Elbit Systems Ltd.
Conference Call
August 14, 2024

Operator: Ladies and gentlemen, thank you for standing by.

Welcome to the Elbit Systems second quarter 2024 results conference call. All participants are at present in a listen-only mode. Following management's formal presentation, instructions will be given for the question-and-answer session. As a reminder, this call is being recorded.

I would now like to hand over the call to David Ravia, Elbit Systems' Investor Relations Director.

David, please go ahead.

David Ravia: Thank you, operator.

Good day everyone, and welcome to our second quarter 2024 Earnings Call. On the call with me today are Butzi Machlis, our President and CEO and Kobi Kagan our CFO.

Before we begin, I would like to point out that the Safe Harbor Statement in the Company's press release issued earlier today also refers to the contents of this conference call.

As we do every quarter, we will provide you with both our regular GAAP financial data and certain supplemental non-GAAP information. We believe that this non-GAAP information provides additional details to help understand the performance of our business. You can find all the detailed GAAP financial data, as well as the non-GAAP information and the reconciliation, in today's press release.

Kobi will begin by providing a discussion of the financial results, followed by Butzi who will talk about some of the significant events during the quarter and beyond. We will then turn the call over to a Q&A session.

With that, I would like now to turn the call over to Kobi.

Kobi – please.

Kobi Kagan: Thank you, David,

Hello everyone and thank you for joining us today.

The second quarter of 2024 yielded positive results, driven by a 12% year-over-year increase in revenues, additional growth of our backlog that now exceeds 21 billion dollars, and improved profitability.

I will now highlight and discuss key figures and trends in our financial results.

Second quarter revenues reached 1 billion 626 million dollars compared to 1 billion 454 million dollars in the second quarter of 2023. This reflects 12% growth and is the second quarter in a row in which we have experienced low double digits revenue growth.

In the second quarter of 2024, Europe contributed 29% of revenues, North America 23% of revenues, Asia-Pacific 15% of revenues and Israel contributed 27% of revenues.

It should be noted that our diverse geographic revenue distribution is a very important factor for the long-term sustainability of our business.

Israeli revenues grew from 245 million dollars in the second quarter of 2023 to 444 million dollars in the second quarter of 2024. This growth reflects the increased demand for a broad range of our solutions following the breakout of the Swords of Iron war.

In addition, we see growth in North America revenues due to increasing demand for Maritime and Warfighter systems.

The non-GAAP gross margin for the second quarter was 24.4%, compared to 26.1% in the second quarter of 2023.

GAAP gross margin in the second quarter was 24.0% of revenues compared to 25.6% in the second quarter of 2023.

The second quarter non-GAAP operating income was 130.5 million dollars or 8.0% of revenues, compared with 115.5 million dollars or 7.9% of revenues in the second quarter of last year. GAAP operating income for the second quarter was 116.5 million dollars or 7.2% of revenues, compared to 101.6 million dollars or 7.0% of revenues in the second quarter of 2023. This growth in operating income and expansion in operating margin are the result of increased operating expenses efficiency.

The operating expense breakdown in the second quarter was as follows:

- Net R&D expenses were 116.8 million dollars or 7.2% of revenues, compared to 93.4 million dollars or 6.4% of revenues in the second quarter of 2023. This increase was due to additional R&D efforts in our Land segment, and continuous investment in high power laser solution.
- Marketing and selling expenses were 87.7 million dollars or 5.4% of revenues, versus 101.7 million dollars or 7.0% in the second quarter of 2023.
- G&A expenses were 68.7 million dollars or 4.2% of revenues, compared to 75.4 million dollars or 5.2% of revenues in the second quarter of 2023.

Financial expenses were 29.1 million dollars in the second quarter of 2024, compared to 32.1 million dollars in the second quarter of 2023.

The financial expenses amount reflects the enduring tightened monetary policy implemented by central banks in the markets in which Elbit operates, including the Bank of Israel and the United States Federal Reserve, in response to rising inflation, by retaining interest rates at a high level. Additionally, our rapidly growing backlog due to the Swords of Iron war, required higher levels of working capital and capital expenditures.

We recorded a tax expense of 11.3 million dollars in the second quarter of 2024, compared to 9.2 million dollars in the second quarter of 2023.

The effective tax rate in the second quarter of 2024 was 13.2% compared to 13.6% in the second quarter of 2023.

Our Non-GAAP diluted EPS was 2 dollars and 8 cents for the second quarter of 2024 compared to 1 dollar and 65 cents in the second quarter of 2023.

GAAP diluted EPS was 1 dollar and 76 cents for the second quarter of 2024 compared to 1 dollar and 40 cents in the second quarter of 2023.

We can see a 26% increase in both Non-GAAP and GAAP diluted EPS in the second quarter of 2024 compared to the second quarter of 2023.

We remain focused on profitability with the aim of achieving additional growth in the next quarters of 2024.

I will now review the second quarter of 2024 year-over-year performance of our business segments. Note that our segmental disclosure is provided on a GAAP basis.

Aerospace revenues were almost similar year-over-year with a small 1% decrease.

C4I and Cyber revenues increased by 11% year-over-year mainly due to radio systems sales.

ISTAR and EW revenues increased by 9% year-over-year, mainly due to Electronic Warfare and Electro Optic systems sales in Israel and Asia Pacific.

Land revenues increased by 37% year-over-year, mainly due to increased ammunition and munitions sales in Israel.

Elbit Systems of America revenues increased by 11% year-over-year.

Our order backlog as of June 30, 2024 reached 21.1 billion dollars, 5 billion dollars higher than our backlog at the end of the second quarter of 2023. Approximately 2.5 billion dollars of this increase came from Israel.

In the second quarter of 2024 the company recorded new orders of 2.4 billion dollars, of which 1.1 billion dollars came out from the Israeli market. Approximately 69% of the current backlog is attributable to orders from outside of Israel. Approximately 43% of the current backlog is scheduled to be performed during 2024 and 2025, while the rest is scheduled to be performed during 2026 and after, which demonstrates the potential growth of the company.

Operating cash flow for the six months ending June 30, 2024 was 26.0 million dollars inflow, compared to 210.7 million dollars outflow for the same period last year. We continue to increase inventories to support the increasing backlog.

The Board of Directors has declared a dividend of 50 cents per share.

I will now turn the call over to Mr. Machlis, Elbit's CEO.

Butzi, please go ahead.

Butzi Machlis: Thank you Kobi.

I would like to start by expressing our sincere gratitude to all Elbit employees worldwide for their unwavering dedication and commitment to our customers in Israel and abroad. Our workforce deserves special recognition for their extraordinary efforts over the past several months, in meeting the urgent needs of the IMOD during the recent conflict, and supporting our international customers.

I, along with the entire company, wish for the immediate return of all hostages held captive in Gaza – they are in our hearts and mind and we are waiting for their return home.

In line with the previous quarter, we are pleased to report continued growth in our order backlog, which now exceeds $21 billion. Revenue increased by approximately 12%, and profitability improved.

Two key factors have been instrumental to our success: Elbit Systems' extensive geographic footprint across Europe, North America, Asia, and Israel; and our portfolio of advanced technological solutions, proven effective in the context of rising global defense budgets.

Elbit Systems remains committed to expanding its global presence while fulfilling our customer commitments.

Our Company continues to implement its transformation plan aiming to meet our internal target of $7 billion revenues, which I believe will be achieved ahead of schedule, and our internal target of around 10% operating margin.

Despite the significant increase in revenues from the Israeli market, the majority of our revenues are generated outside of Israel and our primary focus remains the international market. While supply chain challenges still exist, our diversified supplier base has mitigated their impact. International revenues accounted for 73% of total revenue in the second quarter.

We were pleased to announce several recent international contracts awards that enhance our global presence.

Last week, for example, we announced a $270 million contract to supply rocket artillery to an international customer over a four-year period.

On April 25, 2024, Elbit America celebrated the delivery of the 3,000th F-35 Helmet Mounted Display System (“HMDS”) from the company's site in Merrimack, N.H. The F-35 Gen. III Helmet Mounted Display System is an advanced helmet-mounted display system.

In addition to several contract wins in Israel and the Netherlands for example, we secured an initial $37 million contract in May 2024 to supply Iron Fist Active Protection Systems (APS) to General Dynamics Ordnance and Tactical Systems for upgrades to the US Army Bradley vehicles. This 24-month contract offers significant growth potential. Furthermore, we recently announced a $130 million contract with BAE Systems Hägglunds for Iron Fist APS integration into the CV90 Infantry Fighting Vehicle (IFV) as part of a project of a European country, marking another strategic partnership.

The Iron Fist system provides 360-degree protection against a wide range of anti-armor threats, including rocket-propelled grenades and kinetic energy tank rounds, in both open terrain and urban environments. This advanced technology is the result of substantial R&D investment. The system's growing global demand underscores Elbit Systems' leadership position and the market's appetite for our innovative solutions.

Throughout the recent conflict, we significantly increased production to meet the IDF's urgent needs while maintaining deliveries to international customers. Our focus is on expanding production capacity to drive revenue growth beyond the increase in backlog.

A prime example of our capacity expansion is the recently awarded $340 million contract with the Israeli Ministry of Defense (IMOD) for ammunition supply. This ten-year contract will see the construction of a new manufacturing facility, scheduled for completion within two years. Combining the newly planned facility and the Ramat Beka facility, which is scheduled for completion by the end of this year, our production capabilities will be enhanced and support increased demand from both the Israeli Ministry of Defense and international markets. In support of the surge in demand, we are also adding shifts and recruiting hundreds of new employees.

On July 29th, Elbit Systems was awarded a contract worth approximately $190 million from the Israeli Ministry of Defense for the supply of Iron Sting guided mortar munitions. This two-year contract, which has also international potential, will see the delivery of a precision-guided mortar munition, launched from a 120mm mortar, designed to accurately target and destroy objectives, utilizing both immune GPS and laser guidance technology.

In July 2024 we participated in the Farnborough Air Show in the UK, which was very successful.

During the show we demonstrated a wide range of solutions to our international customers and met with many strategic business partners.

And with that, we will be happy to take your questions.

Operator?

Operator: Thank you. Ladies and gentlemen. At this time we will begin the question-and-answer session. If you have a question, please press star-one. If you wish to cancel your request, please press star-two. If you are using speaker equipment, kindly lift the handset before pressing the numbers. Your questions will be polled in the order they are received. Please stand by we poll for your questions.

The first question is from Pete Skibitski of Alembic Global. Please go ahead.

Pete Skibitski: Yes, hello, good afternoon. A nice quarter.

Butzi Machlis: Thank you, Pete.

Pete Skibitski: First of all, a comment. Just the backlog growth has been very impressive. It looks like backlog has grown about 40% since the end of 2022, which is just incredible, frankly. I would like to make sure I understand the gross margin dynamics a little bit better. It's – obviously, we've seen your geographic mix of revenue shift to Israel, and it looks like that's, you know, over the last three or four quarters that's brought some gross margin compression. And, I'm just wondering, how we should think about the margin dynamics going forward in light of – you know, Butzi, it sounds like you reiterated that 10% operating margin target, which I think is set for 2026. I'm just wondering, in light of the gross margin compression, you know, how you guys attain that 10% target.

Kobi Kagan: Thank you, Pete. We see a five billion dollar increase in our backlog year over year. It is an impressive increase in our backlog, and of course, with this increase, we are mindful of the backlog profitability. As you mention, we see a quarterly lower GP level, but you a higher OP level total result, as M&S expenses are lower with domestic sales, and the total result of the OP level is better. We believe that we are in a good position to reach the 2026 internal target of 10% OP Non-GAAP profitability. As well, you can see a different OP profitability between the segments. We disclosed in the last annual report, the segments revenues and profitability. And this disclosure you may see the segments OP profitability level which is different across the segments, and you may see there a significant decline in our US profitability segment, which we see now a favorable improvement, which supports our believe in continuous OP profitability expansion. Management is closely monitoring our profitability

Pete Skibitski: Okay. That's very helpful, yeah. And I didn't know, it looks like SG&A altogether for this quarter was less than 10% for the first time, I don't know, at least in quite a while. And so that's a trend that we should expect will continue, so that you can get to your OP target, it sounds like.

Kobi Kagan: Thank you. You notice the increased operating expense efficiency that we see this quarter

Pete Skibitski: Okay.

Kobi Kagan: – which more than compensated, for the decline in the GP profitability.

Pete Skibitski: Okay. That makes sense. Just, last one for me. I noticed, you know, cash flow did improve this quarter, and really for the first half of 2024 it's much better versus the first half of '23. Do you think now, do you expect you can be free cash flow positive for 2024, in light of the, you know, the pretty good start to the year?

Kobi Kagan: So, we are very positive hence, I cannot give you a certain answer, as of the profitability level improvement trend, which we can monitor much closer. It depends on continuous payments from the Ministry of Defense in Israel, which paid accurately during the second quarter, but missed payments in the past. We cannot guarantee that it's going to continue to pay in time in the rest of the year. And there are many other different variables and moving parts, especially the fact that we need to be ready with inventories, to support the growth of the company, and supply chain headwinds, that are still pushing us for additional inventories that we need to keep. Those parameters are stressing our cash position. We should expect a positive free cash flow for 2024.

Butzi Machlis: It's Butzi. Hi, Pete. Good to hear from you. We are working very hard –

Pete Skibitski: Hi.

Butzi Machlis: – on the cash flow. We understand the importance of cash flow, specifically because of the current interest rates levels, and that's an area of focus for the entire company.

Pete Skibitski: Okay, that's great. Very helpful, guys. Thank you.

Butzi Machlis: Thank you, Pete. Looking forward to seeing you.

Operator: The next question is from Greg Konrad of Jefferies. Please go ahead.

Greg Konrad: Good afternoon, and great quarter.

[KK & BM together]: Thank you. Good afternoon.

Greg Konrad: Maybe just sticking to margins for a minute, I mean, you called out the higher R&D in the quarter, and the 10% margin target. Any thoughts around how mix evolves over the next couple of years given, you know, some of the development work you talked about, and what that means for, maybe, production mix over the next couple of years, to, kind of, get to that 10% target?

Kobi Kagan: Thank you, Greg, for the question. We can see a shift in the company, in terms of moving from a project company to a company with increased leaning on products. The ratio between projects and products is different now, with increased level of products in our mix. Products, for instance, the sonar buoys in our maritime business, or the night vision googles in our War fighter business in the US, or the ammunition that we are supplying from our Land segment. The fact that we see more products in our mix, is very supportive in terms of our profitability. The certainty in products is much higher than the certainty in projects. You don't see the same phenomenons that you see in projects. We are still a projects company, but the fact that the ratio of products is increasing is supportive in reaching our profitability target.

Greg Konrad: And then, maybe just, transitioning to Land. I mean, obviously, growth was very impressive in the quarter, and has been very impressive the past couple of quarters. I mean, how do you think about the runway there? You know, are there any near-term capacity constraints, just given you called out some of the elements of CapEx. And any way to think about the impact of the capacity coming online, you know, relative to the overall Land business?

Kobi Kagan: As you mentioned, Land segment was very strong this quarter. We saw a 37% growth year-over-year, from the same quarter in 2023. And to support this growth, we need additional investments, additional CapEx investments. We are going to inaugurate the new facility in the south of Israel, Ramat Bekain the end of 2024, which gives us substantial production capacity. With the investment made we focused on better efficiencies , with production technologies such as robots, cobots and additional production stream technologies, which introduce modern and better production than our current facilities in the central of Israel. This is going to give better capacity for the Land business line, but not just for the Land. We have investments that we were doing in Israel and around the world. For instance, we inaugurated a new facility for UAVs in Israel. We are growing our capacity in the factories in the US. Our Charleston facility in the US was inaugurated last year and it's a substantial investment. We have also inaugurated a facility in Germany, and also a new facility in Bristol UK. A substantial investment that was concluded and we see impressive outcomes from is our new corporate ERP system which is being used at all the segments main activities with over 150 million dollars invested so far. This system supported successfully the growth in revenue.

Greg Konrad: And then, just last one for me, and maybe this is somewhat tied to the last question. You mentioned Charleston, but the Americas really seem to turn in the quarter. It had been, you know, somewhat weaker the past couple with a nice uptick in Q2. What's driving the US facing business, just given, you know, it kind of moved more in line with what we're seeing out of peers domestically? Any particular drivers of that normalization to call out?

Butzi Machlis: Hi, good afternoon. We see a different picture, actually. We see a growth of 10% in the US market. The last quarter our revenues in the US were approximately 370 million dollars in comparison to the previous quarter last year which was about 337 million dollars. So it's a 10% growth in the US market, and we have very strong positions in the US market in several domains. We continue to win business and we are confident that our position in the US will continue to grow.

Greg Konrad: Thank you. I'll leave it at that.

Butzi Machlis: Thank you.

Operator: The next question is from Omri Efroni of Oppenheimer. Please go ahead.

Omri Efroni: Hi, guys, and congrats on the great quarter. Great. I was wondering, I have a few questions. My first one is about loitering munitions. I was wondering if Elbit is thinking about entering the loitering munitions segment in a much more aggressive way. We see a lot of demand, like companies from AVAV, like AeroVironment and their Switchblades 300 and 600. And I was wondering if Elbit, with all its experience in this segment, have it any plans in that area? Thanks.

Butzi Machlis: Hi, Omri. Yeah, of course. We believe that loitering munition is an important market for us. We have strong positions in this market. We are one of the first companies to introduce a loitering munition solution to the market, and we have many customers who are acquiring the SkyStriker system, which is a family of loitering munition solutions. And these systems are already operational with several customers. But you are fully right. We are planning to continue to invest in this domain. There are many additional opportunities in this domain. One of them is manned-unmanned teaming. Actually combining several UAVs with one operator, supporting with AI, the way fighting procedures. And that's a segment that we continue to invest in. We are planning to expand the family even more. And based on the current positions we have, in international market, we believe that it's a good opportunity for us.

Omri Efroni: Okay. Great. …

Butzi Machlis: And I also want to mention that we are fully vertical here. We do everything, from the UAVs, from the build, the platform itself, all the communications, all the electro-optics, all the warheads – everything, to the price control. Everything, the command and control, everything is done internally in the company. So, we are fully controlling our destiny, we are fully controlling the costs. It's all in our hands.

Omri Efroni: Mm-hmm. So do you think that –

Butzi Machlis: It's an expansion of other solutions we are providing for these customers.

Omri Efroni: So do you think the time to market is going to be quicker, if you want to go to loitering munitions in the next, two to three quarters? Is it possible to have a new, maybe – much more capacity, and maybe new products in the following two to three quarters?

Butzi Machlis: Yes. I just want to mention that we have delivered already thousands, of SkyStriker systems, to many customers. And we have several production lines for this solution, and we are ready to support any demand that will come from the market.

Omri Efroni: Okay, got it. Thank you. And maybe, more questions from me. Maybe you can give some color about the UAV integration center, or factory, or how it's called, in Rehovot? And – I don't know if in the boundaries that you can speak of, how much capacity it's going to come from there, or maybe how much more efficient it's going to be compared to the integration center you have right now.

Butzi Machlis: We see a growing demand for our UAV solutions, and the beauty here is not just the UAVs themselves. It's the entire system. And there, we provide a variety of payloads, which includes EO payloads, EW payloads, unique other payloads, like sky-high, and many more. We also provide the network, the command and control, everything, once again, is coming from us. We are fully vertical here. And we all see the importance of UAVs here in the current conflict we have in Israel, and we see a growing demand for the family of UAVs that we are providing abroad as well.

We recently introduced a new member to the family, the Hermes 650, which was introduced just recently to the market. And because of the growing demand that we see, and many orders we got, there is a need for a much more modern facility, and we are consolidating several facilities into one. Once again, with a lot of automation and robots, which the new facility, which actually, it's operational already, will be able to deliver many more solutions to the growing demand we see in the market.

Omri Efroni: Got it. Maybe one more question for me, the last one. I was wondering if the situation in the Red Sea has any material effect on the company? And do you think, if so, if you have some problems with the situation, how Elbit is going to mitigate it? Thanks.

Butzi Machlis: As I mentioned in my preview, we see some supply chain issues. However, they are not significant, and we find several ways to overcome them.

Omri Efroni: Okay. Got it. Thank you, and congrats on the quarter again.

[KK & BM together]: Thank you, Omri.

Operator: If there are any additional questions, please press star-one. If you wish to cancel your request, please press star-two. Please stand by while we poll for more questions.

There are no further questions at this time. Before I ask Mr. Machlis to go ahead with his closing statement, I would like to remind participants that a replay of this call will be available two hours after the conference ends. In the US, please call 1-888-782-4291. In Israel, please call 03-9255-900. And internationally, please call 972-3-9255-900. A replay of this call will also be available on the company's website, www.elbitsystems.com. Mr. Machlis, would you like to make your concluding statement?

Butzi Machlis: Thank you. I would like to thank all our employees for their continued hard work and contribution to Elbit Systems' success. To everyone on the call, thank you for joining us today, and for your continued support and interest in our company. Have a good day, and goodbye.

Operator: Thank you. This concludes Elbit System Limited second quarter 2024 results conference call. Thank you for your participation. You may go ahead and disconnect.

[End of conference call.]