

The background of the slide is a close-up, slightly blurred photograph of several stacks of US dollar bills. The bills are arranged in a way that creates a sense of depth and abundance. The colors are muted, with a focus on the greys and blues of the paper.

Capital Markets & Government Contracts

NDIA Atlanta XXIX

April 29, 2003

LOCKHEED MARTIN



*Jerry Van Schaick
Vice President and Treasurer*

Who are the “Capital Markets”



- **Banks**
- **Public debt holders**
 - *Rating agencies*
- **Equity holders**
- **Insurance markets**



All are in a greater or lesser degree of turmoil!

Are capital markets even important?



Yes!

- *Provide capital*
- *Absorb risk*

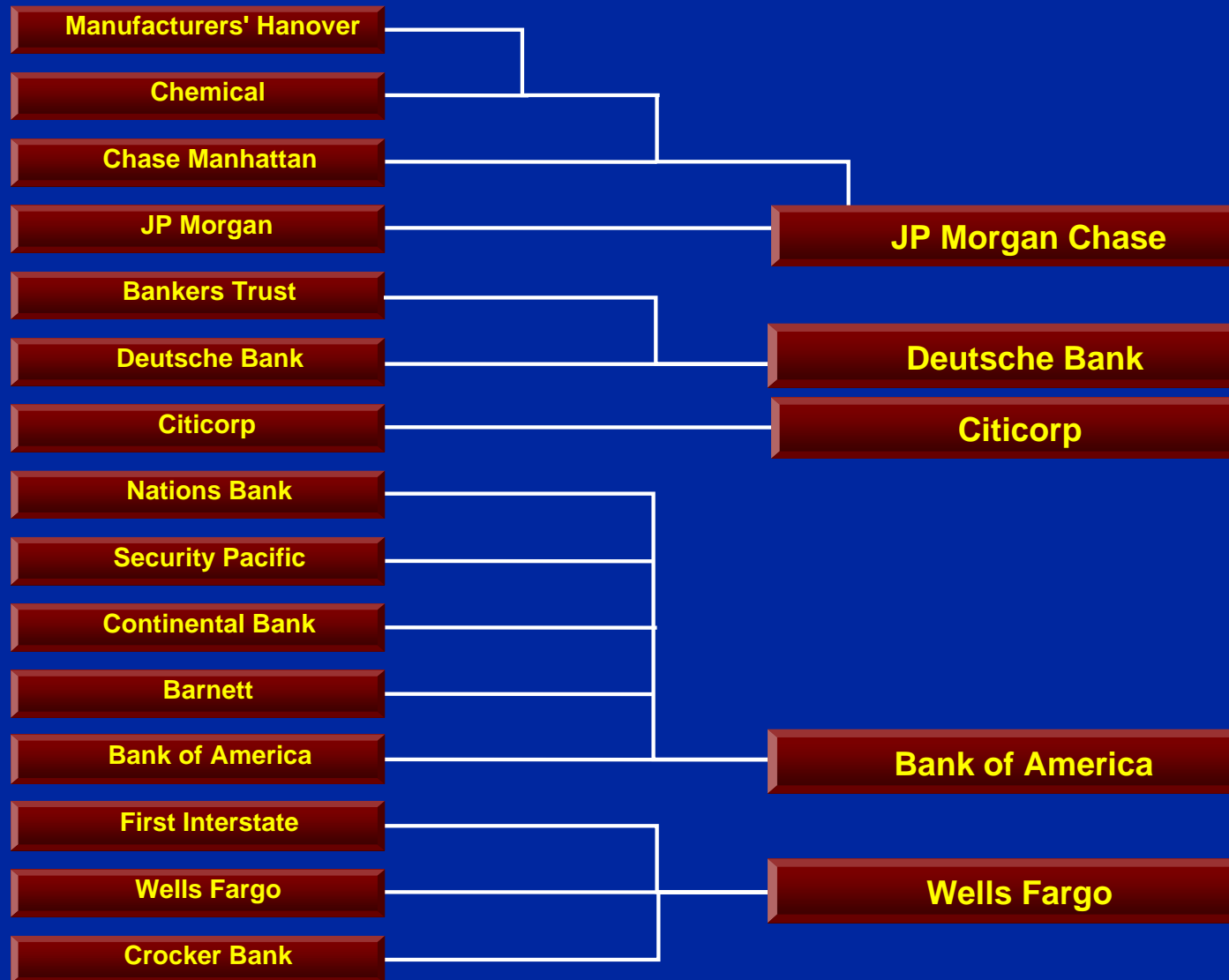
No capital markets support...No business!

Banks



- ***Consolidating***
- ***Contracting***
- ***CoNFUSING !!!***

Consolidating...



Contracting...



“CALL ME GOLDBLOCKS”

Banks want credits that are

- ***Not too strong***
 - *Narrow spreads, minimal fee business*
- ***Not too weak***
 - *Poor credit, non-accrual*
- ***Just right***
 - *Good spreads, good credit, lots of fee business*



Confusing...



- ***Inefficient mergers and bad loans are driving banks to re-evaluate their strategies***



- *Many want to be investment banks*
- *Some want to be “universal” banks*
- *A few want to use their balance sheets*

May be running out of credit providers

Public Debt Holders



- ***Principally***

- *Insurance companies*
- *Pension funds*
- *Mutual funds*



- ***Bond issues reviewed by***

- *Internal credit analysts, portfolio managers*
- *Rating agencies*

Key Ratios



Earnings Before Interest + Taxes (EBIT)

Interest

EBIT + Depreciation + Amortization (EBITDA)

Interest

Funds Flow from Operations

Debt

Debt

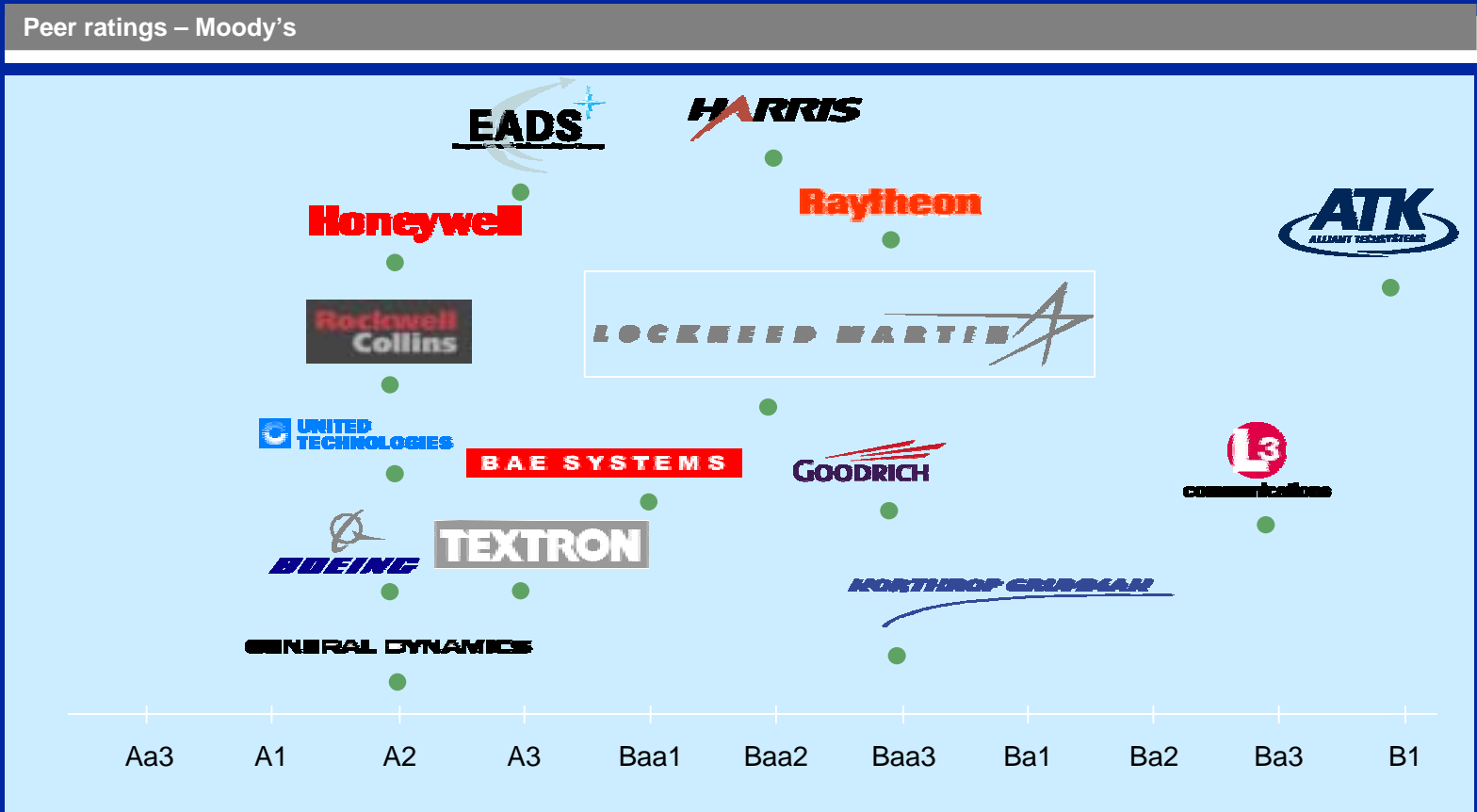
Total Capital

Ratings



<u>Moody's</u>	<u>S&P</u>	<u>Rating Universe</u>
Aaa	AAA	Nobody left up here
Aa1	AA+	
Aa2	AA	Top notch industrials, financials
Aa3	AA-	
A1	A+	
A2	A	Strong companies
A3	A-	
Baa1	BBB+	
Baa2	BBB	Could be better / Could be worse
Baa3	BBB-	
Ba1 ↓ C	BB+ ↓ C	Don't go here !

Peer Ratings



Public debt markets want:

- *Adequate coverage ratios*
- *Stable or improving trends*
- *No surprises*



Equity Markets



- **Hopefully ending a historic “bear” market...**



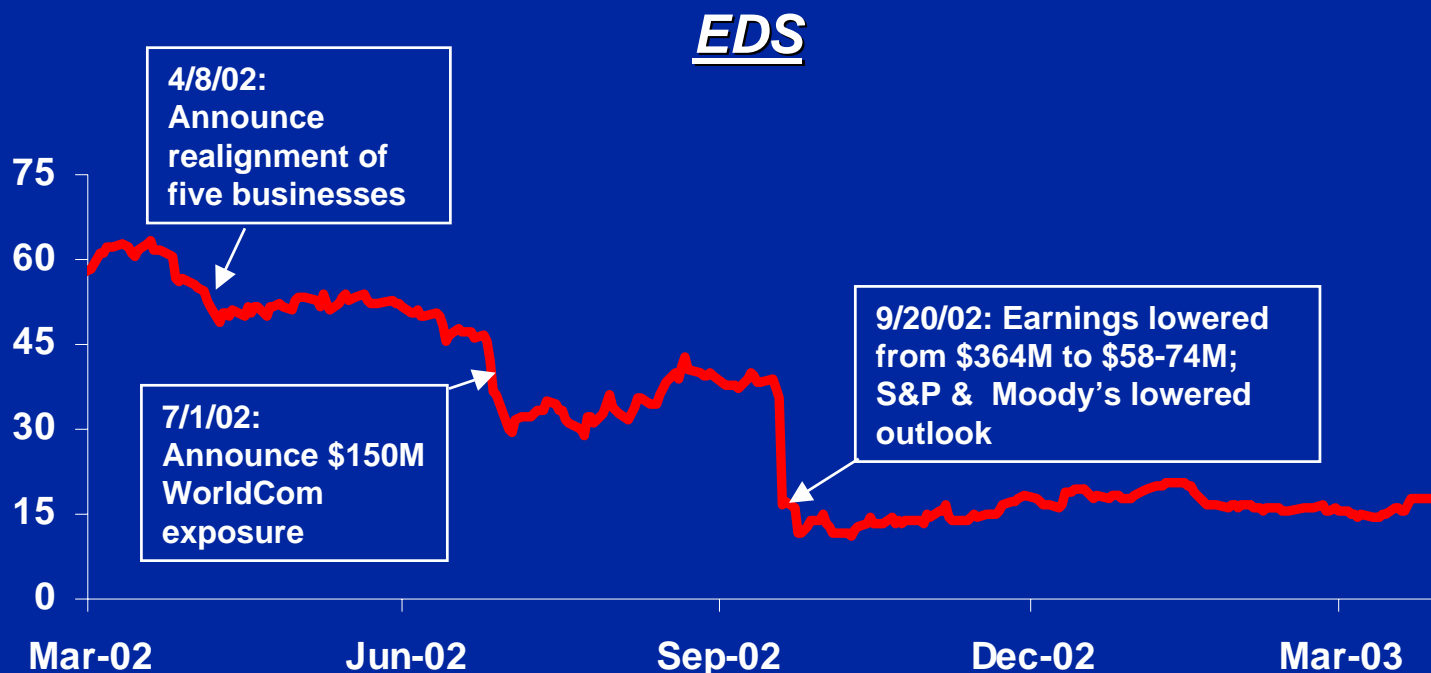
- **4 straight years of decline: 1929-1932**
- **3 straight years of decline: 1939-1941**
2000-2002
- **2 straight years of decline: 1973-1974**

Future returns possibly modest



Markets are risk averse and volatile

- **“Shock and Awe” for missed estimates, negative news**
- **Significant trading impacts**



Lockheed Martin Fluctuations



LMT vs. S&P 500





Reasons for LM stock decline

- *Quick war minimizes need for future military spending, OR*
- *Difficult war sucks all R&D / Procurement funding, OR*
- *Difficult war results in Democratic president, OR*
- *Quick war minimizes need for big ticket programs, OR*
- *Quick war allows growth in other sectors to accelerate, OR*
- *Make up your own!*

Why are stock prices important?



- *Capital flexibility*
- *Input to credit risk assessment models*

IBM	XAU	MSFT	C	GE	DELL	DELL	LU	MRK
172	60 1/16	149 3/4	58	98 7/16	78 1/16	78 1/16	99 3/8	78 3/16
5	-5/8	5000s	2100s	2900s	1000s	2000s	1500s	15000s

Equity markets want:



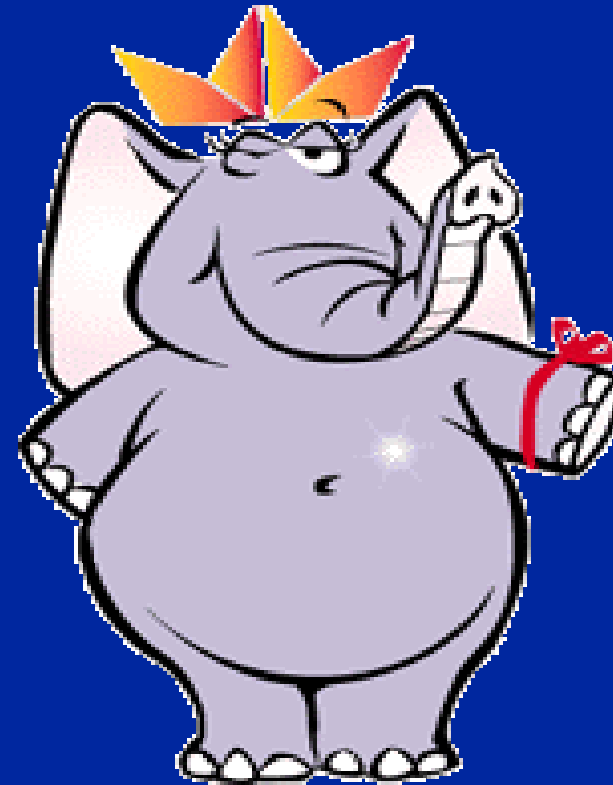
- ***Growth***
- ***Dependability***
- ***Surprise only on the upside***



Pensions



***Elephant in the
middle
of the party!!***



Pension Situation



- *3 yrs of decline, many plans under-funded*
- *Most have returned from their “contribution holiday”*
- *Modest returns going forward, costs will increase*
- *Future accounting uncertain*
- *Credit and equity analysts grappling with issue*

But

Gov’t contractors in better position; CAS cost recoverable

Big issue going forward!



Insurance

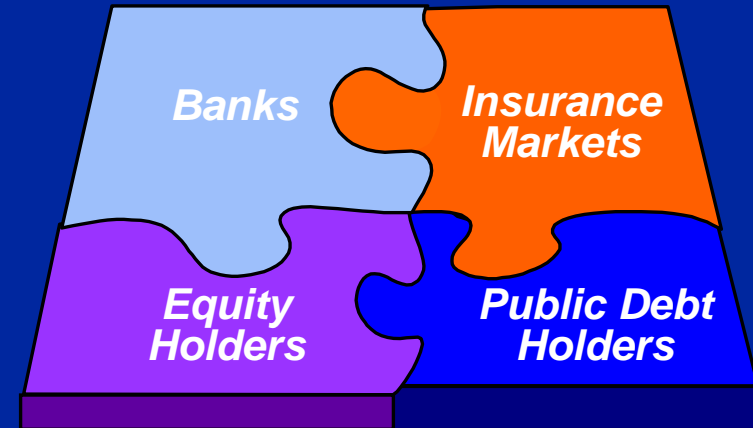
- *More potential sources of liability*
- *Terrorism related issues not solved*
- *Costs of coverage increasing dramatically*



What do the capital markets want?



- *Predictability and certainty*
- *Adequate returns*
- *Appropriate risk / return tradeoffs*
- *Defusing of pension time bomb*





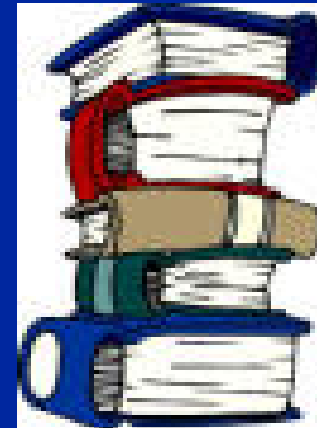
How does government contracting stack up?

- **Pluses**

- + *Short-term predictability*
- + *Maximum flexibility*
- + *Contractor ability to recover cost*

- **Minuses**

- *Limited profitability*
- *Limited growth potential*
- *Risk of major program cancellation*
- *Uncertainty of budget process*



Challenge



***To recognize and respond to the needs
of the capital markets while still protecting
the interests of the U.S. Government***

