Q4 2022

1. Organic growth drivers
- **Narrative:** Management highlighted that the company anticipates robust growth in the engine business as a key driver of organic revenue increase. This growth is expected to stem from the engine manufacturers' need to catch up from the previous year's shortfalls and accommodate future rate increases. The strategic focus on the engine segment is poised to contribute significantly to the company's overall financial performance in the upcoming quarters.
- **Management's Guidance:**
- Management is optimistic about achieving a higher rate of commercial revenue growth in the engine business, potentially reaching around 20% as the company progresses through Q2 and Q3. This anticipated growth is positioned to align with above-trend growth projections for 2023, 2024, and 2025, translating into increased profits and cash flow generation.
- **Actual Results:**
['Q3', '2023']:
- Engine Products: Revenue increased by 17% year-over-year; Adjusted EBITDA Margin was 27.4%.
['Q4', '2022']:
- Engine Products revenue increased by 21% year-over-year in Q4 2022, which aligns with the management's guidance of around 20% growth in the engine business.
['Q1', '2023']:
- Engine Products' revenue was $795 million, an increase of 26% year-over-year.
['Q2', '2023']:
- Engine Products revenue increased by 26% year-over-year in Q2 2023, which aligns with the management's optimistic guidance of achieving around 20% commercial revenue growth in the engine business. This growth exceeded expectations, contributing to the overall financial performance of the company.
- **Evaluation:**
- Expectations Exceeded: The engine business achieved a revenue increase of 26% in Q1 and Q2 2023, surpassing the management's guidance of around 20% growth, indicating stronger-than-expected performance.

2. Revenue diversification
- **Narrative:** In Q4 2022, HowmetAero's management emphasized their strategic focus on revenue diversification. They acknowledged potential challenges in the wheels business, anticipating a revenue decline in the upcoming year. However, they highlighted growth opportunities in the titanium segment, projecting an increase as the year progresses.
- **Management's Guidance:**
- Management anticipates a $50 million to $60 million revenue decline in the wheels segment, primarily impacting the second half of the year. Conversely, they expect growth in the titanium segment throughout 2023.
- **Actual Results:**
['Q1', '2023']:
- Revenue for Q1 2023 is $1.603B, with a Russian Titanium Share Gain of approximately $20M.
['Q2', '2023']:
- Revenue Q2 2023: $1.648B
['Q3', '2023']:
- Data Not Available
['Q4', '2022']:
- Revenue figures for Q4 2022 show third-party revenue of $285 million, which reflects the company's performance in the specified period.
- **Evaluation:**
- Expectations Met: Management anticipated a $50-$60 million revenue decline in the wheels segment, while expecting growth in the titanium segment. The actual results for Q1 2023 show a Russian Titanium Share Gain of approximately $20 million, aligning with management's guidance of growth in the titanium segment.

3. Earnings per share trends
- **Narrative:** The management has provided specific guidance around their earnings per share (EPS) expectations for the upcoming quarters. They have highlighted certain financial impacts related to increases in non-service pension and OPEB expenses, which will affect the EPS. Furthermore, they have laid out precise EPS estimates along with their revenue and EBITDA projections, illustrating a structured outlook for their financial performance.
- **Management's Guidance:**
- - The non-service pension and OPEB expense is expected to increase by approximately $20 million year-over-year, adversely impacting the EPS by approximately $0.04 per share.
- - For the upcoming quarter, the expected EPS is $0.37, plus or minus $0.02.
- - For the full year, the expected EPS is $1.60, plus or minus $0.07.
- **Actual Results:**
['Q2', '2023']:
- Adj Earnings Per Share for Q2 2023 was $0.44, which was up 26% year-over-year, and exceeded the high end of guidance.
['Q3', '2023']:
- Adjusted Earnings Per Share for Q3 2023 was $0.46, up 28% year-over-year, exceeding the high end of the guidance.
['Q4', '2022']:
- EPS (GAAP) for Q4 2022 was reported as $0.26, which is below the management's guidance of $0.37, plus or minus $0.02.
['Q1', '2023']:
- Adjusted Earnings Per Share for Q1 2023 is $0.42, which was up 35% year-over-year, exceeding the high end of guidance.
- **Evaluation:**
- Expectations Exceeded: The actual EPS for each quarter in 2023 significantly surpassed the high end of management's guidance, indicating that the company's earnings performance exceeded expectations despite the anticipated negative impacts on EPS from increased non-service pension and OPEB expenses.

4. Cost management strategies
- **Narrative:** Management has focused on aligning operational efficiency with cost management strategies by optimizing labor resources. The strategic actions taken include trimming labor to manage costs effectively, while simultaneously preparing for future growth by entering a recruitment phase to ensure readiness for increased demand.
- **Management's Guidance:**
- Management anticipates that the actions taken will allow for restoration of margins to levels observed in the first half of 2022. This is supported by a cautious yet optimistic outlook on future rate builds and increases, indicating no fundamental issues in achieving these margin goals.
- **Actual Results:**
['Q2', '2023']:
- Data Not Available
['Q3', '2023']:
- Data Not Available
['Q4', '2022']:
- Data Not Available
['Q1', '2023']:
- Data Not Available
- **Evaluation:**
- Insufficient Info: Data not available.

5. Debt reduction strategies
- **Narrative:** Management has outlined a proactive approach to debt reduction, emphasizing the strategic timing of bond maturities and the maintenance of liquidity through an undrawn revolving credit line. This approach is indicative of their commitment to reducing interest costs and enhancing financial stability.
- **Management's Guidance:**
- Management has indicated that the next bond maturity is scheduled for October 2024, with the $1 billion revolver remaining undrawn, reflecting a disciplined approach to managing debt obligations. They also project a continued year-on-year reduction in interest costs, with 2023 expected to see lower interest expenses compared to 2022.
- **Actual Results:**
['Q2', '2023']:
- We repurchased approximately $176 million of bonds last quarter, which will lower annualized interest costs by an additional $9 million. Net debt to EBITDA improved to a record low of 2.5 times, while bond debt is unsecured and at fixed rates. We amended and extended our $1 billion undrawn credit facility to 2028, providing lower fees and more favorable covenants.
['Q3', '2023']:
- Debt Reduction of ~$200M in Q3, ~$376M Q3 YTD; Annualized Interest Expense savings ~$10M and ~$19M, respectively.
['Q1', '2023']:
- In Q1 2023, Howmet Aerospace reduced the 2024 debt tower by approximately $176 million using cash on hand, resulting in an annualized interest expense savings of approximately $9 million. The net debt-to-LTM EBITDA ratio remained at 2.6x with all long-term debt unsecured at fixed rates, and the $1 billion revolver remained undrawn.
['Q4', '2022']:
- In Q4, Howmet Aero repurchased $9M of debt with cash on hand; for the full year, they repurchased $69M of debt, resulting in annualized interest expense savings of approximately $4M. The net debt-to-LTM EBITDA was reported at a record 2.6x, with all long-term debt unsecured at fixed rates. The $1 billion revolver remained undrawn.
- **Evaluation:**
- Expectations Exceeded: The management's proactive debt reduction strategy surpassed expectations, with a total debt reduction of approximately $376 million year-to-date by Q3 2023 and annualized interest expense savings of $19 million, exceeding the projected savings and demonstrating enhanced financial stability.

6. Dividend distribution
- **Narrative:** During the Q4 2022 earnings call, Howmet Aerospace's management emphasized their commitment to returning value to shareholders through dividend distribution. The discussion highlighted a plan to increase the dividend payout, reflecting confidence in the company's financial health and future cash flow generation capabilities.
- **Management's Guidance:**
- Management indicated that they expect to increase dividends to approximately $68 million in 2023.
- **Actual Results:**
['Q3', '2023']:
- Paid Quarterly Dividend at $0.04 per share of Common Stock in Q3. John Plant announced a 25% increase in the dividend on top of last year's 50% increase. The quarterly stock dividend was $0.04 per share.
['Q2', '2023']:
- Paid Quarterly Dividend at $0.04 per share of Common Stock in Q2 2023. In the second quarter, the quarterly stock dividend was $0.04 per share after it was doubled in the fourth quarter of last year.
['Q4', '2022']:
- In the fourth quarter, the quarterly common stock dividend was doubled to $0.04 per share, dividends in 2022 were $44 million.
['Q1', '2023']:
- Paid Quarterly Dividend at $0.04 per share of Common Stock in Q1 2023. The quarterly common stock dividend remained at $0.04 per share after it was doubled in the fourth quarter of last year.
- **Evaluation:**
- Expectations Met: The management's guidance to increase dividends to approximately $68 million in 2023 was met, as evidenced by the 25% increase in the dividend after a 50% increase the previous year, culminating in a consistent quarterly dividend of $0.04 per share throughout 2023.

7. Cash balance management
- **Narrative:** During the Q4 2022 earnings call, management emphasized a stable approach to cash balance management. They highlighted their strategy to

maintain consistent pension and OPEB cash contributions, indicating a focus on sustaining their financial obligations without significant fluctuation. Additionally, they outlined their capital expenditure plans, reinforcing a commitment to invest in growth while managing cash flow effectively.

- **Management's Guidance:**

- Pension and OPEB cash contributions are expected to remain flat compared to 2022, approximately totaling $56 million for the year. Capital expenditures are projected to be within the range of $230 million to $260 million. The company provided a free cash flow guidance of $615 million, with a variance of plus or minus $35 million.

- **Actual Results:**

['Q1', '2023']:

- Free cash flow was negative $41 million in Q1 2023, with expectations of positive free cash flow in the next three successive quarters. The ending cash balance was $538 million, after approximately $218 million of capital allocation, debt reduction of $176 million, common stock repurchases of $25 million, and quarterly dividends of $17 million. Capital expenditures were $64 million in the quarter.

['Q2', '2023']:

- Record Q2 Free Cash Flow of $188 million, with an ending cash balance of $536 million.

['Q3', '2023']:

- For Q3 2023, the Pension/OPEB Contributions were reported as $56 million, and the Capital Expenditures ranged from $225 million to $245 million. The Free Cash Flow was $132 million, which is below the initial guidance range.

['Q4', '2022']:

- Year-end cash balance was a healthy $792 million after approximately $513 million of capital allocation to common stock repurchases, 2024 bond repurchases, and the quarterly dividends. Free cash flow for the year was a record $540 million, including an inventory build of approximately $235 million.

- **Evaluation:**

- Expectations Not Met: The free cash flow guidance was not met, as the actual free cash flow for Q3 2023 was below the initial guidance range, despite stable Pension/OPEB contributions and capital expenditures within the expected range.

8. Production rate guidance

- **Narrative:** Management provided insights into their production rate expectations, reflecting both caution and awareness of major aircraft manufacturers' plans. They expressed readiness to adjust to higher production rates as indicated by Boeing and Airbus, while also highlighting their current production commitments and long-term agreements (LTAs) which are well on track.

- **Management's Guidance:**

- Boeing reiterated their outlook of 50 units per month for 2025 and 2026, indicating alignment with the anticipated production rates. Should production rates reach higher levels, such as 38-42 units or Airbus rates of 57-58, management is confident in their ability to meet these demands with approximately six months lead time. Current projections for production rates are intentionally cautious, with expectations of 30 units for the 737 and 53-54 units for the A320, acknowledging these figures as potentially conservative. The company's long-term agreements are nearly complete for 2023, providing stability and predictability in production planning. Boeing's target for 10 units per month for the 787 by 2026 is seen as realistic, with similar expectations for Airbus A350 production.

- **Actual Results:**

['Q2', '2023']:

- Data Not Available

['Q3', '2023']:

- Data Not Available

['Q4', '2022']:

- Data Not Available

['Q1', '2023']:

- Data Not Available

- **Evaluation:**

- Insufficient Info: Data not available.

9. Commercial aerospace trends

- **Narrative:** Management outlined expectations for significant growth in the commercial aerospace sector, driven by robust production schedules and increased demand for major aircraft models from Boeing and Airbus. The company anticipates strengthening market conditions, particularly in the latter half of the year, reflecting positive trends in the aerospace industry.

- **Management's Guidance:**

- Management projects a 17% growth in Commercial Aerospace for the year 2023, supported by the outlined production rates of approximately 30 units per month for the Boeing 737 MAX, 53 to 54 units for the Airbus A320 and A321, around 30 units for the Boeing 787 annually, and 65 to 70 units for the Airbus A350. There is an expectation of enhanced performance in the second half of the year based on these build assumptions. Additionally, Airbus is anticipated to reach a production rate of 65 A320s by mid-2024, which aligns with current projections.

- **Actual Results:**

['Q2', '2023']:

- In Q2 2023, management reported that commercial aerospace increased by 23% year-over-year, with continuous growth over 9 consecutive quarters and representing 47% of total revenue.

['Q3', '2023']:

- Ken Giacobbe reported that commercial aerospace increased 23% year-over-year, driven by all three aerospace segments.

['Q4', '2022']:

- In Q4 2022, management reported that commercial aerospace revenue was up 29% year-over-year, with growth continuing for seven consecutive quarters. Commercial aerospace accounted for 48% of total revenue, although it remained below the pre-COVID level of 60%. There was also commentary indicating that commercial aerospace performance was strong and up 29% for the quarter.

['Q1', '2023']:

- Commercial Aerospace was up 15% driven by the narrow-body recovery.

- **Evaluation:**

- Expectations Exceeded: The management projected a 17% growth in commercial aerospace for 2023, but the actual results showed a 23% year-over-year increase by Q2 2023, surpassing the expected growth rate and indicating stronger-than-anticipated demand and performance in the commercial aerospace sector.

10. Defense sector opportunities
- **Narrative:** Management highlighted the strength in demand for the F-35 program as a key driver for growth in the defense sector. The company is optimistic about continued high production rates and expects this to contribute positively to their market position throughout the decade.
- **Management's Guidance:**
- Management anticipates low-single-digit increases in 2023, driven by a robust demand for the F-35, along with increased needs for engine spares and upgrades to meet the 2028 Block 4 requirements.
- **Actual Results:**
['Q2', '2023']:
- John Plant reported that defense sales were strong, increasing by 17%. Additionally, Ken Giacobbe noted that defense aerospace saw a 17% year-over-year increase, driven by the F-35 in legacy fighter programs. The F-35 backlog continued to grow, with recent orders including 126 aircraft for the US government, 25 for Israel, and 25 for the Czech Republic.
['Q3', '2023']:
- Defense Aerospace was up 13% year-over-year driven by the F-35 and Legacy Fighter programs.
['Q4', '2022']:
- Defense Aerospace was up 13% in the fourth quarter, driven by year end seasonality and down 3% for the full year.
['Q1', '2023']:
- Defense Aerospace was up 11% year-over-year.
- **Evaluation:**
- Expectations Exceeded: Management anticipated low-single-digit increases for 2023, yet defense sales surged by 17% in Q2 and 13% in Q3, significantly surpassing expectations due to strong demand for the F-35 program.

11. Commodity price volatility
- **Narrative:** Management highlighted the challenges posed by commodity price volatility, emphasizing the need to effectively manage rising material and inflationary costs. This volatility is a significant operational challenge that the company is actively addressing through strategic measures.
- **Management's Guidance:**
- Management anticipates that the combination of material and inflationary costs will be in the range of $70 million to $100 million for the year.
- **Actual Results:**
['Q1', '2023']:
- Material and other inflationary cost pass through (35)
['Q2', '2023']:
- Data Not Available
['Q3', '2023']:
- Data Not Available
['Q4', '2022']:
- Data Not Available
- **Evaluation:**
- Insufficient Info: Data not available.