



Kratos Reports First Quarter 2019 Financial Results

May 8, 2019

Provides Second Quarter Financial Guidance and Reaffirms Previously Provided Full Year 2019 Guidance

SAN DIEGO, May 08, 2019 (GLOBE NEWSWIRE) -- Kratos Defense & Security Solutions, Inc. (Nasdaq:KTOS), a leading National Security Solutions provider, today reported its first quarter 2019 financial results. For the first quarter 2019, Kratos reported Revenues of \$160.4 million, Adjusted EBITDA of \$17.5 million, or 10.9 percent, a 27.7 percent increase over the first quarter of 2018, Operating Income of \$8.2 million, a 17.1 percent increase over the first quarter of 2018, Cash Flow from Operations of \$16.0 million, and a Free Cash Flow from Operations of \$12.0 million after capital expenditures of \$4.0 million. For the first quarter 2019, the Company reported Adjusted EPS* of \$0.08, a 60.0 percent increase over the first quarter of 2018, Net income of \$3.1 million and GAAP EPS of \$0.03, a 250.0 percent increase over a first quarter 2018 GAAP EPS loss of \$0.02. Included in the first quarter 2019 Net income are acquisition costs of \$1.2 million related to the recently closed FTT acquisition.

First quarter 2019 revenues increased \$17.4 million over first quarter of 2018 revenues of \$143.0 million, or 12.2 percent. Included in first quarter 2019 revenues was approximately \$4.2 million generated from recently acquired FTT. Excluding the impact of FTT, Kratos revenues increased organically 9.2 percent year-over-year.

For the first quarter of 2019, Kratos' Government Solutions Division (KGS) generated Revenues of \$125.5 million, Adjusted EBITDA of \$15.5 million and Operating Income of \$11.4 million, compared to revenues of \$115.2 million, Adjusted EBITDA of \$12.0 million and Operating Income of \$7.9 million for the first quarter of 2018. For the first quarter of 2019, Kratos' Unmanned Systems Division (KUSD) generated Revenues of \$34.9 million, Adjusted EBITDA of \$2.0 million and Operating Income of \$0.6 million, compared to revenues of \$27.8 million, Adjusted EBITDA of \$1.7 million and Operating Income of \$0.8 million in the first quarter of 2018.

For the first quarter of 2019, Kratos reported bookings of \$139.2 million and a book-to-bill ratio of 0.9 to 1.0, with backlog at March 31, 2019 of \$620.2 million, and a last twelve months ending March 31, 2019 book-to-bill ratio of 1.1 to 1. In the first quarter, Kratos' bid and proposal pipeline increased by \$400 million, up to approximately \$7.2 billion, at March 31, 2019.

Eric DeMarco, Kratos' President and CEO, said, "Every Kratos business unit exceeded its financial forecast in the first quarter, with the Company reporting increased revenues, margins, profitability and cash flow. Kratos' Unmanned Systems business had a very successful first quarter, including the initial flight of the XQ-58A Valkyrie and a 1.7 to 1.0 book to bill ratio. Since the first Valkyrie flight, potential customer interest in Kratos' affordable, high performance unmanned aerial drone systems has increased significantly, and we are more confident than ever that we will successfully achieve our strategic objective of being the leader in this expected to be large and fast growing tactical UAS area class. Additionally, Kratos' target drone business continues to ramp, driven by the ongoing recapitalization of strategic weapon systems by the U.S. and its allies, providing good visibility to expected future organic revenue, profit and cash flow growth."

Mr. DeMarco continued, "Kratos' space and satellite command, control, communications and space situational awareness business, our Company's largest, also had a strong first quarter, including a favorable overall mix, and the 2020 DoD budget space funding request increase of approximately 20 percent provides confidence in our long term organic growth forecast. Additionally, Kratos' C5ISR and Microwave Electronics product business, which supports radar, missile, electronic warfare and missile defense systems, including Patriot, THAAD and Iron Dome started the year well, as did our training systems and solutions business which supports operational readiness."

Mr. DeMarco concluded, "We are confident that Kratos' strategy of building an intellectual property focused technology Company that rapidly develops, demonstrates and fields affordable products and systems is a true differentiating model. Kratos is aligned with the U.S. National Defense Strategy and DoD funding priority areas. We believe that our recent awards, new and increasing production programs, under contract tactical unmanned aerial system development programs and increased bid and proposal pipeline are representative of the strength of our business plan, providing a solid foundation for the strong organic growth trajectory we are forecasting."

Financial Guidance

Kratos is providing second quarter 2019 financial guidance of Revenues of \$175 to \$185 million, and Adjusted EBITDA of \$16 to \$18 million, and reaffirming full year 2019 financial guidance of Revenues of \$720 to \$760 million, reflecting organic growth of approximately 12.5 percent, and Adjusted EBITDA of \$71 to \$77 million.

The Company is reaffirming full year 2019 cash flow from operations guidance of \$40 to \$50 million, capital expenditures of \$28 to \$30 million, and free cash flow guidance of \$10 to \$20 million, plus the expected final cash receipt of the retained working capital of the Company's divested PSS business of approximately \$4 to \$6 million. Capital expenditures are expected to continue to be elevated in 2019, reflecting expected outlays associated with manufacturing equipment for the Company's new drone facility in Oklahoma and equipment for a new secured facility of approximately \$6 to \$8 million and approximately \$4 to \$6 million related to

the planned manufacture of company owned aerial target drones in preparation of fulfilling expected customer requirements.

Management will discuss the Company's first quarter 2019 financial results, as well as its second quarter and full year 2019 guidance on a conference call beginning at 2:00 p.m. Pacific (5:00 p.m. Eastern) today. Analysts and institutional investors may participate in the conference call by dialing (866) 393-0674, and referencing the call by ID number 1479806. The general public may access the conference call by dialing (877) 344-3935 or on the day of the event by visiting www.kratosdefense.com for a simultaneous webcast. A replay of the webcast will be available on the Kratos web site approximately two hours after the conclusion of the conference call.

About Kratos Defense & Security Solutions

Kratos Defense & Security Solutions, Inc. (NASDAQ:KTOS) develops and fields transformative, affordable technology, platforms and systems for United States National Security related customers, allies and commercial enterprises. Kratos is changing the way breakthrough technologies for these industries are rapidly brought to market through proven commercial and venture capital backed approaches, including proactive research and streamlined development processes. Kratos specializes in unmanned systems, satellite communications, cyber security/warfare, microwave electronics, missile defense, hypersonic systems, training and combat systems. For more information go to www.kratosdefense.com.

Notice Regarding Forward-Looking Statements

This news release contains certain forward-looking statements that involve risks and uncertainties, including, without limitation, express or implied statements concerning the Company's expectations regarding its future financial performance, including the Company's expectations for its second quarter and full year 2019 revenue and Adjusted EBITDA, full year 2019 capital expenditures and ability to generate positive cash flow from operations and positive free cash flow in 2019, the timing and amount of the Company's receipt of retained working capital from the Company's divested PSS business, the Company's ability to achieve projected growth in certain of the Company's business units and the expected timing of such growth, the Company's expectation of ramp on projects, timing associated with bringing certain contracts back on the planned run rate, the Company's bid and proposal pipeline, demand for its products and services, including the Company's ability to successfully compete in the tactical unmanned aerial system area and expected new customer awards, performance of key contracts and programs, including the timing of production and demonstration related to certain of the Company's contracts and product offerings, the impact of the Company's restructuring efforts and cost reduction measures, including its ability to improve profitability and cash flow in certain business units as a result of these actions, benefits to be realized from the Company's net operating loss carry forwards, the availability and timing of government funding for the Company's offerings, including the strength of the future funding environment, timing of LRIP related to the Company's unmanned aerial target system offerings, as well as the level of recurring revenues expected to be generated by these programs once they achieve full rate production, and market and industry developments, including projected growth. Such statements are only predictions, and the Company's actual results may differ materially from the results expressed or implied by these statements. Investors are cautioned not to place undue reliance on any such forward-looking statements. All such forward-looking statements speak only as of the date they are made, and the Company undertakes no obligation to update or revise these statements, whether as a result of new information, future events or otherwise. Factors that may cause the Company's results to differ include, but are not limited to: risks to our business and financial results related to the reductions and other spending constraints imposed on the U.S. Government and our other customers, including as a result of sequestration and extended continuing resolutions, the Federal budget deficit and Federal government shut-downs; risks of adverse regulatory action or litigation; risks associated with debt leverage and cost savings and cash flow improvements expected as a result of the refinancing of our Senior Notes; risks that our cost-cutting initiatives will not provide the anticipated benefits; risks that changes, cutbacks or delays in spending by the U.S. DoD may occur, which could cause delays or cancellations of key government contracts; risks of delays to or the cancellation of our projects as a result of protest actions submitted by our competitors; risks that changes may occur in Federal government (or other applicable) procurement laws, regulations, policies and budgets; risks of the availability of government funding for the Company's products and services due to performance, cost growth, or other factors, changes in government and customer priorities and requirements (including cost-cutting initiatives, the potential deferral of awards, terminations or reduction of expenditures to respond to the priorities of Congress and the Administration, or budgetary cuts resulting from Congressional committee recommendations or automatic sequestration under the Budget Control Act of 2011, as amended); risks of increases in the Federal government initiatives related to in-sourcing; risks related to security breaches, including cyber security attacks and threats or other significant disruptions of our information systems, facilities and infrastructures; risks related to our compliance with applicable contracting and procurement laws, regulations and standards; risks relating to contract performance; risks related to failure of our products or services; risks associated with our subcontractors' or suppliers' failure to perform their contractual obligations, including the appearance of counterfeit or corrupt parts in our products; changes in the competitive environment (including as a result of bid protests); failure to successfully integrate acquired operations and competition in the marketplace, which could reduce revenues and profit margins; risks that potential future goodwill impairments will adversely affect our operating results; risks that anticipated tax benefits will not be realized in accordance with our expectations; risks that a change in ownership of our stock could cause further limitation to the future utilization of our net operating losses; risks that the current economic environment will adversely impact our business; and risks related to natural disasters or severe weather. These and other risk factors are more fully discussed in the Company's Annual Report on Form 10-K for the period ended December 30, 2018, and in our other filings made with the Securities and Exchange Commission.

Note Regarding Use of Non-GAAP Financial Measures

This news release contains non-GAAP financial measures, including Adjusted income (loss) per share (computed using income (loss) from continuing operations before income taxes, excluding amortization of intangible assets, and capitalized contract and development costs, stock compensation expense, acquisition and restructuring related items and other, which includes but is not

limited to legal related items and foreign transaction gains and losses, less the estimated tax cash payments) and Adjusted EBITDA (which includes net income attributable to noncontrolling interest and excludes, among other things, losses and gains from discontinued operations, restructuring and transaction related items, stock compensation expense, foreign transaction gains and losses, and the associated margin rates). Additional non-GAAP financial measures include Free Cash Flow from Operations and Adjusted EBITDA related to our KUSD and KGS businesses. Kratos believes this information is useful to investors because it provides a basis for measuring the Company's available capital resources, the actual and forecasted operating performance of the Company's business and the Company's cash flow, excluding extraordinary items and non-cash items that would normally be included in the most directly comparable measures calculated and presented in accordance with GAAP. The Company's management uses these non-GAAP financial measures along with the most directly comparable GAAP financial measures in evaluating the Company's actual and forecasted operating performance, capital resources and cash flow. Non-GAAP financial measures should not be considered in isolation from, or as a substitute for, financial information presented in compliance with GAAP, and investors should carefully evaluate the Company's financial results calculated in accordance with GAAP and reconciliations to those financial statements. In addition, non-GAAP financial measures as reported by the Company may not be comparable to similarly titled amounts reported by other companies. As appropriate, the most directly comparable GAAP financial measures and information reconciling these non-GAAP financial measures to the Company's financial results prepared in accordance with GAAP are included in this news release.

*Adjusted earnings per share (Adjusted EPS) excludes loss from discontinued operations, non-cash amortization expense, as the Company has historically been acquisitive, non-cash stock compensation costs, foreign transaction gains and losses, certain non-recurring items such as acquisition and restructuring related items and other, and includes cash actually expected to be paid for income taxes on continuing operations, reflecting the benefit of the Company's net operating loss carry forwards of over \$300 million. Kratos believes that reporting adjusted earnings per share is a meaningful metric to present the Company's financial results.

Kratos Defense & Security Solutions, Inc.
Unaudited Condensed Consolidated Statements of Operations
(in millions, except per share data)

(in millions, except per share data)

| | Three Months Ended | |
|---|--------------------|------------------|
| | March 31, 2019 | April 1, 2018 |
| Service revenues | \$ 62.6 | \$ 46.0 |
| Product sales | 97.8 | 97.0 |
| Total revenues | <u>160.4</u> | <u>143.0</u> |
| Cost of service revenues | 42.0 | 32.9 |
| Cost of product sales | 73.5 | 69.3 |
| Total costs | <u>115.5</u> | <u>102.2</u> |
| Gross profit - service revenues | 20.6 | 13.1 |
| Gross profit - product sales | <u>24.3</u> | <u>27.7</u> |
| Total gross profit | 44.9 | 40.8 |
| Selling, general and administrative expenses | 28.7 | 27.3 |
| Restructuring expenses, and other | 1.3 | 0.4 |
| Research and development expenses | 3.9 | 3.6 |
| Depreciation | 1.3 | 0.8 |
| Amortization of intangible assets | 1.5 | 1.7 |
| Operating income from continuing operations | <u>8.2</u> | <u>7.0</u> |
| Interest expense, net | (5.5) | (5.1) |
| Other income (expense), net | <u>(0.5)</u> | <u>0.3</u> |
| Income from continuing operations before income taxes | 2.2 | 2.2 |
| Provision (benefit) for income taxes from continuing operations | <u>(1.5)</u> | <u>0.9</u> |
| Income from continuing operations | 3.7 | 1.3 |
| Loss from discontinued operations, net of income taxes | <u>(0.6)</u> | <u>(3.5)</u> |
| Net income (loss) | 3.1 | (2.2) |
| Less: Net income (loss) attributable to noncontrolling interest | - | - |

| | | |
|--|----------------|------------------|
| Net income (loss) attributable to Kratos Defense & Security Solutions | \$ 3.1 | \$ (2.2) |
| Basic income (loss) per common share attributable to Kratos Defense: | | |
| Income from continuing operations | \$ 0.04 | \$ 0.01 |
| Loss from discontinued operations | (0.01) | (0.03) |
| Net income (loss) | <u>\$ 0.03</u> | <u>\$ (0.02)</u> |
| Diluted income (loss) per common share attributable to Kratos Defense: | | |
| Income from continuing operations | \$ 0.03 | \$ 0.01 |
| Income (loss) from discontinued operations | - | (0.03) |
| Net income (loss) | <u>\$ 0.03</u> | <u>\$ (0.02)</u> |
| Weighted average common shares outstanding: | | |
| Basic weighted average common shares outstanding | <u>104.9</u> | <u>103.7</u> |
| Diluted weighted average common shares outstanding | <u>107.8</u> | <u>105.7</u> |
| Adjusted EBITDA (1) | <u>\$ 17.5</u> | <u>\$ 13.7</u> |

Unaudited Reconciliation of GAAP to Non-GAAP Measures

Note: (1) Adjusted EBITDA is a non-GAAP measure defined as GAAP net income (loss) attributable to Kratos Defense adjusted for net income attributable to noncontrolling interest, income(loss) from discontinued operations, net interest expense, income taxes, depreciation and amortization expense of intangible assets, and capitalized contract and development costs, stock compensation, acquisition and restructuring related items, and foreign transaction gain (loss).

Adjusted EBITDA as calculated by us may be calculated differently than Adjusted EBITDA for other companies. We have provided Adjusted EBITDA because we believe it is a commonly used measure of financial performance in comparable companies and is provided to help investors evaluate companies on a consistent basis, as well as to enhance understanding of our operating results. Adjusted EBITDA should not be construed as either an alternative to net income or as an indicator of our operating performance or an alternative to cash flows as a measure of liquidity. The adjustments to calculate this non-GAAP financial measure and the basis for such adjustments are outlined below. Please refer to the following table below that reconciles GAAP net income (loss) to Adjusted EBITDA.

The adjustments to calculate this non-GAAP financial measure, and the basis for such adjustments, are outlined below:

Interest income and expense. The Company receives interest income on investments and incurs interest expense on loans, capital leases and other financing arrangements, including the amortization of issue discounts and deferred financing costs. These amounts may vary from period to period due to changes in cash and debt balances.

Income taxes. The Company's tax expense can fluctuate materially from period to period due to tax adjustments that may not be directly related to underlying operating performance or to the current period of operations and may not necessarily reflect the impact of utilization of our NOLs.

Depreciation. The Company incurs depreciation expense (recorded in cost of revenues and in operating expenses) related to capital assets purchased, leased or constructed to support the ongoing operations of the business. The assets are recorded at cost or fair value and are depreciated over the estimated useful lives of individual assets.

Amortization of intangible assets. The Company incurs amortization of intangible expense related to acquisitions it has made. These intangible assets are valued at the time of acquisition and are amortized over the estimated useful lives.

Amortization of capitalized contract and development costs. The Company incurs amortization of previously capitalized software development and non-recurring engineering costs related to certain targets in its Unmanned Systems and ballistic missile target businesses as these units are sold.

Stock-based compensation expense. The Company incurs expense related to stock-based compensation included in its GAAP presentation of selling, general and administrative expense. Although stock-based compensation is an expense of the Company and viewed as a form of compensation, these expenses vary in amount from period to period, and are affected by market forces that are difficult to predict and are not within the control of management, such as the market price and volatility of the Company's shares, risk-free interest rates and the expected term and forfeiture rates of the awards. Management believes that exclusion of these expenses allows comparison of operating results to those of other companies that disclose non-GAAP financial measures that exclude stock-based compensation.

Foreign transaction (gain) loss. The Company incurs transaction gains and losses related to transactions with foreign customers in currencies other than the U.S. dollar. In addition, certain intercompany transactions can give rise to realized and unrealized foreign currency gains and losses.

Acquisition and restructuring related items. The Company incurs transaction related costs, such as legal and accounting fees and other expenses, related to acquisitions and divestiture activities. Management believes these items are outside the normal operations of the Company's business and are not indicative of ongoing operating results.

Restructuring costs. The Company incurs restructuring costs for cost reduction actions which include employee termination costs, facility shut-down related costs and remaining lease commitment costs for excess or exited facilities. Management believes that these costs are not indicative of ongoing operating results as they are either non-recurring and/or not expected when full capacity and volumes are achieved.

Legal related items. The Company incurs costs related to pending legal settlements and other legal related matters. Management believes these items are outside the normal operations of the Company's business and are not indicative of ongoing operating results.

Adjusted EBITDA is a non-GAAP financial measure and should not be considered in isolation or as a substitute for financial information provided in accordance with GAAP. This non-GAAP financial measure may not be computed in the same manner as similarly titled measures used by other companies. The Company expects to continue to incur expenses similar to the Adjusted EBITDA financial adjustments described above, and investors should not infer from the Company's presentation of this non-GAAP financial measure that these costs are unusual, infrequent, or non-recurring.

Three Months Ended
March 31, April 1,

| | <u>2019</u> | <u>2018</u> |
|---|-------------------|-------------------|
| Net income (loss) attributable to Kratos Defense | \$ 3.1 | \$ (2.2) |
| Income (loss) from discontinued operations, net of income taxes | 0.6 | 3.5 |
| Interest expense, net | 5.5 | 5.1 |
| Provision (benefit) for income taxes from continuing operations | (1.5) | 0.9 |
| Depreciation (including cost of service revenues and product sales) | 3.6 | 2.8 |
| Stock-based compensation | 2.6 | 1.7 |
| Foreign transaction (gain) loss | 0.5 | (0.2) |
| Amortization of intangible assets | 1.5 | 1.7 |
| Amortization of capitalized contract and development costs | 0.3 | - |
| Acquisition and restructuring related items and other | 1.3 | 0.4 |
| Plus: Net income (loss) attributable to noncontrolling interest | - | - |
| | <u> </u> | <u> </u> |
| Adjusted EBITDA | <u>\$ 17.5</u> | <u>\$ 13.7</u> |

Reconciliation of acquisition and restructuring related items and other included in Adjusted EBITDA:

| | <u>Three Months Ended</u> | |
|---|---------------------------|-------------------|
| | <u>March 31,</u> | <u>April 1,</u> |
| | <u>2019</u> | <u>2018</u> |
| Acquisition and transaction related items | \$ 1.2 | \$ - |
| Restructuring costs | 0.1 | 0.4 |
| | <u> </u> | <u> </u> |
| | <u>\$ 1.3</u> | <u>\$ 0.4</u> |

Kratos Defense & Security Solutions, Inc.
Unaudited Segment Data
(in millions)

| | <u>Three Months Ended</u> | |
|---|---------------------------|-----------------|
| | <u>March 31,</u> | <u>April 1,</u> |
| | <u>2019</u> | <u>2018</u> |
| Revenues: | | |
| Unmanned Systems | \$ 34.9 | \$ 27.8 |
| Kratos Government Solutions | 125.5 | 115.2 |
| Total revenues | <u>\$ 160.4</u> | <u>\$ 143.0</u> |
| Operating income (loss) from continuing operations: | | |
| Unmanned Systems | \$ 0.6 | \$ 0.8 |
| Kratos Government Solutions | 11.4 | 7.9 |
| Unallocated corporate expense, net | (3.8) | (1.7) |
| Total operating income from continuing operations | <u>\$ 8.2</u> | <u>\$ 7.0</u> |

Note: Unallocated corporate expense, net includes costs for certain stock-based compensation programs (including stock-based compensation costs for stock options, employee stock purchase plan and restricted stock units), the effects of items not considered part of management's evaluation of segment operating performance, and acquisition and restructuring related items, corporate costs not allocated to the segments, legal related items, and other miscellaneous corporate activities.

Reconciliation of consolidated Adjusted EBITDA to Adjusted EBITDA by segment is as follows:

| | <u>Three Months Ended</u> | |
|------------------|---------------------------|-----------------|
| | <u>March 31,</u> | <u>April 1,</u> |
| | <u>2019</u> | <u>2018</u> |
| Unmanned Systems | \$ 2.0 | \$ 1.7 |
| % of revenue | 5.7% | 6.1% |

| | | |
|-----------------------------|---------|---------|
| Kratos Government Solutions | 15.5 | 12.0 |
| % of revenue | 12.4% | 10.4% |
| Total Adjusted EBITDA | \$ 17.5 | \$ 13.7 |
| % of revenue | 10.9% | 9.6% |

Kratos Defense & Security Solutions, Inc.
Unaudited Condensed Consolidated Balance Sheets
(in millions)

| | March 31, 2019 | December 30, 2018 |
|---|---------------------------|------------------------------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 178.4 | \$ 182.7 |
| Restricted cash | - | 0.3 |
| Accounts receivable, net | 239.3 | 237.4 |
| Inventoried costs | 69.2 | 46.8 |
| Prepaid expenses | 13.3 | 8.9 |
| Other current assets | 9.6 | 10.3 |
| Current assets of discontinued operations | 7.3 | 8.3 |
| Total current assets | 517.1 | 494.7 |
| Property, plant and equipment, net | 113.5 | 67.1 |
| Operating lease right-of-use assets | 38.1 | - |
| Goodwill | 459.4 | 425.7 |
| Intangible assets, net | 34.4 | 16.1 |
| Other assets | 6.4 | 6.5 |
| Total assets | <u>\$ 1,168.9</u> | <u>\$ 1,010.1</u> |
| Liabilities and Stockholders' Equity | | |
| Current liabilities: | | |
| Accounts payable | \$ 47.4 | \$ 46.6 |
| Accrued expenses | 36.6 | 38.1 |
| Accrued compensation | 37.2 | 33.5 |
| Accrued interest | 6.5 | 1.6 |
| Billings in excess of costs and earnings on uncompleted contracts | 39.7 | 34.9 |
| Current portion of operating lease liabilities | 13.3 | - |
| Other current liabilities | 9.3 | 4.7 |
| Other current liabilities of discontinued operations | 5.3 | 5.3 |
| Total current liabilities | 195.3 | 164.7 |
| Long-term debt principal, net of current portion | 294.4 | 294.2 |
| Operating lease liabilities, net of current portion | 31.3 | - |
| Other long-term liabilities | 73.5 | 25.5 |
| Other long-term liabilities of discontinued operations | 6.5 | 6.4 |
| Total liabilities | 601.0 | 490.8 |
| Commitments and contingencies | | |
| Redeemable noncontrolling interest | 15.0 | - |
| Stockholders' equity: | | |
| Additional paid-in capital | 1,275.0 | 1,244.5 |
| Accumulated other comprehensive loss | (0.7) | (0.7) |
| Accumulated deficit | (721.4) | (724.5) |
| Total Kratos Defense stockholders' equity | 552.9 | 519.3 |
| Total liabilities and stockholders' equity | <u>\$ 1,168.9</u> | <u>\$ 1,010.1</u> |

Kratos Defense & Security Solutions, Inc.
Unaudited Condensed Consolidated Statements of Cash Flows
(in millions)

| | Three Months Ended | |
|---|---------------------------|--------------------------|
| | March 31, 2019 | April 1, 2018 |
| Operating activities: | | |
| Net income (loss) from consolidated operations | \$ 3.1 | \$ (2.2) |
| Less: (loss) from discontinued operations | (0.6) | (3.5) |
| Income from continuing operations | 3.7 | 1.3 |
| Adjustments to reconcile income from continuing operations to net cash provided by operating activities from continuing operations: | | |
| Depreciation and amortization | 5.1 | 4.5 |
| Amortization of lease right-of-use assets | 3.7 | - |
| Deferred income taxes | (3.4) | - |
| Stock-based compensation | 2.6 | 1.7 |
| Amortization of deferred financing costs | 0.2 | 0.2 |
| Changes in assets and liabilities, net of acquisitions: | | |
| Accounts receivable | (9.0) | 16.4 |
| Unbilled receivables | 19.7 | (14.2) |
| Inventoried costs | (10.8) | 1.3 |
| Advance payments received on contracts | 0.1 | (0.6) |
| Prepaid expenses and other assets | (1.1) | 0.8 |
| Operating lease liabilities | 2.8 | - |
| Accounts payable | (0.8) | (3.0) |
| Accrued compensation | 3.1 | 3.8 |
| Accrued expenses | (2.7) | (6.1) |
| Accrued interest | 4.9 | 4.9 |
| Billings in excess of costs and earnings on uncompleted contracts | 3.0 | (3.7) |
| Income tax receivable and payable | 1.4 | 0.2 |
| Other liabilities | (6.5) | (1.0) |
| Net cash provided by operating activities from continuing operations | 16.0 | 6.5 |
| Investing activities: | | |
| Cash paid for acquisitions, net of cash acquired | (17.6) | - |
| Capital expenditures | (4.0) | (6.7) |
| Net cash used in investing activities from continuing operations | (21.6) | (6.7) |
| Financing activities: | | |
| Proceeds (use) from the issuance of common stock | - | (1.1) |
| Repayment of debt | - | (0.2) |
| Debt issuance costs | - | (0.1) |
| Repayment of lease obligation | (0.1) | - |
| Proceeds from exercise of restricted stock units, employee stock options, and employee stock purchase plan | 0.9 | 1.8 |
| Net cash provided by financing activities from continuing operations | 0.8 | 0.4 |
| Net cash flows from continuing operations | (4.8) | 0.2 |
| Net operating and investing cash flows of discontinued operations | 0.3 | (3.1) |
| Effect of exchange rate changes on cash and cash equivalents | (0.1) | 0.2 |
| Net decrease in cash and cash equivalents | (4.6) | (2.7) |
| Cash and cash equivalents and restricted cash at beginning of period | 183.0 | 130.9 |
| Cash and cash equivalents and restricted cash at end of period | \$ 178.4 | \$ 128.2 |

Kratos Defense & Security Solutions, Inc.
Unaudited Non-GAAP Measures
Computation of Adjusted Earnings Per Share
(in millions, except per share data)

Adjusted income (loss) from continuing operations and adjusted earnings per share (Adjusted EPS) are non-GAAP measures for reporting financial performance and exclude the impact of certain items and, therefore, have not been calculated in accordance with GAAP. Management believes that exclusion of these items assists in providing a more complete understanding of the Company's underlying continuing operations results and trends and allows for comparability with our peer company index and industry. The Company uses these measures along with the corresponding GAAP financial measures to manage the Company's business and to evaluate its performance compared to prior periods and the marketplace. The Company defines adjusted income (loss) from continuing operations before amortization of intangible assets, stock-based compensation, foreign transaction gain/loss, and acquisition and restructuring related items and other. The Company uses the estimated cash tax provision in computing adjusted earnings per share to reflect the benefit from the utilization of the Company's net operating losses. Adjusted EPS expresses adjusted income (loss) from continuing operations on a per share basis using weighted average diluted shares outstanding.

The following table reconciles the most directly comparable GAAP financial measures to the non-GAAP financial measures.

| | Three Months Ended | |
|---|---------------------------|--------------------------|
| | March 31, 2019 | April 1, 2018 |
| Income from continuing operations before taxes | \$ 2.2 | \$ 2.2 |
| Add: Amortization of intangible assets | 1.5 | 1.7 |
| Add: Amortization of capitalized contract and development costs | 0.3 | - |
| Add: Stock-based compensation | 2.6 | 1.7 |
| Add: Foreign transaction (gain) loss | 0.5 | (0.2) |
| Add: Acquisition and restructuring related items and other | 1.3 | 0.4 |
| Adjusted income from continuing operations before income taxes | <u>8.4</u> | <u>5.8</u> |
| Estimated cash tax provision | 0.2 | 0.3 |
| Adjusted income from continuing operations attributable to Kratos Defense | <u>\$ 8.2</u> | <u>\$ 5.5</u> |
| Diluted income per common share attributable to Kratos Defense: | | |
| Adjusted income from continuing operations | <u>\$ 0.08</u> | <u>\$ 0.05</u> |
| Weighted average common shares outstanding | | |
| Diluted | <u>107.8</u> | <u>105.7</u> |

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Source: Kratos Defense & Security Solutions, Inc.