NORTHROP GRUMMAN CORP
Form 10-K/A
March 08, 2001

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K/A

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

For the fiscal year ended December 31, 2000

( ) 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
1-3229

NORTHROP GRUMMAN CORPORATION

(Exact name of registrant as specified in its charter)

DELAWARE (State or other jurisdiction of incorporation or organization)	95-1055798 (I.R.S. Employer Identification Number)

1840 Century Park East, Los Angeles, California 90067

www.northgrum.com
(Address of principal executive offices and internet site)

(310) 553-6262

(Registrant's telephone number, including area code)
Securities registered pursuant to section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, $1 par value	New York Stock Exchange
	Pacific Stock Exchange

Securities Registered pursuant to Section 12(g) of the Act:
None

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 such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. (X)

As of February 19, 2001, 72,126,289 shares of Common Stock were outstanding, and the aggregate market value of the Common Stock (based upon the closing price of the stock on the New York Stock Exchange) of the Registrant held by nonaffiliates was approximately $6,449 million.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the 2001 Annual Meeting of Stockholders. Part III

This amendment on Form 10-K/A is filed to present a composite annual report incorporating the three clerical corrections specified in the 10-K/A filed on March 2, 2001 as well as to make one additional clerical correction contained on the consolidated statements of income on the line item "income from continuing operations before cumulative effect of accounting change." We are filing this composite corrected 10-K in order to provide a single source for the annual report.

NORTHROP GRUMMAN CORPORATION

PART I

Item 1. Business

Northrop Corporation was incorporated in Delaware in 1985. In 1994 the company purchased the outstanding common stock of Grumman Corporation and, effective May 18, 1994, Northrop Corporation was renamed Northrop

Grumman Corporation. Northrop Grumman is an advanced technology company organized to operate in three sectors of the broadly defined defense industry: Integrated Systems Sector (ISS), Electronic Sensors and Systems Sector (ES^3), and Information Technology (Logicon). ISS includes the design, development and manufacturing of aircraft and aircraft subassemblies. ES^3 includes the design, development, manufacturing and integration of electronic systems and components for military and commercial use. Logicon includes the design, development, operation and support of computer systems for defense, scientific and management information.

On December 21, 2000, the Company and Litton Industries, Inc. jointly announced that they had entered into a definitive merger agreement to acquire Litton through a cash tender offer followed by a merger for cash consideration of $80 per common share and $35 per preferred share, or approximately $3.9 billion, plus the assumption of approximately $1.3 billion in Litton net debt.

On January 24, 2001, the transaction was amended to provide for the formation of a new Delaware holding company, NNG, Inc., and an exchange offer in which Litton common stockholders would be entitled to receive for each Litton common share $80 per share in cash, the equivalent of $80.25 in common stock of the new holding company, or the equivalent of $80 in liquidation value of a new preferred stock of the new holding company. Under the terms of the merger agreement, the new holding company cannot issue more than 13,000,000 shares of its common stock nor more than 3,500,000 shares of its new preferred stock in the exchange offer. Therefore, election by Litton stockholders to receive the new holding company's common stock and preferred stock may be subject to proration. Holders of Litton preferred stock may exchange their Litton preferred stock only for $35 per share in cash. Immediately prior to the closing of the exchange offer for Litton stock, the new holding company would exchange its common shares for all of the outstanding Northrop Grumman common shares on a one-for-one basis, through a merger in which Northrop Grumman would become a subsidiary of the new holding company. Following the purchase of Litton shares pursuant to the exchange offer, a subsidiary of the new holding company will be merged into Litton and the remaining common shareholders of Litton will be entitled to receive $80 per share in cash. Shares of Litton preferred stock that are not purchased in the exchange offer will remain outstanding as preferred shares of Litton. Following consummation of the merger, the new holding company will be renamed Northrop Grumman Corporation and the new holding company's common stock will trade on the New York and Pacific Stock Exchanges and each of Northrop Grumman and Litton will be subsidiaries of the new holding company. Northrop Grumman will change its name to Northrop Grumman Operations Corporation.

The obligations of the new holding company to accept shares tendered in the Litton exchange offer is conditioned on among other things: (i) the tender of not less than 25,646,399 shares of Litton common and preferred stock; (ii) the expiration of waiting periods under United States and European Economic Community antitrust regulations; (iii) the effectiveness of the new holding company's registration statement on Form S-4 with respect to the exchange offer; and (iv) the listing of the new holding company's common stock on the New York and Pacific Stock Exchanges.

On February 1, 2001, a new subsidiary of the company, NNG, Inc. filed a registration statement, which details the information concerning the offer, with the Securities and Exchange Commission. This information was distributed to Litton stockholders. Unitrin Inc., which owns through its subsidiaries approximately 28 percent of Litton's common stock, has agreed to tender all of its Litton common stock and to elect to receive a combination of common and preferred stock in exchange for its holdings. Unitrin has also agreed to elect an option that reduces its pro rata allotment of common stock to give priority to other Litton shareholders electing common stock. Subject to the completion of the pending reviews of the company's filings with the appropriate agencies of the United States under the Hart-Scott-Rodino Act and of the European Union, the acquisition is expected to be completed in the first quarter

2001. It will be accounted for using the purchase method of accounting.

Additional information required by this Item is contained in Part II, Item 7 of this Annual Report on Form 10-K.

Item 2. Properties

The major locations, general status of the company's interest in the property, and identity of the industry segments that use the property described are indicated in the following table.

Location	Property Interest
Annapolis, Maryland (2) (a) (b) (d) (e)	Owned, Leased
Arlington, Virginia (1) (2) (3) (4) (a) (c)	Leased
Baltimore, Maryland (2) (3) (a) (c) (e)	Leased
Belcamp, Maryland (2) (a)	Leased
Bellevue, Nebraska (3) (a) (c)	Leased
Bethesda, Maryland (3) (a) (c)	Leased
Bethpage, New York (1) (2) (a) (b) (c) (d) (e)	Owned
Bohemia, New York (3) (a)	Owned, Leased
Brook Park, Ohio (3) (a)	Leased
Buffalo, New York (2) (a)	Leased
Burlington, Canada (2) (3) (a) (b)	Owned, Leased
Carson, California (1) (c)	Leased
Chandler, Arizona (1) (b)	Owned
Cincinnati, Ohio (2) (b)	Leased

Clearfield, Utah (1) (c)	Leased
Cleveland, Ohio (1) (2) (a) (b)	Owned, Leased
Colorado Springs, Colorado (3) (a)	Leased
Dahlgren, Virginia (3) (a) (c)	Leased
Dallas, Texas (1) (3) (a) (b) (e)	Leased
El Segundo, California (1) (3) (a) (b) (c) (d) (e)	Owned, Leased
Elk Grove Village, Illinois (2) (c)	Leased
Elkridge, Maryland (2) (c) (d)	Leased
Fairfax, Virginia (3) (a)	Leased
Falls Church, Virginia (3) (a) (e)	Leased
Fort Tejon, California (1) (d)	Owned
Greenbelt, Maryland (3) (a)	Leased
Hagerstown, Maryland (2) (e)	Leased
Hawthorne, California (1) (2) (3) (4) (a) (b) (c) (d) (e)	Owned, Leased
Herndon, Virginia (2) (3) (a) (c)	Leased
Hicksville, New York (1) (a) (d) (e)	Owned, Leased
Hollywood, Maryland (1) (a)	Leased
Hunt Valley, Maryland (2) (a) (b) (e)	Owned, Leased
Huntsville, Alabama (2) (3) (a) (b) (c) (e)	Leased
Irving, Texas (1) (a)	Leased
Jacksonville, Florida (1) (a) (c) (d) (e)	Leased
Knoxville, Tennessee (2) (3) (a)	Leased
Lake Charles, Louisiana (1) (a) (b) (c) (e)	Owned, Leased
Lexington, South Carolina (1) (2) (a) (c)	Owned, Leased
Linthicum, Maryland (1) (2) (a) (b) (c) (d) (e)	Owned, Leased
Los Angeles, California (3) (4) (a)	Leased

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McLean, Virginia (3) (a) (e)	Leased
Melbourne, Florida (1) (a) (b) (c) (e)	Owned, Leased
Melville, New York (2) (d)	Leased
New Town, North Dakota (1) (b) (c)	Owned, Leased
Newport News, Virginia (3) (a)	Leased
Northfields, United Kingdom (2) (a)	Leased
Norwalk, Connecticut (2) (b)	Leased
Oslo, Norway (2) (a) (b)	Leased
Palmdale, California (1) (a) (b) (c) (d) (e)	Owned, Leased
Philadelphia, Pennsylvania (1) (2) (a) (b)	Leased
Pico Rivera, California (1) (a) (b) (d) (e)	Owned
Pittsburgh, Pennsylvania (2) (d)	Leased
Point Mugu, California (1) (a) (b) (c) (e)	Owned, Leased
Reston, Virginia (3) (a)	Leased
Rockville, Maryland (3) (a)	Leased
Rolling Meadows, Illinois (2) (3) (a) (b) (c) (d) (e)	Owned, Leased
San Diego, California (1) (2) (3) (a) (b) (c) (d) (e)	Owned, Leased
San Pedro, California (3) (a) (c) (e)	Leased
Santa Isabel, Puerto Rico (2) (b)	Leased
St. Augustine, Florida (1) (a) (b) (c) (e)	Owned, Leased
Stafford, Virginia (2) (3) (a)	Leased

Sunnyvale, California (2) (3) (a) (b)	Owned, Leased
Sykesville, Maryland (2) (b)	Owned
Tacoma, Washington (3) (a)	Leased
Virginia Beach, Virginia (1) (3) (a) (c)	Owned, Leased
Warner Robins, Georgia (1) (2) (3) (a) (c)	Owned, Leased
Williamsville, New York (2) (a) (b)	Leased

Following each described property are numbers indicating the reporting segments utilizing the property:

(1) Integrated Systems

(2) Electronic Sensors and Systems

(3) Logicon

(4) General Corporate Asset

Following each described property are letters indicating the types of facilities located at each location:

(a) office

(b) manufacturing

(c) warehouse

(d) research and testing

(e) other

Government-owned facilities used or administered by the company consist of 3 million square feet at various locations across the United States.

The company believes its properties are well-maintained and in good operating condition.

Item 3. Legal Proceedings

U.S. ex rel Jordan v. Northrop Grumman Corporation

In October 1999, the company was served with a fifth amended complaint that was filed by the government in the U.S. District Court for the Central District of California in this action, which was commenced in May 1995. The complaint alleges that the company violated the False Claims Act by knowingly supplying BQM-74C aerial target drones that contained various defective components between 1992 and 1995. The government seeks to recover damages up to $185,000,000 plus pre-judgment interest under theories of fraud, payment by mistake, unjust enrichment, breach of warranty and breach of contract. Damages awarded pursuant to the False Claims Act may be trebled by the court. The company intends to vigorously defend this matter.

Zabielski and related cases

In July and August 1998, three shareholder derivative lawsuits, respectively encaptioned Zabielski v. Kent Kresa, et al., Harbor Finance Partners v. Kent Kresa et al., and Clarren v. Kent Kresa, et al., were filed in the Superior Court of California for the County of Los Angeles. These lawsuits each contain similar allegations that the directors of the company and certain of its officers breached their fiduciary duties in connection with the shareholder vote approving the proposed acquisition of the company by Lockheed Martin Corporation, and that certain defendants engaged in stock trades in violation of federal and state securities laws. The lawsuits are purportedly brought on the company's behalf and do not seek relief against the company. On January 31, 2001 the court dismissed the derivative lawsuits with prejudice. The defendants deny the allegations made in these actions and intend to defend the actions vigorously.

Fanni and related cases

Five shareholder class action lawsuits, making similar allegations, were filed between July and September, 1998 in the United States District Court for the Central District of California against the company, its directors, and certain of its officers. Three of these lawsuits, respectively encaptioned Fanni v. Northrop Grumman Corp., et al., Schnee v. Northrop Grumman Corp., et al., and Florida State Board of Admin. v. Northrop Grumman Corp., et al. allege that defendants issued misleading proxy materials in connection with the proposed acquisition of the company by Lockheed Martin Corporation, in violation of the federal securities laws. These actions seek unspecified damages on behalf of a class of shareholders related to the accelerated vesting of stock incentive plans upon the shareholder vote to approve the merger. Two of these lawsuits, respectively encaptioned Burroughs v. Northrop Grumman Corp., et al., and Miller, et al. v. Northrop Grumman Corp., et al., allege that defendants disseminated misleading information in connection with the proposed acquisition, in violation of the federal securities laws, thereby artificially inflating the market price of the company's common stock. These actions seek unspecified damages for a class of shareholders who purchased Northrop Grumman stock between July 3, 1997 and March 9, 1998. The District Court consolidated Fanni, Schnee and Florida State Board of Admin. into one action, and Burroughs and Miller into another action. The District Court dismissed the Fanni consolidated actions with prejudice in April 2000, and dismissed the Burroughs consolidated actions with prejudice in October 2000. Plaintiffs filed timely appeals and both matters are pending in the Ninth Circuit Court of Appeals. The company and the individual defendants deny the allegations made in these actions and intend to defend the actions vigorously.

General

The company, as a government contractor, is from time to time subject to U.S. Government investigations relating to its operations. Government contractors that are found to have violated the False Claims Act, or are indicted or convicted for violations of other Federal laws, or are considered not to be responsible contractors may be suspended or debarred from government contracting for some period of time. Such convictions could also result in fines. Given the company's dependence on government contracting, suspension or debarment could have a material adverse effect on the company. The company is involved in certain other legal proceedings arising in the ordinary course of business, none of which the company's management believes will have a material adverse effect on the company's financial condition.

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Executive Officers of the Registrant

The following individuals were the elected officers of the Company as of February 2001:

Name	Age	Office Held	Since	Business Experience Last Five Years
Kent Kresa	62	Chairman, President & CEO	1990	
Herbert W. Anderson	61	Corporate Vice President, President and Chief Executive Officer, Logicon, Inc.	1998	Corporate Vice President and General Manager, Data Systems & Services Division
Ralph D. Crosby, Jr.	53	Corporate Vice President and President, Integrated Systems Sector	2000	Corporate Vice President and President Integrated Systems and Aerostructures Sector; Prior to 1999, Corporate Vice President and General Manager, Commercial Aircraft Division; Prior to September 1996, Corporate Vice President and Deputy General Manager, Commercial Aircraft Division; Prior to March 1996, Corporate Vice

				President and Deputy General Manager, Military Aircraft Systems Division
J. Michael Hateley	54	Corporate Vice President and Chief Human Resources and Administrative Officer	2000	Vice President, Personnel; Prior to January 1999, Vice President Human Resources, Security and Administration, Military Aircraft Systems Division
Robert W. Helm	49	Corporate Vice President, Government Relations	1994	
John H. Mullan	58	Corporate Vice President and Secretary	1999	Acting Secretary; Prior to May 1998 Senior Corporate Counsel
Albert F. Myers	55	Corporate Vice President and Treasurer	1994	
Rosanne P. O'Brien	57	Corporate Vice President, Communications	2000	Vice President, Corporate Communications; Prior to 1999, Vice President, Corporate Communications at Alleghany Teledyne

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Name	Age	Office Held	Since	Business Experience Last Five Years
James G. Roche	61	Corporate Vice President and President, Electronic Sensors and Systems Sector	1998	Corporate Vice President and General Manager, Electronic Sensors and Systems Division

Robert B. Spiker	47	Corporate Vice President and Controller	2000	Vice President, Finance and Controller, Electronic Sensors and Systems Sector; Prior to 1999 Business Manager for C^3&I Naval Systems
W. Burks Terry	50	Corporate Vice President and General Counsel	2000	Vice President, Deputy General Counsel and Sector Counsel; Prior to 1998 Vice President and Assistant General Counsel
Richard B. Waugh, Jr.	57	Corporate Vice President and Chief Financial Officer	1993	

Item 4. Submission of Matters to a Vote of Security Holders

No information is required in response to this Item.

PART II

Item 5. Market for Registrant's Common Equity and Related Stockholder Matters

The information required by this Item is contained in Part II, Item 8 of this Annual Report on Form 10-K.

Item 6. Selected Financial Data

The data for all periods presented in the following table, Selected Financial Data, have been restated to reflect Aerostructures as discontinued operations except for number of employees at year-end, floor area, and all balance sheet data, including net working capital, total assets, debt, long-term obligations and shareholders' equity.

NORTHROP GRUMMAN CORPORATION

Selected Financial Data

Years ended December 31, $ in millions except per share	2000	1999	1998	1997	1996
Net sales to					
United States Government	$ 6,662	$ 6,716	$ 6,426	$ 6,921	$ 6,943
Other customers	956	900	941	877	724
Total net sales	$ 7,618	$ 7,616	$ 7,367	$ 7,798	$ 7,667
Operating margin	$ 1,098	$ 954	$ 752	$ 741	$ 752
Income from continuing operations, net of tax	625	474	193	318	330
Basic earnings per share, from continuing operations	8. 86	6.84	2.82	4.76	5.27
Diluted earnings per share, from continuing operations	8. 82	6.80	2.78	4.67	5.18
Cash dividends per share	1.60	1.60	1.60	1.60	1.60
Net working capital	(162)	329	666	221	106

Current ratio	.94 to 1	1.13 to 1	1.28 to 1	1.08 to 1	1.04 to 1
Total assets	$ 9,622	$ 9,285	$ 9,536	$ 9,677	$ 9,645
Long-term debt	1,605	2,000	2,562	2,500	2,950
Total long-term obligations	3,015	3,564	4,319	4,339	4,694
Long-term debt as a percentage of					
shareholders' equity	41.0%	61.4%	89.9%	95.3%	129.3%
Operating margin as a percentage of					
Net sales	14.4	12.5	10.2	9.5	9.8
Average segment assets	14.1	11.7	9.0	8.7	11.0
Income from continuing operations, net of tax,					
as a percentage of					
Net sales	8.2	6.2	2.6	4.1	4.3
Average assets	6.6	5.0	2.0	3.3	4.3
Average shareholders' equity	17.4	15.5	7.1	13.0	17.1
Research and development expenses					
Contract	$ 1,002	$ 1,147	$ 1,478	$ 1,651	$ 1,616
Noncontract	216	195	189	231	218
Payroll and employee benefits	2,581	2,768	2,821	2,922	2,904
Number of employees at year-end	39,300	44,600	49,600	52,000	51,600
Number of shareholders at year-end	11,750	11,173	11,774	11,400	11,773
Depreciation	$ 175	$ 162	$ 179	$ 200	$ 181
Amortization of					
Goodwill	114	99	90	90	79
Other purchased intangibles	92	92	90	90	80
Maintenance and repairs	96	79	74	92	85

Rent expense	122	101	92	95	95
Floor area (in millions of square feet)					
Owned	14.3	18.8	19.2	20.5	22.5
Commercially leased	9.8	10.6	10.6	10.0	9.9
Leased from United States Government	2.9	7.5	7.6	8.8	9.0

Item 7. Management's Discussion and Analysis of the Company's Financial Condition and Results of Operations

BUSINESS CONDITIONS

Northrop Grumman is a leading defense electronics, systems integration and information technology company. As a prime contractor, principal subcontractor, partner, or preferred supplier, Northrop Grumman participates in many high-priority defense and commercial technology programs in the United States and abroad. While Northrop Grumman is subject to the usual vagaries of the marketplace, it is also affected by the unique characteristics of the defense industry and by certain elements peculiar to its own business mix. It is common in this industry for work on major programs to be shared among a number of companies. A company competing to be a prime contractor may, upon ultimate award of the contract, turn out to be a subcontractor. It is not uncommon to compete with customers, and simultaneously on other contracts, to be either a supplier to or a customer of such competitor. The nature of major defense programs, conducted under binding contracts, allows companies that perform well to benefit from a level of program continuity unknown in many industries. While Northrop Grumman conducts most of its business with the U.S. Government, principally the Department of Defense (DOD), domestic and international commercial sales still represent a significant portion of our business.

The collapse of communism has fundamentally altered the landscape of the global defense industry. The defense requirements of the United States and NATO countries have shifted from defending against threats imposed by the former Soviet Union to a focus upon the management of one or more regional conflicts. These engagements may require unilateral or cooperative initiatives, ranging from passive surveillance to active engagement, deterrence, policing or peacekeeping. In addition, the DOD's strategy has been affected by the general public's increasing intolerance for military action which puts military or civilian personnel at risk. As a result of these trends, both the United States and NATO countries are increasingly relying on sophisticated weapon systems which provide long-range surveillance and intelligence, battle management and precision strike capabilities. Accordingly, defense procurement spending is expected to be weighted towards the development and procurement of advanced electronics and software that enhance the capabilities of individual weapons systems and provide for the real-time integration of individual surveillance, information management, strike and battle management platforms.

United States defense contractors have also benefited from an upward trend in defense spending over recent years. Following a period of budget decreases in the post-Cold War era, the aggregate U.S. defense budget, as appropriated by Congress, has increased, principally in the area of equipment procurement. Defense spending by other NATO countries has stabilized, following decreases in the immediate post-Cold War era, while they continue to increase their focus upon the development and procurement of advanced electronics and information systems capabilities.

Although the ultimate size of future defense budgets remains uncertain, current indications are that the defense budget will increase over the next five years. U.S. Government programs in which Northrop Grumman either participates, or strives to participate, must compete with other programs for consideration during our nation's budget formulation and appropriation processes. Budget decisions made in this environment will have long-term consequences for the size and structure of Northrop Grumman and the entire defense industry. While the ultimate distribution of the budget remains uncertain, the company expects that its technologies and programs will be viewed favorably in the upcoming strategic review and budget process.

Northrop Grumman has historically concentrated its efforts in high technology areas such as stealth, airborne surveillance, battle management, precision weapons, systems integration, defense electronics, and information technology. Even though a high priority has been assigned by the DOD to the company's major programs, there remains the possibility that one or more of them may be reduced, extended or terminated.

In the event of termination for the government's convenience, contractors are normally protected by provisions covering reimbursement for costs incurred subsequent to termination. The company received a termination for convenience notice on the Tri-Service Standoff Attack Missile (TSSAM) program in February 1995. In December 1996 the company filed a lawsuit against the U.S. Government in the U.S. Court of Federal Claims seeking the recovery of approximately $750 million for uncompensated performance costs, investments, and a reasonable profit on the program. In prior years the company had charged to operations in excess of $600 million related to this program. Northrop Grumman is unable to predict whether it will realize some or all of its claims, none of which are recorded on its balance sheet, from the U.S. Government on the TSSAM contract.

Prime contracts with various agencies of the U.S. Government and subcontracts with other prime contractors are subject to numerous procurement regulations, including the False Claims Act and The International Traffic in Arms Regulation promulgated under the Arms Export Control Act, with noncompliance found by any one agency possibly resulting in fines, penalties, debarment or suspension from receiving additional contracts with all U. S. Government agencies. Given the company's dependence on U.S. Government business, suspension or debarment could have a material adverse effect on the company's future.

Northrop Grumman pursues new business opportunities when justified by acceptable financial returns and technological risks. The company examines opportunities to acquire or invest in new businesses and technologies to strengthen its traditional business areas. Northrop Grumman continues to capitalize on its technologies and skills by entering into joint ventures, partnerships or associations with other companies, both domestically and internationally.

An individual company's success in the competitive defense industry depends upon its ability to develop and market its products, as well as its ability to provide the people, facilities, equipment and financial capacity needed to deliver those products with maximum efficiency. It is necessary to maintain, as the company has, sources for raw materials, fabricated parts, electronic components and major subassemblies. In this manufacturing and systems integration environment, effective oversight of subcontractors and suppliers is as vital to success as managing internal operations. Northrop Grumman's operating policies are designed to achieve these objectives. The company also believes that it maintains good relations with its employees, approximately 11 percent of whom are covered by collective bargaining agreements.

An important factor in determining Northrop Grumman's ability to compete successfully for future contracts will be its cost structure vis-a-vis other bidders. Since the early 1990's the industry has been going through a consolidation process and, along with it, significant downsizing. These actions, in which Northrop Grumman has participated, have made competition even more intense than in the past. Lockheed Martin Corporation, The Boeing Company, and Raytheon Company are the largest companies in the defense industry at this time. Northrop Grumman competes against these and other companies for a number of programs, both large and small. Intense competition and long operating cycles are both key characteristics of Northrop Grumman's business and the defense industry.

Acquisitions and Divestures

The current composition of Northrop Grumman resulted from a series of strategic acquisitions, mergers and divestures by the former Northrop Corporation beginning in 1992, when the company acquired a 49 percent interest in the Vought Aircraft Company, a designer and builder of commercial and military aerostructures. The remaining 51 percent interest in Vought Aircraft was purchased in 1994. Also in 1994 the company purchased the outstanding common stock of Grumman Corporation and the company was renamed Northrop Grumman Corporation. In 1996 Northrop Grumman acquired the defense electronic systems group of Westinghouse Electric Corporation. Effective August 1, 1997, the company consummated its merger with Logicon, Inc. (Logicon), a leading defense information technology company.

In 1998 and 1999 the company acquired several businesses which strategically fit within its three business sectors: Integrated Systems Sector (ISS), Electronic Sensors and Systems Sector (ES^3) and Logicon, the company's information technology sector. Inter-National Research Institute Inc. (INRI) was acquired in 1998 and was integrated into the Logicon segment. In 1999 Ryan Aeronautical, an operating unit of Alleghany Teledyne Incorporated, the Information Systems Division of California Microwave, Inc., and Data Procurement Corporation (DPC), were acquired and integrated into ISS, ES^3 and Logicon, respectively.

Navia Aviation AS, Comptek Research, Inc., Federal Data Corporation, and Sterling Software, Inc., (known as Sterling's Federal Systems Group) were all acquired in 2000. Navia was integrated into ES^3. The Comptek units were integrated within all three of the business segments. Federal Data and Sterling were both integrated into Logicon. See the footnote to the Consolidated Financial Statements in Part II, Item 8 entitled "Acquisitions" for additional information.

On July 24, 2000, the company completed the sale of its commercial aerostructures (Aerostructures) business to The Carlyle Group. Aerostructures was principally a major producer of commercial aircraft subassemblies, the majority of which were sold to The Boeing Company. The company's Consolidated Statements of Income and related disclosures have been restated to reflect Aerostructures as a discontinued operation for all periods presented. See the footnote to the Consolidated Financial Statements in Part II, Item 8 entitled "Discontinued Operations" for additional information.

On December 21, 2000, the Company and Litton Industries, Inc. jointly announced that they had entered into a definitive merger agreement whereby the company would acquire Litton through a cash tender offer followed by a merger for cash consideration of $80 per common share and $35 per preferred share, or approximately $3.9 billion, plus the assumption of approximately $1.3 billion in Litton net debt. On January 24, 2001, the transaction was amended. See Part I, Item 1 for additional information concerning the Litton acquisition.

BUSINESS SEGMENTS

Northrop Grumman's three reportable segments are its three operating units: Integrated Systems Sector (ISS), Electronic Sensors and Systems Sector (ES^3) and Logicon, the company's information technology sector.

Integrated Systems Sector

Air Combat Systems (ACS), Airborne Early Warning and Electronics Warfare (AEW/EW) systems, and Airborne Ground Surveillance and Battle Management (AGS/BM) systems are the three major business areas within ISS, which is headquartered in Dallas, Texas .

The ACS business area is the principal subcontractor to The Boeing Company on the F/A-18 (Hornet/Super Hornet) program. The F/A-18 is a fighter/ground-attack aircraft with configurations equipped for either one or two crew members. Principally deployed by the U.S. Navy on aircraft carriers, it also has been purchased by several other nations as a land-based combat aircraft. The company builds approximately 40 percent of the aircraft including the center and aft fuselage, vertical tails, and associated subsystems. The F/A-18 single-seat E and two-seat F, enhanced (Super Hornet) versions of the F/A-18C and D (Hornet) models, are currently in production and will serve as the U.S. Navy's next-generation multimission aircraft. The F/A-18 work is performed at the El Segundo, California facility.

On the Joint Strike Fighter (JSF) Program, the ACS business area is teaming with Lockheed Martin Corporation. The JSF is a multi-mission, multi-service weapon system, which is being developed as an affordable fighter/attack platform. The Engineering and Manufacturing Development (EMD) phase is expected to be awarded in the fourth quarter 2001.

ACS is a leader in the unmanned systems market. The major projects under development include Global Hawk, Vertical Takeoff and Landing Tactical Unmanned Aerial Vehicle (VTUAV) and Miniature Air Launched Decoy (MALD). Global Hawk is being developed for the U.S. Air Force to provide battlefield commanders with intelligence imagery from high altitudes for long periods of time. VTUAV is being developed for the U.S. Navy and Marine Corps to perform intelligence, surveillance, reconnaissance and targeting missions. MALD is a small jet powered aerial vehicle designed for the U.S. Air Force to imitate manned jet fighters in radar images and confuse enemy air defense systems. ACS also produces aerial targets for the U. S. Navy, U. S. Air Force and international customers.

Manufacturing for unmanned systems is performed at the Palmdale, California site while engineering, program management and product development are performed in Rancho Bernardo, California.

The company is the prime contractor for the B-2 (Spirit) bomber which is included in the ACS business area. Production deliveries of the B-2 have been completed and the company continues to perform work on the EMD contract as well as upgrade and support activity. The U.S. Air Force currently plans to operate two B-2 bomber squadrons of eight aircraft each with an additional five aircraft available to fill in for those in depot for periodic maintenance. The B-2 work is performed at the Palmdale, California site.

The ACS business area was selected by the U.S. Air Force as the prime systems integrator contractor for the Multi-Platform Radar Technology Insertion Program (MP-RTIP). The objective of the program is to upgrade current aircraft and unmanned vehicles with an advanced technology radar subsystem, which includes higher resolution and greater accuracy. The ACS business area will lead the effort with the AGS/BM business area and the Aerospace Electronics business area of ES^3 as major members of the team.

The AEW/EW business area includes the E-2C (Hawkeye) Airborne Early Warning and the EA-6B (Prowler) Electronic Warfare aircraft. The E-2C has been in active service with the U.S. Navy since 1973 and is employed by the air forces of five other nations. The company is currently performing a multi-year contract to produce 22 aircraft for the U. S. Navy, 1 aircraft for France, and 2 aircraft for Taiwan. The E-2C is kept current through technological upgrades of its mission systems, the latest of which is the Hawkeye 2000 configuration. The EA-6B is the armed services' only offensive tactical radar jamming aircraft. The company is currently developing the next generation mission system for this aircraft under the ICAP (Increased Capability) III contract. Manufacturing for both aircraft is performed at the St. Augustine, Florida site while engineering, program management and product development is performed in Bethpage, New York.

The AGS/BM business area is the prime contractor for the E-8 Joint Surveillance Target Attack Radar System (Joint STARS). Joint STARS detects, locates, classifies, tracks and targets potentially hostile ground movement in all weather conditions. It is designed to operate around the clock in constant communication through secure data links with Air Force command posts, Army mobile ground stations, or centers for military analysis far from the point of conflict. The Joint STARS platform is a Boeing 707-300 airframe that is remanufactured at the Lake Charles, Louisiana site. Final installation of electronics and testing are performed at the test facility in Melbourne, Florida.

The AGS/BM business area was selected by the U.S. Navy as the prime contractor for the Airborne Laser Mine Detection System (ALMDS) Program. The objective of the program is to use a laser-based system mounted in a helicopter to scan a wide path of the ocean and generate a topographic view of the ocean floor together with a computer-enhanced image of the shapes, sizes and locations of mines. This program is also being performed at the Melbourne, Florida facility.

Electronic Sensors and Systems Sector

The ES^3 segment, headquartered in Linthicum, Maryland, comprises four business areas: Aerospace Electronic Systems; Command, Control, Communications, Intelligence and Naval Systems (C^3I&N); Defensive Electronic Systems; and several smaller business elements referred to as "Other". The segment's primary expertise is the ability to conceive, design, produce and support high performance sensors, intelligence and processing systems operating in all environments from under seas to outer space.

Aerospace Electronic Systems includes four business elements: combat avionics systems, land combat systems, airborne surveillance systems, and space systems. Combat avionics systems is focused on providing radar and electro-optic-based avionics systems to meet the needs for targeting and strike missions for armed forces worldwide. The AN/APG-66/68 airborne fire control radar series aboard F-16 fighters throughout the world has set a new standard for performance and reliability over the last two decades. More than six thousand AN/APG-66/68 radars have been produced since 1976. The basic radar, with multiple variants, is currently on 16 airborne platforms deployed in 20 countries. Northrop Grumman currently is leading a team developing the next-generation air-dominance radar (AN/APG-77) featuring a low observable, active electronically scanned array with multiple target, all-weather capability for the U. S. Air Force's F-22 aircraft. Advanced radar concepts for the next generation Joint Strike Fighter have been developed and flown aboard Northrop Grumman flight test aircraft. These radar systems are developed and produced at the Linthicum, Maryland facility.

Northrop Grumman's land combat systems business element, teamed with Lockheed Martin, is producing the Longbow APG-78 fire control radar and the Longbow Hellfire missile for the U. S. Army's AH-64 Apache attack helicopter and the British WAH-64 Westland Apache. Longbow fire control radar work is performed at the Linthicum facility and the Longbow missile work is performed in Huntsville, Alabama. Additionally, Northrop Grumman is currently in Low Rate Initial Production (LRIP) for the Brilliant Anti-Tank (BAT) anti-armor submunition at the new BAT production facility at Huntsville. BAT is an autonomous submunition that uses passive acoustic and infrared sensors to find, attack and destroy moving tanks and other armored vehicles in hostile territory. BAT is designed to be carried and dispensed by the U. S. Army's Tactical Missile System (TACMS) Block II surface-to-surface missile and has potential application for ground-, air-, and sea-launched cruise missiles, artillery rockets, and munitions dispensers.

Airborne surveillance systems products include Airborne Warning and Control System (AWACS) radar (AN/APY-1, APY-2), which are integrated in the highly reliable Boeing 707 and 767 aircraft and have been the surveillance system of choice for U.S. and allied forces worldwide. The AWACS Radar System Improvement Program (RSIP) is currently in production for the U.S. Air Force, the United Kingdom and NATO. RSIP will enhance the performance of the AWACS radar against smaller cross section targets. A new surveillance product, the Multirole Electronically Scanned Array (MESA), is currently being developed for installation on Boeing 737 aircraft for the Royal Australian Air Force. These systems are produced at the Linthicum, Maryland facility. The E-8 Joint STARS is equipped with the Northrop Grumman Norden Systems AN/APY-3 air-to-ground surveillance system, which provides long-range, standoff, real-time surveillance of the battlefield. Aerospace Electronics Systems is a major member of the team, led by ACS, working on MP-RTIP, which, with its advanced active aperture, will provide significant performance upgrades on Joint STARS for its current mission and opens the way for incorporation of new missions.

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The space systems business element develops space sensors and systems, with subsegments of military and civil/commercial space, and intelligence, surveillance and reconnaissance ground-based processing systems.

C^3I&N includes four business elements: airspace management systems; oceanic and naval systems; marine systems, and communications. Airspace management systems produces air defense and air traffic control radar systems for domestic and international customers. Products include the solid-state AN/TPS-70 family of radars and U. S. Air Force AN/TPS-75. The TPS-75 has been the front line U.S. Air Force air defense system standard since 1968. The TPS-70 family of systems currently operates in more than 30 countries, supporting air defense, air sovereignty, air traffic control, and counter-narcotics needs. The ASR-12, a solid-state derivative of the company's FAA standard ASR-9 terminal radar is now in full production and systems are operational in Peru, Mexico, and El Salvador.

The oceanic and naval systems business is headquartered in Annapolis, Maryland. Oceanic and naval systems is the focal point for underseas research, development and production. Products include the Advanced SEAL Delivery System (ASDS) mini-submarine, the SPQ-9B shipboard radar and advanced sensors and processors for minehunting, such as the AN/AQS-14 high-speed airborne minehunting system. The business is also a significant participant in the DD-21 next generation destroyer competition.

C^3I&N provides marine machinery and advanced propulsion systems, missile launchers, shipboard electronics and control systems for naval forces through its marine systems organization in Sunnyvale, CA. Every Nimitz-class aircraft carrier is fitted with eight turbine generator sets. The company produces these generators as well as the main propulsion system for the U.S. Navy's Seawolf and Virginia-class attack submarines. Marine Systems was one of two businesses selected by the Navy to develop the next generation Electro-Magnetic Launcher (EMALS), which could ultimately replace the steam catapult used on Naval aircraft carriers. Marine systems is also responsible for integration of the intercooled recuperated (ICR) gas turbine engine, which is a candidate propulsion system for the DD-21 destroyer.

The communications business provides reliable communications solutions for commercial and defense applications through three subsidiary companies. Xetron is renowned for co-site and spread spectrum communications systems. Park Air Systems is a world leader in ground-to-air communications systems for commercial and defense aviation. The California Microwave communications business offers specialized satellite communications expertise and an array of communications gateways and message processing systems .

The Defensive Electronic Systems business area includes five business elements located in six geographic locations. The primary design and manufacturing center is located in Rolling Meadows, Illinois. The five business elements are: radio frequency (RF) countermeasures, electro optical/infrared (EOIR) countermeasures, targeting systems, simulators, and support systems. The RF countermeasures element designs and produces systems for application on the F-15, F-16, AV8-B, F/A-18 aircraft and for application on helicopters. The AN/ALQ-135 is an internally mounted radar jammer deployed on F-15 fighter aircraft as part of that aircraft's tactical electronic warfare system. The AN/ALQ-165 is an airborne self-protection jammer installed on U.S. and international F/A-18 and F-14 aircraft. The AN/ALQ-165 is being produced in a joint venture with ITT Avionics. The AN/ALQ-162 Shadowbox, a jammer built specifically to counter continuous wave radars, has been installed on the AV-8B and certain foreign owned F/A-18 aircraft. It also is being deployed on U.S. Army helicopters and special mission aircraft and has been sold to the air forces of three other nations. The EOIR countermeasures element is currently producing a directional infrared countermeasures (DIRCM) system which is slated for use on British helicopters and transports and U.S. Special Operations Command C-130 transports to protect the aircraft from heat-seeking missiles. DIRCM is the first infrared countermeasures system of its kind and was developed to accommodate laser capabilities currently in development. The targeting element primary product is the Litening II targeting system for F-16 aircraft. The system is currently in production for the Air National Guard, U. S. Marine Corps and several foreign customers. The electronic warfare simulators element, located in Buffalo, New York, designs and produces electronic warfare signal environment simulation systems, infrared scene simulation systems, and radar signal environment simulation systems. Customers include the U.S. Navy, U.S. Air Force, other defense contractors and numerous international customers. The support systems element designs and produces automated test equipment products for the U.S. Army and Navy.

The business area labeled "Other" includes California Microwave airborne and information systems business, the sector's systems development and technology, automation and information systems, and its logistics systems. California Microwave, which was acquired by Northrop Grumman in April 1999, specializes in airborne reconnaissance and surveillance systems, communications gateway systems, and mission planning. California Microwave's customers include the U.S. military services and other U.S. government agencies. The remaining three areas provide the technology for current and future Northrop Grumman products, provide material handling system solutions for postal services and commercial packages and mail shipping firms, and develop a wide range of logistics services to offer customers.

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Logicon Segment

The three major business areas reported in Logicon, the company's information technology (IT) sector, are Government Information Technology, Technology Services, and Commercial Information Technology. Logicon, which is headquartered in Herndon, Virginia, does business in 13 foreign countries and 43 states, with the largest being Virginia, California and Florida.

The Government Information Technology business area covers a wide range of IT services and support programs. This work is performed for government customers at the DOD, federal, state and local level, and covers the command, control, communications, computers, intelligence, surveillance and reconnaissance (C4ISR); training and simulation; science and technology; and information systems markets. Logicon's Government Information Technology business area grew in size and scope in 2000 following the addition of Comptek's Federal Systems unit, Sterling Software's Federal Systems Group and Federal Data Corporation.

In the C4ISR market, Logicon supports the development, testing and fielding of command and control systems for its primary customer, the U.S. DOD. Specialty areas include mission critical software, systems engineering, tactical data links, information security, information assurance, independent validation and verification, geographic information systems, multispectral imagery analysis, orbital analysis, and modeling and simulation.

In the training and simulation market, Logicon is a prime developer and operator of modeling, simulation and analysis systems, computer-driven war-gaming and training, and flight simulations. Logicon provides these services to the U.S. Navy, Air Force, Army, Special Operations Command and NASA.

In the science and technology market, Logicon's work includes analysis of nuclear weapons effects, high-energy laser technology development, and neural network applications. This technical and scientific support is provided to the U.S. Air Force Research Labs and the Defense Threat Reduction Agency.

The information systems market is Logicon's largest and most diverse. The company offers a complete range of IT services such as high performance computing, electronic commerce, large-scale database design, systems modernization and integration, disaster recovery and planning, enterprise resource planning, and knowledge management solutions. Customers include state governments, federal agencies such as the General Services Administration, Department of Health and Human Services, the Department of Justice, the Internal Revenue Service, and all branches of the DOD.

The Technology Services business area includes Logicon's base and range support work. This includes support of fielded systems, logistics support, data center management, systems engineering and networking, systems integration and facilities management services. Primary customers include the U.S. Army, U.S. Air Force, NASA, the Department of Energy and state and local government agencies.

The Commercial Information Technology business area is where Logicon directs its information systems offerings to the commercial market. This work includes hardware and software maintenance, help desk support, systems administration, network design, systems modernization and integration, and facility management services. Customers include Fortune 500 companies, IT outsourcing providers, original equipment manufacturers, integrators and resellers.

In the following table of segment and major customer data, revenue from the United States Government includes revenue from contracts on which Northrop Grumman is the prime contractor as well as those on which the company is a subcontractor and the ultimate customer is the U.S. Government. All of the data except for assets by segment have been restated to exclude discontinued operations.

RESULTS OF OPERATIONS BY SEGMENT AND MAJOR CUSTOMER

Years ended December 31, $ in millions		2000	1999	1998
Net Sales				
Integrated Systems				
	United States Government	$ 3,103	$ 3,574	$ 3,464
	Other customers	36	38	94
	Intersegment sales	11	6	5
		3,150	3,618	3,563
Electronic Sensors & Systems				
	United States Government	2,102	1,894	2,014
	Other customers	692	673	708
	Intersegment sales	121	146	177
		2,915	2,713	2,899
Logicon				
	United States Government	1,457	1,248	948
	Other customers	228	189	139
	Intersegment sales	32	22	20
		1,717	1,459	1,107
	Intersegment eliminations	(164)	(174)	(202)
	Total net sales	$ 7,618	$ 7,616	$ 7,367
Operating Margin				
	Integrated Systems	$ 316	$ 387	$ 272
	Electronic Sensors & Systems	181	199	218
	Logicon	104	80	60
		601	666	550

Adjustments to reconcile to total operating margin:			
Corporate expenses	(17)	(26)	(58)
Deferred state tax provision	(24)	(29)	(10)
Pension income	538	343	270
Total operating margin	$ 1,098	$ 954	$ 752

NORTHROP GRUMMAN CORPORATION

Years ended December 31, $ in millions	2000	1999	1998
Contract Acquisitions			
Integrated Systems	$ 2,979	$ 3,164	$ 2,489
Electronic Sensors & Systems	4,228	3,055	2,388
Logicon	2,018	1,481	1,205
Total acquisitions	$ 9,225	$ 7,700	$ 6,082
Funded Order Backlog			
Integrated Systems	$ 4,291	$ 4,451	$ 4,899
Electronic Sensors & Systems	4,873	3,439	2,951
Logicon	942	609	565
Total backlog	$ 10,106	$ 8,499	$ 8,415

Assets

Integrated Systems	$ 2,238	$ 3,497	$ 3,797
Electronic Sensors & Systems	4,069	3,883	3,913
Logicon	1,247	618	618
Segment assets	7,554	7,998	8,328
General corporate	2,068	1,287	1,208
Total assets	$ 9,622	$ 9,285	$ 9,536
Capital Expenditures			
Integrated Systems	$ 124	$ 56	$ 48
Electronic Sensors & Systems	118	97	82
Logicon	22	19	19
General corporate	1		
Total expenditures	$ 265	$ 172	$ 149
Depreciation and Amortization			
Integrated Systems	$ 112	$ 97	$ 108
Electronic Sensors & Systems	236	222	211
Logicon	32	32	38
General corporate	1	2	2
Total depreciation and amortization	$ 381	$ 353	$ 359

NORTHROP GRUMMAN CORPORATION

MEASURES OF VOLUME

Contract Acquisitions

Contract acquisitions tend to fluctuate from year to year and are determined by the size and timing of new and add-on orders. The variability resulting from multiyear orders and/or funding are reflected in the following table.

Contract Acquisitions

$ in millions	2000	1999	1998
Integrated Systems			
ACS	$ 1,720	$ 1,421	$ 1,428
AEW/EW	715	1,106	679
AGS/BM	576	686	434
Intrasegment eliminations	(21)	(43)	(47)
	2,990	3,170	2,494
Electronic Sensors & Systems			
Aerospace Electronic Systems	2,444	1,375	1,047
$C^3I\&N$	899	727	907
Defensive Electronic Systems	605	708	311
Other	422	308	225
	4,370	3,118	2,490
Logicon			
Government Information Technology	1,484	1,015	813
Technology Services	382	347	300
Commercial Information Technology	185	140	113
	2,051	1,502	1,226
Intersegment eliminations	(186)	(90)	(128)
Total acquisitions	$ 9,225	$ 7,700	$ 6,082

ISS acquisitions in 2000 were 6 percent lower than in 1999. The ACS business area in 2000 includes funding of $1.1 billion for the multiyear buy for 72 F/A-18E/F shipsets. The company received orders for 30 and 20 F/A-18E/F shipsets in 1999 and 1998, respectively. Acquisitions in 1998 included orders for 6 F/A-18C/D shipsets. The ACS business area recorded incremental B-2 funding for ongoing development work, spares and other customer support for the operational aircraft program in each of the last three years. The company still stands to gain future post production business, such as airframe depot maintenance, repair of components, operational software changes, and product improvement modifications. Two new programs were also captured by the ACS business area in 2000: VTUAV EMD and MP-RTIP program.

The AEW/EW business area includes funding for the multiyear buy for 25 E-2C aircraft of $247 million in 2000 and $679 million in 1999. The AGS/BM business area received orders for one, two and one Joint STARS aircraft in 2000, 1999 and 1998, respectively. The AGS/BM business area also captured the ALMDS EMD program in 2000.

ES^3 acquisitions in 2000 were 40 percent higher than in 1999. The Aerospace Electronic Systems business area received a $1.1 billion award in 2000 for the radar, electronic warfare systems, integrated FLIR targeting systems and common testers for United Arab Emirates (UAE) F-16 aircraft. This business area also received funding for the Longbow missile multiyear contract of $245 million in 2000 and $309 million in 1999 and funding on the BAT LRIP contract totaled $216 million in 1999. In the C^3I&N business area, a higher level of international awards for air defense systems was posted in 2000 than in 1999. The Defensive Electronic Systems business area recorded less funding in 2000 as compared to 1999 for the AN/ALQ-131 and AN/ALQ-165 programs. The increase in the "Other" business area is primarily due to increased orders for automation and information systems.

Logicon acquisitions increased by 37 percent in 2000 over 1999, reflecting increases in all three business areas. The increase in Government Information Technology acquisitions is primarily due to the acquisition of three new businesses: Federal Data Corporation, Sterling Software, Inc., and the Federal Systems unit of Comptek Research, Inc. In 1998 Logicon won the Joint Base Operations Support Contract (J-BOSC), which is reported in the Technology Services business area. Under this contract, which has a five-year basic performance period with a five-year option, the segment provides base operations support for NASA's Kennedy Space Center and the U.S. Air Force's 45th Space Wing, which includes Cape Canaveral Air Station and Patrick Air Force Base.

Sales

Year-to-year sales vary less than contract acquisitions and reflect performance under new and ongoing contracts.

Net Sales

$ in millions	2000	1999	1998

Integrated Systems			
ACS	$ 1,717	$ 2,059	$ 2,114
AEW/EW	780	888	780
AGS/BM	674	714	716
Intrasegment Eliminations	(21)	(43)	(47)
	3,150	3,618	3,563
Electronic Sensors & Systems			
Aerospace Electronic Systems	1,179	1,105	1,265
C^3I&N	902	843	904
Defensive Electronic Systems	511	536	544
Other	323	229	186
	2,915	2,713	2,899
Logicon			
Government Information Technology	1,181	971	787
Technology Services	381	346	213
Commercial Information Technology	155	142	107
	1,717	1,459	1,107
Intersegment eliminations	(164)	(174)	(202)
Total sales	$ 7,618	$ 7,616	$ 7,367

ISS segment sales decreased by 13 percent in 2000 as compared to 1999, reflecting decreases in all three business areas. The decreasing trend in ACS revenues is primarily attributable to the B-2 program, which decreased by $536 million in 2000 as compared to 1999, following an $86 million decrease in 1999 as compared to 1998. The production phase of the B-2 program was substantially completed in 2000; ongoing development work, spares and other customer support for the operational aircraft program will continue into 2001 and beyond. Current planning data indicate that the level of overall B-2 revenue for 2001 will decline by approximately 30 percent from the 2000 level.

Sales on the F/A-18 program increased by $147 million in 2000 as compared to 1999, which follows a $74 million increase in 1999 as compared to 1998. In 2000 the company delivered 28 shipsets under F/A-18E/F production contracts. In 1999 the last five shipsets were delivered under the F/A-18E/F LRIP contract and the first twelve shipsets were delivered under production contracts. The LRIP contract, which began in 1996 and was completed in 1999, was accounted for under the cost-to-cost type of percentage-of-completion method, resulting in revenue being recorded as costs are incurred. The production contracts are accounted for under the units-of-delivery method, which results in revenue being recorded as deliveries are made. In 1999 the last 17 shipsets of the C/D version of the F/A-18 were delivered; in 1998 34 shipsets were delivered. In 2001 the company plans to deliver 37 F/A-18E/F shipsets under production contracts.

Sales for unmanned systems increased by $113 million in 2000 as compared to 1999, primarily due to the purchase of Ryan Aeronautical, which occurred in July 1999.

AEW/EW sales decreased $108 million in 2000 as compared to 1999 primarily due to lower revenue on the E-2C and EA-6B programs. The sales increase in 1999 over 1998 was primarily due to increased EA-6B revenue. AGS/BM sales in 2000 were 6 percent lower than the level reported in 1999, reflecting lower Joint STARS revenue. Overall ISS revenue for 2001, excluding any effect of the pending Litton acquisition, is expected to be approximately $3 billion.

ES^3 segment sales increased by 7 percent in 2000 as compared to 1999, reflecting increases in three of the four business areas. Aerospace Electronics Systems business area increased sales are primarily due to higher Longbow revenues and higher UAE F-16 combat avionics systems sales. The increase in the C^3I&N business area reflects higher airspace management sales. Increased automation and information systems sales are the main reason for higher sales in the "Other" business area.

ES^3 segment sales declined by 6 percent in 1999 as compared to 1998. Lower Aerospace Electronic Systems business area sales were attributable to lower space systems and combat avionics systems sales. The C^3I&N business area reflected lower marine volume. The improvement in the "Other" business area was due to the inclusion of California Microwave Systems, which was acquired by Northrop Grumman in April 1999. For 2001, excluding any effect of the pending Litton acquisition, the company expects ESS segment sales to be approximately $3.5 billion.

Logicon sales increased by 18 percent in 2000 as compared to 1999 and by 32 percent in 1999 as compared to 1998. All three business areas improved in both 2000 and 1999 over prior year sales. The Government Information Technology business area increase in 2000 is primarily due to revenue generated by the three businesses acquired in 2000. The Technology Services business area increase in 2000 reflects higher J-BOSC sales.

The Government Information Technology and Commercial Information Technology business area improvements in 1999 reflect the higher level of acquisitions and higher win rate on contracts bid. Most of the additional sales generated in the Technology Services business area in 1999 are attributable to the commencement of work in the fourth quarter of 1998 on the J-BOSC contract, which was won earlier in that year. For 2001, excluding any effect of the pending Litton acquisition, the company expects Logicon sales to increase to approximately $2.5 billion.

Funded Order Backlog

The year-end funded order backlog is the sum of the previous year-end backlog plus the year's contract acquisitions minus the year's sales. Backlog is converted into the following years' sales as costs are incurred or deliveries are made. It is expected that approximately 63 percent of the 2000 year-end backlog will be converted into sales in 2001.

Funded Order Backlog

$ in millions	2000	1999	1998
Integrated Systems			
ACS	$ 2,363	$ 2,360	$ 2,998
AEW/EW	1,144	1,209	991
AGS/BM	784	882	910
	4,291	4,451	4,899
Electronic Sensors & Systems			
Aerospace Electronic Systems	3,026	1,761	1,491
C^3I&N	772	775	891
Defensive Electronic Systems	883	789	617
Other	298	199	120
	4,979	3,524	3,119
Logicon			
Government Information Technology	715	412	368
Technology Services	150	149	148
Commercial Information Technology	78	48	50
	943	609	566

Intersegment Eliminations	(107)	(85)	(169)
Total backlog	$ 10,106	$ 8,499	$ 8,415

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Total U.S. Government orders, including those made on behalf of foreign governments (FMS), comprised 75 percent of the backlog at the end of 2000 compared with 86 percent at the end of 1999 and 85 percent at the end of 1998. Total foreign customer orders, including FMS, accounted for 22 percent of the backlog at the end of 2000 compared with 16 percent in 1999 and 17 percent in 1998. Domestic commercial business in backlog was 5 percent at the end of 2000 and was 3 percent at the end of both 1999 and 1998.

MEASURES OF PERFORMANCE

The company's operating margin for 2000 was $1,098 million compared to $954 million for 1999 and $752 million for 1998.

ISS segment operating margin in 2000 was $316 million as compared to $387 million in 1999 and $272 million in 1998. In 2000 the ACS business area reported upward cumulative margin rate adjustments totaling $16 million on the F/A-18E/F program. In 1999 the ACS business area benefited from upward cumulative margin rate adjustments totaling $70 million on the B-2 program and $11 million on the F/A-18E/F program.

In 2000 the last three B-2's were delivered under the production contract as compared to five in 1999 and five in 1998. Following the award of the last increment of production funding for the B-2, the company began recording future operating margin increases on all production aircraft as these units were delivered and accepted by the customer. At the time each unit was delivered, an assessment was made of the status of the production contract to estimate the amount of any probable additional margin available beyond that previously recognized. That unit's proportionate share of any such unrecognized remaining balance was then recorded. The company believes that this method allowed margin improvements to be recognized on a more demonstrable basis. All 15 production units have been delivered.

ISS results for 2000 also reflect lower B-2 volume and the effect of nonrecurring relocation and realignment costs associated with the sale of the commercial aerostructures business and the relocation of the sector's headquarters, partially offset by improved Joint STARS operating margin. Since the beginning of the Joint STARS program, the company (and prior to 1994, the Grumman Corporation) as of December 31, 1998 had incurred over $100 million of costs in excess of revenues in the performance of the development and production phases of the program. Including support and other work, the company recorded on the Joint STARS program operating losses of $25 million and $29 million in 1998 and 1997, respectively. In 1998 the company submitted Requests for Equitable Adjustment (REAs) to the U.S. Air Force seeking adjustment to production contracts for cost increases incurred during the refurbishment and conversion of used Boeing 707 aircraft to Joint STARS platforms. The company and the U.S. Air Force executed an Alternate Dispute Resolution Agreement to attempt to resolve these REAs, and in April 1999 the company filed these

REAs as certified claims. In December 1999 the company reached a settlement of these contract claims with the U.S. Air Force, enabling the company to recognize the underlying improved performance on the production phase of this program. As a result, cumulative margin rate adjustments totaling $37 million were recorded in 1999. Revenue on the Joint STARS program is recognized using the cost-to-cost percentage-of-completion method of accounting.

ES^3 segment operating margin in 2000 was $181 million as compared to $199 million in 1999 and $218 million in 1998. The decrease in 2000 operating margin as compared to 1999 is primarily due to a reduction in pension-related margin. As described in more detail below, in July 1999 the company merged three of its pension plans into one, resulting in reduced pension-related margin beginning in July 1999. The decrease in 1999 operating margin as compared to 1998 is a result of lower sales volume as well as a reduction of approximately $44 million resulting from the pension plan merger. The decrease also reflects lower margins in the Defensive Electronic Systems business area, due in part to additional costs incurred in transitioning a development program to production. These reductions were partially offset by an upward cumulative margin adjustment following the wind down of an AWACS RSIP contract in 1999. ES^3 segment 1998 operating margin was reduced by a $21 million fourth quarter charge for estimated future costs not considered recoverable from future revenues on the DIRCM program. The charge resulted from increased costs associated with solving technical design issues as well as difficulties in achieving timely completion of the second series of live-fire tests on the large turret version.

Logicon operating margin in 2000 was $104 million as compared to $80 million in 1999 and $60 million in 1998. The increase in operating margin in 2000 over 1999 reflects higher sales volume in all three business areas and improved performance in both the Technology Services and Commercial Information Technology business areas. Logicon also benefited in 2000 by approximately $6 million from the merger of a defined benefit plan into the company's main pension plan, which is described in more detail below. The 1999 increase over 1998 is attributable to increased sales volume in all business areas and improved performance in the Technology Services business area. These improvements were partially offset by $4 million of nonrecurring charges related to employee termination costs and legal accruals. Logicon operating margin in 1998 was reduced by $8 million for consolidation and reorganization charges.

Operating margin in 2000 included $538 million of pension income compared with $343 million in 1999 and $270 million in 1998. These increases were driven by the high market returns on investments over the past several years. However in 2000, while Northrop Grumman's pension fund returns exceeded benchmark indices, they posted a negative return at slightly less than breakeven. As a result, pension income for 2001 is estimated to be between $250 million and $300 million.

In the first quarter of 2000, the company replaced several defined-contribution employee benefit plans, covering some of the Logicon employees, with a defined-benefit type plan. In December 2000 this plan was merged into the company's main pension plan, resulting in a pretax improvement to Logicon's operating margin of approximately $6 million and a reduction in cash contributions to benefit plans of approximately $20 million.

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In July 1999, in order to reduce future cash contributions, the company merged three of its retirement plans into one, to include the former Northrop Grumman Pension Plan, the Electronic Sensors and Systems Sector Employees Pension Plan (non-represented), and the Commercial Aircraft Employees Pension Plan (salaried). The pension plan merger does not result in any changes to any participant's existing pension benefits, nor does it alter individual plan designs. The retirement plan merger resulted in a reduction to 1999 net income of approximately $16 million, or $.24 per share.

Included in the 1998 results are pretax costs totaling $58 million related to activities to realign operating units, consolidate facilities and laboratories and exit certain business areas, which reduced operating margin by $43 million and other income by $15 million. The operating margin amount was reflected in segment results as follows: ISS, $6 million; ES^3, $13 million; and Logicon, $8 million. The remaining $16 million was included in Corporate expenses. The charge included $20 million for employee termination costs, $12 million for write-down to estimated fair value of assets available for sale, $3 million for losses on disposals of assets, $9 million for write-off of purchased intangible assets no longer considered recoverable from future revenues, $9 million for loss on sale of a business, and $5 million for excess capacity lease costs, net of estimated sublease income through 2008. The employee termination costs represent cash severance payments made to employees.

Capital assets are transferred to assets available for sale when a decision is made to sell the facility and selling efforts are actively underway. In some cases operations continue and, when costs are allowable under government contracts, depreciation expense is recorded until the facility is vacated or sold. In 2000 assets available for sale with a carrying value of $3 million were sold, excluding the sale of Aerostructures. In 1999 $2 million was transferred to assets available for sale and assets with a carrying value of $13 million were sold. In 1998 $37 million was transferred to assets available for sale, $2 million in depreciation expense on these assets was recorded, and assets with a carrying value of $46 million were sold. Assets available for sale are evaluated at least annually for recoverability and written down to estimated fair value as necessary. In 1998 a write down adjustment of $12 million was recorded. The assets available for sale at the end of 2000 are expected to be sold in 2001.

Interest income in 2000 was $29 million compared to $18 million in 1999 and $11 million in 1998. The increase in 2000 interest income over 1999 reflects interest earned on the temporary investment of excess cash and interest earned on the note received in partial payment for the sale of Aerostructures.

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On July 3, 1997, the company announced that it had entered into a definitive agreement with Lockheed Martin Corporation to combine the companies. On February 26, 1998, shareholders of Northrop Grumman approved the merger. On March 23, 1998, the U.S. Government filed suit to block the merger and on July 16, 1998, Lockheed Martin notified the company that it was terminating its merger agreement with the company pursuant to the terms of the agreement. The company recorded charges totaling $186 million in 1998 for costs related to the terminated merger. The charges cover vesting of restricted stock which became issuable following shareholder approval of the merger and other costs associated with the terminated merger, including investment banking fees, legal and accounting fees, and costs related to responding to the Government's request for information.

Interest expense for 2000 was $175 million, a $49 million decrease from 1999, which in turn was down $8 million from the 1998 level. The 1999 interest expense included $11 million related to settlement of various legal and tax issues. Total debt stood at $1.6 billion at the end of 2000 compared to $2.2 billion at the end of 1999 and $2.8 billion at the end of 1998.

Included in the 1998 results is a $30 million write-off of an investment related to Kistler Aerospace Corporation's K-1 program. The investment consisted of advances on behalf of Kistler Aerospace that were made in 1998 to continue the company's efforts in support of the K-1. The write off resulted from the company's assessment that the near-term likelihood of Kistler obtaining additional financing made recovery of the investment uncertain. The company has agreed to invest an additional $30 million in Kistler Aerospace Corporation preferred stock. This investment will only be made when Kistler Aerospace Corporation has obtained additional funding from other sources and will represent the last increment of funding required to complete and test the first K-1 vehicle, and is subject to the company's then determination that the K-1 is a viable launch system. No additional investments were made by the company in 2000 or 1999.

The company's effective federal income tax rate was 35.9 percent in 2000, 36.5 percent in 1999, and 37.5 percent in 1998.

Aerostructures income from discontinued operations, net of tax, was $39 million in 2000, $9 million in 1999, and $1 million in 1998. Included in these amounts are related pretax pension income(expense) of $22 million, $10 million, and $(4) million in 2000, 1999 and 1998, respectively.

The $56 million total after tax loss on the sale of Aerostructures recorded in 2000 includes the settlement and curtailment of various pension and other post-retirement benefit plans, the write-off of goodwill, and final assessment of the value of the promissory note received in partial payment.

Effective January 1, 1999, the company adopted the new accounting standard, SOP 98-5 - *Reporting on the Costs of Start-Up Activities*, which requires that certain costs that previously had been deferred be expensed and reported as a cumulative effect of a change in accounting principle. The company reported a $16 million after-tax charge, or $.24 per share, to write off the previously deferred start-up costs.

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MEASURES OF LIQUIDITY AND CAPITAL RESOURCES

In 2000 cash provided by operations was $1,010 million as compared to the $1,207 million generated in 1999 and the $244 million generated in 1998. The increased levels of cash generated by operations in 2000 and 1999 is attributable to many factors, the more significant of which are: increased operating margin, improved cash management of working capital, and lower pension plan contributions as a result of the pension plan mergers. In 2000 lower interest payments, reflecting the lower level of debt, and an increase in cash advances from customers also benefitted cash from operations. Accelerated cash collections, in part due to customers' Year 2000 concerns, contributed to 1999 cash from operations.

Net working capital (current assets less current liabilities) at December 31, 2000, was a negative $162 million, mainly due to current deferred tax liabilities. The largest component of current deferred tax liabilities is deferred tax expense related to long-term contracts. With the completion of the B-2 EMD contract, federal and state income taxes that have been deferred since the inception of the contract in 1981, will become payable. The contract is expected to be completed in 2002 with taxes of approximately $1 billion due, to be paid that year. The company plans to use cash generated from operations supplemented by additional borrowings under the credit agreement and/or additional borrowings from public or private capital markets to pay these taxes.

In 2000 cash generated by operating activities and the sale of Aerostructures provided sufficient cash flows to finance capital expenditures, pay dividends to shareholders, acquire new businesses for $510 million, and reduce net debt (total debt less cash balances) by $787 million. Cash generated from operating activities in 1999 was sufficient to finance capital expenditures, pay dividends to shareholders, acquire new businesses for $232 million in cash, and reduce net debt (total debt less cash balances) by $704 million.

The following table is a condensed summary of the detailed cash flow information contained in the Consolidated Statements of Cash Flows.

Years ended December 31,		2000	1999	1998
Cash came from				
	Customers	92%	98%	95%
	Lenders			3
	Buyers of assets/other	8	2	2
		100%	100%	100%
Cash went to				
	Employees and suppliers of services and materials	80%	84%	90%
	Sellers of assets	9	5	3
	Lenders	9	9	5
	Suppliers of facilities/other	1	1	1
	Shareholders	1	1	1
		100%	100%	100%

Cash used in investing activities was $78 million in 2000 compared to $392 million in 1999 and $235 million in 1998. The sale of Aerostructures in 2000 generated $668 million in cash. Four businesses were acquired in 2000, three for cash and one for stock, for a total cash expenditure of $510 million. In 1999 three businesses were acquired for cash of $232 million. For 2000 capital expenditures were $274 million, including $9 million for Aerostructures and $32 million for capitalized software costs. Capital expenditures in 1999 were $201 million, including $29 million for Aerostructures and $22 million for capitalized software costs. Capital expenditure commitments at December 31, 2000, were approximately $136 million, including $1 million for environmental control and compliance purposes. For 2001 capital expenditures are expected to be approximately $270 million, including approximately $36 million for capitalized software costs.

Cash used in financing activities was $755 million in 2000 compared to $717 million in 1999 and $28 million in 1998. The company has a credit agreement with a group of domestic and foreign banks to provide for $1.8 billion available on a revolving credit basis through March 2002. Under this credit agreement the company also had a variable interest rate term loan, with a balance of $450 million at December 31, 1999, payable in quarterly installments of $50 million plus interest through March 2002. The company repaid this term loan in 2000. In February 2001 the Company issued $1.5 billion of indebtedness pursuant to its senior debt indenture consisting of $750 million of 7-1/8% Notes due 2011 and $750 million of 7-3/4% Debentures due 2031. In connection with the closing of the Litton acquisition, the Company will enter into unsecured senior credit facilities with lenders which are anticipated to provide for borrowings of up to $4.5 billion (the "New Credit Facilities") and which will replace the Company's existing credit agreement. The New Credit Facilities are expected to consist of a $2.0 billion 364-day revolving credit facility and a $2.5 billion five-year revolving credit facility. Borrowings under the New Credit Facilities, together with the proceeds of the February issuance of notes and debentures, will be used to finance the Litton acquisition by the new holding company and pay related expenses, to refinance outstanding debt under the Company's existing credit agreement, to retire and refinance a portion of the existing Litton debt, and to finance the continuing operations of the Company, the new holding company and Litton. Borrowings under the New Credit Facilities will bear interest, at the borrower's option, at various rates of interest, including adjusted LIBOR or an alternate base rate plus in each case an incremental margin based on the combined company's credit rating. The New Credit Facilities also provide for a facility fee on the daily aggregate amount of commitments under the revolving facilities (whether or not utilized). The facility fee is also based on the combined company's credit rating level. The new holding company and Litton will be co-borrowers on the New Credit Facilities.

To provide for long-term liquidity the company believes it can obtain additional capital from such sources as: the public or private capital markets, the further sale of assets, sale and leaseback of operating assets, and leasing rather than purchasing new assets. Cash generated from operations, supplemented by borrowings under the credit agreement, are expected to be sufficient in 2001 to service debt, finance capital expansion projects, and continue paying dividends to the shareholders.

The company will continue to provide the productive capacity to perform its existing contracts, prepare for future contracts, and conduct R&D in the pursuit of developing opportunities. While these expenditures tend to limit short-term liquidity, they are made with the intention of improving the long-term growth and profitability of the company.

OTHER MATTERS

Environmental Issues

Federal, state and local laws relating to the protection of the environment affect the company's manufacturing operations. The company has provided for the estimated cost to complete remediation where the company has determined that it is probable that the company will incur such costs in the future, including those for which it has been named a Potentially Responsible Party (PRP) by the Environmental Protection Agency or similarly designated by other environmental agencies. The company has been designated a PRP under federal Superfund laws at 14 hazardous waste sites and under state Superfund laws at 10 sites. It is difficult to estimate the timing and ultimate amount of environmental cleanup costs to be incurred in the future due to the uncertainties regarding the extent of the required cleanup and the status of the law, regulations and their interpretations. Nonetheless, to assess the potential impact on the company's financial statements, management estimates the total reasonably possible remediation costs that could be incurred by the company. Such estimates take into consideration the professional judgment of the company's environmental engineers and, when necessary, consultation with outside environmental specialists. In most instances, only a range of reasonably possible costs can be estimated. However, in the determination of accruals, the most probable amount is used when determinable and the minimum is used when no single amount is more probable. The company records accruals for environmental cleanup costs in the accounting period in which the company's responsibility is established and the costs can be reasonably estimated. The company does not anticipate and record insurance recoveries before collection is probable. Management estimates that at December 31, 2000, the range of reasonably possible future costs for environmental remediation, including Superfund sites, is $69 million to $98 million, of which $79 million has been accrued. Should other PRPs not pay their allocable share of remediation costs, the company may have to incur costs in addition to those already estimated and accrued. The company is making the necessary investments to comply with environmental laws; the amounts, while not insignificant, are not considered material to the company's financial position, results of operations, or cash flows.

New Accounting Pronouncements

In December 1999 the Securities and Exchange Commission issued Staff Accounting Bulletin (SAB) No. 101 *Revenue Recognition in Financial Statements*. Since substantially all of the company's revenue is recognized in compliance with Statement of Position (SOP) No. 81-1 *Accounting for Performance of Construction-Type and Certain Production-Type Contracts* and SOP No. 97-2 *Software Revenue Recognition,* implementation of SAB No. 101 has no material effect on the company's results of operations or financial position.

In June 1998 the Financial Accounting Standards Board issued SFAS No. 133 - *Accounting for Derivative Instruments and Hedging Activities*, subsequently amended by SFAS No. 138 - *Accounting for Certain Derivative Instruments and Certain Hedging Activities* which becomes effective for fiscal years beginning after June 15, 2000. This standard provides authoritative guidance on accounting and financial reporting for derivative instruments. The company adopted this standard on January 1, 2001. Adoption of this standard is not expected to have any material effect on the company's financial position, results of operations, or cash flows.

FORWARD LOOKING STATEMENTS AND IMPORTANT FACTORS

Some of the information included in this Form 10-K and in other statements made by the Company are forward-looking statements within the meaning of the securities laws. These statements concern the Company's plans, expectations and objectives for future operations. These include statements and assumptions with respect to expected future revenues, margins, program performance, earnings and cash flows, acquisitions of new contracts, the outcome of competitions for new programs, the outcome of contingencies including litigation and environmental remediation, the effect of completed and planned acquisitions and divestitures of businesses or business assets, the anticipated costs of capital investments, and anticipated industry trends. The Company's actual results and trends may differ materially from the information, statements and assumptions as described, and actual results could be materially less than our planned results.

Important factors that could cause actual results to differ materially from those suggested by the Company's forward-looking statements include:

- The Company depends on a limited number of customers. The Company is heavily dependent on government contracts many of which are only partially funded; the termination or failure to fund one or more significant contracts could have a negative impact on our operations. The Company is a supplier, either directly or as a subcontractor or team member, to the U.S. Government and its agencies as well as foreign governments and agencies. These contracts are subject to each customers' political and budgetary constraints, changes in short-range and long-range plans, the timing of contract awards, the congressional budget authorization and appropriation processes, the government's ability to terminate contracts for convenience or for default, as well as other risks such as contractor suspension or debarment in the event of certain violations of legal and regulatory requirements.

- Many of the Company's contracts are fixed-price contracts. While firm, fixed-price contracts allow the Company to benefit from cost savings, they also expose the Company to the risk of cost overruns. If the Company's initial estimates used for calculating the contract price are incorrect, the Company can incur losses on those contracts. In addition, some of the Company's contracts have provisions relating to cost controls and audit rights and if the Company fails to meet the terms specified in those contracts then the Company may not realize their full benefits. The Company's ability to manage costs on these contracts may effect its financial condition. Lower earnings caused by cost overruns would have an adverse effect on the Company's financial results.

- The Company is subject to significant competition. The Company's markets include defense and commercial areas where we compete with companies of substantial size and resources. The Company's success or failure in winning new contracts or follow on orders for our existing or future products may cause material fluctuations in the Company's future revenues and operating results.

- The Company's operations may be subject to events that cause adverse effects on our ability to meet contract obligations within anticipated cost and time parameters. The Company may encounter internal problems and delays in delivery as a result of issues with respect to design, technology, licensing and patent rights, labor or materials and components that prevent the Company from achieving contract requirements. The Company may be affected by delivery or performance issues with key suppliers and subcontractors, as well as other factors inherent in the Company's businesses that may cause operating results to be adversely affected. Changes in inventory requirements or other production cost increases may also have a negative impact on the Company's operating results.

- The Company must integrate its acquisitions successfully. Acquiring businesses is a significant challenge. If the Company does not execute its acquisition and integration plans for these businesses in accordance with the Company's strategic timetable, the Company's operating results may be adversely affected. The Company acquired several businesses in 2000 and has agreed to acquire Litton. The Company believes its integration processes are well-suited to achieve the anticipated strategic and operating benefits of these acquisitions, but if the Company does not perform its plans as intended, or if the Company encounters unforeseen problems in the acquired businesses, or problems in those businesses develop subsequent to acquisition, the Company's operating results may be adversely affected. Among the factors that may be involved would be unforeseen costs and expenses, previously undisclosed liabilities, diversion of management focus, and any effects of complying with government-imposed organizational conflicts of interest rules as a result of the acquisitions.

- The Company relies on continuous innovation. The Company is dependent upon its ability to anticipate changing needs for defense products, military and civilian electronic systems and support, and information technology. The Company's success is dependent on designing new products that will respond to such requirements within customers' price limitations.

- The Company faces significant challenges in the international marketplace. The Company's international business is subject to changes in import and export policies, technology transfer restrictions, limitations imposed by United States law that are not applicable to foreign competitors, and other legal, financial and governmental risks.

- The Company assumes that any divestiture of non-core businesses and assets will be completed successfully. The Company's performance may be affected by its inability to successfully dispose of assets and businesses that do not fit with or are no longer appropriate to the Company's strategic plan. If any sales of such businesses or assets can be made only at a loss, the Company's earnings will be negatively impacted.

- The Company is subject to environmental litigation and other liabilities. Our performance may be affected by known environmental risks, pending litigation and other loss contingencies, if not resolved within the parameters of the Company's internal plans, and by unanticipated environmental or other liabilities.

- The Company's pension income may fluctuate significantly. Pension income, a non-cash item which is included in the company's earnings, is based on assumptions of market performance and actual performance may differ. If an event causes the Company to revalue its pension income during the calendar year, the portion of its earnings attributed to pension income could vary significantly.

- The indebtedness of the company, incurred and to be incurred in connection with the acquisition of Litton, is and will be higher than the indebtedness of the Company at December 31, 2000. The increase in debt will increase demands on the cash resources of the company after the Litton merger.

The Company intends that all forward-looking statements it makes will be subject to safe harbor protection of the federal securities laws as found in Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934.

Accordingly, you should not rely on the accuracy of predictions contained in forward-looking statements. These statements speak only as of the date when they are made. The Company cannot undertake any obligation to update its forward-looking statements to reflect events, circumstances, changes in expectations or the occurrence of unanticipated events occurring after the date of those statements.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

The company is exposed to market risk, primarily related to interest rates and foreign currency exchange rates. Financial instruments subject to interest rate risk include fixed-rate long-term debt obligations, variable-rate short-term debt outstanding under the credit agreement, short-term investments, and long-term notes receivable. Most of the fixed-rate long-term debt obligations are not callable until maturity. The company may enter into interest rate swap agreements to manage its exposure to interest rate fluctuations. At December 31, 2000, no interest rate swap agreements were in effect. The company enters into foreign currency forward contracts to manage foreign currency exchange rate risk related to receipts from customers and payments to suppliers denominated in foreign currencies. At December 31, 2000, the amount of foreign currency forward contracts outstanding was not material. The company does not consider the market risk exposure relating to foreign currency exchange to be material. The company does not hold or issue derivative financial instruments for trading purposes.

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Item 8. Financial Statements and Supplementary Data

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

December 31, $ in millions	2000	1999
Assets:		
Current assets		
Cash and cash equivalents	$ 319	$ 142
Accounts receivable	1,557	1,402
Inventoried costs	585	1,190
Deferred income taxes	21	23
Prepaid expenses and other current assets	44	36
Total current assets	2,526	2,793

Property, plant and equipment at cost		
Land and land improvements	144	163
Buildings	700	777
Machinery and other equipment	1,444	1,860
Leasehold improvements	55	95
	2,343	2,895
Accumulated depreciation	(1,328)	(1,655)
	1,015	1,240
Other assets		
Notes receivable	135	
Goodwill, net of accumulated amortization of $534 in 2000 and $441 in 1999	3,801	3,469
Other purchased intangibles, net of accumulated amortization of $467 in 2000 and $388 in 1999	631	761
Prepaid retiree benefits cost, and intangible pension asset	1,390	888
Assets available for sale	23	26
Miscellaneous other assets	101	108
	6,081	5,252
	$ 9,622	$ 9,285

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December 31, $ in millions	2000	1999
Liabilities and Shareholders' Equity:		
Current liabilities		
Notes payable to banks	$	$ 25
Current portion of long-term debt	10	200
Trade accounts payable	564	490
Accrued employees' compensation	365	366
Advances on contracts	496	316
Income taxes payable	86	58
Deferred income taxes	681	550
Other current liabilities	486	459
Total current liabilities	2,688	2,464
Long-term debt	1,605	2,000
Accrued retiree benefits	1,095	1,458
Other long-term liabilities	39	42
Deferred income taxes	276	64
Shareholders' equity		
Paid-in capital		
Preferred stock, 10,000,000 shares authorized; none issued		
Common stock, 200,000,000 shares authorized; issued and outstanding: 2000 - 72,058,436 1999 - 69,719,164	1,200	1,028
Retained earnings	2,742	2,248
Accumulated other comprehensive loss	(23)	(19)
	3,919	3,257
	$ 9,622	$ 9,285

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

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CONSOLIDATED STATEMENTS OF INCOME

Years ended December 31, $ in millions, except per share	2000	1999	1998
Sales and service revenues			
Product sales	$ 6,133	$ 6,304	$ 6,381
Service revenues	1,485	1,312	986
Total revenue	7,618	7,616	7,367
Cost of sales			
Cost of product sales	4,160	4,491	4,737
Cost of service revenues	1,286	1,143	867
Administrative and general expenses	1,074	1,028	1,011
Operating margin	1,098	954	752
Other income(deductions)			
Interest income	29	18	11
Merger costs			(186)
Interest expense	(175)	(224)	(232)
Investment loss			(30)
Other, net	23	(1)	(6)
Income from continuing operations before income taxes and cumulative effect of accounting change	975	747	309
Federal and foreign income taxes	350	273	116

Income from continuing operations before cumulative effect of accounting change	625	474	193
Income from discontinued operations, net of federal income tax expense of $22, $6 and $2 in 2000, 1999 and 1998, respectively	39	9	1
Loss on disposal of discontinued operations, net of federal income tax expense of $40	(56)		
Income before cumulative effect of accounting change	608	483	194
Cumulative effect of accounting change, net of income tax benefit of $11		(16)	
Net income	$ 608	$ 467	