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Ball Corporation Agreement to Sell Ball Aerospace Conference Call Edited Transcript.

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Document includes important disclaimers at the conclusion of transcribed comments

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Presentation

Operator

Greetings, and welcome to the Ball Corporation Call regarding the agreement to sell Ball Aerospace. As a reminder, this conference is being recorded today, Thursday, August 17, 2023.

I would now like to turn the conference over to Dan Fisher, Chairman and CEO. Please go ahead.

Daniel William Fisher
Chairman & CEO

Thank you, Tommy, and welcome to the Ball Corporation call to discuss today's announced agreement to sell aerospace. Please advance to Slide 2. The information provided during this call will contain forward-looking statements. Actual results or outcomes may differ materially from those that may be expressed or implied. Some factors that could cause results or outcomes to differ are in the company's latest 10-K and in other company SEC filings and are also reflected on this slide.

In addition, today's transaction is subject to regulatory approvals and customary closing conditions and adjustments. If you do not already have today's release regarding the agreement to sell Ball Aerospace, it is available on our website at ball.com. Information regarding the use of non-GAAP financial measures may also be found on ball.com\investors.

Please advance to Slide 3. Thank you for participating in today's call. Joining me on the call today is Scott Morrison, Executive Vice President and CFO. We will offer a few introductory comments, provide an executive summary of today's transaction and then open up the call for Q&A. Today's call is about the announced transaction. Therefore, we do not intend to provide intra-quarter updates on the company's financial performance.

Earlier this year, we initiated a process to assess options for our aerospace business. Today's announcement to sell Ball Aerospace to BAE Systems for $5.6 billion is the result of that process. The value achieved recognizes the aerospace team's success, leveraging its talents, asset base, capabilities and program execution to accelerate growth fourfold in recent years and position the business as a vital mission partner to the U.S. government.

Since 1956, generations of Ball Aerospace colleagues past and present, have transformed a business of humble beginnings, founded with the 35,000 cash investment from Mr. Ed Ball, the son of one of the company's founders and Ed's collaboration with 7 former CU scientists starting out in a cinder block one story building in the countryside outside of Boulder, Colorado became Ball Brothers Research Corporation.

Ball Aerospace today employs over 5,250 talented people offering innovative capabilities in a world that needs rapid scalable technology solutions and vital national defense capabilities. The complementary culture fit and mission inspired innovation of Ball Aerospace and BAE Systems is well positioned to elevate the business and our mission partner success to new heights.

Please advance to Slide 4. On Slide 4, we have provided an executive summary of the transaction. Ball has entered into a definitive agreement to sell its aerospace business to BAE Systems for $5.6 billion in cash. The rationale for today's announcement is very straightforward. The transaction achieves a premium multiple and is a beneficial outcome for all stakeholders. Strengthens our balance sheet, providing flexibility to drive significant return of value to shareholders, accelerates our low-carbon best value initiatives to enhance organic growth across our global aluminum packaging businesses, and BAE is well positioned to invest in Ball Aerospace in excess of our existing plan.

Advance to Slide 5. Turning to more of the details from a valuation perspective, the purchase price of $5.6 billion in cash is expected to generate approximately $4.5 billion in after-tax cash proceeds. The pretax price represents an implied multiple of 27.1x Ball Aerospace LTM comparable operating earnings of $205 million and 19.6x LTM comparable EBITDA of $284 million. We anticipate the transaction closing in the first half of 2024. Following the required regulatory approvals and customary closing conditions.

Relative to use of proceeds and following a successful closing of today's transaction, we expect to promptly pay down debt to achieve 3x net debt to comparable EBITDA, the low end of our target range. Then pivot to executing a multiyear share buyback utilizing our share repurchase authorization programs, while also continuing to pay our quarterly cash dividends. The precise timing and amount of repurchases and the opportunity to increase the dividend payout will be determined based on market conditions, timing of receipt of proceeds and other factors and position Ball for enhanced organic growth across our global aluminum packaging operations.

Advance to Slide 6. Ball going forward will be a pure-play aluminum packaging leader diversified across the beverage, personal care and household products industries for both single-use and reuse occasions. Over the past 15 years, we have developed a world-class sustainability organization using data and key initiatives to inform key stakeholders and enable the greater use of circular aluminum packaging.

Our low-cost global footprint of 67 facilities, innovative portfolio, best-in-class customer base and manufacturing capabilities continue to drive solutions to our customers and consumers for single-use, limited reuse and refill aluminum packaging. With 2022 net sales of $13.4 billion and EBITDA of $1.7 billion in 2022, excluding aerospace. The business is poised for improved earnings growth, increased free cash flow and EVA generation following a multiyear investment cycle, which is largely concluding in 2023. We look forward to dedicating our resources to accelerating the low-carbon best value package initiatives we are undertaking to grow aluminum packaging sales and accelerate substrate mix shift. We will have an enterprise goal with regional playbooks.

Advance to Slide 7. Moving to capital strategy. Near term and long term, as we mentioned briefly before, the immediate benefits of the post-close net proceeds and the higher level of free cash flow being generated by the packaging businesses in 2023 and beyond are expected to reduce the company's leverage from 4.6x net debt to comparable EBITDA to in the range of 3.0x post-close.

Progressing to the lower end of our target leverage range provides the opportunity to increase share repurchases and deliver a higher level of sustainable return of value to shareholders over a multiyear period. As a result of the aerospace sale, we project EVA dollar accretion to be in the range of $250 million. Our ability to generate higher returns on invested capital in our global packaging businesses as throughput escalates on newly deployed assets will also maximize shareholder returns as we run lean, tight and with an eye on accelerating our ongoing initiatives to accelerate low carbon, best value aluminum packaging particularly in EMEA and North America, where packaging legislation and customer substrate shift is aligning in aluminum packaging's favor.

Please advance to Slide 8. Today's transaction reinforces, who we are and where we are going. We are a focused global aluminum packaging company striving to accelerate our strategy to preserve our planet and deliver value by creating circular solutions for our customers. By operating a lean, agile and results-driven organization, we will unlock innovation and untapped potential and accelerate our low-carbon best-value global aluminum packaging initiatives, which will drive higher sales, free cash flow and comparable earnings per share.

As you saw in the prior slides, our disciplined capital allocation mindset remains. Though the flexibility gain from the successful close of today's transaction strengthens our position to return shareholder value creation faster.

Please advance to Slide 9. As a focused high margin, highly cash generative global aluminum packaging business, today's announced sale accelerates our low-carbon best-value initiatives to enhance organic growth across our global aluminum packaging businesses.

Turning to more of the details, advance to Slide 10. As we conclude our scripted comments, I would like to take a moment to thank our employees. Words cannot express our appreciation for our 5,250 plus aerospace employees. During the period of our business assessment, the team acted with great professionalism with their eye always on executing on our customers' missions and supporting one another. To BAE Systems, we also thank you for seeing in Ball Aerospace, what we have for over 65 years. Excellence, humility, passion, high execution and growth potential. Our complementary cultures are a perfect fit.

Please advance to Slide 11. In summary, our use of net proceeds will drive immediate value for our shareholders. Our ability to execute our strategy by operating a lean, agile and results-driven organization that value our people, culture and ownership mindset is happening today. By leveraging our scale, footprint, portfolio, customer base and plans to accelerate our ongoing sustainability initiatives in coordination with our value chain, our future is bright. Our sales volumes, diluted EPS, free cash flow and EVA dollars will grow, and we will look to future growth through the best return of value outcomes for our fellow shareholders.
That concludes our scripted comments. Tommy, we are ready for questions.

Question and Answer

Operator

We'll proceed with our first question on the line from George Staphos with Bank of America.

George Leon Staphos
BofA Securities, Research Division

Dan, Scott and to everybody, congratulations on the news today and best of luck with the transaction. I guess I'll ask two questions. BAE had figures for the aerospace segment in its slide deck. Do you concur with those figures?

Daniel William Fisher
Chairman & CEO

I have not seen that slide deck, to be honest with you. As you could imagine, things have moved very quickly. So I know the we are getting $5.6 billion, and I know the implied multiple is 27.1x LTM comparable operating earnings and 19.6x LTM comparable EBITDA. [Please refer to the non-gaap disclosure on ball.com/investors.com for more information].

George Leon Staphos
BofA Securities, Research Division

Okay because of what aerospace is and what it's been built into aside from the normal regulatory review, what other authorities would need to approve this transaction? If you can give us some color on how those boxes to some degree, have already been checked. And then you're going to be a lean organization, you're going to accelerate aluminum packaging growth, those have all been sort of consistent themes within Ball. And the packaging business and the aerospace business have always been run somewhat independently. So how does this transaction actually allow you to do any more acceleration, any more focus since packaging has already been in that sphere for a while? How does it help you optimize your business strategy in packaging, specifically going forward two or three things?

Daniel William Fisher
Chairman & CEO

So as you can imagine, given the regulatory environment, when we looked at the things that had to be true in our estimation, I think we've done as much research and as much homework on that and had enough conversations even at the customer level to suggest that this has a high degree to get across the finish line.

I'll reserve the right to get back to you on specific timing, but it's effectively going to be, as you can imagine, the regulatory environment, the customer is signing off. And then there is some uniqueness with what has to be submitted in the U.K. But all of those things, we believe, are in line to be less than a year and potentially faster than that.

And then in terms of the efficiency, I agree. I think when we look at the backdrop of the world as it relates to aluminum, things are moving much, much faster in parts of the world. Europe, in particular, the regulatory environment is at a sprint. And our customers are needing answers, real answers, not theoretical answers in terms of substrate and circularity, and we believe that aluminum in the supply chain in a carbon neutral position and the way we get there and how fast we get there, industry participation is huge with regard to that.

But there's a lot more opportunity in the medium term than there was a year ago. And I want to make sure that enterprise-wide we are consistent with selling an aluminum portfolio. Right now, we're constructed as a beverage business and a cups business and aerosol business, as you understand. But when we're talking to, for instance, mountain towns in Colorado, that are trying to remove plastic waste. They want to know everything that Ball has to offer to solve everything from single-use plastic cups to single-use plastic bottles to very difficult recycling infrastructures. And we need to organize our way to accelerate the growth that's right in front of us.

And we need two things. We need a better carbon footprint story, without repute we believe we have the best, but leaning into that, and making sure that the cost profile and the economics of aluminum are in a position, where it's a lot easier for our customers to move there. And I think we'll be able to do both of those post-transaction focusing on this business with all of our intent and all of our deliberateness and a flexible balance sheet, and an aligned business. So there'll be more of this. I think we're going to get out to you all early early in 2024 with an Investor Day to give you more clarity on that. But I am really excited that we've got our feet under us. We're moving in the right direction and aluminum has a lot of tailwinds that we're just going to be able to accelerate.

Operator

Our next question on the line is from Ghansham Panjabi from Baird.

Ghansham Panjabi
Robert W. Baird & Co. Incorporated, Research Division

Congrats on the sale. I guess we'll no longer be able to ask questions on aerospace that you cannot answer given the classified nature of the customer set, right?

Daniel William Fisher
Chairman & CEO

Well, it's the combination of that and the fact that, in all honesty, my 14-year-old girls think that dad is not near as cool anymore because I'm not associated with this beautiful aerospace business and brilliant scientists, so, please go ahead with your question.

Ghansham Panjabi
Robert W. Baird & Co. Incorporated, Research Division

Yes, I guess, so following up on the sale and just sort of building off of George's question, how does the earnings algorithm for the company change, if at all? You've been very focused on internal growth the last few years, less so on acquisitions. Should we expect a change in terms of how the company once again allocates capital with acquisitions in mind?

Daniel William Fisher
Chairman & CEO

Nothing is going to change. I think the reality is when you look at the pro forma P&L excluding aerospace, aerospace is not a hugely cash-generative business and so when you look at our earnings profile as we retire debt, the EBITDA performance, our operating cash flow largely remains the same with or without. We'll have a lower capital spend rate. This should be a catalyst to do more consistent return of value to our shareholders in line with share repurchases.

We'll look at the dividend, if that's in the right spot moving forward, we'll get our balance sheet in order. So I think relative to the opportunity set we see with aluminum packaging. This is the right answer, both for that business and for our business and our shareholders of Ball moving forward.

Ghansham Panjabi
Robert W. Baird & Co. Incorporated, Research Division

Got it. And then just for my second question, why terminate leverage at 3x, why not 3.5x? Is it just a function of giving you more sort of an opportunity set for the future in terms of what happens with the stock or how did you get to that threshold? And then just lastly, the tax rate, does that change for the company in any material way going forward post the sale?

Daniel William Fisher
Chairman & CEO

Yes, great question. I'll turn it over to Scott.

Scott C. Morrison
Executive VP & CFO

Yes. Ghansham, on the leverage. I think the 3x gives us just more flexibility to return value to shareholders, to look at the low carbon aluminum side of things, it gives us more flexibility. And it's a higher interest rate environment. So taking off some debt makes sense.

The second part of your question was tax rate, it doesn't change materially. It's really more of a function of where we earn profit. That drives it more than this.

Operator

Next question on the line is from Mike Leithead with Barclays.

Michael James Leithead
Barclays Bank PLC, Research Division

Again, congrats on getting this one done here. Dan, can you just speak to the genesis or background of the deal? Were you looking to sell? What was your approach to run an auction? Just any context to how this came about would be helpful?

Daniel William Fisher
Chairman & CEO

So stepping into this role and what transpired with the Russian event and the European backdrop and raising inflation and interest rates, our stock got compressed and got compressed to a point where it was quite clear that the value of this aerospace business was not adequately reflected in the value of our stock. And we needed to do our job as owners to make sure that we had the appropriate share value for the assets that we hold and they were in the right spot in the right home. So we evaluated.

We ran a process, given the nature of our business, very difficult to find out publicly what it's worth unless you were to entertain the process. And through that process, we looked at everything. We looked at spinning it. We looked at mergers, we looked at partnerships. And the 3 items that we agreed to with the Board, myself and our President and CEO of the aerospace business, were threefold.

One, we had to get the best value for our shareholders at the conclusion of this exercise. And if that meant for us to keep running the business, then we were going to keep running the business. Number two, we needed to make sure that we have the right culture fit if we were to do anything. And I believe we've accomplished that. And thirdly, as a patriot and as someone who's got a lineage of veterans in my family like others on the Board, this is a national asset in a world that's becoming less and less safe and this needed to sit in a business that was going to catalyze the existing capabilities and improve upon them and accelerate them.

And we were able to accomplish all 3 of those through this transaction, and it turned out that it was an outright sale, which was the right conclusion for all 3 of those. Very rarely does all of that come together as nicely as this has, but our partners at BAE and the leadership team at Ball Aerospace, our Board, the management team, we all thought this was head and shoulders ahead of anything else and I'm really excited about the outcome here and being able to talk about this today, not only for the aerospace business and the transaction but the future of Ball Corporation.

Michael James Leithead
Barclays Bank PLC, Research Division

Great. That's super helpful color and context. And then just briefly, I appreciate aerospace was run a bit separate from the aluminum packaging businesses. But can you just speak to any stranded costs you expect to incur?

Daniel William Fisher
Chairman & CEO

There's very little, and we will address that over a period of time. There are elements, from an infrastructure standpoint it is running standalone. And a lot of it has to do with cybersecurity, firewalls, et cetera. We have some complementary systems on HR system, some aspects of financial systems that we'll have to unwind, but it will be very clean in terms of that.

Operator

Next question on the line is from Phil Ng from Jefferies.

John Robert Dunigan
Jefferies LLC, Research Division

This is actually John Dunigan on for Phil. Appreciate the information and congratulations on getting the deal announced and hopefully done. I wanted to start with you said you have high confidence in getting this finished in time, Dan. But it's a foreign company buying a U.S. defense business. So I'm just wondering what the potential breakup fee is if the deal is blocked for any reason by any major customers or from a regulatory standpoint?

Daniel William Fisher
Chairman & CEO

There is a fee associated. I won't go into the details of it, but I will clarify this. This is being bought by a U.S. company. Yeah, the holding company and the PLC is in the U.K., but who's purchasing it is the U.S. company. And obviously, they're doing business with the federal government in the defense space and have been for years. So I would think about it slightly differently in terms of the risk of a foreign national ownership structure.

John Robert Dunigan
Jefferies LLC, Research Division

Got it. I appreciate the clarification there. And then I know you had mentioned in the press release that you'll make the determination on a potential increase dividend payout ratio. I mean at this point, is it safe to assume kind of a pro rata decrease in the dividend based on the lost aerospace earnings? Or is there anything else we should consider as we're thinking about our models for next year?

Scott C. Morrison
Executive VP & CFO

We're not thinking of decreasing the dividend by any stretch. I mean from a free cash flow percentage, 95% of the free cash flow of this company comes from the packaging side of the business. So this transaction doesn't really change that at all. Lowering leverage, spending less capital, it just provides us with more financial flexibility to look at increasing the dividend as we go forward, not decreasing it.

Daniel William Fisher
Chairman & CEO

We'd want to make sure that the yield remains where it's at, which would mean most likely an uptick in the share repurchases that happen and that the dividend would move appropriately.

Operator

Our next question on the line is from Gabe Hajde with Wells Fargo Securities.

Gabrial Shane Hajde
Wells Fargo Securities, LLC, Research Division

I'll echo a congratulations for the deal. Scott, I guess, a clarification. In the past, you talked about R&D tax credits that were helping out during the cash tax rate that I think has averaged kind of 15% over the past 5 years. So what you're saying is that you expect the cash tax rate to remain below kind of statutory levels?

Scott C. Morrison
Executive VP & CFO

Well, we'd be creeping up closer to statutory levels as the tax environment gets different, but losing the R&D credits, it adds about 1 point to our tax rate going forward, but like I said in the earlier question, it really is more dependent on where we earn the profitability, whether it's in South America, whether it's in Europe or whether it's in the U.S., that can often outweigh the difference of the R&D tax credit benefit.

Gabrial Shane Hajde
Wells Fargo Securities, LLC, Research Division

Okay. And then I guess more from a strategic standpoint, one of the things that you talked about was potentially co-investing, I think, in an aluminum facility in New Mexico. And it's sort of tough for us on this side of the table to think about the different possibilities for aluminum packaging. But maybe for surety of supply or various strategic reasons from your vantage point, does this transaction kind of bring something like that back to the table in terms of, should we be thinking about you kind of backward integrating or partnering with some folks? Is that what you're referencing there Dan, in terms of low carbon potential?

Daniel William Fisher
Chairman & CEO

The low carbon comment. First of all, you have to think about it as the aluminum industry writ large, because we have such an opportunity, everyone within the supply chain to continue to move to low carbon and away from virgin aluminum, use higher recycled content, and within our coatings structure, getting to water-based coating. There are things that have to continue to happen to ensure that we are in an advantaged position from a circularity position.

The conversation that we had relative to the New Mexico mill was largely and adequately answered by two new mills coming into the U.S., and at the time, we were concerned that we needed enough capacity. And the investments that were made provided us and our partner with an opportunity to not move forward with that project currently. But those things will always be looked at. We've looked at them historically. We want to make sure our surety of supply is right. We want to make sure that we have material content, recycled content, green energy to fill and fund those mills.

And if the supply chain wants to do it themselves, great. We don't have to participate, if we need to help and it could be in the form of an offtake agreement, it could be the form of a small JV investment. We're entertaining all of those and really nothing's changed in that regard, but we'll have to use the right economic allocator, EVA to make sure that, that investment makes sense. But a more flexible balance sheet certainly offers us the opportunity in places like Europe that need to move faster. We need to be having a more robust conversation with the supply base to make sure they're going to give us what we need and our customers what we need to continue to advance aluminum.

Operator

Our next question on the line is from Bill McGowan from Conning.

Bill McGowan

Vice President, Conning Investment Banking

Congrats on the sale. Just wondering if you could provide any details regarding the nature of expected debt reduction like what part of the debt stack would you be looking to target? Term loans versus unsecured? I know you have some $1 billion November maturity. So any thoughts around that would be greatly appreciated. And just secondly, are you looking to target a specific credit rating post close? I know you mentioned the high rate environment, cost of debt. So would there be any interest in attaining IG ratings?

Scott C. Morrison
Executive VP & CFO

In terms of the maturity that comes in November, we actually did a debt offering a short time ago. So we have quite a bit of cash and we'll generate a lot of cash in the back half of the year to take care of that maturity. And then the next maturity comes in March of next year, and that's at extremely low rates. So we won't refinance that until we get to the last day. And beyond that, we'll look across the stack of debt that we have and figure out what is the most optimal to retire or partially retire.

And in terms of credit ratings, I've been here 23 years, and we've had the same rating since the time I got here, and that's served us pretty well. It gives us a lot of financial flexibility. So I don't see us right now looking at a different credit rating than where we're at today.

Operator

Mr. Fisher, we have no further questions at this time. I'll now turn the call back to you.

Daniel William Fisher
Chairman & CEO

Okay. Thank you very much. I appreciate all the questions and the follow-up on this. We're really excited excited for our aerospace employees, excited for Ball in the future. As we get closer to the finality of this transaction, we'll get back together and let you know the timeline and more specific use of the proceeds. And until then, look forward to catching up with everybody here over the next couple of months. Thank you.

Operator
Thank you everyone. That does conclude the conference call for today. We thank you for your participation and ask you to disconnect your lines. Have a good day.

Forward-Looking Statements

This transcript contains “forward-looking” statements concerning future events and financial performance. Words such as “expects,” “anticipates,” “estimates,” “believes,” and similar expressions typically identify forward looking statements, which are generally any statements other than statements of historical fact. Such statements are based on current expectations or views of the future and are subject to risks and uncertainties, which could cause actual results or events to differ materially from those expressed or implied. You should therefore not place undue reliance upon any forward-looking statements, and they should be read in conjunction with, and qualified in their entirety by, the cautionary statements referenced below. Ball undertakes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Key factors, risks and uncertainties that could cause actual outcomes and results to be different are summarized in filings with the Securities and Exchange Commission, including Exhibit 99 in Ball’s Form 10-K, which are available on Ball’s website and at www.sec.gov. Additional factors that might affect: a) Ball’s packaging segments include product capacity, supply, and demand constraints and fluctuations and changes in consumption patterns; availability/cost of raw materials, equipment, and logistics; competitive packaging, pricing and substitution; changes in climate and weather and related events such as drought, wildfires, storms, hurricanes, tornadoes and floods; footprint adjustments and other manufacturing changes, including the startup of new facilities and lines; failure to achieve synergies, productivity improvements or cost reductions; unfavorable mandatory deposit or packaging laws; customer and supplier consolidation; power and supply chain interruptions; changes in major customer or supplier contracts or loss of a major customer or supplier; inability to pass through increased costs; war, political instability and sanctions, including relating to the situation in Russia and Ukraine and its impact on Ball’s supply chain and its ability to operate in Europe, the Middle East and Africa regions generally; changes in foreign exchange or tax rates; and tariffs, trade actions, or other governmental actions, including business restrictions and orders affecting goods produced by Ball or in its supply chain, including imported raw materials; b) Ball’s aerospace segment include funding, authorization, availability and returns of government and commercial contracts; and delays, extensions and technical uncertainties affecting segment contracts; failure to obtain, or delays in obtaining, required regulatory approvals or clearances for the proposed transaction; any failure by the parties to satisfy any of the other conditions to the proposed transaction; the possibility that the proposed transaction is ultimately not consummated; potential adverse effects of the announcement or results of the proposed transaction on the ability to develop and maintain relationships with personnel and customers, suppliers and others with whom it does business or otherwise on the business, financial condition, results of operations and financial performance; risks related to diversion of management’s attention from ongoing business operations due to the proposed transaction; the impact of the proposed transaction on the ability to retain and hire key personnel; and c) Ball as a whole include those listed above plus: the extent to which sustainability-related opportunities arise and can be capitalized upon; changes in senior management, succession, and the ability to attract and retain skilled labor; regulatory actions or issues including those related to tax, environmental, social and governance reporting, competition, environmental, health and workplace safety, including U.S. Federal Drug Administration and other actions or public concerns affecting products filled in Ball’s containers, or chemicals or substances used in raw materials or in the manufacturing process; technological developments and innovations; the ability to manage cyber threats; litigation; strikes; disease; pandemic; labor cost changes; inflation; rates of return on assets of Ball’s defined benefit retirement plans; pension changes; uncertainties surrounding geopolitical events and governmental policies, including policies, orders, and actions related to COVID-19; reduced cash flow; interest rates affecting Ball’s debt; successful or unsuccessful joint ventures, acquisitions and divestitures, and their effects on Ball’s operating results and business generally; and potential adverse effects of the announcement or results of the proposed transaction on the market price of Ball Corporation’s common stock.