

ASTRONICS CORPORATION

CJS SECURITIES NEW IDEAS FOR THE NEW YEAR CONFERENCE TRANSCRIPT

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Presenters and Participant

PRESENTERS

Peter J. Gundermann
Chairman, President & CEO

Nancy L. Hedges
Vice President & CFO

PARTICIPANT

Jon Tanwanteng
Analyst, CJS Securities, Inc.

Presentation

Jon Tanwanteng

Analyst, CJS Securities, Inc.

Good morning, everybody, and welcome. We're happy to have Peter Gundermann, CEO of Astronics, joining us; as well as Nancy Hedges, who recently became CFO after the retirement of David Burney. Astronics is a leader in electrical systems and components for commercial airliners, military aircraft, as well as business jets. They also make test equipment for military and municipal transit applications. A rating on Astronics is a market outperform with a \$28 price target. Pete is going to go ahead and give a short introduction to the company, talk about some of the opportunities and challenges they have in front of them, and then, we're going to go to a fireside chat and Q&A portion of the presentation after that.

So, with that, Pete, go ahead. It's yours.

Peter J. Gundermann

Chairman, President & Chief Executive Officer, Astronics Corp.

Thanks, Jon. And good morning, everybody. A brief overview of Astronics. We're an aerospace company. We report in two segments. Approximately 90% of our sales are in aerospace, though, so we kind of think and act and feel like an aerospace company. 10% of our business, or our smaller segment, is a test business. My comments will be mostly weighted towards aerospace since that's why most investors invest in us.

We're kind of in an interesting time as we exit 2024 and enter 2025. Our company was one that got hit pretty hard by the pandemic, so we saw a pretty big sales decline, and the sales decline was largely driven by our overweighted exposure towards commercial transports. We were, when the pandemic started, approximately 70% commercial transport. Beyond that, 10% business jet, 10% military aircraft, 10% test. Rough numbers. Obviously, commercial transport got hit very hard by the travel shutdown as the pandemic took hold. Compared with most public companies in the space, or suppliers to aerospace, we were comparatively pretty highly exposed.

This chart on the screen right now shows that hit as we entered into the pandemic. We had revenues in 2019 of almost \$800 million. We got down to about \$445 million a couple of years later. Since then, it's been a very quick and abrupt recovery. We're wrapping up a year where we ended up just shy of \$800 million. Again, we're still doing the accounting, but we came out with the press release a couple of days ago on the fourth quarter preliminary sales. So, over the last three years, we've actually averaged over 20% growth per year. That's a pretty chaotic level of growth for any company and it was during a period of pretty significant supply chain challenges, not just for us, but for the entire world, with labor challenges at the same time and pretty big increases in input costs. Inflation was pretty rampant during a lot of those periods, but we got through it. And as we exit 2024 and look at 2025, we are expecting growth to moderate.

Again, a couple of days ago, we came out with a press release with initial revenue guidance for 2025 of \$820 million to \$860 million. That is mid-single-digit growth at the midpoint. There certainly is an upside opportunity to outperform that and, depending on your perspective, there arguably is downside risk; again, given our dependence on commercial transports and production rates of Boeing, in particular, but also at Airbus.

The good thing about 2025, from my perspective, is that, when we're not scrambling for growth, parts and employees, I think we have a really good opportunity ahead of us to kind of dial in and optimize operations, which I believe will show itself in improved financial results down the income statement. It's a relatively stayed environment when you're looking at, say, 5% or 6% or 8% or 10% growth compared with 15% or 20% or 28% that we had two years ago, so I'm looking forward to that.

During the pandemic, we were pretty successful also in winning a number of new programs, which are increasingly going to have positive impacts on our business going forward. One in our Test segment is called the Radio Test program for the US Army. The US Army carries a lot of radios, uses a lot of radios, and wants to develop a standardized test capability to verify radio performance in the field and in the lab. Instead of having, say, one dedicated tester for each family of radios, it's like 28 families.

They want one tester that will test that whole universe. We won that program. We're currently in the development stage or the finalizing stage of the engineering effort, and we expect to be in full rate production on that program towards the tail end of 2025. We believe there's \$215 million dedicated or allocated to that effort by the US Army.

Another example of a big program, which we're working hot and heavy on right now, that's going to have an impact less in 2025 and more in the future is the US Army's FLRAA program, Future Long Range Assault Aircraft. It's the Army's planned replacement for the Black Hawk helicopter. It has been awarded to Textron's Bell operation and Bell has named us as a major partner for developing the electrical power distribution system. This promises to be a very significant program for us. If the production estimates are halfway close to accurate, nobody knows for sure what that number is, it appears that our shipset content, which is still under development and subject to change, is approaching at or above seven digits of size, which would make it one of our largest shipset contents over.

And beyond that, you can argue, is the glass half full or half empty with respect to OEM production rates in the commercial transport business. We think there are upward trends both for Boeing and for Airbus, and that's going to serve us well. We think, also, that business jet production rates, 10% of our business, also have upside potential as backlogs have grown significantly during the pandemic years, and while production rates are up, they're not up that significantly, because capacity is really expensive in that business.

In general, across the board, we're feeling pretty good about where we are as we exit 2024 and get into 2025.

And, Jon, you said 5 or 10 minutes. I think that's 10 minutes. I'll stop there.

Question and Answer Section

Jon Tanwanteng

No. That's good. Thank you for that background, Pete. Now, we'll go to the fireside chat and Q&A. If you're listening in the audience, you can submit questions through the text interface on the website. If you're listening over the phone, please email me questions at jtanwanteng@cjs-securities.com.

Pete, I'm going to start off just with the outlook that you provided as well as the preliminary Q4 numbers. First, what drove the strength in the quarter, especially with Boeing essentially shut down due to the strikes in Q4, number one? And then two, could you just be a little bit more specific what level of Boeing production you're building into 2025? Where it's starting from and what you think it's going to ramp to and how you are shipping against that.

Peter J. Gundermann

Sure. I would say the big driver in the fourth quarter was really a continuation of trends that we have seen over the last three or four quarters, and a big one there is continued improvement of the global supply chain. We're a heavy user of electronics and electronics tends to be very global and was highly problematic during the peak of the COVID crisis but has continued to recover and perform more and more seamlessly. If you look back over the last three or four quarters, we have come in at the very high end of our predicted range, and that happened again in the fourth quarter.

From my perspective, I was a little bit surprised by that, because, as you said, Boeing went on strike. They shut us down. The 737 is our largest single program these days in normal times, so I wasn't sure we were going to get there, but we were able to execute on a number of other pieces of business, some past due backlog, which had accumulated and was something we could address because of the improvement in the supply chain. Also, I think it's worth noting, improvement in labor efficiency is something that we have been seeing and expect to see. Last summer, mid-year, we did an analysis and we found that something like 40% of our employee base, we have about 3,000 employees right now, have been with the company less than three years, which is an extremely high percentage and speaks to the transitions that the labor force in general in our North American economy has been going through. I don't think our struggles are different from anybody else's. Labor was problematic during much of the shutdown. I think as we, again, exit 2024 and go into 2025, the supply chain's improving globally, especially for electronics, and people are getting more efficient, getting more knowledgeable.

The churn in the employee base has really quieted down and stability and improvement in those two areas are critical for us to be able to meet our numbers. So, that's the long answer to your short first question. The second part of your question is what are we assuming for Boeing production rates in particular, I think you were asking about. Right?

Jon Tanwanteng

That's right.

Peter J. Gundermann

So, we are assuming, going forward, that we're going to be building on the 737 at about 20 shipsets a month through the first nine months of 2025; and then, we are predicting that we will ramp up to somewhere in the neighborhood of 30 shipsets towards the end of the year. That is a lower rate than what most forecasters are predicting for Boeing production. That's with an eye towards the reality that there is some inventory built up in the system we expect.

Boeing wants, on the one hand, to chew down that inventory a little bit, so we expect that to hold us back below their anticipated production rates as we move through the year, but they also don't want to harm us in the sense that they need us when their production rates go higher. We have been in dialogue with them saying, basically, that 20 shipsets a month is a good number where we can keep the muscle memory in check. We can keep critical mass of employees on board and trained and proficient, and we can have a pretty solid base to grow from there.

If they were to cut us back significantly less, we think we would be putting that future ramp at risk. It would be harder for us to execute in the future, so we think that they agree with that. Obviously, all this depends on what their ramp is really going to look like. Pessimists might say 20 shipsets is too high; optimists would say 20 shipsets is too low, but we think that's a defensible conservative number that is built into that forecast that we put out there.

Jon Tanwanteng

Got it. That's fair. You mentioned electronic supply has been getting better. You've obviously gone through a lot of pain. It seems like all anyone could talk about these days is tariffs, potentials for retaliatory things. We've seen restrictions on things like rare earth minerals out of China. Can you just talk about how you might be preparing for changes in the supply chain as it relates to all these geopolitical movements going forward and what do you see as the risk?

Peter J. Gundermann

Well, it's obviously a big unknown at this point. There are headlines every day and the headlines are pretty much different every day. Is it a real plan or is it a negotiating tool, is it gradual, is it accelerated, is it focused on certain technologies and certain countries, and we don't have answers to a lot of that, of course.

Our observation is that, on the one hand, like many companies who are heavily involved in electronics, we are dependent on a certain portion of the supply chain that's going to come out of China. That's kind of a reality that some of these parts and materials only come from there, so that's an issue. On the other hand, based on the first Trump presidency in tariffs that were put in place at that time, a lot of the supply chain just kind of corrected itself in the sense that contract manufacturing, particularly in the area of circuit boards or assemblies that involve basic electronic components, a lot of that stuff's already been moved out of China and it's been moved to places like Singapore or Vietnam or Thailand or Mexico. We think that those places are less likely to get the full brunt of any tariffs that Trump might put in place. But again, how do you know?

So, it's a little hard to plan. I think the world is hoping that there will be more of a smooth transition, and we certainly are too. I would also add that there is some room to believe that, based on the inflation that the world has seen and our customers have seen over the last few years, the industry has learned how to deal with price shocks and price changes and, to a certain extent, I believe that, in a worst-case scenario, if there are higher tariffs put in place, our industry knows how to deal with those kinds of changes in a way that we didn't know how to deal with buyers six, eight years ago. I think there will be a level of reasonableness involved here, and I think it'll be inflationary, in the worst case, for sure, but I think the industry knows that the industry has to protect its margins, and we'll find a way through it.

Jon Tanwanteng

Could you expand on that a little bit, because in the past, you've had to deal with fixed cost contracts, especially during a hyper inflationary period? Do you have provisions now to pass things like tariffs or exchange rates or just general price increases easier than you did in the past?

Peter J. Gundermann

I think the whole industry has warmed up a little bit there. There was a time old enough to remember when inflation was a big deal, and it was certainly a part of contracts. For a long time, inflation was much less of a big deal and we all kind of forgot how to deal with it. I think those memories have been refreshed and new contracts have better protections for everybody involved in terms of inflation.

Now, tariff isn't necessarily inflation. That's a little bit of a unique element. I guess what I'm saying is that, even in situations where contracts have been renegotiated mid-term based on the inflation that's happened over the last few years, customers and the industry in general seem willing to understand that and work with it rather than take a punitive kind of approach and stick people with contracts that are outdated based on different input costs.

So, I'm thinking that that kind of performance, that kind of cooperation, is something that will be demonstrated across the industry again as we move forward, because it's an issue for everybody, right? Boeing is going to have to sell airplanes. They're going to have to find a way to do that. And the smaller suppliers are going to supply to bigger companies, four or five steps down the chain. It's going to be an issue across the board for everybody.

Jon Tanwanteng

That's fair. I wanted to switch gears a bit and address something of an elephant in your room. You have an outstanding litigation in the UK as well as a follow-up in Germany. You recently raised capital to cover the potential damages that may be occurring there. Could you just give an overall update on the case, the timing of when you might expect a judgment? And beyond that, help us to understand the best- and worst-case scenarios and how you're going to operate the company, if you have a sudden cash need to pay down these damages, or if you don't have to and you have this cash on hand at a lower rate than you were paying before.

Peter J. Gundermann

Okay. A lot of questions there, right? The short answer for those who have been following our company and following the situation is that we don't really have much of an update. We were told back in October that we should expect something around year-end. Year-end has obviously come and gone, so we don't know. Nothing really has happened beyond that. We're waiting for a judgment to come down.

But I'll talk for a few minutes about the whole situation. For those who are maybe unfamiliar, this has been a long-running patent infringement situation where we have been accused of infringing on a patent. It's been litigation that's been playing out, literally, since like 2010, so it's nothing new.

It's been playing out in four countries: the US, France, the UK, and Germany, and there are battles and wars. To a large extent, I feel like we're winning the war, but the UK is a battle that we're concerned about. The situation first was competed in the US, and in the US, we were successful in getting this subject patent annulled. It was found not to be novel. It was dismissed. No more litigation. It's a done deal. And the US is the biggest single market with this thing is being competed.

The second biggest market is France and, similar to the US, we have been successful in getting the patent annulled or dismissed. Again, because it's not novel in the eyes of the court. That situation is not completely done in that there is an appeal underway to reopen the legitimacy argument for the patent. That should come down sometime in the next quarter. We're hopeful that the lower court ruling is sustained, and the patent is dismissed, but we'll find out.

In Germany, we were successful in getting the patent partially dismissed, but it was partially upheld. Think of it more as an invention patent. It's not very broad based and we have accrued liabilities there of about \$17 million. It's been in place for about a year and a half, I think, and the legal process there is on hold waiting, we believe, to see what happens in the UK. The

UK is different from France, different from the US, different from Germany, in that the patent was totally upheld and we were found to be infringing. At a damages hearing, what happened in October, with the help of our legal team in the UK, we accrued a potential damage of \$7 million or so.

We were given a range, again by our lawyers, in something like \$7 million to \$15 million, accounting rules say you book the low end of the range, so we have accrued a liability on the books of about \$7 million. In the warm-up to that damages hearing, we were somewhat surprised to learn that the other side calculated damages somewhere north of \$100 million, like \$108 million. So, quite a spread. We have a logic that gets us to our number. They have a logic that gets us to their number. It's a single judge, and that single judge will make a ruling here sometime soon.

Now, we don't know which way he's going to go. We obviously felt it was important to be able to handle the high end of the range, so we did a bond offering in late November that is designed to retire some high cost debt and provide available liquidity to cover the high end of that potential range and still operate the business and pursue the business opportunities that we have ahead of us. By the way, I should add that the subject patents here all expired even back in late 2016, 2017, so in no way infringe or impede our ability to pursue our business objectives today.

We expect a ruling in the coming weeks or months, and we also expect that there will be a subsequent appeal. We understand that, with the difference of perspectives going into this case, it's very likely that the decision, whatever it is, will be appealed going forward. We take some comfort in that, even in the worst-case scenario in the lower court, because the higher court is not one judge, it's three judges, and unlike in the lower court, the higher court has some specific IP trained representation on the bench, which is not necessarily always true in the lower court. So, we have to get past this lower court decision.

We have to be ready for a higher court appeal, and we expect that to happen later in 2025. As we understand it, these kinds of things move along relatively quickly in the UK compared with what we might be familiar with here in the United States.

That's about all I know, Jon. I don't know if you have any specific questions beyond that.

Jon Tanwanteng

No. Just in terms of financially, if you do go to like seven or 17, or whatever the low end is, what do you do with all that extra cash? And maybe, Nancy, I don't know if that's a good time for you to jump in or, Pete, if you'd like to go first on that?

Peter J. Gundermann

Well, we'd first breathe a sigh of relief. That would be an important part of the procedure. But then, we would be, obviously, very conservatively capitalized. That 5.5% interest rate on that bond offering is pretty favorable, given what we've been living with over the last few years. We would have the option also of going out and buying in the bonds, which is something we would seriously consider. We have not been taking an active part in acquisitions over the last few years. If we were to end up in the low end of the range, we could, theoretically, get more involved in those pursuits going forward.

But, to be frank, we have a huge backlog and we have won a number of significant programs, including the FLRAA program and the Radio Test program, I talked about earlier, and a few others also that I think offer great potential for our company going forward. The most important thing we can do is exercise the potential of those programs and execute well going forward. So, that would be our focus, even though we might dust off our acquisition initiatives also in the event of the low award.

Nancy L. Hedges

If I could jump in, I have a couple of things that I would add to that. You can see our capital expenditures have been really low for the last several years. We've been very modest with our capital expenditures. When we're in a situation where we have excess liquidity, there are some capital projects, some organic investments, that we would like to make on a more accelerated basis to further our growth and to expand our margins. While we're precluded to some extent from making material acquisitions or stock buybacks under our current loan agreements, to the extent we have significant liquidity and

we could get the relief under our credit agreement, we do believe our stock is trading at a discount at this point, and we would explore the potential, in addition to buying back bonds, to potentially buying back stock.

Jon Tanwanteng

Okay. Great. And then, what if the damages are at the high end? I believe there's an interest on top of that. Just how tight we will be running, and can you talk about cash flow this year, if it does get to that point?

Nancy L. Hedges

We look to see about \$30 million of liquidity to run the business. That's kind of where our dry powder would like to be, but the \$165 million that we raised under the convertible bond, we feel, is sufficient to cover us inclusive of the interest to the extent it's even awarded by the judge. That's actually unclear at this point. It would be sufficient to cover damages at the high end of the range in addition to allowing us that dry powder that I just mentioned to continue to run the business comfortably.

Jon Tanwanteng

Okay. Great. I have a question from the audience here regarding Starlink. Obviously, we've seen some announcements and adoption by the airlines. I know you have a fairly decent business in satellite communications for both commercial and most of business jets, I believe. Can you talk about how that might impact your business? Are you involved there with the retrofits or is that more of a threat for you?

Peter J. Gundermann

It's an interesting question. I would broaden it a little bit beyond Starlink and just say, LEO, low Earth orbit constellations, because there's Kuiper coming on over the next year, also out of Amazon, and it's too early to tell. I mean, part of our business is subject to these technology shifts. If you think of satellite or airplane connectivity, which is something that we're very interested in and involved in, it started off really with air-to-ground topologies and Gogo; then, it went to Ku GEO constellations and then Ka GEO constellations. Both of those were different carriers, different connectivity companies. And now, LEO is coming onto the scene, and it's, I would say, a couple of things. LEO is going to move more slowly than what the headlines in the papers might suggest. United gets a lot of press, but they're not talking about doing more than 5 or 10 airplanes in 2025, as we understand it. It's going to be a more thoughtful implementation and a trial period.

For us, we need to make a transition from Ku, Ka and ATG to LEO and our product offerings will still be needed, and we think desired, by both the connectivity companies and by the airlines. Providing connectivity to an airplane is different than providing connectivity to a boat or to a camper or to a house. It requires a different skill set, so we think that we have good prospects. We're optimistic about where this is going to shake out, but it's going to play out over the course of 2025.

I'll finally add that one of the near-term effects, though, of the advent of LEO connectivity is potentially going to be putting a chill on the market, and that's because airlines make very big investments in some of these types of systems and, when there is a technology shift like this, airlines tend to pull in their expenditures a little bit. They want to wait and see which way the technology goes, and they want to wait and see how the new technology performs relative to the old technology, so there could be a little bit of a cooling off on that market. We'll have to wait and see. Again, it's early innings. It's too early to tell. But, to a certain extent, it's no different than the other shifts we've seen over the last 10, 15 years, and what we were able to put on airplanes in those earlier shifts is consistent with what we would need to do for LEOs also.

Jon Tanwanteng

Got it. Could you talk a little bit more about the FLRAA and the Radio Test programs and what the incrementals might be in 2025? I know that, sometimes, there's a little bit of difficulty in forecasting timing from government contracts. You've had some volatility in the past just trying to figure out when these contracts would be awarded. Help us understand what you're building in and what the opportunity is there this year and maybe going to next year as well.

Peter J. Gundermann

Sure. So, FLRAA is probably the easier one. It's mostly an engineering exercise over the next couple of years. We think that the total engineering build is going to be somewhere in the neighborhood of \$60 million at this point. We're about \$14 million, \$15 million into it, so the remaining \$45 million should be spread pretty evenly between 2025 and 2026. That's significant, but it pales in comparison to what we think it's going to be going forward when we get into production. Again, I'm not sure I can endorse these numbers, but the total production run that seems to keep popping up is somewhere around 2,000 airplanes against 4,000 Black Hawks that are out there in service right now.

So, if you take 2,000 times a \$1 million per ship, it's a big program for us. That \$1 million is not final. Could be higher, could be lower. We're doing some trade studies to finalize that shipset content now, but it's a working number and it's a big program. Not so much in 2025-2026, but as the years go by. They're still building Black Hawks; after all, the airplanes started production in the 1970s.

If you look at the Radio Test program, that's going to be somewhere in the neighborhood of \$10 million engineering over the course of the year. That's pretty solid. And then, our plan is that we'll get into high-rate production in the fourth quarter, but higher rate production is a little bit harder to predict based on timing. I think our model has it as something like \$10 million to \$15 million in the fourth quarter. We'll know whether that's reasonable as we get through the second quarter. And then, we have to get a production order in the third quarter in order to make those numbers work in the fourth quarter. So well, some insight as it happens, but that's the rough order of magnitude in our 2025 plan.

Jon Tanwanteng

Got it. I think that's all we have time for today. Pete, I don't know if you have any closing statements or something you'd like to tell the investors, but thank you, everyone, for coming. This is it.

Peter J. Gundermann

I think we're good. Thanks, Jon.

Nancy L. Hedges

Thank you.

Jon Tanwanteng

Thank you, everyone. Have a great day.

Note: This transcript has been edited slightly to make it more readable. It is not intended to be a verbatim recreation of the Astronics Corp. (ATRO) CJS Conference webcast that occurred on the date noted. Please refer to the webcast version of the call, which is available on the Company's website (astronics.com) before making any investment decisions.