

TEXTRON INC  
Form 10-Q  
July 26, 2012  
[Table of Contents](#)

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

---

**Form 10-Q**

---

(Mark One)

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

For the quarterly period ended June 30, 2012

OR

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

For the transition period from        to        .

Commission File Number 1-5480

## Textron Inc.

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of incorporation or organization)

**05-0315468**

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

**40 Westminster Street, Providence, RI**

(Address of principal executive offices)

**02903**

(Zip code)

**(401) 421-2800**

(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer  x

Accelerated filer  o

Non-accelerated filer  o

Smaller reporting company  o

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

As of July 13, 2012, there were 280,941,251 shares of common stock outstanding.



Table of Contents

## TEXTRON INC.

## INDEX

	Page
<b><u>PART I. FINANCIAL INFORMATION</u></b>	
<u>Item 1. Financial Statements</u>	
<u>Consolidated Statements of Operations (Unaudited)</u>	3
<u>Consolidated Statements of Comprehensive Income (Unaudited)</u>	4
<u>Consolidated Balance Sheets (Unaudited)</u>	5
<u>Consolidated Statements of Cash Flows (Unaudited)</u>	6
<u>Notes to the Consolidated Financial Statements (Unaudited)</u>	
<u>Note 1: Basis of Presentation</u>	8
<u>Note 2: Retirement Plans</u>	9
<u>Note 3: Earnings per Share</u>	9
<u>Note 4: Accounts Receivable and Finance Receivables</u>	10
<u>Note 5: Inventories</u>	13
<u>Note 6: Debt</u>	14
<u>Note 7: Accrued Liabilities</u>	14
<u>Note 8: Commitments and Contingencies</u>	14
<u>Note 9: Derivative Instruments and Fair Value Measurements</u>	14
<u>Note 10: Segment Information</u>	17
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	19
<u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u>	32
<u>Item 4. Controls and Procedures</u>	32
<b><u>PART II. OTHER INFORMATION</u></b>	
<u>Item 1. Legal Proceedings</u>	32
<u>Item 6. Exhibits</u>	33
<u>Signatures</u>	33

---

Table of Contents

## PART I. FINANCIAL INFORMATION

Item 1. FINANCIAL STATEMENTS

## TEXTRON INC.

## Consolidated Statements of Operations (Unaudited)

<i>(In millions, except per share amounts)</i>	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
<b>Revenues</b>				
Manufacturing revenues	\$ 2,964	\$ 2,695	\$ 5,759	\$ 5,148
Finance revenues	55	33	116	59
Total revenues	3,019	2,728	5,875	5,207
<b>Costs, expenses and other</b>				
Cost of sales	2,435	2,225	4,747	4,280
Selling and administrative expense	283	295	591	599
Provision for losses on finance receivables	(7)	12	(3)	24
Interest expense	53	61	108	123
Total costs, expenses and other	2,764	2,593	5,443	5,026
Income from continuing operations before income taxes	255	135	432	181
Income tax expense	82	43	139	58
<b>Income from continuing operations</b>	173	92	293	123
Loss from discontinued operations, net of income taxes	(1)	(2)	(3)	(4)
<b>Net income</b>	\$ 172	\$ 90	\$ 290	\$ 119
<b>Basic earnings per share</b>				
Continuing operations	\$ 0.61	\$ 0.33	\$ 1.04	\$ 0.44
Discontinued operations		(0.01)	(0.01)	(0.01)
<b>Basic earnings per share</b>	\$ 0.61	\$ 0.32	\$ 1.03	\$ 0.43
<b>Diluted earnings per share</b>				
Continuing operations	\$ 0.58	\$ 0.29	\$ 0.99	\$ 0.39
Discontinued operations			(0.01)	(0.01)
<b>Diluted earnings per share</b>	\$ 0.58	\$ 0.29	\$ 0.98	\$ 0.38
<b>Dividends per share</b>				
Common stock	\$ 0.02	\$ 0.02	\$ 0.04	\$ 0.04

See Notes to the consolidated financial statements.

Table of Contents**TEXTRON INC.****Consolidated Statements of Comprehensive Income (Unaudited)**

<i>(In millions)</i>	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
Net income	\$ 172	\$ 90	\$ 290	\$ 119
Other comprehensive income (loss), net of tax:				
Recognition of prior service cost and unrealized losses on pension and postretirement benefits	21	15	42	33
Foreign currency translation	(16)	7	(13)	23
Deferred gains on hedge contracts, net of reclassifications	(3)	(2)	(3)	
Comprehensive income	\$ 174	\$ 110	\$ 316	\$ 175

See Notes to the consolidated financial statements.

Table of Contents

## TEXTRON INC.

## Consolidated Balance Sheets (Unaudited)

<i>(Dollars in millions)</i>	June 30, 2012	December 31, 2011
<b>Assets</b>		
<b>Manufacturing group</b>		
Cash and equivalents	\$ 898	\$ 871
Accounts receivable, net	917	856
Inventories	2,759	2,402
Other current assets	704	1,134
<b>Total current assets</b>	5,278	5,263
Property, plant and equipment, less accumulated depreciation and amortization of \$3,216 and \$3,097	2,027	1,996
Goodwill	1,630	1,635
Other assets	1,510	1,508
<b>Total Manufacturing group assets</b>	10,445	10,402
<b>Finance group</b>		
Cash and equivalents	13	14
Finance receivables held for investment, net	2,006	2,321
Finance receivables held for sale	244	418
Other assets	360	460
<b>Total Finance group assets</b>	2,623	3,213
<b>Total assets</b>	\$ 13,068	\$ 13,615
<b>Liabilities and shareholders equity</b>		
<b>Liabilities</b>		
<b>Manufacturing group</b>		
Current portion of long-term debt	\$ 507	\$ 146
Accounts payable	886	833
Accrued liabilities	1,837	1,952
<b>Total current liabilities</b>	3,230	2,931
Other liabilities	2,668	2,826
Long-term debt	1,809	2,313
<b>Total Manufacturing group liabilities</b>	7,707	8,070
<b>Finance group</b>		
Other liabilities	200	333
Due to Manufacturing group	249	493
Debt	1,810	1,974
<b>Total Finance group liabilities</b>	2,259	2,800
<b>Total liabilities</b>	9,966	10,870
<b>Shareholders equity</b>		
Common stock	35	35
Capital surplus	1,133	1,081
Retained earnings	3,536	3,257
Accumulated other comprehensive loss	(1,599)	(1,625)
	3,105	2,748
Less cost of treasury shares	3	3
<b>Total shareholders equity</b>	3,102	2,745
<b>Total liabilities and shareholders equity</b>	\$ 13,068	\$ 13,615
<b>Common shares outstanding (in thousands)</b>	280,828	278,873

See Notes to the consolidated financial statements.





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

For the Six Months Ended June 30, 2012 and July 2, 2011, respectively

<i>(In millions)</i>	2012	Consolidated	2011
<b>Cash flows from operating activities</b>			
Net income	\$ 290		\$ 119
Less: Loss from discontinued operations	(3)		(4)
Income from continuing operations	293		123
Adjustments to reconcile income from continuing operations to net cash provided by (used in) operating activities:			
Non-cash items:			
Depreciation and amortization	183		195
Provision for losses on finance receivables held for investment	(3)		24
Portfolio losses on finance assets	41		44
Deferred income taxes	85		57
Other, net	6		79
Changes in assets and liabilities:			
Accounts receivable, net	(67)		36
Inventories	(387)		(276)
Other assets	24		(51)
Accounts payable	57		110
Accrued and other liabilities	(317)		(230)
Captive finance receivables, net	117		106
Other operating activities, net	(4)		2
Net cash provided by operating activities of continuing operations	28		219
Net cash used in operating activities of discontinued operations	(3)		(2)
Net cash provided by operating activities	25		217
<b>Cash flows from investing activities</b>			
Finance receivables originated or purchased	(19)		(110)
Finance receivables repaid	336		422
Proceeds on receivable sales	69		257
Capital expenditures	(158)		(169)
Proceeds from sale of repossessed assets and properties	48		72
Other investing activities, net	30		29
Net cash provided by investing activities	306		501
<b>Cash flows from financing activities</b>			
Increase in short-term debt			189
Payments on long-term lines of credit			(940)
Principal payments on long-term and nonrecourse debt	(393)		(511)
Proceeds from issuance of long-term debt	88		265
Dividends paid	(11)		(11)
Other financing activities, net	12		(1)
Net cash used in financing activities	(304)		(1,009)
Effect of exchange rate changes on cash and equivalents	(1)		11
<b>Net increase (decrease) in cash and equivalents</b>	26		(280)
Cash and equivalents at beginning of period	885		931
Cash and equivalents at end of period	\$ 911		\$ 651

See Notes to the consolidated financial statements



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

For the Six Months Ended June 30, 2012 and July 2, 2011, respectively

<i>(In millions)</i>	<b>Manufacturing Group</b>		<b>Finance Group</b>	
	<b>2012</b>	<b>2011</b>	<b>2012</b>	<b>2011</b>
<b>Cash flows from operating activities</b>				
Net income (loss)	\$ 264	\$ 171	\$ 26	\$ (52)
Less: Loss from discontinued operations	(3)	(4)		
Income (loss) from continuing operations	267	175	26	(52)
Adjustments to reconcile income (loss) from continuing operations to net cash provided by (used in) operating activities:				
Dividends received from Finance Group	315	179		
Capital contribution paid to Finance Group	(240)	(112)		
Non-cash items:				
Depreciation and amortization	170	180	13	15
Provision for losses on finance receivables held for investment			(3)	24
Portfolio losses on finance assets			41	44
Deferred income taxes	57	50	28	7
Other, net	50	66	(44)	13
Changes in assets and liabilities:				
Accounts receivable, net	(67)	36		
Inventories	(388)	(279)		
Other assets	26	(51)	(2)	(3)
Accounts payable	57	110		
Accrued and other liabilities	(162)	(210)	(155)	(20)
Other operating activities, net	(4)	2		
Net cash provided by (used in) operating activities of continuing operations	81	146	(96)	28
Net cash used in operating activities of discontinued operations	(3)	(2)		
Net cash provided by (used in) operating activities	78	144	(96)	28
<b>Cash flows from investing activities</b>				
Finance receivables originated or purchased			(114)	(244)
Finance receivables repaid			548	662
Proceeds on receivable sales			69	257
Capital expenditures	(158)	(169)		
Proceeds from sale of repossessed assets and properties			48	72
Other investing activities, net	2	(42)	29	37
Net cash provided by (used in) investing activities	(156)	(211)	580	784
<b>Cash flows from financing activities</b>				
Increase in short-term debt		189		
Payments on long-term lines of credit				(940)
Intergroup financing	245	(395)	(245)	395
Principal payments on long-term and nonrecourse debt	(139)	(13)	(254)	(498)
Proceeds from issuance of long-term debt			88	265
Capital contributions paid to Finance group under Support Agreement			240	112
Other capital contributions paid to Finance group				40
Dividends paid	(11)	(11)	(315)	(179)
Other financing activities, net	11	(1)	1	
Net cash provided by (used in) financing activities	106	(231)	(485)	(805)
Effect of exchange rate changes on cash and equivalents	(1)	10		1
<b>Net increase (decrease) in cash and equivalents</b>	<b>27</b>	<b>(288)</b>	<b>(1)</b>	<b>8</b>

Edgar Filing: TEXTRON INC - Form 10-Q

Cash and equivalents at beginning of period		871		898		14		33
Cash and equivalents at end of period	\$	898	\$	610	\$	13	\$	41

*See Notes to the consolidated financial statements.*

Table of Contents

**TEXTRON INC.**

**Notes to the Consolidated Financial Statements (Unaudited)**

**Note 1: Basis of Presentation**

Our consolidated financial statements include the accounts of Textron Inc. and its majority-owned subsidiaries. We have prepared these unaudited consolidated financial statements in accordance with accounting principles generally accepted in the U.S. for interim financial information. Accordingly, these interim financial statements do not include all of the information and footnotes required by accounting principles generally accepted in the U.S. for complete financial statements. The consolidated interim financial statements included in this quarterly report should be read in conjunction with the consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2011. In the opinion of management, the interim financial statements reflect all adjustments (consisting only of normal recurring adjustments) that are necessary for the fair presentation of our consolidated financial position, results of operations and cash flows for the interim periods presented. The results of operations for the interim periods are not necessarily indicative of the results to be expected for the full year.

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

*Use of Estimates*

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

During 2012 and 2011, we changed our estimates of revenues and costs on certain long-term contracts that are accounted for under the percentage-of-completion method of accounting. The changes in estimates increased income from continuing operations before income taxes in the second quarter of 2012 and 2011 by \$12 million and \$10 million, respectively, (\$8 million and \$7 million after tax, or \$0.03 and \$0.02 per diluted share, respectively). For the second quarter of 2012 and 2011, the gross favorable program profit adjustments totaled \$23 million and \$21 million, respectively, and the gross unfavorable program profit adjustments totaled \$11 million for each quarter.

## Edgar Filing: TEXTRON INC - Form 10-Q

The changes in estimates increased income from continuing operations before income taxes in the first half of 2012 and 2011 by \$16 million and \$24 million, (\$10 million and \$15 million after tax, or \$0.04 and \$0.05 per diluted share, respectively). For the first half of 2012 and 2011, the gross favorable program profit adjustments totaled \$40 million and \$42 million, respectively, and the gross unfavorable program profit adjustments totaled \$24 million and \$18 million, respectively.

Table of Contents**Note 2: Retirement Plans**

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

<i>(In millions)</i>	Pension Benefits		Postretirement Benefits Other Than Pensions	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
<b>Three Months Ended</b>				
Service cost	\$ 29	\$ 32	\$ 1	\$ 2
Interest cost	76	82	7	8
Expected return on plan assets	(102)	(98)		
Amortization of prior service cost (credit)	4	4	(3)	(2)
Amortization of net loss	30	19	1	3
Net periodic benefit cost	\$ 37	\$ 39	\$ 6	\$ 11
<b>Six Months Ended</b>				
Service cost	\$ 59	\$ 64	\$ 3	\$ 4
Interest cost	152	164	13	16
Expected return on plan assets	(203)	(196)		
Amortization of prior service cost (credit)	8	8	(6)	(3)
Amortization of net loss	59	38	3	6
Net periodic benefit cost	\$ 75	\$ 78	\$ 13	\$ 23

**Note 3: Earnings Per Share**

We calculate basic and diluted earnings per share (EPS) based on net income, which approximates income available to common shareholders for each period. Basic EPS is calculated using the two-class method, which includes the weighted-average number of common shares outstanding during the period and restricted stock units to be paid in stock that are deemed participating securities as they provide nonforfeitable rights to dividends. Diluted EPS considers the dilutive effect of all potential future common stock, including stock options, restricted stock units and the shares that could be issued upon the conversion of our convertible notes and upon the exercise of the related warrants. The call options purchased in connection with the issuance of the convertible notes and the capped call transaction entered into in 2011 are excluded from the calculation of diluted EPS as their impact is always anti-dilutive.

Upon conversion of our convertible notes, as described in Note 8 of our 2011 Form 10-K, the principal amount would be settled in cash, and the excess of the conversion value, as defined, over the principal amount may be settled in cash and/or shares of our common stock. Therefore, only the shares of our common stock potentially issuable with respect to the excess of the notes' conversion value over the principal amount, if any, are considered as dilutive potential common shares for purposes of calculating diluted EPS.

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

Edgar Filing: TEXTRON INC - Form 10-Q

<i>(In thousands)</i>	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
Basic weighted-average shares outstanding	281,114	277,406	280,568	276,882
Dilutive effect of:				
Convertible notes and warrants	14,021	36,838	13,960	39,275
Stock options and restricted stock units	412	964	552	1,104
Diluted weighted-average shares outstanding	295,547	315,208	295,080	317,261

Stock options to purchase 7 million shares of common stock outstanding are excluded from our calculation of diluted weighted-average shares outstanding for the three and six months ended June 30, 2012, as the exercise prices were greater than the average market price of our common stock for the periods. Stock options to purchase 3 million shares of common stock outstanding are excluded from our calculation of diluted weighted-average shares outstanding for both the three and six months ended July 2, 2011, as the exercise prices were greater than the average market price of our common stock for the periods. These securities could potentially dilute EPS in the future.



Table of Contents**Note 4: Accounts Receivable and Finance Receivables****Accounts Receivable**

Accounts receivable is composed of the following:

<i>(In millions)</i>	<b>June 30, 2012</b>	<b>December 31, 2011</b>
Commercial	\$ 577	\$ 528
U.S. Government contracts	358	346
	935	874
Allowance for doubtful accounts	(18)	(18)
Total accounts receivable, net	\$ 917	\$ 856

We have unbillable receivables primarily on U.S. Government contracts that arise when the revenues we have appropriately recognized based on performance cannot be billed yet under terms of the contract. Unbillable receivables within accounts receivable totaled \$213 million at June 30, 2012 and \$192 million at December 31, 2011.

**Finance Receivables**

Finance receivables by product line, which includes both finance receivables held for investment and finance receivables held for sale, are presented in the following table. Beginning this quarter, we are reporting our captive business as one product line, which primarily includes aviation finance receivables, and to a limited extent, golf equipment finance receivables.

<i>(In millions)</i>	<b>June 30, 2012</b>	<b>December 31, 2011</b>
Captive	\$ 1,753	\$ 1,945
Golf Mortgage	244	381
Timeshare	203	318
Structured Capital	149	208
Other liquidating	23	43
Total finance receivables	2,372	2,895
Less: Allowance for losses	122	156
Less: Finance receivables held for sale	244	418
Total finance receivables held for investment, net	\$ 2,006	\$ 2,321

*Credit Quality Indicators and Nonaccrual Finance Receivables*

## Edgar Filing: TEXTRON INC - Form 10-Q

We internally assess the quality of our finance receivables held for investment portfolio based on a number of key credit quality indicators and statistics such as delinquency, loan balance to estimated collateral value, the liquidity position of individual borrowers and guarantors and default rates of our notes receivable collateral in the Timeshare product line. Because many of these indicators are difficult to apply across an entire class of receivables, we evaluate individual loans on a quarterly basis and classify these loans into three categories based on the key credit quality indicators for the individual loan. These three categories are performing, watchlist and nonaccrual.

We classify finance receivables held for investment as nonaccrual if credit quality indicators suggest full collection is doubtful. In addition, we automatically classify accounts as nonaccrual once they are contractually delinquent by more than three months unless collection is not doubtful. Cash payments on nonaccrual accounts, including finance charges, generally are applied to reduce the net investment balance. We resume the accrual of interest when the loan becomes contractually current through payment according to the original terms of the loan or, if a loan has been modified, following a period of performance under the terms of the modification, provided we conclude that collection of all principal and interest is no longer doubtful. Previously suspended interest income is recognized at that time.

Accounts are classified as watchlist when credit quality indicators have deteriorated as compared with typical underwriting criteria, and we believe collection of full principal and interest is probable but not certain. All other finance receivables held for investment that do not meet the watchlist or nonaccrual categories are classified as performing.

## Edgar Filing: TEXTRON INC - Form 10-Q

### Table of Contents

A summary of finance receivables held for investment categorized based on the credit quality indicators discussed above is as follows:

<i>(In millions)</i>	June 30, 2012				December 31, 2011			
	Performing	Watchlist	Nonaccrual	Total	Performing	Watchlist	Nonaccrual	Total
Captive	\$ 1,491	\$ 150	\$ 112	\$ 1,753	\$ 1,558	\$ 251	\$ 136	\$ 1,945
Timeshare	73	4	126	203	89	25	167	281
Structured Capital	144	5		149	203	5		208
Other liquidating	9		14	23	25		18	43
<b>Total</b>	<b>\$ 1,717</b>	<b>\$ 159</b>	<b>\$ 252</b>	<b>\$ 2,128</b>	<b>\$ 1,875</b>	<b>\$ 281</b>	<b>\$ 321</b>	<b>\$ 2,477</b>
% of Total	80.7%	7.5%	11.8%		75.7%	11.3%	13.0%	

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

Finance receivables held for investment by delinquency aging category are summarized in the table below:

<i>(In millions)</i>	June 30, 2012					December 31, 2011				
	Less Than 31 Days Past Due	31-60 Days Past Due	61-90 Days Past Due	Over 90 Days Past Due	Total	Less Than 31 Days Past Due	31-60 Days Past Due	61-90 Days Past Due	Over 90 Days Past Due	Total
	Captive	\$ 1,571	\$ 43	\$ 71	\$ 68	\$ 1,753	\$ 1,758	\$ 69	\$ 43	\$ 75
Timeshare	171	10		22	203	238	3		40	281
Structured Capital	149				149	208				208
Other liquidating	15			8	23	35			8	43
<b>Total</b>	<b>\$ 1,906</b>	<b>\$ 53</b>	<b>\$ 71</b>	<b>\$ 98</b>	<b>\$ 2,128</b>	<b>\$ 2,239</b>	<b>\$ 72</b>	<b>\$ 43</b>	<b>\$ 123</b>	<b>\$ 2,477</b>

We had no accrual status loans that were greater than 90 days past due at June 30, 2012 or at December 31, 2011. At June 30, 2012, the 60+ days contractual delinquency as a percentage of finance receivables held for investment was 7.94%, compared with 6.70% at December 31, 2011.

### *Loan Modifications*

Troubled debt restructurings occur when we have either modified the contract terms of finance receivables held for investment for borrowers experiencing financial difficulties or accepted a transfer of assets in full or partial satisfaction of the loan balance. The types of modifications we typically make include extensions of the original maturity date of the contract, extensions of revolving borrowing periods, delays in the timing of required principal payments, deferrals of interest payments, advances to protect the value of our collateral and principal reductions contingent on full repayment prior to the maturity date. The changes effected by modifications made during the first half of 2012 to finance receivables held for investment were not material, primarily as a result of the reclassification of the Golf Mortgage finance receivables from the held for investment classification to the held for sale classification at December 31, 2011.

*Impaired Loans*

We evaluate individual finance receivables held for investment in non-homogeneous portfolios and larger accounts in homogeneous loan portfolios for impairment on a quarterly basis. Finance receivables classified as held for sale are reflected at the lower of cost or fair value and are excluded from these evaluations. A finance receivable is considered impaired when it is probable that we will be unable to collect all amounts due according to the contractual terms of the loan agreement based on our review of the credit quality indicators discussed above. Impaired finance receivables include both nonaccrual accounts and accounts for which full collection of principal and interest remains probable, but the account's original terms have been, or are expected to be, significantly modified. If the modification specifies an interest rate equal to or greater than a market rate for a finance receivable with comparable risk, the account is not considered impaired in years subsequent to the modification. There was no significant interest income recognized on impaired loans in the first half of 2012 or 2011.

Table of Contents

A summary of impaired finance receivables, excluding leveraged leases, is provided below:

<i>(In millions)</i>	<b>Impaired Loans with No Related Allowance for Credit Losses</b>	<b>Recorded Investment Impaired Loans with Related Allowance for Credit Losses</b>	<b>Total Impaired Loans</b>	<b>Unpaid Principal Balance</b>	<b>Allowance For Losses On Impaired Loans</b>	<b>Average Recorded Investment</b>
<b>June 30, 2012</b>						
Captive	\$ 28	\$ 85	\$ 113	\$ 119	\$ 23	\$ 121
Timeshare	95	62	157	214	29	195
Other liquidating	1	12	13	23	9	14
<b>Total</b>	<b>\$ 124</b>	<b>\$ 159</b>	<b>\$ 283</b>	<b>\$ 356</b>	<b>\$ 61</b>	<b>\$ 330</b>
<b>December 31, 2011</b>						
Captive	\$ 47	\$ 94	\$ 141	\$ 144	\$ 40	\$ 149
Timeshare	170	57	227	288	38	315
Golf Mortgage						232
Other liquidating	3	12	15	59	9	30
<b>Total</b>	<b>\$ 220</b>	<b>\$ 163</b>	<b>\$ 383</b>	<b>\$ 491</b>	<b>\$ 87</b>	<b>\$ 726</b>

*Allowance for Losses*

We maintain the allowance for losses on finance receivables held for investment at a level considered adequate to cover inherent losses in the portfolio based on management's evaluation and analysis by product line. For larger balance accounts specifically identified as impaired, including large accounts in homogeneous portfolios, a reserve is established based on comparing the carrying value with either a) the expected future cash flows, discounted at the finance receivable's effective interest rate; or b) the fair value of the underlying collateral, if the finance receivable is collateral dependent. The expected future cash flows consider collateral value; financial performance and liquidity of our borrower; existence and financial strength of guarantors; estimated recovery costs, including legal expenses; and costs associated with the repossession/foreclosure and eventual disposal of collateral. When there is a range of potential outcomes, we perform multiple discounted cash flow analyses and weight the potential outcomes based on their relative likelihood of occurrence.

The evaluation of our portfolios is inherently subjective, as it requires estimates, including the amount and timing of future cash flows expected to be received on impaired finance receivables and the estimated fair value of the underlying collateral, which may differ from actual results. While our analysis is specific to each individual account, critical factors included in this analysis vary by product line and include the following:

- *Captive* - industry valuation guides, age and physical condition of the collateral, payment history, and existence and financial strength of guarantors.
- *Timeshare* - historical performance of consumer notes receivable collateral, real estate valuations, operating expenses of the borrower, the impact of bankruptcy court rulings on the value of the collateral, legal and other professional expenses and borrower's access to capital.

## Edgar Filing: TEXTRON INC - Form 10-Q

We also establish an allowance for losses by product line to cover probable but specifically unknown losses existing in the portfolio. For homogeneous portfolios, including Captive, the allowance is established as a percentage of non-recourse finance receivables, which have not been identified as requiring specific reserves. The percentage is based on a combination of factors, including historical loss experience, current delinquency and default trends, collateral values and both general economic and specific industry trends. For non-homogeneous portfolios, such as Timeshare, the allowance is established as a percentage of watchlist balances, as defined on page 10, which represents a combination of assumed default likelihood and loss severity based on historical experience, industry trends and collateral values. In estimating our allowance for losses to cover accounts not specifically identified, critical factors vary by product line and include the following:

## Edgar Filing: TEXTRON INC - Form 10-Q

### Table of Contents

- *Captive* - the collateral value of the portfolio, historical default experience and delinquency trends.
- *Timeshare* - individual loan credit quality indicators such as borrowing base shortfalls for revolving notes receivable facilities, default rates of our notes receivable collateral, borrower's access to capital, historical progression from watchlist to nonaccrual status and estimates of loss severity based on analysis of impaired loans in the product line.

Finance receivables held for investment are written down to the fair value (less estimated costs to sell) of the related collateral when the collateral is repossessed and are charged off when the remaining balance is deemed to be uncollectible.

A rollforward of the allowances for losses on finance receivables held for investment is provided below:

<i>(In millions)</i>	Captive	Golf Mortgage	Timeshare	Other liquidating	Total
<b>For the six months ended June 30, 2012</b>					
Beginning balance	\$ 101	\$	\$ 40	\$ 15	\$ 156
Provision for losses			2	(5)	(3)
Charge-offs	(26)		(13)	(1)	(40)
Recoveries	7			2	9
Ending balance	\$ 82	\$	\$ 29	\$ 11	\$ 122
<b>For the six months ended July 2, 2011</b>					
Beginning balance	\$ 123	\$ 79	\$ 106	\$ 34	\$ 342
Provision for losses	14	(1)	10	1	24
Charge-offs	(26)	(4)	(28)	(10)	(68)
Recoveries	6			8	14
Transfers				(13)	(13)
Ending balance	\$ 117	\$ 74	\$ 88	\$ 20	\$ 299

A summary of the allowance for losses on finance receivables that are evaluated on an individual and on a collective basis is provided below. The finance receivables reported in this table specifically exclude \$149 million and \$281 million of leveraged leases at June 30, 2012 and July 2, 2011, respectively, in accordance with authoritative accounting standards.

<i>(In millions)</i>	June 30, 2012				July 2, 2011			
	Finance Receivables Evaluated		Allowance Based on Individual Evaluation	Allowance Based on Collective Evaluation	Finance Receivables Evaluated		Allowance Based on Individual Evaluation	Allowance Based on Collective Evaluation
	Individually	Collectively			Individually	Collectively		
Captive	\$ 113	\$ 1,640	\$ 23	\$ 59	\$ 143	\$ 2,009	\$ 44	\$ 73
Timeshare	157	46	29		322	188	86	2
Golf Mortgage					294	325	44	30
Other liquidating	13	10	9	2	28	54	9	11
Total	\$ 283	\$ 1,696	\$ 61	\$ 61	\$ 787	\$ 2,576	\$ 183	\$ 116

### **Note 5: Inventories**

Edgar Filing: TEXTRON INC - Form 10-Q

<i>(In millions)</i>	<b>June 30, 2012</b>		<b>December 31, 2011</b>	
Finished goods	\$	1,288	\$	1,012
Work in process		2,260		2,202
Raw materials		449		399
		3,997		3,613
Progress/milestone payments		(1,238)		(1,211)
	\$	2,759	\$	2,402



Table of Contents**Note 6: Debt**

At June 30, 2012, the principal amount of our convertible senior notes was \$215 million. Our common stock price exceeded the \$17.06 per share conversion threshold price set forth for these convertible notes for at least 20 trading days during the 30 consecutive trading days ended June 30, 2012. Accordingly, these notes are convertible at the holder's option through September 30, 2012. We may deliver shares of common stock, cash or a combination of cash and shares of common stock in satisfaction of our obligations upon conversion of the convertible notes. Based on a June 30, 2012 stock price of \$24.87, the if converted value exceeds the face amount of the remaining notes by \$192 million; however, after giving effect to the exercise of the related outstanding call options and warrants, the incremental cash or share settlement in excess of the face amount would result in either a 6 million net share issuance or a cash payment of \$149 million, or a combination of cash and stock, at our option.

**Note 7: Accrued Liabilities**

We provide limited warranty and product maintenance programs, including parts and labor, for certain products for periods ranging from one to five years. Changes in our warranty and product maintenance liabilities are as follows:

<i>(In millions)</i>	Six Months Ended	
	June 30, 2012	July 2, 2011
Accrual at the beginning of period	\$ 224	\$ 242
Provision	124	111
Settlements	(123)	(116)
Adjustments to prior accrual estimates	(4)	(7)
Accrual at the end of period	\$ 221	\$ 230

**Note 8: Commitments and Contingencies**

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

On February 7, 2012, a lawsuit was filed in the United States Bankruptcy Court, Northern District of Ohio, Eastern Division (Akron) by Brian A. Bash, Chapter 7 Trustee for Fair Finance Company against TFC, Fortress Credit Corp. and Fair Facility I, LLC. TFC provided a revolving line of credit of up to \$17.5 million to Fair Finance Company from 2002 through 2007. The complaint alleges numerous counts against TFC, as Fair Finance Company's working capital lender, including receipt of fraudulent transfers and assisting in fraud perpetrated on Fair Finance investors. The Trustee seeks avoidance and recovery of alleged fraudulent transfers in the amount of \$316 million as well as damages of \$223 million on the other claims. The Trustee also seeks trebled damages on all claims under Ohio law. We intend to vigorously defend this lawsuit,

and on April 20, 2012, TFC moved to dismiss all claims in the complaint. That motion is still pending. An estimate of a range of possible loss cannot be made at this time due to the early stage of the litigation.

**Note 9: Derivative Instruments and Fair Value Measurements**

We measure fair value at the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. We prioritize the assumptions that market participants would use in pricing the asset or liability into a three-tier fair value hierarchy. This fair value hierarchy gives the highest priority (Level 1) to quoted prices in active markets for identical assets or liabilities and the lowest priority (Level 3) to unobservable inputs in which little or no market data exist, requiring companies to develop their own assumptions. Observable inputs that do not meet the criteria of Level 1, which include quoted prices for similar assets or liabilities in active markets or quoted prices for identical assets and liabilities in markets that are not active, are categorized as Level 2. Level 3 inputs are those that reflect our estimates about the assumptions market participants

Table of Contents

would use in pricing the asset or liability based on the best information available in the circumstances. Valuation techniques for assets and liabilities measured using Level 3 inputs may include methodologies such as the market approach, the income approach or the cost approach and may use unobservable inputs such as projections, estimates and management's interpretation of current market data. These unobservable inputs are utilized only to the extent that observable inputs are not available or cost-effective to obtain.

**Assets and Liabilities Recorded at Fair Value on a Recurring Basis**

The assets and liabilities that are recorded at fair value on a recurring basis consist primarily of our derivative financial instruments, which are categorized as Level 2 in the fair value hierarchy. The fair value amounts of these instruments that are designated as hedging instruments are provided below:

<i>(In millions)</i>	<b>Borrowing Group</b>	<b>Balance Sheet Location</b>	<b>Asset (Liability)</b>	
			<b>June 30, 2012</b>	<b>December 31, 2011</b>
<b>Assets</b>				
Interest rate exchange contracts*	Finance	Other assets	\$ 16	\$ 22
Foreign currency exchange contracts	Manufacturing	Other current assets	5	9
Total			\$ 21	\$ 31
<b>Liabilities</b>				
Interest rate exchange contracts*	Finance	Other liabilities	\$ (9)	\$ (7)
Foreign currency exchange contracts	Manufacturing	Accrued liabilities	(1)	(5)
Total			\$ (10)	\$ (12)

\*Interest rate exchange contracts represent fair value hedges.

The Finance group's interest rate exchange contracts are not exchange traded and are measured at fair value utilizing widely accepted, third-party developed valuation models. The actual terms of each individual contract are entered into a valuation model, along with interest rate and foreign exchange rate data, which is based on readily observable market data published by third-party leading financial news and data providers. Credit risk is factored into the fair value of these assets and liabilities based on the differential between both our credit default swap spread for liabilities and the counterparty's credit default swap spread for assets as compared with a standard AA-rated counterparty; however, this had no significant impact on the valuation at June 30, 2012. At June 30, 2012 and December 31, 2011, we had interest rate exchange contracts with notional amounts upon which the contracts were based of \$770 million and \$848 million, respectively.

Foreign currency exchange contracts are measured at fair value using the market method valuation technique. The inputs to this technique utilize current foreign currency exchange forward market rates published by third-party leading financial news and data providers. These are observable data that represent the rates that the financial institution uses for contracts entered into at that date; however, they are not based on actual transactions so they are classified as Level 2. At June 30, 2012 and December 31, 2011, we had foreign currency exchange contracts with notional amounts upon which the contracts were based of \$680 million and \$645 million, respectively.

*Fair Value Hedges*

Our Finance group enters into interest rate exchange contracts to mitigate exposure to changes in the fair value of its fixed-rate receivables and debt due to fluctuations in interest rates. By using these contracts, we are able to convert our fixed-rate cash flows to floating-rate cash flows. The amount of ineffectiveness on our fair value hedges and the gain (loss) recorded in the Consolidated Statements of Operations were both insignificant in the first half of 2012 and 2011.

*Cash Flow Hedges*

We manufacture and sell our products in a number of countries throughout the world, and, therefore, we are exposed to movements in foreign currency exchange rates. The primary purpose of our foreign currency hedging activities is to manage the volatility associated with foreign currency purchases of materials, foreign currency sales of products, and other assets and liabilities in the normal course of business. We primarily utilize forward exchange contracts and purchased options with maturities of no more than three years that qualify as cash flow hedges and are intended to offset the effect of exchange rate fluctuations on forecasted sales, inventory purchases and overhead expenses. At June 30, 2012, we had a net deferred gain of \$5 million in Accumulated other comprehensive loss related to these cash flow hedges. Net gains and losses recognized in earnings and Accumulated other comprehensive loss on these cash flow hedges, including gains and losses related to hedge ineffectiveness, were not material in the three and six months ended June 30, 2012 and July 2, 2011. We do not expect the amount of gains and losses in Accumulated other comprehensive loss that will be reclassified to earnings in the next twelve months to be material.

Table of Contents

We hedge our net investment position in major currencies and generate foreign currency interest payments that offset other transactional exposures in these currencies. To accomplish this, we borrow directly in foreign currency and designate a portion of foreign currency debt as a hedge of net investments. We also may utilize currency forwards as hedges of our related foreign net investments. We record changes in the fair value of these contracts in other comprehensive income to the extent they are effective as cash flow hedges. If a contract does not qualify for hedge accounting or is designated as a fair value hedge, changes in the fair value of the contract are recorded in earnings. Currency effects on the effective portion of these hedges, which are reflected in the foreign currency translation adjustment account within other comprehensive income, produced a \$4 million after-tax gain for the first half of 2012, resulting in an accumulated net gain balance of \$22 million at June 30, 2012. The ineffective portion of these hedges was insignificant.

**Assets Recorded at Fair Value on a Nonrecurring Basis**

The fair value measurement adjustments recorded during the first half of 2012 and 2011 for each asset class measured on a nonrecurring basis are presented in the gain (loss) columns below, along with the balance of the asset class measured at fair value at the end of each period. These assets are in the Finance group and were measured using significant unobservable inputs (Level 3).

(In millions)	Balance at		Gain (Loss) Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
Finance receivables held for sale	\$ 244	\$ 180	\$ 44	\$ (14)
Impaired finance receivables	110	407	(7)	(50)
Repossessed assets and properties	138	91	(32)	(18)

*Finance Receivables Held for Sale* Finance receivables held for sale are recorded at fair value on a nonrecurring basis during periods in which the fair value is lower than the cost value. There are no active, quoted market prices for these finance receivables. At June 30, 2012, our finance receivables held for sale represents the Golf Mortgage portfolio. Fair value of this portfolio was determined based on the use of discounted cash flow models to estimate the price we expect to receive in the principal market for each pool of similar loans, in an orderly transaction. The discount rates utilized in these models are derived from prevailing interest rate indices and are based on the nature of the assets, discussions with market participants and our experience in the actual disposition of similar assets. The cash flow models also include the use of qualitative assumptions regarding the borrower's ability to pay and the period of time that will likely be required to restructure and/or exit the account through acquisition of the underlying collateral. We utilize revenue and earnings multiples to determine the expected value of the loan collateral. The range of multiples used is based on bids from prospective buyers, inputs from market participants and prices at which sales have been transacted for similar properties. The gains on finance receivables held for sale for the six months ended June 30, 2012 are primarily the result of the payoff and sale of loans at prices in excess of the values established in previous periods.

Based on our qualitative assumptions, we separate the loans into three categories for the cash flow models. In the first category, we include loans that we assume will be paid in accordance with the contractual terms of the loan. In the second category, we include loans where we perceive that the borrower has less of an ability to pay, and we assume that the loan will be restructured and resolved typically over a period of one to four years. For the third category, we assume that the borrower will default on the loan and that it will be resolved within an average of 24 months. The fair values of these finance receivables are sensitive to variability in both the quantitative and qualitative assumptions. Changes in the borrower's ability to pay or the period of time required to restructure and/or exit accounts may significantly increase or decrease the fair value of these finance receivables, and, to a lesser extent, fluctuations in discount rates and/or revenue and earnings multiples could also change the fair value of these finance receivables.

## Edgar Filing: TEXTRON INC - Form 10-Q

*Impaired Finance Receivables* Impaired nonaccrual finance receivables represent assets recorded at fair value on a nonrecurring basis since the measurement of required reserves on our impaired finance receivables is significantly dependent on the fair value of the underlying collateral. For our Captive impaired nonaccrual finance receivables, fair values of collateral are determined based on the use of industry pricing guides. Our Timeshare impaired nonaccrual finance receivables largely consist of notes receivable loans to developers of resort properties which are collateralized by pools of consumer notes receivable. Fair values of collateral are estimated using cash flow models incorporating estimates of credit losses in the consumer notes pools and the developer's ability to mitigate losses through the repurchase or replacement of defaulted notes. Fair value measurements recorded on impaired finance receivables resulted in charges to provision for loan losses and primarily related to initial fair value adjustments.

Table of Contents

*Repossessed assets and properties* Repossessed assets and properties in the table above primarily include both golf and hotel properties and aviation assets at June 30, 2012. The fair value of our golf and hotel properties is determined based on the use of discounted cash flow models, bids from prospective buyers or inputs from market participants. The fair value of our aviation assets is largely determined based on the use of industry pricing guides. If the carrying amount of these assets is higher than their estimated fair value, we record a corresponding charge to income for the difference.

**Assets and Liabilities Not Recorded at Fair Value**

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

<i>(In millions)</i>	June 30, 2012		December 31, 2011	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
<b>Manufacturing group</b>				
Long-term debt, excluding leases	\$ (2,189)	\$ (2,536)	\$ (2,328)	\$ (2,561)
<b>Finance group</b>				
Finance receivables held for investment, excluding leases	1,750	1,676	1,997	1,848
Debt	(1,810)	(1,749)	(1,974)	(1,854)

Fair value for the Manufacturing group debt is determined using market observable data for similar transactions or Level 2 inputs. At June 30, 2012 and December 31, 2011, approximately 43% and 53%, respectively, of the fair value of term debt for the Finance group was determined based on observable market transactions (Level 1). The remaining Finance group debt was determined based on discounted cash flow analyses using observable market inputs from debt with similar duration, subordination and credit default expectations (Level 2). Fair value estimates for finance receivables held for investment were determined based on internally developed discounted cash flow models primarily utilizing significant unobservable inputs (Level 3), which include estimates of the rate of return, financing cost, capital structure and/or discount rate expectations of current market participants combined with estimated loan cash flows based on credit losses, payment rates and expectations of borrowers' ability to make payments on a timely basis.

**Note 10: Segment Information**

We operate in, and report financial information for, the following five business segments: Cessna, Bell, Textron Systems, Industrial and Finance. Segment profit is an important measure used for evaluating performance and for decision-making purposes. Segment profit for the manufacturing segments excludes interest expense and certain corporate expenses. The measurement for the Finance segment includes interest income and expense along with intercompany interest expense. Provisions for losses on finance receivables involving the sale or lease of our products are recorded by the selling manufacturing division when our Finance group has recourse to the Manufacturing group.

Table of Contents

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

<i>(In millions)</i>	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
<b>REVENUES</b>				
<i>Manufacturing Group</i>				
Cessna	\$ 763	\$ 652	\$ 1,432	\$ 1,208
Bell	1,056	872	2,050	1,621
Textron Systems	389	452	766	897
Industrial	756	719	1,511	1,422
	2,964	2,695	5,759	5,148
<i>Finance Group</i>	55	33	116	59
Total revenues	\$ 3,019	\$ 2,728	\$ 5,875	\$ 5,207
<b>SEGMENT OPERATING PROFIT</b>				
<i>Manufacturing Group</i>				
Cessna	\$ 35	\$ 5	\$ 29	\$ (33)
Bell	152	120	297	211
Textron Systems	40	49	75	102
Industrial	61	55	134	116
	288	229	535	396
<i>Finance Group</i>	22	(33)	34	(77)
Segment profit	310	196	569	319
Corporate expenses and other, net	(20)	(23)	(67)	(62)
Interest expense, net for Manufacturing group	(35)	(38)	(70)	(76)
Income from continuing operations before income taxes	\$ 255	\$ 135	\$ 432	\$ 181



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

<i>(Dollars in millions)</i>	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
Revenues	\$ 3,019	\$ 2,728	\$ 5,875	\$ 5,207
% change compared with prior period	11%		13%	

Revenues increased \$291 million, 11%, in the second quarter of 2012, compared with the corresponding period of 2011. This increase was due to revenue increases in the Bell, Cessna, Industrial and Finance segments that were partially offset by lower revenues in the Textron Systems segment. The net revenue increase included the following factors:

- Higher Bell revenues of \$184 million, largely due to higher commercial aircraft volume.
- Higher Cessna revenues of \$111 million, primarily due to higher Citation jet volume.
- Increased Industrial segment revenues of \$37 million, primarily due to higher volume, mostly reflecting higher market demand in the Fuel Systems and Functional Components and Golf and Turf Care product lines, partially offset by unfavorable foreign exchange primarily related to the weakening of the euro.
- Higher Finance revenues of \$22 million due to lower portfolio losses and favorable net valuation adjustments related to the non-captive business, partially offset by a decline in revenues attributable to lower average finance receivables of \$1.2 billion.
- Lower Textron Systems revenues of \$63 million, primarily due to lower volume in the Weapons and Sensors and Land & Marine product lines.

Revenues increased \$668 million, 13%, in the first half of 2012, compared with the corresponding period of 2011, as revenue increases in the Bell, Cessna, Industrial and Finance segments were partially offset by lower revenues in the Textron Systems segments. The net revenue increase included the following factors:

- Higher Bell revenues of \$429 million, largely due to higher commercial aircraft volume and higher volume in our military programs.
- Higher Cessna revenues of \$224 million, primarily due to higher Citation jet volume.

## Edgar Filing: TEXTRON INC - Form 10-Q

- Increased Industrial segment revenues of \$89 million, primarily due to higher volume, mostly reflecting higher market demand in the Fuel Systems and Functional Components and Golf and Turf Care product lines, partially offset by unfavorable foreign exchange primarily related to the weakening of the euro.
- Higher Finance revenues of \$57 million as favorable net valuation adjustments related to the non-captive business and lower portfolio losses offset a decline in revenues attributable to lower average finance receivables of \$1.3 billion.
- Lower Textron Systems revenues of \$131 million, primarily due to lower volume across all product lines.

### Cost of Sales and Selling and Administrative Expense

<i>(Dollars in millions)</i>	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
Operating expenses	\$ 2,718	\$ 2,520	\$ 5,338	\$ 4,879
% change compared with prior period	8%		9%	
Cost of sales	\$ 2,435	\$ 2,225	\$ 4,747	\$ 4,280
% change compared with prior period	9%		11%	
Gross margin percentage of Manufacturing revenues	17.8%	17.4%	17.6%	16.9%
Selling and administrative expense	\$ 283	\$ 295	\$ 591	\$ 599
% change compared with prior period	(4)%		(1)%	

Table of Contents

Manufacturing cost of sales and selling and administrative expenses together comprise our operating expenses. Changes in operating expenses are more fully discussed in our Segment Analysis below.

Consolidated manufacturing cost of sales as a percentage of Manufacturing revenues was 82.2% and 82.6% in the second quarter of 2012 and 2011, respectively. On a dollar basis, consolidated manufacturing cost of sales increased \$210 million, 9%, in the second quarter of 2012, compared with the corresponding period of 2011, principally due to higher net sales volume in the Bell, Cessna and Industrial segments, partially offset by lower net sales volume at Textron Systems. Cost of sales was favorably impacted at the Industrial segment due to the impact of foreign exchange on direct materials and labor of \$27 million, largely due to fluctuations with the euro. In the second quarter of 2012, gross margin increased as a percentage of Manufacturing revenues primarily due to favorable product mix at Bell and improved leverage on higher volume at the Bell, Cessna and Industrial segments.

Consolidated manufacturing cost of sales as a percentage of Manufacturing revenues was 82.4% and 83.1% in the first half of 2012 and 2011, respectively. On a dollar basis, consolidated cost of sales increased \$467 million, 11%, in the first half of 2012, principally due to higher net sales volume in the Bell, Cessna and Industrial segments, partially offset by lower net sales volume at Textron Systems. Cost of sales was favorably impacted at the Industrial segment due to the impact of foreign exchange on direct materials and labor of \$33 million, largely due to fluctuations with the euro. In the first half of 2012, gross margin increased as a percentage of Manufacturing revenues primarily due to favorable product mix at Bell and improved leverage on higher volume at the Bell, Cessna and Industrial segments.

On a consolidated basis, selling and administrative expense decreased \$12 million, 4%, to \$283 million in the second quarter of 2012, compared with the corresponding period of 2011. For the first half of 2012, selling and administrative expense decreased \$8 million, 1%, to \$591 million, compared with the corresponding period of 2011. These changes were largely driven by a \$10 million and \$20 million reduction in operating expense at the Finance segment in the second quarter and first half of 2012 compared with the corresponding periods of 2011, respectively, primarily associated with the exit of the non-captive business.

**Backlog**

<i>(In millions)</i>	<b>June 30, 2012</b>	<b>December 31, 2011</b>
Bell	\$ 6,739	\$ 7,346
Cessna	1,526	1,889
Textron Systems	2,653	1,337

Backlog increased \$1.3 billion at Textron Systems in the first half of 2012 largely due to additional orders in the Unmanned Aircraft Systems (UAS) and Land & Marine product lines. Backlog at Bell and Cessna decreased \$0.6 billion and \$0.4 billion, respectively, in the first half of 2012, primarily reflecting deliveries in excess of orders.

Segment Analysis

## Edgar Filing: TEXTRON INC - Form 10-Q

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

In our discussion of comparative results for the Manufacturing group, changes in revenue and segment profit typically are expressed for our commercial business in terms of volume, pricing, foreign exchange and acquisitions. Additionally, changes in segment profit may be expressed in terms of mix, inflation and cost performance. Volume changes in revenue represent increases/decreases in the number of units delivered or services provided. Pricing represents changes in unit pricing. Foreign exchange is the change resulting from translating foreign-denominated amounts into U.S. dollars at exchange rates that are different from the prior period. Acquisitions refer to the results generated from businesses that were acquired within the previous 12 months. For segment profit, mix represents a change due to the composition of products and/or services sold at different profit margins. Inflation represents higher material, wages, benefits, pension or other costs. Cost performance reflects an increase or decrease in research and development, depreciation, selling and administrative costs, warranty, product liability, quality/scrap, labor efficiency, overhead, product line profitability, start-up, ramp up and cost-reduction initiatives or other manufacturing inputs.

Table of Contents

Approximately 31% of our 2011 revenues were derived from contracts with the U.S. Government. For our segments that have significant contracts with the U.S. Government, we typically express changes in segment profit related to the government business in terms of volume, changes in program performance or changes in contract mix. Changes in volume that are discussed in net sales typically drive corresponding changes in our segment profit based on the profit rate for a particular contract. Changes in program performance typically relate to profit recognition associated with revisions to total estimated costs at completion that reflect improved or deteriorated operating performance or award fee rates. Changes in contract mix refer to changes in operating margin due to a change in the relative volume of contracts with higher or lower fee rates such that the overall average margin rate for the segment changes.

**Cessna**

<i>(Dollars in millions)</i>	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
Revenues	\$ 763	\$ 652	\$ 1,432	\$ 1,208
Operating expenses	728	647	1,403	1,241
Segment profit (loss)	35	5	29	(33)
Profit margin	4.6%	0.8%	2.0%	(2.7)%

**Cessna Revenues and Operating Expenses**

The following factors contributed to the change in Cessna's revenues for the periods:

<i>(In millions)</i>	Q2 2012 versus Q2 2011	YTD 2012 versus YTD 2011
Volume	\$ 116	\$ 227
Other	(5)	(3)
Total change	\$ 111	\$ 224

In the second quarter of 2012, Cessna's revenues increased \$111 million, 17%, compared with the corresponding period of 2011, primarily due to higher Citation business jet volume reflecting a modest recovery in the jet market, which had a \$101 million impact. We delivered 49 Citation jets in the second quarter of 2012, compared with 38 jets in the corresponding period of 2011. During the second quarter of 2012, the portion of Cessna's revenues derived from aftermarket sales and services represented 26% of Cessna's revenues, compared with 29% in the second quarter of 2011.

In the first half of 2012, Cessna's revenues increased \$224 million, 19%, compared with the corresponding period of 2011, primarily due to a \$176 million impact from higher Citation business jet volume reflecting a modest recovery in the jet market and an increase of \$24 million resulting from higher aftermarket volume, primarily due to part sales. We delivered 87 and 69 Citation business jets in the first half of 2012 and 2011, respectively. During the first half of 2012, the portion of Cessna's revenues derived from aftermarket sales and services represented 28% of Cessna's revenues, compared with 31% in the first half of 2011.

## Edgar Filing: TEXTRON INC - Form 10-Q

Cessna's operating expenses increased by \$81 million, 13%, in the second quarter of 2012, compared with the corresponding period of 2011, primarily due to higher direct material cost and manufacturing overhead of \$61 million and \$24 million, respectively, resulting from higher sales volume.

Cessna's operating expenses increased by \$162 million, 13%, in the first half of 2012, compared with the corresponding period of 2011, primarily due to higher direct material cost and manufacturing overhead of \$122 million and \$46 million, respectively, resulting from higher sales volume.

### Cessna Segment Profit

The following factors contributed to the change in Cessna's segment profit for the periods:

<i>(In millions)</i>		<b>Q2 2012 versus Q2 2011</b>	<b>YTD 2012 versus YTD 2011</b>
Volume	\$	33	\$ 59
Other		(3)	3
Total change	\$	30	\$ 62

Table of Contents

Cessna's segment profit increased \$30 million in the second quarter of 2012, compared with the corresponding period of 2011, primarily due to higher volume of \$33 million as described above.

Cessna's segment profit was \$62 million higher in the first half of 2012, compared with the corresponding period of 2011, primarily due to higher volume of \$59 million as described above. Profit margins improved primarily due to the leveraging of higher sales volume over fixed operating costs.

**Bell**

<i>(Dollars in millions)</i>	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
Revenues				
V-22 program	\$ 391	\$ 360	\$ 787	\$ 718
Other military	229	259	478	429
Commercial	436	253	785	474
Total revenues	1,056	872	2,050	1,621
Operating expenses	904	752	1,753	1,410
Segment profit	152	120	297	211
Profit margin	14.4%	13.8%	14.5%	13.0%

Bell manufactures helicopters, tiltrotor aircraft, and related spare parts and provides services for military and commercial markets. Bell's major U.S. Government programs at this time are the V-22 tiltrotor aircraft and the H-1 helicopter platforms, which are both in the production stage and represent a significant portion of Bell's revenues from the U.S. Government.

**Bell Revenues and Operating Expenses**

The following factors contributed to the change in Bell's revenues for the periods:

<i>(In millions)</i>	Q2 2012 versus Q2 2011	YTD 2012 versus YTD 2011
Volume	\$ 180	\$ 421
Other	4	8
Total change	\$ 184	\$ 429

Bell's revenues increased \$184 million, 21%, in the second quarter of 2012, compared with the corresponding period of 2011, primarily due to higher volume which included the following factors:

## Edgar Filing: TEXTRON INC - Form 10-Q

- \$179 million increase in commercial volume, largely related to higher deliveries reflecting improved global demand. Bell delivered 47 commercial aircraft in the second quarter of 2012, compared with 22 aircraft in the second quarter of 2011.
- \$31 million increase in volume related to the V-22 program, primarily reflecting higher revenues related to the support of fielded V-22 aircraft. Bell delivered 9 V-22 aircraft in both the second quarters of 2012 and 2011, respectively.
- \$30 million decrease in other military volume, primarily due to the timing of deliveries under our contracts. We delivered 6 H-1 aircraft in the second quarter of 2012, compared with 8 aircraft in the second quarter of 2011.

Bell's revenues increased \$429 million, 26%, in the first half of 2012, compared with the corresponding period of 2011, primarily due to higher volume which included the following factors:

- \$303 million increase in commercial volume, largely related to higher deliveries reflecting improved global demand. Bell delivered 77 commercial aircraft in the first half of 2012, compared with 37 aircraft in the first half of 2011.
- \$69 million increase in volume related to the V-22 program, primarily reflecting higher revenues related to the support of fielded V-22 aircraft and higher aircraft deliveries. Bell delivered 19 V-22 aircraft in the first half of 2012, compared with 18 deliveries in the first half of 2011.



Table of Contents

- \$49 million increase in other military volume, primarily due to the timing of deliveries under our contracts. We delivered 13 H-1 aircraft in the first half of 2012, compared with 12 aircraft in the first half of 2011.

Bell's operating expenses increased \$152 million, 20%, in the second quarter of 2012, compared with the corresponding period of 2011, primarily due to higher sales volume as discussed above.

Bell's operating expenses increased \$343 million, 24%, in the first half of 2012, compared with the corresponding period of 2011, primarily due to higher sales volume discussed above.

**Bell Segment Profit**

The following factors contributed to the change in Bell's segment profit for the periods:

<i>(In millions)</i>	Q2 2012 versus Q2 2011	YTD 2012 versus YTD 2011
Volume and mix	\$ 44	\$ 101
Other	(12)	(15)
Total change	\$ 32	\$ 86

Bell's segment profit increased \$32 million, 27%, in the second quarter of 2012, compared with the second quarter of 2011, primarily due to higher volume and mix in our commercial aircraft business as described above. Segment profit was also impacted by higher research and development expense of \$12 million due to the ramp-up of new product development.

Bell's segment profit increased \$86 million, 41%, in the first half of 2012, compared with the first half of 2011, primarily due to higher volume and mix in our commercial aircraft business as described above. Segment profit was also impacted by higher selling and administrative expenses of \$15 million and higher research and development costs of \$10 million due to the ramp-up of new product development.

**Textron Systems**

<i>(Dollars in millions)</i>	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
Revenues	\$ 389	\$ 452	\$ 766	\$ 897
Operating expenses	349	403	691	795
Segment profit	40	49	75	102

Profit margin	10.3%	10.8%	9.8%	11.4%
---------------	-------	-------	------	-------

**Textron Systems Revenues and Operating Expenses**

The following factors contributed to the change in Textron Systems revenues for the periods:

<i>(In millions)</i>		<b>Q2 2012 versus Q2 2011</b>		<b>YTD 2012 versus YTD 2011</b>
Volume	\$	(65)	\$	(134)
Other		2		3
Total change	\$	(63)	\$	(131)

Revenues at Textron Systems decreased \$63 million, 14%, in the second quarter of 2012, compared with the second quarter of 2011, primarily due to lower volume reflecting the following changes:

- Lower Weapons and Sensors revenues of \$51 million, largely due to the timing of deliveries on our contracts.
- Lower Land & Marine volume of \$12 million, primarily related to lower deliveries based on current contract requirements.

Table of Contents

Revenues at Textron Systems decreased \$131 million, 15%, in the first half of 2012, compared with the first half of 2011, primarily due to lower volume reflecting the following changes:

- Lower UAS volume of \$47 million, largely due to the timing of deliveries.
- Lower Weapons and Sensors revenues of \$32 million, primarily due to the completion of several contracts in the first quarter of 2011.
- Lower Land & Marine volume of \$29 million, primarily related to lower deliveries based on current contract requirements.
- Lower Mission Support and Other product line volume of \$23 million, primarily due to the completion of certain contracts in the first half of 2011.

Textron Systems operating expenses decreased \$54 million, 13%, in the second quarter of 2012, compared with the second quarter of 2011, primarily due to the lower volume.

Textron Systems operating expenses decreased \$104 million, 13%, in the first half of 2012, compared with the first half of 2011, primarily due to the lower volume and the impact of headcount reductions and other cost reduction initiatives.

**Textron Systems Segment Profit**

The following factors contributed to the change in Textron Systems segment profit for the periods:

<i>(In millions)</i>	<b>Q2 2012 versus Q2 2011</b>	<b>YTD 2012 versus YTD 2011</b>
Volume and mix	\$ (24)	\$ (48)
Performance	14	19
Other	1	2
Total change	\$ (9)	\$ (27)

Segment profit at Textron Systems decreased \$9 million, 18%, in the second quarter of 2012, compared with the corresponding period of 2011, primarily due to the impact of lower volume described above and deliveries on lower margin contracts during the current period. The favorable performance of \$14 million primarily reflects the impact of headcount reductions and other cost reduction initiatives.

Segment profit at Textron Systems decreased \$27 million, 26%, in the first half of 2012, compared with the corresponding period of 2011, primarily due to the impact of lower volume described above and deliveries on lower margin contracts during the current period. The favorable

## Edgar Filing: TEXTRON INC - Form 10-Q

performance of \$19 million primarily reflects the impact of headcount reductions and other cost reduction initiatives.

### Industrial

<i>(Dollars in millions)</i>	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
<b>Revenues:</b>				
Fuel Systems and Functional Components	\$ 468	\$ 450	\$ 960	\$ 921
Other Industrial	288	269	551	501
Total revenues	756	719	1,511	1,422
Operating expenses	695	664	1,377	1,306
Segment profit	61	55	134	116
Profit margin	8.1%	7.6%	8.9%	8.2%

Table of Contents**Industrial Revenues and Operating Expenses**

The following factors contributed to the change in Industrial s revenues for the periods:

<i>(In millions)</i>	<b>Q2 2012 versus Q2 2011</b>	<b>YTD 2012 versus YTD 2011</b>
Volume	\$ 70	\$ 128
Foreign exchange	(39)	(51)
Other	6	12
Total change	\$ 37	\$ 89

Industrial segment revenues increased \$37 million, 5%, in the second quarter of 2012, compared with the corresponding period of 2011. Volume increased largely due to a \$51 million increase in the Fuel Systems and Functional Components product line, reflecting higher automotive industry demand in North America and Asia, and \$19 million in the Other Industrial product lines, largely related to higher market demand in the Golf and Turf Care product line. The unfavorable foreign exchange impact was mostly related to the weakening of the euro, which primarily impacted the Fuel Systems and Functional Components product line.

Industrial segment revenues increased \$89 million, 6%, in the first half of 2012, compared with the corresponding period of 2011. Volume increased largely due to an \$87 million increase in the Fuel Systems and Functional Components product line, reflecting higher automotive industry demand in North America and Asia, and \$41 million in the Other Industrial product lines, largely related to higher market demand in the Golf and Turf Care product line. The unfavorable foreign exchange impact was mostly related to the weakening of the euro, which primarily impacted the Fuel Systems and Functional Components product line.

Operating expenses for the Industrial segment increased \$31 million, 5%, in the second quarter of 2012, compared with the corresponding period of 2011, largely due to \$55 million in higher direct material costs in support of higher sales volume. Operating expenses were also impacted by cost inflation of \$12 million primarily due to higher commodity and material component costs. These increases in operating expenses were partially offset by a favorable foreign exchange impact of \$36 million, largely due to the weakening of the euro.

Operating expenses for the Industrial segment increased \$71 million, 5%, in the first half of 2012, compared with the corresponding period of 2011, largely due to \$103 million in higher direct material costs in support of higher sales volume. Operating expenses were also impacted by cost inflation of \$24 million primarily due to higher commodity and material component costs. These increases in operating expenses were partially offset by a favorable foreign exchange impact of \$46 million, largely due to the weakening of the euro.

**Industrial Segment Profit**

The following factors contributed to the change in Industrial s segment profit for the periods:

Edgar Filing: TEXTRON INC - Form 10-Q

<i>(In millions)</i>		<b>Q2 2012 versus Q2 2011</b>		<b>YTD 2012 versus YTD 2011</b>	
Volume	\$	15	\$	26	
Other		(9)		(8)	
Total change	\$	6	\$	18	

Segment profit for the Industrial segment increased \$6 million, 11%, in the second quarter of 2012, compared with the corresponding period of 2011, primarily due to a \$15 million impact from higher volume as described above.

Segment profit for the Industrial segment increased \$18 million, 16%, in the first half of 2012, compared with the corresponding period of 2011, primarily due to a \$26 million impact from higher volume as described above.

Table of Contents**Finance**

<i>(In millions)</i>	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
Revenues	\$ 55	\$ 33	\$ 116	\$ 59
Segment profit (loss)	22	(33)	34	(77)

Our plan to exit the non-captive commercial finance business of our Finance segment is being effected through a combination of orderly liquidation and selected sales. Depending on market conditions, we expect continued progress in liquidating the remaining \$619 million of finance receivables in the non-captive portfolio over the next several years.

Finance segment revenues increased \$22 million in the second quarter of 2012, compared with the second quarter of 2011, primarily attributable to the following factors:

- \$16 million of lower portfolio losses, net of gains, primarily associated with the Structured Capital portfolio.
- \$15 million due to \$8 million in net favorable valuation adjustments in the second quarter of 2012 related to the Golf Mortgage finance receivables held for sale and owned assets, compared with \$7 million in unfavorable valuation adjustments in the second quarter of 2011.
- These increases were partially offset by a \$15 million decrease attributable to lower average finance receivables of \$1.2 billion.

Finance segment revenues increased \$57 million in the first half of 2012, compared with the first half of 2011, primarily attributable to the following factors:

- \$41 million due to \$19 million in net favorable valuation adjustments in the first half of 2012 related to the Golf Mortgage finance receivables held for sale and owned assets, compared with \$22 million in unfavorable valuation adjustments in the first half of 2011.
- \$30 million of lower portfolio losses, net of gains, primarily associated with the Structured Capital and Timeshare portfolios.
- \$9 million increase due to the resolution of one significant Timeshare account that returned to accrual status during 2012.
- These increases were partially offset by a \$30 million decrease attributable to lower average finance receivables of \$1.3 billion.

Finance segment profit increased \$55 million in the second quarter of 2012, compared with the corresponding period of 2011, primarily due to \$19 million in lower provision for loan losses mostly related to specific reserving actions taken in the non-captive portfolio during the second quarter of 2011. In addition, portfolio losses, net of gains, decreased by \$16 million and net valuation adjustments changed by \$15 million as

## Edgar Filing: TEXTRON INC - Form 10-Q

discussed above. In addition, administrative expense declined by \$10 million primarily associated with the exit of the non-captive business.

Finance segment profit increased \$111 million in the first half of 2012, compared with the corresponding period of 2011, primarily due to changes in net valuation adjustments of \$41 million and \$30 million in lower portfolio losses, net of gains, as discussed above. Provision for loan losses also decreased by \$27 million mostly due to specific reserving actions taken on several captive and non-captive accounts during 2011. In addition, administrative expense declined by \$20 million primarily associated with the exit of the non-captive business.

### *Finance Portfolio Quality*

The following table reflects information about the Finance segment's credit performance related to finance receivables held for investment:



Table of Contents

<i>(Dollars in millions)</i>	June 30, 2012	December 31, 2011
Finance receivables	\$ 2,128	\$ 2,477
Nonaccrual finance receivables	252	321
Allowance for losses	122	156
Ratio of nonaccrual finance receivables to finance receivables	11.84%	12.96%
Ratio of allowance for losses on impaired nonaccrual finance receivables to impaired nonaccrual finance receivables	25.19%	28.52%
Ratio of allowance for losses on finance receivables to nonaccrual finance receivables	48.41%	48.60%
Ratio of allowance for losses on finance receivables to finance receivables	5.73%	6.30%
60+ days contractual delinquency as a percentage of finance receivables	7.94%	6.70%
60+ days contractual delinquency	169	166
Repossessed assets and properties	167	199

Finance receivables held for sale are reflected at the lower of cost or fair value on the Consolidated Balance Sheets and are not included in the credit performance statistics above. Finance receivables held for sale in the non-captive portfolio totaled \$244 million at June 30, 2012, compared with \$418 million at the end of 2011.

Nonaccrual finance receivables decreased \$69 million, 21%, from the year-end balance, primarily due to reductions of \$41 million in the Timeshare portfolio and \$24 million in the Captive portfolio. The decrease in these portfolios was mostly due to cash collections and repossession of collateral, partially offset by new accounts identified as nonaccrual in 2012. The 60+ days contractual delinquency percentage increased primarily due to higher delinquencies in the Captive portfolio related to several larger accounts, partially offset by lower delinquencies in the Timeshare portfolio.

**Liquidity and Capital Resources**

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

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

<i>(Dollars in millions)</i>	June 30, 2012	December 31, 2011
<b>Manufacturing group</b>		
Cash and equivalents	\$ 898	\$ 871
Debt	2,316	2,459
Shareholders' equity	3,102	2,745

Edgar Filing: TEXTRON INC - Form 10-Q

Capital (debt plus shareholders' equity)		5,418		5,204
Net debt (net of cash and equivalents) to capital		31.4%		36.6%
Debt to capital		42.7%		47.3%
<b>Finance group</b>				
Cash and equivalents	\$	13	\$	14
Debt		1,810		1,974

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

Table of Contents

Textron Inc. has a senior unsecured revolving credit facility that expires in March 2015 for an aggregate principal amount of \$1.0 billion, up to \$200 million of which is available for the issuance of letters of credit. At June 30, 2012, there were no amounts borrowed against the facility. We also maintain an effective shelf registration statement filed with the Securities and Exchange Commission that allows us to issue an unlimited amount of public debt and other securities.

**Manufacturing Group Cash Flows**

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

<i>(In millions)</i>	Six Months Ended	
	June 30, 2012	July 2, 2011
Operating activities	\$ 81	\$ 146
Investing activities	(156)	(211)
Financing activities	106	(231)

Cash flows from operating activities decreased during the first six months of 2012 as compared with the corresponding period of 2011, largely due to more cash used for our working capital requirements in support of sales growth, partially offset by higher earnings for the Manufacturing group.

Investing cash flows in the first half of 2012 and 2011 primarily included capital expenditures of \$158 million and \$169 million, respectively. We generated cash from financing activities in the first half of 2012, largely due to the receipt of \$245 million from the Finance group in payment of a portion of its intergroup borrowing, partially offset by the repayment of \$139 million of maturing debt. In the first half of 2011, financing activities primarily consisted of \$395 million in intergroup financing for our Finance group, which was partially offset by the issuance of \$189 million in commercial paper.

*Capital Contributions Paid To and Dividends Received From TFC*

Under a Support Agreement between Textron Inc. and TFC, Textron Inc. is required to maintain a controlling interest in TFC. The agreement also requires Textron Inc. to ensure that TFC maintains fixed charge coverage of no less than 125% and consolidated shareholder's equity of no less than \$200 million. Cash contributions paid to TFC to maintain compliance with the Support Agreement and dividends paid by TFC to Textron Inc. are detailed below:

<i>(In millions)</i>	Six Months Ended	
	June 30, 2012	July 2, 2011
Dividends paid by TFC to Textron Inc.	\$ 315	\$ 179

Capital contributions paid to TFC under Support Agreement

(240)

(112)

Due to the nature of these contributions, we classify these contributions within cash flows used by operating activities for the Manufacturing group in the Consolidated Statements of Cash Flows. Capital contributions to support Finance group growth in the ongoing captive finance business are classified as cash flows from financing activities. The Finance group's net income (loss) is excluded from the Manufacturing group's cash flows, while dividends from the Finance group are included within cash flows from operating activities for the Manufacturing group as they represent a return on investment.

**Finance Group Cash Flows**

In the first half of 2012, we liquidated \$523 million of the Finance group's finance receivables, net of originations. These finance receivable reductions occurred in both the non-captive and captive finance portfolios, but were primarily driven by the non-captive portfolio in connection with our exit plan, including \$137 million and \$115 million in the Golf Mortgage and Timeshare product lines, respectively. Depending on market conditions, we expect continued progress in liquidating the remaining \$619 million of finance receivables in the non-captive portfolio over the next several years.

Table of Contents

The cash flows from continuing operations for the Finance group are summarized below:

<i>(In millions)</i>	Six Months Ended	
	June 30, 2012	July 2, 2011
Operating activities	\$ (96)	\$ 28
Investing activities	580	784
Financing activities	(485)	(805)

The Finance group used more cash for operating activities largely due to \$112 million in taxes paid in the first half of 2012, compared with a \$40 million refund in the corresponding period of 2011. The 2012 tax payment was primarily attributable to a 2008 settlement with the Internal Revenue Service related to the challenge of tax deductions we took in prior years for certain leveraged lease transactions.

Cash receipts from the collection of finance receivables continued to exceed finance receivable originations, which resulted in net cash inflow from investing activities in both periods. Finance receivables repaid and proceeds from sales totaled \$617 million and \$919 million in the first half of 2012 and 2011, respectively, while cash outflows for originations declined to \$114 million in the first half of 2012 from \$244 million in the first half of 2011. These decreases were largely driven by the wind down of the non-captive finance receivable portfolio.

Cash used for financing activities in the first half of 2012 primarily related to \$254 million in long-term debt payments and a \$245 million payment to the Manufacturing group in payment of a portion of its intergroup borrowings. As of June 30, 2012 and December 31, 2011, the outstanding balance due to Textron Inc. for these borrowings was \$245 million and \$490 million, respectively. In the first half of 2011, the Finance group made a discretionary payment of \$940 million on its bank line of credit and repaid \$498 million of long-term debt. To pay its maturing debt, the Finance group borrowed \$395 million from Textron Inc. with interest and also received \$265 million in proceeds from the issuance of long-term debt in the first half of 2011.

**Consolidated Cash Flows**

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

<i>(In millions)</i>	Six Months Ended	
	June 30, 2012	July 2, 2011
Operating activities	\$ 28	\$ 219
Investing activities	306	501
Financing activities	(304)	(1,009)

Cash flows from operating activities decreased during the first six months of 2012 as compared with the corresponding period of 2011, largely due to more cash used for our working capital requirements in support of sales growth and an increase in net tax payments, partially offset by higher earnings.

Cash receipts from the collection of finance receivables continued to exceed finance receivable originations, which resulted in net cash inflow from investing activities in both years. Finance receivables repaid and proceeds from sales totaled \$405 million and \$679 million in the first half of 2012 and 2011, respectively, while cash outflows for originations decreased to \$19 million in the first half of 2012 from \$110 million in the first half of 2011. These decreases were largely driven by the wind down of the non-captive finance receivable portfolio.

Total cash used for financing activities was lower in 2012 primarily due to lower repayments of long-term debt of \$393 million in the first half of 2012, compared with \$511 million in the first half of 2011. In addition, TFC made a \$940 million discretionary payment against the outstanding balance on its bank line of credit during the first half of 2011. This decrease in cash used was partially offset by the issuance of \$189 million in commercial paper and \$265 million in long-term debt.

#### **Captive Financing and Other Intercompany Transactions**

The Finance group finances retail purchases and leases for new and used aircraft and equipment manufactured by our Manufacturing group, otherwise known as captive financing. In the Consolidated Statements of Cash Flows, cash received from customers or from the sale of receivables is reflected as operating activities when received from third parties. However, in the cash flow information provided for the separate borrowing groups, cash flows related to

Table of Contents

captive financing activities are reflected based on the operations of each group. For example, when product is sold by our Manufacturing group to a customer and is financed by the Finance group, the origination of the finance receivable is recorded within investing activities as a cash outflow in the Finance group's statement of cash flows. Meanwhile, in the Manufacturing group's statement of cash flows, the cash received from the Finance group on the customer's behalf is recorded within operating cash flows as a cash inflow. Although cash is transferred between the two borrowing groups, there is no cash transaction reported in the consolidated cash flows at the time of the original financing. These captive financing activities, along with all significant intercompany transactions, are reclassified or eliminated from the Consolidated Statements of Cash Flows.

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

<i>(In millions)</i>	Six Months Ended	
	June 30, 2012	July 2, 2011
Reclassifications from investing activities:		
Finance receivable originations for Manufacturing group inventory sales	\$ (95)	\$ (134)
Cash received from customers and sale of receivables	212	240
Other capital contributions made to Finance group		(40)
Other	1	6
Total reclassifications from investing activities	118	72
Reclassifications from financing activities:		
Capital contribution paid by Manufacturing group to Finance group under Support Agreement	240	112
Dividends received by Manufacturing group from Finance group	(315)	(179)
Other capital contributions made to Finance group		40
Total reclassifications from financing activities	(75)	(27)
Total reclassifications and adjustments to cash flow from operating activities	\$ 43	\$ 45

**Critical Accounting Estimates**

The accounting policies that we believe are most critical to the portrayal of our financial condition and results of operations are disclosed on pages 36 through 40 in our 2011 Annual Report on Form 10-K. The following section provides an update of the year-end disclosure for long-term contracts to include program profit adjustments made during the first half of 2012.

**Long-Term Contracts**

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

## Edgar Filing: TEXTRON INC - Form 10-Q

development costs, performance of subcontractors, availability and cost of materials, labor productivity and cost, overhead and capital costs, manufacturing efficiencies and the achievement of contract milestones, including product deliveries.

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



Table of Contents

current period. The following table sets forth the aggregate gross amount of all program profit adjustments that are included within segment profit for the first half of 2012 and 2011:

<i>(In millions)</i>	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
Gross favorable	\$ 23	\$ 21	\$ 40	\$ 42
Gross unfavorable	(11)	(11)	(24)	(18)
Net adjustments	\$ 12	\$ 10	\$ 16	\$ 24

**Forward-Looking Information**

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

- Changing priorities or reductions in the U.S. Government defense budget, including those related to military operations in foreign countries;
- Changes in worldwide economic or political conditions that impact demand for our products, interest rates or foreign exchange rates;
- Our ability to perform as anticipated and to control costs under contracts with the U.S. Government;
- The U.S. Government's ability to unilaterally modify or terminate its contracts with us for the U.S. Government's convenience or for our failure to perform, to change applicable procurement and accounting policies, or, under certain circumstances, to withhold payment or suspend or debar us as a contractor eligible to receive future contract awards;
- Changes in foreign military funding priorities or budget constraints and determinations, or changes in government regulations or policies on the export and import of military and commercial products;
- Our Finance segment's ability to maintain portfolio credit quality or to realize full value of receivables and of assets acquired upon foreclosure of receivables;
- Our ability to access the capital markets at reasonable rates;
- Performance issues with key suppliers, subcontractors or business partners;

## Edgar Filing: TEXTRON INC - Form 10-Q

- Legislative or regulatory actions impacting our operations or demand for our products;
- Our ability to control costs and successfully implement various cost-reduction activities;
- The efficacy of research and development investments to develop new products or unanticipated expenses in connection with the launching of significant new products or programs;
- The timing of our new product launches or certifications of our new aircraft products;
- Our ability to keep pace with our competitors in the introduction of new products and upgrades with features and technologies desired by our customers;
- The extent to which we are able to pass raw material price increases through to customers or offset such price increases by reducing other costs;
- Increases in pension expenses or employee and retiree medical benefits;
- Uncertainty in estimating reserves, including reserves established to address contingent liabilities, unrecognized tax benefits, or potential losses on our Finance segment's receivables;
- Difficult conditions in the financial markets which may adversely impact our customers' ability to fund or finance purchases of our products; and
- Volatility in the global economy resulting in demand softness or volatility in the markets in which we do business.

Table of Contents

**Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

There has been no significant change in our exposure to market risk during the fiscal quarter ended June 30, 2012. For discussion of our exposure to market risk, refer to Item 7A. Quantitative and Qualitative Disclosures about Market Risk contained in Textron's 2011 Annual Report on Form 10-K.

**Item 4. CONTROLS AND PROCEDURES**

We have carried out an evaluation, under the supervision and with the participation of our management, including our Chairman, President and Chief Executive Officer (CEO) and our Executive Vice President and Chief Financial Officer (CFO), of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Act)) as of the end of the fiscal quarter covered by this report. Based upon that evaluation, our CEO and CFO concluded that our disclosure controls and procedures are effective in providing reasonable assurance that (a) the information required to be disclosed by us in the reports that we file or submit under the Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and (b) such information is accumulated and communicated to our management, including our CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

There were no changes in our internal control over financial reporting during the fiscal quarter ended June 30, 2012 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**PART II. OTHER INFORMATION**

**Item 1. LEGAL PROCEEDINGS**

As previously reported and as updated in Textron's Annual Report on Form 10-K for the fiscal year ended December 31, 2011, on August 13, 2009, a purported shareholder class action lawsuit was filed in the United States District Court in Rhode Island against Textron, its then Chairman and former Chief Executive Officer and its former Chief Financial Officer. The suit, filed by the City of Roseville Employees Retirement System, alleged that the defendants violated the federal securities laws by making material misrepresentations or omissions related to Cessna and TFC. The complaint sought unspecified compensatory damages. In December 2009, the Automotive Industries Pension Trust Fund was appointed lead plaintiff in the case. On February 8, 2010, an amended class action complaint was filed with the Court. The amended complaint named as additional defendants TFC and three of its present and former officers. On April 6, 2010, the court entered a stipulation agreed to by the parties in which plaintiffs voluntarily dismissed, without prejudice, certain causes of action in the amended complaint. On April 9, 2010, all defendants moved to dismiss the remaining counts of the amended complaint, and on August 24, 2011, the court granted the motion to dismiss on behalf of all defendants without leave to amend and entered judgment in favor of all defendants. On September 23, 2011, plaintiffs filed a notice of appeal of the dismissal with the First Circuit Court of Appeals, and on June 7, 2012, the First Circuit affirmed the decision of the district court dismissing the suit.

## Edgar Filing: TEXTRON INC - Form 10-Q

As previously reported in Textron's Annual Report on Form 10-K for the fiscal year ended December 31, 2011, on February 7, 2012, a lawsuit was filed in the United States Bankruptcy Court, Northern District of Ohio, Eastern Division (Akron) by Brian A. Bash, Chapter 7 Trustee for Fair Finance Company against TFC, Fortress Credit Corp. and Fair Facility I, LLC. TFC provided a revolving line of credit of up to \$17.5 million to Fair Finance Company from 2002 through 2007. The complaint alleges numerous counts against TFC, as Fair Finance Company's working capital lender, including receipt of fraudulent transfers and assisting in fraud perpetrated on Fair Finance investors. The Trustee seeks avoidance and recovery of alleged fraudulent transfers in the amount of \$316 million as well as damages of \$223 million on the other claims. The Trustee also seeks trebled damages on all claims under Ohio law. We intend to vigorously defend this lawsuit, and on April 20, 2012, TFC moved to dismiss all claims in the complaint. That motion is still pending.

Table of Contents

**Item 6. EXHIBITS**

- 10.1 Letter agreement between Textron and John D. Butler, dated June 4, 2012
- 10.2 Letter agreement between Textron and Cheryl H. Johnson, dated June 12, 2012
- 12.1 Computation of ratio of income to fixed charges of Textron Inc. Manufacturing Group
- 12.2 Computation of ratio of income to fixed charges of Textron Inc. including all majority-owned subsidiaries
- 31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 Certification of Chief Executive Officer Pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 Certification of Chief Financial Officer Pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
  
- 101 The following materials from Textron Inc.'s Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2012, formatted in XBRL (eXtensible Business Reporting Language): (i) the Consolidated Statements of Operations, (ii) the Consolidated Statements of Comprehensive Income, (iii) the Consolidated Balance Sheets, (iv) the Consolidated Statements of Cash Flows and (v) Notes to the Consolidated Financial Statements.

SIGNATURES

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

TEXTRON INC.

Date: July 26, 2012

/s/Richard L. Yates  
Richard L. Yates  
Senior Vice President and Corporate Controller  
(principal accounting officer)

Table of Contents

**LIST OF EXHIBITS**

- 10.1 Letter agreement between Textron and John D. Butler, dated June 4, 2012
- 10.2 Letter agreement between Textron and Cheryl H. Johnson, dated June 12, 2012
- 12.1 Computation of ratio of income to fixed charges of Textron Inc. Manufacturing Group
- 12.2 Computation of ratio of income to fixed charges of Textron Inc. including all majority-owned subsidiaries
- 31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 Certification of Chief Executive Officer Pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 Certification of Chief Financial Officer Pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 101 The following materials from Textron Inc.'s Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2012, formatted in XBRL (eXtensible Business Reporting Language): (i) the Consolidated Statements of Operations, (ii) the Consolidated Statements of Comprehensive Income, (iii) the Consolidated Balance Sheets, (iv) the Consolidated Statements of Cash Flows and (v) Notes to the Consolidated Financial Statements.