

New Accounting Pronouncements

Edgar Filing: TEXTRON INC - Form 10-Q

In February 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-02, *Leases*, that requires all leases with a term greater than 12 months be recognized on the balance sheet, while lease expenses would continue to be recognized in the statement of operations in a manner similar to current accounting guidance. The new standard is effective for our company at the beginning of fiscal 2019 and early adoption is permitted. Entities must adopt the standard on a modified retrospective basis whereby it would be applied at the beginning of the earliest comparative year. We are currently evaluating the impact of adoption on our consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers*, that outlines a comprehensive five-step revenue recognition model based on the principle that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. In July 2015, the FASB approved a one-year deferral of the effective date of the standard to the beginning of 2018 for public companies, with an option that would permit companies to adopt the standard as early as the original effective date of 2017. The new standard may be adopted either retrospectively or on a modified retrospective basis whereby it would be applied to new contracts and existing contracts with remaining performance obligations as of the effective date, with a cumulative catch-up adjustment recorded to beginning retained earnings at the effective date for those contracts. We are currently evaluating the impacts of adoption on our consolidated financial position, results of operations and related disclosures, along with the implementation approach to be used.

Table of Contents**Note 2. Business Acquisitions**

In the first quarter of 2016, we paid \$164 million in cash and assumed debt of \$19 million to acquire four businesses, net of cash acquired and holdbacks. Our acquisition of Able Engineering and Component Services, Inc. and Able Aerospace, Inc. (Able) represented the largest of these businesses and is included in the Textron Aviation segment. Able is an industry-leading repair and overhaul business that provides component repairs, component exchanges and replacement parts, among other support and service offerings for commercial rotorcraft and fixed-wing aircraft customers around the world. We are in the process of allocating the purchase price and valuing the acquired assets and liabilities for these acquisitions. Based on the preliminary allocation of the aggregate purchase price for these acquisitions, \$87 million has been allocated to goodwill, related to expected synergies and the value of the existing workforce, and \$59 million to intangible assets. Of the recorded goodwill, approximately \$33 million is deductible for tax purposes. The intangible assets are primarily related to customer relationships and technologies, which will be amortized over 10 to 18 years. The operating results of these acquisitions have been included in the Consolidated Statements of Operations since their respective closing dates.

Note 3. Retirement Plans

We provide defined benefit pension plans and other postretirement benefits to eligible employees. The components of net periodic benefit cost (credit) for these plans are as follows:

	Pension Benefits		Postretirement Benefits Other Than Pensions	
	April 2, 2016	April 4, 2015	April 2, 2016	April 4, 2015
<i>(In millions)</i>				
Three Months Ended				
Interest cost	\$ 85	\$ 81	\$ 4	\$ 4
Service cost	24	30	1	1
Expected return on plan assets	(123)	(121)		
Amortization of net actuarial loss	26	39		
Amortization of prior service cost (credit)	4	4	(6)	(6)
Net periodic benefit cost (credit)	\$ 16	\$ 33	\$ (1)	\$ (1)

Note 4. Share-Based Compensation

Our share-based compensation plans provide stock options, restricted stock, restricted stock units, stock appreciation rights, performance stock, performance share units and other awards. Compensation expense included in net income for these plans is as follows:

	Three Months Ended	
	April 2, 2016	April 4, 2015
<i>(In millions)</i>		
Compensation expense	\$ 7	\$ 31
Income tax benefit	(3)	(11)
Total net compensation expense included in net income	\$ 4	\$ 20

Stock Options

Edgar Filing: TEXTRON INC - Form 10-Q

Options to purchase our shares have a maximum term of ten years and generally vest ratably over a three-year period. The stock option compensation cost calculated under the fair value approach is recognized over the vesting period of the stock options. We estimate the fair value of options granted on the date of grant using the Black-Scholes option-pricing model. Expected volatilities are based on implied volatilities from traded options on our common stock, historical volatilities and other factors. The expected term is based on historical option exercise data, which is adjusted to reflect any anticipated changes in expected behavior.

The weighted-average fair value of options granted and the assumptions used in our option-pricing model for such grants are as follows:

		Three Months Ended	
		April 2, 2016	April 4, 2015
Fair value of options at grant date	\$	10.33	\$ 14.03
Dividend yield		0.2%	0.2%
Expected volatility		33.6%	34.9%
Risk-free interest rate		1.2%	1.5%
Expected term (in years)		4.8	4.8

Table of Contents

The stock option activity during the first quarter of 2016 is provided below:

<i>(Options in thousands)</i>	Number of Options		Weighted- Average Exercise Price
Outstanding at beginning of period	8,808	\$	32.91
Granted	1,792		34.50
Exercised	(114)		(25.97)
Forfeited or expired	(48)		(41.94)
Outstanding at end of period	10,438	\$	33.21
Exercisable at end of period	6,780	\$	30.24

At April 2, 2016, our outstanding options had an aggregate intrinsic value of \$57 million and a weighted-average remaining contractual life of seven years. Our exercisable options had an aggregate intrinsic value of \$53 million and a weighted-average remaining contractual life of six years at April 2, 2016. The total intrinsic value of options exercised was \$1 million and \$8 million during the first quarter of 2016 and 2015, respectively.

Restricted Stock Units

The activity for restricted stock units payable in both stock and cash during the first quarter of 2016 is provided below:

<i>(Shares/Units in thousands)</i>	Units Payable in Stock		Units Payable in Cash	
	Number of Shares	Weighted- Average Grant Date Fair Value	Number of Units	Weighted- Average Grant Date Fair Value
Outstanding at beginning of period, nonvested	880	\$ 33.97	1,492	\$ 34.84
Granted	189	34.50	397	34.50
Vested	(196)	(27.53)	(334)	(27.73)
Forfeited			(36)	(38.99)
Outstanding at end of period, nonvested	873	\$ 35.54	1,519	\$ 36.21

The fair value of the restricted stock awards that vested and/or amounts paid under these awards is as follows:

<i>(In millions)</i>	Three Months Ended	
	April 2, 2016	April 4, 2015
Fair value of awards vested	\$ 17	\$ 22
Cash paid	12	18

Performance Share Units

The activity for our performance share units during the first quarter of 2016 is provided below:

<i>(Units in thousands)</i>	Number of Units	Weighted- Average Grant Date
-----------------------------	----------------------------	---

Edgar Filing: TEXTRON INC - Form 10-Q

		Fair Value
Outstanding at beginning of period, nonvested	549 \$	41.84
Granted	284	34.50
Forfeited	(9)	(39.56)
Outstanding at end of period, nonvested	824 \$	39.33

Cash paid under these awards totaled \$13 million and \$17 million during the first quarter of 2016 and 2015, respectively.

Table of Contents**Note 5. Earnings Per Share**

We calculate basic and diluted earnings per share (EPS) based on net income, which approximates income available to common shareholders for each period. Basic EPS is calculated using the two-class method, which includes the weighted-average number of common shares outstanding during the period and restricted stock units to be paid in stock that are deemed participating securities as they provide nonforfeitable rights to dividends. Diluted EPS considers the dilutive effect of all potential future common stock, including stock options.

The weighted-average shares outstanding for basic and diluted EPS are as follows:

	Three Months Ended	
	April 2,	April 4,
<i>(In thousands)</i>	2016	2015
Basic weighted-average shares outstanding	271,660	277,902
Dilutive effect of stock options	1,362	2,175
Diluted weighted-average shares outstanding	273,022	280,077

Stock options to purchase 4 million and 1 million shares of common stock outstanding are excluded from the calculation of diluted weighted average shares outstanding for the first quarter of 2016 and 2015, respectively, as their effect would have been anti-dilutive.

Note 6. Accounts Receivable and Finance Receivables**Accounts Receivable**

Accounts receivable is composed of the following:

	April 2,		January 2,
	2016	2016	2016
<i>(In millions)</i>			
Commercial	\$ 914	\$	841
U.S. Government contracts	327		239
	1,241		1,080
Allowance for doubtful accounts	(32)		(33)
Total	\$ 1,209	\$	1,047

We have unbillable receivables, primarily on U.S. Government contracts, that arise when the revenues we have appropriately recognized based on performance cannot be billed yet under terms of the contract. Unbillable receivables within accounts receivable totaled \$196 million at April 2, 2016 and \$135 million at January 2, 2016.

Finance Receivables

Finance receivables are presented in the following table:

<i>(In millions)</i>		April 2,		January 2,
		2016		2016
Finance receivables*	\$	1,114	\$	1,135
Allowance for losses		(48)		(48)
Total finance receivables, net	\$	1,066	\$	1,087

* Includes finance receivables held for sale of \$30 million at both April 2, 2016 and January 2, 2016.

Credit Quality Indicators and Nonaccrual Finance Receivables

We internally assess the quality of our finance receivables based on a number of key credit quality indicators and statistics such as delinquency, loan balance to estimated collateral value and the financial strength of individual borrowers and guarantors. Because many of these indicators are difficult to apply across an entire class of receivables, we evaluate individual loans on a quarterly basis and classify these loans into three categories based on the key credit quality indicators for the individual loan. These three categories are performing, watchlist and nonaccrual.

We classify finance receivables as nonaccrual if credit quality indicators suggest full collection of principal and interest is doubtful, we automatically classify accounts as nonaccrual once they are contractually delinquent by more than three months unless collection of principal and interest is not doubtful. Accrual of interest income is suspended for these accounts and all cash collections are generally applied to reduce the net investment balance. Once we conclude that the collection of all principal and interest is no longer doubtful, we resume the accrual of interest and recognize previously suspended interest income at the time either a) the loan becomes contractually current through payment according to the original terms of the loan, or b) if the loan has been modified, following a period of performance under the terms of the modification. Accounts are classified as watchlist when credit quality indicators have deteriorated as compared with typical underwriting criteria, and we believe collection of full

Table of Contents

principal and interest is probable but not certain. All other finance receivables that do not meet the watchlist or nonaccrual categories are classified as performing.

Delinquency

We measure delinquency based on the contractual payment terms of our finance receivables. In determining the delinquency aging category of an account, any/all principal and interest received is applied to the most past-due principal and/or interest amounts due. If a significant portion of the contractually due payment is delinquent, the entire finance receivable balance is reported in accordance with the most past-due delinquency aging category.

Finance receivables categorized based on the credit quality indicators and by the delinquency aging category are summarized as follows:

<i>(In millions)</i>	April 2, 2016	January 2, 2016
Performing	\$ 866	\$ 891
Watchlist	139	130
Nonaccrual	79	84
Nonaccrual as a percentage of finance receivables	7.29%	7.60%
Less than 31 days past due	\$ 934	\$ 950
31-60 days past due	56	86
61-90 days past due	69	42
Over 90 days past due	25	27
60 + days contractual delinquency as a percentage of finance receivables	8.67%	6.24%

Impaired Loans

On a quarterly basis, we evaluate individual finance receivables for impairment in non-homogeneous portfolios and larger balance accounts in homogeneous loan portfolios. A finance receivable is considered impaired when it is probable that we will be unable to collect all amounts due according to the contractual terms of the loan agreement based on our review of the credit quality indicators described above. Impaired finance receivables include both nonaccrual accounts and accounts for which full collection of principal and interest remains probable, but the account's original terms have been, or are expected to be, significantly modified. If the modification specifies an interest rate equal to or greater than a market rate for a finance receivable with comparable risk, the account is not considered impaired in years subsequent to the modification. Interest income recognized on impaired loans was not significant in the first quarter of 2016 or 2015.

A summary of impaired finance receivables, excluding leveraged leases, and the average recorded investment is provided below:

<i>(In millions)</i>	April 2, 2016	January 2, 2016
Recorded investment:		
Impaired loans with related allowance for losses	\$ 54	\$ 62
Impaired loans with no related allowance for losses	25	42

Edgar Filing: TEXTRON INC - Form 10-Q

Total	\$	79	\$	104
Unpaid principal balance	\$	88	\$	113
Allowance for losses on impaired loans		15		17
Average recorded investment		92		102

A summary of the allowance for losses on finance receivables, based on how the underlying finance receivables are evaluated for impairment, is provided below. The finance receivables reported in this table specifically exclude leveraged leases in accordance with U.S. generally accepted accounting principles.

<i>(In millions)</i>		April 2, 2016		January 2, 2016
Allowance based on collective evaluation	\$	33	\$	31
Allowance based on individual evaluation		15		17
Finance receivables evaluated collectively	\$	902	\$	883
Finance receivables evaluated individually		79		104

Allowance for Losses

We maintain an allowance for losses on finance receivables at a level considered adequate to cover inherent losses in the portfolio based on management's evaluation. For larger balance accounts specifically identified as impaired, a reserve is established based on comparing the expected future cash flows, discounted at the finance receivable's effective interest rate, or the fair value of the underlying collateral if the finance receivable is collateral dependent, to its carrying amount. The expected future cash flows

Table of Contents

consider collateral value; financial performance and liquidity of our borrower; existence and financial strength of guarantors; estimated recovery costs, including legal expenses; and costs associated with the repossession and eventual disposal of collateral. When there is a range of potential outcomes, we perform multiple discounted cash flow analyses and weight the potential outcomes based on their relative likelihood of occurrence. The evaluation of our portfolio is inherently subjective, as it requires estimates, including the amount and timing of future cash flows expected to be received on impaired finance receivables and the estimated fair value of the underlying collateral, which may differ from actual results. While our analysis is specific to each individual account, critical factors included in this analysis include industry valuation guides, age and physical condition of the collateral, payment history and existence and financial strength of guarantors.

We also establish an allowance for losses to cover probable but specifically unknown losses existing in the portfolio. This allowance is established as a percentage of non-recourse finance receivables, which have not been identified as requiring specific reserves. The percentage is based on a combination of factors, including historical loss experience, current delinquency and default trends, collateral values and both general economic and specific industry trends. Finance receivables are charged off at the earlier of the date the collateral is repossessed or when no payment has been received for six months, unless management deems the receivable collectible.

A rollforward of the allowance for losses on finance receivables is provided below:

	Three Months Ended	
	April 2, 2016	April 4, 2015
<i>(In millions)</i>		
Beginning of period	\$ 48	\$ 51
Provision for losses		1
Charge-offs	(3)	
Recoveries	3	1
End of period	\$ 48	\$ 53

Note 7. Inventories

Inventories are composed of the following:

	April 2, 2016	January 2, 2016
<i>(In millions)</i>		
Finished goods	\$ 1,907	\$ 1,735
Work in process	2,973	2,921
Raw materials and components	633	605
Progress/milestone payments	5,513	5,261
Total	(1,036)	(1,117)
	\$ 4,477	\$ 4,144

Note 8. Accrued Liabilities

Edgar Filing: TEXTRON INC - Form 10-Q

Changes in our warranty liability are as follows:

	Three Months Ended	
	April 2, 2016	April 4, 2015
<i>(In millions)</i>		
Beginning of period	\$ 143	\$ 148
Provision	16	16
Settlements	(16)	(17)
Acquisitions	1	4
Adjustments*	(6)	
End of period	\$ 138	\$ 151

* Adjustments include changes to prior year estimates, new issues on prior year sales and currency translation adjustments.

Note 9. Debt

Under our shelf registration statement, on March 11, 2016, we issued \$350 million of fixed-rate notes due March 15, 2026 that bear an annual interest rate of 4.0%. The net proceeds of the issuance totaled \$345 million, after deducting underwriting discounts, commissions and offering expenses.

Table of Contents

Note 10. Derivative Instruments and Fair Value Measurements

We measure fair value at the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. We prioritize the assumptions that market participants would use in pricing the asset or liability into a three-tier fair value hierarchy. This fair value hierarchy gives the highest priority (Level 1) to quoted prices in active markets for identical assets or liabilities and the lowest priority (Level 3) to unobservable inputs in which little or no market data exist, requiring companies to develop their own assumptions. Observable inputs that do not meet the criteria of Level 1, which include quoted prices for similar assets or liabilities in active markets or quoted prices for identical assets and liabilities in markets that are not active, are categorized as Level 2. Level 3 inputs are those that reflect our estimates about the assumptions market participants would use in pricing the asset or liability based on the best information available in the circumstances. Valuation techniques for assets and liabilities measured using Level 3 inputs may include methodologies such as the market approach, the income approach or the cost approach and may use unobservable inputs such as projections, estimates and management's interpretation of current market data. These unobservable inputs are utilized only to the extent that observable inputs are not available or cost effective to obtain.

Assets and Liabilities Recorded at Fair Value on a Recurring Basis

We manufacture and sell our products in a number of countries throughout the world, and, therefore, we are exposed to movements in foreign currency exchange rates. We utilize foreign currency exchange contracts to manage this volatility. Our foreign currency exchange contracts are measured at fair value using the market method valuation technique. The inputs to this technique utilize current foreign currency exchange forward market rates published by third-party leading financial news and data providers. These are observable data that represent the rates that the financial institution uses for contracts entered into at that date; however, they are not based on actual transactions so they are classified as Level 2. At April 2, 2016 and January 2, 2016, we had foreign currency exchange contracts with notional amounts upon which the contracts were based of \$776 million and \$706 million, respectively. At April 2, 2016, the fair value amounts of our foreign currency exchange contracts were not significant. At January 2, 2016, the fair value amounts of our foreign currency exchange contracts were a \$7 million asset and a \$28 million liability.

We primarily utilize forward exchange contracts which have maturities of no more than three years. These contracts qualify as cash flow hedges and are intended to offset the effect of exchange rate fluctuations on forecasted sales, inventory purchases and overhead expenses. At April 2, 2016, we had a net deferred loss of \$3 million in Accumulated other comprehensive loss related to these cash flow hedges. Net gains and losses recognized in earnings and Accumulated other comprehensive loss on cash flow hedges, including gains and losses related to hedge ineffectiveness, were not significant in the periods presented.

We hedge our net investment position in major currencies and generate foreign currency interest payments that offset other transactional exposures in these currencies. To accomplish this, we borrow directly in foreign currency and designate a portion of foreign currency debt as a hedge of a net investment. We record changes in the fair value of these contracts in other comprehensive income to the extent they are effective as cash flow hedges. Currency effects on the effective portion of these hedges, which are reflected in the foreign currency translation adjustments within Accumulated other comprehensive loss, were not significant in the periods presented.

Assets Recorded at Fair Value on a Nonrecurring Basis

During the periods ended April 2, 2016 and January 2, 2016, the Finance group's impaired nonaccrual finance receivables of \$39 million and \$45 million, respectively, were measured at fair value on a nonrecurring basis using significant unobservable inputs (Level 3). Impaired nonaccrual finance receivables represent assets recorded at fair value on a nonrecurring basis since the measurement of required reserves on our impaired finance receivables is significantly dependent on the fair value of the underlying collateral. For impaired nonaccrual finance receivables secured

Edgar Filing: TEXTRON INC - Form 10-Q

by aviation assets, the fair values of collateral are determined primarily based on the use of industry pricing guides. Fair value measurements recorded on impaired finance receivables were not significant for both the three months ended April 2, 2016 and April 4, 2015.

Assets and Liabilities Not Recorded at Fair Value

The carrying value and estimated fair value of our financial instruments that are not reflected in the financial statements at fair value are as follows:

<i>(In millions)</i>	April 2, 2016		January 2, 2016	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Manufacturing group				
Long-term debt, excluding leases	\$ (2,972)	\$ (3,127)	\$ (2,628)	\$ (2,744)
Finance group				
Finance receivables, excluding leases	860	834	863	820
Debt	(888)	(817)	(913)	(840)

Table of Contents

Fair value for the Manufacturing group debt is determined using market observable data for similar transactions (Level 2). At both April 2, 2016 and January 2, 2016, approximately 75% of the fair value of term debt for the Finance group was determined based on discounted cash flow analyses using observable market inputs from debt with similar duration, subordination and credit default expectations (Level 2). Fair value estimates for finance receivables were determined based on internally developed discounted cash flow models primarily utilizing significant unobservable inputs (Level 3), which include estimates of the rate of return, financing cost, capital structure and/or discount rate expectations of current market participants combined with estimated loan cash flows based on credit losses, payment rates and expectations of borrowers ability to make payments on a timely basis.

Note 11. Accumulated Other Comprehensive Loss and Other Comprehensive Income (Loss)

The components of Accumulated Other Comprehensive Loss are presented below:

<i>(In millions)</i>	Pension and Postretirement Benefits Adjustments	Deferred Gains (Losses) on Hedge Contracts	Foreign Currency Translation Adjustment	Accumulated Other Comprehensive Loss
For the three months ended April 2, 2016				
Beginning of the period	\$ (1,327)	\$ (24)	\$ (47)	\$ (1,398)
Other comprehensive income before reclassifications		16	24	40
Reclassified from Accumulated other comprehensive loss	21	5		26
Other comprehensive income	21	21	24	66
End of the period	\$ (1,306)	\$ (3)	\$ (23)	\$ (1,332)
For the three months ended April 4, 2015				
Beginning of the period	\$ (1,511)	\$ (13)	\$ 18	\$ (1,506)
Other comprehensive loss before reclassifications		(16)	(56)	(72)
Reclassified from Accumulated other comprehensive loss	24	4		28
Other comprehensive income (loss)	24	(12)	(56)	(44)
End of the period	\$ (1,487)	\$ (25)	\$ (38)	\$ (1,550)

The before and after-tax components of other comprehensive income (loss) are presented below:

<i>(In millions)</i>	April 2, 2016			April 4, 2015		
	Pre-Tax Amount	Tax (Expense) Benefit	After-Tax Amount	Pre-Tax Amount	Tax (Expense) Benefit	After-Tax Amount
Three Months Ended						
Pension and postretirement benefits adjustments:						
Amortization of net actuarial loss*	\$ 26	\$ (9)	\$ 17	\$ 39	\$ (14)	\$ 25
Amortization of prior service credit*	(2)	1	(1)	(2)	1	(1)
Unrealized gains	7	(2)	5			
Pension and postretirement benefits adjustments, net	31	(10)	21	37	(13)	24
Deferred gains (losses) on hedge contracts:						

Edgar Filing: TEXTRON INC - Form 10-Q

Current deferrals	22	(6)	16	(21)	5	(16)
Reclassification adjustments	7	(2)	5	6	(2)	4
Deferred gains (losses) on hedge contracts, net	29	(8)	21	(15)	3	(12)
Foreign currency translation adjustments	25	(1)	24	(52)	(4)	(56)
Total	\$ 85	\$ (19)	\$ 66	\$ (30)	\$ (14)	\$ (44)

**These components of other comprehensive income are included in the computation of net periodic pension cost. See Note 11 of our 2015 Annual Report on Form 10-K for additional information.*

Note 12. Commitments and Contingencies

We are subject to legal proceedings and other claims arising out of the conduct of our business, including proceedings and claims relating to commercial and financial transactions; government contracts; alleged lack of compliance with applicable laws and regulations; production partners; product liability; patent and trademark infringement; employment disputes; and environmental, safety and health matters. Some of these legal proceedings and claims seek damages, fines or penalties in substantial amounts or remediation of environmental contamination. As a government contractor, we are subject to audits, reviews and investigations to determine whether our operations are being conducted in accordance with applicable regulatory requirements. Under federal government procurement regulations, certain claims brought by the U.S. Government could result in our suspension or debarment from U.S. Government contracting for a period of time. On the basis of information presently available, we do not believe that existing proceedings and claims will have a material effect on our financial position or results of operations.

Table of Contents**Note 13. Segment Information**

We operate in, and report financial information for, the following five business segments: Textron Aviation, Bell, Textron Systems, Industrial and Finance. Segment profit is an important measure used for evaluating performance and for decision-making purposes. Segment profit for the manufacturing segments excludes interest expense and certain corporate expenses. The measurement for the Finance segment includes interest income and expense.

Our revenues by segment, along with a reconciliation of segment profit to income from continuing operations before income taxes, are as follows:

	Three Months Ended	
	April 2, 2016	April 4, 2015
<i>(In millions)</i>		
Revenues		
Textron Aviation	\$ 1,091	\$ 1,051
Bell	814	813
Textron Systems	324	315
Industrial	952	872
Finance	20	22
Total revenues	\$ 3,201	\$ 3,073
Segment Profit		
Textron Aviation	\$ 73	\$ 67
Bell	82	76
Textron Systems	29	28
Industrial	91	82
Finance	5	6
Segment profit	280	259
Corporate expenses and other, net	(32)	(42)
Interest expense, net for Manufacturing group	(33)	(33)
Income from continuing operations before income taxes	\$ 215	\$ 184

Table of Contents**Item 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS****Consolidated Results of Operations**

	Three Months Ended		% Change
	April 2, 2016	April 4, 2015	
<i>(Dollars in millions)</i>			
Revenues	\$ 3,201	\$ 3,073	4%
Operating expenses	2,943	2,846	3%
Cost of sales	2,635	2,509	5%
Selling and administrative expense	308	337	(9)%
Gross margin as a percentage of Manufacturing revenues	17.2%	17.8%	

An analysis of our consolidated operating results is set forth below. A more detailed analysis of our segments' operating results is provided in the Segment Analysis section on pages 17 to 21.

Revenues

Revenues increased \$128 million, 4%, in the first quarter of 2016, compared with the first quarter of 2015, largely driven by increases in the Industrial, Textron Aviation and Textron Systems segments.

- Higher Industrial revenues of \$80 million, primarily due to higher volume of \$62 million, largely in the Fuel Systems and Functional Components product line, and the impact from an acquired business of \$37 million.
- Higher Textron Aviation revenues of \$40 million, primarily due to higher Citation jet volume and mix.
- Higher Textron Systems revenues of \$9 million, primarily due to higher volume of \$46 million in the Unmanned Systems product line, partially offset by lower volume of \$42 million in the Weapons and Sensors product line.

Cost of Sales and Selling and Administrative Expense

Manufacturing cost of sales and selling and administrative expense together comprise our operating expenses. Cost of sales increased \$126 million, 5%, in the first quarter of 2016, compared with the first quarter of 2015, largely due to higher volume at the Industrial and Textron Aviation segments and an increase from acquired businesses.

Selling and administrative expense decreased \$29 million, 9%, in the first quarter of 2016, compared with the first quarter of 2015, primarily due to lower share-based compensation expense.

Backlog

<i>(In millions)</i>		April 2,		January 2,
		2016		2016
Bell	\$	5,284	\$	5,224
Textron Systems		2,524		2,328
Textron Aviation		1,027		1,074
Total backlog	\$	8,835	\$	8,626

Segment Analysis

We operate in, and report financial information for, the following five business segments: Textron Aviation, Bell, Textron Systems, Industrial and Finance. Segment profit is an important measure used for evaluating performance and for decision-making purposes. Segment profit for the manufacturing segments excludes interest expense and certain corporate expenses. The measurement for the Finance segment includes interest income and expense.

In our discussion of comparative results for the Manufacturing group, changes in revenue and segment profit typically are expressed for our commercial business in terms of volume, pricing, foreign exchange and acquisitions. Additionally, changes in segment profit may be expressed in terms of mix, inflation and cost performance. Volume changes in revenue represent increases/decreases in the number of units delivered or services provided. Pricing represents changes in unit pricing. Foreign exchange is the change resulting from translating foreign-denominated amounts into U.S. dollars at exchange rates that are different from the prior period. Revenues generated by acquired businesses are reflected in Acquisitions for a twelve-month period. For segment profit, mix represents a change due to the composition of products and/or services sold at different profit margins. Inflation represents higher material, wages, benefits, pension or other costs. Performance reflects an increase or decrease in research and development, depreciation, selling and administrative costs, warranty, product liability, quality/scrap, labor efficiency, overhead, product line profitability, start-up, ramp up and cost-reduction initiatives or other manufacturing inputs.

Table of Contents

Approximately 24% of our 2015 revenues were derived from contracts with the U.S. Government. For our segments that have significant contracts with the U.S. Government, we typically express changes in segment profit related to the government business in terms of volume, changes in program performance or changes in contract mix. Changes in volume that are described in net sales typically drive corresponding changes in our segment profit based on the profit rate for a particular contract. Changes in program performance typically relate to profit recognition associated with revisions to total estimated costs at completion that reflect improved or deteriorated operating performance or award fee rates. Changes in contract mix refers to changes in operating margin due to a change in the relative volume of contracts with higher or lower fee rates such that the overall average margin rate for the segment changes.

Textron Aviation

	Three Months Ended		April 4,
	April 2,	2015	
<i>(Dollars in millions)</i>			
Revenues	\$ 1,091	\$	1,051
Operating expenses			984
Segment profit			67
Profit margin			6.4%

Textron Aviation Revenues and Operating Expenses

The following factors contributed to the change in Textron Aviation's revenues from the prior year quarter:

		2016 versus
<i>(In millions)</i>		2015
Volume and mix	\$	32
Acquisitions		14
Other		(6)
Total change	\$	40

Textron Aviation's revenues increased \$40 million, 4%, in the first quarter of 2016, compared with the first quarter of 2015, primarily due to higher Citation jet volume and mix. We delivered 34 Citation jets and 26 King Air turboprops in the first quarter of 2016, compared with 33 Citation jets and 25 King Air turboprops in the first quarter of 2015. The portion of the segment's revenues derived from aftermarket sales and services represented 35% of its total revenues in both the first quarter of 2016 and 2015.

Textron Aviation's operating expenses increased \$34 million, 4%, in the first quarter of 2016, compared with the first quarter of 2015, primarily due to higher volume as described above.

Textron Aviation Segment Profit

The following factors contributed to the change in Textron Aviation's segment profit from the prior year quarter:

		2016 versus
<i>(In millions)</i>		2015
Performance	\$	7

Edgar Filing: TEXTRON INC - Form 10-Q

Volume and mix		2
Other		(3)
Total change	\$	6

Textron Aviation's segment profit increased \$6 million, 9%, in the first quarter of 2016, compared with the first quarter of 2015.

Table of Contents**Bell**

	Three Months Ended	
	April 2, 2016	April 4, 2015
<i>(Dollars in millions)</i>		
Revenues:		
V-22 program	\$ 278	\$ 296
Other military	253	218
Commercial	283	299
Total revenues	814	813
Operating expenses	732	737
Segment profit	82	76
Profit margin	10.1%	9.3%

Bell's major U.S. Government programs at this time are the V-22 tiltrotor aircraft and the H-1 helicopter platforms, which are both in the production stage and represent a significant portion of Bell's revenues from the U.S. Government.

Bell Revenues and Operating Expenses

Bell's revenues and operating expenses were largely unchanged in the first quarter of 2016, compared with the first quarter of 2015. Revenues were impacted by the following:

- \$35 million increase in other military, primarily resulting from higher H-1 program revenues, largely reflecting higher aircraft deliveries that were partially offset by lower product support. Bell delivered 10 H-1 aircraft in the first quarter of 2016, compared with 4 H-1 aircraft in the first quarter of 2015.
- \$18 million decrease in V-22 program revenues, primarily reflecting lower product support. Bell delivered 6 V-22 aircraft in both the first quarter of 2016 and 2015.
- \$16 million decrease in commercial revenues, primarily due to lower commercial aftermarket volume. Lower commercial aircraft deliveries were offset by a change in mix of commercial aircraft sold during the period. Bell delivered 30 commercial aircraft in the first quarter of 2016, compared with 35 commercial aircraft in the first quarter of 2015.

Bell Segment Profit

The following factors contributed to the change in Bell's segment profit from the prior year quarter:

	2016 versus	
<i>(In millions)</i>		2015
Performance	\$	13
Volume and mix		(7)
Total change	\$	6

Edgar Filing: TEXTRON INC - Form 10-Q

Bell's segment profit increased \$6 million, 8%, in the first quarter of 2016, compared with the first quarter of 2015, primarily due to improved performance, largely driven by favorable program adjustments.

Textron Systems

<i>(Dollars in millions)</i>		Three Months Ended	
		April 2, 2016	April 4, 2015
Revenues	\$	324	\$ 315
Operating expenses		295	287
Segment profit		29	28
Profit margin		9.0%	8.9%

Table of Contents**Textron Systems Revenues and Operating Expenses**

The following factors contributed to the change in Textron Systems revenues from the prior year quarter:

<i>(In millions)</i>	2016 versus	
		2015
Volume	\$	8
Other		1
Total change	\$	9

Revenues at Textron Systems increased \$9 million, 3%, in the first quarter of 2016, compared with the first quarter of 2015, primarily due to higher volume of \$46 million in the Unmanned Systems product line, partially offset by lower volume of \$42 million in the Weapons and Sensors product line.

Textron Systems operating expenses increased \$8 million, 3%, in the first quarter of 2016, compared with the first quarter of 2015, primarily driven by higher volume as described above.

Textron Systems Segment Profit

The following factors contributed to the change in Textron Systems segment profit from the prior year quarter:

<i>(In millions)</i>	2016 versus	
		2015
Performance	\$	4
Volume and mix		(3)
Total change	\$	1

Textron Systems segment profit was largely unchanged in the first quarter of 2016, compared with the first quarter of 2015.

Industrial

<i>(Dollars in millions)</i>	Three Months Ended	
	April 2, 2016	April 4, 2015
Revenues:		
Fuel Systems and Functional Components	\$ 580	\$ 513
Other Industrial	372	359

Total revenues	952	872
Operating expenses	861	790
Segment profit	91	82
Profit margin	9.6%	9.4%

Industrial Revenues and Operating Expenses

The following factors contributed to the change in Industrial s revenues from the prior year quarter:

<i>(In millions)</i>	2016 versus	2015
Volume	\$	62
Acquisitions		37
Foreign exchange		(14)
Other		(5)
Total change	\$	80

Industrial segment revenues increased \$80 million, 9%, in the first quarter of 2016, compared with the first quarter of 2015, primarily due to higher volume of \$62 million and the impact from an acquired business of \$37 million. Higher volume was primarily related to the Fuel Systems and Functional Components product line, largely reflecting automotive industry demand in Europe.

Operating expenses for the Industrial segment increased \$71 million, 9%, in the first quarter of 2016, compared with the first quarter of 2015, primarily due to the impact from higher volume as described above and additional operating expenses from an acquired business.

Table of Contents**Industrial Segment Profit**

The following factors contributed to the change in Industrial s segment profit from the prior year quarter:

		2016 versus
<i>(In millions)</i>		2015
Volume	\$	8
Foreign exchange		(5)
Other		6
Total change	\$	9

Segment profit for the Industrial segment increased \$9 million, 11%, in the first quarter of 2016, compared with the first quarter of 2015, largely due to the impact from higher volume as described above.

Finance

		Three Months Ended		
<i>(In millions)</i>		April 2,		April 4,
		2016		2015
Revenues	\$	20	\$	22
Segment profit		5		6

Finance segment revenues and profit were largely unchanged in the first quarter of 2016, compared with the first quarter of 2015.

Finance Portfolio Quality

The following table reflects information about the Finance segment s credit performance related to finance receivables.

		April 2,		January 2,
<i>(Dollars in millions)</i>		2016		2016
Finance receivables*	\$	1,084	\$	1,105
Nonaccrual finance receivables		79		84
Ratio of nonaccrual finance receivables to finance receivables		7.29%		7.60%
60+ days contractual delinquency	\$	94	\$	69
60+ days contractual delinquency as a percentage of finance receivables		8.67%		6.24%

* Excludes finance receivables held for sale.

Liquidity and Capital Resources

Our financings are conducted through two separate borrowing groups. The Manufacturing group consists of Textron consolidated with its majority-owned subsidiaries that operate in the Textron Aviation, Bell, Textron Systems and Industrial segments. The Finance group, which also is the Finance segment, consists of Textron Financial Corporation and its consolidated subsidiaries. We designed this framework to enhance our borrowing power by separating the Finance group. Our Manufacturing group operations include the development, production and

Edgar Filing: TEXTRON INC - Form 10-Q

delivery of tangible goods and services, while our Finance group provides financial services. Due to the fundamental differences between each borrowing group's activities, investors, rating agencies and analysts use different measures to evaluate each group's performance. To support those evaluations, we present balance sheet and cash flow information for each borrowing group within the Consolidated Financial Statements.

Key information that is utilized in assessing our liquidity is summarized below:

<i>(Dollars in millions)</i>	April 2, 2016	January 2, 2016
Manufacturing group		
Cash and equivalents	\$ 723	\$ 946
Debt	3,109	2,697
Shareholders' equity	4,989	4,964
Capital (debt plus shareholders' equity)	8,098	7,661
Net debt (net of cash and equivalents) to capital	32%	26%
Debt to capital	38%	35%
Finance group		
Cash and equivalents	\$ 55	\$ 59
Debt	888	913

Table of Contents

We believe that our calculations of debt to capital and net debt to capital are useful measures as they provide a summary indication of the level of debt financing (i.e., leverage) that is in place to support our capital structure, as well as to provide an indication of the capacity to add further leverage. We believe that we will have sufficient cash to meet our future needs, based on our existing cash balances, the cash we expect to generate from our manufacturing operations and other available funding alternatives, as appropriate.

Textron has a senior unsecured revolving credit facility that expires in October 2018 for an aggregate principal amount of \$1.0 billion, of which up to \$100 million is available for the issuance of letters of credit. At April 2, 2016, there were no amounts borrowed against the facility.

We also maintain an effective shelf registration statement filed with the Securities and Exchange Commission that allows us to issue an unlimited amount of public debt and other securities. In March 2016, we issued \$350 million in 4.0% Notes due March 2026 under this registration statement.

Manufacturing Group Cash Flows

Cash flows from continuing operations for the Manufacturing group as presented in our Consolidated Statements of Cash Flows are summarized below:

	Three Months Ended	
	April 2, 2016	April 4, 2015
<i>(In millions)</i>		
Operating activities	\$ (148)	\$ (67)
Investing activities	(252)	(117)
Financing activities	173	21

The first quarter of our fiscal year typically results in net cash outflow from operating activities. Consistent with prior years, we expect positive cash flows from operating activities for the full year.

Cash flows used in operating activities in the first quarter of 2016 primarily related to higher inventory levels of \$313 million and incentive and deferred compensation payments of \$139 million, partially offset by earnings. The higher inventory levels in the first quarter of 2016 were largely due to increases at Textron Aviation and Textron Systems to support sales growth. In the first quarter of 2015, cash flows used in operating activities primarily related to higher inventory levels of \$327 million and incentive and deferred compensation payments of \$152 million, partially offset by earnings. The decrease in cash flows from operating activities of \$81 million in the first quarter of 2016, compared with the first quarter of 2015, was primarily due to a decrease in customer deposits related to performance-based payments on certain military contracts.

During the first quarter of 2016, investing activities reflected aggregate cash payments of \$164 million for four business acquisitions, compared with payments of \$32 million for acquisitions in the first quarter of 2015. Cash used for investing activities also included capital expenditures of \$88 million and \$79 million in the first quarter of 2016 and 2015, respectively.

Financing activities in the first quarter of 2016 primarily included proceeds of \$345 million from long-term debt, partially offset by \$215 million in cash paid to repurchase an aggregate of 6.2 million shares of our outstanding common stock under a 2013 share repurchase authorization.

Finance Group Cash Flows

Cash flows from continuing operations for the Finance group as presented in our Consolidated Statements of Cash Flows are summarized below:

	Three Months Ended	
	April 2,	April 4,
<i>(In millions)</i>	2016	2015
Operating activities	\$ 2	\$ 17
Investing activities	23	91
Financing activities	(29)	(52)

The Finance group's cash flows from investing activities primarily included collections on finance receivables totaling \$68 million and \$112 million in the first quarter of 2016 and 2015, respectively, partially offset by finance receivable originations of \$55 million and \$50 million, respectively. Cash used for financing activities included payments on long-term and nonrecourse debt of \$46 million in the first quarter of 2016, compared with \$70 million of payments in the first quarter of 2015.

Table of Contents**Consolidated Cash Flows**

The consolidated cash flows from continuing operations, after elimination of activity between the borrowing groups, are summarized below:

	Three Months Ended	
	April 2, 2016	April 4, 2015
<i>(In millions)</i>		
Operating activities	\$ (150)	\$ (19)
Investing activities	(225)	(57)
Financing activities	144	(31)

Cash flows used in operating activities in the first quarter of 2016 primarily related to higher inventory levels of \$313 million and incentive and deferred compensation payments of \$142 million, partially offset by earnings. The higher inventory levels in the first quarter of 2016 were largely due to increases at Textron Aviation and Textron Systems to support sales growth. In the first quarter of 2015, cash flows used in operating activities primarily related to higher inventory levels of \$327 million and incentive and deferred compensation payments of \$155 million, partially offset by earnings. The decrease in cash flows from operating activities of \$131 million in the first quarter of 2016, compared with the first quarter of 2015, was primarily due to a decrease in customer deposits related to performance-based payments on certain military contracts.

Investing cash flows included cash used for acquisitions of \$164 million and \$32 million and capital expenditures of \$88 million and \$79 million in the first quarter of 2016 and 2015, respectively. Total cash flows from financing activities in the first quarter of 2016, primarily included proceeds of \$362 million from long-term debt, partially offset by \$215 million of share repurchases.

Captive Financing and Other Intercompany Transactions

The Finance group finances retail purchases and leases for new and pre-owned aircraft and helicopters manufactured by our Manufacturing group, otherwise known as captive financing. In the Consolidated Statements of Cash Flows, cash received from customers or from the sale of receivables is reflected as operating activities when received from third parties. However, in the cash flow information provided for the separate borrowing groups, cash flows related to captive financing activities are reflected based on the operations of each group. For example, when product is sold by our Manufacturing group to a customer and is financed by the Finance group, the origination of the finance receivable is recorded within investing activities as a cash outflow in the Finance group's statement of cash flows. Meanwhile, in the Manufacturing group's statement of cash flows, the cash received from the Finance group on the customer's behalf is recorded within operating cash flows as a cash inflow. Although cash is transferred between the two borrowing groups, there is no cash transaction reported in the consolidated cash flows at the time of the original financing. These captive financing activities, along with all significant intercompany transactions, are reclassified or eliminated from the Consolidated Statements of Cash Flows.

Reclassification adjustments included in the Consolidated Statements of Cash Flows are summarized below:

	Three Months Ended	
	April 2, 2016	April 4, 2015
<i>(In millions)</i>		

Edgar Filing: TEXTRON INC - Form 10-Q

Reclassifications adjustments from investing to operating activities:

Finance receivable originations for Manufacturing group inventory sales	\$	(55)	\$	(50)
Cash received from customers		51		81
Total reclassifications adjustments from investing to operating activities	\$	(4)	\$	31

Critical Accounting Estimates

The accounting policies that we believe are most critical to the portrayal of our financial condition and results of operations are disclosed on pages 31 through 33 in our 2015 Annual Report on Form 10-K. The following section provides an update of the year-end disclosure for long-term contracts to include program profit adjustments made during the quarter.

Long-Term Contracts

We make a substantial portion of our sales to government customers pursuant to long-term contracts. These contracts require development and delivery of products over multiple years and may contain fixed-price purchase options for additional products. We account for these long-term contracts under the percentage-of-completion method of accounting. Under this method, we estimate profit as the difference between total estimated revenues and cost of a contract. The percentage-of-completion method of accounting involves the use of various estimating techniques to project costs at completion and, in some cases, includes estimates of recoveries asserted against the customer for changes in specifications. Due to the size, length of time and nature of many of our contracts, the estimation of total contract costs and revenues through completion is complicated and subject to many variables relative to the outcome of future events over a period of several years. We are required to make numerous assumptions and estimates relating to items such as expected engineering requirements, complexity of design and related development costs, product performance, performance of subcontractors, availability and cost of materials, labor productivity and cost, overhead and

Table of Contents

capital costs, manufacturing efficiencies and the achievement of contract milestones, including product deliveries, technical requirements, or schedule.

At the outset of each contract, we estimate the initial profit booking rate. The initial profit booking rate of each contract considers risks surrounding the ability to achieve the technical requirements (for example, a newly-developed product versus a mature product), schedule (for example, the number and type of milestone events), and costs by contract requirements in the initial estimated costs at completion. Profit booking rates may increase during the performance of the contract if we successfully retire risks surrounding the technical, schedule, and costs aspects of the contract. Likewise, the profit booking rate may decrease if we are not successful in retiring the risks; and, as a result, our estimated costs at completion increase. All of the estimates are subject to change during the performance of the contract and, therefore, may affect the profit booking rate. When adjustments are required, any changes from prior estimates are recognized using the cumulative catch-up method with the impact of the change from inception-to-date recorded in the current period. The aggregate gross amount of all program profit adjustments that are included within segment profit are presented below.

	Three Months Ended	
	April 2, 2016	April 4, 2015
<i>(In millions)</i>		
Gross favorable	\$ 34	\$ 33
Gross unfavorable	(5)	(15)
Net adjustments	\$ 29	\$ 18

Forward-Looking Information

Certain statements in this Quarterly Report on Form 10-Q and other oral and written statements made by us from time to time are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements, which may describe strategies, goals, outlook or other non-historical matters, or project revenues, income, returns or other financial measures, often include words such as believe, expect, anticipate, intend, plan, estimate, guidance, project, target, potential, will, shall, may and similar expressions intended to identify forward-looking statements. These statements are only predictions and involve known and unknown risks, uncertainties, and other factors that may cause our actual results to differ materially from those expressed or implied by such forward-looking statements. Given these uncertainties, you should not place undue reliance on these forward-looking statements. Forward-looking statements speak only as of the date on which they are made, and we undertake no obligation to update or revise any forward-looking statements. In addition to those factors described in our 2015 Annual Report on Form 10-K under RISK FACTORS, among the factors that could cause actual results to differ materially from past and projected future results are the following:

- Interruptions in the U.S. Government's ability to fund its activities and/or pay its obligations;
- Changing priorities or reductions in the U.S. Government defense budget, including those related to military operations in foreign countries;
- Our ability to perform as anticipated and to control costs under contracts with the U.S. Government;
- The U.S. Government's ability to unilaterally modify or terminate its contracts with us for the U.S. Government's convenience or for our failure to perform, to change applicable procurement and accounting policies, or, under certain circumstances, to withhold payment or suspend or debar us as a contractor eligible to receive future contract awards;
- Changes in foreign military funding priorities or budget constraints and determinations, or changes in government regulations or policies on the export and import of military and commercial products;
- Volatility in the global economy or changes in worldwide political conditions that adversely impact demand for our products;
- Volatility in interest rates or foreign exchange rates;
- Risks related to our international business, including establishing and maintaining facilities in locations around the world and relying on joint venture partners, subcontractors, suppliers, representatives, consultants and other business partners in connection with international business, including in emerging market countries;

Edgar Filing: TEXTRON INC - Form 10-Q

- Our Finance segment's ability to maintain portfolio credit quality or to realize full value of receivables;
- Performance issues with key suppliers or subcontractors;
- Legislative or regulatory actions, both domestic and foreign, impacting our operations or demand for our products;
- Our ability to control costs and successfully implement various cost-reduction activities;
- The efficacy of research and development investments to develop new products or unanticipated expenses in connection with the launching of significant new products or programs;
- The timing of our new product launches or certifications of our new aircraft products;
- Our ability to keep pace with our competitors in the introduction of new products and upgrades with features and technologies desired by our customers;
- Pension plan assumptions and future contributions;
- Demand softness or volatility in the markets in which we do business; and

Table of Contents

- Cybersecurity threats, including the potential misappropriation of assets or sensitive information, corruption of data or operational disruption.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There has been no significant change in our exposure to market risk during the fiscal quarter ended April 2, 2016. For discussion of our exposure to market risk, refer to Item 7A. Quantitative and Qualitative Disclosures about Market Risk contained in Textron's 2015 Annual Report on Form 10-K.

Item 4. CONTROLS AND PROCEDURES

We performed an evaluation of the effectiveness of our disclosure controls and procedures as of April 2, 2016. The evaluation was performed with the participation of senior management of each business segment and key Corporate functions, under the supervision of our Chairman, President and Chief Executive Officer (CEO) and our Executive Vice President and Chief Financial Officer (CFO). Based on this evaluation, the CEO and CFO concluded that our disclosure controls and procedures were operating and effective as of April 2, 2016.

There were no changes in our internal control over financial reporting during the fiscal quarter ended April 2, 2016 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

The following provides information about our first quarter 2016 repurchases of equity securities that are registered pursuant to Section 12 of the Securities Exchange Act of 1934, as amended:

Period (<i>shares in thousands</i>)	Total Number of Shares Purchased (1)	Average Price Paid per Share (excluding commissions)	Total Number of Shares Purchased as part of Publicly Announced Plan (1)	Maximum Number of Shares that may yet be Purchased under
--	---	---	--	---

Edgar Filing: TEXTRON INC - Form 10-Q

					the Plan	
January 3, 2016	February 6, 2016	3,298	\$	35.96	3,298	7,584
February 7, 2016	March 5, 2016	2,350		32.43	2,350	5,234
March 6, 2016	April 2, 2016	600		33.32	600	4,634
Total		6,248	\$	34.38	6,248	

(1) *These shares were purchased pursuant to a plan authorizing the repurchase of up to 25 million shares of Textron common stock that had been announced on January 23, 2013. This plan has no expiration date.*

Table of Contents**Item 5. OTHER INFORMATION**

(a) The 2016 Annual Meeting of Shareholders of Textron was held on April 27, 2016.

The results of the voting on the matters submitted to our shareholders are as follows:

1. The following persons were elected to serve as directors until the next annual shareholders meeting and received the following votes:

	For	Against	Abstain	Broker Non-Vote
Scott C. Donnelly	244,597,525	6,154,441	1,220,499	17,488,909
Kathleen M. Bader	224,409,625	5,954,190	1,608,650	17,488,909
R. Kerry Clark	224,126,528	6,279,308	1,566,629	17,488,909
James T. Conway	225,631,815	4,812,847	1,527,803	17,488,909
Ivor J. Evans	224,150,498	6,017,046	1,804,921	17,488,909
Lawrence K. Fish	223,615,202	6,529,838	1,827,425	17,488,909
Paul E. Gagné	222,799,248	7,399,416	1,773,801	17,488,909
Dain M. Hancock	224,616,412	5,581,948	1,774,105	17,488,909
Lord Powell of Bayswater KCMG	222,619,217	7,613,289	1,739,959	17,488,909
Lloyd G. Trotter	225,334,277	4,956,882	1,681,306	17,488,909
James L. Ziemer	225,617,941	4,649,697	1,704,827	17,488,909

2. The advisory (non-binding) resolution to approve the compensation of our named executive officers, as disclosed in our proxy statement, was approved by the following vote:

For	Against	Abstain	Broker Non-Vote
220,163,954	9,735,325	2,073,186	17,488,909

3. The appointment of Ernst & Young LLP by the Audit Committee as Textron's independent registered public accounting firm for 2016 was ratified by the following vote:

For	Against	Abstain	Broker Non-Vote
244,424,043	3,984,194	1,053,137	

Table of Contents

Item 6. EXHIBITS

- 10.1 Form of Non-Qualified Stock Option Agreement under 2015 Long-Term Incentive Plan.
- 10.2 Form of Stock-Settled Restricted Stock Unit (with Dividend Equivalents) Grant Agreement under 2015 Long-Term Incentive Plan.
- 10.3 Form of Performance Share Unit Grant Agreement under 2015 Long-Term Incentive Plan.
- 12.1 Computation of ratio of income to fixed charges of Textron Inc. Manufacturing Group
- 12.2 Computation of ratio of income to fixed charges of Textron Inc. including all majority-owned subsidiaries
- 31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 Certification of Chief Executive Officer Pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 Certification of Chief Financial Officer Pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 101 The following materials from Textron Inc. s Quarterly Report on Form 10-Q for the quarterly period ended April 2, 2016, formatted in XBRL (eXtensible Business Reporting Language): (i) the Consolidated Statements of Operations, (ii) the Consolidated Statements of Comprehensive Income, (iii) the Consolidated Balance Sheets, (iv) the Consolidated Statements of Cash Flows and (v) the Notes to the Consolidated Financial Statements.

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.

TEXTRON INC.

Date: April 28, 2016

/s/ Mark S. Bamford
Mark S. Bamford
Vice President and Corporate Controller
(principal accounting officer)

Table of Contents

LIST OF EXHIBITS

- 10.1 Form of Non-Qualified Stock Option Agreement under 2015 Long-Term Incentive Plan.
- 10.2 Form of Stock-Settled Restricted Stock Unit (with Dividend Equivalents) Grant Agreement under 2015 Long-Term Incentive Plan.
- 10.3 Form of Performance Share Unit Grant Agreement under 2015 Long-Term Incentive Plan.
- 12.1 Computation of ratio of income to fixed charges of Textron Inc. Manufacturing Group
- 12.2 Computation of ratio of income to fixed charges of Textron Inc. including all majority-owned subsidiaries
- 31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 Certification of Chief Executive Officer Pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 Certification of Chief Financial Officer Pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 101 The following materials from Textron Inc.'s Quarterly Report on Form 10-Q for the quarterly period ended April 2, 2016, formatted in XBRL (eXtensible Business Reporting Language): (i) the Consolidated Statements of Operations, (ii) the Consolidated Statements of Comprehensive Income, (iii) the Consolidated Balance Sheets, (iv) the Consolidated Statements of Cash Flows and (v) the Notes to the Consolidated Financial Statements.