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## PRESENTATION

**Operator**

Ladies and gentlemen, thank you for standing by, and welcome to the AeroVironment Fiscal Year 2022 Third Quarter Conference Call. (Operator Instructions) Please be advised that today's conference is being recorded for replay purposes. (Operator Instructions)

I would now like to hand the conference over to Jonah Teeter-Balin. Thank you. Please go ahead, sir.

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**Jonah Teeter-Balin** - *AeroVironment, Inc. - Senior Director of Corporate Development & IR*

Thank you, and good afternoon, ladies and gentlemen. Welcome to AeroVironment's Fiscal Year 2022 Third Quarter Earnings Call. This is Jonah Teeter-Balin, Senior Director of Corporate Development and Investor Relations for AeroVironment.

Before we begin, please note that on this call certain information presented contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements include without limitation any statement that may predict, forecast, indicate or imply future results, performance or achievements and may contain words such as believe, anticipate, expect, estimate, intend, project, plan or words or phrases with similar meaning.

Forward-looking statements are based on current expectations, forecasts and assumptions, which involve risks and uncertainties, including, but not limited to, economic, competitive, governmental and technological factors outside of our control that may cause our business, strategy or actual results to differ materially from the forward-looking statements. For further information on these risks, we encourage you to review the risk factors discussed in AeroVironment's periodic reports on Form 10-K and other filings with the SEC, along with the associated earnings release and safe harbor statement contained therein.

This afternoon, we also filed a slide presentation with our earnings release and posted the presentation on our website at avinc.com in the Events and Presentations section. The content of this conference call contains time-sensitive information that is accurate only as of today, March 3, 2022. The company undertakes no obligation to make any revision to any forward-looking statements contained in our remarks today or to update them to reflect the events or circumstances occurring after this conference call.

Joining me today from AeroVironment are Chairman, President, and Chief Executive Officer, Mr. Wahid Nawabi; and Senior Vice President and Chief Financial Officer, Mr. Kevin McDonnell.

We will now begin with remarks from Wahid Nawabi. Wahid?

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**Wahid Nawabi** - *AeroVironment, Inc. - Chairman of the Board, President & CEO*

Thank you, Jonah. Welcome to our fiscal year 2022 third quarter earnings conference call. I will start by summarizing last quarter's performance and discuss recent achievements. Next, Kevin will provide a more detailed summary of our financial results, after which I will follow up with a discussion of goals for the remainder of fiscal year 2022 before Kevin, Jonah, and I take your questions.

Let me emphasize a few key messages, which are included on Slide #3 of our earnings presentation. First, AeroVironment, like many other businesses in our industry, faced continued headwinds last quarter, as anticipated, notably with regards to supply chain constraints, the federal government's continuing resolution, entire labor market. Second, that said, third quarter results were largely in line with our expectations, and we are maintaining our previously stated guidance for fiscal year 2022. Historically, our fourth fiscal quarter has been our strongest, and we expect that trend to continue this year.

Third, we continue to make strides in reducing costs, managing working capital, and increasing operational efficiency during this challenging period. And fourth, with a solid backlog and multiple expense reduction actions, we are positioned to deliver a strong fiscal year 2022 performance and even better performance in fiscal year 2023.

Before going through these themes in more detail, let me summarize our financial results for the third quarter. We delivered revenue of $90.1 million compared to $78.8 million last year, a 14% increase year-over-year. The revenue growth was primarily due to increased sales in our medium unmanned aircraft systems and unmanned ground vehicle segment. This, along with other organic and acquisition-led increases offset the negative impact from lower Small Unmanned Aircraft Systems product line shipments, which we had already anticipated. We ended the quarter with a backlog of $226 million compared to $252 million in Q2, with wins tempered due to the ongoing continuing resolution.

Despite the lower backlog, we have higher visibility to meet our current fiscal year guidance. Further, we're seeing additional contract opportunities both here and abroad that are helping to lay the foundation for growth in fiscal year 2023. Gross profit for the third quarter was $21.4 million, a decrease of 25% year-over-year. Gross margin percentage decreased to 24% from 36%, reflecting a heavier mix of service revenue. We're not content with this margin performance, and we'll touch on some of our cost-saving initiatives in a moment. Net income for the third quarter was breakeven or $0 per diluted share as compared to net profit of $0.2 million or $0.01 per diluted share for the third quarter of fiscal year 2021.

As I noted earlier, we're continuing to deal with the issues discussed on our last earnings call, but I would like to provide an update on these dynamic conditions. First and foremost are supply chain constraints, which have impacted product shipments and the company's underlying results. The overall situation has not changed materially as certain areas have recovered while others remain challenging. The bottom line is that we're having difficulty getting certain components in the quantities or lead times that we would like. Despite the uncertainty, we're attacking the various supply chain issues in every conceivable way to improve order fulfillment and ensure customer satisfaction.

This is a work in progress, but we took several steps in the quarter. These steps include developing new tools to help us with marketplace component visibility, preordering material when appropriate, paying additional logistics expenses where necessary, and working with our suppliers under long-term agreements to consolidate demand. Not surprisingly, this disruption is negatively impacting our working capital, including higher inventory levels. However, we believe such near-term costs will result in better revenue visibility along with expanded margins as prices and lead times stabilize.

Last quarter, I also spoke about hiring constraints in a tight labor market, which continues to impact our ability to recruit top talent and certain engineering disciplines. While this has improved, there are still gaps in staffing, particularly in the engineering arena. In response, we have increased our use of select outsourced talent firms, which in near term have enabled us to achieve our goals.

At the same time, we remain focused on managing our general and administrative expenses, which includes reducing headcount in noncore functions. During the quarter, we initiated cost savings actions totaling more than $10 million of annual savings in both headcount and facilities footprint. In summary, we're taking an active approach to ensure we can achieve our future growth objectives while operating our business efficiently.

Lastly, the continuing resolution in Washington continues to impact decision-making on projects and contract awards. We are closely monitoring the situation and are hopeful that a budget will pass soon. Nevertheless, our products and programs are prioritized in the 2022 Defense Authorization Act reflecting sustained demand. While the company continues to cope with the -- with headwinds and changing industrial conditions, we are confident in our ability to meet our previously stated guidance. Our recent acquisitions are performing well, and we're taking multiple steps to manage our business efficiently in this challenging environment. Even though challenges persist, we believe AeroVironment is positioned well to capitalize on the long-term growth potential and value creation opportunities presented by our unique portfolio of intelligent multi-domain robotic systems.

Let me briefly comment on the significant world event that is currently unfolding in Europe. We, at AeroVironment, are truly saddened by the Russian invasion of Ukraine. Our hearts go out to all those impacted by the ongoing crisis and especially the citizens of Ukraine who are heroically defending their nation against a superior force. Moreover, this event is a stark reminder that our country and our allies need to be prepared to defend ourselves against such unpredictable and unreasonable authoritarian regimes. Our family of loitering missiles and other products are ideal in helping defend against such current and future aggressions. And we stand ready to assist our country and our allies around the world in any way necessary.

Now before turning the call over to Kevin, I would like to provide some updates on current developments within each of our product lines. I'll start with our Small Unmanned Aircraft Systems, or SUAS product line, our largest franchise. As discussed above, this segment's revenue has declined this year, driven primarily by lower domestic demand. We believe this is due to both the continuing resolution, environment, and the Army's focus on the next generation of Small UAS, which we expect to be completed in the next few years. On the other hand, our Puma and Raven systems are benefiting from enduring demand overseas. As an example, we recently booked 2 international orders from new European and Asian allies totaling nearly $20 million. To address the weaker domestic demand and position this franchise for continued success, we're investing in developing new capabilities for our platforms, especially those that allow us to leverage our installed base of tens of thousands of units across the globe while competing against near-peer adversaries.

On this note, we recently announced the launch of our i45 night gimbal, which has seen strong interest from customers. We are also excited about the enhanced sensor-to-shooter capabilities, which are achieved by integrating our Small UAS products with our Tactical Missile Systems products. We continue to allocate a healthy portion of our R&D investment to realize our future SUS solution road map and look forward to sharing additional developments over the coming quarters.

That brings me to our Tactical Missile symptoms or TMS product line, where we continue to see strong demand for our solutions, both domestically and internationally. We believe there are growing opportunities for our TMS products to replace traditional munitions and ground, air, and sea applications, especially with our new and larger Switchblade 600 variant.

Deliveries of the first international order for Switchblade 300 are expected to take place this month, reflecting increased interest from international customers for this innovative technology. Additionally, we are actively engaged with multiple international customers who have both the interest and the need for Switchblade's unique capabilities. We recently met with the U.S. export authorities who support enabling our allies with our Switchblade family of loitering missiles. In addition, we recently introduced the Switchblade 300 Sensor To Shooter solution, which enables operators to [absolutely] and seamlessly transfer target coordinates from our Small UAS to Switchblade loitering missile systems.

By implementing this solution, we're able to provide end-to-end interoperability that significantly reduces the cognitive load on soldiers handling the processing, evaluation, and dissemination, or PED, of our UAS data. The Switchblade 300 sensor to shooter solution includes everything needed to quickly update mission planning applications with the sensor shooter software. Target coordinates are instantly transferred from our Small UAS to Switchblade 300, creating an automated mission plan and launch sequence with no chance of data entry error. Upon launch, the Switchblade 300 can autonomously navigate to the designated coordinate core position, allowing operators to match full-motion video from both assets to ensure positive identification of the target.

Finally, our Small UAS provides overwatch that can verify mission success. The Switchblade 300 sensor-to-shooter solution builds on AeroVironment's commitment to deliver innovative, streamlined, interoperable solutions that elevate the warfighter's situational awareness, reduce engagement timelines and cognitive load, and increase mission success and operational safety, Further, this solution demonstrates how interoperability between our different product lines can lead to better customer outcomes and build upon our prior integration of the Switchblade with the JUMP 20 Medium UAS, thus expanding the breadth of our capabilities available to our customers.

I will now move to our medium unmet aircraft systems or MUAS product line. As previously announced, we submitted a JUMP 20 proposal for the U.S. Army's Future Tactical UAS or FTUAS Increment 1 and more recently Increment 2. This contract serves as the proving ground for our technology by placing a half a dozen JUMP 20 systems in the hands of the U.S. Army combat brigades for testing. We look forward to hearing that on this award any day now. Assuming all goes well, we believe our win on Increment 1 will put us in a favorable position to win Increment 2 later this year, which could be worked up to $50 million in new contract value. As a reminder, the FTUAS program in aggregate is expected to be valued at over $1 billion over a 10-year period after full testing is complete. The U.S. Army's proposed fiscal year 2022 budget called for over $140 million of funding for advancing this potential program of record. In the meantime, we're submitting proposals to U.S. allies across the globe and are upgrading our JUMP 20 with a new autopilot to improve its ability to operate in environments with limited GPS availability.

We currently have several RFPs being evaluated by European and Middle Eastern countries and have conducted demonstrations for numerous U.S. allies overseas. So far, we have built a healthy sales pipeline since this acquisition and expect first awards from these international efforts in fiscal year 2023. It's exciting to see the level of interest our JUMP 20 systems have generated with our international customers and installed base, validating a key synergy of the acquisition.

Moving to our Unmanned Ground Vehicles or UGV product line, the business is performing well. We have seen strong customer interest, especially in Europe and the Southern Pacific, and we're continuing to position the business to compete for domestic programs over the coming years. Further, our team has been working to expand the market opportunities in chemical, biological, radiological, nuclear, or CBRN and tactical use cases. We are pleased with the expanding interest in our UGV products and believe in the solid value potential for our shareholders.

Within our HAPS product line, we continue to move ahead in designing the next-generation aircraft under the terms of our 5-year master design and development agreement with SoftBank. As we said last quarter, we are progressing with Phase 2 of our partnership during which we will build a third aircraft to perform further flight testing, demonstrate longer duration flights and progress through FAA certification. At the same time, we continue to assess various U.S. DoD opportunities that can leverage Sunglider's unique capabilities.

And finally, our MacCready Works Advanced Solutions group continues to develop new applications in autonomy and artificial intelligence. In the quarter, we secured multiple new programs to advance the autonomy and swarming capabilities of AV's existing products. One of these programs leverages technology from our Progeny ISG acquisition to automatically detect and classify targets before transmitting target coordinates to a swarm of Switchblades.

As a reminder, our ISG team is a leader in the development of AI-enabled computer vision, machine learning, and perceptive autonomy technologies. We're also a provider of related autonomy and computer vision services to U.S. government customers. We're excited that our ISG acquisition is bearing fruit and look forward to creating further value at our core products through these advanced technologies.

In summary, we're taking the steps within our control to manage the global headwinds impacting our industry and company. We've had to make some difficult decisions in the quarter but believe these decisions are better positioning us for even stronger growth in the years ahead. While there is more work to be done, our portfolio of intelligent multi-domain robotic systems provide a unique competitive advantage for our company, which should generate long-term shareholder value.

With that, I would like to now turn the call over to Kevin McDonnell for a review of third quarter financials. Kevin?

**Kevin Patrick McDonnell** - *AeroVironment, Inc. - Senior VP & CFO*

Thank you, Wahid. Today, I'll be reviewing the highlights of our third quarter performance, during which I will occasionally refer to both our press release and earnings presentation available on our website. Revenue for the third quarter of fiscal 2022 was $90.1 million, a 14% increase from the prior year's comparable period.

Slide 5 of the earnings presentation provides a breakdown of revenue by segment for the quarter. Our largest segment during the quarter was Small UAS with $24.4 million of revenue, down from last year's $50.5 million in revenue. Reiterating what Wahid said, the client's Small UAS -- the Small UAS business was primarily driven by reduced U.S. DoD spending, while international demand continues to be consistent with historical patterns. We expect the demand for Small UAS from the DoD to continue below historical levels in the near term.

Our acquired Median UAS segment had another solid quarter with revenue of $21.2 million, a small increase over the second quarter. Most of our Medium UAS revenue is classified as service revenue as we anticipate growth in this segment to be in the form of product sales. As Wahid indicated, we are well positioned for the Army's FTUAS program and our international pipeline for the JUMP 20 continues to build. Our Tactical Missile Systems business or TMS segment contributed $18.6 million of revenue during the quarter.

TMS continued to be impacted by ongoing supply chain issues in Q3, and we expect these issues to continue at least for the remainder of the fiscal year. But to repeat what Wahid said, we are seeing an increased opportunity for international sales of our TMS products. Revenue from the Other segment, which includes HAPS and our acquired Telerob and Progeny ISG businesses, increased year-over-year to $26 million versus $8.6 million in the fiscal 2021 third quarter. The increase is primarily a result of revenue from the acquired Progeny ISG and UGV businesses.

Turning to gross margins. Slide 5 of the earnings presentation shows the mix of product versus service margins -- service revenue, sorry. Our mix of product and service revenues is a major factor in our overall gross margins. For Q3, we saw a decline in the mix to 47% product, down from 58% product in Q2 and 74% in the prior year third quarter. For the full year, we are tracking towards the 55% product mix, down from our original expectation of 60% and below our historical 70% level. Despite this negative mix trend, our guidance remains unchanged as Wahid indicated in his remarks.

Slide 6 of the earnings presentation shows the trend of adjusted product and service gross margins, while Slide 7 -- 12 reconciles the GAAP gross margin to adjusted gross margins. which excludes intangible amortization expense and other noncash purchase accounting items.

I'll now speak to our adjusted gross margins. Overall adjusted gross margins for the quarter were 29%, down sequentially from 39% in the second quarter of FY '22. The 2 primary factors in the lower adjusted gross margins are lower product mix as product revenue traditionally has higher gross margins than our service revenue and lower product gross margins as a result of lower Small UAS sales mix.

Adjusted product margins for the quarter were 37% versus 48% in the second quarter, reflecting the product mix shift I just mentioned. However, for the remainder of the year, we expect to see adjusted product gross margins to be in the mid to low 40s. In terms of adjusted service gross margins, we also saw a decrease to 23% in the third quarter versus 27% in the second quarter of the year. The service margin declined sequentially and year-over-year reflects the impact from our acquired Medium UAS COCO business, which has lower gross -- lower margins than our traditional service businesses. We are expecting adjusted service margins to end up in the mid-20s for the full fiscal 2022.

Next, turning to operating expenses. SG&A expense for the third quarter was $22.5 million and includes intangible amortization and acquisition-related expenses of $4.6 million compared to just $0.7 million last year. Excluding intangible amortization and acquisition-related expenses, SG&A for the third quarter was $17.9 million or 20% of revenue compared to $12.2 million or 15% of revenue in the prior year period. The increase was primarily a result of added expense from the 3 acquisitions we completed over the past year. Year-to-date, SG&A excluding intangible amortization and acquisition-related expense was 18% of revenue. We expect SG&A as a percentage of revenue to be 17% for the full year, again, excluding the intangible amortization and acquisition-related expenses.

R&D for the third quarter was 14% of revenue and 13% year-to-date. We expect R&D as a percentage of revenue to be in line with our guidance of 11% to 12% for the full year. At this point, I'd like to take note that we took several cost reduction measures during the quarter to reflect current business conditions. This includes headcount reductions and facility consolidation. We incurred some onetime costs and other nonrecurring expenses in Q3 of $1.5 million impact -- $1.5 million, impacting both the cost of goods sold and operating expenses. These costs will continue into Q4 but have been included in our guidance.

Looking at the bottom line, our GAAP net income for the third quarter of fiscal 2022 rounds to $0.00 per diluted share compared to net income of $0.2 million or $0.01 per diluted share for the third quarter of fiscal 2021. While the year-over-year difference wasn't significant, it reflects a decrease of $13.5 million in our operating income, driven in large part by the increase in intangible amortization related to our acquisitions. During the quarter, we also incurred $1.5 million of additional operating expenses related to cost-saving initiatives, as I just mentioned. This was largely offset below the operating line by $15.4 million tax benefit driven by a combination of our year-to-date and projected full year pretax losses and R&D tax credits.

In terms of adjusted EPS, Slide 10 of our earnings presentation shows the reconciliation of GAAP and adjusted or non-GAAP diluted EPS. The company posted adjusted earnings per share of $0.32 for the third quarter of fiscal 2022 versus $0.14 per diluted share for the third quarter of fiscal '21. The difference between GAAP and non-GAAP earnings reflects acquisition-related expenses and intangible amortization. We have not added back onetime costs related to seeing the cost saving actions expense during the quarter.

Turning to the balance sheet. Total cash and investments at the end of the third quarter was $100.7 million, which is slightly up from the second quarter of this fiscal year. We continue to have a strong balance sheet with over $100 million of cash and investments and $100 million working capital facility.

Next, I'd like to highlight some of our backlog metrics. Slide 7 of the earnings presentation provides a summary of our current fiscal 2022 visibility. As of today, total visibility towards the midpoint of our $440 million to $460 million revenue guidance range is 95%. Our funded backlog at the end of the third fiscal quarter of 2022 was $226.3 million.

Now I'd like to turn things back to Wahid.

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**Wahid Nawabi** - *AeroVironment, Inc. - Chairman of the Board, President & CEO*

Thanks, Kevin. Before turning the call over for questions, let me just reiterate a few key points from earlier today. With 95% visibility to the midpoint of our previously stated guidance, we are reaffirming our guidance for fiscal year 2022 as follows: Full year revenue between $440 million and $460 million, net loss from continuing operations between 12 and $8 million, adjusted EBITDA between 59 and $65 million, diluted loss per share between $0.47 and $0.33, and non-GAAP diluted earnings per share is forecasted to be between $1.23 and $1.37. While facing the ongoing challenges caused by our supply chain constraints, the continuing resolution in Washington and a tight labor market, we have and will continue to aggressively reduce costs, manage working capital and improve AeroVironment's long-term growth profile.

While I'm proud of our team and the progress shown in tackling the various macro challenges, I'm also excited by the many opportunities which lie ahead. Given the potential FTUAS program win, the solid performance of our recently acquired businesses, and expanding demand from overseas customers, I believe AeroVironment is on the right path for growth, which will yield improved financial and operational results. That means better margins and higher cash flow as well as an even larger international presence.

We believe in the future of AeroVironment, and we're investing in leading-edge technologies that will accelerate the top line and provide for years of solid performance. So as we approach the end of fiscal year 2022, I speak for the entire team here at AeroVironment and are resolved to serve our customers to the best of our abilities, capitalize on new market opportunities and ensure the returns that our investors have come to expect.

And with that, Kevin, Jonah, and I will now take your questions.

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## QUESTIONS AND ANSWERS

**Operator**

(Operator Instructions) So our first question comes from the line of Ken Herbert from RBC Capital Markets.

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**Kenneth George Herbert** - *RBC Capital Markets, Research Division - Analyst*

Wahid, just a first question. Can you provide any more color on the expected timing of the FTUAS contract announcement and what -- assuming you're successful with the -- assuming you're successful with the -- with Increment 1, what that could contribute to this year, if anything, but I guess, more importantly, to fiscal '23?

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**Wahid Nawabi** - *AeroVironment, Inc. - Chairman of the Board, President & CEO*

Sure, Ken. So the U.S. Army has basically told us that they are planning on awarding that contract and make an announcement sometime in our fourth fiscal quarter right now. So we're hopeful that by the end of this quarter, we will have that outcome basically announced and communicated. That's for Increment 1. Fairly soon after that, the Army also plans to award Increment 2. Whoever wins increment 1, the probability of being successful, winning increment obviously increases, which is good for us. And then that also increases the probability of success for the longer-term program of record acquisition if it were to become a program of record.

So in terms of the actual award, we expect that to happen sometime in this quarter. And in terms of contributions, we may recognize a small amount of revenue for that in fiscal year '22 this fourth quarter, but majority of that most likely will be in the next quarter. And that's primarily predicated by how fast our customer can move and being able to assume deliveries or accept deliveries and deploy these systems out there. It is a very large strategic opportunity that we're very focused on. And we're so far engaged with the U.S. Army very actively on a regular basis, and we hope to provide you with more updates in the near future.

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**Kenneth George Herbert** - *RBC Capital Markets, Research Division - Analyst*

And as a follow-up, with the situation currently in Eastern Europe, there's some speculation about reinstatement of maybe OCO accounts. How, if anything, have you seen that situation in Europe impacting your business today? Or how should we think about that to potentially impact the business in fiscal '23?

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**Wahid Nawabi** - *AeroVironment, Inc. - Chairman of the Board, President & CEO*

Sure. So Ken, the recent events in Ukraine and Europe, obviously, is very heartbreaking and our hearts and minds and prayers go to the Ukrainian citizens and others. At the same time, the solutions that we have developed such as Switchblade 300 and 600, JUMP 20 in our Small UAS is perfectly designed and suited for those types of conflicts. We truly believe that our Switchblade family of loitering missiles could be a gamechanger, literally a gamechanger for the Ukrainian military. The ability to shoot these things very easily and identify target and designate them automatically and take them out and disable them or destroy them with no collateral damage is absolutely phenomenally well situated for that type of a conflict.

In terms of a OCO budget and account, historically, we have benefited from that during the conflicts in the Middle East in Afghanistan. We use -- historically received significant amount of funding for both our Small UAS and TMS as a result of that. It is not clear to me now whether that is going to happen again in the case of Ukraine. If it does, I believe that would be a positive contributor to our business. And even besides that, I do believe that all the activity that's going on right now is sort of becoming a wake-up call for a lot of our allies in Europe as well as the U.S. military that systems like Switchblade and JUMP 20 could be extremely effective and vital to these types of conflicts in the future.

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**Operator**

Our next question comes from the line of Austin Moeller from Canaccord.

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**Austin Nathan Moeller** - *Canaccord Genuity Corp., Research Division - Associate*

Just my first question here. The last time that we spoke, I was wondering if there was any timing around when you think the supply chain component procurement issues might be resolved. Do you guys have any better visibility into that now relative to the last quarter?

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**Wahid Nawabi** - *AeroVironment, Inc. - Chairman of the Board, President & CEO*

The short answer is that we have some visibility to the best of our abilities, and we're taking a lot of actions related to the supply chain constraints. And I mentioned a few of them on my remarks, but it is an ongoing effort and challenge on a daily basis. In some areas, we have seen improvements. And in some areas, we have seen a lack of improvements. I tend to believe that those challenges will continue into next fiscal year of ours. And I don't see how all those issues are going to go away within the next 3 to 6 months. I tend to believe that while some areas have shown some improvement, overall, the situation still exists, and we've taken an enormous amount of effort to address many of those.

And I think we've done an incredible job of addressing the issues that are out there working with our suppliers and how that could be mitigated. But we do this on an ongoing basis, we evaluate the impact due to this and also there may be some issues related to the Ukraine situation that could cause this in some ways to improve by putting a priority for defense, acquisitions, and supply chain, but also may negatively impact it because of the global supply chain constraints in general. So it's an ongoing challenge that I see it continuing into next fiscal year for us.

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**Austin Nathan Moeller** - *Canaccord Genuity Corp., Research Division - Associate*

And just a follow-up there. So say that some countries in Europe wanted to procure some Switchblades, could you potentially prioritize using components for TMS relative to some other product lines just to get them shipped out faster?

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**Wahid Nawabi** - *AeroVironment, Inc. - Chairman of the Board, President & CEO*

Yes, we could. There's multiple ways that we can address that potential new increased demand. First and foremost, we have some inventory within our U.S. defense -- with our defense customers themselves. So U.S. military can provide some of those directly to those customers and wait for us to backfill their needs and their supply from AeroVironment in the next few months, number one.

Number two, we already are working all of our supply chain avenues and relationships and suppliers to see if we can get more of those components that are in high demand that could be useful for those needs. And third, another key item in here is the U.S. Department of Defense could always activate a higher priority for military or active war type of situations that could put us and many other defense contractors on the higher priority with these suppliers.

Fundamentally, our volumes in some of these areas are not that big relative to the global demands and volumes for these microprocessors and chips. However, if the U.S. duty enacted such a priority on it, it will give us priority within the suppliers and the whole global supply chain in general. So there are at least 3 ways that I can think of that we're actively working, all 3. If there was to be a stronger demand then we could address that.

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**Operator**

Our next question comes from the line of Brian Ruttenbur from Imperial Capital.

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**Brian William Ruttenbur** - *Imperial Capital, LLC, Research Division - Research Analyst*

First question is just helping us understand your revenue visibility going into the quarter. You cited supply chain issues, continuing resolution, delays like that. What is your visibility? I know you have great backlogs and things like that. Do you have the supplies in place right now? Do you have the orders in hand to ship in this fourth quarter?

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**Wahid Nawabi** - *AeroVironment, Inc. - Chairman of the Board, President & CEO*

And the short answer is, overall, we, as I said in the comments, that we feel confident about our ability to achieve the reaffirmed guidance that we provided based on the variables and the facts and the conditions that we see today. There are several reasons as to why. Number one, we have a visibility, which we refer to as our visibility for achieving the midpoint of our guidance, we're about 95% visibility to the midpoint of our current guidance on revenue. Compared to our historical levels, that's pretty much in line with it and maybe to some extent, slightly better.

Number two, we have a strong backlog that contributes a backlog to that visibility. And three is we have already started this process internally with suppliers. Are there still some risks? Absolutely. There always has been and there will continue to be as the quarter goes on. But overall, based on all the indicators that we have and based on all the factors that we see, we believe that we should be able to achieve our guidance as we confirm today for the full fiscal year and fourth quarter.

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**Brian William Ruttenbur** - *Imperial Capital, LLC, Research Division - Research Analyst*

Just as a follow-up on a slightly different subject, if I can, in terms of you sell to 50 countries roughly. Have you sold to Ukraine in the past or sold to Turkey that sells to Ukraine? I didn't know if there's any direct exposure with your systems right now.

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**Wahid Nawabi** - *AeroVironment, Inc. - Chairman of the Board, President & CEO*

Yes. So Brian, I'm not able to comment on any specific country for sensitivity reasons. What I can tell you is that absolutely positively majority, if not most of the European countries, Western European, Eastern European, the Baltics, the Scandinavian, Middle Eastern, Northern African countries are our existing customers, and that list continues to grow. So that's number one.

Number two, given the fact that we already do business with 50-plus countries around the world and have a very large installed base, helps us execute our strategy and provide more of our products and portfolio to various countries around the world. So we generally feel very good about that because our installed base and customer base is very robust, very broad, probably unmatched in the industry and many aspects of it internationally. And it's actually one of the strong [seats] of AeroVironment. We're very fortunate to have a diversified product portfolio, diversified customer base geographically as well as different types of customers and different services of the military, Army, Marines, Navy, Air Force, et cetera.

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**Operator**

(Operator Instructions) Our next question comes from the line of Christopher Rieger from Berenburg.

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**Christopher Thomas Rieger** - *Joh. Berenberg, Gossler & Co. KG, Research Division - Analyst*

Just sort of piggybacking on Austin's first question. I'd like to double-click on a comment you made regarding the supply chain difficulties you are experiencing. You mentioned that some areas are better and some are worse. Could you sort of speak to the specifics as best you can as to how the situation has changed from last quarter?

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**Wahid Nawabi** - *AeroVironment, Inc. - Chairman of the Board, President & CEO*

Sure. Chris, so generally speaking, because our systems are extremely innovative in terms of cutting-edge technology. We use some of the most highest-performing GPUs as graphic processor -- processing units and CPUs and other various types of semiconductor that addresses and in terms of performance, they're on the most extreme of what's referred to as SWAP, Size, Weight, and Power performance.

So these are the types of things that are highly, highly in demand in many other industries besides ours. And so it is the cutting edge and the leading edge. And based on that, the supply in general for those systems are very, very high globally besides just in the United States. Historically, we've done a really good job of working with our suppliers to not only give them long-term forecast, but we've also provided them with requirements that they have to actually carry inventory based on our forecast. And that's really helped us over the last 2.5, 3 years considerably.

What's changed from last quarter to this quarter? In some areas, we see some improvements. And those improvements are such that a supplier might have quoted us an x amount of weeks of lead time. And as time has gone by, they've been able to improve that lead time. And in some cases, that has actually eroded. So net-net, I would say that there's been pockets of positives, but there's also some pockets of negatives or setbacks in that regard.

Overall, we've been able to manage that, and it's a daily effort, daily activity to address the issues that come up and to go away. It's a dynamic environment. Overall, given our forecast today and how we've executed so far, we believe we're well positioned to achieve our full year results that we -- what we've discussed earlier.

So again, I'm very proud of our teams being able to execute on the third quarter and deliver the results that we expected. And we believe that we're positioned well for not only this fiscal year, but even for fiscal year '23 and beyond.

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**Christopher Thomas Rieger** - *Joh. Berenberg, Gossler & Co. KG, Research Division - Analyst*

And just switching gears here. On the labor front, has your utilization of outsourced engineering services had a material impact on your margins? And if so, could you quantify the impact?

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**Wahid Nawabi** - *AeroVironment, Inc. - Chairman of the Board, President & CEO*

Brian, I'm sorry, Chris, the outsourced labor effort has had some effect, not very material in general but has had some effect. We don't typically break them down by specific drivers or contributors. Overall, there are certain areas that we could use outside labors -- labors or engineering resources for some of the work. But some of it is very, very high-tech work, which requires a lot of training and knowledge transfer, which we are very hesitant to do and it's not practically to do that easily. So overall, we've made progress on both fronts, bringing some outside outsourced labor in, but also actually increasing our headcount and hiring. And so we've made some progress since last quarter, but it still remains a challenging environment. Overall, the demand for the type of resources that we're looking for primarily in autonomy, AI, guidance navigation and control air mechanical design, robotics engineering. These are the areas that we look for and we have needs. And the demand for those still remains to be very, very high and competitive overall.

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**Operator**

So our next question comes from the line of Louie DiPalma from William Blair.

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**Michael Louie DiPalma** - *William Blair & Company L.L.C., Research Division - Analyst*

Wahid, can you discuss opportunities and the developmental progress with the Switchblade 600. You previously have discussed how there is some strategic overlap with the 600 and Javelin missiles amongst other types of missiles. And specifically, the Javelin missiles have been in the news a lot as it relates to Ukraine. So I was just wondering if you could discuss at a high level the different types of end markets and applications you see for the 600?

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**Wahid Nawabi** - *AeroVironment, Inc. - Chairman of the Board, President & CEO*

Sure. So Louie, so far, it's a strong belief of ours that a loitering missile such as Switchblade 300 or 600 and particularly Switchblade 600 is an ideal capability that today the Ukrainian military and the other allies and neighbors in Eastern Europe, Western Europe could absolutely benefit from and use. As you know, they carry similar warheads in them, and they have similar amounts of warhead capacity and payload capacity. But in terms of its other performance characteristics, Switchblade 600 is extremely superior.

Being able to travel 50-plus kilometers, not have to have the target on your visual site and then designate it and then take it out. These are all the competitive, compelling unique value proposition, and differentiators of Switchblade 600, which I believe makes it a superior weapon and missile system for the type of conflict that we see today and Ukraine and possibly in other areas all over the world eventually. So we feel very good. This is something that we've been talking about, and we believe them for years and years. That's why we invested in it. I think our domestic customers see that as well, and we're hopeful that with our latest engagements with the U.S. State Department and the Pentagon, we will get more of their support to be able to export these store allies. And that's really the key for us to be able to do that.

Again, one of the other things I want to mention, Louie, is that we have received authorization, as you know, to export that to one country to Switchblade 300. We had some very favorable and positive engagements with the U.S. State Department and officials from the U.S. Department of Defense in the last quarter, where they are quite supportive of helping us equip our allies with more of our Switchblade 300 and 600 in the next few months to come. Obviously, this is going to take some time because the process doesn't go -- doesn't happen overnight. But we believe that those engagements is very positive in terms of encouraging us and giving us optimism that the U.S. military and state department is very much supportive of enabling our allies with this capability.

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**Operator**

(Operator Instructions) I'm showing no further questions in the queue. Ladies and gentlemen, this concludes today's conference call. Thank you again for participating, and we look forward to speaking with you again next quarter. You may now disconnect.

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