AAR CORP
Form 10-K
July 13, 2016

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)

ý **Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the fiscal year ended May 31, 2016
or

o **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 1-6263

AAR CORP.

(Exact name of registrant as specified in its charter)

Delaware	**36-2334820**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

One AAR Place, 1100 N. Wood Dale Road, Wood Dale, Illinois 60191
(Address of principal executive offices, including zip code)

Registrant's telephone number, including area code: **(630) 227-2000**

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	*Name of Each Exchange on Which Registered*
Common Stock, $1.00 par value	**New York Stock Exchange** **Chicago Stock Exchange**
Common Stock Purchase Rights	

New York Stock Exchange
Chicago Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: **None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ý No o

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. Yes o No ý

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 ý No o

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 ý No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

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 ý Accelerated filer o Non-Accelerated filer o Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No ý

The aggregate market value of the registrant's voting stock held by nonaffiliates was approximately $806 million (based upon the closing price of the Common Stock at November 30, 2015 as reported on the New York Stock Exchange).

On June 30, 2016, there were 34,698,633 shares of Common Stock outstanding.

Documents Incorporated by Reference

Portions of the Company's proxy statement for the Company's 2016 Annual Meeting of Stockholders, to be held October 13, 2016, are incorporated by reference in Part III of this report.

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PART I

ITEM 1. BUSINESS
(Dollars in millions)

General

AAR CORP. and its subsidiaries are referred to herein collectively as "AAR," "Company," "we," "us," and "our" unless the context indicates otherwise. AAR was founded in 1951, organized in 1955 and reincorporated in Delaware in 1966. We are a diversified provider of products and services to the worldwide aviation and government and defense markets.

During fiscal 2015, we executed on a comprehensive strategic plan that included:

- The sale of our Telair Cargo Group for cash of $714 million, resulting in pre-tax gains of $198.6 million in the fourth quarter of fiscal 2015 (and $27.7 million in the first quarter of fiscal 2016 from the receipt of contingent consideration);
- A decision to divest our Precision Systems Manufacturing business;
- The exit of certain product lines and inventories in our aviation services businesses that were underperforming or not part of our strategy going forward;
- The reduction of our total debt by $480 million;
- The return of capital to shareholders through $151.5 million in common stock repurchases and $12.5 million of dividends.

The divestiture of these manufacturing businesses allowed us to narrow our strategy to focus on our best in class aviation and expeditionary services. In fiscal 2016, our Aviation Services segment succeeded in expanding existing customer relationships in distribution and securing new program work with multiple international carriers. In our Expeditionary Services segment, we have completed the successful start-up of our new contract with the U.K. Ministry of Defense providing search and rescue services in the Falkland Islands.

As we enter fiscal 2017, we remain in a strong financial position to further execute on our strategy as a best in class aviation and expeditionary services company. Our cash on hand plus unused capacity on our Revolving Credit Facility was $409 million at May 31, 2016. We expect to invest opportunistically in expanding our comprehensive suite of services to the global commercial aviation and government and defense markets.

Business Segments

Aviation Services

The Aviation Services segment provides aftermarket support and services for the commercial aviation and government and defense markets and accounted for 86%, 83%, and 72% of our sales in fiscal 2016, 2015, and 2014, respectively. In this segment, we also provide inventory management and distribution services, maintenance, repair and overhaul ("MRO") and engineering services. Business activities in this segment are primarily conducted through AAR Supply Chain, Inc. (formerly known as AAR Parts Trading, Inc.); AAR Aircraft & Engine Sales & Leasing, Inc.; AAR Aircraft Services, Inc.; AAR Allen Services, Inc. (a wholly-owned subsidiary of AAR Parts Trading, Inc.); AAR Landing Gear LLC; and AAR International, Inc.

We sell and lease a wide variety of new, overhauled and repaired engine and airframe parts and components to our commercial aviation and government/defense customers.

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We provide customized inventory supply and management, warranty claim management, and outsourcing programs for engine and airframe parts and components in support of our airline and government customers' maintenance activities. The types of services provided under these programs include material planning, sourcing, logistics, information and program management, and parts and component repair and overhaul. We are also an authorized distributor for more than 60 leading aviation product manufacturers.

We also provide customized performance-based supply chain logistics programs in support of the U.S. Department of Defense ("DoD") and foreign governments. The types of services provided under these programs include material planning, sourcing, logistics, information and program management, airframe maintenance and maintenance planning, and component repair and overhaul.

We provide major airframe inspection, maintenance, repair and overhaul, painting services, line maintenance, airframe modifications, structural repairs, avionic service and installation, exterior and interior refurbishment, and engineering services and support for many types of commercial and military aircraft. We also repair and overhaul landing gears, wheels, and brakes for commercial and military aircraft.

We operate five airframe maintenance facilities and one landing gear overhaul facility. Our landing gear overhaul facility is in Miami, Florida, where we repair and overhaul landing gear, wheels, brakes, and actuators for different types of commercial and military aircraft. Our airframe maintenance facilities are in Indianapolis, Indiana; Oklahoma City, Oklahoma; Duluth, Minnesota; Miami, Florida; and Lake Charles, Louisiana. In fiscal 2016, we closed a regional aircraft maintenance facility in Hot Springs, Arkansas.

Activities in our Aviation Services segment also include the sale and lease of used commercial aircraft. Each sale or lease is negotiated as a separate agreement that includes term, price, representations, warranties, and lease return provisions. During fiscal 2015, we sold our last two remaining wholly-owned aircraft and one aircraft owned with joint venture partners. At May 31, 2016, our remaining portfolio consisted of three aircraft owned through joint ventures.

The majority of our sales are made pursuant to standard commercial purchase orders. U.S. government sales are generally made under standard types of government contracts, including definite contracts which call for the performance of specified services or the delivery of specified products and ID/IQ (i.e., indefinite delivery/indefinite quantity) contracts. Certain inventory supply and management and performance-based logistics program agreements reflect negotiated terms and conditions.

To support activities within the Aviation Services segment, we acquire aviation parts and components from domestic and foreign airlines, independent aviation service companies, aircraft leasing companies, and original equipment manufacturers ("OEM"s). We have ongoing arrangements with OEMs that provide us access to parts, repair manuals, and service bulletins in support of parts manufactured by them. Although the terms of each arrangement vary, they typically are made on standard OEM terms as to duration, price, and delivery. From time to time, we purchase engines for disassembly into individual parts and components. These engines may be leased to airlines on a short-term basis prior to disassembly.

Expeditionary Services

The Expeditionary Services segment consists of businesses that provide products and services supporting the movement of equipment and personnel by the DoD, foreign governments and non-governmental organizations. The Expeditionary Services segment accounted for 14%, 17%, and 28% of our sales in fiscal 2016, 2015, and 2014, respectively. Business activities in this segment are primarily conducted through AAR Airlift Group, Inc.; AAR Manufacturing, Inc. and Brown International Corporation (a wholly-owned subsidiary of AAR Manufacturing, Inc.).

We provide expeditionary airlift services to the United States and other government customers. Our expeditionary airlift services provide fixed- and rotary-wing flight operations. These operations include

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search and rescue operations and transporting personnel and cargo principally in support of the DoD. We operate and maintain a fleet of special mission customized fixed- and rotary-wing aircraft, principally in Afghanistan, Falkland Islands, Northern Africa, and Western Pacific regions. We hold FAR Part 133 and 135 certificates to operate aircraft and a FAR Part 145 certificate to operate a repair station. We are also Commercial Airlift Review Board certified with the DoD.

We design, manufacture, and repair transportation pallets, and a wide variety of containers and shelters used in support of military and humanitarian tactical deployment activities. The containers and shelters are used in numerous mission requirements, including armories, supply and parts storage, refrigeration systems, tactical operation centers, briefing rooms, laundry and kitchen facilities, water treatment, and sleeping quarters. Shelters include both stationary and vehicle-mounted applications.

We also provide engineering, design, and system integration services for specialized command and control systems.

Sales in this segment are made to customers pursuant to standard commercial purchase orders and contracts. U.S. government sales are generally made under standard types of government contracts, including definite contracts which call for the performance of specified services or the delivery of specified products and ID/IQ (i.e., indefinite delivery/indefinite quantity) contracts. The majority of our products and services are procured via definite contracts. We purchase raw materials for this segment, including steel, aluminum, extrusions, and other necessary supplies from several vendors.

Raw Materials

Although we generated 54% of our fiscal 2016 sales from the sale of products, our businesses are generally engaged in limited manufacturing activities and have minimal exposure to fluctuations in both the availability and pricing for raw materials. Where necessary, we have been able to obtain raw materials and other inventory items from numerous sources for each segment at competitive prices, terms, and conditions, and we expect to be able to continue to do so.

Terms of Sale

We generally sell our products and services under standard 30-day payment terms. On occasion, certain customers, principally foreign customers, will negotiate extended payment terms of 60-90 days. Except for customary warranty provisions, customers neither have the right to return products nor do they have the right to extended financing. Our contracts with the DoD and its contractors and other governmental agencies are typically firm agreements to provide products and services at a fixed price or on a time and material basis, and have a term of one year or less, frequently subject to extension for one or more additional periods of one year at the option of the government customer.

Customers

The principal customers for our products and services in the Aviation Services segment are domestic and foreign commercial airlines, domestic and foreign freight airlines, regional and commuter airlines, business and general aviation operators, OEMs, aircraft leasing companies, aftermarket aviation support companies, the DoD and its contractors, and foreign military organizations or governments. In the Expeditionary Services segment, our principal customers include the DoD and its contractors and foreign governmental and defense organizations.

Sales of aviation products and services to our commercial airline customers are generally affected by such factors as the number, type and average age of aircraft in service, the levels of aircraft utilization (e.g., frequency of schedules), the number of airline operators, the general economy, and the level of sales of new and used aircraft. Sales to the DoD and other government agencies are subject to a number of

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factors, including the level of troop deployment worldwide, government funding, competitive bidding, and requirements generated by worldwide geopolitical events.

We primarily market and sell products and services through our own employees. In certain markets outside of the United States, we rely on foreign sales representatives to assist in the sale of our products and services.

Sales to Government and Defense Customers

Sales to global government and defense customers (including sales to branches, agencies, and departments of the U.S. government) were $642.6 million (38.7% of consolidated sales), $589.8 million (37.0% of consolidated sales) and $777.5 million (45.4% of consolidated sales) in fiscal 2016, 2015 and 2014, respectively. Sales to branches, agencies, and departments of the U.S. government and their contractors were $513.8 million (30.9% of consolidated sales), $493.1 million (30.9% of consolidated sales), and $661.7 million (38.7% of consolidated sales) in fiscal 2016, 2015, and 2014, respectively. Sales to government and defense customers are reported in each of our reportable segments (See Note 14 of Notes to Consolidated Financial Statements). Since such sales are subject to competitive bidding and government funding, no assurance can be given that such sales will continue at levels previously experienced. The majority of our U.S. government contracts are for products and services supporting the DoD logistics and mobility strategy, as well as for expeditionary airlift services. Thus, our government contracts have changed, and may continue to change, with fluctuations in defense and other governmental agency spending. Our government contracts are also subject to termination by the customer; in the event of such a termination we would be entitled to recover all allowable costs incurred by us through the date of termination.

Government Regulation and Certificates

The Federal Aviation Administration ("FAA") regulates the manufacture, repair, distribution, and operation of all aircraft and aircraft parts operated in the United States. Similar rules and regulatory authorities exist in other countries. The inspection, maintenance and repair procedures for the various types of aircraft and equipment are prescribed by these regulatory authorities and can be performed only by certified repair facilities utilizing certified technicians. The FAA requires that various maintenance routines be performed on aircraft engines, certain engine parts, and airframes at regular intervals based on take off and landing cycles or flight time. Our businesses which sell defense products and services directly to the U.S. government or through its contractors can be subject to various laws and regulations governing pricing and other factors.

We have 12 FAA certificated repair stations in the United States and Europe. Of the 12 certificated FAA repair stations, seven are also European Aviation Safety Agency ("EASA") certificated repair stations. Such certificates, which are ongoing in duration, are required for us to perform authorized maintenance, repair and overhaul services for our customers and are subject to revocation by the government for non-compliance with applicable regulations. Of the 12 FAA certificated repair stations, 11 are in the Aviation Services segment and one is in the Expeditionary Services segment. The seven EASA certificated repair stations are in the Aviation Services segment. We also hold FAR Part 133 and 135 certificates to operate aircraft in our Expeditionary Services segment. We are also Commercial Airlift Review Board certified with the DoD. We believe that we possess all licenses and certifications that are material to the conduct of our business.

Competition

Competition in each of our markets is based on quality, ability to provide a broad range of products and services, speed of delivery, and price. Competitors in our Aviation Services segment include OEMs, the service divisions of large commercial airlines, and other independent suppliers of parts, repair, and

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overhaul services to the commercial and defense markets. Our Expeditionary Services segment competes with domestic and foreign contracting companies and a number of divisions of large corporations and other large and small companies. Although certain of our competitors have substantially greater financial and other resources than we do, we believe that we have maintained a satisfactory competitive position through our responsiveness to customer needs, our attention to quality, and our unique combination of market expertise and technical and financial capabilities.

Backlog

Backlog represents the amount of revenue that we expect to derive from unshipped orders or signed contracts. At May 31, 2016, backlog was approximately $953.9 million compared to $920.3 million at May 31, 2015. Approximately $506.7 million of our May 31, 2016 backlog is expected to be filled within the next 12 months.

Employees

At May 31, 2016, we employed approximately 4,700 employees worldwide, of which approximately 110 employees are subject to a collective bargaining agreement. We also retain approximately 830 contract workers, the majority of whom are located at our airframe maintenance facilities.

Available Information

For additional information concerning our business segments, see Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Business Segment Information" in Note 14 of Notes to Consolidated Financial Statements under Item 8, "Financial Statements and Supplementary Data."

Our internet address is www.aarcorp.com. We make available free of charge through our web site our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 as soon as reasonably practicable after we electronically file such material with, or furnish such material to, the Securities and Exchange Commission. Information contained on our web site is not a part of this report.

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ITEM 1A. RISK FACTORS

The following is a description of the principal risks inherent in our business.

We are affected by factors that adversely impact the commercial aviation industry.

As a provider of products and services to the commercial aviation industry, we are greatly affected by overall economic conditions of that industry. The commercial aviation industry is historically cyclical and has been negatively affected in the past by geopolitical events, high fuel and oil prices, lack of capital, and weak economic conditions. As a result of these and other events, from time to time certain of our customers have filed for bankruptcy protection or ceased operation. The impact of instability in the global financial markets may lead airlines to reduce domestic or international capacity. In addition, certain of our airline customers have in the past been impacted by tight credit markets, which limited their ability to buy parts, services, engines, and aircraft.

A reduction in the operating fleet of aircraft both in the U.S. and abroad will result in reduced demand for parts support and maintenance activities for the type of aircraft affected. Further, tight credit conditions negatively impact the amount of liquidity available to buy parts, services, engines, and aircraft. A deteriorating airline environment may also result in additional airline bankruptcies, and in such circumstances we may not be able to fully collect outstanding accounts receivable. Reduced demand from customers caused by weak economic conditions, including tight credit conditions and customer bankruptcies, may adversely impact our financial condition or results of operations.

Our business, financial condition, results of operations, and growth rates may be adversely affected by these and other events that impact the aviation industry, including the following:

- deterioration in the financial condition of our existing and potential customers;
- reductions in the need for, or the deferral of, aircraft maintenance and repair services and spare parts support;
- retirement of older generation aircraft, resulting in lower prices for spare parts and services for those aircraft;
- reductions in demand for used aircraft and engines;
- increased in-house maintenance by airlines;
- lack of parts in the marketplace;
- terrorist attacks;
- future outbreaks of infectious diseases; and
- acts of God.

Our U.S. government contracts may not continue at present sales levels, which may have a material adverse effect on our financial condition and results of operations.

Our sales to branches, agencies and departments of the U.S. government and their contractors were $513.8 million (30.9% of consolidated sales) in fiscal 2016 (See Note 14 of Notes to Consolidated Financial Statements). The majority of our U.S. government contracts is for products and services supporting DoD logistics and mobility strategy, as well as for expeditionary airlift services and is, therefore, subject to changes in defense and other governmental agency funding and spending. Our contracts with the U.S. government, including the DoD and its contractors, are typically agreements to provide products and services at a fixed price and have a term of one year or less, frequently subject to extension for one or more additional periods of one year at the option of the government customer. Sales to agencies of the U.S. government and their contractors are subject to a number of factors, including the level of troop

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deployment worldwide, competitive bidding, U.S. government funding, requirements generated by world events, and budgetary constraints.

The President signed the Bipartisan Budget Act of 2015 (the "Budget Act") on November 2, 2015. The Budget Act raises the statutory limit on the amount of permissible federal debt until March 2017 and raises the sequester caps imposed by the Budget Control Act of 2011. However, unforeseen circumstances could cause an extended debt ceiling breach, which could negatively affect the timely collection of our U.S. government invoices.

Future congressional appropriation and authorization of defense spending and the application of sequestration remain marked by significant debate and an uncertain schedule. The federal debt limit continues to be actively debated as plans for long-term national fiscal policy are discussed. The outcome of these debates could have a significant impact on defense spending broadly and programs we support in particular.

If the existing federal debt limit is not raised, we may be required to continue to perform for some period of time on certain of our U.S. government contracts even if the U.S. government is unable to make timely payments. Future budget cuts, including cuts mandated by sequestration, or future procurement decisions could result in reductions, cancellations, and/or delays of existing contracts or programs which could adversely affect our results of operations and financial condition.

We face risks of cost overruns and losses on fixed-price contracts.

We sell certain of our products and services to our commercial, government, and defense customers under firm contracts providing for fixed unit prices, regardless of costs incurred by us. The cost of producing products or providing services may be adversely affected by increases in the cost of labor, materials, fuel, overhead, and other unknown variants, including manufacturing and other operational inefficiencies and differences between assumptions used by us to price a contract and actual results. Increased costs may result in cost overruns and losses on such contracts, which could adversely affect our results of operations and financial condition.

Success at our airframe maintenance facilities is dependent upon continued outsourcing by the airlines.

We currently perform airframe maintenance, repair and overhaul activities at five leased facilities. Revenues at these facilities fluctuate based on demand for maintenance which, in turn, is driven by the number of aircraft operating and the extent of outsourcing of maintenance activities by airlines. In addition, certain airlines operate certain new fleet types and/or newer generation aircraft and we may not have contractual arrangements to service these aircraft nor technicians trained and certified to perform the required airframe maintenance, repair and overhaul activities. If either the number of aircraft operating or the level of outsourcing of maintenance activities declines, we may not be able to execute our operational and financial plans at our maintenance, repair and overhaul facilities, which could adversely affect our results of operations and financial condition.

We operate in highly competitive markets, and competitive pressures may adversely affect us.

The markets for our products and services to our commercial, government, and defense customers are highly competitive, and we face competition from a number of sources, both domestic and international. Our competitors include aircraft manufacturers, aircraft component and parts manufacturers, airline and aircraft service companies, other companies providing maintenance, repair and overhaul services, other aircraft spare parts distributors and redistributors, and other expeditionary airlift service providers. Some of our competitors have substantially greater financial and other resources than we have and others may price their products and services below our selling prices. We believe that our ability to compete depends on superior customer service and support, on-time delivery, sufficient inventory availability, competitive pricing and effective quality assurance programs.

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Our government customers, including the DoD, may turn to commercial contractors, rather than traditional defense contractors, for certain work, or may utilize small business contractors or determine to source work internally rather than use us. We are also impacted by bid protests from unsuccessful bidders on new program awards. Bid protests could result in significant expense for us, contract modifications, or the award decision being overturned and loss of the contract award. Even where a bid protest does not result in the loss of an award, the resolution can extend the time until the contract activity can begin, and delay earnings. These competitive pressures, with potential impacts on both our commercial and government business, could adversely affect our results of operations and financial condition.

We are subject to significant government regulation and may need to incur significant expenses to comply with new or more stringent governmental regulation.

The aviation industry is highly regulated by the FAA in the United States and equivalent regulatory agencies in other countries. Before we sell any of our products that are to be installed in an aircraft, such as engines, engine parts and components, and airframe and accessory parts and components, they must meet certain standards of airworthiness established by the FAA or the equivalent regulatory agencies in certain other countries. We operate repair stations that are licensed by the FAA and the equivalent regulatory agencies in certain other countries, and hold certificates to operate aircraft. Specific regulations vary from country to country, although regulatory requirements in other countries are generally satisfied by compliance with FAA requirements. New and more stringent governmental regulations may be adopted in the future that, if enacted, may have an adverse impact on us.

If any of our material licenses, certificates, authorizations, or approvals were revoked or suspended by the FAA or equivalent regulatory agencies in other countries, our results of operations and financial condition may be adversely affected.

If we fail to comply with government procurement laws and regulations, we could lose business and be liable for various penalties or sanctions.

We must comply with laws and regulations relating to the formation, administration, and performance of U.S. government contracts. These laws and regulations include the Federal Acquisition Regulations, Defense Federal Acquisition Regulations, the Truth in Negotiations Act, Cost Accounting Standards, and laws, regulations, and orders restricting the use and dissemination of classified information under the U.S. export control laws and the export of certain products and technical information. Certain government contracts provide audit rights by government agencies, including with respect to performance, costs, internal controls and compliance with applicable laws and regulations. In complying with these laws and regulations, we may incur significant costs, and non-compliance may result in the imposition of fines and penalties, including contractual damages. If we fail to comply with these laws and regulations or if a government audit, review, or investigation uncovers improper or illegal activities, we may be subject to civil penalties, criminal penalties, or administrative sanctions, including suspension or debarment from contracting with the U.S. government. Our reputation could suffer harm if allegations of impropriety were made or found against us, which could adversely affect our operating performance and may result in additional expenses and possible loss of revenue.

A significant portion of our expeditionary airlift revenue is derived from providing expeditionary airlift services in Afghanistan.

Our expeditionary airlift business derives a significant portion of its revenue from providing expeditionary airlift services in Afghanistan for the DoD. The U.S. has been reducing military activities in Afghanistan and had previously announced plans to reduce the number of troops in Afghanistan to 5,500 by the end of calendar year 2016. Recent announcements by the President have indicated the draw down will be slower than originally planned due to the precarious security situation in Afghanistan with the

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number of troops expected to be 8,400 by January 2017. Our expeditionary airlift services revenue will likely experience further declines should troop reductions occur in Afghanistan.

We are bidding on expeditionary airlift contracts in other regions supporting both DoD and non-DoD customers, although there can be no assurance we will be awarded any of these contracts. Although we expect ongoing demand for expeditionary airlift services in Afghanistan and other regions from the DoD and other governmental departments, we are exposed to the risk that our expeditionary airlift revenues may further decline if contracts are not renewed, renewed only in part, or are terminated, which could adversely affect our results of operations and financial condition. If we are unable to successfully redeploy aircraft not actively supporting current customers at favorable rates or sell them on favorable terms, it could have a material adverse effect on our business, results of operations and financial condition.

U.S. government contractors that provide support services in theaters of conflict such as Afghanistan have come under increasing scrutiny by agency inspectors general, government auditors and congressional committees. Investigations pursued by any or all of these groups may result in additional expense, adverse publicity for us and reputational harm, regardless of the underlying merit of the allegations being investigated.

We are exposed to risks associated with operating internationally.

We conduct our business in certain foreign countries, some of which are politically unstable or subject to military or civil conflicts. Consequently, we are subject to a variety of risks that are specific to international operations, including the following:

- military conflicts, civil strife, and political risks;
- export regulations that could erode profit margins or restrict exports;
- compliance with the U.S. Foreign Corrupt Practices Act, United Kingdom ("UK") Anti-bribery Act, and other anti-bribery laws;
- the burden and cost of compliance with foreign laws, treaties, and technical standards and changes in those regulations;
- contract award and funding delays;
- potential restrictions on transfers of funds;
- import and export duties and value added taxes;
- foreign exchange risk;
- transportation delays and interruptions; and
- uncertainties arising from foreign local business practices and cultural considerations.

In addition, the UK held a referendum in which voters approved an exit from the European Union ("EU"). The terms of the UK's potential exit from the EU have yet to be determined and it is possible there will be greater restrictions on imports and exports between the UK and EU countries along with increased regulatory complexities.

While we have adopted and will continue to adopt measures to reduce the potential impact of losses resulting from the risks of doing business internationally, we cannot ensure that such measures will be adequate or that the regions in which we operate will continue to be stable enough to allow us to operate profitably or at all.

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Acquisitions expose us to risks, including the risk that we may be unable to effectively integrate acquired businesses.

We explore and have discussions with third parties regarding acquisitions on a regular basis. Acquisitions involve risks, including difficulties in integrating the operations and personnel, the effects of amortization of any acquired intangible assets and the potential impairment of goodwill, and the potential loss of key employees of the acquired business. In addition, acquisitions often require substantial management resources and have the potential to divert our attention from our existing business. For any businesses we may acquire in the future, we may not be able to execute our operational, financial, or integration plans for the acquired businesses, which could adversely affect our results of operations and financial condition.

Market values for our aviation products fluctuate, and we may be unable to re-lease or sell aircraft and engines when their current leases expire.

We make a number of assumptions when determining the recoverability of inventories, aircraft, and engines, which are on lease or available for lease. These assumptions include historical sales trends, current and expected usage trends, replacement values, current and expected lease rates, residual values, future demand, and future cash flows. Reductions in demand for our inventories or declining market values, as well as differences between actual results and the assumptions utilized by us when determining the recoverability of our inventories, aircraft, and engines, could result in impairment charges in future periods, which would adversely affect our results of operations and financial condition.

We lease aircraft and engines to our customers on an operating lease basis. Our ability to re-lease or sell these assets on acceptable terms when the lease expires is subject to a number of factors which drive industry capacity, including new aircraft deliveries, availability of used aircraft and engines in the marketplace, competition, financial condition of our customers, overall health of the airline industry, and general economic conditions. Our inability to re-lease or sell aircraft and engines could adversely affect our results of operations and financial condition.

We may need to reduce the carrying value of our assets.

We own and distribute a significant amount of aircraft, aircraft parts and components, and manufacturing facilities and related equipment. The removal of aircraft from service or recurring losses in certain operations could require us to evaluate the recoverability of the carrying value of those assets and record an impairment charge through earnings to reduce the carrying value. We recognized impairment charges and other losses of $71.4 million in fiscal 2015 related to our actions to address underperforming product lines and inventories. In addition, if aircraft or engines for which we offer replacement parts or supply repair and overhaul services are retired and there are fewer aircraft that require these parts or services, our revenues may decline.

We have recorded goodwill and other intangible assets related to acquisitions. If we are unable to achieve the projected levels of operating results, it may be necessary to record an impairment charge to reduce the carrying value of goodwill and related intangible assets. Similarly, if we were to lose a key customer or one of our airframe maintenance or landing gear facilities were to lose its authority to operate, we might be required to record an impairment charge.

We are dependent upon continued availability of financing to manage our business and to execute our business strategy, and additional financing may not be available on terms acceptable to us.

Our ability to manage our business and to execute our business strategy is dependent, in part, on the continued availability of debt and equity capital. Access to the debt and equity capital markets may be limited by various factors, including the condition of overall credit markets, general economic factors, state of the aviation industry, our financial performance, and credit ratings. Debt and equity capital may not continue to be available to us on favorable terms, or at all. Our inability to obtain financing on favorable terms could adversely affect our results of operations and financial condition.

Our existing debt includes restrictive and financial covenants.

Certain loan and debt agreements, including our Credit Facility, require us to comply with various restrictive covenants and some contain financial covenants that require us to comply with specified financial ratios and tests. Our failure to meet these covenants could result in default under these loan and debt agreements and may result in a cross-default under other debt agreements. In the event of a default and our inability to obtain a waiver of the default, all amounts outstanding under our debt agreements could be declared immediately due and payable. Our failure to comply with these covenants could adversely affect our results of operations and financial condition.

Our industry is susceptible to product and other liability claims, and claims not adequately covered by insurance may adversely affect our financial condition.

Our business exposes us to possible claims for property damage and bodily injury or death which may result if an engine, engine part or component, airframe part or accessory, or any other aviation product which we have sold, manufactured, or repaired fails, or if an aircraft we operated, serviced, or in which our products are installed, crashes. We carry substantial liability insurance in amounts that we believe are adequate for our risk exposure and commensurate with industry norms. However, claims may arise in the future, and our insurance coverage may not be adequate to protect us in all circumstances. Additionally, we might not be able to maintain adequate insurance coverage in the future at an acceptable cost. Any liability claim not covered by adequate insurance could adversely affect our results of operations and financial condition.

Our business could be negatively affected by cyber or other security threats or other disruptions.

Our businesses depend heavily on information technology and computerized systems to communicate and operate effectively. The Company's systems and technologies, or those of third parties on which we rely, could fail or become unreliable due to equipment failures, software viruses, cyber threats, terrorist acts, natural disasters, power failures or other causes. These threats arise in some cases as a result of our role as a defense contractor.

Cyber security threats are evolving and include, but are not limited to, malicious software, attempts to gain unauthorized access to our sensitive information, including our customers, suppliers, subcontractors, and joint venture partners, and other electronic security breaches that could lead to disruptions in mission critical systems, unauthorized release of confidential or otherwise protected information, and corruption of data.

Although we utilize various procedures and controls to monitor and mitigate these threats, there can be no assurance that these procedures and controls will be sufficient to prevent security threats from materializing. If any of these events were to materialize, the costs related to cyber or other security threats or disruptions may not be fully insured or indemnified and could have a material adverse effect on our reputation, operating results, and financial condition.

Moreover, expenditures incurred in implementing cyber security and other procedures and controls could adversely affect our results of operations and financial condition.

We must comply with extensive environmental requirements, and any exposure to environmental liabilities may adversely affect us.

Federal, state, and local requirements relating to the discharge and emission of substances into the environment, the disposal of hazardous wastes, the remediation and abatement of contaminants, and other

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activities affecting the environment have had and may continue to have an impact on our operations. Management cannot assess the possible effect of compliance with future environmental requirements or of future environmental claims for which we may not have adequate indemnification or insurance coverage. If we were required to pay the expenses related to any future environmental claims for which neither indemnification nor insurance coverage were available, these expenses could have an adverse impact on our results of operations and financial condition.

Future environmental regulatory developments in the United States and abroad concerning environmental issues, such as climate change, could adversely affect our operations and increase operating costs and, through their impact on our customers, reduce demand for our products and services. Actions may be taken in the future by the U.S. government, state governments within the United States, foreign governments, the International Civil Aviation Organization, or by signatory countries through a new global climate change treaty to regulate the emission of greenhouse gases by the aviation industry. The precise nature of any such requirements and their applicability to us and our customers are difficult to predict, but the impact to us and the aviation industry would likely be adverse and could be significant, including the potential for increased fuel costs, carbon taxes or fees, or a requirement to purchase carbon credits.

We may need to make significant capital expenditures to keep pace with technological developments in our industry.

The industries in which we participate are constantly undergoing development and change, and it is likely that new products, equipment, and methods of repair and overhaul services will be introduced in the future. We may need to make significant expenditures to purchase new equipment and to train our employees to keep pace with any new technological developments. These expenditures could adversely affect our results of operations and financial condition.

Our operations would be adversely affected by a shortage of skilled personnel or work stoppages.

We are dependent on an educated and highly skilled workforce because of the complex nature of many of our products and services. Furthermore, we have a collective bargaining agreement covering approximately 110 employees. Our ability to operate successfully and meet our customers' demands could be jeopardized if we are unable to attract and retain a sufficient number of skilled personnel, including qualified licensed mechanics, to conduct our business, or if we experience a significant or prolonged work stoppage. These and similar events may adversely affect our results of operations and financial condition.

ITEM 1B. UNRESOLVED STAFF COMMENTS

Not Applicable.

ITEM 2. PROPERTIES

In the Aviation Services segment, we conduct inventory management and distribution activities from our headquarters in Wood Dale, Illinois, which we own. In addition to warehouse space, this facility includes executive, sales and administrative offices. Our principal maintenance, repair, overhaul, and engineering activities for this segment are conducted at facilities leased by us in Indianapolis, Indiana; Oklahoma City, Oklahoma; Miami, Florida; Duluth, Minnesota; and Lake Charles, Louisiana.

We also lease facilities in Garden City, New York; Jacksonville, Florida; Brussels, Belgium; Singapore, Republic of Singapore; and London, England, and own a building near Schiphol International Airport in the Netherlands to support activities in the Aviation Services segment.

Our principal activities in the Expeditionary Services segment are conducted at facilities we lease in Melbourne, Florida and own in Cadillac, Michigan and Goldsboro, North Carolina.

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We also operate sales offices which support all our activities and are leased in London, England; Crawley, England; Paris, France; Rio de Janeiro, Brazil; Shanghai, China; Singapore, Republic of Singapore; and Abu Dhabi, UAE.

We believe that our owned and leased facilities are suitable and adequate for our operational requirements.

ITEM 3. LEGAL PROCEEDINGS

We are not a party to any material pending legal proceeding (including any governmental or environmental proceeding) other than routine litigation incidental to our business except for the following:

DynCorp International LLC v. AAR Airlift Group, Inc.

On November 5, 2015, AAR Airlift Group, Inc. ("AAR Airlift"), a wholly-owned subsidiary of AAR CORP. filed a motion to dismiss a First Amended Complaint filed by DynCorp International LLC ("DynCorp") alleging that AAR Airlift misappropriated DynCorp's trade secrets in connection with the submission of proposals pursuant to the solicitation issued by the Department of State Bureau of International Narcotics and Law Enforcement Affairs, Office of Aviation ("INL/A") in support of the Department of State's Worldwide Aviation Support Services ("WASS") program.

On January 14, 2016, the Court granted AAR Airlift's motion to dismiss the First Amended Complaint. On February 2, 2016, DynCorp filed an appeal to the United States Court of Appeals for the Eleventh Circuit with respect to the Court's order on the motion to dismiss and other orders issued by the Court in this case.

AAR Airlift will continue to defend itself vigorously against DynCorp's lawsuit and any attempt to invalidate or interfere with AAR Airlift's lawful participation in the INL/A contract award competition. As of the date of this filing and as described elsewhere, the Department of State has not yet awarded the INL/A contract.

OIG Investigation

The U.S. Department of State received and referred to its Office of Inspector General ("OIG") a May 2015 letter from DynCorp in which DynCorp made substantially the same allegations against AAR Airlift as set forth in both its original complaint and its First Amended Complaint. The OIG is investigating these allegations, and AAR Airlift is cooperating fully in that investigation.

For additional information about this lawsuit, please refer to the "Legal Proceedings" section of the Company's Quarterly Reports on Form 10-Q filed with respect to the quarters ended August 31, 2015 and November 30, 2015.

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable.

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Supplemental Item:

EXECUTIVE OFFICERS OF THE REGISTRANT

Information concerning each of our executive officers is set forth below:

Name	Age	Present Position with the Company
David P. Storch	63	Chairman, President and Chief Executive Officer, Director
Timothy J. Romenesko	59	Vice Chairman and Chief Operating Officer Expeditionary Services, Director
Michael J. Sharp	54	Vice President and Chief Financial Officer
Robert J. Regan	58	Vice President, General Counsel and Secretary
John Holmes	39	Chief Operating Officer Aviation Services
Eric S. Pachapa	43	Vice President, Controller and Chief Accounting Officer

Mr. Storch is Chairman of the Board, President and Chief Executive Officer of AAR, having served in that capacity since August 2015 and from 2005 to 2007. From 2007 to August 2015, Mr. Storch served as Chairman of the Board and Chief Executive Officer. From 1996 to 2005, Mr. Storch served as President and Chief Executive Officer and from 1989 to 1996 he served as Chief Operating Officer. Prior to that, Mr. Storch served as a Vice President of the Company from 1988 to 1989. Mr. Storch joined the Company in 1979 and also served as president of a major subsidiary from 1984 to 1988. Mr. Storch has been a director of the Company since 1989.

Mr. Romenesko is Vice Chairman and Chief Operating Officer Expeditionary Services, having served in that capacity since August 2015. From March 2015 to August 2015, Mr. Romenesko served as President and Chief Operating Officer Expeditionary Services. Previously, he served as President and Chief Operating Officer of the Company from 2007, and Vice President and Chief Financial Officer from 1994 to 2007. Mr. Romenesko also served as Controller from 1991 to 1995, and in various other positions since joining AAR in 1981. Mr. Romenesko has been a director of the Company since 2007.

Mr. Sharp is Vice President and Chief Financial Officer, having served in that capacity since October 2015. Mr. Sharp previously served as Vice President, Controller since July 1996 and Chief Accounting Officer since April 1999. Mr. Sharp was also acting Chief Financial Officer and Treasurer from October 2012 to July 2013. Prior to joining the Company, he was with Kraft Foods from 1994 to 1996, and with KPMG LLP from 1984 to 1994.

Mr. Regan is Vice President, General Counsel and Secretary, having served in that capacity since June 2009. From 2008 to June 2009, Mr. Regan served as Vice President and General Counsel and, prior to that, Associate General Counsel since joining AAR in February 2008. Prior to joining AAR, he was a partner at the law firm of Schiff Hardin LLP since 1989.

Mr. Holmes is Chief Operating Officer Aviation Services, having served in that capacity since February 2015. Mr. Holmes previously served as Group Vice President, Aviation Services Inventory Management and Distribution since 2012, General Manager and Division President of our Allen Asset Management business since 2003, and in various other positions since joining the Company in September 2001.

Mr. Pachapa is Vice President, Controller and Chief Accounting Officer, having served in that capacity since July 2016. Mr. Pachapa previously served as Controller since October 2015 and Senior Director of Accounting and Reporting since April 2014. Prior to joining the Company, he was with Glanbia plc from 2011 to 2014, and with Ernst & Young LLP from 1996 to 2011.

Each executive officer is elected annually by the Board of Directors at the first meeting of the Board held after the annual meeting of stockholders. Executive officers continue to hold office until their successors are duly elected or until their death, resignation, termination or reassignment.

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PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common stock is traded on the New York Stock Exchange and the Chicago Stock Exchange under the symbol "AIR." On June 30, 2016, there were approximately 996 holders of common stock, including participants in security position listings.

The following table shows the range of prices for our common stock and the amount of dividends declared per share during each quarter of our last two fiscal years:

Fiscal 2016

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Full Year
Market price					
High	$ 32.60	$ 24.56	$ 26.66	$ 24.61	$ 32.60
Low	23.51	18.69	18.93	21.00	18.69
Dividends declared	0.075	0.075	0.075	0.075	0.30

Fiscal 2015

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Full Year
Market price					
High	$ 28.33	$ 29.05	$ 31.93	$ 34.24	$ 34.24
Low	23.74	22.37	25.04	29.18	22.37
Dividends declared	0.075	0.075	0.075	0.075	0.30

Stockholder Return Performance Graph

The following graph compares the total return on a cumulative basis of $100 invested, and reinvestment of dividends in our common stock on May 31, 2011 to the Standard and Poor's ("S&P") 500 Index and the Proxy Peer Groups.

Comparison of Cumulative Five Year Total Return

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The S&P 500 Index is comprised of domestic industry leaders in four major sectors: Industrial, Financial, Utility, and Transportation, and serves as a broad indicator of the performance of the U.S. equity market. The Fiscal 2016 Proxy Peer Group companies are listed as follows:

Aerojet Rocketdyne Holdings, Inc.
Barnes Group Inc.[1]
CACI International Inc[1]
Crane Co.
Cubic Corporation
Curtiss-Wright Corporation
Esterline Technologies Corporation
Heico Corporation[1]
Hexcel Corporation
Kaman Corporation
KLX Inc.[1]
Moog Inc.
Rockwell Collins, Inc.
Science Application International Corporation[1]
Teledyne Technologies Incorporated
TransDigm Group Incorporated
Triumph Group, Inc.
Wesco International, Inc.
Woodward, Inc.

1 These companies are new peer group companies added during fiscal 2016.

Applied Industrial Technologies, Inc., B/E Aerospace, Inc., Kratos Defense & Security Solutions, Inc., Orbital ATK, Inc., and Spirit AeroSystems Holdings, Inc. are no longer included in our Proxy Peer Group. The Company annually revisits the composition of the peer group to ensure that the Company's performance is measured against those of comparably-sized and situated companies. The mix of the Company's commercial and defense businesses presents a challenge in constructing a peer group, given that many defense contractors have substantially greater resources than the Company.

Issuer Purchases of Equity Securities

The following table provides information about purchases we made during the quarter ended May 31, 2016 of equity securities that are registered by us pursuant to Section 12 of the Exchange Act:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs[1]	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs[1]
3/1/2016 - 3/31/2016	20,000	$ 22.65	20,000	
4/1/2016 - 4/30/2016	41,000	23.33	41,000	
5/1/2016 - 5/31/2016				
Total	61,000	$ 23.11	61,000	$ 82,687,485

1 On March 16, 2015, we announced a Board of Directors authorization to purchase up to $250 million of our common stock with no expiration date.

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ITEM 6. SELECTED FINANCIAL DATA
(In millions, except per share amounts)

	For the Year Ended May 31,				
	2016	2015	2014	2013	2012
RESULTS OF OPERATIONS					
Sales	$ 1,662.6	$ 1,594.3	$ 1,709.1	$ 1,807.9	$ 1,865.7
Gross profit[1]	236.9	159.3	288.9	259.5	287.7
Operating income (loss)[1]	65.8	(11.9)	125.6	102.2	118.4
Loss on extinguishment of debt[2]	(0.4)	(44.9)		(0.3)	(0.7)
Interest expense	6.4	26.5	28.3	29.1	30.2
Income (Loss) from continuing operations	40.5	(54.5)	67.2	48.8	64.9
Income from discontinued operations[3]	7.2	64.7	5.7	6.2	2.8
Net income attributable to AAR	47.7	10.2	72.9	55.0	67.7
Share data:					
Earnings per share basic:					
Earnings (Loss) from continuing operations	$ 1.16	$ (1.40)	$ 1.70	$ 1.23	$ 1.61
Earnings from discontinued operations	0.21	1.66	0.15	0.15	0.07
Earnings per share basic	$ 1.37	$ 0.26	$ 1.85	$ 1.38	$ 1.68
Earnings per share diluted:					
Earnings (Loss) from continuing operations	$ 1.16	$ (1.40)	$ 1.68	$ 1.23	$ 1.58
Earnings from discontinued operations	0.21	1.64	0.15	0.15	0.07
Earnings per share diluted	$ 1.37	$ 0.24	$ 1.83	$ 1.38	$ 1.65
Cash dividends declared per share	$ 0.30	$ 0.30	$ 0.30	$ 0.30	$ 0.30
Weighted average common shares outstanding basic	34.4	39.1	38.6	38.3	38.8
Weighted average common shares outstanding diluted	34.6	39.4	39.1	40.6	43.1

	May 31,				
	2016	2015	2014	2013	2012
FINANCIAL POSITION[5]					
Total cash and cash equivalents	$ 31.2	$ 54.7	$ 89.2	$ 75.3	$ 67.7
Working capital	544.1	483.8	684.7	626.7	567.5
Total assets	1,442.1	1,454.1	2,159.8	2,107.0	2,163.1
Total debt[2]	150.1	154.0	634.0	708.6	792.2
Equity[4]	865.8	845.1	1,000.7	919.5	866.0

Number of shares outstanding at end of year[4]		34.5		35.4		39.6		39.4		40.3
Book value per share of common stock	$	25.10	$	23.87	$	25.27	$	23.34	$	21.50

Notes:

1 In fiscal 2015, we recognized $71.4 million in impairment charges and other losses related to product lines and inventories identified as underperforming or not part of our strategy going forward. These actions included aircraft in our aircraft lease portfolio, inventory in our supply chain and MRO operations, and certain aircraft and inventory in our expeditionary airlift business.

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In fiscal 2013, we recorded a $29.8 million charge due to lower revenue and profit expectations on a contract supporting the KC10 aircraft as a result of lower than expected flight hours of the KC10 aircraft and changes to our anticipated recovery of costs in excess of amounts billed within this contract.

2

In fiscal 2015, we redeemed our $325 million 7.25% Senior Notes due 2022 for $370.6 million. We recognized a loss on extinguishment of debt of $44.9 million comprised of a make-whole premium of $45.6 million and unamortized deferred financing costs of $6.2 million, partially offset by an unamortized net premium of $6.9 million.

3

In fiscal 2015, we sold our Telair Cargo Group for $725 million resulting in a $198.6 million pre-tax gain. We also recognized impairment charges of $57.5 million in fiscal 2015 to reduce the carrying value of Precision Systems Manufacturing business's net assets to their expected value at the time of sale.

In fiscal 2016, we received contingent consideration from the sale of Telair Cargo Group and recognized a pre-tax gain of $27.7 million.

4

On May 29, 2015, we repurchased 4,185,960 shares of our common stock at a price of $31.90 per share pursuant to a tender offer utilizing $133.5 million cash on hand. Fees and expenses of $1.2 million were incurred related to the tender offer and were recorded in treasury stock.

5

The Financial Position data has been recast to reflect the retrospective adoption of Accounting Standards Update ("ASU") No. 2015-03, *Simplifying the Presentation of Debt Issuance Costs*. This ASU was adopted in the fourth quarter of fiscal 2016 and amends existing guidance to require the presentation of debt issuance costs in the balance sheet as a deduction from the carrying amount of the related debt liability instead of a deferred charge. The Financial Position data has also been recast to reflect the retrospective adoption of ASU No. 2015-17, *Balance Sheet Classification of Deferred Taxes*. This ASU was adopted in the fourth quarter of fiscal 2016 and amends existing guidance to require the presentation of deferred tax liabilities and assets as noncurrent within a classified statement of financial position.

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ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Dollars in millions)

Forward-Looking Statements

Management's Discussion and Analysis of Financial Condition and Results of Operations contain certain statements relating to future results, which are forward-looking statements as that term is defined in the Private Securities Litigation Reform Act of 1995. These forward-looking statements are based on the beliefs of management, as well as assumptions and estimates based on information available to us as of the dates such assumptions and estimates are made, and are subject to certain risks and uncertainties that could cause actual results to differ materially from historical results or those anticipated, depending on a variety of factors, including those factors discussed under Item 1A, "Risk Factors." Should one or more of those risks or uncertainties materialize adversely, or should underlying assumptions or estimates prove incorrect, actual results may vary materially from those described. Those events and uncertainties are difficult or impossible to predict accurately and many are beyond our control. We assume no obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements or to reflect the occurrence of anticipated or unanticipated events.

General Overview

During fiscal 2015, we executed on a comprehensive strategic plan that included:

- The sale of our Telair Cargo Group for cash of $714 million, resulting in pre-tax gains of $198.6 million in the fourth quarter of fiscal 2015 (and $27.7 million in the first quarter of fiscal 2016 from the receipt of contingent consideration);
- A decision to divest our Precision Systems Manufacturing business;
- The exit of certain product lines and inventories in our aviation services businesses that were underperforming or not part of our strategy going forward;
- The reduction of our total debt by $480 million;
- The return of capital to shareholders through $151.5 million in common stock repurchases and $12.5 million of dividends.

The divestiture of these manufacturing businesses allowed us to narrow our strategy to focus on our best in class aviation and expeditionary services. In fiscal 2016, our Aviation Services segment succeeded in expanding existing customer relationships in distribution and securing new program work with multiple international carriers. In our Expeditionary Services segment, we have completed the successful start-up of our new contract with the U.K. Ministry of Defense providing search and rescue services in the Falkland Islands.

As we enter fiscal 2017, we remain in a strong financial position to further execute on our strategy as a best in class aviation and expeditionary services company. Our cash on hand plus unused capacity on our Revolving Credit Facility was $409 million at May 31, 2016. We expect to invest opportunistically in expanding our comprehensive suite of services to the global commercial aviation and government and defense markets.

We report our activities in two business segments: Aviation Services and Expeditionary Services.

The Aviation Services segment consists of businesses that provide spares and maintenance support for aircraft operated by our commercial and government/defense customers. Sales in the Aviation Services segment are derived from the sale and lease of a wide variety of new, overhauled and repaired engine and airframe parts and components to the commercial aviation and government and defense markets. We provide customized inventory supply chain management, performance based logistics programs, aircraft

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component repair management services, and aircraft modifications. The segment also includes repair, maintenance and overhaul of aircraft, landing gear and components. We also sell and lease used commercial aircraft (exclusively through joint ventures following the sale of our last two wholly-owned aircraft in the fourth quarter of fiscal 2015). Cost of sales consists principally of the cost of product, direct labor, and overhead.

The Expeditionary Services segment consists of businesses that provide products and services supporting the movement of equipment and personnel by the U.S. Department of Defense ("DoD"), foreign governments and non-governmental organizations. Sales in the Expeditionary Services segment are derived from the delivery of airlift services to mostly government and defense customers and the design and manufacture of pallets, shelters, and containers used to support the U.S. military's requirements for a mobile and agile force. We also provide system integration services for specialized command and control systems. Cost of sales consists principally of aircraft maintenance costs, depreciation, the cost of material to manufacture products, direct labor and overhead.

Our chief operating decision making officer (Chief Executive Officer) evaluates performance based on the reportable segments and utilizes gross profit as a primary profitability measure. Gross profit is calculated by subtracting cost of sales from sales. The assets and certain expenses related to corporate activities are not allocated to the segments. Our reportable segments are aligned principally around differences in products and services.

Business Trends and Outlook for Fiscal 2017

Consolidated sales for fiscal 2016 increased $68.3 million or 4.3% compared to the prior year primarily due to an increase in sales of $108.9 million or 8.3% in our Aviation Services segment. This growth was driven by higher volumes in distribution of $58.6 million and increased MRO sales of $53.2 million partially offset by lower demand in aftermarket parts trading of $34.2 million. Sales in the Expeditionary Services segment decreased $40.6 million or 14.6% from the prior year period due to lower demand for mobility products as the DoD reduced its purchases of these products due to reduced troop activity.

For fiscal 2017, we expect to see continued strength in our Aviation Services segment given its strong positions in the growing global aviation market. We believe there continues to be a favorable trend by both commercial and government and defense customers for comprehensive supply chain and maintenance programs, as these customers continue to seek ways to reduce their operating cost structure. While defense budgets are expected to remain under pressure due to budgetary constraints and the current geopolitical environment, we see ongoing demand for our low cost solutions, services, and products in our Expeditionary Services segment.

For the fiscal 2017, we expect the Company's consolidated sales in the range of $1.7 billion to $1.8 billion. Diluted earnings per share from continuing operations for fiscal 2017 is expected to be in the range of $1.30 to $1.40.

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Results of Operations Fiscal 2016 Compared with Fiscal 2015

Sales and gross profit for our two business segments for the two years ended May 31, 2016 and 2015 were as follows:

	For the Year Ended May 31,		
	2016	2015	% Change
Sales:			
Aviation Services			
Commercial	$ 1,003.5	$ 985.7	1.8%
Defense	421.5	330.4	27.6%
	$ 1,425.0	$ 1,316.1	8.3%
Expeditionary Services			
Commercial	$ 16.5	$ 18.8	(12.2)%
Defense	221.1	259.4	(14.8)%
	$ 237.6	$ 278.2	(14.6)%

	For the Year Ended May 31,		
	2016	2015	% Change
Gross Profit:			
Aviation Services			
Commercial	$ 157.5	$ 93.5	68.4%
Defense	72.3	50.3	43.7%
	$ 229.8	$ 143.8	59.8%
Expeditionary Services			
Commercial	$ (0.1)	$ 1.5	(106.7)%
Defense	7.2	14.0	(48.6)%
	$ 7.1	$ 15.5	(54.2)%

Aviation Services Segment

Sales in the Aviation Services segment increased $108.9 million or 8.3% over the prior year due to a $91.1 million or 27.6% increase in sales to government and defense customers. The increase in sales to government and defense customers was primarily attributable to increased volumes in both programs of $59.0 million and distribution of $27.5 million largely from the continued ramp up of programs announced in the second half of fiscal 2014.

During fiscal 2016, sales in this segment to commercial customers increased $17.8 million or 1.8% over the prior year primarily due to higher MRO sales of $49.8 million and higher volumes in distribution of $31.2 million. These increases were partially offset by lower demand in aftermarket parts trading of $37.2 million. In fiscal 2015, we sold our last two wholly-owned aircraft for $11.0 million.

Cost of sales in Aviation Services increased $22.9 million or 2.0% over the prior year primarily due to growth in sales volume partially offset by charges and other actions in fiscal 2015 that did not occur in fiscal 2016, including that in fiscal 2015 (i) we recognized an impairment charge of $19.5 million for rotable assets and inventory supporting certain product lines we exited in our landing gear business, (ii) we sold our last two remaining wholly-owned aircraft in our aircraft leasing portfolio resulting in a loss of $14.8 million, and (iii) we took actions to address underperforming inventories and equipment available for lease resulting in losses in the fourth quarter of fiscal 2015 of $24.0 million.

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Gross profit in the Aviation Services segment increased $86.0 million or 59.8% over the prior year. Gross profit on sales to commercial customers increased $64.0 million or 68.4% over the prior year primarily driven by the fiscal 2015 charges and other actions discussed above. The gross profit margin on sales to commercial customers increased to 15.7% compared to 9.5% in the prior year which was also attributable to the fiscal 2015 actions discussed above.

Gross profit in this segment on sales to government and defense customers increased $22.0 million or 43.7% over the prior year with programs contributing the majority of the increase. Gross profit margin increased from 15.2% to 17.2% primarily due to these increased volumes.

Since 2009, we have served as a subcontractor providing supply chain services and logistics support for the prime contractor on the KC10 Extender Contractor Logistics Support Program ("KC10 Program"). In February 2016, we submitted our final bid on the new KC10 Program contract, and in June 2016, the U.S. Air Force awarded the contract to a competitor. We have filed a protest with the U.S. Government Accountability Office. Due to the pending protest and the routine transition period of the services to the new provider, we expect to continue to provide KC10 logistics services through late fiscal 2017. Average annual revenue and gross profit recognized over the last three years for our KC10 logistics support services was $115.9 million and $7.4 million, respectively.

Expeditionary Services Segment

Sales in the Expeditionary Services segment decreased $40.6 million or 14.6% from the prior year period. The decrease in sales was driven by a decrease of $40.7 million due to lower demand for mobility products as the DoD reduced its purchases of these products due to reduced troop activity.

Cost of sales in Expeditionary Services decreased $32.2 million or 12.3% from the prior year primarily due to the decrease in sales volume and by charges and other actions in fiscal 2015 that did not occur in fiscal 2016. Fiscal 2015 cost of sales included impairment charges of $8.9 million related to expeditionary airlift services for inventory, rotable assets and aircraft.

Gross profit in the Expeditionary Services segment decreased $8.1 million or 54.2% from the prior year period. Lower sales of mobility products decreased gross profit $8.5 million.

Selling, General and Administrative Expenses and Earnings from Aircraft Joint Ventures

Selling, general and administrative expenses decreased $0.6 million in fiscal 2016 or 0.4% from the prior year as fiscal 2015 included asset impairment charges on corporate assets of $3.5 million and severance costs of $1.7 million which did not occur in fiscal 2016. Incremental investments in business development activities in fiscal 2016 partially offset the benefit of the non-recurring fiscal 2015 costs.

Loss on Extinguishment of Debt and Interest Expense

On April 30, 2015, we redeemed our $325 million 7.25% Senior Notes due 2022 for $370.6 million. We recognized a loss on extinguishment of debt of $44.9 million comprised of a make-whole premium of $45.6 million and unamortized deferred financing costs of $6.2 million, partially offset by an unamortized net premium of $6.9 million. Interest expense decreased $20.1 million in fiscal 2016 primarily as a result of the redemption of the Senior Notes.

Income Taxes

Our fiscal 2016 effective income tax rate for continuing operations was 31.7% compared to 34.3% in the prior year period. The effective income tax rate for fiscal 2016 includes a benefit of $2.5 million related to the correction of prior year immaterial errors.

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Results of Operations Fiscal 2015 Compared with Fiscal 2014

Sales and gross profit for our two business segments for the two years ended May 31, 2015 and 2014 were as follows:

	For the Year Ended May 31, 2015	2014	% Change
Sales:			
Aviation Services			
Commercial	$ 985.7	$ 919.9	7.2%
Defense	330.4	311.3	6.1%
	$ 1,316.1	$ 1,231.2	6.9%
Expeditionary Services			
Commercial	$ 18.8	$ 11.7	60.7%
Defense			