

TELEDYNE TECHNOLOGIES INC
Form 10-Q
October 31, 2014
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SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 28, 2014

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 1-15295

TELEDYNE TECHNOLOGIES INCORPORATED
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

25-1843385
(I.R.S. Employer
Identification Number)

1049 Camino Dos Rios
Thousand Oaks, California
(Address of principal executive offices)
(805) 373-4545

91360-2362
(Zip Code)

(Registrant’s telephone number, including area code)

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

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

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

Large accelerated filer Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

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

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

Class Outstanding at October 24, 2014
Common Stock, \$.01 par value per share 36,555,065 shares

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

TELEDYNE TECHNOLOGIES INCORPORATED AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

FOR THE THIRD QUARTER AND NINE MONTHS ENDED SEPTEMBER 28, 2014 AND SEPTEMBER 29, 2013

(Unaudited - Amounts in millions, except per-share amounts)

	Third Quarter		Nine Months		
	2014	2013	2014	2013	
Net sales	\$601.1	\$571.6	\$1,771.7	\$1,742.0	
Costs and expenses					
Cost of sales	375.4	369.0	1,095.5	1,118.0	
Selling, general and administrative expenses	151.4	149.6	461.6	447.2	
Total costs and expenses	526.8	518.6	1,557.1	1,565.2	
Operating income	74.3	53.0	214.6	176.8	
Other income/(expense), net	(1.8) (0.7) 7.0	(1.2)
Interest and debt expense, net	(4.6) (5.1) (13.9) (15.6)
Income before income taxes	67.9	47.2	207.7	160.0	
Provision for income taxes	13.0	0.3	51.0	30.0	
Net income	54.9	46.9	156.7	130.0	
Noncontrolling interest	0.7	(0.1	) 0.8	0.1
Net income attributable to Teledyne	\$55.6	\$46.8	\$157.5	\$130.1	
Basic earnings per common share	\$1.49	\$1.25	\$4.21	\$3.49	
Weighted average common shares outstanding	37.2	37.3	37.4	37.3	
Diluted earnings per common share	\$1.47	\$1.23	\$4.13	\$3.42	
Weighted average diluted common shares outstanding	37.8	38.1	38.1	38.0	

The accompanying notes are an integral part of these financial statements.

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TELEDYNE TECHNOLOGIES INCORPORATED AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
 FOR THE THIRD QUARTER AND NINE MONTHS ENDED SEPTEMBER 28, 2014 AND SEPTEMBER 29,
 2013

(Unaudited - Amounts in millions)

	Third Quarter		Nine Months	
	2014	2013	2014	2013
Net income	\$54.9	\$46.9	\$156.7	\$130.0
Other comprehensive income (loss):				
Foreign exchange translation adjustment	(35.8	) 21.7	(28.7	) (7.7
Hedge activity and interest rate swap, net of tax	(1.9	) 1.5	(0.4	) (0.3
Pension and postretirement benefit adjustments, net of tax	3.1	5.2	8.0	16.3
Other comprehensive income (loss)	(34.6	) 28.4	(21.1	) 8.3
Comprehensive income	20.3	75.3	135.6	138.3
Noncontrolling interest	0.7	(0.1	) 0.8	0.1
Comprehensive income attributable to Teledyne	\$21.0	\$75.2	\$136.4	\$138.4

The accompanying notes are an integral part of these financial statements.

Table of ContentsTELEDYNE TECHNOLOGIES INCORPORATED AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

(Current period unaudited - Amounts in millions, except share amounts)

	September 28, 2014	December 29, 2013
Assets		
Current Assets		
Cash and cash equivalents	\$ 125.8	\$ 66.0
Accounts receivable, net	374.4	378.0
Inventories, net	310.9	294.3
Prepaid expenses and other current assets	66.6	60.8
Total current assets	877.7	799.1
Property, plant and equipment, at cost, net of accumulated depreciation and amortization of \$407.2 at September 28, 2014 and \$367.0 at December 29, 2013	335.1	357.7
Goodwill, net	1,028.0	1,037.8
Acquired intangibles, net	244.5	270.9
Prepaid pension assets	238.6	222.0
Other assets, net	69.0	63.6
Total Assets	\$2,792.9	\$2,751.1
Liabilities and Stockholders' Equity		
Current Liabilities		
Accounts payable	\$ 147.9	\$ 147.5
Accrued liabilities	268.9	267.1
Current portion of long-term debt and capital leases	85.0	3.5
Total current liabilities	501.8	418.1
Long-term debt and capital leases	492.8	549.0
Other long-term liabilities	260.6	265.3
Total Liabilities	1,255.2	1,232.4
Stockholders' Equity		
Preferred stock, \$0.01 par value; outstanding shares - none	—	—
Common stock, \$0.01 par value; authorized 125 million shares; issued shares: 37,697,865 at September 28, 2014 and 37,571,182 at December 29, 2013 Outstanding shares: 36,551,765 at September 28, 2014 and 37,571,182 at December 29, 2013	0.4	0.4
Additional paid-in capital	326.1	328.8
Retained earnings	1,465.4	1,308.0
Treasury stock	(111.9) —
Accumulated other comprehensive loss	(186.6	) (165.5
Total Teledyne Stockholders' Equity	1,493.4	1,471.7
Noncontrolling interest	44.3	47.0
Total Stockholders' Equity	1,537.7	1,518.7
Total Liabilities and Stockholders' Equity	\$2,792.9	\$2,751.1

The accompanying notes are an integral part of these financial statements.

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TELEDYNE TECHNOLOGIES INCORPORATED AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 FOR THE NINE MONTHS ENDED SEPTEMBER 28, 2014 AND SEPTEMBER 29, 2013
 (Unaudited - Amounts in millions)

	Nine Months 2014	2013	
Operating Activities			
Net income	\$156.7	\$130.0	
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	70.1	67.1	
Deferred income taxes	(3.3)	) 33.2	
Stock option expense	10.1	7.6	
Excess income tax benefits from stock options exercised	(4.2)	) (3.8))
Changes in operating assets and liabilities, excluding the effect of businesses acquired:			
Accounts receivable	1.0	(0.1))
Inventories	(17.3)	) (10.2))
Prepaid expenses and other assets	(0.6)	) 0.9	
Accounts payable	(0.4)	) 2.2	
Accrued liabilities	(5.0)	) (16.0))
Income taxes payable, net	11.0	(22.2))
Long-term assets	(5.7)	) (8.2))
Other long-term liabilities	1.0	4.9	
Accrued pension obligation	(11.5)	) (80.7))
Accrued postretirement benefits	(0.2)	) (0.5))
Other operating, net	(2.1)	) 1.4	
Net cash provided by operating activities	199.6	105.6	
Investing Activities			
Purchases of property, plant and equipment	(29.7)	) (54.0))
Purchase of businesses and other investments	(8.1)	) (106.4))
Proceeds from the disposal of fixed assets	0.2	0.2	
Net cash used by investing activities	(37.6)	) (160.2))
Financing Activities			
Net proceeds from debt	26.3	84.0	
Proceeds from exercise of stock options	14.2	10.0	
Purchase of treasury stock	(146.6)) —	
Excess income tax benefits from stock options exercised	4.2	3.8	
Issuance of cash flow hedges	(0.3)	) (0.3))
Net cash provided (used) by financing activities	(102.2)	) 97.5	
Increase in cash and cash equivalents	59.8	42.9	
Cash and cash equivalents—beginning of period	66.0	45.8	
Cash and cash equivalents—end of period	\$125.8	\$88.7	

The accompanying notes are an integral part of these financial statements.

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TELEDYNE TECHNOLOGIES INCORPORATED AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
September 28, 2014

Note 1. General

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared by Teledyne Technologies Incorporated (“Teledyne” or the “Company”) pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and disclosures normally included in notes to consolidated financial statements have been condensed or omitted pursuant to such rules and regulations, but resultant disclosures are in accordance with accounting principles generally accepted in the United States as they apply to interim reporting. The condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto in Teledyne’s Annual Report on Form 10-K for the fiscal year ended December 29, 2013 (“2013 Form 10-K”).

In the opinion of Teledyne’s management, the accompanying unaudited condensed consolidated financial statements contain all adjustments (consisting of normal recurring adjustments) necessary to present fairly, in all material respects, Teledyne’s consolidated financial position as of September 28, 2014 and the consolidated results of operations and consolidated comprehensive income for the third quarter and nine months then ended and consolidated cash flows for the nine months then ended. The results of operations and cash flows for the periods ended September 28, 2014 are not necessarily indicative of the results of operations or cash flows to be expected for any subsequent quarter or the full fiscal year. Certain prior year amounts have been reclassified to conform to the current period presentation.

Recent Accounting Pronouncements

Effective December 30, 2013, the Company adopted accounting guidance related to the presentation of an unrecognized tax benefit when a net operating loss carryforward (“NOL”), a similar tax loss or a tax credit carryforward exists. Under the guidance, an entity will be required to present an unrecognized tax benefit as a reduction of a deferred tax asset for a NOL or tax credit carryforward whenever the NOL or tax credit carryforward would be available to reduce the additional taxable income or tax due if the tax position is disallowed. The Company's adoption of the guidance did not have a material impact on its consolidated financial statements.

In May 2014, the Financial Accounting Standards Board issued Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers, which provides a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and will supersede most current revenue recognition guidance. This new guidance is effective for fiscal years, and interim periods within those years, beginning after December 15, 2016, and can be adopted either retrospectively to each prior reporting period presented or as a cumulative-effect adjustment as of the date of adoption, with early application not permitted. The Company is currently in the process of determining its implementation approach and assessing the impact on the consolidated financial statements and footnote disclosures.

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Note 2. Accumulated Other Comprehensive Income

The changes in accumulated other comprehensive income (“AOCI”) by component, net of tax, for the third quarter and nine months ended September 28, 2014 and September 29, 2013 are as follows (in millions):

	Foreign Currency Translation	Cash Flow Hedges	Pension and Postretirement Benefits	Total
Balance as of June 29, 2014	\$(25.3)	\$(1.8)	\$(124.9)	\$(152.0)
Other comprehensive loss before reclassifications	(35.8)	(2.4)	—	(38.2)
Amounts reclassified from AOCI	—	0.5	3.1	3.6
Net other comprehensive income (loss)	(35.8)	(1.9)	3.1	(34.6)
Balance as of September 28, 2014	\$(61.1)	\$(3.7)	\$(121.8)	\$(186.6)

	Foreign Currency Translation	Cash Flow Hedges	Pension and Postretirement Benefits	Total
Balance as of June 30, 2013	\$(46.6)	\$(3.7)	\$(243.2)	\$(293.5)
Other comprehensive income (loss) before reclassifications	21.7	1.0	(0.2)	22.5
Amounts reclassified from AOCI	—	0.5	5.4	5.9
Net other comprehensive income	21.7	1.5	5.2	28.4
Balance as of September 29, 2013	\$(24.9)	\$(2.2)	\$(238.0)	\$(265.1)

	Foreign Currency Translation	Cash Flow Hedges	Pension and Postretirement Benefits	Total
Balance as of December 29, 2013	\$(32.4)	\$(3.3)	\$(129.8)	\$(165.5)
Other comprehensive loss before reclassifications	(28.7)	(2.2)	—	(30.9)
Amounts reclassified from AOCI	—	1.8	8.0	9.8
Net other comprehensive (loss) income	(28.7)	(0.4)	8.0	(21.1)
Balance as of September 28, 2014	\$(61.1)	\$(3.7)	\$(121.8)	\$(186.6)

	Foreign Currency Translation	Cash Flow Hedges	Pension and Postretirement Benefits	Total
Balance as of December 30, 2012	\$(17.2)	\$(1.9)	\$(254.3)	\$(273.4)
Other comprehensive loss before reclassifications	(7.7)	(1.1)	—	(8.8)
Amounts reclassified from AOCI	—	0.8	16.3	17.1
Net other comprehensive income (loss)	(7.7)	(0.3)	16.3	8.3
Balance as of September 29, 2013	\$(24.9)	\$(2.2)	\$(238.0)	\$(265.1)

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The reclassifications out of AOCI for the third quarter and nine months ended September 28, 2014 and September 29, 2013 are as follows (in millions):

	Amount Reclassified from AOCI Three Months Ended September 28, 2014	Amount Reclassified from AOCI Nine Months Ended September 28, 2014	Statement of Income Presentation
Loss on cash flow hedges:			
Loss recognized in income on derivatives	\$0.6	\$2.4	Other expense
Income tax benefit	(0.1	) (0.6	) Income tax benefit
Total	\$0.5	\$1.8	
Amortization of defined benefit pension and postretirement plan items:			
Amortization of prior service cost	\$(1.2	) \$(3.6	) Pension expense
Amortization of net actuarial loss	6.1	16.4	Pension expense
Total before tax	4.9	12.8	
Income tax benefit	(1.8	) (4.8	) Income tax benefit
Total	\$3.1	\$8.0	
	Amount Reclassified from AOCI Three Months Ended September 29, 2013	Amount Reclassified from AOCI Nine Months Ended September 29, 2013	Statement of Income Presentation
Loss on cash flow hedges:			
Loss recognized in income on derivatives	\$0.7	\$1.0	Other expense
Income tax benefit	(0.2	) (0.2	) Income tax benefit
Total	\$0.5	\$0.8	
Amortization of defined benefit pension and postretirement plan items:			
Amortization of prior service cost	(1.3	) (3.9	) Pension expense
Amortization of net actuarial loss	10.1	30.5	Pension expense
Total before tax	8.8	26.6	
Income tax benefit	(3.4	) (10.3	) Income tax benefit
Total	\$5.4	\$16.3	

Note 3. Business Combinations and Investments, Goodwill and Acquired Intangible Assets

On August 18, 2014, a subsidiary of Teledyne acquired assets of Atlas Hydrographic GmbH (“Atlas”) for \$5.2 million. On March 31, 2014, a subsidiary of Teledyne acquired Photon Machines, Inc. (“Photon”) for an initial payment of \$3.3 million. Teledyne expects to pay an additional \$0.7 million in equal installments over the next three years.

On October 22, 2013, a subsidiary of Teledyne acquired C.D. Limited (“CDL”) for \$21.8 million in cash, net of cash acquired. On August 30, 2013, a subsidiary of Teledyne acquired the assets of SD Acquisition, Inc. d/b/a CETAC Technologies (“CETAC”) for \$26.4 million and paid a \$0.4 million purchase price adjustment in the fourth quarter of 2013. On July 5, 2013, a subsidiary of Teledyne purchased the remaining 49% interest in Nova Research, Inc. (“Nova Sensors”) that it did not already own for \$4.9 million. On May 8, 2013, a subsidiary of Teledyne acquired Axiom IC B.V. (“Axiom”), for an initial payment of \$4.0 million, net of cash acquired, with an additional \$1.3 million expected to be paid in equal installments over three years. The first of the three installments was made in May 2014. On March 1,

2013, a subsidiary of Teledyne acquired all the outstanding shares of RESON A/S (“RESON”) for \$69.7 million, net of cash acquired. Atlas, Photon, CDL, CETAC and RESON are part of the Instrumentation segment and Nova Sensors and Axiom are part of the Digital Imaging segment.

Teledyne funded the purchases from borrowings under its credit facility and cash on hand. The results of the acquisitions have been included in Teledyne's results since the dates of the respective acquisition.

In the third quarter of 2014, Teledyne announced an agreement to acquire all of the outstanding common shares of Bolt Technology Corporation ("Bolt") for \$22.00 per share payable in cash. The aggregate value for the transaction is approximately \$171.1 million, excluding transaction costs and taking into account Bolt's stock options, other liabilities and net cash as of June 30, 2014. Bolt is a developer and manufacturer of marine seismic data acquisition equipment used for offshore oil and natural gas exploration. Bolt is also a developer and manufacturer of remotely operated robotic vehicles systems used for a variety of underwater tasks. The transaction is expected to close in November 2014, subject to customary closing conditions. See also Note 15 regarding the fourth quarter 2014 acquisition of the business and substantially all of the assets of The Oceanscience Group Ltd. ("Oceanscience").

For a further description of the Company's acquisition activity for the fiscal year ended December 29, 2013, please refer to Note 3 of our 2013 Form 10-K.

Teledyne's goodwill was \$1,028.0 million at September 28, 2014 and \$1,037.8 million at December 29, 2013. The decrease in the balance of goodwill in 2014 resulted from the impact of exchange rate changes, partially offset by the Photon and Atlas acquisitions. Except for the CETAC, Atlas and Oceanscience acquisitions, goodwill resulting from the acquisitions made in fiscal 2014 and 2013 will not be deductible for tax purposes. Teledyne's net acquired intangible assets were \$244.5 million at September 28, 2014 and \$270.9 million at December 29, 2013. The decrease in the balance of acquired intangible assets in 2014 primarily resulted from amortization, partially offset by acquired intangibles for the Photon and Atlas acquisitions. The Company is in the process of specifically identifying the amounts assigned to certain assets and liabilities, acquired intangible assets and the related impact on goodwill for the Photon and Atlas acquisitions.

Note 4. Derivative Instruments

Teledyne transacts business in various foreign currencies and has international sales and expenses denominated in foreign currencies, subjecting the Company to foreign currency risk. The Company's primary foreign currency risk management objective is to protect the United States dollar value of future cash flows and minimize the volatility of reported earnings. The Company utilizes foreign currency forward contracts to reduce the volatility of cash flows primarily related to forecasted revenues and expenses denominated in Canadian dollars. These contracts are designated and qualify as cash flow hedges.

Cash Flow Hedging Activities

The effectiveness of the cash flow hedge contracts, excluding time value, is assessed prospectively and retrospectively on a monthly basis using regression analysis, as well as using other timing and probability criteria. To receive hedge accounting treatment, all hedging relationships are formally documented at the inception of the hedges and must be highly effective in offsetting changes to future cash flows on hedged transactions. The effective portion of the cash flow hedge contracts' gains or losses resulting from changes in the fair value of these hedges is initially reported, net of tax, as a component of AOCI in stockholders' equity until the underlying hedged item is reflected in our consolidated statements of income, at which time the effective amount in AOCI is reclassified to cost of sales in our consolidated statements of income. Net deferred gains recorded in AOCI, net of tax, for contracts that will mature in the next twelve months total \$1.3 million. These gains are expected to be offset by anticipated losses in the value of the forecasted underlying hedged item.

In the event that the gains or losses in AOCI are deemed to be ineffective, the ineffective portion of gains or losses resulting from changes in fair value, if any, is reclassified to other income and expense. In the event that the underlying forecasted transactions do not occur, or it becomes remote that they will occur, within the defined hedge period, the gains or losses on the related cash flow hedges will be reclassified from AOCI to other income and expense. During the current reporting period, all forecasted transactions occurred and, therefore, there were no such gains or losses reclassified to other income and expense. As of September 28, 2014, Teledyne had foreign currency forward contracts designated as cash flow hedges to buy Canadian dollars and to sell U.S. dollars totaling \$96.6 million. These foreign currency forward contracts have maturities ranging from October 2014 to June 2016.

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Non-Designated Hedging Activities

In addition, the Company utilizes foreign currency forward contracts to mitigate foreign exchange rate risk associated with foreign-currency-denominated monetary assets and liabilities, including intercompany receivables and payables. As of September 28, 2014, Teledyne had foreign currency contracts of this type in the following pairs (in millions):

Contracts to Buy		Contracts to Sell	
Currency	Amount	Currency	Amount
Canadian Dollars	C\$ 85.3	U.S. Dollars	US\$78.0
Euros	€ 25.3	U.S. Dollars	US\$32.6
Great Britain Pounds	£ 36.6	U.S. Dollars	US\$59.7
U.S. Dollars	US\$31.4	Canadian Dollars	C\$ 34.9
U.S. Dollars	US\$29.2	Euros	€ 22.6
U.S. Dollars	US\$29.7	Great Britain Pounds	£ 18.2

The gains and losses on these derivatives which are not designated as hedging instruments are intended to, at a minimum, partially offset the transaction gains and losses recognized in earnings. All derivatives are recorded on the balance sheet at fair value. As discussed below, the accounting for gains and losses resulting from changes in fair value depends on the use of the derivative and whether it is designated and qualifies for hedge accounting. Teledyne does not use foreign currency forward contracts for speculative or trading purposes.

The effect of derivative instruments designated as cash flow hedges in our condensed consolidated financial statements for the third quarter and nine months ended September 28, 2014 and September 29, 2013 was as follows (in millions):

	Third Quarter		Nine Months	
	2014	2013	2014	2013
Net income (loss) recognized in AOCI (a)	\$ (3.1)	\$ 1.1	\$ (2.9)	\$ (1.6)
Net loss reclassified from AOCI into cost of sales (a)	\$ (0.6)	\$ (0.7)	\$ (2.4)	\$ (1.0)
Net foreign exchange gain recognized in other income and expense (b)	\$ 0.2	\$ 0.2	\$ 0.5	\$ 0.4
a) Effective portion, pre-tax				
b) Amount excluded from effectiveness testing				

The effect of derivative instruments not designated as cash flow hedges recognized in other income and expense for the third quarter and nine months ended September 28, 2014 was \$3.1 million and \$2.0 million of gain, respectively. The effect of derivative instruments not designated as cash flow hedges recognized in other income and expense for the third quarter and nine months ended September 29, 2013 was \$1.0 million and \$0.6 million of expense, respectively.

Fair Value of Derivative Financial Instruments

The fair values of the Company's derivative financial instruments are presented below. All fair values for these derivatives were measured using Level 2 information as defined by the accounting standard hierarchy (in millions):

Asset/(Liability) Derivatives	Balance sheet location	September 28, 2014	December 29, 2013
Derivatives designated as hedging instruments:			
Cash flow forward contracts	Other assets	\$0.1	\$—
Cash flow forward contracts	Accrued liabilities	(1.7)	(1.2)
Total derivatives designated as hedging instruments		(1.6)	(1.2)
Derivatives not designated as hedging instruments:			
Non-designated forward contracts	Other current assets	0.4	0.2
Non-designated forward contracts	Accrued liabilities	(2.3)	(0.9)
Total derivatives not designated as hedging instruments		(1.9)	(0.7)
Total asset (liability) derivatives		\$(3.5)	\$(1.9)

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Note 5. Earnings Per Share

Basic and diluted earnings per share were computed based on net earnings. The weighted average number of common shares outstanding during the period was used in the calculation of basic earnings per share. This number of shares was increased by contingent shares that could be issued under various compensation plans as well as by the dilutive effect of stock options based on the treasury stock method in the calculation of diluted earnings per share.

In September 2014, the Company entered into a \$101.6 million accelerated share repurchase agreement (“ASR”) with a financial institution (“ASR Counterparty”) in a privately negotiated transaction for 1,030,000 shares of the Company's common stock at an initial price of \$98.62 per share. Pursuant to the ASR agreement, in September 2014, the Company advanced \$101.6 million to the ASR counterparty and received 927,000 shares of common stock, representing 90% of the estimated shares to be repurchased under the ASR agreement. The Company treated the ASR as a treasury share purchase of common stock in the period the shares were delivered for purposes of calculating earnings per share. The up-front payment was accounted for as a reduction to stockholders' equity in the Company's Condensed Consolidated Balance Sheet in the period the payment was made. The total number of shares of common stock that the Company will repurchase under the ASR will be based on the average of the daily volume-weighted average prices of the common stock during the term of the ASR, less a discount. At settlement, the ASR Counterparty may be required to deliver additional shares of the Company's common stock to the Company or, under certain circumstances, the Company may be required to deliver shares of its common stock or make a cash payment to the ASR Counterparty. Final settlement of the ASR agreement is expected to occur in June 2015, although the settlement may be accelerated at the ASR Counterparty's option. The Company will treat the ASR as a treasury share repurchase of common stock in the period the shares are delivered for purposes of calculating earnings per share and as a forward contract indexed to its own common stock. The ASR meets all of the applicable criteria for equity classification, and, therefore, is not accounted for as a derivative instrument.

In the first nine months of 2014, the Company spent \$146.6 million, which includes \$101.6 million advanced under the ASR to repurchase its common stock. In the first nine months of 2014, the Company repurchased 1,396,290 shares of its common stock at an average price \$97.70 per share.

For the third quarter and first nine months of 2014, 6,500 stock options were excluded in the computation of diluted earnings per share because they had exercise prices that were greater than the average market price of the Company's common stock during the respective periods. For the third quarter and first nine months of 2013, no stock options were excluded in the computation of diluted earnings per share. The following table sets forth the computations of basic and diluted earnings per share (amounts in millions, except per share data):

	Third Quarter		Nine Months	
	2014	2013	2014	2013
Net income attributable to Teledyne	\$55.6	\$46.8	\$157.5	\$130.1
Basic earnings per share:				
Weighted average common shares outstanding	37.2	37.3	37.4	37.3
Basic earnings per common share	\$1.49	\$1.25	\$4.21	\$3.49
Diluted earnings per share:				
Weighted average common shares outstanding	37.2	37.3	37.4	37.3
Dilutive effect of exercise of options outstanding	0.6	0.8	0.7	0.7
Weighted average diluted common shares outstanding	37.8	38.1	38.1	38.0
Diluted earnings per common share	\$1.47	\$1.23	\$4.13	\$3.42

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Note 6. Stock-Based Compensation Plans

Teledyne has long-term incentive plans pursuant to which it has granted non-qualified stock options, restricted stock and performance shares to certain employees. The Company also has non-employee director stock compensation plans, pursuant to which non-qualified stock options and common stock have been issued to its directors.

Stock Incentive Plan

The following disclosures are based on stock options granted to Teledyne's employees and directors. The Company recorded a total of \$3.9 million and \$10.1 million in stock option compensation expense for the third quarter and first nine months of 2014, respectively. For the third quarter and first nine months of 2013, the company recorded a total of \$3.0 million and \$7.6 million, in stock option compensation expense, respectively. Employee stock option grants are charged to expense evenly over the three year vesting period. Director stock option grants are charged to expense evenly over the one-year vesting period. For 2014, the Company currently expects approximately \$14.2 million in stock option compensation expense based on stock options already granted and current assumptions regarding the estimated fair value of stock option grants expected to be issued during the remainder of the year. However, our assessment of the estimated compensation expense will be affected by our stock price, actual stock option grants during the remainder of the year and employee retirements and termination as well as assumptions regarding a number of complex and subjective variables and the related tax impact. These variables include, but are not limited to, the volatility of our stock price and employee stock option exercise behaviors. The Company issues shares of common stock upon the exercise of stock options.

The Company uses its historical stock price volatility on the Company stock to compute the expected volatility for purposes of valuing stock options issued. The period used for the historical stock price corresponded to the expected term of the options and was seven years, five months. The expected dividend yield is based on Teledyne's practice of not paying dividends. The risk-free rate of return is based on the yield of U. S. Treasury Strips with terms equal to the expected life of the options as of the grant date. The expected life in years is based on historical actual stock option exercise experience.

The following assumptions will be used in the valuation of stock options granted in 2014 and 2013:

	2014	2013	
Expected dividend yield	—	—	
Expected volatility	30.7	% 31.9	%
Risk-free interest rate	1.7	% 0.9	%
Expected life in years	7.4	7.3	

Based on the assumptions in the table above, the grant date weighted average fair value of stock options granted in 2014 and 2013 was \$36.19 and \$27.17, respectively.

Stock option transactions for Teledyne's employee stock option plans for the third quarter and nine months ended September 28, 2014 are summarized as follows:

	2014		2013	
	Third Quarter	Weighted Average Exercise Price	Nine Months	Weighted Average Exercise Price
	Shares		Shares	
Beginning balance	2,645,094	\$63.15	2,419,372	\$53.77
Granted	6,500	\$95.74	567,008	\$94.22
Exercised	(21,291)	\$46.58	(320,436)	\$44.40
Canceled or expired	(30,471)	\$74.39	(66,112)	\$73.49
Ending balance	2,599,832	\$63.24	2,599,832	\$63.24
Options exercisable at end of period	1,562,436	\$49.41	1,562,436	\$49.41

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Stock option transactions for Teledyne's non-employee director stock option plans for the third quarter and nine months ended September 28, 2014 are summarized as follows:

	2014		Nine Months	
	Third Quarter	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Beginning balance	364,190	\$50.03	324,381	\$44.99
Granted	2,824	\$65.96	42,633	\$89.37
Ending balance	367,014	\$50.15	367,014	\$50.15
Options exercisable at end of period	324,129	\$44.98	324,129	\$44.98

Performance Share Plan and Restricted Stock Award Program

For the third and final installment of the 2009 to 2011 Performance Share Plan, 19,742 shares of Teledyne common stock were issued in the first quarter of 2014. Also in the first quarter of 2014, the restriction was removed for 40,257 shares of Teledyne common stock and 3,397 shares were forfeited related to the 2011 to 2013 Restricted Stock Award Program. In the first nine months of 2014, the Company granted 37,688 shares of restricted stock at a weighted average fair value of \$88.05 per share.

Note 7. Cash Equivalents

Cash equivalents consist of highly liquid money-market mutual funds and bank deposits with maturities of three months or less when purchased. Cash equivalents totaled \$0.5 million at September 28, 2014 and \$0.3 million at December 29, 2013.

Note 8. Inventories

Inventories are stated at the lower of cost or market, less progress payments. Inventories are valued under the FIFO method, LIFO method and average cost method. Inventories at cost determined on the average cost or the FIFO methods were \$239.5 million at September 28, 2014 and \$240.2 million at December 29, 2013. The remainder of the inventories using the LIFO method were \$96.1 million at September 28, 2014 and \$83.4 million at December 29, 2013. Interim LIFO calculations are based on the Company's estimates of expected year-end inventory levels and costs since an actual valuation of inventory under the LIFO method can be made only at the end of each year based on the inventory levels and costs at that time. Because these are subject to many factors beyond the Company's control, interim results are subject to the final year-end LIFO inventory valuation. Inventories consist of the following (in millions):

Balance at	September 28, 2014	December 29, 2013
Raw materials and supplies	\$134.8	\$130.7
Work in process	159.6	151.5
Finished goods	41.2	41.4
	335.6	323.6
Progress payments	(8.2)	(12.7)
LIFO reserve	(16.5)	(16.6)
Total inventories, net	\$310.9	\$294.3

Note 9. Supplemental Balance Sheet Information

The following table presents the balance of selected components of Teledyne's balance sheet (in millions):

Balance sheet items	Balance sheet location	September 28, 2014	December 29, 2013
Deferred tax assets	Prepaid expenses and other current assets	\$37.3	\$31.9
Deferred compensation assets	Other assets, net	\$48.8	\$44.7
Salaries and wages	Accrued liabilities	\$95.5	\$103.2
Customer deposits and credits	Accrued liabilities	\$58.3	\$55.6
Deferred compensation liabilities	Other long-term liabilities	\$45.7	\$43.1

Deferred income taxes	Other long-term liabilities	\$115.2	\$112.3
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During 2013, in an effort to reduce ongoing costs and improve operating performance, the Company took actions to consolidate and relocate certain facilities and reduce headcount across various businesses. The actions taken were substantially completed by year end 2013. At September 28, 2014 and December 29, 2013, the Company had \$8.8 million and \$11.4 million in short-term reserves related to these actions, which includes \$5.2 million in short-term environmental reserves at September 28, 2014.

Some of the Company's products are subject to specified warranties and the Company provides for the estimated cost of product warranties. The adequacy of the pre-existing warranty liabilities is assessed regularly and the reserve is adjusted as necessary based on a review of historic warranty experience with respect to the applicable business or products, as well as the length and actual terms of the warranties, which are typically one year. The product warranty reserve is included in current and long term accrued liabilities on the balance sheet. Changes in the Company's product warranty reserve during the first nine months of 2014 and 2013 are as follows (in millions):

	Nine Months	
	2014	2013
Balance at beginning of year	\$17.3	\$17.8
Accruals for product warranties charged to expense	2.7	4.7
Cost of product warranty claims	(4.1	) (4.2
Acquisitions	0.1	0.3
Balance at end of period	\$16.0	\$18.6

Note 10. Income Taxes

The income tax provision is calculated using an estimated annual effective tax rate, based upon expected annual income, permanent items, statutory rates and planned tax strategies in the various jurisdictions in which the Company operates. However, losses in certain jurisdictions and discrete items, such as the resolution of uncertain tax positions, are treated separately.

The Company's effective income tax rate for the third quarter and nine months of 2014 was 19.2% and 24.6%, respectively. The Company's effective income tax rate for the third quarter and nine months of 2013 was 0.6% and 18.8%, respectively. The third quarter of 2014 included net tax benefits for discrete items of \$6.1 million and the first nine months of 2014 included net tax benefits for discrete items of \$8.2 million, compared with net tax benefits for discrete items of \$11.6 million and \$15.2 million for the third quarter and first nine months of 2013, respectively. The net tax benefits for the first nine months of 2014 included the remeasurement of uncertain tax positions primarily due to the expiration of statute of limitations and a favorable resolution of a tax matter. The net tax benefits for the first nine months of 2013 primarily related to the remeasurement of uncertain tax positions including the expiration of statute of limitations, and a favorable resolution of a tax matter. Excluding net discrete tax benefits in all periods, the effective tax rates would have been 28.1% for the third quarter and 28.5% for the first nine months of 2014 and 25.2% for the third quarter of 2013 and 28.3% for the first nine months of 2013.

During the next twelve months, it is reasonably possible that expirations of the statutes of limitations could reduce unrecognized tax benefits by \$7.5 million, of which \$0.6 million would not impact tax expense as it would be offset by the reversal of deferred tax assets.

Note 11. Long-Term Debt and Capital Leases

Long-term debt consisted of the following (in millions):

	September 28, 2014	December 29, 2013
Balance at		
4.04% Notes due September 2015	\$75.0	\$75.0
4.74% Notes due September 2017	100.0	100.0
5.30% Notes due September 2020	75.0	75.0
Term loans due through March 2019, weighted average rate of 1.16% at September 28, 2014 and 1.29% at December 29, 2013	200.0	200.0
Other debt at various rates due through 2031	16.7	16.0
\$750.0 million revolving credit facility due March 2018, weighted average rate of 1.13% at September 28, 2014 and 1.26% at December 29, 2013	100.0	74.2

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Total debt	566.7	540.2
Less: current portion of long-term debt	(83.7) (2.1
Total long-term debt	\$483.0) \$538.1

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Available borrowing capacity under the \$750.0 million credit facility, which is reduced by borrowings and certain outstanding letters of credit, was \$634.5 million at September 28, 2014. The credit agreement requires the Company to comply with various financial and operating covenants and at September 28, 2014, the Company was in compliance with these covenants. In September 2014 Teledyne priced \$125.0 million senior unsecured notes with an average fixed rate of 2.97%. The senior unsecured notes are expected to be issued in December 2014 and will consist of \$30.0 million of 2.61% senior unsecured notes due December 4, 2019, and \$95.0 million of 3.09% senior unsecured notes due December 6, 2021.

Teledyne estimates the fair value of its long-term debt based on debt of similar type, rating and maturity and at comparable interest rates. The estimated fair value of Teledyne's long-term debt at September 28, 2014 and December 29, 2013, approximated the carrying value.

As September 28, 2014, the Company has \$11.1 million in capital leases, of which \$1.3 million is current. At December 29, 2013, the Company had \$12.3 million in capital leases, of which \$1.4 million was current. At September 28, 2014, Teledyne had \$17.1 million in outstanding letters of credit.

Note 12. Lawsuits, Claims, Commitments, Contingencies and Related Matters

For a further description of the Company's commitments and contingencies, reference is made to Note 15 of the Company's financial statements as of and for the fiscal year ended December 29, 2013, included in our 2013 Form 10-K.

At September 28, 2014, the Company's reserves for environmental remediation obligations totaled \$8.9 million, of which \$5.7 million is included in current accrued liabilities. The Company periodically evaluates whether it may be able to recover a portion of future costs for environmental liabilities from its insurance carriers and from third parties. The timing of expenditures depends on a number of factors that vary by site, including the nature and extent of contamination, the number of potentially responsible parties, the timing of regulatory approvals, the complexity of the investigation and remediation, and the standards for remediation. The Company expects that it will expend present accruals over many years, and will complete remediation of all sites with which it has been identified in up to 30 years.

A number of other lawsuits, claims and proceedings have been or may be asserted against the Company, including those pertaining to product liability, acquisitions, patent infringement, commercial contracts, environmental, employment and employee benefits matters. While the outcome of litigation cannot be predicted with certainty, and some of these lawsuits, claims or proceedings may be determined adversely to the Company, management does not believe that the disposition of any such pending matters is likely to have a material adverse effect on the Company's financial condition. The resolution in any reporting period of one or more of these matters could have a material adverse effect on the Company's results of operations for that period.

Note 13. Pension Plans and Postretirement Benefits

Teledyne's pension income was \$0.3 million and \$1.0 million for the third quarter and first nine months of 2014, respectively, compared with pension expense of \$4.3 million and \$13.0 million for the third quarter and first nine months of 2013, respectively. The change to pension income in 2014, from pension expense in 2013, primarily reflected the impact of using a 5.4 percent discount rate to determine the benefit obligation for the domestic plan in 2014 compared with a 4.4 percent discount rate used in 2013. Pension expense allocated to contracts pursuant to U.S. Government Cost Accounting Standards ("CAS") was \$3.4 million and \$10.3 million for the third quarter and first nine months of 2014, respectively, compared with \$3.6 million and \$10.8 million for the third quarter and first nine months of 2013, respectively. Pension expense determined under CAS can generally be recovered through the pricing of products and services sold to the U.S. Government. Teledyne did not make any cash pension contributions to its domestic pension plan in the first nine months of 2014, compared with voluntary pretax cash pension contributions totaling \$83.0 million to its domestic pension plan in the first nine months of 2013. No cash pension contributions are planned for 2014 for the domestic pension plan.

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The Company sponsors several postretirement defined benefit plans that provide health care and life insurance benefits for certain eligible retirees. The following tables set forth the components of net income/expense for Teledyne's pension plans and postretirement benefit plans for the third quarter and first nine months of 2014 and 2013 (in millions):

	Third Quarter		Nine Months	
	2014	2013	2014	2013
Pension Benefits				
Service cost — benefits earned during the period	\$3.2	\$3.8	\$9.4	\$11.4
Interest cost on benefit obligation	10.6	9.5	31.9	28.6
Expected return on plan assets	(19.1)	(18.0)	(57.3)	(54.1)
Amortization of prior service cost	(1.2)	(1.1)	(3.5)	(3.4)
Amortization of net actuarial loss	6.2	10.1	18.5	30.5
Net (income)/expense	\$(0.3)	\$4.3	\$(1.0)	\$13.0
	Third Quarter		Nine Months	
	2014	2013	2014	2013
Postretirement Benefits				
Interest cost on benefit obligation	\$0.2	\$0.1	\$0.5	\$0.3
Amortization of prior service cost	(0.1)	(0.1)	(0.2)	(0.3)
Amortization of net actuarial gain	(0.1)	—	(0.4)	(0.1)
Net income	\$—	\$—	\$(0.1)	\$(0.1)

Note 14. Industry Segments

Teledyne is a leading provider of sophisticated instrumentation, digital imaging products and software, aerospace and defense electronics, and engineered systems. Our customers include government agencies, aerospace prime contractors, energy exploration and production companies, major industrial companies and airlines.

The Company has four reportable segments: Instrumentation; Digital Imaging; Aerospace and Defense Electronics; and Engineered Systems. The Company manages, evaluates and aggregates its operating segments for segment reporting purposes primarily on the basis of product and service type, production process, distribution methods, type of customer, management organization, sales growth potential and long-term profitability. The Instrumentation segment provides monitoring and control equipment for marine, environmental, scientific, industrial and defense applications, electronic test and measurement instruments and harsh environment interconnect products. The Digital Imaging segment includes high performance sensors, cameras and systems, within the visible, infrared and X-ray spectra, for use in industrial, government and medical applications, as well as micro electro-mechanical systems. It also includes our sponsored and centralized research laboratories benefiting government programs and businesses. The Aerospace and Defense Electronics segment provides sophisticated electronic components and subsystems and communications products, including defense electronics, harsh environment interconnects, data acquisition and communications equipment for aircraft and components and subsystems for wireless and satellite communications, as well as general aviation batteries. The Engineered Systems segment provides innovative systems engineering and integration, advanced technology application, software development and manufacturing solutions for defense, space, environmental and energy applications. The Engineered Systems segment also designs and manufactures electrochemical energy systems and small turbine engines.

Segment operating profit includes other income and expense directly related to the segment, but excludes noncontrolling interest, equity income or loss, unusual non-recurring legal matter settlements, interest income and expense, gains and losses on the disposition of assets, sublease rental income and non-revenue licensing and royalty income, domestic and foreign income taxes and corporate office expenses.

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The following table presents Teledyne's interim industry segment disclosures for net sales and operating profit including other segment income. The table also provides a reconciliation of segment operating profit to total net income attributable to Teledyne (dollars in millions):

	Third Quarter		% Change	Nine Months		% Change		
	2014	2013		2014	2013			
Net sales:								
Instrumentation	\$280.4	\$256.6	9.3	%	\$815.9	\$747.0	9.2	%
Digital Imaging	95.6	105.2	(9.1)	)%	301.2	311.9	(3.4))%
Aerospace and Defense Electronics	151.8	143.1	6.1	%	457.3	475.7	(3.9))%
Engineered Systems	73.3	66.7	9.9	%	197.3	207.4	(4.9))%
Total net sales	\$601.1	\$571.6	5.2	%	\$1,771.7	\$1,742.0	1.7	%
Segment operating profit:								
Instrumentation	\$46.9	\$39.9	17.5	%	\$128.2	\$117.6	9.0	%
Digital Imaging	7.9	11.5	(31.3)	)%	29.3	24.6	19.1	%
Aerospace and Defense Electronics	21.6	9.3	132.3	%	68.3	50.1	36.3	%
Engineered Systems	8.5	2.7	214.8	%	21.4	14.8	44.6	%
Segment operating profit	84.9	63.4	33.9	%	247.2	207.1	19.4	%
Corporate expense	(10.6)	(10.4)	1.9	%	(32.6)	(30.3)	7.6	%
Operating income	74.3	53.0	40.2	%	214.6	176.8	21.4	%
Other income/(expense), net	(1.8)	(0.7)	157.1	%	7.0	(1.2)	*	
Interest and debt expense, net	(4.6)	(5.1)	(9.8)	)%	(13.9)	(15.6)	(10.9))%
Income before income taxes	67.9	47.2	43.9	%	207.7	160.0	29.8	%
Provision for income taxes	13.0	0.3	*		51.0	30.0	70.0	%
Net income	54.9	46.9	17.1	%	156.7	130.0	20.5	%
Noncontrolling interest	0.7	(0.1)	*		0.8	0.1	*	
Net income attributable to Teledyne	\$55.6	\$46.8	18.8	%	\$157.5	\$130.1	21.1	%

* not meaningful

Product Lines

The Instrumentation segment includes three product lines: Environmental Instrumentation, Marine Instrumentation and Test and Measurement Instrumentation. Beginning in the first quarter of 2014, within the instrumentation segment, one business unit previously reported in the environmental instrumentation product line is now reported as part of the test and measurement instrumentation product line. Total sales for the business unit for 2013 were \$9.4 million. Previously reported product line data has been restated to reflect this change. The Digital Imaging segment contains one product line as does the Aerospace and Defense Electronics segment. The Engineered Systems segment includes three product lines: Engineered Products and Services, Turbine Engines and Energy Systems.

The following tables provide a summary of the sales by product line for the Instrumentation segment and the Engineered Systems segment (in millions):

	Third Quarter		Nine Months	
	2014	2013	2014	2013
Instrumentation				
Environmental Instrumentation	\$66.1	\$57.1	\$196.8	\$180.2
Marine Instrumentation	167.4	151.6	478.1	424.3
Test and Measurement Instrumentation	46.9	47.9	141.0	142.5
Total	\$280.4	\$256.6	\$815.9	\$747.0
Engineered Systems				
Engineered Products and Services	\$57.1	\$51.1	\$155.0	\$163.4
Turbine Engines	6.2	6.4	19.0	21.1
Energy Systems	10.0	9.2	23.3	22.9

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Total	\$73.3	\$66.7	\$197.3	\$207.4
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Note 15. Subsequent Event

On October 23, 2014, a subsidiary of Teledyne acquired the business and substantially all of the assets of Oceanscience for \$15.0 million. Based in Carlsbad, California, Oceanscience designs and manufactures marine sensor platforms and unmanned surface vehicles.

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

Teledyne Technologies Incorporated provides enabling technologies for industrial growth markets. We have evolved from a company that was primarily focused on aerospace and defense to one that serves multiple markets that require advanced technology and high reliability. These markets include deepwater oil and gas exploration and production, oceanographic research, air and water quality environmental monitoring, factory automation and medical imaging. Our products include monitoring instrumentation for marine and environmental applications, harsh environment interconnects, electronic test and measurement equipment, digital imaging sensors and cameras, aircraft information management systems, and defense electronic and satellite communication subsystems. We also supply engineered systems for defense, space, environmental and energy applications. We differentiate ourselves from many of our direct competitors by having a customer and company sponsored applied research center that augments our product development expertise.

Strategy/Overview

Our strategy continues to emphasize growth in our core markets of instrumentation, digital imaging, aerospace and defense electronics and engineered systems. Our core markets are characterized by high barriers to entry and include specialized products and services not likely to be commoditized. We intend to strengthen and expand our core businesses with targeted acquisitions and through product development. We aggressively pursue operational excellence to continually improve our margins and earnings. Operational excellence includes the rapid integration of the businesses we acquire. Using complementary technology across our businesses and internal research and development, we seek to create new products to grow our company and expand our addressable markets. We continue to evaluate our businesses to ensure that they are aligned with our strategy.

Our third quarter 2014 sales were \$601.1 million, compared with sales of \$571.6 million for the same period of 2013, an increase of 5.2%. Net income attributable to Teledyne was \$55.6 million (\$1.47 per diluted share) for the third quarter of 2014, compared with \$46.8 million (\$1.23 per diluted share) for the third quarter of 2013, an increase of 18.8%.

Our Recent Acquisitions

On August 18, 2014, a subsidiary of Teledyne acquired assets of Atlas Hydrographic GmbH ("Atlas") for \$5.2 million. On March 31, 2014, a subsidiary of Teledyne acquired Photon Machines, Inc. ("Photon") for an initial payment of \$3.3 million. Teledyne expects to pay an additional \$0.7 million in equal installments over the next three years.

In October 2013, a subsidiary of Teledyne acquired C.D. Limited ("CDL") for \$21.8 million in cash, net of cash acquired. In August 2013, a subsidiary of Teledyne acquired the assets of SD Acquisition, Inc. d/b/a CETAC Technologies ("CETAC") for \$26.4 million and paid a \$0.4 million purchase price adjustment in the fourth quarter. In July 2013, a subsidiary of Teledyne purchased the remaining 49% interest in Nova Research, Inc. ("Nova Sensors") that it did not already own for \$4.9 million. In May 2013, a subsidiary of Teledyne acquired Axiom IC B.V. ("Axiom") for an initial payment of \$4.0 million, net of cash acquired, with an additional \$1.3 million expected to be paid in equal installments over three years. The first of the three installments was made in May 2014. In March 2013, a subsidiary of Teledyne acquired all the outstanding shares of RESON A/S ("RESON") for \$69.7 million, net of cash acquired.

Atlas, Photon, CDL, CETAC and RESON are part of the Instrumentation segment and Nova Sensors and Axiom are part of the Digital Imaging segment.

Teledyne funded the purchases from borrowings under its credit facility and cash on hand. The results of these acquisitions have been included in Teledyne's results since the dates of the respective acquisitions.

In the third quarter of 2014, Teledyne announced an agreement to acquire all of the outstanding common shares of Bolt Technology Corporation ("Bolt") for \$22.00 per share payable in cash. The aggregate value for the transaction is approximately \$171.1 million, excluding transaction costs and taking into account Bolt's stock options, other liabilities and net cash as of June 30, 2014. Bolt is a developer and manufacturer of marine seismic data acquisition equipment used for offshore oil and natural gas exploration. Bolt is also a developer and manufacturer of remotely operated robotic vehicles systems used for a variety of underwater tasks. When closed, Bolt will broaden our portfolio of marine instrumentation with a number of highly complementary products. The transaction is expected to close in November 2014, subject to customary closing conditions. In the fourth quarter of 2014, a subsidiary of Teledyne acquired the business and substantially all of the assets of The Oceanscience Group Ltd. ("Oceanscience") for \$15.0

million. Oceanscience designs and manufactures marine sensor platforms and unmanned surface vehicles. For a further description of the Company's acquisition activity for the fiscal year ended December 29, 2013, please refer to Note 3 of our 2013 Form 10-K ("2013 Form 10-K").

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Results of Operations

(in millions)	Third Quarter		Nine Months	
	2014	2013	2014	2013
Net Sales	\$601.1	\$571.6	\$1,771.7	\$1,742.0
Costs and expenses				
Cost of sales	375.4	369.0	1,095.5	1,118.0
Selling, general and administrative expenses	151.4	149.6	461.6	447.2
Total costs and expenses	526.8	518.6	1,557.1	1,565.2
Operating income	74.3	53.0	214.6	176.8
Other income/(expense), net	(1.8)	(0.7)	7.0	(1.2)
Interest and debt expense, net	(4.6)	(5.1)	(13.9)	(15.6)
Income before income taxes	67.9	47.2	207.7	160.0
Provision for income taxes	13.0	0.3	51.0	30.0
Net income	54.9	46.9	156.7	130.0
Noncontrolling interest	0.7	(0.1)	0.8	0.1
Net income attributable to Teledyne	\$55.6	\$46.8	\$157.5	\$130.1

The table below presents sales and cost of sales by segment and total company:

(Dollars in millions)	Third Quarter		Nine Months	
	2014	2013	2014	2013
Instrumentation				
Sales	\$280.4	\$256.6	\$815.9	\$747.0
Cost of sales	\$156.8	\$144.9	\$456.5	\$414.0
Cost of sales % of sales	55.9	% 56.5	% 56.0	% 55.5
Digital Imaging				
Sales	\$95.6	\$105.2	\$301.2	\$311.9
Cost of sales	\$59.7	\$64.3	\$187.4	\$196.0
Cost of sales % of sales	62.4	% 61.2	% 62.2	% 62.8
Aerospace and Defense Electronics				
Sales	\$151.8	\$143.1	\$457.3	\$475.7
Cost of Sales	\$99.7	\$102.0	\$291.9	\$332.9
Cost of sales % of sales	65.7	% 71.3	% 63.9	% 70.0
Engineered Systems				
Sales	\$73.3	\$66.7	\$197.3	\$207.4
Costs of sales	\$59.2	\$57.8	\$159.7	\$175.1
Cost of sales % of sales	80.8	% 86.7	% 81.0	% 84.4
Total Company				
Sales	\$601.1	\$571.6	\$1,771.7	\$1,742.0
Costs of sales	\$375.4	\$369.0	\$1,095.5	\$1,118.0
Cost of sales % of sales	62.5	% 64.5	% 61.8	% 64.2

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Third quarter of 2014 compared with the third quarter of 2013

Our third quarter 2014 sales were \$601.1 million, compared with sales of \$571.6 million for the third quarter of 2013, an increase of 5.2%. Net income attributable to Teledyne was \$55.6 million (\$1.47 per diluted share) for the third quarter of 2014, compared with \$46.8 million (\$1.23 per diluted share) for the third quarter of 2013, an increase of 18.8%.

Sales

The third quarter of 2014, compared with the third quarter of 2013, reflected higher sales in each segment except the Digital Imaging segment. Third quarter 2014 sales included the impact of acquisitions and higher organic sales. Incremental revenue in the third quarter of 2014 from recent acquisitions was \$10.2 million. The third quarter of 2014, compared with the third quarter of 2013, reflected higher operating profit in each business segment except the Digital Imaging segment.

Operating Income

Operating income increased to \$74.3 million for the third quarter of 2014, from \$53.0 million for the third quarter of 2013, an increase of 40.2%. Operating income reflected lower costs as a result of the cost reduction actions taken in 2013 and the impact of pension income. Operating income in the third quarter of 2014 included \$1.2 million in severance and facility consolidation costs, compared with \$14.3 million of similar costs in the third quarter of 2013. The incremental operating income included in the results for the third quarter of 2014 from recent acquisitions was \$0.4 million which included \$0.2 million in additional intangible asset amortization expense.

Pension Income/Expense

The third quarter of 2014 included pension income of \$0.3 million, compared with pension expense of \$4.3 million in the third quarter of 2013. The change to pension income in 2014 from pension expense in 2013, primarily reflected the impact of using a 5.4 percent discount rate to determine the benefit obligation for the domestic plan in 2014 compared with a 4.4 percent discount rate used in 2013. Pension expense allocated to contracts pursuant to U.S. Government Cost Accounting Standards ("CAS") was \$3.4 million in the third quarter of 2014, compared with \$3.6 million in the third quarter of 2013. Pension expense determined allowable under CAS can generally be recovered through the pricing of products and services sold to the U.S. Government.

Cost of Sales

Cost of sales increased by \$6.4 million in the third quarter of 2014, compared with the third quarter of 2013, which primarily reflected the impact of higher sales, partially offset by pension income in 2014 compared with pension expense in 2013 and lower severance and facility consolidation and environmental costs. Cost of sales as a percentage of sales for the third quarter of 2014 decreased to 62.5% from 64.6% in the third quarter of 2013 and reflected lower costs as a result of the cost reduction actions taken in 2013 and also reflected pension income in 2014 compared with pension expense in 2013 and lower severance and facility consolidation costs.

Certain contracts are accounted for under the percentage of completion ("POC") method and related contract cost and revenue estimates for significant contracts are generally reviewed and reassessed quarterly. The aggregate effects of these changes in estimates on contracts accounted for under the POC accounting method, in the third quarter of 2014 and 2013, were \$5.4 million and \$5.3 million of favorable operating income and \$5.6 million and \$5.2 million of unfavorable operating income, respectively.

Selling, general and administrative expenses

Selling, general and administrative expenses, including research and development and bid and proposal expense, increased by \$1.8 million in the third quarter of 2014, compared with the third quarter of 2013, and primarily reflected the impact of higher sales. Selling, general and administrative expenses for the third quarter of 2014, as a percentage of sales, decreased to 25.1%, compared with 26.2% in the third quarter of 2013. Corporate expense was \$10.6 million for the third quarter of 2014, compared with \$10.4 million for the third quarter of 2013. In the third quarter of 2014 and 2013, we recorded a total of \$3.9 million and \$3.0 million, respectively, in stock option compensation expense. Employee stock option grants are expensed evenly over the three year vesting period.

Interest Expense and Other Income and Expense

Interest expense, net of interest income, was \$4.6 million for the third quarter of 2014, compared with \$5.1 million for the third quarter of 2013. The decrease in interest expense primarily reflected the impact of lower outstanding debt

levels. Other income and expense was \$1.8 million of expense for the third quarter of 2014, compared with expense of \$0.7 million for the third quarter of 2013. The 2014 amount included accruals for legal matters of \$1.6 million.

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Income Taxes

The income tax provision is calculated using an estimated annual effective tax rate, based upon estimates of annual income, permanent items, statutory tax rates and planned tax strategies in the various jurisdictions in which we operate except that certain loss jurisdictions and discrete items, such as the resolution of uncertain tax positions, are treated separately. The Company's effective income tax rate for the third quarter of 2014 was 19.2% compared with 0.6% for the third quarter of 2013.

The third quarter of 2014 reflected \$6.1 million in net discrete tax benefits which included the remeasurement of uncertain tax positions including the expiration of statute of limitations and a favorable resolution of a tax matter. The third quarter of 2013 reflected \$11.6 million in net discrete tax benefits primarily related to the remeasurement of uncertain tax positions including expiration of statute of limitations and a favorable resolution of a tax matter.

Excluding the net discrete tax benefits in both periods, the effective tax rates would have been 28.1% and 25.2% for the third quarters of 2014 and 2013, respectively. The Company's effective tax rate for fiscal year 2014 is expected to be 28.5%, based on the projected mix of earnings before tax by jurisdiction, excluding the impact of any matters that would be treated as discrete. The increase in the effective tax rates, excluding discrete items, primarily reflected a change in the proportion of domestic and foreign income.

First nine months of 2014 compared with the first nine months of 2013

Teledyne's first nine months of 2014 sales were \$1,771.7 million, compared with sales of \$1,742.0 million for the same period of 2013, an increase of 1.7%. Net income attributable to Teledyne was \$157.5 million (\$4.13 per diluted share) for the first nine months of 2014, compared with \$130.1 million (\$3.42 per diluted share) for the first nine months of 2013, an increase of 21.1%.

Sales

The first nine months of 2014, compared with the same period in 2013, reflected higher sales in the Instrumentation segment, partially offset by lower sales in the Aerospace and Defense Electronics, Digital Imaging and the Engineered Systems segments. Incremental revenue in the first nine months of 2014 from recent acquisitions was \$40.1 million.

Operating Income

Operating income increased to \$214.6 million for the first nine months of 2014, from \$176.8 million for the same period of 2013, and reflected improved results in each business segment, despite lower sales in three business segments. Operating income reflected lower costs as a result of the cost reduction actions taken in 2013 and the impact of pension income, as well as lower severance and facility consolidation and environmental costs. Operating income in the first nine months of 2014 included \$2.0 million in severance and facility consolidation costs, compared with \$18.7 million of similar costs in the first nine months of 2013. The incremental operating income included in the results for the first nine months of 2014 from recent acquisitions was \$2.9 million which included \$1.0 million in additional intangible asset amortization.

Pension Income/Expense

The first nine months of 2014 included pension income of \$1.0 million, compared with pension expense of \$13.0 million in the first nine months of 2013. Pension expense allocated to contracts pursuant to CAS was \$10.3 million in the first nine months of 2014, compared with \$10.8 million in the first nine months of 2013. The change to pension income in 2014 from pension expense in 2013 primarily reflected the impact of using a 5.4 percent discount rate to determine the benefit obligation for the domestic plan in 2014 compared with a 4.4 percent discount rate used in 2013.

Cost of Sales

Cost of sales decreased by \$22.5 million in the first nine months of 2014, compared with the first nine months of 2013, which primarily reflected lower costs as a result of the cost reduction actions taken in 2013 and the impact of pension income, as well as lower severance and facility consolidation costs. Cost of sales as a percentage of sales for the first nine months of 2014, was 61.8%, compared with 64.2% for the first nine months of 2013 and reflected lower costs as a result of the cost reduction actions taken in 2013, the impact of pension income, as well as lower severance and facility consolidation costs.

The aggregate effects of changes in estimates on contracts accounted for under the POC accounting method, in the first nine months of 2014 and 2013 were \$16.7 million and \$14.5 million of favorable operating income and \$18.4 million and \$16.4 million of unfavorable operating income, respectively.

Selling, general and administrative expenses

Selling, general and administrative expenses, including research and development and bid and proposal expense, in total dollars were higher by \$14.4 million in the first nine months of 2014, compared with the first nine months of 2013, and primarily included higher research and development expenses. Selling, general and administrative expenses for the first nine months of 2014, as a percentage of sales, increased to 26.1%, compared with 25.7% in the first nine months of 2013 and primarily reflected the impact of higher research and development expenses. Corporate expense was \$32.6 million for the first nine months of 2014, compared with \$30.3 million for the first nine months of 2013, and primarily reflected higher compensation

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expense. In the first nine months of 2014 and 2013, we recorded a total of \$10.1 million and \$7.6 million, respectively, in stock option compensation expense.

Interest Expense and Other Income and Expense

Interest expense, net of interest income, was \$13.9 million in the first nine months of 2014, compared with \$15.6 million for the first nine months of 2013. The decrease in interest expense primarily reflected the impact of lower outstanding debt levels. Other income and expense was income of \$7.0 million for the first nine months of 2014, compared with expense of \$1.2 million for the first nine months of 2013. The 2014 amount included a net gain on legal settlements of \$7.0 million.

Income Taxes

The Company's effective income tax rate for the first nine months of 2014 was 24.6%, compared with 18.8% for the first nine months of 2013. The first nine months of 2014 included net tax benefits for discrete items of \$8.2 million compared with net tax benefits for discrete items of \$15.2 million for the first nine months of 2013. The net tax benefits in 2014 included the remeasurement of uncertain tax positions, primarily due to an expiration of statute of limitations and the favorable resolution of a tax matter. The net tax benefits in 2013 primarily related to the remeasurement of uncertain tax positions, including the expiration of statute of limitations and a favorable resolution of a tax matter. Excluding net tax benefits in both periods, the effective tax rates would have been 28.5% for the first nine months of 2014 and 28.3% for the first nine months of 2013.

Segment Results

The following table sets forth the sales and operating profit for each segment (dollars in millions):

	Third Quarter		%	Nine Months		%	
	2014	2013		Change	2014			2013	Change
Net sales:							
Instrumentation	\$280.4	\$256.6	9.3	% \$815.9	\$747.0	9.2	%
Digital Imaging	95.6	105.2	(9.1)	)% 301.2	311.9	(3.4))%
Aerospace and Defense Electronics	151.8	143.1	6.1	% 457.3	475.7	(3.9))%
Engineered Systems	73.3	66.7	9.9	% 197.3	207.4	(4.9))%
Total net sales	\$601.1	\$571.6	5.2	% \$1,771.7	\$1,742.0	1.7	%
Segment operating profit:							
Instrumentation	\$46.9	\$39.9	17.5	% \$128.2	\$117.6	9.0	%
Digital Imaging	7.9	11.5	(31.3)	)% 29.3	24.6	19.1	%
Aerospace and Defense Electronics	21.6	9.3	132.3	% 68.3	50.1	36.3	%
Engineered Systems	8.5	2.7	214.8	% 21.4	14.8	44.6	%
Segment operating profit	84.9	63.4	33.9	% 247.2	207.1	19.4	%
Corporate expense	(10.6	) (10.4	) 1.9	% (32.6	) (30.3	) 7.6	%
Operating income	74.3	53.0	40.2	% 214.6	176.8	21.4	%
Other income/(expense), net	(1.8	) (0.7	) 157.1	% 7.0	(1.2) *	
Interest expense, net	(4.6	) (5.1	) (9.8)	)% (13.9	) (15.6	) (10.9))%
Income before income taxes	67.9	47.2	43.9	% 207.7	160.0	29.8	%
Provision for income taxes	13.0	0.3	*	51.0	30.0	70.0	%
Net income	54.9	46.9	17.1	% 156.7	130.0	20.5	%
Noncontrolling interest	0.7	(0.1	) *	0.8	0.1	*	
Net income attributable to Teledyne	\$55.6	\$46.8	18.8	% \$157.5	\$130.1	21.1	%

* not meaningful

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Instrumentation

(Dollars in millions)	Third Quarter		Nine Months		
	2014	2013	2014	2013	
Sales	\$280.4	\$256.6	\$815.9	\$747.0	
Cost of sales	\$156.8	\$144.9	\$456.5	\$414.0	
Selling, general and administrative expenses	\$76.7	\$71.8	\$231.2	\$215.4	
Operating profit	\$46.9	\$39.9	\$128.2	\$117.6	
Cost of sales % of sales	55.9	% 56.5	% 56.0	% 55.5	%
Selling, general and administrative expenses % of sales	27.4	% 28.0	% 28.3	% 28.8	%
Operating profit % of sales	16.7	% 15.5	% 15.7	% 15.7	%

Third quarter of 2014 compared with the third quarter of 2013

The Instrumentation segment's third quarter 2014 sales were \$280.4 million, compared with \$256.6 million in the third quarter of 2013, an increase of 9.3%. Operating profit for the third quarter of 2014 was \$46.9 million, compared with operating profit of \$39.9 million in the third quarter of 2013, an increase of 17.5%.

The third quarter 2014 sales increase resulted from higher sales in the marine instrumentation and environmental instrumentation product lines, partially offset by lower sales of electronic test and measurement instrumentation. The higher sales of \$15.8 million for marine instrumentation primarily reflected increased sales of interconnect systems used in offshore energy production, and also included \$4.3 million in sales from the recent acquisitions. Sales for environmental instrumentation increased \$9.0 million and included \$5.9 million in sales from recent acquisitions. Sales of electronic test and measurement instrumentation decreased \$1.0 million. The increase in operating profit reflected the impact of higher sales, as well as aggregate margin improvement from businesses acquired within the last two years. The incremental operating profit included in the results for the third quarter of 2014 from recent acquisitions was \$0.4 million, which included \$0.2 million in additional intangible asset amortization expense. In 2014, we expect increased sales of marine instrumentation for subsea oil and gas production, as well as increased sales of most marine sensors and systems, partially offset by reduced sales of geophysical sensors for oil and gas exploration.

Third quarter 2014 cost of sales increased by \$11.9 million, compared with the third quarter of 2013, and primarily reflected the impact of higher sales. The decrease in the cost of sales percentage to 55.9% from 56.5% reflected the impact of product mix differences. Third quarter 2014 selling, general and administrative expenses, including research and development and bid and proposal expense, increased by \$4.9 million, compared with the third quarter of 2013, and primarily reflected the impact of higher sales. The selling, general and administrative expense percentage decreased slightly to 27.4% in the third quarter of 2014 from 28.0% in the third quarter of 2013.

First nine months of 2014 compared with the first nine months of 2013

The Instrumentation segment's first nine months of 2014 sales were \$815.9 million, compared with \$747.0 million for the first nine months of 2013, an increase of 9.2%. Operating profit for the first nine months of 2014 was \$128.2 million, compared with operating profit of \$117.6 million for the first nine months of 2013, an increase of 9.0%.

The first nine months of 2014 sales increased \$68.9 million, which resulted from higher sales in the marine instrumentation and environmental instrumentation product lines. The higher sales of \$53.8 million for marine instrumentation reflected increased sales of marine acoustic sensors and systems, as well as interconnect systems used in offshore energy production, and also included a total of \$20.2 million in incremental revenue from recent acquisitions. Sales for environmental instrumentation increased \$19.4 million and included \$5.9 million from recent acquisitions. Sales for electronic test and measurement instrumentation decreased by \$1.5 million. The increase in operating profit primarily reflected the impact of higher sales. The incremental operating profit included in the results for the first nine months of 2014 from recent acquisitions was \$3.4 million, which included \$1.0 million in additional intangible asset amortization.

The first nine months of 2014 cost of sales increased by \$42.5 million, compared with the first nine months of 2013, and primarily reflected the impact of higher sales. The increase in the cost of sales percentage primarily reflected product mix differences. The first nine months of 2014, selling, general and administrative expenses, including

research and development and bid and proposal expense, increased by \$15.8 million, compared with the first nine months of 2013, and primarily reflected the impact of higher sales. The selling, general and administrative expense percentage decreased slightly to 28.3% in the first nine months of 2014 from 28.8% in the first nine months of 2013.

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Digital Imaging

(Dollars in millions)	Third Quarter		Nine Months		
	2014	2013	2014	2013	
Sales	\$95.6	\$105.2	\$301.2	\$311.9	
Cost of sales	\$59.7	\$64.3	\$187.4	\$196.0	
Selling, general and administrative expenses	\$28.0	\$29.4	\$84.5	\$91.3	
Operating profit	\$7.9	\$11.5	\$29.3	\$24.6	
Cost of sales % of sales	62.4	% 61.2	% 62.2	% 62.8	%
Selling, general and administrative expenses % of sales	29.3	% 27.9	% 28.1	% 29.3	%
Operating profit % of sales	8.3	% 10.9	% 9.7	% 7.9	%

Third quarter of 2014 compared with the third quarter of 2013

The Digital Imaging segment's third quarter 2014 sales were \$95.6 million, compared with \$105.2 million in the third quarter of 2013, a decrease of 9.1%. Operating profit was \$7.9 million for the third quarter of 2014, compared with operating profit of \$11.5 million in the third quarter of 2013, a decrease of 31.3%.

The third quarter 2014 sales primarily reflected lower sales of infrared imaging sensors for government applications. Operating profit in 2014 reflected the impact of lower sales, lower margins for infrared imaging sensors and LIDAR systems and \$0.7 million in asset write downs.

Third quarter 2014 cost of sales decreased by \$4.6 million, compared with the third quarter of 2013 and primarily reflected the impact of lower sales. The cost of sales percentage in 2014 increased to 62.4% in the third quarter of 2014, compared with 61.2% for the third quarter of 2013 and reflected lower fixed-cost absorption from lower sales. Selling, general and administrative expenses, including research and development and bid and proposal expense, decreased to \$28.0 million in 2014, from \$29.4 million in 2013 and reflected the impact of lower sales. The increase in the selling, general and administrative expense percentage to 29.3% in the third quarter of 2014 from 27.9% in the third quarter of 2013, reflected the impact of lower sales while selling, general and administrative expense did not decrease in the same proportion.

First nine months of 2014 compared with the first nine months of 2013

The Digital Imaging segment's first nine months of 2014 sales were \$301.2 million, compared with \$311.9 million for the first nine months of 2013, a decrease of 3.4%. Operating profit was \$29.3 million for the first nine months of 2014, compared with operating profit of \$24.6 million for the first nine months of 2013, an increase of 19.1%.

The first nine months of 2014 sales decrease reflected increased sales of sensors and cameras for commercial machine vision applications, offset by lower sales of infrared imaging sensors and LIDAR systems. The increase in operating profit reflected improved margins across most product lines.

Cost of sales decreased by \$8.6 million in the first nine months of 2014, compared with the first nine months of 2013, and primarily reflected lower costs as a result of cost reduction actions taken in 2013 and a greater mix of higher gross margin sales of sensors and cameras for commercial machine vision applications. The decrease in the cost of sales percentage primarily reflected lower costs as a result of cost reduction actions taken in 2013 and a greater mix of higher gross margin commercial sales. The first nine months of 2014, selling, general and administrative expenses, decreased to \$84.5 million, compared with \$91.3 million in the first nine months of 2013, and reflected lower research and development expenses. The decrease in the selling, general and administrative expense percentage to 28.1% in the first nine months of 2014 from 29.3% in the first nine months of 2013, reflected lower expense in each major category of selling, general and administrative expense.

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Aerospace and Defense Electronics

(Dollars in millions)	Third Quarter		Nine Months		
	2014	2013	2014	2013	
Sales	\$151.8	\$143.1	\$457.3	\$475.7	
Cost of sales	\$99.7	\$102.0	\$291.9	\$332.9	
Selling, general and administrative expenses	\$30.5	\$31.8	\$97.1	\$92.7	
Operating profit	\$21.6	\$9.3	\$68.3	\$50.1	
Cost of sales % of sales	65.7	% 71.3	% 63.9	% 70.0	%
Selling, general and administrative expenses % of sales	20.1	% 22.2	% 21.2	% 19.5	%
Operating profit % of sales	14.2	% 6.5	% 14.9	% 10.5	%

Third quarter of 2014 compared with the third quarter of 2013

The Aerospace and Defense Electronics segment's third quarter 2014 sales were \$151.8 million, compared with \$143.1 million in the third quarter of 2013, an increase of 6.1%. Operating profit was \$21.6 million for the third quarter of 2014, compared with operating profit of \$9.3 million in the third quarter of 2013, an increase of 132.3%.

The third quarter 2014 sales increase reflected higher sales of \$4.6 million from avionics products and electronic relays, \$2.7 million from microwave and interconnect systems and higher sales of \$1.4 million from electronic manufacturing services products. Operating profit in the third quarter of 2014 reflected the impact of higher sales. The third quarter 2014 operating profit also reflected pension income of \$0.2 million compared with \$2.1 million of pension expense, and the third quarter of 2013 included \$3.4 million in severance and facility consolidation expenses and a \$5.3 million charge for estimated environmental liabilities.

Third quarter 2014 cost of sales decreased by \$2.3 million, compared with the third quarter of 2013, and reflected the impact of lower costs as a result of the cost reduction actions taken in 2013 and lower severance and facility consolidation and environmental expenses, and also reflected pension income in 2014 compared with pension expense for 2013. Cost of sales as a percentage of sales for the third quarter of 2014 decreased to 65.7% from 71.3% in the third quarter of 2013 and reflected the impact of lower costs as a result of the cost reduction actions taken in 2013 and also reflected pension income in 2014 compared with pension expense for 2013, and lower severance and facility consolidation and environmental expenses. Selling, general and administrative expenses, including research and development and bid and proposal expense, decreased to \$30.5 million in the third quarter of 2014, compared with \$31.8 million in the third quarter of 2013. The decrease in the selling, general and administrative expense percentage to 20.1% in the third quarter of 2014, compared with 22.2% in the third quarter of 2013 primarily reflected lower general and administrative expense.

First nine months of 2014 compared with the first nine months of 2013

The Aerospace and Defense Electronics segment's first nine months of 2014 sales were \$457.3 million, compared with \$475.7 million for the first nine months of 2013, a decrease of