

LOCKHEED MARTIN CORP
Form 10-Q
October 27, 2011
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

Quarterly Report Pursuant To Section 13 or 15(d)

of the Securities Exchange Act of 1934

For the quarterly period ended September 25, 2011

Commission File Number: 1-11437

LOCKHEED MARTIN CORPORATION

(Exact name of registrant as specified in its charter)

Maryland
(State or other jurisdiction of

52-1893632
(I.R.S. Employer Identification Number)

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incorporation or organization)

6801 Rockledge Drive, Bethesda, MD
(Address of principal executive offices)

(301) 897-6000

20817
(Zip Code)

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES NO

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES NO

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

Large Accelerated Filer Accelerated Filer Non-Accelerated Filer Smaller Reporting Company

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

| Class | Outstanding as of September 25, 2011 |
|---------------------------------------|--------------------------------------|
| Common stock, \$1 par value per share | 323,570,483 |

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LOCKHEED MARTIN CORPORATION

FORM 10-Q

FOR THE QUARTER ENDED SEPTEMBER 25, 2011

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Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****Lockheed Martin Corporation****Unaudited Condensed Consolidated Statements of Earnings**

| | Quarter Ended | | Nine Months Ended | |
|---|---|-----------------------|-----------------------|-----------------------|
| | September 25, 2011 | September 26, 2010 | September 25, 2011 | September 26, 2010 |
| | <i>(In millions, except per share data)</i> | | | |
| Net Sales | | | | |
| Products | \$ 9,680 | \$ 8,948 | \$ 27,293 | \$ 26,269 |
| Services | 2,439 | 2,395 | 6,995 | 6,641 |
| Total net sales | 12,119 | 11,343 | 34,288 | 32,910 |
| Cost of Sales | | | | |
| Products | (8,667) | (8,017) | (24,361) | (23,469) |
| Services | (2,138) | (2,156) | (6,241) | (6,003) |
| Severance charges | (39) | (178) | (136) | (178) |
| Other unallocated corporate costs | (279) | (203) | (834) | (529) |
| Total cost of sales | (11,123) | (10,554) | (31,572) | (30,179) |
| Gross profit | 996 | 789 | 2,716 | 2,731 |
| Other income, net | 45 | 88 | 182 | 203 |
| Operating Profit | 1,041 | 877 | 2,898 | 2,934 |
| Interest expense | (89) | (85) | (258) | (258) |
| Other non-operating income (expense), net | (3) | 37 | 25 | 46 |
| Earnings from continuing operations before income taxes | 949 | 829 | 2,665 | 2,722 |
| Income tax expense | (284) | (272) | (696) | (929) |
| Net earnings from continuing operations | 665 | 557 | 1,969 | 1,793 |
| Net earnings from discontinued operations | 35 | 3 | 3 | 124 |
| Net Earnings | \$ 700 | \$ 560 | \$ 1,972 | \$ 1,917 |
| Earnings Per Common Share | | | | |
| Basic | | | | |
| Continuing operations | \$ 2.01 | \$ 1.55 | \$ 5.78 | \$ 4.88 |
| Discontinued operations | .11 | .01 | .01 | .34 |
| Basic earnings per common share | \$ 2.12 | \$ 1.56 | \$ 5.79 | \$ 5.22 |

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| | | | | |
|---|---------|---------|---------|---------|
| Diluted | | | | |
| Continuing operations | \$ 1.99 | \$ 1.53 | \$ 5.72 | \$ 4.84 |
| Discontinued operations | .11 | .01 | .01 | .33 |
| Diluted earnings per common share | \$ 2.10 | \$ 1.54 | \$ 5.73 | \$ 5.17 |
| Cash Dividends Paid Per Common Share | \$.75 | \$.63 | \$ 2.25 | \$ 1.89 |

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

Table of Contents**Lockheed Martin Corporation****Unaudited Condensed Consolidated Balance Sheets**

| | September 25, 2011 | December 31, 2010 |
|---|---|----------------------|
| | <i>(In millions, except per share data)</i> | |
| Assets | | |
| Current assets | | |
| Cash and cash equivalents | \$ 4,564 | \$ 2,261 |
| Short-term investments | 3 | 516 |
| Receivables, net | 6,523 | 5,692 |
| Inventories | 1,789 | 2,363 |
| Deferred income taxes | 1,184 | 1,147 |
| Other current assets | 606 | 518 |
| Assets of discontinued operation held for sale | | 396 |
| Total current assets | 14,669 | 12,893 |
| Property, plant and equipment, net | 4,428 | 4,554 |
| Goodwill | 9,606 | 9,605 |
| Deferred income taxes | 3,096 | 3,485 |
| Other assets | 4,388 | 4,576 |
| Total assets | \$ 36,187 | \$ 35,113 |
| Liabilities and Stockholders' Equity | | |
| Current liabilities | | |
| Accounts payable | \$ 2,328 | \$ 1,627 |
| Customer advances and amounts in excess of costs incurred | 5,544 | 5,890 |
| Salaries, benefits and payroll taxes | 1,800 | 1,870 |
| Current portion of long-term debt | 500 | |
| Other current liabilities | 1,972 | 1,810 |
| Liabilities of discontinued operation held for sale | | 204 |
| Total current liabilities | 12,144 | 11,401 |
| Long-term debt, net | 6,538 | 5,019 |
| Accrued pension liabilities | 9,979 | 10,607 |
| Other postretirement benefit liabilities | 1,254 | 1,213 |
| Other liabilities | 3,329 | 3,376 |
| Total liabilities | 33,244 | 31,616 |
| Stockholders' equity | | |
| Common stock, \$1 par value per share | 321 | 346 |
| Additional paid-in capital | | |
| Retained earnings | 11,189 | 12,161 |
| Accumulated other comprehensive loss | (8,567) | (9,010) |
| Total stockholders' equity | 2,943 | 3,497 |
| Total liabilities and stockholders' equity | \$ 36,187 | \$ 35,113 |

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

Table of Contents**Lockheed Martin Corporation****Unaudited Condensed Consolidated Statements of Cash Flows**

| | Nine Months Ended | |
|--|-----------------------|-----------------------|
| | September 25, 2011 | September 26, 2010 |
| | (In millions) | |
| Operating Activities | | |
| Net earnings | \$ 1,972 | \$ 1,917 |
| Adjustments to reconcile net earnings to net cash provided by operating activities | | |
| Depreciation and amortization of plant and equipment | 524 | 539 |
| Amortization of purchased intangibles | 60 | 74 |
| Stock-based compensation | 116 | 100 |
| Deferred income taxes | 178 | 354 |
| Severance charges | 136 | 178 |
| Reduction in tax expense from resolution of certain tax matters | (89) | |
| Tax benefit related to discontinued operations | (81) | (96) |
| Tax expense related to Medicare Part D reimbursement | | 96 |
| Changes in operating assets and liabilities | | |
| Receivables, net | (853) | (483) |
| Inventories | 575 | 60 |
| Accounts payable | 707 | 354 |
| Customer advances and amounts in excess of costs incurred | (342) | 26 |
| Postretirement benefit plans | 134 | (344) |
| Income taxes | 7 | 161 |
| Other, net | (6) | 451 |
| Net cash provided by operating activities | 3,038 | 3,387 |
| Investing Activities | | |
| Expenditures for property, plant and equipment | (443) | (394) |
| Net cash provided by (used for) short-term investment transactions | 510 | (421) |
| Other, net | 270 | (52) |
| Net cash provided by (used for) investing activities | 337 | (867) |
| Financing Activities | | |
| Issuance of long-term debt, net of related costs | 1,980 | |
| Repurchases of common stock | (2,317) | (1,566) |
| Common stock dividends | (770) | (700) |
| Issuances of common stock and related amounts | 90 | 57 |
| Other | (46) | (47) |
| Net cash used for financing activities | (1,063) | (2,256) |
| Effect of exchange rate changes on cash and cash equivalents | (9) | 1 |
| Net increase in cash and cash equivalents | 2,303 | 265 |
| Cash and cash equivalents at beginning of period | 2,261 | 2,391 |
| Cash and cash equivalents at end of period | \$ 4,564 | \$ 2,656 |

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

Table of Contents**Lockheed Martin Corporation****Unaudited Condensed Consolidated Statements of Stockholders' Equity**

| | Common Stock | Additional Paid-in Capital | Retained Earnings | Accumulated Other Comprehensive Loss | Total Stockholders Equity |
|---|-------------------------|---|------------------------------|---|--|
| | <i>(In millions)</i> | | | | |
| Balance at December 31, 2009 | \$ 373 | \$ | \$ 12,351 | \$ (8,595) | \$ 4,129 |
| Cumulative effect of a change in accounting principle (Note 1) | | | (163) | | (163) |
| Balance at December 31, 2009, as adjusted | 373 | | 12,188 | (8,595) | 3,966 |
| Net earnings | | | 1,917 | | 1,917 |
| Repurchases of common stock | (20) | (375) | (1,171) | | (1,566) |
| Common stock dividends declared | | | (973) | | (973) |
| Stock-based awards and ESOP activity | 5 | 375 | | | 380 |
| Other comprehensive income | | | | 352 | 352 |
| Balance at September 26, 2010 | \$ 358 | \$ | \$ 11,961 | \$ (8,243) | \$ 4,076 |
| Balance at December 31, 2010 | \$ 346 | \$ | \$ 12,372 | \$ (9,010) | \$ 3,708 |
| Cumulative effect of a change in accounting principle (Note 1) | | | (211) | | (211) |
| Balance at December 31, 2010, as adjusted | 346 | | 12,161 | (9,010) | 3,497 |
| Net earnings | | | 1,972 | | 1,972 |
| Repurchases of common stock | (30) | (387) | (1,846) | | (2,263) |
| Common stock dividends declared | | | (1,098) | | (1,098) |
| Stock-based awards and ESOP activity | 5 | 387 | | | 392 |
| Other comprehensive income | | | | 443 | 443 |
| Balance at September 25, 2011 | \$ 321 | \$ | \$ 11,189 | \$ (8,567) | \$ 2,943 |

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

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Lockheed Martin Corporation

Notes to Unaudited Condensed Consolidated Financial Statements

NOTE 1 BASIS OF PRESENTATION

We prepared the condensed consolidated financial statements in this Form 10-Q in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. We followed the accounting policies used and disclosed in the consolidated financial statements included in our Form 10-K for the year ended December 31, 2010 (2010 Form 10-K) filed with the Securities and Exchange Commission, except as described below.

We close our books and records on the Sunday prior to the end of the calendar quarter to align our financial closing with our business processes. The interim financial statements and tables of financial information included herein are labeled based on that convention. This practice only affects interim periods, as our fiscal years end on December 31.

The interim financial information in this Form 10-Q reflects all adjustments, consisting of normal recurring adjustments, except as otherwise disclosed, necessary for a fair presentation of our results of operations for the interim periods presented. We have reclassified certain amounts in prior periods to conform to the current year presentation. The results of operations for the quarter or nine months ended September 25, 2011 are not necessarily indicative of results to be expected for the full year. Unless otherwise noted, we present all per share amounts cited in these consolidated financial statements on a per diluted share basis from continuing operations.

Change in Accounting Principle

On January 1, 2011, we changed the way we account for our services contracts with the U.S. Government. We now recognize sales on those contracts using the percentage-of-completion (POC) method that we use on our product contracts with the U.S. Government, such that approximately 95% of our sales are recognized under the POC method. All prior period amounts have been adjusted to reflect the new method of accounting.

The effect of this change in accounting was not material to our consolidated results of operations or financial position for any period, including the quarters and nine months ended September 25, 2011 and September 26, 2010, and did not impact cash flows. We reduced retained earnings by \$211 million at December 31, 2010 to reflect the cumulative effect of adopting the new method. This adjustment reflects the inception-to-date timing differences between the two methods. Specifically, under the POC method, we typically record sales based on costs incurred and an estimated profit margin instead of recording sales ratably over the contract period. We record a loss on a contract in the period it is determined to be probable rather than recording a loss each period over the contract life, and recognize expected award fees over the contract period instead of when notified by the customer of the amount awarded.

We believe the POC method is preferable to the service accounting method we previously used, as consistent sales recognition for all contracts with the U.S. Government better reflects the underlying economics of those contracts and aligns our financial reporting with other companies in our industry. We classify net sales as products or services on our Statements of Earnings based on the attributes of the underlying contracts.

Adoption of New Accounting Standard

On January 1, 2011, we prospectively adopted a new accounting standard that revised accounting guidance related to sales arrangements with multiple deliverables. This standard potentially applies to new or materially modified contracts that are not accounted for under the POC method described above. The adoption did not have a material effect on our financial results in the quarter and nine months ended September 25, 2011, and is not expected to have a material effect in future periods.

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Lockheed Martin Corporation

Notes to Unaudited Condensed Consolidated Financial Statements (continued)

NOTE 2 CERTAIN MATTERS INCLUDED IN EARNINGS

Severance Charges

During the quarter and nine months ended September 25, 2011, we recorded severance charges totaling \$39 million and \$136 million, net of state tax benefits. The severance charges recorded in the third quarter of 2011 related to our Information Systems & Global Solutions (IS&GS) business segment and Corporate Headquarters. In the second quarter of 2011, we recorded severance charges totaling \$97 million, net of state tax benefits, of which \$49 million and \$48 million related to our Aeronautics and Space Systems business segments. These charges reduced our net earnings in the third quarter by \$25 million (\$.07 per share) and for the nine-month period by \$88 million (\$.25 per share). The charges consisted of severance costs associated with the planned elimination of certain positions through either voluntary or involuntary actions. Upon separation, terminated employees will receive lump-sum severance payments based on years of service, which are expected to be paid through the first half of 2012.

These severance actions resulted from a strategic review of these businesses and our Corporate Headquarters to better align our organization and cost structure with changing economic conditions. The workforce reductions at the business segments also reflect changes in program lifecycles, where several of our major programs are transitioning out of development and into production, and certain programs are ending. In the third quarter of 2011, we made approximately half of the severance payments associated with the severance charge related to Space Systems. As of September 25, 2011, no other significant payments associated with the severance actions noted above have been made.

In the third quarter of 2010, we recorded a severance charge of \$178 million, net of state income tax benefits, related to the Voluntary Executive Separation Program (VESP). The charge, which included lump-sum special payments for qualifying executives, reduced our net earnings by \$116 million (\$.32 per share for the third quarter and \$.31 per share for the nine-month period). The effective date of termination of employment for most participants was February 1, 2011, with the lump-sum special payments to be made within 90 days from separation of service. As of September 25, 2011, substantially all payments under the VESP have been made.

Income Tax Items

In April 2011, the U.S. Congressional Joint Committee on Taxation completed its review of the Internal Revenue Service (IRS) Appeals Division's resolution of certain adjustments related to our tax years 2003-2008. As a result, during the second quarter of 2011, we recorded a reduction in our income tax expense of \$89 million (\$.26 per share for the nine months ended September 25, 2011), through the elimination of liabilities for unrecognized tax benefits. The remaining balance of our unrecognized tax benefits as of September 25, 2011 is not material.

In March 2010, the President signed into law the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010. Beginning January 1, 2013, these laws change the tax treatment for retiree prescription drug expenses by eliminating the tax deduction available to the extent that those expenses are reimbursed under Medicare Part D. Because the tax benefits associated with these future deductions were reflected as deferred tax assets, the elimination of the tax deductions resulted in a reduction in deferred tax assets and an increase in income tax expense for the first quarter of 2010 of \$96 million (\$.26 per share for the nine months ended September 26, 2010).

Table of Contents**Lockheed Martin Corporation****Notes to Unaudited Condensed Consolidated Financial Statements (continued)****NOTE 3 DISCONTINUED OPERATIONS**

During the third quarter of 2011, we committed to a plan to sell Savi Technology, Inc. (Savi), a logistics business within our Electronic Systems business segment. The operating results of Savi are included in discontinued operations on our Statements of Earnings for all periods presented, as we believe that the sale of Savi within the next twelve months is probable. The assets and liabilities of Savi have not been classified as held for sale on our September 25, 2011 Balance Sheet, as the amounts are not material.

In June 2010, we announced plans to divest Pacific Architects and Engineers, Inc. (PAE) and most of our Enterprise Integration Group (EIG), two businesses within our IS&GS business segment. In November 2010, we closed on the sale of EIG. In April 2011, we closed on the sale of PAE for cash and the beneficial interest in certain receivables. Additional amounts related to the completion of certain post-closing items, such as working capital adjustments, may be recorded in discontinued operations in periods subsequent to the sale dates. EIG's operating results are included in discontinued operations on our Statements of Earnings for the quarter and nine months ended September 26, 2010. PAE's operating results are included in discontinued operations on our Statements of Earnings for the quarter and nine months ended September 26, 2010 and through the date of sale in 2011. PAE's assets and liabilities are classified as held for sale on our December 31, 2010 Balance Sheet.

As a result of our decision to sell PAE and Savi, we were required to record deferred tax assets to reflect the tax benefit that we expected to realize on the sale of those businesses because our tax basis was higher than our book basis. Accordingly, we recorded a \$15 million deferred tax asset in the first quarter of 2011 and a \$96 million deferred tax asset in the second quarter of 2010 related to PAE, and we recorded a \$66 million deferred tax asset in the third quarter of 2011 related to Savi. These amounts are included in Adjustments from planned sale of businesses in the table below, which also includes other charges associated with Savi in the third quarter of 2011 and the sale of PAE that were incurred in the quarter and nine months ended September 25, 2011.

In the following table, we have combined the results of operations of PAE, EIG, and Savi, as the amounts for the individual businesses are not material. Summary financial information related to discontinued operations is as follows:

| | Quarter Ended | | Nine Months Ended | |
|---|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 25, 2011 | September 26, 2010 | September 25, 2011 | September 26, 2010 |
| | <i>(In millions)</i> | | | |
| Net sales | \$ 17 | \$ 285 | \$ 184 | \$ 932 |
| Earnings (loss) before income taxes | \$ (4) | \$ 6 | \$ (35) | \$ 45 |
| Earnings (loss) after income taxes | \$ (2) | \$ 3 | \$ (24) | \$ 28 |
| Adjustments from planned sale of businesses | 37 | | 27 | 96 |
| Net earnings from discontinued operations | \$ 35 | \$ 3 | \$ 3 | \$ 124 |

The major classes of assets and liabilities related to PAE and classified as held for sale on our December 31, 2010 Balance Sheet consisted of the following: receivables, net of \$253 million, goodwill and other assets of \$143 million, accounts payable and accrued expenses of \$125 million, and other liabilities of \$79 million.

Table of Contents**Lockheed Martin Corporation****Notes to Unaudited Condensed Consolidated Financial Statements (continued)****NOTE 4 EARNINGS PER COMMON SHARE**

We compute basic and diluted earnings per share amounts based on net earnings for the periods presented. We use the weighted average number of common shares outstanding during the period to calculate basic earnings per share. Our calculation of diluted per share amounts includes the dilutive effects of stock options and restricted stock units based on the treasury stock method. Basic and diluted weighted average shares outstanding were as follows:

| | Quarter Ended | | Nine Months Ended | |
|--|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 25, 2011 | September 26, 2010 | September 25, 2011 | September 26, 2010 |
| | <i>(In millions)</i> | | | |
| Average number of common shares outstanding for basic computations | 329.8 | 360.1 | 340.4 | 367.1 |
| Dilutive stock options and restricted stock units | 3.8 | 3.8 | 3.9 | 4.0 |
| Average number of common shares outstanding for diluted computations | 333.6 | 363.9 | 344.3 | 371.1 |

Stock options to purchase 16.8 million shares of common stock for both the quarter and nine months ended September 25, 2011 and 14.6 million shares of common stock for both the quarter and nine months ended September 26, 2010 were not included in the computation of diluted weighted average shares outstanding, as their effect would have been anti-dilutive.

NOTE 5 BUSINESS SEGMENT INFORMATION

We operate in four principal business segments: Aeronautics, Electronic Systems, IS&GS, and Space Systems. We organize our business segments based on the nature of the products and services offered.

The operating results in the following table for all periods presented excludes the PAE and EIG businesses from the IS&GS business segment information and the Savi business from the Electronics Systems business segment information (Note 3). Also, the financial information in the following table for 2010 has been adjusted to reflect our change in the methodology for recognizing net sales for services contracts with the U.S. Government (Note 1).

The following table presents net sales and operating profit of our four business segments. Net sales exclude intersegment revenue, as these activities are eliminated in consolidation. Intercompany transactions are generally negotiated under terms and conditions similar to other government and commercial contracts. Operating profit of the business segments includes the equity earnings or losses from investees in which certain of our business segments hold equity interests, because the activities of the investees are closely aligned with the operations of those segments.

Operating profit of the business segments excludes the FAS/CAS pension adjustment (defined below); expense for certain stock-based compensation programs, including costs for stock options and restricted stock units; the effects of items not considered part of management's evaluation of segment operating performance, such as severance charges (Note 2); gains or losses from divestitures (Note 3); the effects of legal settlements; corporate costs not allocated to the business segments; and other miscellaneous corporate activities. The items other than severance charges are included in Other unallocated corporate expense, net in the following table which reconciles operating profit from the business segments to operating profit in our Statements of Earnings. Severance charges are presented as a separate reconciling item.

Table of Contents**Lockheed Martin Corporation****Notes to Unaudited Condensed Consolidated Financial Statements (continued)**

The results of operations of our business segments include pension expense only as determined and funded in accordance with U.S. Government Cost Accounting Standards (CAS) rules. The FAS/CAS pension adjustment represents the difference between pension expense or income calculated under financial accounting standards (FAS) in accordance with GAAP and pension expense calculated and funded in accordance with CAS. CAS is a major factor in determining our pension funding requirements, and governs the extent to which pension costs can be allocated to and recovered on U.S. Government contracts. The CAS expense is recovered through the pricing of our products and services on U.S. Government contracts and, therefore, is recognized in each of our business segments' net sales and cost of sales.

Selected Financial Data by Business Segment

| | Quarter Ended | | Nine Months Ended | |
|--|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 25, 2011 | September 26, 2010 | September 25, 2011 | September 26, 2010 |
| <i>(In millions)</i> | | | | |
| Net sales | | | | |
| Aeronautics | \$ 3,995 | \$ 3,294 | \$ 10,600 | \$ 9,377 |
| Electronic Systems | 3,633 | 3,556 | 10,832 | 10,290 |
| Information Systems & Global Solutions | 2,323 | 2,525 | 6,833 | 7,281 |
| Space Systems | 2,168 | 1,968 | 6,023 | 5,962 |
| Total | \$ 12,119 | \$ 11,343 | \$ 34,288 | \$ 32,910 |
| Operating profit | | | | |
| Aeronautics | \$ 447 | \$ 389 | \$ 1,178 | \$ 1,090 |
| Electronic Systems | 444 | 428 | 1,348 | 1,252 |
| Information Systems & Global Solutions | 213 | 208 | 620 | 615 |
| Space Systems | 251 | 236 | 731 | 689 |
| Total business segments | 1,355 | 1,261 | 3,877 | 3,646 |
| Severance charges | (39) | (178) | (136) | (178) |
| Other unallocated corporate expense, net | (275) | (206) | (843) | (534) |
| Total | \$ 1,041 | \$ 877 | \$ 2,898 | \$ 2,934 |
| Intersegment revenue | | | | |
| Aeronautics | \$ 58 | \$ 16 | \$ 140 | \$ 90 |
| Electronic Systems | 266 | 249 | 770 | 698 |
| Information Systems & Global Solutions | 227 | 239 | 635 | 690 |
| Space Systems | 30 | 28 | 81 | 88 |
| Total | \$ 581 | \$ 532 | \$ 1,626 | \$ 1,566 |

September 25,
2011 December 31,
2010
(In millions)

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| Assets | | |
|--|------------------|------------------|
| Aeronautics | \$ 5,644 | \$ 5,231 |
| Electronic Systems | 9,899 | 9,925 |
| Information Systems & Global Solutions | 5,332 | 5,463 |
| Space Systems | 3,177 | 3,041 |
| | | |
| Total business segments | 24,052 | 23,660 |
| Corporate assets ⁽¹⁾ | 12,135 | 11,057 |
| Assets of discontinued operation held for sale | | 396 |
| | | |
| Total | \$ 36,187 | \$ 35,113 |

(1) Corporate assets primarily include cash and cash equivalents, short-term investments, deferred income taxes, environmental assets, and investments held in a Rabbi Trust.

Table of Contents**Lockheed Martin Corporation****Notes to Unaudited Condensed Consolidated Financial Statements (continued)****NOTE 6 INVENTORIES**

Inventories consisted of the following components:

| | September 25, 2011 | December 31, 2010 |
|--|-----------------------|----------------------|
| | <i>(In millions)</i> | |
| Work-in-process, primarily related to long-term contracts and programs in progress | \$ 6,801 | \$ 6,508 |
| Less: Customer advances and progress payments | (5,317) | (4,788) |
| | 1,484 | 1,720 |
| Other inventories | 305 | 643 |
| Total inventories | \$ 1,789 | \$ 2,363 |

NOTE 7 POSTRETIREMENT BENEFIT PLANS

The net pension cost and the net postretirement benefit cost related to our qualified defined benefit pension plans and our retiree medical and life insurance plans include the following components:

| | Quarter Ended | | Nine Months Ended | |
|---|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 25, 2011 | September 26, 2010 | September 25, 2011 | September 26, 2010 |
| | <i>(In millions)</i> | | | |
| Qualified defined benefit pension plans | | | | |
| Service cost | \$ 244 | \$ 226 | \$ 731 | \$ 677 |
| Interest cost | 479 | 469 | 1,438 | 1,407 |
| Expected return on plan assets | (509) | (506) | (1,525) | (1,520) |
| Amortization of prior service cost | 21 | 21 | 62 | 62 |
| Recognized net actuarial losses | 220 | 148 | 660 | 446 |
| Total net pension expense | \$ 455 | \$ 358 | \$ 1,366 | \$ 1,072 |
| Retiree medical and life insurance plans | | | | |
| Service cost | \$ 8 | \$ 9 | \$ 24 | \$ 27 |
| Interest cost | 41 | 42 | 122 | 124 |
| Expected return on plan assets | (35) | (32) | (105) | (96) |
| Amortization of prior service cost | (4) | (4) | (12) | (12) |
| Recognized net actuarial losses | 8 | 6 | 25 | 19 |
| Total net postretirement expense | \$ 18 | \$ 21 | \$ 54 | \$ 62 |

We made \$960 million and \$1.3 billion in contributions to our qualified defined benefit pension plans during the quarter and nine months ended September 25, 2011, including required amounts of approximately \$1.0 billion. We also may review options for further voluntary contributions in 2011. We do not expect any contributions to be required related to the retiree medical and life insurance plans in 2011.

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Lockheed Martin Corporation

Notes to Unaudited Condensed Consolidated Financial Statements (continued)

NOTE 8 LEGAL PROCEEDINGS AND CONTINGENCIES

We are a party to or have property subject to litigation and other proceedings, including matters arising under provisions relating to the protection of the environment. We believe the probability is remote that the outcome of each of these matters, including the legal proceedings discussed below, will have a material adverse effect on the Corporation as a whole, notwithstanding that the unfavorable resolution of any matter may have a material effect on our net earnings in any particular quarter. Among the factors that we consider in this assessment are the nature of existing legal proceedings and claims, the asserted or possible damages or loss contingency (if estimable), the progress of the case, existing law and precedent, the opinions or views of legal counsel and other advisers, our experience in similar cases and the experience of other companies, the facts available to us at the time of assessment, and how we intend to respond to the proceeding or claim. Our assessment of these factors may change over time as individual proceedings or claims progress. Unless otherwise indicated, a range of loss associated with any individual legal proceeding set forth below reasonably cannot be estimated. We cannot predict the outcome of legal proceedings with certainty. These matters include the following items.

Legal Proceedings

On July 20, 2011, the City of Pontiac General Employees Retirement System filed a class action lawsuit against us and two of our executive officers (Robert J. Stevens, Chairman and Chief Executive Officer, and Bruce L. Tanner, Executive Vice President and Chief Financial Officer) in the U.S. District Court for the Southern District of New York. On October 6, 2011, the complaint was amended, adding Linda R. Gooden, Executive Vice President, IS&GS, as a defendant. The complaint, filed on behalf of purchasers of our common stock from April 21, 2009, through July 21, 2009, alleges that we violated certain sections of the federal securities laws (including Sections 10(b) and 20(a) of the Securities Exchange Act of 1934) by allegedly making statements, primarily about the then-expected performance of our IS&GS business segment, that contained either false statements of material facts or omitted material facts necessary to make the statements made not misleading, or engaged in other acts that operated as an alleged fraud upon class members who purchased our common stock during that period. The complaint further alleges that the statutory safe harbor provided for forward-looking statements does not apply to any of the allegedly false statements. The complaint does not allege a specific amount of monetary damages. We believe that the allegations are without merit and will defend against them.

Two additional actions recently were filed that repeat substantially the same allegations as those in the City of Pontiac General Employees Retirement System case (described above). On September 9, 2011, Joyce Cavanagh-Wood, filed a shareholder derivative action in the Circuit Court for Montgomery County, Maryland, naming Mr. Stevens, Mr. Tanner, and each of the current directors of Lockheed Martin as well as the individuals who were Lockheed Martin directors at the time of the activities alleged in the complaint. The two actions allege breach of fiduciary duty, mismanagement, unjust enrichment, abuse of control, and waste of corporate assets relating to substantially the same allegations as the City of Pontiac General Employees Retirement System case. Similarly, on October 11, 2011, Renee Smith, individually and on behalf of others, filed a shareholder derivative action in the U.S. District Court for the Southern District of New York, naming the same defendants (excluding Rosalind Brewer) and making substantially the same allegations. We believe that the allegations are without merit and will defend against them and any related actions that may be filed.

On June 24, 2009, the U.K. Ministry of Defence (MoD) sent us a letter alleging that we were in default on the Soothsayer contract under which we were providing electronic warfare equipment to the British military. The total value of the contract is UK £144 million, of which UK £39 million has been paid to date (representing approximately US \$222 million and US \$60 million, based on the exchange rate as of September 25, 2011). The MoD has demanded repayment of amounts

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Notes to Unaudited Condensed Consolidated Financial Statements (continued)

paid under the contract, liquidated damages of UK £2 million (representing approximately US \$3 million based on the exchange rate as of September 25, 2011), and interest on those amounts, and has reserved the right to collect any excess future re-procurement costs. We dispute the MoD's position. We have commenced an arbitration proceeding against the MoD pursuant to the contract terms and are seeking damages for wrongful termination of the contract.

On April 24, 2009, we filed a declaratory judgment action against the N.Y. Metropolitan Transportation Authority and its Capital Construction Company (collectively, the MTA) asking the U.S. District Court for the Southern District of N.Y. to find that the MTA is in material breach of our agreement based on the MTA's failure to provide access to sites where work must be performed and customer-furnished equipment necessary to complete the contract. The contract has a total value of \$323 million, of which \$241 million has been paid to date. The MTA filed an answer and counterclaim alleging that we breached the contract, and subsequently terminated the contract for alleged default. The MTA is seeking monetary damages and other relief under the contract, including the cost to complete the contract and potential re-procurement costs. We dispute the MTA's allegations and are defending against them.

On November 30, 2007, the Department of Justice (DoJ) filed a complaint in partial intervention in a lawsuit filed under the qui tam provisions of the Civil False Claims Act in the U.S. District Court for the Northern District of Texas, United States ex rel. Becker and Spencer v. Lockheed Martin Corporation, et al., alleging that we should have known that a subcontractor falsified and inflated invoices submitted to us that were passed through to the government. The DoJ is seeking approximately \$80 million in damages, including interest but excluding potential penalties under the False Claims Act. We dispute the allegations and are defending against them.

On September 11, 2006, we and Lockheed Martin Investment Management Company (LMIMCo), a subsidiary, were named as defendants in a lawsuit filed in the U.S. District Court for the Southern District of Illinois, seeking to represent a class of purportedly similarly situated participants and beneficiaries in two of our 401(k) plans. Plaintiffs allege that we or LMIMCo caused our plans to pay expenses that were higher than reasonable by, among other actions, permitting service providers of the plans to engage in revenue sharing, paying investment management fees for the company stock funds, and causing the company stock funds to hold cash for liquidity, thus reducing the return on those funds. The plaintiffs also allege that we failed to disclose information appropriately relating to the fees associated with managing the plans. In August 2008, plaintiffs filed an amended complaint, adding allegations that we breached fiduciary duties under ERISA by providing inadequate disclosures with respect to the Stable Value Fund offered under our 401(k) plans. The complaint does not allege a specific calculation of damages, and we cannot reasonably estimate the possible loss, or range of loss, which could be incurred if the plaintiffs were to prevail in the allegations, but believe that we have substantial defenses. We dispute the allegations and are defending against them. On March 31, 2009, the Judge dismissed a number of the plaintiffs' claims, leaving three claims for trial, specifically the plaintiffs' claims involving the company stock funds, the Stable Value Fund, and overall fees. The Court also granted class certification on two of the plaintiffs' claims. We appealed the class certification. On March 15, 2011, the U.S. Court of Appeals for the Seventh Circuit vacated the Court's class certification. The case has been remanded to the District Court.

On August 28, 2003, the DoJ filed complaints in partial intervention in two lawsuits filed under the qui tam provisions of the Civil False Claims Act in the United States District Court for the Western District of Kentucky, United States ex rel. Natural Resources Defense Council, et al., v. Lockheed Martin Corporation, et al., and United States ex rel. John D. Tillson v. Lockheed Martin Energy Systems, Inc., et al. The DoJ alleges that we committed violations of the Resource Conservation and Recovery Act at the Paducah Gaseous Diffusion Plant by not properly handling, storing, and transporting hazardous waste and that we violated the False Claims Act by misleading Department of Energy officials and state regulators about the nature and extent of environmental noncompliance at the plant. The complaint does not allege a specific calculation of damages, and we cannot reasonably estimate the possible loss, or range of loss, which could be incurred if the plaintiff were to prevail in the allegations, but believe that we have substantial defenses. We dispute the allegations and are defending against them.

Table of Contents**Lockheed Martin Corporation****Notes to Unaudited Condensed Consolidated Financial Statements (continued)**

As described in the *Environmental Matters* discussion below, we are subject to federal and state requirements for protection of the environment, including those for discharge of hazardous materials and remediation of contaminated sites. As a result, we are a party to or have property subject to various other lawsuits or proceedings involving environmental matters and remediation obligations. This includes the litigation we have been in with certain residents of Redlands, California, since 1997 before the California Superior Court for San Bernardino County regarding allegations of personal injury, property damage, and other tort claims on behalf of individuals arising from our alleged contribution to regional groundwater contamination. In 2006, the California Court of Appeal dismissed the plaintiffs' punitive damages claim. In 2008, the trial court dismissed the remaining first tier plaintiffs, ending the first round of individual trials. The dismissal was affirmed by both the California Court of Appeal and the California Supreme Court. The trial court has now established the procedures for the litigation of the next round of individual plaintiffs, and pre-trial proceedings are now underway. The complaint does not allege a specific calculation of damages, and we cannot reasonably estimate the possible loss, or range of loss, which could be incurred if the plaintiffs were to prevail in the allegations, but believe that we have substantial defenses. We dispute the allegations and are defending against them.

Environmental Matters

We are involved in environmental proceedings and potential proceedings relating to soil and groundwater contamination, disposal of hazardous waste, and other environmental matters at several of our current or former facilities, or at third-party sites where we have been designated as a potentially responsible party (PRP). A substantial portion of environmental costs will be included in our net sales and cost of sales in future periods pursuant to U.S. Government regulations. At the time a liability is recorded for future environmental costs, we record an asset for estimated future recovery considered probable through the pricing of products and services to agencies of the U.S. Government, regardless of the contract form (*e.g.*, cost-reimbursable, fixed price). We continuously evaluate the recoverability of our environmental receivables by assessing, among other factors, U.S. Government regulations, our U.S. Government business base and contract mix, and our history of receiving reimbursement of such costs. We include the portion of those environmental costs expected to be allocated to our non-U.S. Government contracts, or that is determined to be unallowable for pricing under U.S. Government contracts, in our cost of sales at the time the liability is established. At September 25, 2011, and December 31, 2010, the aggregate amount of liabilities recorded relative to environmental matters was \$948 million and \$935 million, of which \$836 million and \$807 million is recorded in other liabilities on the Balance Sheets at September 25, 2011 and December 31, 2010, with the remainder recorded in other current liabilities. We have recorded assets totaling \$821 million and \$810 million at September 25, 2011, and December 31, 2010, for the estimated future recovery of these costs, as we consider the recovery probable based on the factors previously mentioned. Of those amounts, \$723 million and \$699 million are recorded in other assets on the Balance Sheets at September 25, 2011 and December 31, 2010, with the remainder recorded in other current assets. We project costs and recovery of costs over approximately twenty years.

Environmental cleanup activities usually span several years, which make estimating liabilities a matter of judgment because of such factors as changing remediation technologies, assessments of the extent of contamination, and continually evolving regulatory environmental standards. We consider these and other factors in estimates of the timing and amount of any future costs that may be required for remediation actions, which results in the calculation of a range of estimates for a particular environmental remediation site.

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Lockheed Martin Corporation

Notes to Unaudited Condensed Consolidated Financial Statements (continued)

We perform quarterly reviews of the status of our environmental remediation sites and the related liabilities and assets. We record a liability when it is probable that a liability has been incurred and the amount can be reasonably estimated. The amount of liability recorded is based on our best estimate of the costs to be incurred for remediation at a particular site within a range of estimates for that site or, in cases where no amount within the range is better than another, we record an amount at the low end of the range. We do not discount the recorded liabilities, as the amount and timing of future cash payments are not fixed or cannot be reliably determined.

We cannot reasonably determine the extent of our financial exposure in all cases at this time. There are a number of former operating facilities that we are monitoring or investigating for potential future remediation. In some cases, although a loss may be probable, it is not possible at this time to reasonably estimate the amount of any obligation for remediation activities because of uncertainties with respect to assessing the extent of the contamination or the applicable regulatory standard. We also are pursuing claims for contribution to site cleanup costs against other PRPs, including the U.S. Government.

In January 2011, both the U.S. Environmental Protection Agency and the California Office of Environmental Health Hazard Assessment announced plans to regulate two chemicals, perchlorate and hexavalent chromium, to levels that are expected to be substantially lower than the existing respective standards established in California. The rulemaking processes are lengthy ones and may take one or more years to complete. If substantially lower standards are adopted, we would expect a material increase in our estimates for environmental liabilities and the related assets for the portion of the increased costs that are probable of future recovery in the pricing of our products and services for the U.S. Government. The amount that would be allocable to our non-U.S. Government contracts or that is determined to be unallowable for pricing under U.S. Government contracts would be expensed, which may have a material effect on our earnings in any particular quarter.

We are conducting remediation activities, including under various consent decrees and orders, relating to soil or groundwater contamination at certain sites of former or current operations. Under an agreement related to our Burbank and Glendale, California, sites, the U.S. Government reimburses us an amount equal to approximately 50% of expenditures for certain remediation activities in its capacity as a PRP under the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA).

Letters of Credit, Surety Bonds, and Third-Party Guarantees

We have entered into standby letters of credit, surety bonds, and third-party guarantees with financial institutions and other third parties primarily relating to advances received from customers and the guarantee of future performance on certain contracts. Letters of credit and surety bonds generally are available for draw down in the event we do not perform. In some cases, we may guarantee the contractual performance of third parties such as joint venture partners. We have total outstanding letters of credit, surety bonds, and third-party guarantees aggregating \$4.0 billion and \$4.2 billion at September 25, 2011 and December 31, 2010. Of these amounts, approximately \$1.0 billion relate to third-party guarantees.

Approximately 90% and 85% of the \$1.0 billion in third-party guarantees outstanding at September 25, 2011 and December 31, 2010 related to guarantees of the contractual performance of joint ventures to which we currently are or previously were a party. This amount represents our estimate of the maximum amount we would expect to incur upon the contractual non-performance of the joint venture partners. We evaluate the reputation, technical capabilities, and credit quality of potential joint venture partners. In addition, we generally have cross-indemnities in place that may enable us to recover amounts that may be paid on behalf of a joint venture partner. We believe our current and former joint venture partners will be able to perform their obligations, as they have done through September 25, 2011, and that it will not be necessary to make payments under the guarantees.

Table of Contents**Lockheed Martin Corporation****Notes to Unaudited Condensed Consolidated Financial Statements (continued)****United Launch Alliance**

In connection with our 50% ownership interest of United Launch Alliance, L.L.C. (ULA), we and The Boeing Company (Boeing) have each received distributions totaling \$327 million which are subject to agreements between us, Boeing, and ULA, whereby, if ULA does not have sufficient cash resources or credit capacity to make payments under the inventory supply agreement it has with Boeing, both we and Boeing would provide to ULA, in the form of an additional capital contribution, the level of funding required for ULA to make those payments. Any such capital contributions would not exceed the amount of the distributions subject to the agreements. We currently believe that ULA will have sufficient operating cash flows and credit capacity, including access to its \$400 million revolving credit agreement from third-party financial institutions, to meet its obligations such that we would not be required to make a contribution under these agreements.

In addition, both we and Boeing have cross-indemnified each other for certain financial support arrangements (*e.g.*, letters of credit, surety bonds, or foreign exchange contracts provided by either party) and guarantees by us and Boeing of the performance and financial obligations of ULA under certain launch service contracts. We believe ULA will be able to fully perform its obligations, as it has done through September 25, 2011, and that it will not be necessary to make payments under the cross-indemnities or guarantees.

NOTE 9 FAIR VALUE MEASUREMENTS

The following table presents assets and liabilities measured and recorded at fair value on our Balance Sheets on a recurring basis, and their level within the fair value hierarchy:

| | September 25, 2011 | | | December 31, 2010 | | |
|---|----------------------|---------|---------|-------------------|---------|---------|
| | Total | Level 1 | Level 2 | Total | Level 1 | Level 2 |
| | <i>(In millions)</i> | | | | | |
| Assets | | | | | | |
| Equity securities ⁽¹⁾ | \$ 76 | \$ 76 | \$ | \$ 86 | \$ 86 | \$ |
| Mutual funds ⁽¹⁾ | 316 | 316 | | 450 | 450 | |
| U.S. Government securities ⁽²⁾ | 225 | | 225 | 719 | | 719 |
| Other securities ⁽²⁾ | 98 | | 98 | 104 | | 104 |
| Derivative assets ⁽³⁾ | 49 | | 49 | 26 | | 26 |
| Liabilities | | | | | | |
| Derivative liabilities ⁽³⁾ | 25 | | 25 | 33 | | 33 |

(1) Equity securities and interests in mutual funds are valued using quoted market prices.

(2) U.S. Government securities and other securities, which consist primarily of corporate debt securities, U.S. Government-sponsored enterprise securities, and mortgage-backed securities, are valued based on inputs other than quoted prices that are observable for the asset (*e.g.*, interest rates and yield curves observable at commonly quoted intervals).

(3) Derivative assets and liabilities relate to foreign currency exchange and interest rate swap contracts and are valued based on observable market prices (*e.g.*, interest rates and yield curves observable at commonly quoted intervals), but are not exchanged in an active market.

We maintain a Rabbi Trust which includes investments to fund certain of our non-qualified deferred compensation plans. Investments in the trust are classified as trading securities and, accordingly, changes in their fair values are recorded in other non-operating income (expense), net. As of September 25, 2011 and December 31, 2010, investments in the trust totaled \$712 million and \$843 million and are included within the investment securities categories listed in the table above. Those investment categories also include available-for-sale securities held for general corporate purposes that we have classified as short-term investments on our Balance Sheets. As of December 31, 2010, these securities primarily consisted of U.S. Treasury securities with a fair value of approximately \$500 million, which matured during the nine months ended September 25, 2011. The cost basis of these securities was not materially different from their respective fair value as of December 31, 2010.

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Lockheed Martin Corporation

Notes to Unaudited Condensed Consolidated Financial Statements (continued)

Derivative assets and liabilities included in the table above relate to derivative financial instruments that we use to manage our exposure to fluctuations in foreign currency exchange rates and interest rates. Foreign currency exchange contracts are entered into to manage the exchange rate risk of forecasted foreign currency denominated cash receipts and cash payments. The majority of our foreign currency exchange contracts are designated as cash flow hedges. We also use derivative financial instruments to manage our exposure to changes in interest rates. Our financial instruments that are subject to interest rate risk principally include fixed-rate, long-term debt. Our interest rate swap contracts are designated as fair value hedges. We do not hold or issue derivative financial instruments for trading or speculative purposes.

The classification of gains and losses resulting from changes in the fair values of derivatives is dependent on our intended use of the derivative and its resulting designation. Adjustments to reflect changes in fair values of derivatives attributable to the effective portion of hedges that we consider highly effective hedges are either reflected in earnings and largely offset by corresponding adjustments to the hedged items, or reflected net of income taxes in accumulated other comprehensive loss until the hedged transaction is recognized in earnings. Changes in the fair value of the derivatives that are attributable to the ineffective portion of the hedges, or of derivatives that are not considered to be highly effective hedges, if any, are immediately recognized in earnings. The aggregate notional amount of our outstanding foreign currency exchange contracts at September 25, 2011 and December 31, 2010 was \$1.9 billion and \$2.2 billion. The aggregate notional amount of our interest rate swap contracts at September 25, 2011 was \$450 million, and we had no interest rate swap contracts outstanding at December 31, 2010. The effect of our derivative instruments on our Statements of Earnings for the quarters and nine months ended September 25, 2011 and September 26, 2010, and on our Balance Sheets as of September 25, 2011 and December 31, 2010, was not material.

Our cash equivalents include highly liquid instruments with remaining maturities at the date of acquisition of 90 days or less. Due to the short maturity of these instruments, the carrying amount on our Balance Sheets approximates fair value. Our accounts receivable and accounts payable are carried at cost, which approximates fair value. The estimated fair values of our long-term debt instruments at September 25, 2011 and December 31, 2010, aggregated \$8,627 million and \$6,211 million, compared with a carrying amount of \$7,545 million and \$5,524 million, which excludes the \$507 million and \$505 million unamortized discount. The fair values of our long-term debt instruments were estimated based on quoted market prices of debt with terms and due dates similar to our long-term debt instruments.

NOTE 10 OTHER

Long-term Debt

On September 9, 2011, we issued \$2.0 billion of long-term notes in a registered public offering consisting of \$500 million due in 2016 with a fixed coupon interest rate of 2.13%, \$900 million due in 2021 with a fixed coupon interest rate of 3.35%, and \$600 million due in 2041 with a fixed coupon interest rate of 4.85%. We may, at our option, redeem some or all of the notes at any time by paying a make-whole premium, plus accrued and unpaid interest, if any, to the date of repurchase. Interest on the notes is payable on March 15 and September 15 of each year, beginning on March 15, 2012.

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Notes to Unaudited Condensed Consolidated Financial Statements (continued)

In October 2011, subsequent to our 2011 third quarter, we used a portion of the proceeds to redeem all of our \$500 million long-term notes due in 2013 with a fixed coupon rate of 4.12% (the 2013 Notes). As a result of this redemption, we have classified the 2013 Notes on our September 25, 2011 Balance Sheet as current portion of long-term debt. The redemption included a make-whole premium of \$26 million that will be recognized in other non-operating income (expense), net in the fourth quarter of 2011.

In August 2011, we entered into a new \$1.5 billion revolving credit facility (the new credit facility) with a group of banks and terminated our existing \$1.5 billion revolving credit facility which was to expire in June 2012. The new credit facility expires August 2016, and we may request an increase to the new credit facility by an additional amount up to \$500 million, at the banks' discretion. There were no borrowings outstanding under either facility through September 25, 2011. Borrowings under the new credit facility would be unsecured and bear interest at rates based, at our option, on the Eurodollar rate or a bank defined Base Rate, as defined in the new credit facility. Each bank's obligation to make loans under the new credit facility is subject to, among other things, our compliance with various representations, warranties and covenants, including covenants limiting our ability and certain of our subsidiaries to encumber assets and a covenant not to exceed a maximum leverage ratio, as defined in the new credit facility. As of September 25, 2011, we were in compliance with all covenants contained in the new credit facility, as well as in our debt agreements.

Stockholders' Equity

Share Repurchase Program

During the first nine months of 2011, we repurchased a total of 29.9 million shares of our common stock for \$2,263 million, of which 0.1 million shares for \$9 million were settled and paid for in October 2011. We paid cash totaling \$2,317 million for share repurchases in the first nine months of 2011, which included \$63 million for shares we repurchased in December 2010 but that were not paid for until January 2011. During the first nine months of 2010, we repurchased a total of 19.8 million shares for \$1,566 million.

Our share repurchase program provides for the repurchase of our common stock from time-to-time. Under the program, we have discretion to determine the dollar amount of shares to be repurchased and the timing of any repurchases in compliance with applicable law and regulation. In the third quarter of 2011, our Board authorized an additional \$1.0 billion in August and \$2.5 billion in September for share repurchases, bringing the total authorized amount under the program to \$6.5 billion. As of September 25, 2011, we had repurchased a total of 41.1 million shares under the program for \$3,038 million, and there remained \$3,462 million authorized for additional share repurchases.

As we repurchase our common shares, we reduce common stock for the \$1 of par value of the shares repurchased, with the remainder of the purchase price over par value recorded as a reduction of additional paid-in capital. If additional paid-in capital is reduced to zero, we record the remainder of the excess of purchase price over par value as a reduction of retained earnings.

Stock Option and Restricted Stock Unit Grants

In January 2011, we granted a total of 2.5 million options to purchase our common stock to key employees at an exercise price of \$79.60. The fair value of each option on the date of grant was \$13.06. We recognize compensation cost for most of these stock options ratably over the three-year vesting period. In addition, we granted 1.9 million restricted stock units (RSUs) to key employees. The fair value of each RSU on the date of grant was \$79.43 and was based on the market value of a share of our common stock on the date of the award. We recognize the related compensation expense ratably over the three-year vesting period.

Table of Contents**Lockheed Martin Corporation****Notes to Unaudited Condensed Consolidated Financial Statements (continued)***Dividends*

During the first nine months of 2011, we declared and paid quarterly dividends totaling \$770 million (\$.75 per share). In September 2011, we also declared our fourth quarter dividend which was increased to \$1.00 per share. The fourth quarter dividend totaled \$323 million and was recorded as a current liability and a reduction of retained earnings on the declaration date. The dividend will be paid in December 2011. During the first nine months of 2010, we declared and paid quarterly dividends totaling \$700 million (\$.63 per share).

Comprehensive Income

The components of comprehensive income consisted of the following:

| | Quarter Ended | | Nine Months Ended | |
|---|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 25, 2011 | September 26, 2010 | September 25, 2011 | September 26, 2010 |
| | <i>(In millions)</i> | | | |
| Net earnings | \$ 700 | \$ 560 | \$ 1,972 | \$ 1,917 |
| Other comprehensive income (loss): | | | | |
| Adjustment for postretirement benefit plans, net of tax | 171 | 116 | 501 | 347 |
| Other, net | (67) | 24 | (58) | 5 |
| Total other comprehensive income | 104 | 140 | 443 | 352 |
| Comprehensive income | \$ 804 | \$ 700 | \$ 2,415 | \$ 2,269 |

The adjustment for postretirement benefit plans relates to the components of net postretirement benefit plan expense that represent recognized net actuarial losses and the amortization of prior service costs, net of tax (Note 7). The net actuarial loss recognition relates primarily to investment losses incurred in 2008 on the assets held in a trust to support our qualified defined benefit pension plans, which previously had been recorded on the Balance Sheet as a reduction to stockholders' equity in other comprehensive income (loss). When we recognize expense for such items in subsequent periods, we record an increase to stockholders' equity in other comprehensive income (loss) for the after-tax effects. We have revised the September 26, 2010 Statement of Stockholders' Equity to include a reclassification adjustment for these items by increasing stockholders' equity through other comprehensive income (loss) by \$347 million, with related adjustments to deferred income taxes and postretirement benefit plan liabilities.

Income Taxes

We made federal and foreign income tax payments, net of refunds received, of \$562 million and \$326 million during the first nine months of 2011 and 2010. These amounts included refunds of \$250 million and \$325 million received in the first quarter of 2011 and 2010 from the IRS related to estimated taxes paid for the 2010 and 2009 calendar years.

Changes in Estimates

Accounting for contracts under the POC method requires judgment relative to assessing risks, estimating contract revenues and costs (including estimating award and incentive fees and penalties related to performance), and making assumptions for schedule and technical issues. Due to the scope and nature of the work required to be performed on many of our contracts, the estimation of total revenue and cost at completion is complicated and subject to many variables and, accordingly, are subject to change. When adjustments in estimated contract revenues or estimated costs at completion are required, any changes from prior estimates are recognized in the current period for the inception-to-date effect of such changes.

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Lockheed Martin Corporation

Notes to Unaudited Condensed Consolidated Financial Statements (continued)

At the outset of each contract, we estimate the initial profit booking rate. The initial profit booking rate of each contract is based on the initial estimated costs at completion considering 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. 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, or may decrease if we are not successful in retiring the risks and, as a result, our estimated costs at completion increase.

Our net profit booking rate adjustments resulting from changes in estimates increased operating profit, net of state taxes, by approximately \$425 million and \$325 million for the quarters ended September 25, 2011 and September 26, 2010, and approximately \$1,175 million and \$975 million for the nine months ended September 25, 2011 and September 26, 2010. These adjustments increased net earnings by approximately \$275 million (\$.80 per share) and \$200 million (\$.55 per share) for the quarters ended September 25, 2011 and September 26, 2010, and approximately \$775 million (\$2.25 per share) and \$625 million (\$1.70 per share) for the nine months ended September 25, 2011 and September 26, 2010.

Recent Accounting Pronouncements

In June 2011, the Financial Accounting Standards Board (FASB) issued a new standard, which eliminates the option to present other comprehensive income (OCI) in the statement of stockholders' equity and instead requires net income, the components of OCI, and total comprehensive income to be presented in either one continuous statement or two separate but consecutive statements. The standard also requires that items reclassified from OCI to net income be presented on the face of the financial statements. As currently issued, the new standard will be effective for us beginning with our first quarter 2012 reporting and will be applied retrospectively. However, in October 2011, the FASB announced it would issue an exposure draft in the near term with a proposal to defer the requirement to present reclassifications from OCI to net income on the face of the financial statements and consider whether such reclassification adjustments should be disclosed in the notes to the financial statements, consistent with the existing disclosure requirements. The deferral, if finalized, would not change the requirement to present net income, components of OCI, and total comprehensive income in either one continuous statement or two separate but consecutive statements. We do not expect the adoption of the new standard or exposure draft will have an effect on our results of operations, financial position, or cash flows as it only requires a change in the presentation of OCI in our consolidated financial statements.

In September 2011, the FASB issued a new standard which amends the existing guidance on goodwill impairment testing. The new standard allows an entity the option to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If this is the case, the entity will need to perform a more detailed two-step goodwill impairment test which is used to identify potential goodwill impairments and to measure the amount of goodwill impairment losses to be recognized, if any. The standard will be effective for annual or interim goodwill impairment tests performed by us after December 31, 2011. The adoption of the standard will not have an effect on our results of operations, financial position, or cash flows.

Subsequent Event

On September 27, 2011, we acquired QTC Holdings Inc. (QTC), which provides outsourced medical evaluation services to the U.S. Government, for a payment of approximately \$420 million, net of cash acquired. QTC will be integrated within our IS&GS business segment. The acquisition is not expected to have a material effect on our future results of operations, financial position, or cash flows.

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Lockheed Martin Corporation

Report of Ernst & Young LLP,

Independent Registered Public Accounting Firm

Board of Directors

Lockheed Martin Corporation

We have reviewed the condensed consolidated balance sheet of Lockheed Martin Corporation as of September 25, 2011, and the related condensed consolidated statements of earnings for the quarters and nine months ended September 25, 2011 and September 26, 2010, and the condensed consolidated statements of cash flows and stockholders' equity for the nine months ended September 25, 2011 and September 26, 2010. These financial statements are the responsibility of the Corporation's management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the condensed consolidated financial statements referred to above for them to be in conformity with U.S. generally accepted accounting principles.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of Lockheed Martin Corporation as of December 31, 2010, and the related consolidated statements of earnings, stockholders' equity, and cash flows for the year then ended (not presented herein) and in our report dated February 24, 2011, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2010, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ Ernst & Young LLP

McLean, Virginia

October 27, 2011

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Lockheed Martin Corporation

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

We are a global security company and principally engage in the research, design, development, manufacture, integration, and sustainment of advanced technology systems and products. We provide a broad range of management, engineering, technical, scientific, logistic, and information services. We serve both domestic and international customers with products and services that have defense, civil, and commercial applications, with our principal customers being agencies of the U.S. Government. In 2010, approximately 85% of our \$45.7 billion in net sales were to the U.S. Government, either as a prime contractor or as a subcontractor. Our U.S. Government sales were to both Department of Defense (DoD) and non-DoD agencies. The remainder of our net sales primarily were to international customers (including foreign military sales funded, in whole or in part, by the U.S. Government), which represented approximately 14% of our 2010 net sales. Our main areas of focus are in defense, space, intelligence, homeland security, and government information technology.

We operate in four principal business segments: Aeronautics, Electronic Systems, Information Systems & Global Solutions (IS&GS), and Space Systems. We organize our business segments based on the nature of the products and services offered. Amounts in prior periods have been reclassified to reflect the planned divestiture of Savi Technology, Inc. (Savi), a logistics business within our Electronic Systems business segment (Note 3).

The following discussion should be read along with our 2010 Form 10-K filed with the Securities and Exchange Commission, and with the unaudited condensed consolidated financial statements included in this Form 10-Q.

As disclosed in Note 1, on January 1, 2011, we changed the way we account for our services contracts with the U.S. Government. We now recognize sales on those contracts using the percentage-of-completion (POC) method that we use on our product contracts with the U.S. Government. The effect of this change in accounting was not material to our consolidated results of operations or financial position for any period, including the quarters and nine months ended September 25, 2011 and September 26, 2010, and is expected to have an immaterial effect on net sales and segment operating profit for the year 2011, and does not impact cash flows. All prior period amounts included in Management's Discussion and Analysis of Financial Condition and Results of Operations have been adjusted to reflect the new method of accounting.

2012 EXPECTED OPERATING TRENDS

Our preliminary outlook for 2012 is premised on the U.S. Government's timely approval of 2012 defense budget legislation at a level consistent with the President's proposed 2012 defense budget as well as continued support and funding of our programs. If this occurs, we expect 2012 net sales to be flattish as compared to 2011 levels, and that consolidated 2012 segment operating profit margin will remain at approximately 11%.

UPDATE ON INDUSTRY CONSIDERATIONS

The U.S. Government continues to focus on developing and implementing spending, tax, and other initiatives to reduce the deficit, create jobs, and stimulate the economy. The recently enacted Budget Control Act of 2011 (Budget Act) permits an increase in the federal government's borrowing limit while reducing projected net government spending over the next 10 years. The Budget Act sets \$900 billion in immediate cuts to discretionary spending for 2012-2021. It also establishes a bi-partisan congressional Joint Select Committee on Deficit Reduction, sometimes

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Management's Discussion and Analysis of Financial Condition

and Results of Operations (continued)

referred to as the Super Committee, which is charged with recommending legislation by November 23, 2011, the enactment of which would result in spending and revenue changes that would reduce net government spending by at least \$1.2 trillion over the next 10 years, in addition to the \$900 billion in immediate discretionary spending reductions referenced above.

Congress and the administration are attempting to balance decisions regarding defense, homeland security, and other federal spending priorities as well as revenue and entitlement changes within the framework and limitations of the Budget Act. In the event that the Super Committee fails to recommend legislation, Congress fails to approve that legislation by late December 2011, or the President fails to sign the legislation into law, an automatic sequestration of discretionary appropriations would be triggered, which would make up any shortfall necessary to achieve the \$1.2 trillion target. Under the Budget Act, 50% of any shortfall from the \$1.2 trillion target would automatically be applied as a reduction to discretionary appropriations for national defense programs.

In October 2011, Congress passed a continuing resolution funding measure for fiscal year 2012 to finance all U.S. Government activities through November 18, 2011. Under this continuing resolution, partial-year funding at amounts consistent with appropriated levels for fiscal year 2011 are available, subject to certain restrictions, but new spending initiatives are not authorized. Our key programs continue to be supported and funded despite the continuing resolution financing mechanism. However, during periods covered by continuing resolutions (or until the regular appropriation bills are passed), we may experience delays in procurement of products and services due to lack of funding, and those delays may affect our results of operations.

This process and the spending reductions to defense programs have the potential to significantly impact our portfolio of business, which is heavily dependent upon discretionary appropriations for defense programs. Although we believe that our programs are well aligned with national defense and other priorities, shifts in domestic and international spending and tax policy, changes in security, defense and intelligence priorities, the affordability of our products and services, general economic conditions and developments, and other factors may affect the level of funding for existing or proposed programs. We cannot predict the outcome of Budget Act deliberations or actions of the Super Committee at this time.

CONSOLIDATED RESULTS OF OPERATIONS

Since our operating cycle is long-term and involves many types of design, development, and production (DD&P) contracts with varying production delivery schedules, the results of operations of a particular quarter or year-to-date period, or quarter-to-quarter or year-to-date comparisons of recorded sales and profits, may not be indicative of future operating results. The following discussions of comparative results among periods should be viewed in this context. All per share amounts cited in these discussions are presented on a per diluted share basis from continuing operations, unless otherwise noted.

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and Results of Operations (continued)

| | Quarter Ended | | Nine Months Ended | |
|---|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 25, 2011 | September 26, 2010 | September 25, 2011 | September 26, 2010 |
| <i>(In millions, except per share data)</i> | | | | |
| Operating Results | | | | |
| Net sales | \$ 12,119 | \$ 11,343 | \$ 34,288 | \$ 32,910 |
| Cost of sales | (11,123) | (10,554) | (31,572) | (30,179) |
| Operating profit | 1,041 | 877 | 2,898 | 2,934 |
| Interest expense | (89) | (85) | (258) | (258) |
| Other non-operating income (expense), net | (3) | 37 | 25 | 46 |
| Income tax expense | (284) | (272) | (696) | (929) |
| Net earnings from continuing operations | 665 | 557 | 1,969 | 1,793 |
| Net earnings from discontinued operations | 35 | 3 | 3 | 124 |
| Net earnings | 700 | 560 | 1,972 | 1,917 |
| Diluted Earnings Per Common Share | | | | |
| Continuing operations | \$ 1.99 | \$ 1.53 | \$ 5.72 | \$ 4.84 |
| Discontinued operations | .11 | .01 | .01 | .33 |
| Total | \$ 2.10 | \$ 1.54 | \$ 5.73 | \$ 5.17 |

The following provides an overview of our consolidated results of operations by focusing on key elements in our Statements of Earnings. Product sales are predominantly generated in the Aeronautics, Electronic Systems, and Space Systems segments, and most of our services sales are generated in our Electronic Systems and IS&GS segments.

Net Sales

| | Quarter Ended | | Nine Months Ended | |
|----------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 25, 2011 | September 26, 2010 | September 25, 2011 | September 26, 2010 |
| <i>(In millions)</i> | | | | |
| Net Sales | | | | |
| Products | \$ 9,680 | \$ 8,948 | \$ 27,293 | \$ 26,269 |
| Services | 2,439 | 2,395 | 6,995 | 6,641 |
| Total | \$ 12,119 | \$ 11,343 | \$ 34,288 | \$ 32,910 |

Net sales for the third quarter of 2011 were \$12.1 billion, a \$776 million or 7% increase over the third quarter of 2010 net sales of \$11.3 billion. The increase was due to an 8% increase in product sales and a 2% increase in services sales. Product sales increases in Aeronautics and Space Systems of about \$895 million partially were offset by lower product sales in IS&GS. The services sales increase of about \$45 million primarily was attributable to Aeronautics and Electronic Systems.

Net sales for the first nine months of 2011 were \$34.3 billion, a \$1.4 billion or 4% increase over the \$32.9 billion recorded in the comparable 2010 period. The increase was due to a 4% increase in product sales and a 5% increase in services sales. Product sales increases in Aeronautics and Electronic Systems of about \$1,495 million partially were offset by lower product sales in IS&GS. The services sales increase of about \$355 million primarily was attributable to Electronic Systems & IS&GS.

Cost of Sales

Cost of sales, for both products and services, consist of materials, labor, and subcontracting costs, as well as an allocation of indirect costs (overhead and general and administrative). For each of our contracts, we manage the nature and amount of costs at the contract level, which form the basis for estimating our total costs at completion of the contract.

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Management evaluates performance on our contracts by focusing on net sales and operating profit, and not by type or amount of operating expense. Consequently, our discussion of business segment performance focuses on net sales and operating profit, consistent with our approach for managing the business. This approach is consistent with the overall life cycle of our contracts, as management assesses the bidding of each contract by focusing on net sales and operating profit, and monitors performance on our contracts in a similar manner through their completion.

We regularly provide customers with reports of our costs as the contract progresses. The cost information in the reports is accumulated in a manner specified by the requirements of each contract. For example, cost data provided to our customer for a product would typically align to the subcomponents of that product (such as a wing-box on an aircraft) or for services, the type of work being performed (such as help-desk support).

Our contracts generally are cost-based, which allows for the recovery of costs in the pricing of our products and services. Most of our contracts generally are bid and negotiated with our customers based on the mutual awareness of our estimated costs to provide the product or service. This approach for negotiating contracts with our U.S. Government customers generally allows for the recovery of our costs. We also may enter into long-term supply contracts for certain materials or components, to coincide with the production schedule of certain products and to ensure their availability at known unit prices.

| | Quarter Ended | | Nine Months Ended | |
|-----------------------------------|--|-----------------------|-----------------------|-----------------------|
| | September 25, 2011 | September 26, 2010 | September 25, 2011 | September 26, 2010 |
| | <i>(In millions, except percentages)</i> | | | |
| Cost of Sales | | | | |
| Cost of product sales | \$ (8,667) | \$ (8,017) | \$ (24,361) | \$ (23,469) |
| % of product sales | 89.5% | 89.6% | 89.3% | 89.3% |
| Cost of services sales | (2,138) | (2,156) | (6,241) | (6,003) |
| % of services sales | 87.7% | 90.0% | 89.2% | 90.4% |
| Severance charges | (39) | (178) | (136) | (178) |
| Other unallocated corporate costs | (279) | (203) | (834) | (529) |
| Total | \$ (11,123) | \$ (10,554) | \$ (31,572) | \$ (30,179) |

Approximately 95% of our contracts are accounted for using the POC method of accounting. Under the POC method, we record net sales on contracts based upon our progress towards completion on a particular contract, as well as our estimate of the profit to be earned at completion. The following discussion of material changes in our cost of sales at the consolidated level should be read in tandem with our Discussion of Business Segments, because, due to the nature of POC accounting, changes in our cost of sales are typically accompanied by a corresponding change in our net sales.

Cost of product sales Cost of product sales increased by \$650 million or 8% for the third quarter of 2011 from the comparable 2010 period. This increase primarily was due to higher product volume, as the percentage of cost of product sales relative to product sales has remained consistent period over period. For the quarter, cost of product sales increased primarily due to higher volume associated with the delivery of six additional C-130J aircraft, work performed on C-5 programs and F-35 low-rate initial production (LRIP) contracts as well as F-16 support activities of about \$795 million at Aeronautics. Also, increased production on air defense (including Terminal High Altitude Defense (THAAD) and Patriot Advanced Capability-3 (PAC-3)) and tactical missile (including Hellfire) programs at Electronic Systems increased cost of product sales by approximately \$190 million. Lastly, cost of product sales increased due to higher volume primarily associated with a commercial satellite delivery and government satellite activities at Space Systems of approximately \$110 million. These increases partially were offset by lower production levels on the F-22 and F-35 System Development and Demonstration (SDD)

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Management's Discussion and Analysis of Financial Condition

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programs at Aeronautics of about \$150 million, lower costs due to the absence of the Decennial Response Integration System (DRIS) program that supported the 2010 United States census at IS&GS of approximately \$130 million, and lower volume on ship and aviation systems programs (including the Persistent Threat Detection System (PTDS) program) at Electronic Systems of about \$100 million.

Cost of product sales increased by \$892 million or 4% for the nine months ended September 25, 2011 from the comparable 2010 period. This increase primarily was due to higher product volume, as the percentage of cost of product sales relative to product sales has remained consistent period over period. For the year-to-date period, cost of product sales increased primarily due to higher volume associated with the delivery of ten additional C-130J aircraft, work performed on C-5 programs and F-35 LRIP contracts as well as F-16 support activities of about \$1,645 million at Aeronautics. Also, production on air defense (including THAAD and PAC-3), tactical missile (including Hellfire), and radar programs at Electronic Systems increased cost of product sales by approximately \$530 million. Lastly, cost of product sales increased primarily due to higher volume associated with a commercial satellite delivery and government satellite activities at Space Systems of approximately \$165 million. These increases partially were offset by lower production levels on the F-22 and F-35 SDD programs at Aeronautics of about \$530 million and on the NASA Orion and NASA external tank programs at Space Systems of approximately \$225 million, lower costs due to the absence of the DRIS program at IS&GS of approximately \$450 million, and lower volume on ship and aviation systems programs (including the PTDS program) at Electronic Systems of about \$175 million.

Cost of services sales Cost of services sales decreased by \$18 million or 1% for the third quarter of 2011 from the comparable 2010 period. The decrease primarily was attributable to lower services volume on numerous small programs at IS&GS and on various training and logistics support services at Electronic Systems. These decreases partially were offset by higher services volume on the Special Operations Forces Contractor Logistics Support Services (SOF CLSS) program within the logistics support services at Electronic Systems of approximately \$100 million. For the quarter, the approximate 2% decrease in percentage of cost of services sales relative to services sales primarily was due to the retirement of risks and other factors on numerous programs at IS&GS.

Cost of services sales increased by \$238 million or 4% for the nine months ended September 25, 2011 from the comparable 2010 period. This increase primarily was due to higher services volume in logistics support services at Electronic Systems, primarily due to the SOF CLSS program of approximately \$280 million, which partially was offset by lower services volume on numerous small programs at IS&GS and various other training and logistics support services at Electronic Systems. For the year-to-date period, the percentage of cost of services sales relative to services sales declined slightly primarily due to the retirement of risks and other factors on numerous programs at IS&GS, partially offset by volume on SOF CLSS, which provides a lower margin relative to other Electronic Systems programs.

Severance charges During the quarter and nine months ended September 25, 2011, we recorded severance charges totaling \$39 million and \$136 million, net of state tax benefits. The severance charges recorded in the third quarter of 2011 related to our IS&GS business segment and Corporate Headquarters. In the second quarter of 2011, we recorded severance charges totaling \$97 million, net of state tax benefits, of which \$49 million and \$48 million related to our Aeronautics and Space Systems business segments. These charges reduced our net earnings in the third quarter by \$25 million (\$.07 per share) and for the nine-month period by \$88 million (\$.25 per share). The charges consisted of severance costs associated with the planned elimination of certain positions through either voluntary or involuntary actions. Upon separation, terminated employees will receive lump-sum severance payments based on years of service, which are expected to be paid through the first half of 2012.

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These severance actions resulted from a strategic review of these businesses and our Corporate Headquarters to better align our organization and cost structure with changing economic conditions. The workforce reductions at the business segments also reflect changes in program lifecycles, where several of our major programs are transitioning out of development and into production, and certain programs are ending. In the third quarter of 2011, we made approximately half of the severance payments associated with the severance charge related to Space Systems. As of September 25, 2011, no other significant payments associated with the severance actions noted above have been made.

In the third quarter of 2010, we recorded a severance charge of \$178 million, net of state income tax benefits, related to the Voluntary Executive Separation Program (VESP). The charge, which included lump-sum special payments for qualifying executives, reduced our net earnings by \$116 million (\$.32 per share for the third quarter and \$.31 per share for the nine-month period). The effective date of termination of employment for most participants was February 1, 2011, with the lump-sum special payments to be made within 90 days from separation of service. As of September 25, 2011, substantially all payments under the VESP have been made.

We expect to recover a substantial amount of these severance charges, including the severance related to the VESP, in future periods through the pricing of our products and services to the U.S. Government and other customers. While the VESP is expected to be recovered over several years, the other severance charges would typically be expected to be recovered within a one year period. For example, Space Systems recovered about half of its second quarter 2011 severance charge in the third quarter of 2011, which largely was offset by about a \$15 million charge related to excess inventory.

Other unallocated corporate costs Unallocated corporate costs were \$279 million and \$834 million for the quarter and nine months ended September 25, 2011 compared to \$203 million and \$529 million for the quarter and nine months ended September 26, 2010. In both periods, the increase primarily was attributable to an increase in the FAS/CAS pension adjustment (see Discussion of Business Segments for a description of this amount).

Changes in our cost of sales between periods were not material, except as described above. The period-over-period change in our cost of sales was due to the volume of costs resulting from production, deliveries of products, and/or services provided on our portfolio of contracts. We have not identified any developing trends in cost of sales that would have a material impact on our future operations.

Operating Profit

Our operating profit for the third quarter of 2011 was \$1,041 million, an increase of 19% from the \$877 million recorded in the comparable 2010 period. The increase in operating profit of \$164 million primarily was attributable to a decrease in severance charges and increased operating profit in every business segment. These increases partially were offset by an increase in the FAS/CAS pension adjustment. Operating profit for the nine months ended September 25, 2011 was \$2,898 million, a decrease of 1% from the \$2,934 million recorded in the comparable 2010 period. The decrease in operating profit of \$36 million primarily was attributable to an increase in the FAS/CAS pension adjustment, which partially was offset by increased operating profit in every business segment and a decrease in severance charges.

Interest Expense

Interest expense for the quarter and nine months ended September 25, 2011 was \$89 million and \$258 million, about the same as the comparable periods in 2010. The initial net impact of the issuance of the \$2.0 billion of fixed rate notes in September 2011 and the redemption of the \$500 million 4.12% notes in October 2011 (Note 10 under the caption Long-term Debt) is expected to increase our quarterly interest expense by approximately \$13 million.

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Other Non-operating Income (Expense), Net

Other non-operating income (expense), net was expense of \$3 million in the third quarter of 2011, compared to income of \$37 million in the third quarter of 2010. Other non-operating income (expense), net was income of \$25 million in the first nine months of 2011, compared to income of \$46 million in the comparable 2010 period. The decrease in both periods primarily was due to net unrealized losses on marketable securities held to fund certain non-qualified employee benefit obligations.

Income Tax Expense

Our effective income tax rates from continuing operations were 29.9% and 26.1% for the quarter and nine months ended September 25, 2011, compared to 32.8% and 34.1% for the third quarter and nine months ended September 26, 2010. The rates for all periods benefited from tax deductions for U.S. manufacturing activities and dividends related to certain of our defined contribution plans with an employee stock ownership plan feature.

The effective tax rate for the quarter ended September 25, 2011 was lower than the comparable period in 2010 primarily due to the Research and Development (R&D) tax credit. In the fourth quarter of 2010, tax legislation retroactively extended the R&D tax credit for two years, from January 1, 2010 to December 31, 2011. While the R&D tax credit extension was retroactive to January 1, 2010, we did not recognize the benefit until the fourth quarter of 2010.

The effective tax rate for the nine months ended September 25, 2011 was lower than the comparable period in 2010 primarily due to the completion by the U.S. Congressional Joint Committee on Taxation (JCT) of its review of IRS Appeals' resolution of certain adjustments related to tax years 2003-2008, and the R&D tax credit. As a result of the JCT's completion of its review in April 2011, during the second quarter of 2011, we recorded a reduction in income tax expense of \$89 million (\$.26 per share for the nine months ended September 25, 2011).

The effective tax rate for the nine months ended September 26, 2010 was also impacted by legislation enacted in 2010 related to Medicare Part D. In the first quarter of 2010, health care legislation eliminated the tax deduction for company-paid retiree prescription drug expenses to the extent they are reimbursed under Medicare Part D, beginning in 2013. As a result, during the first quarter of 2010, we recorded additional income tax expense of \$96 million (\$.26 per share for the nine months ended September 26, 2010).

Net Earnings from Continuing Operations

Net earnings from continuing operations for the third quarter of 2011 were \$665 million (\$1.99 per share), compared to \$557 million (\$1.53 per share) reported in the third quarter of 2010. Net earnings from continuing operations for the nine months ended September 25, 2011 were \$1,969 million (\$5.72 per share), compared to \$1,793 million (\$4.84 per share) reported in the comparable 2010 period. Both net earnings from continuing operations and earnings per share were affected by the factors discussed above. In addition, earnings per share has benefited from the significant number of shares repurchased under our share repurchase program (Note 10 under the caption "Stockholders' Equity").

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Net Earnings from Discontinued Operations

Net earnings from discontinued operations included the operating results of Savi, a logistics business within our Electronics Systems business segment, for all periods presented. Discontinued operations also include Pacific Architects and Engineers, Inc. (PAE) for 2010 and through the date of its sale on April 4, 2011, and those of Enterprise Integration Group for 2010, which was sold on November 22, 2010.

Net earnings from discontinued operations were \$35 million (\$.11 per share) and \$3 million (\$.01 per share) for the quarter and nine months ended September 25, 2011, and was \$3 million (\$.01 per share) and \$124 million (\$.33 per share) for the quarter and nine months ended September 26, 2010. Earnings from discontinued operations for the quarter and nine months ended September 25, 2011, included a benefit of approximately \$50 million related to the decision to sell Savi, the principal driver of which is the recognition of a deferred tax asset for book and tax differences. Similar tax benefits of \$15 million and \$96 million related to the sale of PAE were recorded in the first quarter of 2011 and second quarter of 2010. For additional information, see Note 3 to the accompanying consolidated financial statements.

DISCUSSION OF BUSINESS SEGMENTS

The following tables of financial information and related discussion of the results of operations of our business segments are consistent with the presentation of segment information in Note 5 to the financial statements. The discussion describes the contributions of each of our business segments to our consolidated net sales and operating profit for the quarters and nine months ended September 25, 2011 and September 26, 2010. We follow an integrated approach for managing the performance of our business segments, and discuss business segment results of operations around major products and services.

The following table presents net sales and operating profit of our four business segments. Net sales exclude intersegment revenue, as these activities are eliminated in consolidation. Intercompany transactions are generally negotiated under terms and conditions similar to other government and commercial contracts. Operating profit of the business segments includes the equity earnings or losses from investees in which certain of our business segments hold equity interests, because the activities of the investees are closely aligned with the operations of those segments.

Operating profit of the business segments excludes the FAS/CAS pension adjustment (Note 5); expense for certain stock-based compensation programs, including costs for stock options and restricted stock units; the effects of items not considered part of management's evaluation of segment operating performance, such as severance charges (Note 2); gains or losses from divestitures (Note 3); the effects of legal settlements; corporate costs not allocated to the business segments; and other miscellaneous corporate activities. These items other than severance charges are included in Other unallocated corporate expense, net in the following table which reconciles operating profit from the business segments to operating profit in our Statements of Earnings. Severance charges are presented as a separate reconciling item.

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| | Quarter Ended | | Nine Months Ended | |
|--|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 25, 2011 | September 26, 2010 | September 25, 2011 | September 26, 2010 |
| | <i>(In millions)</i> | | | |
| Net Sales | | | | |
| Aeronautics | \$ 3,995 | \$ 3,294 | \$ 10,600 | \$ 9,377 |
| Electronic Systems | 3,633 | 3,556 | 10,832 | 10,290 |
| Information Systems & Global Solutions | 2,323 | 2,525 | 6,833 | 7,281 |
| Space Systems | 2,168 | 1,968 | 6,023 | 5,962 |
| Total | 12,119 | 11,343 | 34,288 | 32,910 |
| Operating Profit | | | | |
| Aeronautics | 447 | 389 | 1,178 | 1,090 |
| Electronic Systems | 444 | 428 | 1,348 | 1,252 |
| Information Systems & Global Solutions | 213 | 208 | 620 | 615 |
| Space Systems | 251 | 236 | 731 | 689 |
| Total business segments | 1,355 | 1,261 | 3,877 | 3,646 |
| Severance charges | (39) | (178) | (136) | (178) |
| Other unallocated corporate expense, net | (275) | (206) | (843) | (534) |
| Total | \$ 1,041 | \$ 877 | \$ 2,898 | \$ 2,934 |

Our net sales are derived from long-term contracts for DD&P activities and for services provided to the U.S. Government as well as foreign military sales conducted through the U.S. Government. We account for these contracts, as well as DD&P contracts with non-U.S. Government customers, under the POC method of accounting which represent approximately 95% of our net sales. Our remaining net sales are derived from contracts to provide services to non-U.S. Government customers, which we account for under the services accounting model.

Under the POC method of accounting, we record sales on contracts based upon our progress towards completion on a particular contract as well as our estimate of the profit to be earned at completion. Cost-reimbursable contracts, which account for the majority of our net sales, provide for the payment of allowable costs plus a fee. For fixed-priced contracts, net sales and cost of sales are recognized as products are delivered or as costs are incurred. Due to the nature of the POC method of accounting, changes in our costs of sales are typically accompanied by a related change in our net sales.

Changes in volume refer to increases or decreases in sales resulting from varying production activity levels, deliveries, or service levels on individual contracts. Volume changes typically include a corresponding change in operating profit based on the estimate of profit at completion for a particular contract. For example, if the cost volume on a cost-reimbursement-type contract increased or decreased compared with a prior period, sales and operating profit for that contract will also be increased or decreased.

Changes in performance refer to increases or decreases in the estimated profit booking rates on our contracts accounted for using the POC method of accounting and usually relate to revisions in the total estimated costs at completion that reflect improved or deteriorated conditions on a particular contract. For example, improved conditions typically result from the retirement of risks on contracts. Such changes in estimated profit booking rates are recognized in the current period and reflect the inception-to-date effect of such changes. For example, if we increase the estimated profit booking rate on a cost-reimbursable contract, the increase in sales and operating profit for that contract will reflect a higher return on sales in the current period due to the recognition of the higher profit booking rate on both current period costs as well as previously incurred costs.

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Many of our contracts are long-term in nature and often span several years. At the outset of each contract, we estimate the total costs to complete the contract. The estimates consider the technical requirements (for example, a newly-developed product versus a mature product), the schedule and associated tasks (for example, the number and type of milestone events), and costs (for example, material, labor, subcontractor and overhead). The initial profit booking rate of each contract considers risks surrounding the ability to achieve the technical requirements, schedule, and costs 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. All of the estimates are subject to change during the performance of the contract and therefore may affect the profit booking rate.

We have a number of programs that are designated as classified by the U.S. Government and cannot be specifically described. The operating results of these classified programs are included in our consolidated and business segment results, and are subjected to the same oversight and internal controls as our other programs.

Aeronautics

Our Aeronautics business segment is engaged in the research, design, development, manufacture, integration, sustainment, support, and upgrade of advanced military aircraft, including combat and air mobility aircraft, unmanned air vehicles, and related technologies. Key programs include the F-35 Lightning II, F-16 Fighting Falcon, F-22 Raptor, C-130J Super Hercules, and the C-5M Super Galaxy. Aeronautics provides logistics support, sustainment, and upgrade modification services for its aircraft. Aeronautics' operating results included the following:

| | Quarter Ended | | Nine Months Ended | |
|------------------|--|-----------------------|-----------------------|-----------------------|
| | September 25, 2011 | September 26, 2010 | September 25, 2011 | September 26, 2010 |
| | <i>(In millions, except percentages)</i> | | | |
| Net sales | \$ 3,995 | \$ 3,294 | \$ 10,600 | \$ 9,377 |
| Operating profit | \$ 447 | \$ 389 | \$ 1,178 | \$ 1,090 |
| Operating margin | 11.2% | 11.8% | 11.1% | 11.6% |

Net sales in the Aeronautics segment increased \$701 million, or 21%, during the third quarter of 2011, as compared to the corresponding period in 2010. The increase in net sales primarily was attributable to higher volume of about \$495 million for C-130 programs due to an increase in deliveries (13 C-130J aircraft delivered in the third quarter of 2011 as compared to seven during the same 2010 period) and support activities, approximately \$115 million driven by higher volume for the F-35 LRIP program, approximately \$135 million for F-16 support activities, and about \$100 million for higher volume on C-5 programs (one C-5 aircraft delivered in the third quarter of 2011 as compared to none during the same 2010 period). The increases partially were offset by a decline of about \$75 million in net sales due to lower volume on the F-22 program, which will continue to decline as the program winds down with final deliveries expected to be completed in 2012.

During the first nine months of 2011, net sales in the Aeronautics segment increased \$1.2 billion, or 13%, as compared to the corresponding period in 2010. The growth in net sales primarily was due to higher volume of about \$825 million for C-130 programs due to an increase in deliveries (26 C-130J aircraft delivered in the first nine months of 2011 as compared to 16 during the same 2010 period) and support activities, approximately \$500 million due to an increase in volume for work performed on the F-35 LRIP program, about \$235 million for F-16 support activities, and approximately \$205 million for higher volume on C-5 programs (two C-5 aircraft delivered in the first nine months of 2011 as compared to none during the same 2010 period). These increases partially were offset by a decline in net sales of approximately \$435 million due to lower volume on the F-22 program, and lower net sales of about \$105 million for the F-35 SDD program.

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Operating profit in the Aeronautics segment increased \$58 million, or 15%, during the third quarter of 2011, as compared to the corresponding period in 2010. The primary contributors to the growth were an increase of about \$55 million on the F-22 program due to risk retirements in 2011 and approximately \$55 million for C-130 programs as a result of higher volume and the retirement of risks in 2011, partially offset by a decline of approximately \$40 million in operating profit for the F-16 program due to risk retirements in 2010.

During the first nine months of 2011, operating profit in the Aeronautics segment increased \$88 million, or 8%, as compared to the corresponding period in 2010. The increase primarily was attributable to approximately \$95 million of higher operating profit on C-130 programs due to increased volume and the retirement of risks in 2011, and about \$70 million due to risk retirements on other Aeronautics sustainment activities in 2011. These increases partially were offset by lower operating profit of approximately \$60 million on several programs (F-35, F-16 and other combat aircraft and other Aeronautics programs) due to risk retirements in 2010.

We expect Aeronautics will have sales growth in the upper single digit percentage range for 2011 as compared to 2010. This increase primarily is driven by growth on F-35 LRIP contracts, the C-130J program, and the C-5 Reliability Enhancement and Re-engining Program (RERP) that will more than offset a decline on the F-22 program. Operating profit is projected to increase at a mid-single digit percentage rate above 2010 levels, resulting in a decline in operating margins between the years. Aeronautics operating margins are declining in 2011 as compared to those reported over the last few years due to the changing life cycle of significant Aeronautics programs. Specifically, Aeronautics sales are being driven by a larger share of LRIP activities on the F-35 production and C-5 modernization programs with less volume on the F-22 and F-16 production programs. LRIP contracts typically yield lower margins than more mature production programs. We expect Aeronautics' 2012 net sales will be flat or slightly higher than net sales for 2011 as a result of growth on F-35 LRIP contracts mostly offsetting lower volume on the F-22 production and F-35 SDD programs.

Electronic Systems

Our Electronic Systems business segment manages complex programs and designs, develops, produces, and integrates hardware and software solutions to ensure the mission readiness of armed forces and government agencies worldwide. Global security solutions include advanced sensors, decision systems, and weapons for air-, land-, and sea-based platforms. The segment integrates land vehicles, ships, and fixed- and rotary-wing aircraft. Major products and programs include air and missile defense; tactical missiles; weapon fire control systems; surface ship and submarine combat systems; anti-submarine and undersea warfare systems; land, sea-based, and airborne radars; surveillance and reconnaissance systems; simulation and training systems; and integrated logistics and sustainment services. Electronic Systems also manages and operates the Sandia National Laboratories for the U.S. Department of Energy and is part of the consortium that manages the United Kingdom's Atomic Weapons Establishment.

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We have classified Savi as discontinued operations (Note 3) and, therefore, financial information related to this business has been excluded from the segment information below. Electronic Systems' operating results included the following:

| | Quarter Ended | | Nine Months Ended | |
|------------------|--|-----------------------|-----------------------|-----------------------|
| | September 25, 2011 | September 26, 2010 | September 25, 2011 | September 26, 2010 |
| | <i>(In millions, except percentages)</i> | | | |
| Net sales | \$ 3,633 | \$ 3,556 | \$ 10,832 | \$ 10,290 |
| Operating profit | \$ 444 | \$ 428 | \$ 1,348 | \$ 1,252 |
| Operating margin | 12.2% | 12.0% | 12.4% | 12.2% |

Net sales in the Electronic Systems segment increased \$77 million, or 2%, during the third quarter and \$542 million, or 5%, during the first nine months of 2011, as compared to the corresponding periods in 2010. Contributing to the increases were higher volume on air defense programs (including THAAD and PAC-3) of approximately \$125 million during the third quarter and about \$330 million during the first nine months of 2011. Additional volume for logistics activities related to the SOF CLSS program, which began late in the third quarter of 2010, increased sales by about \$105 million during the third quarter and approximately \$295 million during the first nine months of 2011. Increased deliveries on tactical missiles programs (including Hellfire) resulted in increased net sales of approximately \$95 million during the third quarter and about \$175 million during the first nine months of 2011. Higher volume on the Littoral Combat Ship program contributed to an increase in net sales of approximately \$65 million for the third quarter and about \$115 million for the first nine months of 2011. The net sales increase during the first nine months of 2011 also was attributable to higher volume on various radar system programs of about \$115 million.

These increases partially were offset by a decline in volume on other ship and aviation systems programs (primarily the 2010 deliveries of PTDS) of about \$195 million during the third quarter and approximately \$340 million during the first nine months of 2011, lower volume on various other training and logistics services programs of approximately \$65 million during the third quarter and about \$135 million during the first nine months of 2011, and declines in volume on fire control systems of about \$40 million for the third quarter and approximately \$60 million for the first nine months of 2011.

During the third quarter and first nine months of 2011, operating profit in the Electronic Systems segment increased \$16 million, or 4%, and \$96 million, or 8%, as compared to the corresponding periods in 2010. Operating profit increased about \$40 million during the third quarter and approximately \$50 million during the first nine months of 2011 on tactical missiles programs (including Hellfire and High Mobility Artillery Rocket System) due to volume and the retirement of risks, and about \$20 million during the third quarter and about \$15 million during the first nine months of 2011 for various training and logistics services programs, partially offset by decreases in operating profit of about \$30 million and approximately \$50 million on ship and aviation systems programs for the third quarter and first nine months of 2011. Additionally, the operating profit increase during the first nine months of 2011 was attributable to radar system programs and undersea warfare programs of approximately \$35 million due to volume and air defense programs (PAC-3) of about \$40 million due to volume and risk retirements.

We expect Electronic Systems' sales, operating profit, and margins in 2011 will be comparable with 2010 results. A decline in volume on the PTDS program will be more than offset by an increase in volume on the SOF CLSS program and various air defense programs. We expect Electronic Systems' net sales in 2012 will be flat or slightly higher as compared to 2011.

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Our IS&GS business segment provides management services, Information Technology (IT) solutions, and advanced technology expertise across a broad spectrum of applications to U.S. Government and other customers. IS&GS key programs and activities include the En-Route Automation Modernization (ERAM) program, the Airborne Maritime Fixed Joint Tactical Radio System (JTRS) program, the Hanford Mission Support contract, and the DRIS program. The DRIS program, in support of the 2010 census for the U.S. Government, substantially was completed in 2010. IS&GS programs also include a large number of indefinite-delivery, indefinite-quantity (IDIQ) and task order types of contracts.

We have classified PAE and EIG as discontinued operations (Note 3) and, therefore, financial information related to these businesses has been excluded from the segment information below. IS&GS operating results included the following:

| | Quarter Ended | | Nine Months Ended | |
|------------------|--|-----------------------|-----------------------|-----------------------|
| | September 25, 2011 | September 26, 2010 | September 25, 2011 | September 26, 2010 |
| | <i>(In millions, except percentages)</i> | | | |
| Net sales | \$ 2,323 | \$ 2,525 | \$ 6,833 | \$ 7,281 |
| Operating profit | \$ 213 | \$ 208 | \$ 620 | \$ 615 |
| Operating margin | 9.2% | 8.2% | 9.1% | 8.4% |

Net sales in the IS&GS segment decreased \$202 million, or 8%, during the third quarter and \$448 million, or 6%, during the first nine months of 2011, as compared to the corresponding periods in 2010. The decreases primarily were attributable to lower volume of about \$150 million during the third quarter and approximately \$500 million during the first nine months of 2011 due to the absence of the DRIS program that supported the 2010 United States census.

Operating profit in the IS&GS segment during the third quarter and first nine months of 2011 essentially was unchanged as compared to the corresponding periods in 2010. A decrease in operating profit for both the third quarter and first nine months of 2011 from the absence of the DRIS program in 2011 was offset by higher operating profit from numerous smaller programs, including about \$25 million during the third quarter and about \$40 million for the first nine months of 2011 from the retirement of risks on several programs, including Transportation Worker Identification Credential and Automated Flight Service Station.

We expect IS&GS sales to decline in 2011 in the mid-single digit percentage range as compared to 2010 results. The decrease primarily is due to the completion of the DRIS program in 2010. Operating profit is expected to increase over 2010 in the high single digit percentage range due to program performance, resulting in an increase in operating margins. The backlog of our IS&GS business has been reduced to \$8.3 billion since December 31, 2010 primarily due to fiscal pressures constraining government purchases of information technology and other products and services. Due to the nature of its activities, backlog is converted into sales more quickly in IS&GS than our other business segments. We expect IS&GS will experience a mid single digit percentage decrease in net sales for 2012 as compared to 2011. This expected decline primarily is due to continued budget pressure in the government IT market.

Space Systems

Our Space Systems business segment is engaged in the design, research and development, engineering, and production of satellites, strategic and defensive missile systems, and space transportation systems, including activities related to the planned replacement of the Space Shuttle. Government satellite programs include the Advanced Extremely High Frequency (AEHF)

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system, the Mobile User Objective System (MUOS), the Global Positioning Satellite III (GPS III) system, the Space-Based Infrared System (SBIRS), and the Geostationary Operational Environmental Satellite R-Series (GOES-R). Strategic and missile defense programs include the targets and countermeasures program and the fleet ballistic missile program. Space transportation includes the NASA Orion program and, through ownership interests in two joint ventures, expendable launch services (United Launch Alliance, or ULA) and Space Shuttle processing activities for the U.S. Government (United Space Alliance, or USA). The Space Shuttle completed its final flight mission in July 2011 and our involvement with its launch and launch support activities ended at that time. Space Systems' operating results included the following:

| | Quarter Ended | | Nine Months Ended | |
|------------------|--|-----------------------|-----------------------|-----------------------|
| | September 25, 2011 | September 26, 2010 | September 25, 2011 | September 26, 2010 |
| | <i>(In millions, except percentages)</i> | | | |
| Net sales | \$ 2,168 | \$ 1,968 | \$ 6,023 | \$ 5,962 |
| Operating profit | \$ 251 | \$ 236 | \$ 731 | \$ 689 |
| Operating margin | 11.6% | 12.0% | 12.1% | 11.6% |

Net sales in the Space Systems segment increased \$200 million, or 10%, during the third quarter and \$61 million, or 1%, during the first nine months of 2011, as compared to the corresponding periods in 2010. The increases in net sales were attributable to increased volume of about \$145 million during the third quarter primarily related to commercial satellites (one delivery in the third quarter of 2011 and none in the same 2010 period), approximately \$250 million during the first nine months due to commercial satellites and government satellite activities, and higher volume for fleet ballistic and defensive missile systems of about \$45 million during the third quarter and approximately \$70 million during the first nine months of 2011. These increases partially were offset by declines of about \$25 million for the third quarter and approximately \$85 million for the first nine months of 2011 related to the NASA External Tank program, which ended in connection with the completion of the space shuttle program in July 2011. Additionally, changes in volume on the NASA Orion program increased net sales by about \$35 million during the third quarter of 2011, but decreased net sales by approximately \$150 million during the first nine months of 2011.

During the third quarter and first nine months of 2011, operating profit in the Space Systems segment increased \$15 million, or 6%, and \$42 million, or 6%, as compared to the corresponding periods in 2010. The increases in operating profit principally were attributable to volume and retirement of risks on government satellite programs of about \$35 million for the third quarter and approximately \$75 million for the first nine months of 2011. Operating profit also increased about \$15 million during the third quarter of 2011, primarily due to defensive missile systems. Partially offsetting this increase was lower equity earnings from ULA and USA of about \$40 million for the third quarter and approximately \$30 million for the first nine months of 2011 as compared to 2010.

Total equity earnings recognized by the Space Systems segment from ULA and USA represented about \$35 million, or 15%, and approximately \$165 million, or 23%, of the segment's operating profit during the third quarter and first nine months of 2011. During the third quarter and first nine months of 2010, total equity earnings recognized by the Space Systems segment from ULA and USA represented about \$75 million, or 33%, and approximately \$195 million, or 28%.

We expect Space Systems' sales to decline in 2011 in the low single digit percentage range as compared to 2010 results. Sales are expected to decline due to the end of our production of the external tank for the space shuttle, partially offset by growth in satellite activities. Segment operating profit and margin in 2011 are expected to be comparable with 2010. We expect Space Systems' net sales for 2012 will be comparable with 2011 net sales.

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The following table shows the components of unallocated corporate expense, net, including the CAS expense that is included as expense in the segments' operating results, the related FAS pension expense, and the resulting FAS/CAS pension adjustment:

| | Quarter Ended | | Nine Months Ended | |
|---|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 25, 2011 | September 26, 2010 | September 25, 2011 | September 26, 2010 |
| | <i>(In millions)</i> | | | |
| FAS/CAS pension adjustment: | | | | |
| FAS pension expense | \$ (455) | \$ (358) | \$ (1,366) | \$ (1,072) |
| Less: CAS expense | (224) | (247) | (674) | (741) |
| FAS/CAS pension adjustment expense | (231) | (111) | (692) | (331) |
| Severance charges ⁽¹⁾ | (39) | (178) | (136) | (178) |
| Stock compensation expense and other, net | (44) | (95) | (151) | (203) |
| Total | \$ (314) | \$ (384) | \$ (979) | \$ (712) |

⁽¹⁾ The amounts for 2011 consist of severance charges as described in Note 2. For the quarter and nine months ended September 26, 2010, the approximate amounts of the VESP attributable to our business segments were as follows: Aeronautics \$25 million; Electronic Systems \$38 million; IS&GS \$42 million; and Space Systems \$41 million. The remaining \$32 million was attributable to our Corporate Headquarters.

The increase in the FAS pension expense for 2011 as compared to 2010 primarily was due to the decrease in the discount rate at December 31, 2010 compared to December 31, 2009, together with the effect of the recognition of the 2008 investment losses, partially offset by the effects of investment gains in 2009 and 2010 (each as compared to our 8.50% long-term rate of return assumption). This trend is consistent with the assumptions we used in computing the FAS pension expense and CAS funding amounts as discussed in the Management's Discussion and Analysis of Financial Condition and Results of Operations section of our 2010 Form 10-K under the caption Critical Accounting Policies Postretirement Benefit Plans.

LIQUIDITY AND CASH FLOWS

Our access to capital resources that provide liquidity has not been materially affected by the changing economic and market conditions over the past few years. We continually monitor changes in such conditions so that we can timely respond to any related developments. We have generated strong operating cash flows which have been the primary source of funding for our operations, debt service and repayments, capital expenditures, share repurchases, dividends, acquisitions, and postretirement benefit plan funding. We have accessed the capital markets on limited occasions, as needed or when opportunistic.

We expect our cash from operations to continue to be sufficient to support our operations and anticipated capital expenditures for the foreseeable future. We have financing resources available to fund potential cash outflows that are less predictable or more discretionary, as discussed under Capital Resources. We have access to the credit markets, if needed, for liquidity or general corporate purposes, including letters of credit to support customer advance payments and for other trade finance purposes such as guaranteeing our performance on particular contracts.

We have a balanced cash deployment and disciplined growth strategy to enhance shareholder value and position ourselves to take advantage of new business opportunities when

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they arise. Consistent with that strategy, we have invested in our business, including capital expenditures and independent research and development, repurchased shares, increased our dividends, made selective acquisitions of businesses, and managed our debt levels. The following table provides a summary of our cash flow information and the subsequent discussion provides an overview of our execution of this strategy.

| | Nine Months Ended | |
|--|-----------------------|-----------------------|
| | September 25, 2011 | September 26, 2010 |
| | (In millions) | |
| Net cash provided by operating activities | \$ 3,038 | \$ 3,387 |
| Net cash provided by (used for) investing activities | 337 | (867) |
| Net cash used for financing activities | (1,063) | (2,256) |

Operating Activities

Net cash provided by operating activities for the nine months of 2011 was \$3,038 million, which was \$349 million lower than the same period in 2010. The decrease primarily was attributable to a net increase in income tax payments of about \$240 million and payments totaling \$168 million related to the previously announced VESP (Note 2). In the first nine months of 2011, there were \$1.3 billion in contributions made to our qualified defined benefit pension plans compared to \$1.4 billion in the first nine months of 2010. We may review options for further contributions in 2011. We anticipate recovering approximately \$900 million as CAS cost during 2011, with the remainder being recoverable in future years.

Investing Activities

Capital expenditures The majority of our capital expenditures relate to facilities infrastructure and equipment which are generally incurred to support new and existing programs across all of our business segments. We also incur capital expenditures for IT to support programs and general enterprise IT infrastructure. Capital expenditures for property, plant and equipment amounted to \$443 million in the first nine months of 2011 and \$394 million in the comparable 2010 period. We expect that our operating cash flows will continue to be sufficient to fund our annual capital expenditures over the next few years.

Divestitures and other activities In the first nine months of 2011, we received proceeds related to the sale of PAE (Note 3). There were no material divestiture activities in the comparable period of 2010. During the first nine months of 2011, we decreased our short-term investments by \$510 million compared to an increase of \$421 million during the comparable 2010 period. In the fourth quarter of 2011, we acquired QTC Holdings Inc., which provides outsourced medical evaluation services to the U.S. Government, for a payment of approximately \$420 million, net of cash acquired (Note 10 under the caption "Subsequent Event").

Financing Activities

Share activity and dividends We paid cash totaling \$2,317 million for share repurchases during the first nine months of 2011, which included \$63 million for shares we repurchased in December 2010 but that were not paid for until January 2011 (Note 10 under the caption "Stockholders Equity").

Our share repurchase program provides for the repurchase of our common stock from time-to-time. Under the program, we have discretion to determine the dollar amount of shares to be repurchased and the timing of any repurchases in compliance with applicable law and regulation. In the third quarter of 2011, our Board authorized an additional \$1.0 billion in August and \$2.5 billion in September for share repurchases, bringing the total authorized amount under the

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program to \$6.5 billion. As of September 25, 2011, we had repurchased a total of 41.1 million shares under the program for \$3,038 million, and there remained \$3,462 million authorized for additional share repurchases. See Part II, Item 2 of this Form 10-Q for additional information regarding the repurchase of shares during the third quarter of 2011.

During the first nine months of 2011, we declared and paid quarterly dividends totaling \$770 million (\$.75 per share). During the first nine months of 2010, we declared and paid dividends totaling \$700 million (\$.63 per share). We also declared our fourth quarter dividend of \$323 million (\$1.00 per share) in September 2011. This dividend will be paid in December 2011.

Cash received from the issuance of our common stock in connection with stock option exercises and tax benefits associated with stock-based compensation during the first nine months of 2011 and 2010 totaled \$90 million and \$57 million. Those activities resulted in the issuance of 1.6 million shares and 1.1 million shares during the respective periods.

Long-term debt On September 9, 2011, we issued a total of \$2.0 billion in long-term notes (Note 10 under the caption *Long-term Debt*). We used a portion of the net proceeds in the fourth quarter of 2011 to repay all of our outstanding \$500 million 4.12% notes due March 2013 as well as to pay \$26 million for the early redemption of the notes (Note 10 under the caption *Long-term Debt*).

CAPITAL RESOURCES

At September 25, 2011, we held cash and cash equivalents of \$4.6 billion. Our long-term debt, net of amortized discounts, amounted to \$7.0 billion, including the current portion, as of September 25, 2011, and mainly is in the form of publicly-issued notes and debentures that bear interest at fixed rates.

In August 2011, we entered into a new \$1.5 billion revolving credit facility (the new credit facility) with a group of banks and terminated our existing \$1.5 billion revolving credit facility which was to expire in June 2012. The new credit facility expires August 2016, and we may request an increase to the new credit facility by an additional amount up to \$500 million, at the banks' discretion. There were no borrowings outstanding under either facility through September 25, 2011. Borrowings under the new credit facility would be unsecured and bear interest at rates based, at our option, on the Eurodollar rate or a bank defined Base Rate, as defined in the new credit facility. Each bank's obligation to make loans under the credit facility is subject to, among other things, our compliance with various representations, warranties and covenants, including covenants limiting our ability and certain of our subsidiaries' ability to encumber assets and a covenant not to exceed a maximum leverage ratio, as defined in the new credit facility. As of September 25, 2011, we were in compliance with all covenants contained in the new credit facility, as well as in our debt agreements.

We have agreements in place with banking institutions to provide for the issuance of commercial paper. There were no commercial paper borrowings outstanding during the first nine months of 2011. If we were to issue commercial paper, the borrowings would be supported by the new credit facility. We also have an effective shelf registration statement on Form S-3 on file with the Securities and Exchange Commission through August 2014 to provide for the issuance of an indeterminate amount of debt securities.

Our stockholders' equity was \$3.0 billion at September 25, 2011, a decrease of \$554 million from December 31, 2010. The decrease primarily was due to the repurchase of 29.9 million common shares for \$2,263 million and dividends declared of \$1,098 million during the first nine months of 2011. These decreases partially were offset by net earnings of \$1,972 million, a reclassification adjustment of \$443 million, primarily related to our postretirement benefit plans, and employee stock activity of \$392 million. As we repurchase our common shares, we reduce common stock for the \$1 of par value of the shares repurchased, with the remainder of the

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purchase price over par value recorded as a reduction of additional paid-in capital. Due to the volume of repurchases made under our share repurchase program, additional paid-in capital was reduced to zero, with the remainder of the excess of purchase price over par value of \$1,846 million recorded as a reduction of retained earnings.

OTHER MATTERS***Postretirement Benefit Plans***

Our postretirement benefit plans are measured annually at year-end and are largely dependent upon several key economic assumptions. The decline in discount rates experienced to date in 2011 could negatively affect our year-end 2011 balance sheet and 2012 earnings if this trend continues through to the end of 2011. If we were to assume that the discount rate we were going to use at the end of 2011 was 4.5% and our actual investment return for 2011 was 5.0%, our pension liabilities would increase by approximately \$5.7 billion and the accumulated other comprehensive loss within stockholders' equity would increase by approximately \$3.5 billion. This could result in our reporting negative stockholders' equity at year-end. If this occurs, this will not impact our debt covenants nor hinder our ability to pay dividends. Using these same assumptions, along with a potential reduction of our expected long-term rate of return on plan assets from 8.5% to 8.0%, our 2012 non-cash FAS/CAS pension expense adjustment could be comparable to the 2011 adjustment of approximately \$925 million. This estimate for the 2012 FAS/CAS pension adjustment is significantly higher than our previous expectations due to the impact of changes in the economic factors from those used at year-end 2010 and a delay in the CAS harmonization beyond 2012.

In developing the sensitivity analysis above, we made the following assumptions that are different than those at the beginning of this year: 1) the discount rate at the end of 2011 would equal 4.5%; 2) the actual rate of return on plan assets for the full year 2011 would equal 5.0%; 3) the expected long-term rate of return on plan assets for 2012 would equal 8.0%; and 4) the cash contributions to our pension plans total approximately \$1.3 billion in 2011 and \$2.1 billion in 2012. These are the only changes in valuation assumptions we have assumed. Further, we have assumed the revised CAS rules, as discussed below, will not be effective until after 2012 (and thus no change in estimated CAS expense has been factored into our sensitivity analysis).

The Pension Protection Act (PPA) required the CAS Board to modify its pension accounting rules by 2010 to better align the recovery of pension contributions on U.S. Government contracts with the new accelerated funding required by the PPA. To date, the CAS Board has not published final changes to its pension accounting rules. Our inability to allocate the accelerated pension contributions required under the PPA in the pricing of our products and services on U.S. Government contracts in the period during which the contributions are required will have the effect of increasing the amount of the FAS/CAS pension expense that is charged to earnings in 2012 and negatively affecting our cash from operations.

A change of plus or minus 25 basis points to the 4.5% assumed discount rate above, with all other assumptions held constant, would result in an incremental noncash, after-tax increase or decrease to stockholders' equity at the end of 2011 of approximately \$875 million, with a corresponding decrease or increase of approximately \$115 million in our estimated 2012 FAS/CAS pension expense adjustment. For each 100 basis points our actual return on plan assets for the full year 2011 is below 5%, cash contributions to our pension plans in 2012 would be expected to increase by approximately \$85 million.

Accounting for postretirement benefit plans under GAAP requires that the amounts we record be computed using actuarial valuations. These valuations include many assumptions, including those we make regarding financial markets and other economic conditions. Changes in those annual assumptions can impact our total stockholders' equity at any given year's end, and the

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amount of expense we record for our postretirement benefits plans in the following year. We will not finalize our postretirement benefit plan assumptions, or determine the actual return on plan assets, until our December 31, 2011 measurement date and they may not be the same as those discussed above.

Please refer to the Postretirement Benefit Plans section under *Critical Accounting Policies* in our December 31, 2010 Form 10-K for a more detailed discussion of the significant assumptions we must make, in addition to information regarding our ability to recover our pension costs in the pricing of our contracts.

Status of F-35 LRIP 5

The F-35 program consists of multiple contracts. The customer's acquisition strategy contemplates that the SDD contract will be performed concurrently with the LRIP contracts. Concurrent performance of development and production contracts is advantageous in complex programs to test airplanes, shorten the time to field systems, as well as achieve overall cost savings. Accordingly, we are performing the SDD contract concurrently with LRIP aircraft lots 2 through 4, as lot 1 has been completed.

The SDD portion of the F-35 program has approximately \$575 million of fee remaining, of which a minor portion has been tied to 2011 performance milestones. Any portion of the remaining fee that we or our partners receive is dependent upon completion of milestones, most of which have not yet been determined.

With respect to LRIP 5, we received customer authorization and initial funding to begin work in July 2010. In January 2011, we notified our customer that additional funding would be required to continue the advanced procurement. Despite not yet receiving such funding, we and our industry team have continued work in an effort to meet our customer's desired aircraft delivery dates for the LRIP 5 aircraft. As a result, as of September 25, 2011, we have approximately \$750 million in potential termination liability exposure. Without additional funding or contract coverage, we estimate that our exposure by the end of 2011 will be approximately \$1.2 billion. We are in the process of negotiating with our customer to obtain additional funding and finalize contract negotiations.

Given the size and complexity of the F-35 program, we anticipate that there will be continual reviews related to program schedule, cost, requirements, and aircraft quantities as part of the DoD, Congressional, and international partners' oversight and budgeting processes. Current program challenges include, but are not limited to, executing flight tests, supplier and partner performance, software development, and negotiating acceptable terms and conditions for LRIP 5, including exploring a fair and equitable cost share related to changes arising from the concurrent performance of development and production contracts as described above.

Although not exclusively related to the F-35 program, on October 4, 2010, the Defense Contracting Management Agency (DCMA) withdrew its prior validation and determination of compliance of the earned value management system (EVMS) at our Fort Worth, Texas location. EVMS is a tool for managing cost and schedule performance on complex programs. The DCMA may choose to re-audit our EVMS system at any time, but we understand that the DCMA will do so once a performance history on the new SDD baseline is established. The new SDD baseline may not be established until after the initial baseline review is completed in late 2011.

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United Launch Alliance

In connection with our 50% ownership interest of United Launch Alliance, L.L.C. (ULA), we and The Boeing Company (Boeing) have each received distributions totaling \$327 million which are subject to agreements between us, Boeing, and ULA, whereby, if ULA does not have sufficient cash resources or credit capacity to make payments under the inventory supply agreement it has with Boeing, both we and Boeing would provide to ULA, in the form of an additional capital contribution, the level of funding required for ULA to make those payments. Any such capital contributions would not exceed the amount of the distributions subject to the agreements. We currently believe that ULA will have sufficient operating cash flows and credit capacity, including access to its \$400 million revolving credit agreement from third-party financial institutions, to meet its obligations such that we would not be required to make a contribution under these agreements.

In addition, both we and Boeing have cross-indemnified each other for certain financial support arrangements (*e.g.*, letters of credit, surety bonds, or foreign exchange contracts provided by either party) and guarantees by us and Boeing of the performance and financial obligations of ULA under certain launch service contracts. We believe ULA will be able to fully perform its obligations, as it has done through September 25, 2011, and that it will not be necessary to make payments under the cross-indemnities or guarantees.

CRITICAL ACCOUNTING POLICIES

The foregoing discussion of our financial condition and results of operations is based on the consolidated financial statements included in this Quarterly Report on Form 10-Q, which have been prepared in accordance with accounting principles generally accepted in the U.S. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, sales and expenses, and the related disclosures of contingencies. We base these estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

During the nine months ended September 25, 2011, there were no significant changes to the critical accounting policies we disclosed in Management's Discussion and Analysis of Financial Condition and Results of Operations in our 2010 Form 10-K, except as disclosed in Note 1 to the accompanying consolidated financial statements. On January 1, 2011, we changed our methodology for recognizing net sales for services contracts with the U.S. Government to the POC method, and the way we evaluate new or significantly modified contracts with customers other than the U.S. Government, to the extent the contracts include multiple elements, to determine if the individual deliverables should be accounted for as separate units of accounting. However, these changes did not have a material effect on our consolidated results of operations, financial position, or cash flows, or on our related accounting policies. Due to the pervasiveness of the estimates and judgments that are necessary under the POC method of accounting and as a result of the changes disclosed in Note 1, we have revised our critical accounting policy related to contract accounting and sales recognition as set forth below.

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Lockheed Martin Corporation

Management's Discussion and Analysis of Financial Condition

and Results of Operations (continued)

Contract Accounting / Sales Recognition

Approximately 90% of our net sales are derived from long-term contracts for design, development, and production activities (also referred to as DD&P contracts) and services provided to the U.S. Government, and foreign military sales conducted through the U.S. Government. Approximately 95% of our net sales, including net sales related to DD&P contracts with non-U.S. Government customers, are accounted for using the POC method. The POC model requires that significant estimates and assumptions be made in accounting for the contracts. Our remaining net sales are derived from contracts to provide services to non-U.S. Government customers that are not associated with DD&P activities, which we continue to account for under the services accounting model.

Beginning January 1, 2011, we evaluate new or significantly modified contracts with customers other than the U.S. Government, to the extent the contracts include multiple elements, to determine if the individual deliverables should be accounted for as separate units of accounting. When we determine that accounting for the deliverables as separate units is appropriate, we allocate the contract value to the deliverables based on their relative estimated selling prices. The contracts or contract modifications we evaluate for multiple elements typically are long term in nature and include the provision of both DD&P activities and services. Based on the nature of our business, we generally account for components of such contracts using the POC accounting model or the services accounting model, as appropriate. This change in accounting has not had a material effect on our financial results, and is not expected to have a material effect in future periods.

We classify net sales as products or services on our Statements of Earnings based on the predominant attributes of the underlying contract. Most of our long-term contracts are denominated in U.S. dollars, including contracts for sales of military products and services to foreign governments conducted through the U.S. Government. We record sales for both DD&P activities and services under cost-reimbursable, fixed-price, and time-and-materials contracts.

Contract Types

Cost-reimbursable contracts

Cost-reimbursable contracts, which accounted for about 60% of our total net sales over the last three years, provide for the payment of allowable costs incurred during performance of the contract plus a fee, up to a ceiling based on the amount that has been funded. We generate revenue under two general types of cost-reimbursable contracts: cost-plus-award-fee/incentive fee (which represent a substantial majority of our cost-reimbursable contracts) and cost-plus-fixed-fee contracts.

Cost-plus-award-fee contracts provide for an award fee that varies within specified limits based on the customer's assessment of our performance against a predetermined set of criteria, such as targets based on cost, quality, technical, and schedule criteria. Cost-plus-incentive-fee contracts provide for reimbursement of costs plus a fee which is adjusted by a formula based on the relationship of total allowable costs to total target costs (incentive based on cost) or reimbursement of costs plus an incentive to exceed stated performance targets (incentive based on performance). The fixed fee in a cost-plus-fixed-fee contract is negotiated at the inception of the contract and that fixed fee does not vary with actual costs.

Fixed-price and other contracts

Under fixed-price contracts, which accounted for about 35% of our total net sales over the last three years, we agree to perform the specified work for a pre-determined price. To the extent our actual costs vary from the estimates upon which the price was negotiated, we will generate more or less profit, or could incur a loss. Some fixed-price contracts have a performance-based component under which we may earn incentive payments or incur financial penalties based on our performance.

Under time-and-materials contracts, which accounted for about 5% of our total net sales over the last three years, we are paid a fixed hourly rate for each direct labor hour expended, and we are reimbursed for allowable material costs and allowable out-of-pocket expenses. To the extent our

actual direct labor and associated costs vary in relation to the fixed hourly billing rates provided in the contract, we will generate more or less profit, or could incur a loss.

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Lockheed Martin Corporation

Management's Discussion and Analysis of Financial Condition

and Results of Operations (continued)

POC Method of Accounting

We record net sales and an estimated profit on a POC basis for cost-reimbursable and fixed-price contracts for DD&P activities, and services contracts with the U.S. Government. Sales are recorded on all time-and-materials contracts as the work is performed based on agreed-upon hourly rates and allowable costs.

The POC method for DD&P contracts depends on the nature of the products provided under the contract. For example, for contracts that require us to perform a significant level of development effort in comparison to the total value of the contract and/or to deliver minimal quantities, sales are recorded using the cost-to-cost method to measure progress toward completion. Under the cost-to-cost method of accounting, we recognize sales and an estimated profit as costs are incurred based on the proportion that the incurred costs bear to total estimated costs. For contracts that require us to provide a substantial number of similar items without a significant level of development, we record sales and an estimated profit on a percentage-of-completion basis using units-of-delivery as the basis to measure progress toward completing the contract. For contracts to provide services to the U.S. Government, sales are generally recorded using the cost-to-cost method.

Award fees and incentives, as well as penalties related to contract performance, are considered in estimating sales and profit rates on contracts accounted for under the POC method. Estimates of award fees are based on past experience and anticipated performance. We record incentives or penalties when there is sufficient information to assess anticipated contract performance. Incentive provisions that increase or decrease earnings based solely on a single significant event are not recognized until the event occurs. For contract change orders, claims, or similar items, we apply judgment in estimating the amounts and assessing the potential for realization. These amounts are only included in contract value when they can be reliably estimated and realization is considered probable.

Accounting for contracts under the POC method requires judgment relative to assessing risks, estimating contract revenues and costs (including estimating award and incentive fees and penalties related to performance), and making assumptions for schedule and technical issues. Due to the scope and nature of the work required to be performed on many of our contracts, the estimation of total revenue and cost at completion is complicated and subject to many variables.

Contract costs include material, labor, and subcontracting costs, as well as an allocation of indirect costs. We have to make assumptions regarding labor productivity and availability, the complexity of the work to be performed, the availability of materials, the length of time to complete the contract (to estimate increases in wages and prices for materials), performance by our subcontractors, and the availability and timing of funding from our customer, among other variables. When estimates of total costs to be incurred on a contract exceed total estimates of revenue to be earned, a provision for the entire loss on the contract is recorded in the period in which the loss is determined.

At the outset of each contract, we estimate the initial profit booking rate. The initial profit booking rate of each contract is based on the initial estimated costs at completion considering 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. Business segment personnel evaluate our contracts through periodic reviews. Management personnel independent from the business segment performing work under the contract also perform recurring evaluations of technical matters, scheduling, and contract costs. 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.

Table of Contents**Lockheed Martin Corporation****Management's Discussion and Analysis of Financial Condition****and Results of Operations (continued)**

When adjustments in estimated contract revenues or estimated costs at completion are required, any changes from prior estimates are recognized in the current period for the inception-to-date effect of the changes. For example, if we increase the estimated profit booking rate on a cost-reimbursable contract, the increase in sales and operating profit for that contract will reflect a higher return on sales in the current period due to the recognition of the higher profit booking rate on both current period costs, as well as previously incurred costs. As examples of how changes in profit booking rates can affect our financial statements, our net profit booking rate adjustments increased operating profit, net of state taxes, by approximately \$425 million and \$1,175 million for the quarter and nine months ended September 25, 2011, approximately \$325 million and \$975 million for the quarter and nine months ended September 26, 2010, and approximately \$1.4 billion and \$1.6 billion for 2010 and 2009, as we were able to successfully retire risks across a broad portfolio of contracts in those periods.

Services Method of Accounting

For cost-reimbursable contracts for services to non-U.S. Government customers that provide for award and incentive fees, we record net sales as services are performed, except for award and incentive fees. Award and incentive fees are recorded when they are fixed or determinable, generally at the date the amount is communicated to us by the customer. This approach results in the recognition of such fees at contractual intervals (typically every six months) throughout the contract and is dependent on the customer's processes for notification of awards and issuance of formal notifications. Under a fixed-price service contract, we are paid a predetermined fixed amount for a specified scope of work and generally have full responsibility for the costs associated with the contract and the resulting profit or loss. We record net sales under fixed-price service contracts on a straight-line basis over the period of contract performance, unless evidence suggests that net sales are earned or the obligations are fulfilled in a different pattern. Costs for all service contracts are expensed as incurred.

Other Contract Accounting Considerations

The majority of our sales are driven by pricing based on costs incurred to produce products or perform services under contracts with the U.S. Government. Cost-based pricing is determined under the Federal Acquisition Regulation (FAR). The FAR provides guidance on the types of costs that are allowable in establishing prices for goods and services under U.S. Government contracts. For example, costs such as those related to charitable contributions, interest expense, and certain advertising and public relations activities are unallowable and, therefore, not recoverable through sales. In addition, we may enter into advance agreements with the U.S. Government that address the subjects of allowability and allocability of costs to contracts for specific matters. For example, most of the environmental costs we incur for groundwater treatment and soil remediation related to sites operated in prior years are allocated to our current operations as general and administrative costs under FAR provisions and supporting advance agreements reached with the U.S. Government.

We closely monitor compliance with, and the consistent application of, our critical accounting policies related to contract accounting. Costs incurred and allocated to contracts are reviewed for compliance with U.S. Government regulations by our personnel, and are subject to audit by the Defense Contract Audit Agency.

Goodwill

Our goodwill at September 25, 2011 amounted to \$9.6 billion, including \$5.6 billion and \$3.4 billion for the reporting units in our Electronic Systems and IS&GS business segments. We review goodwill for impairment on an annual basis at the reporting unit level in the fourth quarter and whenever events or changes in circumstances indicate the carrying value of goodwill may not be recoverable. Such events or circumstances could include significant changes in the business climate of our industry, operating performance indicators, competition, or sale or disposal of a portion of a reporting unit. While there have been no events or changes in circumstances to date, government spending reductions, as discussed in the Update on Industry Considerations section on pages 23 and 24, as well as other factors have the potential to significantly impact our portfolio of business, which is heavily dependent upon discretionary appropriations for defense and other programs.

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Lockheed Martin Corporation

Item 3. Quantitative and Qualitative Disclosures About Market Risk

For quantitative and qualitative disclosures about market risk, see the following sections of our Annual Report on Form 10-K for the year ended December 31, 2010: Management's Discussion and Analysis of Financial Condition and Results of Operations under the caption Quantitative and Qualitative Disclosures About Market Risk on page 47; Note 1 under the caption Derivative financial instruments on page 58; and Note 10 beginning on page 68. During the first nine months of 2011, we entered into interest rate swap contracts that were not material to our financial statements (Note 9). Our exposures to market risk have not changed materially since December 31, 2010.

Item 4. Controls and Procedures

We performed an evaluation of the effectiveness of our disclosure controls and procedures as of September 25, 2011. The evaluation was performed with the participation of senior management of each business segment and key Corporate functions, and under the supervision of the Chief Executive Officer (CEO) 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 September 25, 2011.

There were no changes in our internal control over financial reporting during the most recently completed fiscal quarter that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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Lockheed Martin Corporation

FORWARD-LOOKING STATEMENTS

This Form 10-Q contains statements which, to the extent that they are not recitations of historical fact, constitute forward-looking statements within the meaning of the federal securities laws, and are based on our current expectations and assumptions. The words believe, estimate, anticipate, project, intend, expect, plan, outlook, forecast and similar expressions are intended to identify forward-looking statements. statements are not guarantees of future performance and are subject to risks and uncertainties. Actual results could differ materially due to factors such as:

- The availability of government funding for the Corporation's products and services both domestically and internationally due to performance, cost growth, or other factors;
- Changes in government and customer priorities and requirements (including cost-cutting initiatives, the potential deferral of awards, terminations or reduction of expenditures to respond to the priorities of Congress and the Administration, or budgetary cuts resulting from Congressional committee recommendations or automatic sequestration under the Budget Control Act of 2011);
- Additional costs or schedule revisions to the F-35 program that may result from the detailed re-planning of the restructured program that is ongoing following completion of the technical baseline review;
- Actual returns (or losses) on pension plan assets, movements in interest and discount rates and other changes that may affect pension plan assumptions;
- The effect of capitalization changes (such as share repurchase activity, advance pension funding, option exercises, or debt levels) on earnings per share;
- Difficulties in developing and producing operationally advanced technology systems;
- The timing and customer acceptance of product deliveries;
- Materials availability and performance by key suppliers, subcontractors and customers;
- Charges from any future impairment reviews that may result in the recognition of losses and a reduction in the book value of goodwill or other long-term assets;
- The future effect of legislation, rulemaking, and changes in accounting, tax, defense procurement, changes in policy, interpretations or challenges to the allowability of costs incurred under government cost accounting standards or export policies;
- The future impact of acquisitions or divestitures, joint ventures or teaming arrangements;
- The outcome of legal proceedings and other contingencies (including lawsuits, government investigations or audits, and the cost of completing environmental remediation efforts);
- The competitive environment for the Corporation's products and services and potential for delays in procurement due to bid protests;
- The ability to attract and retain key personnel; and
- Economic, business and political conditions domestically and internationally.

These are only some of the factors that may affect the forward-looking statements contained in this Form 10-Q. For a discussion identifying additional important factors that could cause actual results to vary materially from those anticipated in the forward-looking statements, see our filings with the SEC including, but not limited to, the discussions of Government Contracts and Regulation on page 9 and Risk Factors on pages 10 through 16, respectively, of our Annual Report on Form 10-K for the year ended December 31, 2010; Management's Discussion and Analysis of Financial Condition and Results of Operations on pages 23 through 45 of this Form 10-Q; and Note 3 Discontinued Operations, Note 7 Postretirement Benefit Plans, and Note 8 Legal Proceedings and Contingencies of the Notes to Unaudited Condensed Consolidated Financial Statements on page 9, page 12, and pages 13 through 17, respectively, included in this Form 10-Q.

Our actual financial results likely will be different from those projected due to the inherent nature of projections. Given these uncertainties, you should not rely on forward-looking statements in making investment decisions. The forward-looking statements contained in this

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Lockheed Martin Corporation

Form 10-Q speak only as of the date of its filing. We expressly disclaim a duty to provide updates to forward-looking statements after the date of this Form 10-Q to reflect subsequent events that have occurred, changed circumstances, changes in expectations, or the estimates and assumptions associated with them. The forward-looking statements in this Form 10-Q are intended to be subject to the safe harbor protection provided by the federal securities laws.

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Lockheed Martin Corporation

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

We are a party to or have property subject to litigation and other proceedings, including matters arising under provisions relating to the protection of the environment, as described in Note 8 Legal Proceedings and Contingencies in this Form 10-Q, and in our 2010 Annual Report on Form 10-K filed with the Securities Exchange Commission (Form 10-K). In the opinion of management and in-house counsel, the probability is remote that the outcome of each of those matters will have a material adverse effect on the Corporation as a whole, notwithstanding that the unfavorable resolution of any matter may have a material effect on our net earnings in any particular quarter. The results of legal proceedings, however, cannot be predicted with certainty.

We primarily are engaged in providing products and services under contracts with the U.S. Government and, to a lesser degree, under direct foreign sales contracts, some of which are funded by the U.S. Government. These contracts are subject to extensive legal and regulatory requirements and, from time to time, agencies of the U.S. Government investigate whether our operations are being conducted in accordance with these requirements. U.S. Government investigations of us, whether relating to these contracts or conducted for other reasons, could result in administrative, civil, or criminal liabilities, including repayments, fines, or penalties being imposed on us, or could lead to our suspension or debarment from future U.S. Government contracting. U.S. Government investigations often take years to complete and many result in no adverse action against us.

We are subject to federal and state requirements for protection of the environment, including those for discharge of hazardous materials and remediation of contaminated sites. Due in part to their complexity and pervasiveness, such requirements have resulted in us being involved with related legal proceedings, claims, and remediation obligations. The extent of our financial exposure cannot in all cases be reasonably estimated at this time. For information regarding these matters, including current estimates of the amounts that we believe are required for environmental remediation to the extent estimable, see Note 8 Legal Proceedings and Contingencies under the caption Environmental Matters in this Form 10-Q. In addition, in July 2011, Sandia Corporation, a subsidiary of the Corporation which manages Sandia National Laboratories for the Department of Energy, agreed to pay \$182,500 in penalties and costs in settlement of alleged violations related to the handling of hazardous waste treatment and storage at a facility in Livermore, California.

In addition, see the Legal Proceedings section of the Form 10-K for a description of previously reported matters.

Item 1A. Risk Factors

While we attempt to identify, manage, and mitigate risks and uncertainties associated with our business to the extent practical under the circumstances, some level of risk and uncertainty will always be present. Item 1A of our 2010 Form 10-K (pages 10 through 16) describes some of the risks and uncertainties associated with our business. These risks and uncertainties have the potential to materially affect our business, financial condition, results of operations, cash flows, projected results, and future prospects. We do not believe that there have been any material changes to the risk factors previously disclosed in our 2010 Form 10-K. See Update on Industry Considerations on pages 23 and 24 for an updated discussion of certain trends affecting our industry.

Table of Contents**Lockheed Martin Corporation****Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

There were no sales of unregistered equity securities during the quarter ended September 25, 2011.

The following table provides information about the purchases during the quarter ended September 25, 2011 of our equity securities that had been registered pursuant to Section 12 of the Exchange Act.

Issuer Purchases of Equity Securities

| Period | Total Number of Shares Purchased | Average Price Paid Per Share | Total Number of Shares Purchased as Part of Publicly Announced Program ⁽¹⁾ | Amount Available for Future Share Repurchases Under the Program ⁽²⁾ <i>(in millions)</i> |
|--|----------------------------------|------------------------------|---|--|
| July (June 27, 2011 – July 31, 2011) | 1,872,618 | \$ 77.98 | 1,872,618 | \$ 780 |
| August (August 1, 2011 – August 28, 2011) | 9,544,634 | \$ 70.46 | 9,544,634 | \$ 1,107 |
| September (August 29, 2011 – September 25, 2011) | 2,029,918 | \$ 71.70 | 2,029,918 | \$ 3,462 |
| Total | 13,447,170 | \$ 71.69 | 13,447,170 | \$ 3,462 |

⁽¹⁾ We repurchased a total of 13.4 million shares of our common stock for approximately \$964 million during the quarter ended September 25, 2011 under a share repurchase program that we announced in October 2010.

⁽²⁾ Our Board of Directors has approved a share repurchase program for the repurchase of our common stock from time-to-time, authorizing an amount available for share repurchases of \$6.5 billion, including \$1.0 billion and \$2.5 billion authorized for repurchase by our Board of Directors on August 22, 2011 and September 22, 2011. Under the program, management has discretion to determine the dollar amount of shares to be repurchased and the timing of any repurchases in compliance with applicable law and regulation. The program does not have an expiration date. As of September 25, 2011, we had repurchased a total of 41.1 million shares under the program for \$3,038 million.

Item 3. Defaults Upon Senior Securities

None.

Item 4. (Removed and Reserved)**Item 5. Other Information**

None.

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Lockheed Martin Corporation

Item 6. Exhibits

(a) Exhibits

| | |
|-----------------|---|
| Exhibit 10.1 | Lockheed Martin Corporation Deferred Management Incentive Compensation Plan, as amended |
| Exhibit 15 | Acknowledgment of Ernst & Young LLP, Independent Registered Public Accounting Firm |
| Exhibit 31.1 | Rule 13a-14(a) Certification of Robert J. Stevens |
| Exhibit 31.2 | Rule 13a-14(a) Certification of Bruce L. Tanner |
| Exhibit 32.1 | Certification Pursuant to 18 U.S.C. Section 1350 of Robert J. Stevens |
| Exhibit 32.2 | Certification Pursuant to 18 U.S.C. Section 1350 of Bruce L. Tanner |
| Exhibit 101.INS | XBRL Instance Document |
| Exhibit 101.SCH | XBRL Taxonomy Extension Schema Document |
| Exhibit 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document |
| Exhibit 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document |
| Exhibit 101.LAB | XBRL Taxonomy Extension Label Linkbase Document |
| Exhibit 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document |

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Lockheed Martin Corporation

SIGNATURE

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.

Lockheed Martin Corporation
(Registrant)

Date: October 27, 2011

by: /s/ Christopher J. Gregoire
Christopher J. Gregoire
Vice President and Controller
(Chief Accounting Officer)