

DUCOMMUN INC /DE/
Form 10-Q
October 28, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 28, 2013

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 1-8174

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

| | |
|---|--|
| Delaware (State or other jurisdiction of | 95-0693330 (I.R.S. Employer |
| incorporation or organization) | Identification No.) |
| 23301 Wilmington Avenue, Carson, California (Address of principal executive offices) | 90745-6209 (Zip Code) |
| Registrant's telephone number, including area code: (310) 513-7200 | |
| (Former name, former address and former fiscal year, if changed since last report) | |

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

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

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

Large accelerated filer Accelerated filer

Non-accelerated filer Smaller reporting company

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

As of September 28, 2013, there were outstanding 10,780,169 shares of common stock.

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DUCOMMUN INCORPORATED

FORM 10-Q

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Ducommun Incorporated
Condensed Consolidated Statements of Income
(Unaudited)

(In thousands, except per share amounts)

| | Three Months Ended | | Nine Months Ended | |
|---|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 28, 2013 | September 29, 2012 | September 28, 2013 | September 29, 2012 |
| Net Sales | \$ 181,288 | \$ 184,097 | \$ 548,675 | \$ 553,145 |
| Cost of Sales | 148,984 | 148,517 | 446,202 | 447,143 |
| Gross Profit | 32,304 | 35,580 | 102,473 | 106,002 |
| Selling, General and Administrative Expenses | 20,351 | 21,340 | 65,175 | 65,891 |
| Operating Income | 11,953 | 14,240 | 37,298 | 40,111 |
| Interest Expense | 7,403 | 8,241 | 22,668 | 24,714 |
| Income Before Taxes | 4,550 | 5,999 | 14,630 | 15,397 |
| Income Tax Expense (Benefit) | (86) | 894 | 783 | 2,395 |
| Net Income | \$ 4,636 | \$ 5,105 | \$ 13,847 | \$ 13,002 |
| Earnings Per Share | | | | |
| Basic earnings per share | \$ 0.43 | \$ 0.48 | \$ 1.30 | \$ 1.23 |
| Diluted earnings per share | \$ 0.42 | \$ 0.48 | \$ 1.28 | \$ 1.23 |
| Weighted-Average Number of Common Shares Outstanding | | | | |
| Basic | 10,722 | 10,595 | 10,657 | 10,575 |
| Diluted | 10,917 | 10,633 | 10,785 | 10,588 |

See accompanying notes to condensed consolidated financial statements.

Table of Contents**Ducommun Incorporated****Condensed Consolidated Statements of Comprehensive Income****(Unaudited)**

(In thousands)

| | Three Months Ended | | Nine Months Ended | |
|---|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 28, 2013 | September 29, 2012 | September 28, 2013 | September 29, 2012 |
| Net Income | \$ 4,636 | \$ 5,105 | \$ 13,847 | \$ 13,002 |
| Other Comprehensive Loss | | | | |
| Amortization of actuarial loss and prior service costs, net of tax benefit of \$102 and \$306 for the three and nine months of 2013, respectively | (172) | | (516) | |
| Other Comprehensive Loss | (172) | | (516) | |
| Comprehensive Income | \$ 4,464 | \$ 5,105 | \$ 13,331 | \$ 13,002 |

See accompanying notes to condensed consolidated financial statements.

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Ducommun Incorporated
Condensed Consolidated Balance Sheets
(Unaudited)

(In thousands, except share and per share data)

| | September 28, 2013 | December 31, 2012 |
|---|-----------------------|----------------------|
| Assets | | |
| Current Assets | | |
| Cash and cash equivalents | \$ 32,597 | \$ 46,537 |
| Accounts receivable, net | 92,637 | 97,300 |
| Unbilled receivables | 6,615 | 3,556 |
| Inventories | 148,524 | 148,318 |
| Production cost of contracts | 19,926 | 17,960 |
| Deferred income taxes | 7,110 | 10,459 |
| Other current assets | 16,890 | 10,441 |
| Total Current Assets | 324,299 | 334,571 |
| Property and Equipment, Net | 93,840 | 98,383 |
| Goodwill | 161,940 | 161,940 |
| Intangibles, Net | 168,188 | 176,356 |
| Other Assets | 11,779 | 13,824 |
| Total Assets | \$ 760,046 | \$ 785,074 |
| Liabilities and Shareholders Equity | | |
| Current Liabilities | | |
| Current portion of long-term debt | \$ 3,029 | \$ 3,042 |
| Accounts payable | 49,668 | 52,578 |
| Accrued liabilities | 39,320 | 52,716 |
| Total Current Liabilities | 92,017 | 108,336 |
| Long-Term Debt, Less Current Portion | 340,184 | 362,702 |
| Deferred Income Taxes | 64,504 | 67,808 |
| Other Long-Term Liabilities | 22,097 | 23,553 |
| Total Liabilities | 518,802 | 562,399 |
| Commitments and Contingencies | | |
| Shareholders Equity | | |
| Common stock \$0.01 par value; authorized 35,000,000 shares; issued 10,923,469 shares in 2013 and 10,738,065 shares in 2012 | 109 | 107 |

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| | | |
|---|-------------------|-------------------|
| Treasury stock held in treasury 143,300 shares in 2013 and 2012 | (1,924) | (1,924) |
| Additional paid-in capital | 70,679 | 66,475 |
| Retained earnings | 179,332 | 165,485 |
| Accumulated other comprehensive loss | (6,952) | (7,468) |
| Total Shareholders Equity | 241,244 | 222,675 |
| Total Liabilities and Shareholders Equity | \$ 760,046 | \$ 785,074 |

See accompanying notes to condensed consolidated financial statements.

Table of Contents**Ducommun Incorporated****Condensed Consolidated Statements of Cash Flows****(Unaudited)**

(In thousands)

| | Nine Months Ended | |
|--|-----------------------|-----------------------|
| | September 28, 2013 | September 29, 2012 |
| Cash Flows from Operating Activities | | |
| Net Income | \$ 13,847 | \$ 13,002 |
| Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities | | |
| Depreciation and amortization | 21,375 | 21,461 |
| Stock-based compensation expense | 1,711 | 1,528 |
| Deferred income tax provision (benefit) | 45 | (3,600) |
| Income tax benefit from stock-based compensation | 1,250 | 324 |
| Excess tax benefit from stock-based compensation | (217) | |
| Provision for (recovery of) doubtful accounts | (141) | 59 |
| Other | 1,434 | 2,080 |
| Changes in Assets and Liabilities | | |
| Accounts receivable (increase) decrease | 4,804 | (6,934) |
| Unbilled receivables increase | (3,059) | (241) |
| Inventories increase | (206) | (7,962) |
| Production cost of contracts increase | (3,396) | (1,473) |
| Other assets (increase) decrease | (5,974) | 6,398 |
| Accounts payable decrease | (2,910) | (3,076) |
| Accrued and other liabilities decrease | (14,069) | (10,182) |
| Net Cash Provided by Operating Activities | 14,494 | 11,384 |
| Cash Flows from Investing Activities | | |
| Purchases of property and equipment | (7,321) | (12,330) |
| Proceeds from the sales of assets | 123 | 18 |
| Net Cash Used in Investing Activities | (7,198) | (12,312) |
| Cash Flows from Financing Activities | | |
| Repayments of term loan and other debt | (22,518) | (11,464) |
| Net cash effect of exercise related to stock options | 1,246 | (186) |
| Excess tax benefit from stock-based compensation | 217 | |
| Deferred financing cost paid | (181) | |
| Net Cash Used in Financing Activities | (21,236) | (11,650) |

| | | |
|---|------------------|------------------|
| Net Decrease in Cash and Cash Equivalents | (13,940) | (12,578) |
| Cash and Cash Equivalents at Beginning of Period | 46,537 | 41,449 |
| Cash and Cash Equivalents at End of Period | \$ 32,597 | \$ 28,871 |

See accompanying notes to condensed consolidated financial statements.

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DUCOMMUN INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. Summary of Significant Accounting Policies

Basis of Presentation

The consolidated financial statements include the accounts of Ducommun Incorporated and its subsidiaries (Ducommun , the Company , we , us or our), after eliminating intercompany balances and transactions. The December 31, 2012 condensed consolidated balance sheet data was derived from audited financial statements, but does not contain all disclosures required by accounting principles generally accepted in the United States of America (GAAP).

Our significant accounting policies were described in Part II, Item 8. Note 1. Summary of Significant Accounting Policies in our Annual Report on Form 10-K for the year ended December 31, 2012. We follow the same accounting policies for interim reporting, with the exception of accounting principles adopted as of January 1, 2013, as discussed below in Recent Accounting Pronouncements. The financial information included in this Quarterly Report on Form 10-Q should be read in conjunction with our consolidated financial statements and related notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2012.

In the opinion of management, all adjustments, consisting of recurring accruals, have been made that are necessary to fairly state our condensed consolidated financial position, statements of income, comprehensive income and cash flows in accordance with GAAP for the periods covered by this Quarterly Report on Form 10-Q. The results of operations for the three and nine months ended September 28, 2013 are not necessarily indicative of the results to be expected for the full year ending December 31, 2013.

Certain prior year reclassifications have been made to conform to the current year financial statement presentation.

Use of Estimates

Certain amounts and disclosures included in the condensed consolidated financial statements required management to make estimates and judgments that affect the amounts of assets, liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities. These estimates are based on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

Table of Contents**Description of Business**

We are a global provider of engineering and manufacturing products and services primarily to the aerospace and defense industry through a wide range of products and services in the primary businesses of electronics, structures and integrated solutions. Our subsidiaries are organized into two strategic businesses, each of which is a reportable operating segment. Ducommun AeroStructures (DAS) designs, engineers and manufactures large, complex contoured aerospace structural components and assemblies and supplies composite and metal bonded structures and assemblies. Ducommun LaBarge Technologies (DLT) designs, engineers and manufactures high-reliability products used in worldwide technology-driven markets including aerospace and defense, natural resources, industrial and medical and other end-use markets. DLT 's product offerings range from prototype development to complex assemblies. Each reportable operating segment follows the same accounting principles.

Accumulated Other Comprehensive Loss

Accumulated other comprehensive loss, as reflected on the condensed consolidated balance sheets, was composed of cumulative pension and liability adjustments of \$7.0 million and \$7.5 million, net of tax, at September 28, 2013 and December 31, 2012, respectively.

Earnings per Share

Basic earnings per share are computed by dividing income available to common shareholders by the weighted-average number of common shares outstanding in each period. Diluted earnings per share are computed by dividing the sum of income available to common shareholders plus income associated with dilutive securities by the weighted-average number of common shares outstanding, plus any potential dilutive shares that could be issued if exercised or converted into common stock in each period.

The net earnings and weighted-average number of common shares outstanding used to compute earnings per share were as follows:

| | (In thousands, except per share amounts) | | | |
|--|--|-----------------------|-----------------------|-----------------------|
| | Three Months Ended | | Nine Months Ended | |
| | September 28, 2013 | September 29, 2012 | September 28, 2013 | September 29, 2012 |
| Net earnings (a) | \$ 4,636 | \$ 5,105 | \$ 13,847 | \$ 13,002 |
| Weighted-average number of common shares outstanding | | | | |
| Basic weighted-average common shares outstanding (b) | 10,722 | 10,595 | 10,657 | 10,575 |
| Dilutive potential common shares | 195 | 38 | 128 | 13 |
| Diluted weighted-average common shares outstanding (c) | 10,917 | 10,633 | 10,785 | 10,588 |
| Earnings per share | | | | |
| Basic (a/b) | \$ 0.43 | \$ 0.48 | \$ 1.30 | \$ 1.23 |

| | | | | |
|---------------|---------|---------|---------|---------|
| Diluted (a/c) | \$ 0.42 | \$ 0.48 | \$ 1.28 | \$ 1.23 |
|---------------|---------|---------|---------|---------|

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Potentially dilutive stock options and stock units to purchase common stock, as shown below, were excluded from the computation of diluted earnings per share because their inclusion would have been anti-dilutive. However, these shares may be potentially dilutive common shares in the future.

| | (In thousands) | | | |
|-------------------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| | Three Months Ended | | Nine Months Ended | |
| | September 28, 2013 | September 29, 2012 | September 28, 2013 | September 29, 2012 |
| Stock options and stock units | 219 | 1,012 | 612 | 1,015 |

Cash Equivalents

Cash equivalents consist of highly liquid instruments purchased with original maturities of three months or less. These assets are valued at cost, which approximates fair value, which we classify as Level 1. See Fair Value below.

Out of Period Adjustments

During the third quarter of 2013, we determined that approximately \$1.1 million of inventory had not been valued correctly at our DLT operating segment for periods originating in 2010 through the second quarter of 2013. The errors were attributed to the following quarters; \$0.3 million in Q2 2010, \$0.5 million in Q2 2011, \$0.1 million in Q4 2012, \$0.1 million in Q1 2013 and \$0.1 million in Q2 2013. We assessed the materiality of these errors and concluded they were immaterial to currently forecasted annual amounts and previously reported annual and interim amounts. We corrected the errors in the third quarter of 2013 and recorded a \$1.1 million charge for inventory reserves for the DLT operating segment.

During the first quarter of 2012, we determined that approximately \$0.4 million of engineering research and development costs had been capitalized in error in inventory in prior periods. We assessed the materiality of this error and concluded it was immaterial to currently reported annual and previously reported annual and interim amounts. We corrected the error in the first quarter of 2012 and did not restate our condensed consolidated financial statements for the prior annual or interim periods.

Fair Value

Assets and liabilities that are measured, recorded or disclosed at fair value on a recurring basis are categorized using the fair value hierarchy. The fair value hierarchy has three levels based on the reliability of the inputs used to determine fair value. Level 1, the highest level, refers to the values determined based on quoted prices in active markets for identical assets. Level 2 refers to fair values estimated using significant observable inputs. Level 3, the lowest level, includes fair values estimated using significant unobservable inputs.

Recent Accounting Pronouncements*New Accounting Guidance Adopted in 2013*

In February 2013, the Financial Accounting Standards Board (the FASB) issued guidance to improve the reporting of reclassifications out of accumulated other comprehensive income/loss. The new guidance requires an entity to report the effect of significant reclassifications out of accumulated other comprehensive income/loss on the respective line

items in net income if the amount being reclassified is required under GAAP to be reclassified in its entirety to net income. For other amounts that are not required under GAAP to be reclassified in their entirety to net income in the same reporting period, cross-reference to other disclosures that provide additional detail is required. Early adoption is permitted. We adopted this new guidance effective January 1, 2013. This guidance affects disclosures only.

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In January 2013, the FASB issued guidance clarifying the scope of disclosures about offsetting assets and liabilities and requires retrospective application for all periods presented. We adopted this new guidance effective January 1, 2013. The adoption of this new guidance did not have any effect on our condensed consolidated financial statements. In December 2011, the FASB issued guidance enhancing disclosure requirements about the nature of an entity's right to offset and related arrangements associated with its financial instruments and derivative instruments. The new guidance requires the disclosure of the gross amounts subject to rights of set-off, amounts offset in accordance with the accounting standards followed, and the related net exposure. The new guidance requires retrospective application for all comparable periods presented. We adopted this new guidance effective January 1, 2013. The adoption of this new guidance did not have any effect on our condensed consolidated financial statements.

New Accounting Guidance Not Yet Adopted

In July 2013, the FASB issued guidance that requires the netting of unrecognized tax benefits against a deferred tax asset for a loss or other carryforward that would apply in settlement of the uncertain tax positions. This guidance will be effective for fiscal years beginning after December 15, 2013, which will be our fiscal year 2014, with early adoption permitted. We currently expect the adoption of this guidance will reduce deferred tax assets by approximately \$2.2 million.

In February 2013, the FASB issued guidance for the recognition, measurement and disclosure of obligations resulting from joint and several liability arrangements for which the total amount of the obligation is fixed at the reporting date, except for obligations addressed within existing guidance in GAAP. The new guidance will be effective for us beginning January 1, 2014. Early adoption is permitted. We do not expect the adoption of this guidance to have a material impact on our condensed consolidated financial statements.

Note 2. Inventories

Inventories consisted of the following:

| | (In thousands) | |
|----------------------------|-----------------------|----------------------|
| | September 28, 2013 | December 31, 2012 |
| Raw materials and supplies | \$ 80,672 | \$ 84,545 |
| Work in process | 68,688 | 67,132 |
| Finished goods | 10,816 | 13,031 |
| | 160,176 | 164,708 |
| Less progress payments | 11,652 | 16,390 |
| Total | \$ 148,524 | \$ 148,318 |

Table of Contents**Note 3. Goodwill**

Goodwill was as follows:

| | (In thousands) | | |
|---------------------------------|----------------------------|-------------------------------------|--------------------------|
| | Ducommun AeroStructures | Ducommun LaBarge Technologies | Consolidated Ducommun |
| Gross goodwill | \$ 57,243 | \$ 184,970 | \$ 242,213 |
| Accumulated goodwill impairment | | (80,273) | (80,273) |
| Balance at December 31, 2012 | \$ 57,243 | \$ 104,697 | \$ 161,940 |
| Balance at September 28, 2013 | \$ 57,243 | \$ 104,697 | \$ 161,940 |

Note 4. Long-Term Debt

Long-term debt and the current period interest rates were as follows:

| | (In thousands) | |
|---|-----------------------|----------------------|
| | September 28, 2013 | December 31, 2012 |
| Senior unsecured notes (fixed 9.75%) | \$ 200,000 | \$ 200,000 |
| Senior secured term loan (floating 4.75%) | 140,125 | 162,625 |
| Promissory note (fixed 5.0%) and other debt (fixed 5.41%) | 3,088 | 3,119 |
| Total Debt | 343,213 | 365,744 |
| Less Current Portion | 3,029 | 3,042 |
| Total Long-Term Debt | \$ 340,184 | \$ 362,702 |
| Weighted-average interest rate | 7.67% | 7.82% |

We made voluntary principal prepayments of \$7.5 million each on our senior secured term loan on September 27, 2013, April 30, 2013 and March 28, 2013.

On March 28, 2013, we executed an amendment to our Credit Agreement dated June 11, 2011 (Credit Agreement) which completed a repricing of our senior secured term loan and revolving credit facility. The repricing reduced the interest rate spread on the senior secured term loan and revolving credit facility by 50 basis points and the interest rate floor by 25 basis points. In connection with this repricing, we recognized \$0.5 million of financing and legal costs which were included in selling, general and administrative expenses in the first quarter of 2013.

At September 28, 2013, we had \$58.4 million of unused borrowing capacity under the revolving credit facility, after deducting \$1.6 million for standby letters of credit.

At September 28, 2013, we were in compliance with all covenants required by the Credit Agreement. At September 28, 2013, there were no amounts outstanding that would have triggered the leverage covenant under the Credit Agreement. However, we would have been in compliance with such leverage covenant. Under the terms of the

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Credit Agreement, if, during a given fiscal quarter, (i) the sum of (a) any amounts outstanding under the revolving credit facility plus (b) the amount drawn under any letters of credit exceeds \$1.0 million; or (ii) the aggregate amount of outstanding letters of credit exceeds \$5.0 million, the revolving credit facility will be subject to a maximum total leverage ratio.

On October 18, 2013, we executed an amendment to our Credit Agreement, which increases the maximum leverage ratio, as defined, by 0.75 in all future periods.

The carrying amount of long-term debt approximates fair value, except for the senior unsecured notes for which the fair value was \$223.5 million. Fair value was estimated using Level 2 inputs, based on the terms of the related debt, recent transactions and estimates using interest rates currently available to us for debt with similar terms and remaining maturities.

Note 5. Shareholders Equity

We are authorized to issue five million shares of preferred stock. At September 28, 2013 and December 31, 2012, no preferred shares were issued or outstanding.

Note 6. Employee Benefit Plans

The components of net periodic pension expense were as follows:

| | (In thousands) | | | |
|--|-----------------------|-----------------------|-----------------------|-----------------------|
| | Three Months Ended | | Nine Months Ended | |
| | September 28, 2013 | September 29, 2012 | September 28, 2013 | September 29, 2012 |
| Service cost | \$ 211 | \$ 241 | \$ 633 | \$ 723 |
| Interest cost | 290 | 238 | 870 | 714 |
| Expected return on plan assets | (306) | (265) | (918) | (795) |
| Amortization of actuarial loss and prior service costs | 274 | 287 | 822 | 861 |
| Net periodic pension cost | \$ 469 | \$ 501 | \$ 1,407 | \$ 1,503 |

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The components of the reclassifications from accumulated other comprehensive loss to net income during the three and nine months ended September 28, 2013 were as follows:

| | (In thousands) | |
|---|--|--|
| | Three Months Ended September 28, 2013 (a) | Nine Months Ended September 28, 2013 (a) |
| Amortization of actuarial loss and prior service costs-total before tax (b) | \$ (274) | \$ (822) |
| Tax benefit | 102 | 306 |
| Net of tax | \$ (172) | \$ (516) |

(a) Amounts in parenthesis indicate reductions to net income upon reclassification from accumulated other comprehensive loss.

(b) The amount is included in the computation of net periodic pension cost.

Note 7. Indemnification

We have made guarantees and indemnities under which we may be required to make payments to a guaranteed or indemnified party, in relation to certain transactions, including revenue transactions in the ordinary course of business. In connection with certain facility leases, we have indemnified our lessors for certain claims arising from the facility or the lease. We indemnify our directors and officers to the maximum extent permitted under the laws of the State of Delaware. However, we have a directors and officers insurance policy that may reduce our exposure in certain circumstances and may enable us to recover a portion of future amounts that may be payable, if any. The duration of the guarantees and indemnities varies and, in many cases, is indefinite but subject to statute of limitations. The majority of guarantees and indemnities do not provide any limitations of the maximum potential future payments we could be obligated to make. Historically, payments related to these guarantees and indemnities have been immaterial. We estimate the fair value of our indemnification obligations as insignificant based on this history and insurance coverage and have, therefore, not recorded any liability for these guarantees and indemnities in the accompanying condensed consolidated balance sheets.

Note 8. Income Taxes

We recorded an income tax benefit of \$0.1 million (an effective tax benefit of 1.9%) in the third quarter of 2013, compared to an income tax expense of \$0.9 million (an effective tax rate of 14.9%) in the third quarter of 2012. We recorded an income tax expense of \$0.8 million (an effective tax rate of 5.4%) in the first nine months of 2013, compared to an income tax expense of \$2.4 million (an effective tax rate of 15.6%) in the comparable period of 2012.

The effective tax rate in the nine months ended September 28, 2013 included \$2.0 million of 2012 federal research and development tax credit benefits recognized in the first quarter of 2013 as a result of the American Taxpayer Relief Act of 2012, passed in January 2013. This Act includes an extension of the federal research and development tax credit for the amounts paid or incurred after December 31, 2011 and before January 1, 2014. We recognized total federal research and development tax credit benefits of \$2.5 million in the first quarter of 2013, \$0.5

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million in the second quarter of 2013, and \$0.7 million in the third quarter of 2013. We expect to recognize approximately \$0.5 million for these benefits in the fourth quarter of 2013. The effective tax rate for the three and nine months ended September 29, 2012 included no federal research and development tax credit benefits. The effective tax rate for the third quarters of both 2013 and 2012 benefitted from expiring statutes and other favorable tax adjustments. In addition, the first nine months of 2012 included a tax benefit of \$1.6 million as a result of the 2011 acquisition of LaBarge Inc., which allowed us to file state consolidated tax returns in certain states.

Our unrecognized tax benefits were \$2.5 million and \$1.7 million at September 28, 2013 and December 31, 2012, respectively. Most of these amounts, if recognized, would affect our annual income tax rate.

Note 9. Contingencies

Ducommun is a defendant in a lawsuit entitled *United States of America ex rel Taylor Smith, Jeannine Prewitt and James Ailes v. The Boeing Company and Ducommun Inc.*, filed in the United States District Court for the District of Kansas (the District Court). The lawsuit is a qui tam action brought by three former Boeing employees (Relators) against Boeing and Ducommun on behalf of the United States of America for violations of the United States False Claims Act. The lawsuit alleges that Ducommun sold unapproved parts to the Boeing Company (Boeing), which were installed by Boeing in aircraft ultimately sold to the United States Government and that Boeing and Ducommun submitted or caused to be submitted false claims for payment relating to 21 aircraft sold by Boeing to the United States Government. The lawsuit seeks damages in an amount equal to three times the amount of damages the United States Government sustained because of the defendants' actions, plus a civil penalty of \$10 thousand for each false claim made on or before September 28, 1999, and \$11 thousand for each false claim made on or after September 28, 1999, together with attorneys' fees and costs. The Relators claim that the United States Government sustained damages of \$1.6 billion (the contract purchase price of 21 aircraft) or, alternatively, \$851 million (the alleged diminished value and increased maintenance cost of the 21 aircraft). After investigating the allegations, the United States Government has declined to intervene in the lawsuit. Ducommun and Boeing have filed motions for summary judgment to dismiss the lawsuit. The motions for summary judgment are pending before the District Court. Ducommun intends to defend itself vigorously against the lawsuit. Ducommun, at this time, is unable to estimate what, if any, liability it may have in connection with the lawsuit.

DAS has been directed by California environmental agencies to investigate and take corrective action for groundwater contamination at its facilities located in El Mirage and Monrovia, California. Based on currently available information, Ducommun has established a reserve for its estimated liability for such investigation and corrective action of approximately \$1.5 million at September 28, 2013, which is reflected in other long-term liabilities on its condensed consolidated balance sheet.

DAS also faces liability as a potentially responsible party for hazardous waste disposed at landfills located in Casmalia and West Covina, California. DAS and other companies and

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government entities have entered into consent decrees with respect to these landfills with the United States Environmental Protection Agency and/or California environmental agencies under which certain investigation, remediation and maintenance activities are being performed. Based on currently available information, Ducommun preliminarily estimates that the range of its future liabilities in connection with the landfill located in West Covina, is between approximately \$0.4 million and \$3.1 million. Ducommun has established a reserve for its estimated liability, in connection with the West Covina landfill of approximately \$0.4 million at September 28, 2013, which is reflected in other long-term liabilities on its condensed consolidated balance sheet. Ducommun's ultimate liability in connection with these matters will depend upon a number of factors, including changes in existing laws and regulations, the design and cost of construction, operation and maintenance activities, and the allocation of liability among potentially responsible parties.

In the normal course of business, Ducommun and its subsidiaries are defendants in certain other litigation, claims and inquiries, including matters relating to environmental laws. In addition, Ducommun makes various commitments and incurs contingent liabilities. While it is not feasible to predict the outcome of these matters, Ducommun does not presently expect that any sum it may be required to pay in connection with these matters would have a material adverse effect on its consolidated financial position, results of operations or cash flows.

Note 10. Business Segment Information

We supply products and services primarily to the aerospace and defense industries. Our subsidiaries are organized into two strategic businesses, DAS and DLT, each of which is a reportable operating segment.

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Financial information by reportable segment was as follows:

| | (In thousands) | | | (In thousands) | | |
|---|----------------|-----------------------|-----------------------|----------------|-----------------------|-----------------------|
| | % Change | September 29, 2013 | September 29, 2012 | % Change | September 29, 2013 | September 29, 2012 |
| Net Sales | | | | | | |
| DAS | 1.4% | \$ 77,740 | \$ 76,655 | 2.9% | \$ 234,437 | \$ 227,832 |
| DLT | (3.6)% | 103,548 | 107,442 | (3.4)% | 314,238 | 325,313 |
| Total Net Sales | (1.5)% | \$ 181,288 | \$ 184,097 | (0.8)% | \$ 548,675 | \$ 553,145 |
| Segment Operating Income | | | | | | |
| DAS | | \$ 7,633 | \$ 7,410 | | \$ 23,766 | \$ 21,575 |
| DLT ⁽²⁾ | | 7,596 | 10,472 | | 26,772 | 29,260 |
| | | 15,229 | 17,882 | | 50,538 | 50,835 |
| Corporate General and Administrative Expenses ^{(1) (2) (3)} | | | | | | |
| | | (3,276) | (3,642) | | (13,240) | (10,724) |
| Total Operating Income | | \$ 11,953 | \$ 14,240 | | \$ 37,298 | \$ 40,111 |
| Depreciation and Amortization Expenses | | | | | | |
| DAS | | \$ 2,621 | \$ 2,903 | | \$ 7,386 | \$ 7,200 |
| DLT | | 4,540 | 4,710 | | 13,863 | 14,139 |
| Corporate Administration | | 41 | 42 | | 126 | 122 |
| Total Depreciation and Amortization Expenses | | \$ 7,202 | \$ 7,655 | | \$ 21,375 | \$ 21,461 |
| Capital Expenditures | | | | | | |
| DAS | | \$ 1,159 | \$ 2,074 | | \$ 4,208 | \$ 6,360 |
| DLT | | 866 | 1,472 | | 3,046 | 5,921 |
| Corporate Administration | | 43 | 21 | | 67 | 49 |
| Total Capital Expenditures | | \$ 2,068 | \$ 3,567 | | \$ 7,321 | \$ 12,330 |

(1) Includes costs not allocated to either the DLT or DAS operating segments.

(2) The nine-month period of 2012 includes merger-related transaction costs of \$0.3 million in Corporate General and Administrative Expenses and \$0.4 million in DLT resulting from a change in control provision for certain key executives and employees arising in connection with the acquisition of LaBarge Inc. in June 2011.

(3) The three- and nine-month periods of 2013 include \$0.1 million and \$1.2 million, respectively, of workers compensation insurance expenses included in gross profit and not allocated to the operating segments. The three-

and nine-month periods of 2012 include \$(0.2) million and \$0.4 million, respectively, of workers compensation insurance expenses (credits) included in gross profit and not allocated to the operating segments.

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Segment assets include assets directly identifiable with each segment. Corporate Administration assets include assets not specifically identified with a business segment, including cash.

| | (In thousands) | |
|---------------------------------------|-----------------------|----------------------|
| | September 28, 2013 | December 31, 2012 |
| Total Assets | | |
| DAS | \$ 252,476 | \$ 248,326 |
| DLT | 447,827 | 465,217 |
| Corporate Administration | 59,743 | 71,531 |
| Total Assets | \$ 760,046 | \$ 785,074 |
| Goodwill and Intangibles | | |
| DAS | \$ 65,775 | \$ 67,459 |
| DLT | 264,353 | 270,837 |
| Total Goodwill and Intangibles | \$ 330,128 | \$ 338,296 |

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**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS
OPERATIONS**

OVERVIEW

Ducommun Incorporated (Ducommun , the Company , we , us or our), through its subsidiaries, is a leading global provider of engineering and manufacturing services for high-performance products and high-cost-of-failure applications used primarily in the aerospace, defense, industrial, energy, and medical industries. Ducommun differentiates itself as a full-service provider, offering a wide range of value-added products and services in our primary businesses of electronics, structures and integrated solutions. We operate through two primary business units: Ducommun AeroStructures (DAS) and Ducommun LaBarge Technologies (DLT).

Third quarter 2013 highlights were as follows:

Net income was \$4.6 million, or \$0.42 per diluted share;

Adjusted EBITDA was \$19.2 million;

Cash flow from operations was \$7.6 million;

We made a voluntary \$7.5 million term loan principal prepayment on September 27, 2013; and

Firm backlog at the end of the third quarter was \$609 million.

Earnings before interest, taxes and depreciation and amortization (EBITDA) and Adjusted EBITDA for the three months ended September 28, 2013 were both \$19.2 million. See Non-GAAP Financial Measures below for certain information regarding EBITDA and Adjusted EBITDA, including reconciliations of EBITDA and Adjusted EBITDA to net income.

Non-GAAP Financial Measures

When viewed with our financial results prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) and accompanying reconciliations, we believe EBITDA and Adjusted EBITDA provide additional useful information to clarify and enhance the understanding of the factors and trends affecting our past performance and future prospects. We define these measures, explain how they are calculated and provide reconciliations of these measures to the most comparable GAAP measure in the tables below. EBITDA, Adjusted EBITDA and the related financial ratios, as presented in this Form 10-Q, are supplemental measures of our performance that are not required by, or presented in accordance with, GAAP. They are not a measurement of our financial performance under GAAP and should not be considered as alternatives to net income or any other performance measures derived in accordance with GAAP, or as an alternative to net cash provided by operating activities as measures of our liquidity. The presentation of these measures should not be interpreted to mean that our future results will be unaffected by unusual or nonrecurring items.

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We use EBITDA and Adjusted EBITDA non-GAAP operating performance measures internally as complementary financial measures to evaluate the performance and trends of our businesses. We present EBITDA, Adjusted EBITDA and the related financial ratios, as applicable, because we believe that measures such as these provide useful information with respect to our ability to meet our future debt service, capital expenditures, working capital requirements and overall operating performance.

EBITDA and Adjusted EBITDA have limitations as analytical tools, and you should not consider them in isolation or as substitutes for analysis of our results as reported under GAAP. Some of these limitations are:

They do not reflect our cash expenditures, future requirements for capital expenditures or contractual commitments;

They do not reflect changes in, or cash requirements for, our working capital needs;

They do not reflect the significant interest expense or the cash requirements necessary to service interest or principal payments on our debt;

Although depreciation and amortization are non-cash charges, the assets being depreciated and amortized will often have to be replaced in the future, and EBITDA and Adjusted EBITDA do not reflect any cash requirements for such replacements;

They are not adjusted for all non-cash income or expense items that are reflected in our statements of cash flows;

They do not reflect the impact on earnings of charges resulting from matters unrelated to our ongoing operations; and

Other companies in our industry may calculate EBITDA and Adjusted EBITDA differently from us, limiting their usefulness as comparative measures.

Because of these limitations, EBITDA, Adjusted EBITDA and the related financial ratios should not be considered as measures of discretionary cash available to us to invest in the growth of our business or as a measure of cash that will be available to us to meet our obligations. You should compensate for these limitations by relying primarily on our GAAP results and using EBITDA and Adjusted EBITDA only supplementally. See our condensed consolidated financial statements contained in this Form 10-Q report.

However, in spite of the above limitations, we believe that EBITDA and Adjusted EBITDA are useful to an investor in evaluating our results of operations because these measures:

Are widely used by investors to measure a company's operating performance without regard to items excluded from the calculation of such terms, which can vary substantially from company to company depending upon accounting methods and book value of assets, capital structure and the method by which assets were acquired, among other factors;

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Help investors to evaluate and compare the results of our operations from period to period by removing the effect of our capital structure from our operating performance; and

Are used by our management team for various other purposes in presentations to our Board of Directors as a basis for strategic planning and forecasting.

EBITDA and Adjusted EBITDA provide meaningful information about the operating performance of our businesses apart from amortization, merger-related expenses, as well as interest and tax expenses.

The following financial items have been added back to our net income when calculating EBITDA and Adjusted EBITDA:

Amortization expense may be useful to investors because it represents the estimated attrition of our acquired customer base and the diminishing value of product rights;

Depreciation may be useful to investors because it generally represents the wear and tear on our property and equipment used in our operations;

Merger-related expenses may be useful to investors for determining current cash flow;

Interest expense may be useful to investors for determining current cash flow; and

Income tax expense may be useful to investors because it represents the taxes which may be payable for the period and the change in deferred taxes during the period, and may reduce cash flow available for use in our business.

Reconciliations of net income to EBITDA and Adjusted EBITDA and the presentation of Adjusted EBITDA as a percentage of net sales were as follows:

| | (In thousands) | | | |
|--|-----------------------|-----------------------|-----------------------|-----------------------|
| | Three Months Ended | | Nine Months Ended | |
| | September 28, 2013 | September 29, 2012 | September 28, 2013 | September 29, 2012 |
| Net income | \$ 4,636 | \$ 5,105 | \$ 13,847 | \$ 13,002 |
| Depreciation and amortization | 7,202 | 7,654 | 21,375 | 21,461 |
| Interest expense | 7,403 | 8,241 | 22,668 | 24,714 |
| Income tax expense (benefit) | (86) | 894 | 783 | 2,395 |
| EBITDA | \$ 19,155 | \$ 21,894 | \$ 58,673 | \$ 61,572 |
| Merger-related expenses ⁽¹⁾ | | 7 | | 702 |

| | | | | |
|-----------------|-----------|-----------|-----------|-----------|
| Adjusted EBITDA | \$ 19,155 | \$ 21,901 | \$ 58,673 | \$ 62,274 |
| % of net sales | 10.6% | 11.9% | 10.7% | 11.3% |

- (1) The three- and nine-month periods of 2012 include merger-related transaction costs and a change-in-control provision for certain key executives and employees arising in connection with the acquisition of LaBarge Inc. in June 2011.

Adjusted EBITDA decreased for the three- and nine-month periods of 2013 compared to 2012 primarily due to decreased net sales, mainly in non-aerospace and defense end-use markets, while also reflecting lower gross profit dollars and higher inventory reserve charges.

Table of Contents**RESULTS OF OPERATIONS****Third Quarter and Year to Date 2013 Compared to Third Quarter and Year to Date 2012**

The following table sets forth net sales, selected financial data, the effective tax rate and diluted earnings per share:

| | (In thousands, except per share data) | | | | (In thousands, except per share data) | | | |
|---|---------------------------------------|-------------------|-----------------------|-------------------|---------------------------------------|-------------------|-----------------------|-------------------|
| | Three Months Ended | | Three Months Ended | | Nine Months Ended | | Nine Months Ended | |
| | September 28, 2013 | % of Net Sales | September 29, 2012 | % of Net Sales | September 28, 2013 | % of Net Sales | September 29, 2012 | % of Net Sales |
| Net Sales | \$ 181,288 | 100.0% | \$ 184,097 | 100.0% | \$ 548,675 | 100.0% | \$ 553,145 | 100.0% |
| Cost of Sales | 148,984 | 82.2% | 148,517 | 80.7% | 446,202 | 81.3% | 447,143 | 80.8% |
| Gross Profit | 32,304 | 17.8% | 35,580 | 19.3% | 102,473 | 18.7% | 106,002 | 19.2% |
| Selling, General and Administrative Expenses | 20,351 | 11.2% | 21,340 | 11.6% | 65,175 | 11.9% | 65,891 | 11.9% |
| Operating Income | 11,953 | 6.6% | 14,240 | 7.7% | 37,298 | 6.8% | 40,111 | 7.3% |
| Interest Expense | 7,403 | 4.1% | 8,241 | 4.5% | 22,668 | 4.1% | 24,714 | 4.5% |
| Income Before Taxes | 4,550 | 2.5% | 5,999 | 3.3% | 14,630 | 2.7% | 15,397 | 2.8% |
| Income Tax Expense (Benefit) | (86) | nm | 894 | nm | 783 | nm | 2,395 | nm |
| Net Income | \$ 4,636 | 2.6% | \$ 5,105 | 2.8% | \$ 13,847 | 2.5% | \$ 13,002 | 2.4% |
| Effective Tax Rate (Benefit) | (1.9)% | nm | 14.9% | nm | 5.4% | nm | 15.6% | nm |
| Diluted Earnings Per Share | \$ 0.42 | nm | \$ 0.48 | nm | \$ 1.28 | nm | \$ 1.23 | nm |

nm = not meaningful

Table of Contents**Net Sales by End-Use Market and Operating Segment**

Net sales by end-use market and operating segment during the three- and nine-month periods of 2013 and 2012, respectively, were as follows:

| | (In thousands) | | | | | (In thousands) | | | | |
|----------------------|--------------------|--------------------|--------------------|----------------|---------------|-------------------|--------------------|--------------------|----------------|---------------|
| | Three Months Ended | | | % of Net Sales | | Nine Months Ended | | | % of Net Sales | |
| | Change | September 28, 2013 | September 29, 2012 | 2013 | 2012 | Change | September 28, 2013 | September 29, 2012 | 2013 | 2012 |
| Consolidated | | | | | | | | | | |
| Ducommun | | | | | | | | | | |
| Military and space | | | | | | | | | | |
| Defense technologies | \$ 3,164 | \$ 63,954 | \$ 60,790 | 35.3% | 33.0% | \$ 21,889 | \$ 194,385 | \$ 172,496 | 35.4% | 31.2% |
| Defense structures | 1,269 | 35,424 | 34,155 | 19.5% | 18.6% | 537 | 99,796 | 99,259 | 18.2% | 17.9% |
| Commercial aerospace | 2,650 | 51,811 | 49,161 | 28.6% | 26.7% | 8,468 | 161,295 | 152,827 | 29.4% | 27.6% |
| Natural resources | (2,790) | 9,335 | 12,125 | 5.1% | 6.6% | (18,035) | 28,388 | 46,423 | 5.2% | 8.4% |
| Industrial | (3,764) | 12,051 | 15,815 | 6.7% | 8.6% | (14,953) | 33,593 | 48,546 | 6.1% | 8.8% |
| Medical and other | (3,338) | 8,713 | 12,051 | 4.8% | 6.5% | (2,376) | 31,218 | 33,594 | 5.7% | 6.1% |
| Total | \$ (2,809) | \$ 181,288 | \$ 184,097 | 100.0% | 100.0% | \$ (4,470) | \$ 548,675 | \$ 553,145 | 100.0% | 100.0% |
| DAS | | | | | | | | | | |
| Military and space | | | | | | | | | | |
| Defense structures | \$ 1,269 | \$ 35,424 | \$ 34,155 | 45.6% | 44.6% | \$ 537 | \$ 99,796 | \$ 99,259 | 42.6% | 43.6% |
| Commercial aerospace | (184) | 42,316 | 42,500 | 54.4% | 55.4% | 6,068 | 134,641 | 128,573 | 57.4% | 56.4% |
| Total | \$ 1,085 | \$ 77,740 | \$ 76,655 | 100.0% | 100.0% | \$ 6,605 | \$ 234,437 | \$ 227,832 | 100.0% | 100.0% |
| DLT | | | | | | | | | | |
| Military and space | | | | | | | | | | |
| Defense technologies | \$ 3,164 | \$ 63,954 | \$ 60,790 | 61.8% | 56.6% | \$ 21,889 | \$ 194,385 | \$ 172,496 | 61.9% | 53.0% |
| Commercial aerospace | 2,834 | 9,495 | 6,661 | 9.2% | 6.2% | 2,400 | 26,654 | 24,254 | 8.5% | 7.5% |
| | (2,790) | 9,335 | 12,125 | 9.0% | 11.3% | (18,035) | 28,388 | 46,423 | 9.0% | 14.3% |

| | | | | | | | | | | |
|-------------------|------------|------------|------------|--------|--------|-------------|------------|------------|--------|--------|
| Natural resources | | | | | | | | | | |
| Industrial | (3,764) | 12,051 | 15,815 | 11.6% | 14.7% | (14,953) | 33,593 | 48,546 | 10.7% | 14.9% |
| Medical and other | (3,338) | 8,713 | 12,051 | 8.4% | 11.2% | (2,376) | 31,218 | 33,594 | 9.9% | 10.3% |
| Total | \$ (3,894) | \$ 103,548 | \$ 107,442 | 100.0% | 100.0% | \$ (11,075) | \$ 314,238 | \$ 325,313 | 100.0% | 100.0% |

The net sales for the three- and nine-month periods of 2013 reflected growth in the aerospace and defense end-use markets, which were more than offset by lower sales in the non-aerospace and defense end-use markets.

Net Sales to Major Customers

Boeing and Raytheon each exceeded ten percent of net sales for the third quarter of 2013. Net sales to Boeing and Raytheon and the related accounts receivable are diversified over a number of different commercial, military and space programs and were made by both operating segments. Net sales to our top ten customers, including Boeing and Raytheon, represented the following percentages of total net sales:

| | Three Months Ended | | Nine Months Ended | |
|-------------------|--------------------|--------------------|--------------------|--------------------|
| | September 28, 2013 | September 29, 2012 | September 28, 2013 | September 29, 2012 |
| Boeing | 19.1% | 16.9% | 17.8% | 16.2% |
| Raytheon | 10.1% | 7.2% | 9.7% | 6.6% |
| Top ten customers | 59.6% | 54.3% | 57.3% | 54.3% |

Boeing and Raytheon represented the following percentages of total accounts receivable:

| | September 28, 2013 | December 31, 2012 |
|----------|--------------------|-------------------|
| Boeing | 15.0% | 12.4% |
| Raytheon | 9.0% | 10.4% |

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Gross Profit

Gross profit dollars decreased for the three- and nine-month periods of 2013 due to lower net sales and a \$1.1 million inventory reserve charge, as discussed below. Gross profit margins as a percentage of net sales decreased for both the three- and nine-month periods of 2013 due to unfavorable product mix and the impact of the lower net sales in the non-aerospace and defense end use markets and the inventory reserve charge.

During the third quarter of 2013, we determined that approximately \$1.1 million of inventory relating to prior periods had not been valued correctly at our DLT operating segment. We corrected these errors in the third quarter of 2013 and recorded a \$1.1 million charge for inventory reserves for the DLT operating segment. This charge reduced the third quarter of 2013 gross margins by 60 basis points and the first nine months of 2013 gross margins by 20 basis points.

Selling, General and Administrative Expenses

The SG&A expenses for the third quarter of 2013 decreased primarily due to lower accrued compensation and benefits costs. Year-to-date 2013 SG&A expenses decreased due to lower accrued compensation and benefits costs and lower intangible asset amortization, partially offset by a charge of \$0.5 million related to the debt repricing and professional fees. Year-to-date 2012 SG&A expenses included a charge of \$0.4 million for engineering research and development cost that were capitalized in error in inventory in prior periods.

Interest Expense

Interest expense decreased in both the three- and nine-month periods of 2013 mainly due to lower outstanding debt balances and a lower interest rate on the term loan beginning in April 2013.

Income Tax Expense

We recorded an income tax benefit of \$0.1 million (an effective tax benefit of 1.9%) in the third quarter of 2013, compared to an income tax expense of \$0.9 million (an effective tax rate of 14.9%) in the third quarter of 2012. We recorded an income tax expense of \$0.8 million (an effective tax rate of 5.4%) in the first nine months of 2013, compared to an income tax expense of \$2.4 million (an effective tax rate of 15.6%) in the comparable period of 2012.

The effective tax rate in the nine months ended September 28, 2013 included \$2.0 million of 2012 federal research and development tax credit benefits recognized in the first quarter of 2013 as a result of the American Taxpayer Relief Act of 2012, passed in January 2013. This Act includes an extension of the federal research and development tax credit for the amounts paid or incurred after December 31, 2011 and before January 1, 2014. We recognized total federal research and development tax credit benefits of \$2.5 million in the first quarter of 2013, \$0.5 million in the second quarter of 2013, and \$0.7 million in the third quarter of 2013. We expect to recognize approximately \$0.5 million for these benefits in the fourth quarter of 2013. The effective tax rate for the three and nine months ended September 29, 2012 included no federal research and development tax credit benefits. The effective tax rate for the third quarters of both 2013 and 2012 benefitted from expiring statutes and other favorable tax adjustments. In addition, the first nine months of 2012 included a tax benefit of \$1.6 million as a result of the 2011 acquisition of LaBarge Inc., which allowed us to file state consolidated tax returns in certain states.

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Net Income and Diluted Earnings per Share

Net income and earnings per diluted share for the third quarter of 2013 were \$4.6 million, or \$0.42 per diluted share, compared to \$5.1 million, or \$0.48 per diluted share, in the third quarter of 2012. Diluted earnings per share for the three-month period of 2013 included a federal research and development tax benefit of \$0.7 million while the 2012 period included no such benefit. Diluted earnings per share for the third quarters of both 2013 and 2012 included tax benefits from expiring statutes and other favorable tax adjustments.

Net income and earnings per diluted share for the nine-month period of 2013 were \$13.8 million, or \$1.28 per diluted share, compared to \$13.0 million, or \$1.23 per diluted share, in the comparable period of 2012. Diluted earnings per share for the nine-month period of 2013 also included a federal research and development tax benefit of \$3.7 million while the 2012 period included no such benefit. Diluted earnings per share for the nine-month period of 2012 included a state tax benefit of \$1.6 million. Diluted earnings per share for the nine-month periods of both 2013 and 2012 included tax benefits from expiring statutes and other favorable tax adjustments.

Business Segment Performance

We report our financial performance based on the following two reportable segments; Ducommun AeroStructures (DAS) and Ducommun LaBarge Technologies (DLT). The results of operations differ between our reportable operating segments due to differences in competitors, customers, extent of proprietary deliverables and performance.

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The following table summarizes our business segment performance for the third quarters and first nine months of 2013 and 2012:

| | (In thousands) Three Months Ended | | | | | (In thousands) Nine Months Ended | | | | |
|---|--------------------------------------|----------------|----------------|---------------------------|---------------------------|-------------------------------------|----------------|----------------|---------------------------|---------------------------|
| | % Change | September 2013 | September 2012 | % of Net Sales 2013 | % of Net Sales 2012 | % Change | September 2013 | September 2012 | % of Net Sales 2013 | % of Net Sales 2012 |
| Net Sales | | | | | | | | | | |
| DAS | 1.4% | \$ 77,740 | \$ 76,655 | 42.9% | 41.6% | 2.9% | \$ 234,437 | \$ 227,832 | 42.7% | 41.2% |
| DLT | (3.6)% | 103,548 | 107,442 | 57.1% | 58.4% | (3.4)% | 314,238 | 325,313 | 57.3% | 58.8% |
| Total Net Sales | (1.5)% | \$ 181,288 | \$ 184,097 | 100.0% | 100.0% | (0.8)% | \$ 548,675 | \$ 553,145 | 100.0% | 100.0% |
| Segment Operating Income | | | | | | | | | | |
| DAS | | \$ 7,633 | \$ 7,410 | 9.8% | 9.7% | | \$ 23,766 | \$ 21,575 | 10.1% | 9.5% |
| DLT ⁽²⁾ | | 7,596 | 10,472 | 7.3% | 9.7% | | 26,772 | 29,260 | 8.5% | 9.0% |
| | | 15,229 | 17,882 | | | | 50,538 | 50,835 | | |
| Corporate General and Administrative Expenses ^{(1) (2) (3)} | | | | | | | | | | |
| | | (3,276) | (3,642) | (1.8)% | (2.0)% | | (13,240) | (10,724) | (2.4)% | (1.9)% |
| Total Operating Income | | \$ 11,953 | \$ 14,240 | 6.6% | 7.7% | | \$ 37,298 | \$ 40,111 | 6.8% | 7.3% |
| EBITDA ⁽¹⁾ | | | | | | | | | | |
| DAS | | | | | | | | | | |
| Operating Income | | \$ 7,633 | \$ 7,410 | | | | \$ 23,766 | \$ 21,575 | | |
| Depreciation and Amortization | | 2,621 | 2,903 | | | | 7,386 | 7,200 | | |
| | | 10,254 | 10,313 | 13.2% | 13.5% | | 31,152 | 28,775 | 13.3% | 12.6% |
| DLT | | | | | | | | | | |
| Operating Income | | 7,596 | 10,472 | | | | 26,772 | 29,260 | | |
| Depreciation and Amortization | | 4,540 | 4,710 | | | | 13,863 | 14,139 | | |

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| | | | | | | | | |
|---|-----------|-----------|-------|-------|-----------|-----------|-------|-------|
| | 12,136 | 15,182 | 11.7% | 14.1% | 40,635 | 43,399 | 12.9% | 13.3% |
| Corporate General and Administrative Expenses | | | | | | | | |
| Operating Loss | (3,276) | (3,642) | | | (13,240) | (10,724) | | |
| Depreciation and Amortization | 41 | 42 | | | 126 | 122 | | |
| | (3,235) | (3,600) | | | (13,114) | (10,602) | | |
| EBITDA | \$ 19,155 | \$ 21,895 | | | \$ 58,673 | \$ 61,572 | | |
| Adjusted EBITDA | | | | | | | | |
| Merger-related expenses ⁽²⁾ | \$ | \$ 7 | | | \$ | \$ 702 | | |
| Adjusted EBITDA | \$ 19,155 | \$ 21,902 | 10.6% | 11.9% | \$ 58,673 | \$ 62,274 | 10.7% | 11.3% |
| Capital Expenditures | | | | | | | | |
| DAS | \$ 1,159 | \$ 2,074 | | | \$ 4,208 | \$ 6,360 | | |
| DLT | 866 | 1,472 | | | 3,046 | 5,921 | | |
| Corporate Administration | 43 | 21 | | | 67 | 49 | | |
| Total Capital Expenditures | \$ 2,068 | \$ 3,567 | | | \$ 7,321 | \$ 12,330 | | |

(1) Includes costs not allocated to either the DLT or DAS operating segments.

(2) The nine-month period of 2012 includes merger-related transaction costs of \$0.3 million in Corporate General and Administrative Expenses and \$0.4 million in DLT resulting from a change in control provision for key certain executives and employees arising in connection with the acquisition of LaBarge Inc. in June 2011.

(3) The three- and nine-month periods of 2013 include \$0.1 million and \$1.2 million, respectively, of workers compensation insurance expenses included in gross profit and not allocated to the operating segments. The three- and nine-month periods of 2012 include \$(0.2) million and \$0.4 million, respectively, of workers compensation insurance expenses (credits) included in gross profit and not allocated to the operating segments.

Ducommun AeroStructures (DAS)

DAS net sales in the three-month period of 2013 increased 1.4% due to higher net sales of large commercial aircraft products, and slightly higher net sales of military aircraft, partially offset by lower sales of commercial helicopter products. DAS net sales for the nine-month period of 2013 increased 2.9% due to higher net sales of large commercial aircraft products, partially offset by lower net sales of commercial helicopter products.

The DAS segment operating income and EBITDA increased in the three-month period of 2013, reflecting higher operating margin from improved product mix. The DAS segment operating income and EBITDA for the nine-month

period of 2013 also reflect improved operating efficiencies.

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Ducommun LaBarge Technologies (DLT)

DLT's net sales in the three-month period of 2013 decreased 3.6%. The year-over-year decline reflects a 24.7% decrease in non-aerospace and defense revenue, partially offset by an 8.9% increase in defense electronics and commercial aerospace revenue. Net sales for the nine-month period of 2013 decreased 3.4%. The lower revenue reflects a 27.5% decline in non-aerospace and defense sales, partially offset by a 12.3% increase in defense electronics and commercial aerospace revenue.

DLT's segment operating income and EBITDA decreased in the three-month period of 2013 primarily due to lower operating margin from reduced sales and a \$1.1 million charge for inventory reserves. In addition, for the nine-month period of 2013, lower operating income and EBITDA were partially offset by the realization of cost synergies achieved during the latter part of 2012 following the LaBarge acquisition.

Corporate General and Administrative (CG&A)

The CG&A expenses decreased in the third quarter 2013 due to lower accrued compensation and benefits costs. In addition, the CG&A expenses for the first nine months of 2013 increased primarily due to a workers' compensation insurance payroll audit charge of \$0.6 million and \$0.5 million related to our debt repricing transaction and professional fees, partially offset by lower accrued compensation and benefits costs.

Table of Contents**Backlog**

Backlog is subject to delivery delays or program cancellations, which are beyond our control. Backlog is affected by timing differences in the placement of customer orders and tends to be concentrated in several programs to a greater extent than our net sales. Backlog in non-aerospace and defense markets tends to be of a shorter duration and is generally fulfilled within a three-month period. As a result of these factors, trends in our overall level of backlog may not be indicative of trends in our future net sales. Approximately \$152 million of total backlog is expected to be delivered during the remainder of 2013.

| | | (In thousands) | |
|-------------------------------------|--------------------|-----------------------|----------------------|
| | Change | September 28, 2013 | December 31, 2012 |
| <u>Consolidated Ducommun</u> | | | |
| Military and space | | | |
| Defense technologies | \$ (20,070) | \$ 233,349 | \$ 253,419 |
| Defense structures | (4,565) | 111,908 | 116,473 |
| Commercial aerospace | (20,740) | 208,811 | 229,551 |
| Natural resources | (7,822) | 16,474 | 24,296 |
| Industrial | (2,200) | 14,787 | 16,987 |
| Medical and other | 7,911 | 23,786 | 15,875 |
| Total | \$ (47,486) | \$ 609,115 | \$ 656,601 |
| <u>DAS</u> | | | |
| Military and space | | | |
| Defense structures | \$ (4,565) | \$ 111,908 | \$ 116,473 |
| Commercial aerospace | (22,323) | 181,302 | 203,625 |
| Total | \$ (26,888) | \$ 293,210 | \$ 320,098 |
| <u>DLT</u> | | | |
| Military and space | | | |
| Defense technologies | \$ (20,070) | \$ 233,349 | \$ 253,419 |
| Commercial aerospace | 1,583 | 27,509 | 25,926 |
| Natural resources | (7,822) | 16,474 | 24,296 |
| Industrial | (2,200) | 14,787 | 16,987 |
| Medical and other | 7,911 | 23,786 | 15,875 |
| Total | \$ (20,598) | \$ 315,905 | \$ 336,503 |

Table of Contents**LIQUIDITY AND CAPITAL RESOURCES****Available Liquidity**

| | (In millions) | |
|---|-----------------------|----------------------|
| | September 28, 2013 | December 31, 2012 |
| Total debt, including long-term portion | \$ 343.2 | \$ 365.7 |
| Weighted-average interest rate on debt | 7.67% | 7.82% |
| Term loan interest rate | 4.75% | 5.50% |
| Cash and cash equivalents | \$ 32.6 | \$ 46.5 |
| Unused revolving credit facility | \$ 58.4 | \$ 58.4 |

In the third quarter of 2013, we made a voluntary principal prepayment of \$7.5 million on our term loan, bringing the total such payments in 2013 to \$22.5 million. We expect to pay down up to \$30 million on the term loan in 2013.

The revolving credit facility and term loan covenants require EBITDA of more than \$50.0 million and a maximum leverage ratio under certain circumstances, as well as annual limitations on capital expenditures and limitations on future disposition of property, investments, acquisitions, repurchase of stock, dividends, and outside indebtedness. At September 28, 2013, we were in compliance with all covenants. At September 28, 2013, there were no amounts outstanding that would have triggered the leverage ratio covenant.

On October 18, 2013, we executed an amendment to our Credit Agreement dated June 11, 2011, which increases the maximum leverage ratio, as defined, by 0.75 in all future periods.

We expect to spend a total of approximately \$11 million in 2013, compared to \$16 million in 2012, for capital expenditures mainly for investment in tooling to support new contract awards at DAS and DLT, financed by cash generated from operations.

We continue to depend on operating cash flow and the availability of our revolving credit facility to provide short-term liquidity. Cash generated from operations and bank borrowing capacity is expected to provide sufficient liquidity to meet our obligations during the next twelve months.

Cash Flow Summary

Net cash provided by operating activities for the first nine months of 2013 and 2012 was \$14.5 million and \$11.4 million, respectively. The higher cash provided by operating activities in the first nine months of 2013 reflects improved working capital management, partially offset by utilization in 2012 of income tax prepayments from 2011.

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Net cash used in investing activities of \$7.2 million for the first nine months of 2013 included capital expenditures, principally to support new contract awards at DAS and DLT.

Net cash used in financing activities for the first nine months of 2013 of \$21.2 million included \$22.5 million of voluntary principal prepayments on our term loan, offset by \$1.2 million from stock option exercises.

Off-Balance Sheet Arrangements

Our off-balance sheet arrangements consist of operating leases and indemnities.

Recent Accounting Pronouncements

For a discussion of new accounting guidance affecting Ducommun, see Ducommun Incorporated and Subsidiaries Notes to Condensed Consolidated Financial Statements Note 1. Summary of Significant Accounting Policies Recent Accounting Pronouncements.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our main market risk exposure relates to changes in U.S. interest rates on our outstanding long-term debt that is subject to variable interest rates. At September 28, 2013, we had borrowings of \$140.1 million under our term loan, with an interest rate of 4.75%.

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

The Company's chief executive officer and chief financial officer have concluded, based on an evaluation of the Company's disclosure controls and procedures (as defined in the Securities Exchange Act of 1934 Rules 13a-15(e) and 15d-15(e)), that such disclosure controls and procedures were effective as of the end of the period covered by this report.

Internal Control Over Financial Reporting

There has been no change in the Company's internal control over financial reporting during the three months ended September 28, 2013 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

See Item 3 of our Annual Report on Form 10-K for the year ended December 31, 2012 for information on legal proceedings.

ITEM 1A. RISK FACTORS

See Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2012 for a discussion of risk factors.

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ITEM 6. EXHIBITS

| | |
|---------|--|
| 31.1 | Certification of Principal Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 31.2 | Certification of Principal Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 32 | Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |
| 101.INS | XBRL Instance Document |
| 101.SCH | XBRL Taxonomy Extension Schema |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase |

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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.

DUCOMMUN INCORPORATED
(Registrant)

By: /s/ Joseph P. Bellino
Joseph P. Bellino
Vice President, Treasurer and Chief
Financial Officer
(Principal Financial Officer)

By: /s/ Douglas L. Groves
Douglas L. Groves
Vice President, Controller and Chief
Accounting Officer
(Principal Accounting Officer)

Date: October 28, 2013