

Q1 2018 Earnings Release

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Allison Transmission’s business is subject to numerous risks and uncertainties, which may cause future results of operations to vary significantly from those presented herein. Important factors that could cause actual results to differ materially are discussed in Allison Transmission’s Annual Report on Form 10-K for the year ended December 31, 2017.

Non-GAAP Financial Information

We use Adjusted EBITDA and Adjusted EBITDA as a percent of net sales to measure our operating profitability. We believe that Adjusted EBITDA and Adjusted EBITDA as a percent of net sales provide management, investors and creditors with useful measures of the operational results of our business and increase the period-to-period comparability of our operating profitability and comparability with other companies. Adjusted EBITDA as a percent of net sales is also used in the calculation of management's incentive compensation program. The most directly comparable U.S. generally accepted accounting principles ("GAAP") measure to Adjusted EBITDA is Net income. Adjusted EBITDA is calculated as the earnings before interest expense, income tax expense, amortization of intangible assets, depreciation of property, plant and equipment and other adjustments as defined by Allison Transmission, Inc.'s, the Company's wholly-owned subsidiary, Senior Secured Credit Facility.

We use Adjusted Free Cash Flow to evaluate the amount of cash generated by our business that, after the capital investment needed to maintain and grow our business and certain mandatory debt service requirements, can be used for repayment of debt, stockholder distributions and strategic opportunities. We believe that Adjusted Free Cash Flow enhances the understanding of the cash flows of our business for management, investors and creditors. Adjusted Free Cash Flow is also used in the calculation of management's incentive compensation program. The most directly comparable GAAP measure to Adjusted Free Cash Flow is Net cash provided by operating activities. Adjusted Free Cash Flow is calculated as Net cash provided by operating activities after additions of long-lived assets and certain other adjustments.

Call Agenda

- **Q1 2018 Performance**
- **2018 Guidance Update**

Q1 2018 Performance Summary

(\$ in millions)	Q1 2018	Q1 2017	% Variance
Net Sales	\$663	\$499	32.9%
Gross Margin %	51.6%	50.3%	130 bps
Net Income	\$151	\$83	81.9%
Adjusted EBITDA ⁽¹⁾	\$275	\$192	43.2%

Commentary

Net Sales: increase was principally driven by higher demand in the Global On-Highway, Service Parts, Support Equipment & Other and Global Off-Highway end markets.

Gross Margin: increase was principally driven by increased net sales and price increases on certain products partially offset by expenses related to a retirement incentive program for certain UAW Local 933 employees and unfavorable material cost.

Net Income: increase was principally driven by increased gross profit and decreased income tax expense partially offset by increased selling, general and administrative expenses, increased product initiatives spending and increased interest expense.

Adjusted EBITDA: increase was principally driven by increased net sales and price increases on certain products partially offset by increased selling, general and administrative expenses, increased manufacturing expense commensurate with increased net sales, increased product initiatives spending and unfavorable material cost.

(1) See Appendix for a reconciliation of Adjusted EBITDA.

Q1 2018 Sales Performance

(\$ in millions)

End Markets	Q1 2018	Q1 2017	% Variance	Commentary
North America On-Hwy	\$315	\$255	24%	Principally driven by higher demand for Rugged Duty Series models
North America Electric Hybrid-Propulsion Systems for Transit Bus	\$24	\$20	20%	Principally driven by the timing of certain transit property orders
North America Off-Hwy	\$33	\$1	3200%	Principally driven by higher demand from hydraulic fracturing applications
Defense	\$37	\$27	37%	Principally driven by higher Tracked and Wheeled demand
Outside North America On-Hwy	\$91	\$72	26%	Principally driven by higher demand in Europe, Asia and South America
Outside North America Off-Hwy	\$12	\$6	100%	Principally driven by improved demand in the mining and construction sectors
Service Parts, Support Equipment & Other	\$151	\$118	28%	Principally driven by higher demand for North America Off-Highway service parts and global support equipment
Total	\$663	\$499	33%	

Q1 2018 Financial Performance

(\$ in millions, except per share data)	Q1 2018	Q1 2017	\$ Var	% Var	Commentary
Net Sales	\$663	\$499	\$164	32.9%	Increase was principally driven by higher demand in the Global On-Highway, Service Parts, Support Equipment & Other and Global Off-Highway end markets
Cost of Sales	\$321	\$248	(\$73)	(29.4%)	
Gross Profit	\$342	\$251	\$91	36.3%	Increase was principally driven by increased net sales and price increases on certain products partially offset by expenses related to a retirement incentive program for certain UAW Local 933 employees, higher manufacturing expense commensurate with increased net sales and unfavorable material cost
Operating Expenses					
Selling, General and Administrative	\$92	\$79	(\$13)	(16.5%)	Increase was principally driven by unfavorable product warranty adjustments and higher warranty expense commensurate with increased net sales partially offset by lower incentive compensation expense
Engineering – Research and Development	\$28	\$23	(\$5)	(21.7%)	Increase was principally driven by increased product initiatives spending
Total Operating Expenses	\$120	\$102	(\$18)	(17.6%)	
Operating Income	\$222	\$149	\$73	49.0%	
Interest Expense, net	(\$30)	(\$25)	(\$5)	(20.0%)	Increase was principally driven by interest expense for 4.75% Senior Notes due October 2027
Other (Expense) Income, net	(\$1)	\$3	(\$4)	(133.3%)	Change was principally driven by unfavorable changes in foreign exchange on intercompany financing, partially offset by net periodic benefit credits related to postretirement benefit plan amendments
Income Before Income Taxes	\$191	\$127	\$64	50.4%	
Income Tax Expense	(\$40)	(\$44)	\$4	9.1%	Decrease in the effective tax rate was principally driven by the U.S. Tax Cuts and Jobs Act enacted into law in December 2017
Net Income	\$151	\$83	\$68	81.9%	
Diluted Earnings Per Share	\$1.08	\$0.52	\$0.56	107.7%	Q1 2018: 140M shares; Q1 2017: 159M shares
Adjusted EBITDA ⁽¹⁾	\$275	\$192	\$83	43.2%	

(1) See appendix for the reconciliation from Net Income.

Q1 2018 Cash Flow Performance

(\$ in millions)	Q1 2018	Q1 2017	\$ Variance	% Variance	Commentary
Net Cash Provided by Operating Activities	\$153	\$111	\$42	37.8%	Principally driven by increased gross profit, higher accounts payable, decreased cash interest expense and decreased cash income taxes partially offset by higher accounts receivable, increased incentive compensation payments and increased product initiatives spending
CapEx	\$10	\$8	\$2	25.0%	
Adjusted Free Cash Flow ⁽¹⁾	\$143	\$103	\$40	38.8%	Due to increased Net Cash Provided by Operating Activities partially offset by increased capital expenditures

(\$ in millions)	Q1 2018	Q1 2017	\$ Variance	% Variance	Commentary
Operating Working Capital ⁽²⁾ Percentage of LTM Sales	11.6%	12.6%	N/A	(100 Bps)	Principally driven by higher net sales partially offset by increased operating working capital commensurate with increased net sales
Cash Paid for Interest	\$10	\$14	(\$4)	(28.6%)	Principally driven by Q1 2017 interest rate hedging settlement payments for contracts which were terminated in December 2017
Cash Paid for Income Taxes	\$1	\$3	(\$2)	(66.7%)	Principally driven by timing of payments

(1) See Appendix for a reconciliation of Adjusted Free Cash Flow.

(2) Operating Working Capital = A/R + Inventory – A/P.

2018 Guidance Update

	Guidance	Commentary
Net Sales Change from 2017	10 to 14 percent	Guidance reflects stronger demand for Global On-Highway products and Global Off-Highway products and price increases on certain products
Net Income (\$ in millions)	\$515 to \$550	
Adjusted EBITDA (\$ in millions)	\$975 to \$1,025	
Net Cash provided by Operating Activities (\$ in millions)	\$720 to \$760	
CapEx (\$ in millions)	\$85 to \$95	Subject to timely completion of development and sourcing milestones
Adjusted Free Cash Flow (\$ in millions)	\$625 to \$675	Net Cash Provided by Operating Activities less CapEx
Cash Income Taxes (\$ in millions)	\$80 to \$90	

APPENDIX

Non-GAAP Financial Information

Non-GAAP Reconciliations (1 of 3)

Adjusted EBITDA reconciliation

\$ in millions, Unaudited	For the year ended December 31,					Three months ended		Last twelve
						March 31,		months ended
	2013	2014	2015	2016	2017	2017	2018	March 31,
	2013	2014	2015	2016	2017	2017	2018	2018
Net income (GAAP)	\$165	\$229	\$182	\$215	\$504	\$83	\$151	\$572
plus:								
Interest expense, net	133	138	114	101	103	25	30	108
Income tax expense	101	139	107	126	23	44	40	19
Technology-related investment expenses	5	2	—	1	16	—	—	16
Public offering expenses	2	1	—	—	—	—	—	—
Impairments	—	15	81	—	32	—	—	32
Environmental remediation	—	—	14	—	—	—	—	—
Amortization of intangible assets	105	99	97	92	90	22	22	90
Depreciation of property, plant and equipment	99	94	88	84	80	19	20	81
Loss on redemptions and repayments of long-term debt	1	1	1	—	—	—	—	—
Stockholder activism expenses	—	—	—	4	—	—	—	—
Dual power inverter module extended coverage	(2)	1	(2)	1	(2)	—	—	(2)
UAW Local 933 signing bonus	—	—	—	—	10	—	—	10
UAW Local 933 retirement incentive	—	—	—	—	—	—	7	7
Unrealized loss (gain) on commodity hedge contracts	2	(1)	1	(2)	—	(1)	—	1
Unrealized loss (gain) on foreign exchange	2	5	1	1	—	(2)	2	4
Expenses related to long-term debt refinancing	—	—	25	12	—	—	—	—
Restructuring charges	1	1	—	—	—	—	—	—
Stock-based compensation expense	13	15	11	9	12	2	3	13
Adjusted EBITDA (non-GAAP)	\$627	\$739	\$720	\$644	\$868	\$192	\$275	\$951
Net Sales (GAAP)	\$1,927	\$2,127	\$1,986	\$1,840	\$2,262	\$499	\$663	\$2,426
Net income as a percent of net sales	8.6%	10.8%	9.2%	11.7%	22.3%	16.6%	22.8%	23.6%
Adjusted EBITDA as a percent of net sales	32.5%	34.7%	36.2%	35.0%	38.4%	38.5%	41.5%	39.2%

Non-GAAP Reconciliations (2 of 3)

Adjusted Free Cash Flow reconciliation

\$ in millions, Unaudited	For the year ended December 31,					Three months ended March 31,		Last twelve months ended March 31,
	2013	2014	2015	2016	2017	2017	2018	2018
Net Cash Provided by Operating Activities (GAAP)	\$464	\$573	\$580	\$591	\$658	\$111	\$153	\$700
(Deductions) or Additions:								
Long-lived assets	(75)	(64)	(58)	(71)	(91)	(8)	(10)	(93)
Technology-related license expenses	6	6	—	—	—	—	—	—
Stockholder activism expenses	—	—	—	4	—	—	—	—
Excess tax benefit from stock-based compensation	14	25	8	6	—	—	—	—
Adjusted Free Cash Flow (non-GAAP)	\$409	\$540	\$530	\$530	\$567	\$103	\$143	\$607

Non-GAAP Reconciliations (3 of 3)

Guidance reconciliation

\$ in millions	Guidance	
	Year Ending December 31, 2018	
	Low	High
Net Income (GAAP)	\$ 515	\$ 550
plus:		
Income tax expense	144	154
Interest expense, net	118	123
Depreciation and amortization	168	168
UAW Local 933 retirement incentive (a)	15	15
Stock-based compensation expense (b)	13	13
Unrealized loss on foreign exchange (c)	2	2
Adjusted EBITDA (Non-GAAP)	<u>\$ 975</u>	<u>\$ 1,025</u>
Net Cash Provided by Operating Activities (GAAP)	\$ 720	\$ 760
Deductions to Reconcile to Adjusted Free Cash Flow:		
Additions of long-lived assets	(95)	(85)
Adjusted Free Cash Flow (Non-GAAP)	<u>\$ 625</u>	<u>\$ 675</u>

(a) Represents a charge (recorded in Cost of sales) related to a retirement incentive program for certain employees represented by the International Union, United Automobile, Aerospace and Agricultural Implement Workers of America ("UAW") pursuant to the UAW Local 933 collective bargaining agreement effective through November 2023.

(b) Represents stock-based compensation expense (recorded in Cost of sales, Selling, general and administrative, and Engineering – research and development).

(c) Represents losses (recorded in Other (expense) income, net) on intercompany financing transactions related to investments in plant assets for our India facility.