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Moog, Inc. (MOG.A)

Q1 2025 Earnings Call

CORPORATE PARTICIPANTS

Aaron Astrachan
Director-Investor Relations & Financial Planning and Analysis, Moog, Inc.

Jennifer Walter
Executive Vice President & Chief Financial Officer, Moog, Inc.

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

OTHER PARTICIPANTS

Jon Tanwanteng
Analyst, CJS Securities, Inc.

Jack Ayers
Analyst, TD Securities (USA) LLC

Michael Ciarmoli
Analyst, Truist Securities, Inc.

MANAGEMENT DISCUSSION SECTION

Operator: Good morning, ladies and gentlemen, and welcome to Moog, Inc. First Quarter Fiscal 2025 Earnings Conference Call. At this time, all lines are in a listen-only mode. Following the presentation, we will conduct a question-and-answer session. Instructions will be provided at that time for you to queue up for a question. [Operator Instructions]

I would now like to turn the conference over to Aaron Astrachan, Director of Investor Relations. Please go ahead.

Aaron Astrachan

Director-Investor Relations & Financial Planning and Analysis, Moog, Inc.

Good morning, and thank you for joining Moog's first quarter 2025 earnings release conference call. I am Aaron Astrachan. With me today is Pat Roche, our Chief Executive Officer; and Jennifer Walter, our Chief Financial Officer.

Earlier this morning, we released our results and our supplemental slides, both of which are available on our website. Our earnings press release, our supplemental slides, and remarks made during our call today contain adjusted non-GAAP results. Reconciliations for these adjusted results to GAAP results are contained within the provided materials.

Lastly, our comments today may include statements related to expected future results and other forward-looking statements, which are not guarantees. Our actual results may differ materially from those described in our forward-looking statements and are subject to a variety of risks and uncertainties that are described in our earnings press release and in our other SEC filings.

Now, I'm happy to turn the call over to Pat.

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

Good morning, and welcome to the call. Today, we will share an update on the first quarter financial and operational performance, and an updated outlook for the year. We've delivered a great quarter, with strong sales growth, impressive bookings, and solid margin enhancement. We're delivering value for our customers, and we're being rewarded with significant program wins. Our operational initiatives will deliver continued margin enhancement and strong free cash flow in the second half of fiscal 2025.

Now, let me provide further detail on our operational initiatives that are driving this strong performance.

Firstly, our customer focus. Our performance in delivering for our customers has put us in a great position to pursue and capture significant opportunities arising from broad-based defense demand. We secured record quarterly bookings of over $450 million in our Space and Defense segment. These wins cover a range of applications and leverage our technical leadership and our operational performance. Close to half of the bookings were within our missiles business, with the largest single award being a production order for over $100 million from Lockheed for the control actuation system on the PAC-3 program. We also captured initial bookings on collaborative combat aircraft platforms, demonstrating the relevance of our technology in this fast-moving segment.

Bookings were also very impressive in Commercial Aircraft, with close to $400 million in orders with almost 60% aftermarket content. We continue to grow our customer base for Moog total support with additional long-term agreements with airlines around the world.

In December, the German government delivered to the Ukrainian armed forces the first of 54 self-propelled RCH 155 howitzers produced by KNDS. In support of our growing Defense business in Europe, we've recently added manufacturing space to our Böblingen site in Germany.

Next, turning to people, community, and planet. I want to return to the impact of extreme weather with an update on Tewkesbury. As you may recall, we experienced severe damage to our Tewkesbury commercial aircraft facility in September. I'm pleased to report that we have regained production capacity within eight weeks of the event. This is a remarkable achievement. It's a credit to the dedication of our staff who continue to drive the recovery so that we can deliver on our customers' commitments. Reinstatement of our production facility will continue through fiscal 2025.

It is heartbreaking to see the loss of life and the destruction wrought by the wildfires in Los Angeles. We are concerned for all those impacted, including our staff at our Torrance and Chatsworth operations. To-date, there has been no impact on our facilities.

We published our second sustainability report in December 2024. In its broadest sense, sustainability is about adapting to the evolving needs of our stakeholders. And we've made significant strides. Some highlights include CO_2 emission reduction through HVAC upgrades and the deployment of solar arrays, installation of water purification projects in our communities in India and the Philippines, and progress in tackling hazardous wastes. In addition, we made a commitment to cut water consumption by 20% relative to an fiscal 2022 baseline in areas that are designated water-stressed and to better manage our water resources across our footprint.

In relation to supporting sustainable aviation industry, we are pleased to be collaborating with JetZero on their blended wing body demonstrator, which promises to halve fuel burn and emissions as a step towards net zero carbon emissions by 2050. Moog is providing the flight control actuation on this aircraft.

Finally, turning to financial strength. We continue to make excellent progress on driving margin enhancement through pricing and simplification. Our execution is in line with our Investor Day commitments. We continue to simplify our operations. The transfer of all production from our Radford, Virginia motors manufacturing site is complete, and we will soon exit that facility. This completes the consolidation of our industrial electric motors in the US to our focused factory in Murphy, North Carolina.

In addition, in November, we entered a collective [audio gap] (00:06:51) process with staff on the proposed closure of our slip ring manufacturing site in Reading in United Kingdom. The consultation process will conclude by end of January.

We expanded 80/20 deployment to cover 75% of our business by sales and trained more than 60 leaders, bringing the total to over 900. We're on a plan to deploy to all manufacturing locations by the end of fiscal 2026. We continue to develop our capabilities and are using insights gained to drive productivity and reduce complexity in the business. We're building momentum by using our own success stories to educate the [ph] wider (00:07:30) organization and to show what is possible through 80/20. As part of 80/20, we've continued to expand Voice of the Customer interviews, and we're using that feedback to drive improvement, further building customer loyalty.

Finally, during a recent visit to our German industrial manufacturing facilities, I saw firsthand the strong commitment to driving production efficiency achieved through innovation within our manufacturing process and the integration of robotics and automation.

Now turning to the macroeconomic and end market conditions. With a change of administration in Washington this week, let me start with a few comments on our Defense business. The geopolitical environment remains extremely challenging. Whilst the recent ceasefire in Gaza is an extremely welcome development, there is still an ongoing war in Ukraine and tensions over Taiwan. The threat from growing military capability of near peers is undiminished. Consequently, there is no lessening of the need to replenish arsenals over the next few years, to modernize and upgrade existing platforms, and to develop new strategic capabilities.

For these reasons, we believe that our FY 2025 guidance is solid, and we foresee continued expansion in our Defense business based on our significant bookings. While the new administration will certainly define its own Department of Defense priorities, we believe that our broad-based exposure across all defense domains positions us well. In addition, we expect to see a continuing growth in international demand.

The new administration will likely introduce tariffs, although it is not clear how widely they will be applied, nor at what level. We've experienced the impact of tariffs in the past, and we will work with our customers and suppliers to mitigate any impact.

On the Commercial side, we remain optimistic that wide-body platforms will ramp in fiscal 2026, given the feedback received from our customers and their actions. The fact that Boeing recently announced a $1 billion investment into its Charleston facility is strong commitment to the 787 ramp plan. Airbus also reaffirmed their A350 ramp plan. We're well-positioned to support this, and we look forward to that increased demand flowing through our business.

Finally, the Industrial business has stabilized despite the soft market conditions. In fact, our book-to-bill ratio was greater than 1 for the first time in two years.

Now, let's turn to the guidance for fiscal 2025. We had a good start to the fiscal year, and we're maintaining our full-year guidance. This means solid revenue growth, strong adjusted operating margin improvement in line with our investor plan, and a significant improvement in free cash flow relative to fiscal 2024. Our revenue guide is unchanged, with just minor updates by segment to reflect what was achieved in quarter one and the impact of unfavorable exchange rates within the Industrial business. Our margin guide also remains unchanged.

Finally, our free cash flow is unchanged for the year. Whilst our use of cash in the quarter was high, we have a clear line of sight to its improvement in quarter three and strong cash flows for the back half of the year.

Now, let me hand over to Jennifer with a more detailed breakdown on the quarter and our guidance.

....

Jennifer Walter

Executive Vice President & Chief Financial Officer, Moog, Inc.

Thanks, Pat. I'll begin with our first quarter financial performance. I'll then provide an update on our guidance for FY 2025.

We had a great start to the year from an earnings perspective. Sales were up nicely over last year's first quarter, and adjusted operating margin and earnings per share were strong. We continue to simplify our business. As a result, we took $6 million of charges largely associated with our footprint rationalization activities in the first quarter.

I'll now talk through our first quarter adjusted results, which exclude these charges. Sales in the first quarter of $910 million were 6% higher than last year's first quarter. Military Aircraft, Commercial Aircraft, and Space and Defense sales were up considerably, while Industrial sales were down due to our simplification efforts.

The most significant increases in segment sales were in Military Aircraft and Commercial Aircraft. In Military Aircraft, sales of $213 million were up 15% over the first quarter of last year. Activity on the FLRAA program began to ramp midway through FY 2023 and steadily has increased since that time, accounting for half of the sales increase this quarter. In addition, over the past couple of years, certain other development work has shifted into production, and we're seeing a ramp in that production that will continue for the next few years.

Commercial Aircraft sales of $221 million increased 14% over the same quarter a year ago. Aftermarket sales were particularly strong. It was a good quarter for repair activity. In addition, we're partnering with airlines to ensure they can meet early demand on their fleets, and this resulted in strong provisioning for spares. In addition, OE sales were up due to the timing of orders. In the second half of FY 2024, we saw short-term delay in sales, and we're now seeing those orders catch up, thereby increasing our sales.

Space and Defense sales of $248 million increased 8% over the first quarter last year. We're seeing broad-based defense demand that's driving the growth within this segment. This quarter, the growth is most notable for European defense needs and satellite and launch vehicle activity.

Industrial sales were $228 million in the first quarter. That's down 7% from the same quarter a year ago. Half of the decrease relates to the divestitures we completed at the beginning of the first quarter. Otherwise, sales in our Industrial Automation business have stabilized, consistent with the fourth quarter last year and down from the strong level a year ago.

Strength in our medical pump business, which reached a record high this quarter, helped to offset this decline as we benefited from a competitor's challenges.

We'll now shift to operating margin. Adjusted operating margin of 11.8% in the first quarter was up from 11.3% in the first quarter last year. Adjusted operating margins increased over the first quarter of last year in each of our segments. We achieved this margin expansion despite 80 basis points of pressure from recording an out-of-period warranty expense this quarter.

The most impactful increase was in Space and Defense where operating margin increased 90 basis points to 11.9%. This increase is associated with our strong growth, partially offset by a less favorable program mix and investments to prepare for upcoming major program.

Industrial operating margin was 13.2% in the first quarter, up 60 basis points. This increase is attributable to benefits from simplification initiatives, including the divestitures we completed at the beginning of the first quarter.

Military Aircraft operating margin was 11.0% in the first quarter, 50 basis points higher than in the first quarter last year. We benefited from efficiencies associated with higher volume on the FLRAA program and lower research and development expense. These benefits were partially offset by a less favorable sales mix.

Commercial Aircraft operating margin was 11.0%, up 40 basis points from the first quarter last year. Underlying operational performance was robust, reflecting very strong aftermarket sales. This strength was largely offset by 340 basis points of pressure related to recording the out-of-period warranty expense.

Putting it all together, adjusted earnings per share came in at $1.78, up 16% compared to last year's first quarter, despite $0.18 of pressure associated with the out-of-period expense. The increase is attributable to higher operating margin and additional operating profit associated with higher sales.

Let's shift over to cash flow. In the first quarter, we used $165 million of free cash flow. The use of cash was driven by working capital requirements. We use cash for physical inventory to support future sales growth. We also use cash for receivables as our strong collections in the first – in the fourth quarter last year left less to collect this quarter. In addition, timing of compensation payments impacted us in the first quarter.

Capital expenditures at $33 million were relatively light compared to recent quarters. We're continuing to invest in facilities and equipment to support longer term growth opportunities. The lower level of capital expenditures this quarter simply reflects timing, and we're expecting spend to pick up next quarter. Capital expenditures represent a key opportunity for us to invest for organic growth, and this continues to be a priority within our capital allocation strategy.

Over time, we strive to have a balanced approach to capital allocation. In that regard, we repurchased roughly 220,000 shares of our stock in the first quarter, spending just over $40 million. In addition, we remain committed to our dividend policy, and, as announced, we're increasing our quarterly dividend by 4% to $0.29 per share. Our leverage ratio was 2.4 times as of the end of the first quarter, nicely within our target range of 2 to 3 times.

We'll now shift over to our updated guidance for this year, which is unchanged from 90 days ago at a company level. Fiscal year 2025 is shaping up to be another strong year with growth in sales, continued operating margin expansion, and enhanced free cash flow generation. Both pricing and simplification will drive our operating margin expansion this year, while our focus on optimizing our planning and sourcing activities will contribute to our significant cash generation in the back half of this year. We're projecting sales of $3.7 billion in fiscal year 2025, a 3% increase compared to fiscal year 2024.

We're projecting sales growth in Space and Defense, Commercial Aircraft, and Military Aircraft, and expecting a decrease in sales in Industrial. We're maintaining the sales guidance for FY 2025 that we shared a quarter ago with a modest shift between segments to reflect what we've seen in the first quarter. We're increasing our sales guidance in Commercial Aircraft by $20 million to reflect a strong first quarter aftermarket activity. We're increasing sales guidance for Military Aircraft by $10 million to reflect our current run rate. And we're decreasing sales guidance by $30 million in Industrial to reflect the weakening of foreign currencies against the US dollar that we saw in the first quarter.

We're holding our adjusted operating margin for FY 2025 at 13.0%, a 60-basis-point increase over FY 2024, or 120 basis points after factoring out FY 2024 employee retention credit and FY 2025 out-of-period warranty expense. Operating margin will be 14.2% in Space and Defense, 13.1% in Military Aircraft, 11.0% in Commercial Aircraft, and 13.4% in Industrial, all the same as our previous guidance.

We're affirming our FY 2025 adjusted earnings per share guidance at $8.20, plus or minus $0.20. That's up 5% over FY 2024 or 14% normalizing for this year's out-of-period expense and last year's benefits that are not reflective of operational performance. For the second quarter, we're forecasting earnings per share to be $1.75, plus or minus $0.10. This reflects a similar operating margin in Q2 relative to Q1 with neither the out-of-period warranty expense, nor the extraordinary commercial aftermarket strength [ph] repeating (00:20:39) in Q2.

Finally, turning to cash. We're still projecting free cash flow conversion in FY 2025 to be in the 50% to 75% range, a solid improvement from the modest level of cash we generated in FY 2024. Free cash flow in the second quarter will improve markedly from the first quarter as we are projecting no cash usage in the second quarter. The real improvement though will be in the back half of the year as we reduce inventories from our planning and sourcing activities and collect on receivables. Overall, FY 2025 is shaping up to be another great year.

And now, I'll turn it over to Pat.

Patrick J. Roche

President, Chief Executive Officer & Director, Moog, Inc.

Thank you, Jennifer. Our first quarter was a strong start to the fiscal year. It provides us with increased confidence in our guidance for the year, and we will continue to see our performance improvements reflected in those results.

Now, let us turn it over to your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. [Operator Instructions] And your first question is from Jon Tanwanteng from CJS Securities. Your line is now open.

Jon Tanwanteng
Analyst, CJS Securities, Inc.

Q

Hi. Good morning. Thank you for taking my questions. My first one, Pat, is I was wondering if you could talk about your CCA involvements. It's nice to hear you're having some activity there. How much of an opportunity is that relative to other large programs such as FLRAA or F-35? And kind of when do you see that layering in?

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

A

Hi, Jon. Welcome to the call. Thanks for the question. Yeah. I think the reason for indicating our work on CCA is to say that we have relevant technologies that we can offer in this space, we have been engaged in conversations on several of the CCA programs, and we have development activity underway to prove out our concepts. So, it's early stages, I would describe. But as a mechanical component supplier into these, we feel that we have a valuable role that we can provide on the flight control side.

Jon Tanwanteng
Analyst, CJS Securities, Inc.

Q

Understood. And are you involved with all the players who are competing there? Or is it just one or two of those platforms?

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

A

Yeah. It's in the one or two. It's...

Jon Tanwanteng
Analyst, CJS Securities, Inc.

Q

Understood.

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

A

...less than a handful at this point.

Jon Tanwanteng
Analyst, CJS Securities, Inc.

Q

Got it. Okay. And then I was wondering if you could talk about the Boeing investment in the 787 production line. I was wondering how much capacity does that enable for them? Or is that more just catching back up to where they were producing before COVID? A little more detail on that and kind of what that kind of forecast of their production rates in the future, if that – if you have that kind of detail.

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.
A

Yeah. I mean, Boeing is still working towards achieving a rate of 10 for the 787 wide-body aircraft by the end of – by fiscal 2026. So, that's the goal, and their investment is to enable them to achieve that through the Charleston facility.

Jon Tanwanteng
Analyst, CJS Securities, Inc.
Q

Okay. Understood. And then finally, I was wondering how you drove some of the aftermarket orders with – in the Commercial space with Tewkesbury down. Is that just a testament to how quickly you're getting it back up? Or is there other capacity or – those orders for a future date?

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.
A

Yeah. I mean, our repair work goes through both Tewkesbury, but other facilities around the world as well. We have quite enough backlog of work on the aftermarket side, so we were able to get that through our production environment. So, that's what helped boost the sales level. We also provisioned airlines directly with spares that enables them to ensure fleet readiness. So, that was additional work that came through within the quarter. So, I would describe it as having a very strong book of business on the aftermarket side with the benefit of some additional work that we were able to push through during the quarter itself.

And if I turn to the Tewkesbury side, I think we got back to having our interim production environment working in a relatively short period of time, which is allowing us get production through that plant again and meet the customer commitments. We actually still have quite an amount of work to do to rebuild the full production environment. That gets us back to our, let me say, our full capacity where we have some headroom and some additional capability or capacity available to us. At the moment, we're very constrained with what we have, but we're working and we're getting stuff through the plant.

Jon Tanwanteng
Analyst, CJS Securities, Inc.
Q

Great. Thank you. I'll jump back in queue.

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.
A

Thank you very much, Jon.

Operator: Thank you. Your next question is from Michael Ciarmoli from Truist Securities. Your line is now open.

Michael Ciarmoli
Analyst, Truist Securities, Inc.
Q

Hey.

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.
A

[ph] Michael, good morning (00:25:55).

Michael Ciarmoli
Analyst, Truist Securities, Inc.

Q

Good morning, guys. Good morning. Nice results. Thanks for taking the question. Pat, maybe just to stay on that aftermarket a bit – and I don't know how you want to take this – but you called out in the release the warranty expense, excluding that 14.4% margins. That looks to be a multiyear high.

I guess two questions. Why didn't you opt to just adjust out that warranty expense? I can't recall, and I checked my notes. I don't know when the last time you had one of those charges were. And I guess should we think about that level being sustainable? It sounds like you got a lot of aftermarket through some provisioning, but just trying to get some color on that 14.4% as it relates to kind of longer term targets, and you're going to get some [ph] volume (00:26:47) increases. So, how should we think about that?

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

A

I think we had a really good quarter, obviously. And if you back it out – back out that onetime expense, it was very strong, and it is a record margin quarter for the Commercial Aircraft group. So, all that is correct, Michael. We anticipate continuing strength on the aftermarket side, but we had the extra boost coming through from that provisioning and getting some of our Tewkesbury output back out again. So, there's some gain coming from those things, but we're just not banking on that repeating in the subsequent quarters. But we do still have a really solid level of aftermarket business planned in for the rest of the year.

Michael Ciarmoli
Analyst, Truist Securities, Inc.

Q

Okay. Okay. So, within...

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

A

But I think it is a positive story, Michael, about that strength in the aftermarket and...

Michael Ciarmoli
Analyst, Truist Securities, Inc.

Q

Okay.

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

A

...operational improvement on the Commercial side.

Michael Ciarmoli
Analyst, Truist Securities, Inc.

Q

Got it. So, fair to say more skewed towards aftermarket versus OE, there wasn't any additional pricing, maybe just kind of ongoing operational excellence and improvements on the OE side?

Jennifer Walter
Executive Vice President & Chief Financial Officer, Moog, Inc.

A

The aftermarket was a significant driver to the underlying performance that we saw...

Michael Ciarmoli
Analyst, Truist Securities, Inc.

Q

Okay.

Jennifer Walter
Executive Vice President & Chief Financial Officer, Moog, Inc.

A

...in the operating margin performance. And to your question, as far as the out-of-period adjustment, yeah, you can think of this as it's not an ongoing type of thing. It doesn't change our warranty expense going forward or anything like that. That's why we tried to give you a trail to say how much was included in our numbers. Typically, in our adjustments, we only keep things like restructuring and those types of activities in there.

Michael Ciarmoli
Analyst, Truist Securities, Inc.

Q

Yes. Fair. Jennifer, do you have the Commercial OE revenue growth and aftermarket growth in the quarter handy?

Jennifer Walter
Executive Vice President & Chief Financial Officer, Moog, Inc.

A

Yeah. They were – they actually both grew. Aftermarket was a little bit more of growth than the – a little more than half of the growth compared to the total growth in the segment.

Michael Ciarmoli
Analyst, Truist Securities, Inc.

Q

Okay. Perfect. And then just shifting on Industrial, I think you called out that the bookings were greater than – book-to-bill was greater than 1 time. Any color there what drove – what you're kind of seeing in those markets? It sounds like you've got presumably better visibility here, and whether or not that bookings trend kind of continues.

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

A

Yeah. I mean, I think this is a long-running story, Michael, where we've been talking about that softening of the economy in Germany, and then therefore the softening in our orders. As you know, that predominantly affects the Industrial Automation piece of the business, and we've had some counterbalancing going on because medical has been strong. We actually had record sales in our medical pumps business in this quarter. We had in prior quarters some strength in the simulation and test, which was helping us as well.

But if I take those back out of it and I just focus on that Industrial Automation piece, that Industrial Automation piece, I believe, is relatively stable at this point. That's what I was saying in the fourth quarter. And when I look forward, I still have that view that we keep running at roughly the same level of Industrial Automation activity through fiscal 2025.

Michael Ciarmoli
Analyst, Truist Securities, Inc.

Q

Okay. Okay.

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

A

So, the message is stable, and the book-to-bill is a positive sign. We'd like to see that continue for another few quarters before we are certain that the business is picking up again, but that's still in line with what we built into the 2025 plans by saying that it was going to be stable for the year.

Michael Ciarmoli
Analyst, Truist Securities, Inc.

Q

Got it. Okay. And then just one last one for me. The second quarter earnings guidance at the midpoint sequentially down versus first quarter. I think that's kind of an anomaly for you guys. Can you give any color as to why we should expect earnings to be down at the midpoint versus the first quarter here?

Jennifer Walter
Executive Vice President & Chief Financial Officer, Moog, Inc.

A

Yeah. Largely, it's about the same. We've got – when we think about the out-of-period and the warranty, we think about either one of those repeating into the next quarter. So, largely, it's pretty much flat. Just a small tick down in EPS.

Michael Ciarmoli
Analyst, Truist Securities, Inc.

Q

Okay. Fair. Thanks, guys. I'll jump back in the queue.

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

A

Thanks, Jon – Michael.

Operator: Thank you. Your next question is from Jack Ayers from TD Cowen. Your line is now open.

Jack Ayers
Analyst, TD Securities (USA) LLC

Q

Yeah. Hey. Thanks, guys. Good morning.

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

A

Good morning, Jack.

Jack Ayers
Analyst, TD Securities (USA) LLC

Q

Just – good morning. Quick question on cash, Jennifer. I would love to kind of dig in on – you burned $165 million this quarter. Just kind of moving forward, some of the buckets of working capital, I don't know if you want to hit on inventory or unbilled. So, just how we get conviction in that free cash flow conversion guide reiterated? Thanks.

Jennifer Walter
Executive Vice President & Chief Financial Officer, Moog, Inc.

A

Yeah. Yeah. So, I can go through it. I'll start with Q2 then, and then basically for the rest of the year. The improvement that we're going to see in Q2 – so, again, I said we're not going to have a use of cash in Q2 – we're going to see it come across a number of places. So, if I do it relative to where we were in Q1, physical inventories will improve. We do have stronger shipments that we've got line of sight too, and milestones that are going to help our physical inventories.

We also had the compensation payments in Q1, which is normally happens in Q1. It doesn't happen in Q2. So, that is actually another benefit from Q1 to Q2 as we look there.

Customer advances is another one. We do have some defense advances that are on the horizon for us that we expect to come in in the second quarter.

And finally, in receivables, while still a use of cash, not the level of use of cash that we had in the first quarter. In the first quarter, we just had that excessive level of pressure because we had such strong collections in the fourth quarter. So, we're seeing a little bit of an up and down, which is quite typical for our receivables. So, there's a number of things that are driving our improvement in the second quarter.

As I mentioned though, the real improvement that we're going to see where we're going to generate the cash is going to be in our third and fourth quarters, and it's going to be in a number of places. Physical inventories is a really important place for us. Again, we're going to have a strong operational performance. There's milestones and things that we've got going on there.

In physical inventory, we've got an increase in OE shipments. We're also taking efforts to constrain our incoming levels of inventory. We're optimizing our buffer stock levels so that we are reducing it in the places where we can still meet our customers' requirements, but not carry higher levels of inventory. And we're reducing excess levels of production to only what we need in areas where we can do that without risk to deliveries. We also – the benefit that Pat talked about as far as the Tewkesbury output, that's recovering. It's drawing down inventory. And to the extent we can, we are delaying receipts and pushing out demand in our supply chain.

We are starting these activities. It takes a little while for that to turn through. So, that's why we don't have the significant amount of relief in the second quarter, but we are projecting these things to materialize and get into our financial results in the back half of the year.

The other area that we'll see improvement in the back half of the year is going to be in receivables. We're looking to have the strong collections, and then including on some milestones that are on the horizon as well. So, we've got some visibility as far as that goes as well. So, those will be the big drivers in the back half of the year.

So, with those activities that we've got in place, the customer advances that we have some line of sight to, the collections that we've got in place, we're feeling confident to hold our 50% to 75% free cash flow conversion through the year.

Jack Ayers
Analyst, TD Securities (USA) LLC

Q

Okay. Okay. That's awesome.

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

A

And then...

Jack Ayers
Analyst, TD Securities (USA) LLC

Q

Yeah. Go ahead. Sorry.

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

A

Sorry, Jack. I was just going to say, where we've been working to drive increased profitability with defined initiatives, we have a similar approach now internally on cash flow. And we know what we're trying to drive within each of the businesses, and we're tracking that as we go through into each of our internal reviews to make sure we are delivering.

Jack Ayers
Analyst, TD Securities (USA) LLC

Q

Okay. That's good insight. And I guess just switching gears back to Commercial – and I'm not sure if you covered it, Pat. Just maybe an update on OE rate just kind of assumptions, maybe 787, A350, because it looks like Commercial OE was actually up pretty strongly sequentially from Q4 to Q1, which is kind of surprising. Just any update on OE assumptions, where you were, and where you're kind of looking to go to through 2025 would be helpful. Thanks.

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

A

So, I think both of us are going to come in on this one, Jack. So, just the first high-level comment, I mean, when we built out the FY 2025 plan, we had lots of conversations back and forth with the customers on the wide-body programs, which are really important to our numbers. And we have strong alignment now between their plans and our plans, and are very confident in those levels that we have loaded into our plan. So, that's the first comment. And we've seen no change in that over the last 90 days. So, I would describe that as very stable for us at the moment.

And, Jennifer, you had a comment as well.

Jennifer Walter
Executive Vice President & Chief Financial Officer, Moog, Inc.

A

Related to the back half of last year and the strong OE this quarter, it's an element basically just of timing. In the third quarter last year, we actually started to see a short-term delay, and that carried in both Q3 and in Q4 related to some orders – ordering patterns of a customer. That has normalized, and we've essentially caught up in those orders. So, it's really just affecting the timing of orders that has otherwise been very stable and normalized. A little bit of a down dip in the last half of last year when we actually brought our sales guidance down. Now we've actually seen the catch-up of those orders, have fulfilled such that we could have that higher level that we saw this time. So, it's more – so we got a little bit of a pop from that catch-up.

Jack Ayers
Analyst, TD Securities (USA) LLC

Q

Got it. Thank you.

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

A

Great.

Operator: Thank you. Your next question is from Jon Tanwanteng from CJS Securities. Your line is now open.

Jon Tanwanteng
Analyst, CJS Securities, Inc.

Q

Hi. Thanks for the follow-up. I was just curious about the medical device business. You've mentioned to me that it achieved a record. Based on a competitor having challenges, I'm wondering how long that window might be open for. And do you expect a reversal or just stabilization if your competitor catches up?

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

A

Think about the timeframe around those type of events in the six or nine months period. It's – it takes a little bit of time to work through issues when they do arise, and that's what our competitor is experiencing. We have been gaining from this over the prior quarter, and we will continue to for the rest of the year. So, we're up mid single digits to high single digits relative to the prior year in that product line.

Jon Tanwanteng
Analyst, CJS Securities, Inc.

Q

Okay. And would you expect to give that back or more of maybe hold some of the share that you took when you compare [indiscernible] (00:38:55)?

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

A

Yeah. We would expect to hold, Jon, because once you get that fleet out into the field, it continues actually to draw down consumables from us as well. So, people don't like flipping or moving around too much. So, I think it's relatively sticky.

Jon Tanwanteng
Analyst, CJS Securities, Inc.

Q

Okay. Got it. That's what I thought. Okay. And then just could you maybe provide a little more detail on your international exposure by currency? I know you mentioned the headwind in the Industrial business, but I know you do have foreign military sales as well. Are those sales in dollars? Or are they denominated in any other currency?

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

A

So, that question is relating to our sales rather than our purchases, is that right? You're not – they're not full.

Jon Tanwanteng
Analyst, CJS Securities, Inc.

Q

Correct. Yes. Correct.

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

A

You're [ph] not on the tariff line (00:39:39) here? Yeah. Okay.

Jon Tanwanteng
Analyst, CJS Securities, Inc.

Q

Yeah.

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

A

[ph] We're just calling it up (00:39:42) for you. Sorry, Jon. We're nearly there.

Jon Tanwanteng
Analyst, CJS Securities, Inc.

Q

No worries. We can also do it off-line later if you need.

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

A

Yeah. Well, I just could give you a quick summary now. Our sales regionally, let's say, 72% of the sales for fiscal 2024 were in the US, 18% in Europe, 3% in Asia-Pacific, and then 7% in various other currencies around the world.

Jon Tanwanteng
Analyst, CJS Securities, Inc.

Q

Okay. Great. Thank you.

Operator: Thank you. There are no further questions at this time. I will now hand the call back to Pat Roche for the closing remarks.

Patrick J. Roche
President, Chief Executive Officer & Director, Moog, Inc.

Thank you. Thanks very much for the questions, everyone. That closes out our first quarter call. It's been a good quarter for us and a good start to the year. Strong sales, record orders, impressive margin performance. We have had heavy use of cash in the quarter, but we can see a line of sight to improving that in the back half of the year. So, we remain confident in our full year guidance.

So, thank you for your time and attention, and look forward to talking to you again on the next call.

Operator: Thank you. Ladies and gentlemen, the conference has now ended. Thank you, all, for joining. You may all disconnect your lines.