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Greg Konrad, Analyst, Jefferies LLC

Good morning. I'm Greg Konrad, Vice President of Equity Research at Jefferies with Howard Rubel. And I'm a very excited to have Paul Lundstrom, VP and CFO of Aerojet Rocketdyne with us today. He'll start by giving a short presentation and then we'll do some questions and open it up to the audience afterwards. Thanks, Paul.

Paul R. Lundstrom, Vice President & Chief Financial Officer

Okay. Thanks, Greg, and happy to be here. So before we get into the some – a couple prepared remarks and the Q&A. I just want to make a couple comments regarding forward-looking statements. There will be some, both in the prepared remarks as well as in the Q&A. We'll also likely reference some non-GAAP measures, so sort of keep in mind. Any other questions on those disclosures, you can go to aerojet.com, into the Investor Relations section where we have all this material posted. I'll also note that this is being webcast so that everybody has access to the same information at the same time.

So a couple comments, just overall company information for those of you unfamiliar. Aerojet Rocketdyne is a technology-driven manufacturing company. We focus on propulsion and power for space and missile systems. 2016 revenue was about \$1.8 billion. We're on our way up; looking like over the next couple of years we'll be closer to \$2 billion, balanced space and defense portfolio that is strongly aligned with DoD and NASA priorities.

And I'd say over the last couple of decades, we have accumulated excess real estate in Northern California that is non-core to our aerospace operations and we're looking to monetize that as quickly as we can. I will say it does take some time, though. Looking at

the business, for those following along on the webcast, I'm on Slide 4; two broad categories for this business: space and defense.

On the space side, we have the largest portfolio of space propulsion and power systems in the U.S., a wide range from ultra-heavy lift – I say ultra-heavy lift, like 800,000 pounds of thrust, pretty incredible, to almost imperceptible in-orbit repositioning systems that you might find on satellites. We've been part of the U.S. space program since its inception in the late 1950s and that will continue in 2019 when the U.S. resumes manned missions.

On the defense side, great breadth in this portfolio as well; I would say very importantly with U.S. budget dollars allocated to them. FMS sales as well; that's foreign military sales as well, top of mind programs, you very likely heard of our standard missile: TOW, Stinger, Patriot and one that's getting a lot of news lately very important to the DoD and also for our company and that's THAAD, a lot of systems on THAAD.

In terms of positioning, I'd say very well positioned. We have a solid base of core programs; again very closely aligned with our customers. If you look at the top of Slide 6: THAAD and SLS programs; SLS that would be the RS-25 engine, which is a derivative of the space shuttle main engine and then RL10, very strong programs for us. Those two between THAAD and SLS generated about 26% of our overall volume last quarter, very strong. Next-gen programs on the horizon over the next couple years that we're excited about.

GBSD: that stands for Ground Based Strategic Deterrent; that's the replacement to the Minuteman fleet; hypersonics is getting a lot of press lately. We are very much part of those future programs. And then the XS-1 or now I think it's XSP. It is the experimental spaceplane. There's a partnership between Boeing and DARPA to create this new spaceplane exciting mission. We're part of that as the main engine provider by the way with reusable technology, so very interesting to see, potentially very bright future.

In terms of our core operations, the good news is we have all the critical mass to do this stuff. We're U.S. based. All our operations are here in the U.S. We span the country. On real estate and our operations, you probably have heard us talk about the competitive improvement program. It's a cost out plan that the company announced in 2015. We announced the second wave of that program in the middle of the second quarter of this year.

Goal is continuing to take cost out of the structure, make ourselves as affordable as possible. This next wave of the CIP program: goal would be taking about \$85 million of cost out. You lump that together with the broader CIP program that was announced a couple years ago. We would be theoretically saving \$230 million on a run rate basis by the time we get out to 2021. I would say that's very much on track. We feel pretty good about it.

Couple comments on the financials before we get into the Q&A. First half looks quite strong, sales growth robust. Overall, we're up about 13% to \$865 million. A couple of points of that growth came from M&A that was the tuck-in of the Coleman Aerospace acquisition that we announced in the first quarter. If you look at what's fueling the growth right now, it's funny – there's this press about defense. It's not actually defense at the moment. It's NASA. NASA work is quite strong. I mentioned a couple minutes ago that the SLS program, that's Space Launch System program, has been strong.

It was 16% of sales in the first half and that's up from 12% in the first half a year ago. You just do the math on a dollar basis, that's about 50% growth for the SLS program, very, very strong. If you look at commercial crew, also a NASA program, that's been strong as well. It looks like that's going to continue as we move into the second half, so good to see from a top-line perspective, not exactly how I would have thought it would have played out if I look back four, five, six months ago. My thought would be it would probably be a little bit more balanced between 2017 and 2018.

So as I look ahead to 2018, we're going to have some pressure on the comps, but again, all good to see that now rather than later sort of proves the story, so happy about that. Other caution statement I would make is: if you think about the margin drop through from growth from development programs, drop through tends to be a little bit lower. So, again as I look to the second half, you want to think about that if we continue to have strong growth from development, the margin mix might not be all that good.

A couple comments on earnings on the next page: EPS was solid in the quarter also in the half. If you look at Adjusted EBITDAP, which is one of our profit metrics up 21% in the half with 80 basis points of margin expansion very nice to see that sort of progress.

A lot of that earnings growth on a dollar basis came from favorable contract adjustments in the half that was about \$14 million or \$0.17 on an EPS basis. The tailwind came from overhead under runs. I think we're seeing some benefits of the CIP program; that's good news. But we also had some other programmatic cost and risk reductions, which helped.

If you look at our business, a significant portion of our fixed price contracts, we recognize revenue on a percentage of completion basis which means you have re-estimates from time-to-time. We had good news re-estimates in the second quarter. It doesn't always go that way. We had some pretty significant favorable EAC adjustments in the fourth quarter of last year. You will want to think about that as you look ahead to the fourth quarter comps, but I'd say right now all good, quite happy with our progress.

In terms of recent accomplishments on Slide 10, a lot of activity in the business right now; first on AR1, you've likely heard about the congressional mandate to eliminate U.S. DoD reliance on the Russian engines, the RD180s. AR1 is our answer. We had a successful CDR a couple of months ago. I think that was back in May. CDR stands for

critical design review. It's essentially an independent technical review, the grades of a program's readiness to move forward.

At this point, we feel very confident in our planned performance for this program and its ability to meet cost schedule and risk requirements. So, if you're really good about AR1 and where we are at least in terms of the technical progress of the engine XSP or XS-1--, you may have heard is the experimental spaceplane I mentioned a couple of minutes ago. And then again that's the partnership between Boeing and DARPA for this next-gen experimental spaceplane goal; it would be rapid launch responsiveness.

For DoD, essentially put as many assets into space in a short amount of time, as we can. I think the goal right now is ten launches in ten days, which would be unheard of and very much game changing. So, very nice to see that program again; we have the main engine, which is reusable.

A lot of news lately, given all the sabre-rattling on missile defense, we've had some very successful tests over the last few months. One, end of May, was the EKV test. That was for the ground-based Midcourse Defense Program. We had a successful intercept. It was our DACS system on the EKV. Apologies for all the acronyms. DACS is Divert and Attitude Control System; the EKV is the Exoatmospheric Kill Vehicle. It's essentially what's at the tip of the interceptor that creates that collision to take out the ballistic missile.

THAAD has been in the news a lot lately. We had another successful intercept test on July 30, just a little over a week ago. That was a very interesting test from our perspective. Any of these, any of these intercepts are interesting. This one in particular was a medium range ballistic missile, but we were on both ends of the collision.

If you recall, we acquired Coleman Aerospace back in the first quarter. Coleman Aerospace provides targets for intercepts like these. Basically, it's target practice for the Missile Defense Agency. So it was a Coleman Aerospace ballistic missile that was dropped out of the back of a C-17; it fired-off a THAAD interceptor, took out that target in a violent successful collision. It didn't end well for either of our products but it ended very well for the customers and also for our shareholders, because it yet again proves that THAAD is an absolutely world-class missile defense system. So very, very good to see that.

And then lastly, just a couple of comments on our stock: Look, why get into the company? I'll say new leadership team redefining the path to success. We're very excited and energized about the future of this company. We have a very solid industry foundation, strong technological leadership, diversified, well-balanced portfolio. We have made and continue to make significant operational improvements in the business. I referenced the competitive improvement program that we're working on today.

And then lastly very much focused on revenue and profitability growth, ultimate goal is continuing to drive shareholder value. So with that, maybe Greg and I have a seat.

Greg Konrad, Analyst, Jefferies LLC

I mean the stock has done exceptionally well since you joined, so I mean, I attribute most of that to you. Just one thing that you said that stood out was that you're the largest portfolio of space propulsion and it seems SpaceX is still in a lot of the headlines. They're kind of the new entrant; maybe talk a little bit about how that defines the strategy going forward or change kind of the way you go to market a bit?

Paul R. Lundstrom, Vice President & Chief Financial Officer

So SpaceX, rightfully so gets a lot of press. I would say they do a very good job marketing as well, but with commercial entrants into the aerospace and defense market, the rocket business in particular, it's not just SpaceX, it's Blue Origin as well and there's a couple of others; it's put pressure on some of the old school legacy aerospace and defense companies because they don't bring with them all the decades of cost baggage frankly. They don't have pension plans, they don't have environmental liabilities, they don't necessarily have the infrastructure that is typically required to be a DoD contractor – CAS, TINA compliance, FAR compliance -- all that stuff they don't bring with them. And so that's put pressure on aerospace defense companies like Aerojet Rocketdyne, and we've responded.

You look at what we launched back in 2015 that was the competitive improvement program that I referenced a couple of minutes ago. I wouldn't say that was a direct response to SpaceX and Blue Origin, but it's certainly helped to move it along. Goal is, look, we have to be as competitive as we possibly can be. We have to continue to work to take cost out of the structure. And that's what we're doing with the CIP program. You look at a business our size, last year I mentioned, we were \$1.8 billion.

Over the next few years we're going to take \$240 million of cost out of the system. That's incredible. And so certainly on a percentage basis that's incredible, and again, goal being we're trying to make ourselves as competitive as we can be within the confines of being a DOD contractor. So we can continue to win work going forward.

Greg Konrad, Analyst, Jefferies LLC

That makes sense. And I guess one of the places where you're directly competing with these new entrants is the RD-180 replacement competing with Blue Origin. How do you kind of handicap that competition and kind of your offering versus what Blue Origin

brings to the table.

Paul R. Lundstrom, Vice President & Chief Financial Officer

Yeah, so for those unfamiliar with the competition or what that engine is, so the RD-180 is a Russian-built engine, it's the booster engine for the Atlas V. And so today if you look at U.S. DoD national security missions, we're using Russian engines for those missions. And if you go back to 2014 when Russia invaded Crimea, there was a congressional mandate that came out that basically said: look, enough. We can no longer rely on Russian-built engines for U.S. national security missions. So there's essentially a mandate in place that says, by the time you get to 2019 you have to be using U.S.-built products, okay. So it kicks off this competition.

The AR1 offering, which is the Aerojet Rocketdyne offering, was designed to be a direct replacement to the RD-180. And so what that means is, with as a little cost as possible that engine can directly replace the RD-180, which means same launch vehicle, same pad, same infrastructure, same propellant, it's a LOX or liquid oxygen, kerosene fuel booster. Contrast that with the Blue Origin option; it's a completely new system. It's also a new engine but it's a liquid oxygen methane, which is different. Which means you need a brand new launch vehicle, you need a new launch pad, you need new infrastructure.

And so the goal of the AR1 program was let's do this in a very tight cost envelope without a whole bunch of incremental investment required, no new launch vehicle, no new launch pad, you can use the existing Atlas launch vehicle to power these national security missions. Blue Origin is everything, is going to be new. And so you asked how do I handicap it? At this point all the press would suggest that Blue Origin and their BE-4 offering is the heir apparent. I would just ask, okay that's fine. And if that's the case and that's ULA and the Air Force's decision, that's fine. We support them, they're fantastic customers, we want them to be successful, we want to partnership with them.

But me, Paul Lundstrom, I would independently just say, okay fine. Who's going to pay for the launch vehicle and the pad? All that's incremental cost. Someone is going to have to pay for it. And if getting off that Russian engine by 2019 is the objective, how are we going to meet schedule if no one is working on that new launch vehicle or all that infrastructure?

So I know it's going to be interesting to launch right now. And like I said, it looks like the BE-4 is the heir apparent, but we stand by, ready as the backup engine. If we're selected, which we would love to be, we'll move forward and hopefully help the U.S. with those missions for many years to come.

Greg Konrad, Analyst, Jefferies LLC

And just one follow-up on that line of questioning: How important is the development versus the production? We're talking about the development phase you'll have a decision going forward from 2019 on. How complicated is the production part of any program as it transitions from development?

Paul R. Lundstrom, Vice President & Chief Financial Officer

Well, if you're going to – it's a really good question, Greg. I'm glad you asked. If you look at a rocket engine production program, particularly one that is going to be used for DoD, you need a certified rocket factory. We have one; not everyone does. I'll just say it like that. So we could produce the ARI today. Not everybody can do that.

And so how difficult is it to do a full-on production program? It's extremely difficult. I mean we've been doing that since the 1950s with the launch of the U.S. space program, not everybody has. And I'll just say there are years and years of standard work, and learning and legacy really does help on a run rate production program, experience matters.

Greg Konrad, Analyst, Jefferies LLC

And then last quarter was a little surprising to see NASA driving a lot of the growth, you working under \$1 billion plus contracts for the Space Launch System. Where is that program relative to the contract? And how large do you think that program can be?

Paul R. Lundstrom, Vice President & Chief Financial Officer

So Space Launch System is a very exciting potential for us. Right now I would say it's running at a fever pitch. What I think is exciting about it, Greg, is right now that Space Launch System, I think, they're talking about one mission every other year. So you think about it as half a launch per year. The potential to grow that from our perspective, and as we think about our longer-term strategic plan, if they change that to just one launch a year, we're up, we double on that SLS. You go to two launches a year, it's just incredible.

So where are we in terms of program? Look, we're running through the development phase right now, right now it's at a fever pitch. The outlook is one launch every other year to the extent they can take that number up that would be upside for us, but look it's a big, huge future program that has tremendous potential.

Greg Konrad, Analyst, Jefferies LLC

And then just transitioning to defense, I mean, I'm a little bit surprised to see the main missile defense programs down in Q2. Can you maybe talk kind of about the outlook there and as we progress it seems like a lot of these programs from a volume perspective is up, how that kind of relates to your outlook for those programs?

Paul R. Lundstrom, Vice President & Chief Financial Officer

Yes, so everything you've seen in news with all the sabre-rattling and intercept tests and all that stuff sort of makes everyone think that the missile defense business is going to be up 20% this year; that's not the case. I wouldn't be the least bit concerned about a little bit of softness that we've seen in the first half of this year for missile defense. If you look at our longer term outlook, and I know we don't disclose all the stuff, but I'll just tell you that the outlook is robust; you look at U.S. buy for THAAD systems for example and that should be strong over the next several years. You probably saw the deal that the administration made with Saudi Arabia a couple of months ago.

We expect THAAD systems to be part of that, so that's upside. So the combination of U.S. DoD buy and foreign military sales should be quite robust for missile defense systems. So I look at 2017, I think we'll have really solid growth from NASA, not so much on the missile defense side but as I look to 2018 and beyond I think our top line will be driven largely by missile defense.

Greg Konrad, Analyst, Jefferies LLC

I mean and then similarly on the...

Paul R. Lundstrom, Vice President & Chief Financial Officer

And tactical too, yeah.

Greg Konrad, Analyst, Jefferies LLC

All right, that was going to be the next question, so that's a good segue. I mean that's another place; I mean if just looking at what you guys do disclose, it seems like that business is also not growing and if we kind of look at the headlines of usage of tactical, munition overseas, it's grown 30% or 40% just from a usage perspective. What type of trends are you seeing in that?

Paul R. Lundstrom, Vice President & Chief Financial Officer

Yes, the news usually leads the buy and you know you see the buy come after, and what I'll say in terms of tactical, you look at important part of business for us; I named some of the programs a couple of minutes ago. If you look at current budget allocations to tactical, the original budget requests what the house has been kicking around, none of this is through the Senate yet as you look out to 2018, but it's nice to see quite a few plus ups on the tactical side. And you've seen more Patriot, you've seen more GMLRS, you've seen more TOW all of that is those are tactical systems that we're part of. And I view that as – that sort of have an upbeat view on tactical.

Greg Konrad, Analyst, Jefferies LLC

I mean, in hypersonics, it seemed to be kind of the next big thing for a while now but it seems like the headlines are starting to pick up. Lockheed acknowledged that you're working on a program with them. Are you starting to see some of those programs really materialize versus maybe just conceptual over the past 10 years and some of those opportunities that are emerging?

Paul R. Lundstrom, Vice President & Chief Financial Officer

Yes, so I'm new to the hypersonics technology. So I can't comment too much technically, other than to say when you – on paper you look at the speeds of some of these things, it's absolutely stunning. What you read in the press about foreign militaries hypersonics' capability, a little alarming. And so there's no doubt in my mind that the DoD is and will continue to respond with that, the continued maturation of that technology. You mentioned the Lockheed discussion; I can't comment more about that. A lot of these programs frankly are – we just can't talk about it. As Eileen said it in our Investor Day, a couple of months ago but yes, exciting potential for sure, and I would say from a technology perspective we are right in the middle of it all.

Greg Konrad, Analyst, Jefferies LLC

I mean in the second quarter, you did 13% margins A&D ex items, you mentioned some of the moving pieces, you've taken a lot of cost out of the fixed cost base, some of that's given back to the customer. I mean, how should we think about margins longer term versus peers? And what type of levels you think you can reach?

Paul R. Lundstrom, Vice President & Chief Financial Officer

So I'm not going to give a specific target today but what I'll say is: if you were to just put together a pareto, high to low and show aerospace and defense margins in a peer group, tough to argue our peer group because we're a very specialized company. But just look at A&D, run off a pareto and you'll see that we're in the bottom quartile. My personal view is that we have upside potential. We're going to work hard on that. It's tough to move the needle quickly. So you see a top like we saw in the second quarter; that's a little bit of an anomaly, frankly; good news contract re-estimates and it's great to see the cost progress.

But if I were to look over the next couple years, can we see a couple points of margin expansion, maybe couple is too small a number, over the next five, can I see a couple of points in margin expansion? Yeah, potentially. Again, not going to set a target at this point, we need to go through it and then really have a – excuse me – a solid bottoms-up strategic plan. But I look at things like program execution, continued overhead cost out; I mean, there's plenty of opportunity to do better.

Greg Konrad, Analyst, Jefferies LLC

And it seems like you've been utilizing additive manufacturing, some of the press release talks about how much of the cost can be taken out by using that manufacturing technique where you in that evolution I mean how much of the business can that touch – and how much cost can that take out?

Paul R. Lundstrom, Vice President & Chief Financial Officer

So from a tribal knowledge perspective, I would say we're well on our way. We've been working additive manufacturing for many, many years now. Anyone can go out and buy a 3D printer and some metal dust; it takes something entirely different to engineer it into your products and really take cost out of your structure. There have been some press releases from Aerojet Rocketdyne where we have talked about that.

I view it as huge potential and I sort of think about a couple of ways: one is if you look at subtractive manufacturing, from an engineering design perspective, you're sort of limited. When you narrow yourself only to subtractive manufacturing because you're relying on castings, you're relying on machining and boring out channels and veins, when you can print something from the ground up, it opens up doors from an engineering perspective.

So that's exciting; it has the potential to change the performance and cost attributes of a product very, very early in the product lifecycle, literally at design. You look at the lead times and cost associated with casting and machining, it's really expensive. If you can just print the part, kick it off, and let the program run, you can take lead time and cost out, so that's huge. And then you look at some of the – and this is a little bit more specific to Aerojet Rocketdyne, but we have some proprietary blends that are ours; it's high

performance burn resistant alloys like Mondaloy 200, which is – that's an Aerojet Rocketdyne, their proprietary blend, again very specific to us, but that's exciting as well. So it's a good question additive, I'd say we're very well progressed, but there's massive potential, I think not just in the aerospace and defense industry, but other industries as well.

Greg Konrad, Analyst, Jefferies LLC

And just to touch on the land that you mentioned, I mean, that was obviously a big part of the investment story six years ago and it's a little bit deemphasized. But how should we think about any timing or value that could be attributed to that land there? And maybe some of the options that you're looking at?

Paul R. Lundstrom, Vice President & Chief Financial Officer

Yes. So the background on land is if you look at the legacy Aerojet company, which was in Sacramento going all the way back to the 1950s. You're testing, testing and building big rocket engines, we had massive buffer land, for noise abatement and safety reasons. And that facility over the years has shrunk; at one point we had 20,000 employees; over time that's come down. We had been left with land that we just no longer have use for. And so – it's a significant, I think you mentioned 5,600 acres that's not an insignificant number.

So we are actively working to monetize that. And look I think there's a lot of potential value there, but you can't just dump 5,600 acres on to the open market and not expect a major absorption and pricing issue. And so my view of the likely outcome for that is over time we'll parcel it off. If we can come up with some bigger, better deal that's attractive to shareholders, then we'll certainly entertain it. But I sort of – a proxy might be the Hillsborough transaction that we did a couple of years ago, and that was – we parceled off 700 acres, I think, all in, top line price on that was \$57 million. You do the math on a per acre basis, you come about \$80,000 an acre. Are all 5,600 acres that remain worth \$80,000 an acre? Probably not, but over time we're going to work to carve that out and get some cash for it.

Greg Konrad, Analyst, Jefferies LLC

And then just from a free cash flow perspective, I mean, how should we think about an appropriate level is that net income 100% of net income, more or less, kind of what's the free cash target?

Paul R. Lundstrom, Vice President & Chief Financial Officer

Yes. That would be our line in the sand, cash flow greater than net income. What's a little challenging about a business like ours is and you can see it just in our disclosures, I mean, one program can easily be mid-teens as a percentage of total revenue. And in aerospace and defense you can be largely milestone driven. And so you look at our cash generation in 2016, it was incredible as a percentage net income, and that's just timing of advances in other stuff. So it will ebb and flow but over a long – over the long-term cash flow well in excess of net income would be – would certainly be our goal. Driving cash flow is very much something that we're trying to instill into the culture.

Greg Konrad, Analyst, Jefferies LLC

And then I think one of the questions I get most is: what are you going to do with the cash? I mean, you did the convertible offering at the end of last year, you have over \$400 million. Maybe what's the appropriate safety level of cash and kind of how do you think about capital deployment going forward?

Paul R. Lundstrom, Vice President & Chief Financial Officer

Safety level, I would say \$50 million to \$100 million just to sort of finance your daily operations. You're right, we're sitting on about \$400 million, at the end of quarter I think \$413 million of cash; that's a fair amount for a company our size. Goal would be smart capital deployment, M&A is certainly what we had intended that convert for. We had some very specific things in mind and we continue to work on that.

We have plenty of room in our revolver as well. You look at what we have today, I think we have a \$350 million revolver and we probably have \$40 million or so that is sort of set aside for LCs or letters of credit. But that still leaves us better than \$300 million that we have, but the potential to play with so, I would say, we have M&A capacity that was the intent to the convert and we continue to look at that.

Greg Konrad, Analyst, Jefferies LLC

And then we have time for one question from the audience. Then I'll ask another one. Anyone?

Q&A

<Q>: I guess then one more quick one would be: you've been at the company since November...

<A – Paul R. Lundstrom>: November 7th of 2016.

<Q>: Exact date. What's your agenda? You come from a UTC background. I think you guys have maybe focused a little bit more on the investor outreach. Maybe just talk a little bit about kind of what you've done? Since you got there and kind of what you're up to accomplish?

<A – Paul R. Lundstrom>: United Technologies is a fantastic company. I left United Technologies because this was a very unique opportunity. I was already familiar with Rocketdyne, because Rocketdyne was part of Pratt back in the day. There's a lot of potential in this industry and in this business, and I sort of looked at that and said, wow, I think this is an opportunity I just can't pass up.

The potential is great. I sort of look at the margin levels as I'm a bit of a contrarian, and so I look at margins, I look at cash, sort of look at the investment upside and said, this is something I want to be part of, because it's a brand new leadership team that is very committed and focused on driving this company forward, and it was just something that I want to be part of and a place where I thought I could make a really positive contribution. So I look for very good things to come that's why I came, I sort of saw the opportunity.

Greg Konrad, Analyst, Jefferies LLC

Thanks, Paul.

Paul R. Lundstrom, Vice President & Chief Financial Officer

Yes. Thanks Greg.