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# EDITED TRANSCRIPT

AVAV.OQ - Q2 2026 AeroVironment Inc Earnings Call

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## PRESENTATION

### Operator

Good day and thank you for standing by. Welcome to the AeroVironment second-quarter fiscal year 2026 earnings conference call. (Operator Instructions) Please be advised that today's conference is being recorded.

I would now like to hand the conference over to the Head of Investor Relations, Denise Pacioni. Please proceed.

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### Denise Pacioni - AeroVironment Inc - Investor Relations

Thank you, and good afternoon, ladies and gentlemen. Welcome to AeroVironment's second-quarter fiscal year 2026 earnings call. My name is Denise Pacioni, Head of Investor Relations for AeroVironment.

Before we begin, please note that certain information presented on this call contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements involve many risks and uncertainties that could cause actual results to differ materially from our expectations.

Further information on these risks and uncertainties is contained in the company's 10-K and other filings with the SEC, in particular, in the risk factors and forward-looking statement portions of such filings. Copies are available from the SEC on the AeroVironment website, [www.avinc.com](http://www.avinc.com) or from our Investor Relations team.

This afternoon, we also filed a slide presentation with our earnings release and posted the presentation to the Investors section of our website under Events & Presentations.

The content of this conference call contains time-sensitive information that is accurate only as of today, December 9, 2025. The company undertakes no obligation to update any forward-looking statements whether as a result of new information, future events or otherwise.

Joining me today from AeroVironment are Chairman, President and Chief Executive Officer, Mr. Wahid Nawabi; and Executive 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, Chief Executive Officer*

Thank you, Denise. Welcome, everyone, to our second-quarter fiscal year 2026 earnings conference call. I'll begin by summarizing our quarterly performance followed by Kevin, who will review our financial results in greater detail and then discuss guidance for fiscal year 2026. After this, Kevin, Denise, and I will take your questions.

I'm pleased to report excellent quarter financial results while setting new records in multiple areas of our business. Despite the challenges posed by the elongated US government shutdown, we delivered excellent financial results and achieved several strategic milestones that we believe position AV for strong, sustained growth well into the future.

During the quarter, we introduced several innovative products and secured multiple large long-term contracts, a testament to our recipe for innovation and proof that our strategy is winning. The total ceiling value of new contract awards during Q2 reached \$3.5 billion, a historic record achievement by AV.

This also resulted in record second quarter bookings of nearly \$1.4 billion. These achievements underscore that our strategic investments are delivering results and progressing our business to new heights.

We also made significant progress on multiple programs of record that we believe will solidify our leadership in all of the domains in which we participate: air, land, sea, space, and cyber. With strong top-line growth expected on the horizon, we are executing on our expansion plans to further scale our manufacturing capacity and meet accelerating demand across several of our products and programs.

Our proven execution capabilities, combined with the robust pipeline of orders and operational readiness, reinforce our confidence in achieving our industry-leading long-term growth objectives. At the same time, overall, the integration of BlueHalo is exceeding expectations, strengthening our capabilities and positioning AV as the premier next-generation defense tech company.

Let me summarize our key messages for the second quarter of fiscal year 2026, which are (technical difficulty) towards with a total contract value of \$3.5 billion bolstered bookings to reach an all-time high of nearly \$1.4 billion, driven by key program wins that support AV's long-term growth.

Second, we also achieved another record second quarter revenue of nearly \$473 million.

Third, we launched several new innovative products aligned to our customers' highest priorities and continue to execute on expanding our manufacturing capacity to meet accelerated demand.

And fourth, we're raising the lower end of our fiscal year 2026 revenue guidance and now expect revenues between \$1.95 billion and \$2 billion.

Beyond these strong results, the defense industry is at an inflection point, and AV is not just prepared to lead. We are ahead of the curve setting the pace for everyone else to follow.

Let's not forget, the US Department of War is firmly committed to shifting their procurement practices towards agile, commercially available products and capabilities, favoring companies that invest their own capital, develop disruptive solutions at speed while transitioning them to full rate production and scaling capacity quickly. This validates the business model AV has embraced not just in the past few years, but over multiple decades.

AV's business model and strategy have always been to invest in innovative and disruptive solutions ahead of customer requirements, scale their production rapidly, and deliver decisive advantages that enable our customers to acquire capabilities quickly.

Looking ahead, cost-efficient autonomous drones and counter drone systems enabled by AI and machine learning will define the battlefield. Known for uncrude aircraft systems and leading AI integration, we believe AV is uniquely positioned to capitalize on this transformation.

AV\_Halo, our open architecture software platform, is designed to unify command and control intelligence analysis, synthetic training and autonomous targeting across all domains, creating advanced communication among critical assets during conflict. By integrating AV\_Halo into our portfolio and other platforms, we're delivering a powerful hardware-agnostic ecosystem that enhances the speed, autonomy, and interoperability of AV's platforms for our customers.

Moreover, we expect that AV\_Halo's ability to enable competing products to operate on a common command and control software system will play in an increasingly crucial role in US defense procurement decisions. Our investment and development in AV\_Halo is just one example of how AV is ahead of this transformation and is well positioned within the industry.

Our level of internal R&D investment and proactive CapEx strategy enable us to accelerate development and scale production ahead of demand. Using internal R&D to advance new products allows our technology to outpace our peers and leads to a faster time to market. We believe this core competency is a key differentiator that allows us to stay ahead of our customers' needs.

Unlike traditional contractors that wait for contract vehicles before building prototypes, we innovate first, bring solutions to market faster. These forward-looking investments are not only fueling the launch of new products, but also translating into significant contract wins, reinforcing our ability to capture emerging opportunities.

For example, in our Autonomous Systems segment, our P550 was recently down selected by the US Army's Long-Range Reconnaissance program or LRR estimated to be worth approximately \$1 billion. Internal investments made on this group to uncrewed solution allowed us to quickly meet the needs and requirements included in the LRR program, and we're confident that our P550 is the best solution for the US Army.

We've also prudently invested in upgrades to our Group 3 uncrewed aircraft system, JUMP 20 and JUMP20-X, which was recently selected as one of four options on the US Navy's basic ordering agreement. This significant achievement allows AV to compete for specific US Navy intelligence, surveillance and reconnaissance, or ISR, task orders over the next five years in a large and rapidly growing UAS maritime defense market.

In addition to these domestic achievements, we're also expanding and experiencing an increase in international demand. Within our Autonomous Systems segment, we were recently awarded an \$874 million sole source IDIQ contract from the US Army for international sales of our small UAS products to include Raven, Puma AE, and Puma LE.

This IDIQ contract vehicle also allows for the sale of our JUMP 20 medium UAS and tightened series of counter UAS solutions. Our strategy is driving tangible results, which is evident in the successful product launches this quarter. We recently unveiled several new offerings, including our next generation of Switchblade loading munitions with our Switchblade 600 Block 2, Switchblade 400, and Switchblade 300 Block 20.

These products were mostly internally funded and developed quickly, helping to expand the Switchblade product line and create long-endurance, multi-domain, anti-armor solutions, ensuring warfighters maintain tactical overmatch in contested environments.

We also debuted our next-generation vapor compact long-endurance helicopter or VAPOR CLE. This Group 2 VTOL UAV is fully autonomous and can deliver up to two hours of flight, which has doubled the endurance of typical Group 2 quadrotor UAV platforms.

Our newly integrated NVIDIA Orin onboard computer makes the VAPOR CLE fully autonomous and enables automatic target recognition through AV\_Halo VISION computer vision software and AV\_Halo Wizard artificial intelligence machine learning AI/ML processing suite.

On our last earnings call, we discussed the significance of our software solution, AV\_Halo. Since then, we have announced that AV was awarded the US Army's contract for Human Machine Integrated Formation, or HMIF program. This award accelerates fielding of multi-domain robotic formations using AV's unified interface of command and control, tactical awareness, and autonomy solutions at the tactical edge.

As part of this win, AV is going to be the lead software and system integrator for robotic systems on the edge of the battlefield. This award also validates the strength of our approach to software solutions, common controllers, and user interfaces and underscores the Army's confidence and AV's ability to deliver mission-critical solutions.

We also just released two new products from the AV\_Halo suite, including AV\_Halo CORTEX, a next-generation intelligence fusion and analysis environment; and AV\_Halo MENTOR, a warfighter readiness suite that leans on virtual and augmented reality weapons training and mission rehearsal.

AV\_Halo will continue to roll out more products and offerings that position AV as the core and leading developer in this space.

Furthermore, we recently announced a collaboration with OpenJAUS or OpenJAUS. OpenJAUS is an open architecture for software framework that allows robots, drones, missiles, and ground vehicles to speak the same language. This integration extends AV\_Halo compatibility to seamlessly incorporate robotics, allowing original equipment manufacturers to integrate their platforms faster and more easily.

This collaboration strengthens AV's role as a driver and leader of the industry's push towards interoperability. In addition, AV won several key awards in our Space, Cyber & Directed Energy segment with critical new contracts and laser communications, space-related satellite communications, and directed energy.

For example, AV received a \$240 million contract for our long-haul laser communication terminals, one of the largest to ever be awarded in this category. This disruptive innovation is moving from lab to orbit, a critical step for AV and the industry.

Long-haul laser communications use precision optical links to move enormous amounts of data between satellites faster, more securely, and without the vulnerabilities of traditional radio frequency or RF signals. This capability is critical because it creates a resilient high-bandwidth backbone for future space networks, ensuring warfighters and decision-makers get the right information instantly even in contested environments.

This win continues to push AV to the center of innovation and space.

Additionally, AV secured a new firm fixed price option for two BADGER phased array systems under the SCAR or Satellite Communication Augmentation Resource program. This program represents a tremendous growth opportunity for AV as more BADGER systems move into production.

Lastly, AV was awarded a contract valued at \$499 million by the US Air Force Research Laboratory to develop material technology and deploy protective solutions to the front lines to guard war fighters against exposure to harm for electromagnetic radiation. Work under this large program known as HELMSSMAN, will help the turn against directed energy strikes in the future.

We continue to set the standard in advanced protective technologies and directed energy defense, positioning AV as a clear leader in safeguarding war fighters against emerging threats.

Further, our disruptive solutions continue to position AV as a leader in next-generation defense. From our family of Switchblade loitering munitions to advance counter UAS solutions, we're redefining the battle space. We have unseated incumbents with our LOCUST laser weapon system and secured key wins like Freedom Eagle-1 or FE1, delivering cost-effective kinetic counter UAS solutions for Group 3 and 4 drones and beyond.

With our AI and machine learning-driven platforms, we believe AV continues to set the industry standard, positioning us to fully capitalize on the generational opportunities ahead.

During the quarter, we continued to form additional strategic alliances and collaborations that will help AV expand domestically and internationally. In September, we signed a memorandum of understanding with Taiwan's National Chung-Shan Institute of Science and Technology, or NCS IST to collaborate on autonomous systems and technology to support Taiwan's defense and security needs.

We also signed a memorandum of understanding with Korean Air to advance medium and crude aircraft systems to the Republic of South Korea. Both of these agreements underscore our expanding international presence and steadfast commitment to providing flexible mission-ready solutions for our customers.

Both agreements are centered around AV's JUMP 20 and JUMP20-X systems. The systems provide the kind of operational versatility that continues to grow in popularity in international markets.

We also announced a collaboration with GrandSKY to establish the foundation for a Golden Dome for America Limited Area Defense architecture at Grand Forks Air Force Base in North Dakota. This collaboration is significant as it marks the first deployment of AV's critical counter UAS solution set to secure a US Air Force base, creating a model that can be replicated across other critical US national security sites.

As the demand for our innovative offerings accelerates, we recognize the critical importance of scaling quickly. Since last year, we have been focused on securing a new facility in Salt Lake City to expand our Switchblade manufacturing further. Plans are progressing on a 100,000-square foot facility that will allow for multiple Switchblade lines and provide additional capacity.

This new factory has the potential capacity to produce over \$2 billion worth of Switchblades or other AV products per year. We anticipate this factory to be operational about a year from now.

Beyond expanding our own footprint, we're also actively strengthening our supply chain to support anticipated demand continuing to stay ahead of the market. As part of our distributed approach to manufacturing for resiliency and risk diversification, we now have manufacturing sites operating across 12 different states, reinforcing our ability to scale rapidly and reliably.

In addition to scaling operations, we're transforming the defense technology landscape through our acquisition of BlueHalo. We are already realizing meaningful synergies from the BlueHalo acquisition, which Kevin will discuss in further detail. Together, we're building next-generation platforms that fuse counter UAS space technologies, directed energy, electronic warfare, cyber and integrated software solutions, creating a suite of capabilities unmatched in the industry.

This combination accelerates innovation and continues to position AV as the disruptor driving rapid change in a market hungry for speed, agility, and advanced solutions. We are reshaping expectations and setting a new standard for what can be delivered to the US and our Allied forces.

Before turning the call over to Kevin, who will provide more financial details on our second-quarter results, let me conclude with the following comments. Despite a challenging environment, we delivered a strong quarter. Our continued investment in R&D and capacity expansion is translating into strong growth in key program wins and positioning AV for even more growth in the coming years.

We recognize there is a generational shift in the US Department of Defense's procurement strategy and product needs. Our offerings are designed to meet warfighter requirements, and our strategy is fully aligned with these new practices. We're executing on manufacturing expansion and are confident that we can meet increased demand.

Integration of BlueHalo is progressing well, and this acquisition is helping to establish AV as a next-generation defense technology company with unmatched capabilities across multiple domains.

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

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**Kevin McDonnell** - AeroVironment Inc - Chief Financial Officer, Senior Vice President

Thank you, Wahid. Today, I'll be reviewing the highlights of our second-quarter performance, during which I will occasionally refer to both our press release and earnings presentation available on our website. I will start by commenting on our results for the quarter and then turn to guidance for the remainder of FY26.

While this quarter presented challenges in terms of the US government shutdown and our transition to new operational systems, we are very pleased with the continued business momentum and more importantly, our revenue and adjusted EBITDA outlook for the year remains in the same range despite some of the challenges in Q2.

Next, I'd like to draw your attention to slide 17 of the earnings presentation, which sets forth on definitions for our customer contracting activity. Going forward, each quarter will present a report the total contract awards, bookings, funded backlog, and underfunded backlog in the quarter.

Now I'll highlight some of that customer contra activity in the quarter. As Wahid mentioned, we earned awards with totaling ceiling of \$3.5 billion, and we achieved \$1.4 billion of bookings and ended the quarter with \$1.1 billion of funded backlog and \$1.8 billion of unfunded backlog. We're very pleased at the US Department of War contract activity continued progressing despite the shutdown, and we view this as a testament to the importance of the programs we're involved in.

Some of the recent key awards are highlighted on slide 10 of the earnings presentation. Both segments captured multiple large awards during the quarter.

As Wahid mentioned in his remarks, total revenue totaled \$472.5 million in the second quarter, which represented a 151% increase over the prior year as reported or a 9% increase on a pro forma basis. Legacy AV organic growth was 21% in the second quarter.

Slide 6 and 7 of the earnings presentation show the second quarter and the year-to-date revenue by operating group for each of our two segments compared to pro forma FY25 revenue. The AxS segment recognized \$302 million in revenue in the quarter, which represented a 15.7% increase over the FY25 pro forma revenues.

Precision strike and counter UAS products led revenue growth for the segment with nearly 38% increase at -- nearly a 38% increase compared to the pro forma FY25 second-quarter results. Strong Switchblade 600 and Titan sales led to the growth in this (inaudible) group.

Uncrewed systems, including both our small UAS and medium UAS products improved more than 8% from the pro forma results from the same quarter last year. Uncrewed systems without Ukraine revenues grew more than 50% year over year, driven by strong JUMP 20 revenue increase.

The Space, Cyber & Directed Energy segment recognized \$171 million of revenue in the quarter, which was similar to the pro forma results from the same quarter last year. The space and directed energy products grew more than 20% in the quarter versus the prior year with the LOCUST-directed energy counter UAS growth being one of the key drivers.

As Wahid mentioned earlier, this segment also received several large contracts this past quarter to include a significant contract for our long-haul laser communications and two BADGERS for the US Space Force's SCAR program.

Cyber Mission Systems showed a decline in revenue largely a result of programs that were discontinued and was negatively impacted by the government shutdown. As mentioned earlier, this segment had a strong quarter with new contracts with nearly \$500 million HELMSSMAN award among others.

Moving on to gross margins. Slide 13 shows the adjusted product and service gross margin, including reconciliations to GAAP gross margin. Second-quarter overall adjusted gross margins were 27% versus 41% in the second quarter of FY25. As noted, the business landscape of the combined new company has changed significantly with a higher service mix and several products in the early stages of maturation.

The second quarter did present some additional challenges to adjusted gross margin. We went live with our Oracle Fusion ERP system upgrade in the quarter. As a result, we experienced some operational inefficiencies and onetime costs related to the [go live].

With that said, we've made a major leap forward in our operational systems as we transition to the cloud to support a multibillion-dollar company.

In addition, we saw an unfavorable service product mix and unfavorable product mix partially as a result of the government shutdown caused by delays in FMS shipments. In addition, we lost revenues in our Space, Cyber & Directory Energy businesses during the shutdown. However, we believe the adjusted gross margin should improve in Q3 and be in the high 30s by Q4. We are maintaining our full year outlook for adjusted gross margins in the low 30s.

Moving on to operating expenses. Adjusted SG&A, which is net of intangible amortization and deal integration costs, was \$66.1 million versus \$33.2 million in the prior year. The increase is largely a result of a combination with BlueHalo.

As a percentage of revenue, adjusted SG&A in the quarter was 14% of revenue versus 17.6% in FY25. Again, these adjusted SG&A levels represent a shift in the business model, and we expect to end the year in the 12% to 13% range as we begin to realize synergies and achieve higher revenue levels.

R&D expense for the second quarter was \$36 million or 7.6% of revenue compared to \$28.7 million or 15.2% of revenue in the prior year. Again, this is a shift in the business model, and we expect R&D as a percentage of revenue to end the year between 6% and 7% of revenue, which represents an increase in R&D dollars over the prior year for the combined company.

In terms of adjusted EBITDA, slide 14 of our earnings presentation shows a reconciliation of GAAP net income to adjusted EBITDA. Adjusted EBITDA for Q2 was \$45 million, up from last year's Q2 of \$25.9 million as reported, primarily due to the incremental BlueHalo results. EBITDA as a percentage of revenue was 9.5% in the quarter.

Despite some of these onetime costs and impacts from the government shutdown, we continue to forecast the full year adjusted EBITDA between 15% and 16% of revenue.

Now turning to non-GAAP earnings per share. Slide 12 shows the reconciliation of GAAP and adjusted or non-GAAP diluted EPS. The company posted adjusted earnings per diluted share of \$0.44 for the second quarter of fiscal 2026 versus \$0.47 per diluted share for the second quarter of fiscal 2025, slightly lower due to the same reasons as stated previously.

Moving to the balance sheet. At the close of the second quarter, our total cash and investments amounted to \$669 million. As reported last quarter, we now have a completely new balance sheet as a result of the BlueHalo transaction and the convertible debt equity financings completed in Q1. Consequently, many of our balances are not comparable to the prior periods.

For instance, our overtime revenue recognition has increased from 41% to 75% year over year, driving that unbilled receivables. With that said, unbilled receivables continue to be at a higher level than we are targeting.

Turning to backlog. As noted earlier, our funded backlog at the end of the second quarter was \$1.1 billion, and unfunded backlog was \$2.8 billion. Our visibility to the midpoint of the revenue guidance range is now 93%. I should note that this is consistent with past practice that we include within our visibility revenue from long-term contracts we expect to perform during the fiscal year, but which have not been funded as of this date.

Finally, I'd like to provide you with our updated FY26 guidance. On slide 8 of the presentation, we provide fiscal 2026 guidance. Fiscal year revenue is expected to be between \$1.95 billion and \$2 billion. Adjusted EBITDA remains between \$300 million and \$320 million. And non-GAAP adjusted EPS is now projected to be between \$3.40 and \$3.55.

The midpoint of our revenue guidance range represents nearly a 15% growth over the pro forma FY25 results. The lower non-GAAP EPS range is a result of a higher full year projected tax rate, largely driven by the Q2 update of the purchase price allocation of the BlueHalo acquisition. With the government shutdown impacting both our fiscal Q2 and Q3, we have seen delays in some of the orders and therefore are shifting the projected revenues to the right.

Second half revenue should be split approximately 45% in Q3 and 55% in Q4. The adjusted EBITDA shift will be more pronounced with 70% of the second half EBITDA coming in the fourth quarter.

I'd like to close by echoing Wahid's remarks. We are very well aligned with the US Department of Word priorities and those of our allies, and we are excited about our prospects. Despite some of the challenges in Q2, we are confident of meeting our guidance for the year.

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

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**Wahid Nawabi** - AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer

Thanks, Kevin. Before turning the call over for questions, I'd like to reiterate some of the positive momentum entering the third quarter of fiscal year 2026.

First, record second-quarter awards with a total contract value of \$3.5 billion bolstered bookings to reach an all-time high of nearly \$1.4 billion, driven by key program wins that support AV's long-term growth.

Second, we also achieved another record second quarter revenue of nearly \$473 million.

Third, we launched several new innovative products aligned to our customers' highest priorities and continue to execute on expanding our manufacturing capacity to meet accelerated demand.

And fourth, with 93% visibility to the midpoint of our guidance range, we are raising the lower end of our fiscal year 2026 revenue guidance and now expect revenues between \$1.95 billion and \$2 billion.

Our strong second-quarter results reinforce our confidence in AV's future and our role in shaping the next era of defense with integrated capabilities across multiple domains of modern warfare, advanced technologies and the ability to scale rapidly, we believe we are well positioned to meet the department of the world's highest priorities and sustained significant growth in a demand-driven market.

The Department of War has reiterated sharpened focus on speed, scale, and commercially driven procurement strategies, all of which plays directly to AV's strengths. This has been our strategy from the very beginning, investing in innovative solutions ahead of demand, scaling rapidly, and driving innovation to deliver decisive advantages for our customers.

Our alignment with these priorities, combined with our successful track record and best-in-class production capacity creates a powerful competitive advantage and positions AV as a trusted partner ready to deliver at the pace the mission demands.

I want to thank our employees, shareholders, and customers for their continued commitment to AV and our mission. We're honored to support the most critical defense missions at this pivotal moment and we're ready to seize the tremendous opportunities ahead.

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

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions) Greg Konrad, Jefferies.

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### Greg Konrad - Jefferies LLC - Analyst

Maybe just one on programs. I think you announced that you got two more BADGER units in the quarter. Can you just remind us how you're thinking about the current scheduled SCAR and maybe how that contributes to the expected ramp for that program?

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### Wahid Nawabi - AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer

Sure. So Greg, as I mentioned in my remarks, we did secure an additional task order and award from the US space force for additional BADGERS, two more additional BADGERS. The whole SCAR program, as we mentioned in our comments before, has been so far in a customer-funded development process. We're shifting now from development activity to delivering products, most of which is going to end up eventually going into our firm fixed price contracts.

That transition not only ramps up the revenue for the second half of the year, but also improves the margin profile of that business. So we're very much on track with our plans. We're pleased with the performance so far, and we expect the margins as well as the revenue of that business actually improve in the third and fourth quarter of this year and continue to improve beyond this fiscal year.

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### Greg Konrad - Jefferies LLC - Analyst

And then maybe just one follow-up to that. I mean, I think you've talked about a couple of the headwinds that you saw in the quarter around profitability, including Oracle and the shutdown. If you kind of think about that ramp of profitability and margin, given the 70% in Q4, how are you thinking about that progression? How much is operating leverage versus maybe mix and just the biggest drivers that you see as you head into the second half?

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### Kevin McDonnell - AeroVironment Inc - Chief Financial Officer, Senior Vice President

Well, I think mix is going to be a big part of that as Wahid just mentioned about the BADGER program and going into fixed price product revenues, some of our other programs and LOCUST and things like this being product revenues and a ramp-up in delivering across the other business units increasing the proportion of product revenues versus service revenues.

We don't see the service revenues growing significantly in the second half, whereas the product revenue is going to drive most of that growth. So that's going to give us better mix. And that's why we're going to be able to achieve the high 30s adjusted gross margins by the fourth quarter.

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**Wahid Nawabi** - AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer

And Greg, let's also keep in mind that we have secured nearly \$3.5 billion worth of almost all sole source IDIQ contracts that allows us now to receive task orders underneath those contracts. Once the funding from the Big Beautiful Bill and the budgets for the Department of War comes through as a result of the shutdown that has been delayed, those product revenues are going to and task order is going to be received in the next one or two months.

That's what we expect, and we want to convert those to revenues. So the volume goes up, the mix improves, and also the profile of the profitability of some of these products and businesses are going to improve, and that's precisely what we expected at the beginning of the fiscal year.

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**Operator**

Ronald Epstein, Bank of America.

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**Unidentified Participant**

This is [Amanda] on for Ron today. I was wondering if you could -- in the past, you've given a breakout of buy products in the portfolio. I was wondering if you had any color there or if you could talk a little bit about the relative growth levels by product?

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**Kevin McDonnell** - AeroVironment Inc - Chief Financial Officer, Senior Vice President

Well, I mean, we try to give as much granularity -- we've improved our granularity this quarter by giving you further breakout of the different major product groupings for each segment. And so I try to give some color behind that that shows what products are driving the different growth in those different product categories.

So they're kind of combinations of products, obviously, but we're trying to provide more color for you on that. Was there something specific you were wondering about?

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**Unidentified Participant**

Just if you could talk about Switchblade growth. I think you mentioned Ukraine, if there's any color you could provide there?

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**Kevin McDonnell** - AeroVironment Inc - Chief Financial Officer, Senior Vice President

Yes. I mean, year over year, Switchblade by far is the fastest-growing product in the COES precision strike category. Overall, we saw significant growth, multiple x for the JUMP 20 in Q2 versus the prior year.

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**Operator**

Anthony Valentini, Goldman Sachs.

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**Anthony Valentini** - *Goldman Sachs Group Inc - Analyst*

It seems pretty obvious you guys have massive growth opportunities here across the 5 to 10 different products that you guys have been highlighting, but maybe like put a finer point on it, is there a way to think through the catalyst path over the next few months as some of the reconciliation funding starts to hit backlog? Like what should people be looking for?

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**Wahid Nawabi** - *AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer*

Anthony, yes, of course. I'll be glad to provide some more color there. We certainly have a significant amount of opportunity for growth and value creation here in the next -- not only just a couple of quarters, but next few years. We're positioned really, really well. If you look at the key catalysts for growth, loitering munition, of course, we continue to grow that category of the Switchblade and one-way attack drones that are in that bucket.

Our risk counter UAS solutions, the Titan family of products is another contributor of significant growth year over year. Our medium UAS product line, which is JUMP 20 and JUMP20-X is another category of strong growth and contributor to our growth in general as well as profitability.

Our P550, we expect significant orders for that in the third and fourth quarter of this year. The US Army is intending to purchase a lot. There's a lot of dollars in the budget for that, and we expect to have a fairly large share of that spend with the US Army. And we're also lining up a bunch of national customers for that product line.

The SCAR and BADGER program and product is also transitioning to production, and we're going to deliver more (inaudible) numbers, and we're going to ramp up revenue, the profile of that revenue was a higher margin as well as the volume is higher, that helps.

So in a nutshell, if you look at across our portfolio, we've got growth across almost every one of our key product lines. Some of them are contributing to some smaller extent versus larger ones, but they're all growing quite rapidly.

One area that may not grow as much as our cybersecurity business, and that's primarily because of it's a customer-funded engineering services and software solution business. That really doesn't ramp up aggressively in terms of growth. But overall, we're very pleased with the performance. We're looking for multiple quarters and years of growth. We're positioned really well with the shift in the US DoD and administration strategies.

The kind of business model and products and go-to-market strategy that we have is precisely what the US Department of Board is looking for, and we're positioned incredibly well. There's going to be a lot of money spent. It is really hard to predict exactly how much. There is a lot of demand coming our way, and we're getting ready for it as we speak.

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**Kevin McDonnell** - *AeroVironment Inc - Chief Financial Officer, Senior Vice President*

Yes. I mean, we think we're on the precipice of significant growth across all those categories. But as with anything in defense, it's difficult to predict the exact timing of that. But we definitely think we're very close to some breakthroughs on some of these products Wahid mentioned.

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**Anthony Valentini** - *Goldman Sachs Group Inc - Analyst*

Okay. Great. That's helpful. I appreciate all that color. One other quick one. I guess I'm just curious, like how do we square that with -- if I'm looking at the backlog in 1Q versus 2Q, it's slightly down. So can you guys help me understand like why that's the case?

And should we see the backlog is like significantly ramping into the back half of the year? Or is it just so unpredictable? It's more that you guys have a feel over the next 12 to 18 months versus the next 6.

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**Kevin McDonnell** - AeroVironment Inc - Chief Financial Officer, Senior Vice President

Well, I think it's pretty flat from Q1 in terms of the funded backlog. The underfunded backlog grew significantly. But remember, we were in the CR and the shutdown. So while we got many of these contracts through, which was great, a lot of them didn't come with significant funding.

And we expect that to be coming as they get back and our funding back to business on funding new contracts within the Department of War. So it's a little bit of an issue with the shutdown happening and delay in some of the actual funding on these contracts.

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**Anthony Valentini** - Goldman Sachs Group Inc - Analyst

Okay. And Kevin, do you have a number for like what you guys expect Switchblade to be in 2026? I know you guys gave the color on what the production capacity will be out of the Utah facility in the future, but is there a way for us to think about the 2026 forecast?

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**Kevin McDonnell** - AeroVironment Inc - Chief Financial Officer, Senior Vice President

I don't think -- we're not really giving specific guidance on the different products. But I think we talked about before roughly \$500 million of capacity before we increase to the new facilities. So you can build plus or minus that, probably.

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**Operator**

Louie DiPalma, William Blair.

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**Louie DiPalma** - William Blair Capital Partners - Analyst

Wahid, what was the tone from the Reagan Defense Forum over the weekend? And are you increasingly confident given all of the presentations of AeroVironment's positioning across your current product lines, whether it's your drones, your attack drones, the electronic warfare and space?

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**Wahid Nawabi** - AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer

Louie, I personally attended the Reagan National Defense Forum this past weekend. The overall sentiment is that we are the role model company that the US Department of War and the current administration wants to see a lot more of. We're setting the pace for everyone else. The procurement strategies are shifting to companies that develop things on their own dime.

They're doing it ahead of product program requirements. They're doing it at agile and warp speeds, then we're transitioning into production quickly. They're focused -- we're focused on all the right areas with the US Department of Board needs and has major capability gaps. These are critical areas of gap, capability gap, and it's required for the future defense of US and our allies.

We believe we're positioned incredibly well, and I think we're going to see continued demand to come our way because of the fact that we can also produce at scale today. We're one of the very, very few companies in these categories that actually has the capacity today and continue to expand it even further to deliver reliable, battle-proven products to our customers at scale.

That is a huge competitive advantage that we have compared to everyone else in the market. And we'll send the pace for everybody. So I think the sentiment is very positive and strong for AV.

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**Louie DiPalma** - *William Blair Capital Partners - Analyst*

And on this call, you've discussed many of your product lines, such as the P550, your BADGER with the SCAR program, your JUMP 20s. I was wondering, did your long-haul laser communications program from the undisclosed customer, was that contract recently upsized from \$240 million to \$385 million? It shows the larger number in your slide presentation.

And I was also wondering, have you started delivering terminals as part of that program?

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**Wahid Nawabi** - *AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer*

So Louie, I can only speak to that program at a very high level due to sensitivity of that program and customer. We are incredibly delighted and pleased with the success that we're having in long-haul laser communication terminal. Essentially, we all know from the conflicts of Ukraine that RF communication is very susceptible to jamming.

Every satellite that the US has in space essentially is susceptible to that jamming problem. If we cannot control and talk to our satellites, especially in the geosynchronous satellites, we've got a major problem. Those assets are not useful. And we are one of the only companies that we know of that has been awarded a contract to this magnitude up to \$240 million to actually provide the laser communication terminals to overhaul and upgrade the US geosynchronous satellite constellation for national security.

That is a massive, massive step forward for a company [in automation]. And we beat many of the major prime contractors in that competition. And so there's certainly a lot more upside on that contract because we're just beginning to deliver systems. We haven't delivered much yet.

We continue to work with the customer. Our system is performing really well, and it takes a while for that to happen. That's part of the program. So we're very excited, and there are options for them to increase that significantly.

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**Kevin McDonnell** - *AeroVironment Inc - Chief Financial Officer, Senior Vice President*

The two [381] includes the options as we put forth our new definitions here, to make sure we're all on the same page. That \$240 million was the original committed contract and the \$380 million was taking the options.

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**Louie DiPalma** - *William Blair Capital Partners - Analyst*

Great. So as part of the original committed contract, does that mean that is it funded already?

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**Wahid Nawabi** - *AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer*

No. So Louie, a vast majority of that contract is not funded yet. As Kevin said earlier, one of the reasons why our funded backlog nearly the same as last quarter, and it did not grow as much is because there's two things that has happened.

One, the government shutdown put employees of the government not coming to the office and being able to actually put contracts and award things at one. But the bigger problem was that because of the continuing resolution in the budget that just passed with the Big Beautiful Bill, those dollars have not made it into the accounts of our customers to be able to then award task orders against those IDIQs.

So we expect a significant number of additional funded task orders in Q3 and Q4, all of which is going to improve our backlog and will allow us to deliver more products and more revenue on third and fourth this year.

Additionally, will set us up really well for fiscal year 2017. We're not ready to provide any guidance for that yet. But that is going to be benefiting from the demand that's coming our way in terms of task orders and more funding.

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**Operator**

Ken Herbert, RBC Capital Markets.

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**Unidentified Participant**

This is (inaudible) on for Ken Herbert. Could you maybe discuss the margin profile of the SCDE segment? Is there maybe a time when you think that the adjusted EBITDA will be breakeven?

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**Kevin McDonnell - AeroVironment Inc - Chief Financial Officer, Senior Vice President**

Yes. It will continue to grow throughout the year. I mean, they were probably the most impacted by the government shutdown of any of our businesses. And they also had some delays in some of their receipts for their revenue recognition on their system. So they'll definitely be on track as we move forward throughout the year.

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**Wahid Nawabi - AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer**

And Peter, also, we strongly believe in that business, it is a very profitable, reliable, consistent business and business model. Both of those two businesses in the long run, are going to be profitable like they were in the past. There are going to be just these lumps of fluctuations that happen, but the businesses models are sound. They're very reliable in that regard, and we expect them to actually improve in Q3 and Q4 as we go.

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**Kevin McDonnell - AeroVironment Inc - Chief Financial Officer, Senior Vice President**

Yes. And their product mix is going to increase over their service mix. So that is going to drive their EBITDA margins up.

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**Unidentified Participant**

And I'm assuming the next piece of my question kind of goes hand in hand. But can you talk about the free cash for maybe the second half of the year? Or do you have a kind of a full year outlook for it as well?

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**Kevin McDonnell - AeroVironment Inc - Chief Financial Officer, Senior Vice President**

Well, we've always tried to say that we can get our EBITDA cash conversion over 50% is the goal for the year. And I still believe that's an achievable goal.

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**Operator**

Andrew Madrid, BTIG.

**Andre Madrid** - BTIG LLC - Equity Analyst

I wanted to dive a little bit deeper into the almost \$900 million Army contract, IDIQ, that you guys got. I think the initial award had said that it was pretty much exclusively small UAS and then you guys announced earlier this week that it also included C-UAS, namely the Titan.

I mean, can you tell us more about what the international opportunity looks like for these C-UAS platforms? I think this is about one of the first times we've really heard about it. Also, can LOCUST be sold internationally?

And then I guess also broadly, just how should we think about the margin distinction between domestic and international C-UAS sales?

**Wahid Nawabi** - AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer

So Andre, yes, the nearly \$900 million sole source IDIQ contract, multiyear, of course, from the US Army for our products. now includes Raven, Puma AE, Puma LE, but we could also sell our Titan counter UAS solutions as well as potentially in the future of the low-cost direct energy solutions.

This is a significant milestone because the US Army could have purchased these things under the existing contracts that we have, but they chose to actually add an additional contract with an additional \$900 million nearly ceiling for it allow us to deliver more products over the next couple of three to four years to our international customers. So that's a very positive news.

Secondly, the margins for international sales historically and in the future, will continue to be slightly more favorable than the domestic markets. Those customers do not buy as much as US DoD and generally, the margins are a little bit better. If we sell FMS, the margins are not a lot better. The best margins are international DCS sales. But FMS has less expenses, too, because we do not have the responsibility for exporting it. The US military does.

So we deliver the product to the US military and they deliver that to the customer -- the international customer. The market opportunity internationally is massive for us. Really, we're at the beginning phases of that for our counter UAS for directed energy for our Switchblade for one-way attack and for our SCAR BADGER systems that we have in our product portfolio.

We're just scratching the surface on those items, and some of them are literally just starting with no international sales. The area we're really strong is our small UAS, but we've got tremendous potential here. I expect the international market over the next several years to grow significantly and be a major contributor.

**Andre Madrid** - BTIG LLC - Equity Analyst

Got it. Got it. That's super helpful. And then maybe just to pivot to Switchblade, I think you said that by next year, you could support capacity of \$2 billion sales. I think previously, the number that you had disclosed was about \$1 billion. I just wanted to see what might be driving that difference?

**Wahid Nawabi** - AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer

Sure. So Andre, as we keep building these new factories, we're also improving a lot in terms of automation, and ability for us to produce and ramp up production. So we're -- as you know, we're ramping up production for Switchblade significantly already. We've already tripled -- doubled and tripled the year for the last couple of years. And we're going to continue to improve it even further.

The new facility that we have now in Salt Lake City going to come online later next calendar year, towards the end of next calendar year, has the potential to go above \$2 billion worth of production with multiple shifts. If we get to that level, it's going to be well over \$2 billion

factory. And I expect that to even go higher than that because there is so much more potential room for growth in terms of our automation and efficiencies in the production processes.

Last thing I want to mention about that is that that's factory is also very flexible. We can produce any variance of Switchblade, but we could also produce other products such as our one-way attack product solutions and our nonlethal UAS and other platforms that we have such as (inaudible) 1, et cetera, et cetera.

So we're setting the factory to be flexible and agile for a lot of our products, and we can shift production on that factory as we go forward.

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### Operator

Trevor Walsh, Citizens.

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### Trevor Walsh - Citizens JMP Securities LLC - Analyst

Great. Maybe just to touch on AV\_Halo a little bit. Wahid, great to see the new products or the new, I guess, module being added on to that. Can you maybe just take a step back though, around that whole product opportunity? Just given all of the different systems from both AV as well as the other providers in the ecosystem that you're partnering and OEMing with and they're able to kind of link in.

How much of that do this needs to work its way through the system in terms of getting those systems out into the field so that the customer can actually just know what's the right sort of overall software packages to go with those? I guess it's another way of asking kind of you have these wins around AV\_Halo now, but is there really a kind of much wider opportunity that's kind of going to, I guess, materialize later?

Again, what's the actual hardware piece a little bit more locked down, I guess? Does that make sense?

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### Wahid Nawabi - AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer

Yes, of course, Trevor. So let me provide you some color on that. First of all, I'm really excited about the AV\_Halo suite of software solutions. It's not just one particular product. Think of it as a very robust and broad portfolio of solution sets, a software stack and an ecosystem that provides lots and lots of different capabilities with different modules, such as AV\_Halo COMMAND, AV\_Halo CORTEX, AV\_Halo PINPOINT, et cetera, cetera.

So we launched two new modules, number one, and we're going to continue to launch more new modules to that. And the best way to think about it in a very simplistic way is like the Microsoft Office suite of products, Excel, Word, Outlook, all these different modules are underneath the office suite, right? The same thing applies to AV\_Halo.

AV\_Halo has several modules. In terms of deployment, we already have thousands, if not tens of thousands of some of their modules already deployed in the field. That is the beauty of our system that is all notable and integrated. And so what we've done is try to actually bring the ecosystem cohesively together and mesh it all together into one umbrella software solution.

Secondly, it is also at a very open architecture. We can integrate with any other platform, including competitor platforms, and we can also talk to any other systems and other battle management systems. And so our belief is that our solution set is incredibly not well understood yet, and we have a long way to go in terms of the opportunity set here over the next several years.

One example of that success story is in my comments about the US Army, who selected us for the human machine integrated formation, HIMF program record. That is a very strategic and critical program. We competed with very large companies and small companies that are trying to copy our model and we won. And US Army selected us.

That means that the future battle space on the edge of the battlefield, the systems and the controllers that they're going to use to operate these robotic systems, whether on the ground or air on land or sea, it's going to be ours. And we are open, interoperable, and we will integrate with many other systems that are better. And so we got a lot more coming in this area, and I can't be more excited about it in the future.

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**Kevin McDonnell** - AeroVironment Inc - Chief Financial Officer, Senior Vice President

And we already support multiple platforms with our AV COMMAND.

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**Wahid Nawabi** - AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer

We support not only our own platform, we support more competitor platforms today than our own, actually. And that's the testament that how open we are with our architecture and our platform for our customers. And that's one advantage that we have that most other systems that are not that open.

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**Operator**

Jonathan Siegmann, Stifel.

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**Jonathan Siegmann** - Stifel, Nicolaus & Company Inc - Equity Analyst

(multiple speakers) the shutdown. I thought that was great. And it's a really interesting time with signal flashing green here with a lot of intent of where we want to spend money, but with the shutdown causing a real wrinkle.

Historically, your January quarter hasn't been the strongest booking quarter for you guys. I'm just wondering if there's going to be some additional frictions this year you anticipate that we just can't catch up with all this pent-up demand and funded order? Is that a worry for you guys?

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**Wahid Nawabi** - AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer

Yes. Jonathan, that's a very well-put comment because the reason why we do not want to -- or we hesitated to raise the guidance even more is because there's still some timing risk on when we are going to get some of these task orders. The government came out of the shutdown, but still the budget for the fiscal year is not fully approved.

We have funding until January -- end of January. And while we expect some cost quarters to come in exactly when they're going to come in is anybody's guess. And so therefore, we expect -- we are confident that we're going to achieve our guidance that we've just provided. And anything above and beyond that, we're going to update you as we go in the next quarter.

Lastly, we did really well. We are on track with our plans on first quarter and second quarter, and we are exactly where we want it to be, despite the fact that the whole industry was dealing with a month of complete government shutdown.

And so I think our results are very good, and we're very pleased with our results, and we're looking forward to the second half of the year. we got aggressive goals, but we're very confident that we can achieve that. We've got the capacity, we've got the team, and we've got the demand from the customer and the support from our customers to get it done.

**Jonathan Siegmann** - *Stifel, Nicolaus & Company Inc - Equity Analyst*

That's great. And thank you for the details on the product lines, I appreciate it.

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**Operator**

Austin Moeller, Canaccord Genuity.

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**Austin Moeller** - *Canaccord Genuity LLC - Equity Analyst*

Just my first question here. Can you discuss how much of the backlog today is related to Ukraine and when that might convert? And similarly, how much of the backlog is from European allies ex-Ukraine?

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**Wahid Nawabi** - *AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer*

Well, Austin, we do not break down specific backlog by customer regions or by specific products. What I can tell you is the following. We have derisked and pivoted from our two years ago Ukraine demand almost entirely. It represents less than 5% of our revenue for the full year. Number one.

Number two, so far, we're on track with our plans and international demand is still back-end loaded a little bit because of the government shutdown and the contracting process, some of those FMS sales have not made it yet to actual contracts to us.

Do we continue to get contracts? Yes. But there's a lot more to come towards the second half as well as the next fiscal year. Overall, our backlog is pretty strong. \$1.1 billion worth of funded backlog, we had a \$1.4 billion worth of funded bookings. And I mean, very strong orders and backlog and visibility numbers given where we are with the quarter.

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**Kevin McDonnell** - *AeroVironment Inc - Chief Financial Officer, Senior Vice President*

Yes. We've been saying consistently that Ukraine should be less than 10% of our revenue for the year, and there would be no additional orders in our guidance for Ukraine this year. So if we did see some additional business from Ukraine, that would be positive for us. But we're not counting on any additional new orders for our Ukraine --

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**Wahid Nawabi** - *AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer*

On our forecast.

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**Kevin McDonnell** - *AeroVironment Inc - Chief Financial Officer, Senior Vice President*

In our forecast.

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**Jonathan Siegmann** - *Stifel, Nicolaus & Company Inc - Equity Analyst*

Okay. And just a follow-up. I know the Genesis of Red Dragon was to enable international sales by having an open payload bay that was payload agnostic and didn't have ammunition in it. But do you expect that Red Dragon could replace or take additional share from the Switchblade 600 over time with the US military in a long-range anti-armor, [anti-Fc] installation role?

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**Wahid Nawabi** - AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer

Austin, no, the short answer for that question is no. We do not expect that to take share away from Switchblade primarily because they're designed for very different mission sets. The missions that loading munitions such as Switchblade 300, 600, and now 400 are very different than the missions of one-way attack drones such as our Red Dragon.

And our family of Red Dragon is expanding. We believe both of those two product lines are going to grow significantly over the next few years. The demand for those systems are very robust from more than one service and more than one customer in country.

And so I think we're going to continue to see significant growth on both categories. They're actually complementary to each other in many ways as to how they engage with different targets and different missions for our customers.

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**Kevin McDonnell** - AeroVironment Inc - Chief Financial Officer, Senior Vice President

Yes. And our current volumes, we're only going to see growth in all those products. Red Dragon to potentially grow faster, but that doesn't necessarily mean it's taking away share from the other Switchblade products.

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**Operator**

Pete Skibitski, Alembic Global.

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**Pete Skibitski** - Alembic Global Advisors - Analyst

Just wondered if you could level set us. I'm still a little confused with where we're at with the Army long-range reconnaissance. I know that you guys as well as Edge both got contract in August, and then you announced another award yesterday. Are you guys sole source now on LRR with the P550? Or is there going to be kind of an ongoing competition over the next few years?

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**Wahid Nawabi** - AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer

More the latter, Pete. So what the Army has done, and this is consistent with many programs within the US Army and even other branches of the US Department of War services, is that the traditional construct and concept of a program of record single winner probably is not going to be that popular in that comment.

What they're going to do is they're going to pick at least two players. And from those two players, they want to field some systems and see who performs better. As the performance of that system is better, that vendor or that supplier most likely is going to get the lion's share of the volume of that program or requirement a capability gap. We believe our solution set is the best performing.

We have very strong fee from the customer that the customer is extremely satisfied with our systems. Yes, we announced a couple of quarters and awards, but we expect more. We're actually expanding and ramping up production in anticipation of more P550 orders from the US Army as well as additional international customers.

We believe that P550 product is a \$1 billion-plus franchise for the company over the next several years. We are such a strong believer in that product. I am personally very, very high on that product.

Now in terms of going forward, is it going to be just us? Most likely not. Do we expect to get a very large share of that spend? Yes. We expect to get a large share of it, and that's probably going to be consistent across multiple programs, not just LRR.

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**Pete Skibitski** - *Alembic Global Advisors - Analyst*

Got it. Okay. Very helpful. I appreciate that. And just on the P550 specifically, are you clear to export that internationally already? And if so, how many countries can you export it to? And how do you expect that to grow?

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**Wahid Nawabi** - *AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer*

Yes, Pete, that's a great question, and that product line was developed from the ground up. Number one, to be MOSA or Modular Open Systems Approach interoperable and compatible and compliant, A.

Two, it is developed primarily all with our own R&D dollars. So it's a non-ITAR product and its base configuration. There are modules within it that can make it ITAR, but we can -- we believe that we can sell the P550 to almost every customer that we sell are Pumas and Ravens and other products today.

So the market for P550 internationally is equally as large, if not larger, than our domestic market. And I believe that we're going to have several customers internationally that's going to come online and place orders for that capability later this fiscal year and even beyond this fiscal year.

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**Operator**

Colin Canfield, Cantor.

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**Colin Canfield** - *Cantor Fitzgerald LP - Analyst*

Maybe just figured it all home to cash and profitability. If we can kind of think about the building blocks of EBITDA, I think the 4Q guidance on adjusted EBITDA assumes roughly same ballpark as kind of combined whole company pro forma results as last year. So maybe just kind of walk us through how you think of the progression on SG&A and essentially kind of how we think about that EBITDA step up versus the supply chain kind of dynamics that you're focusing on?

And then bridging that over, I think Street is probably close to free cash flow breakeven this year. So is it fair to assume that kind of the timing and the shift that you talk about requires investment? Or is it fair to assume that this kind of quick book and turn -- or excuse me, shipping kind of picked book and ship business can allow you to hit something like that in terms of free cash flow?

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**Wahid Nawabi** - *AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer*

So Colin, let me just add some color to this. We do expect Q4 to be the largest quarter as we provided some color, almost 55% of our second half revenues are in the fourth quarter, number one. So the overall volume in fourth quarter is higher, number one.

Number two, the mix keeps getting more favorable in the fourth quarter from Q1 to Q2 to Q3 and Q4. So that's also a positive trend that's affecting Q4. We expect SG&A and R&D spending not to be a lot higher and not to be a lot lower. We're going to continue to maintain those levels, but the mix shift in the volume is going to help make a profitability much more pronounced in the fourth quarter in that regard.

Now in terms of the overall outlook, we've provided the full year numbers on profitability, and we're confident that we're going to be able to achieve that.

**Kevin McDonnell** - AeroVironment Inc - Chief Financial Officer, Senior Vice President

Yes. And I gave color in my script on SG&A and R&D and margins for the year. So that's really how you get there. It really comes from improved gross margins and some leverage on things like SG&A, partly because we realized some of the synergies that we've established in the first half but don't really realize for the second half of the year.

And in terms of capacity, those numbers really represent where we're at in terms of capacity, where we are increasing incrementally in many places in the second half or prior -- or even today, and that -- those reflected -- are reflected in the numbers.

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**Colin Canfield** - Cantor Fitzgerald LP - Analyst

Got it. And just to clarify, is it fair to assume that you're free cash flow breakeven this year?

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**Kevin McDonnell** - AeroVironment Inc - Chief Financial Officer, Senior Vice President

Well, we're looking for 50% -- it depends when you define all that, but we're looking at 50% cash conversion to our EBITDA.

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**Wahid Nawabi** - AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer

For the year.

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**Kevin McDonnell** - AeroVironment Inc - Chief Financial Officer, Senior Vice President

For the year.

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**Wahid Nawabi** - AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer

Which is a significant improvement over last year.

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**Kevin McDonnell** - AeroVironment Inc - Chief Financial Officer, Senior Vice President

Yes, which is a big improvement. So basically, that's EBITDA less our CapEx, less our working capital change from EBITDA.

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**Operator**

Peter Arment, Baird.

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**Peter Arment** - Robert W. Baird & Co Inc - Analyst

Wahid, could you -- maybe we'll just touch upon the cash comment that you guys just talked about it. Your precision strike kind of product revenues were up 68% for the first six months of this year, but unbilled continues to grow. And I thought we were under a new contract or payment schedule. Could you maybe give us a little more color on what's going on there?

**Kevin McDonnell** - AeroVironment Inc - Chief Financial Officer, Senior Vice President

Yes. I mean, as we've talked in many quarters, there's been a whole transition period there. There's been some changes in our contract office, our contracting personnel that have all been positive. And at this point, we feel like we have a clear to continue to start bringing that down the second half of this year.

And plus, we have this -- we do -- as we mentioned in the script, we are -- the amount of unbilled business is significant, particularly as the service businesses.

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**Wahid Nawabi** - AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer

And the revenue over time, a portion of our overall revenue is also increasing, primarily because of the BlueHalo and that also is playing a factor in this equation, Peter. And just one other comment to make on this topic is that we're really more focused on the top-line growth and making sure that we capture the opportunities and not lose momentum on the significant upside that we have in our long-term plan.

So we're really optimizing to make sure that we deliver for our customers. We deliver capability, develop the products. We're anticipating a lot more task orders in the second half of the year. And so we have to really start building products in advance. We can't wait until the last moment.

And while we're taking not all the risks, but we are taking some calculated risks to position ourselves to deliver for our customers because we know that they need these systems very desperately.

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**Peter Arment** - Robert W. Baird & Co Inc - Analyst

Okay. So just to be clear, you expect unbilled to be probably materially lower as we get through the fourth quarter, just given your comments about cash conversion on EBITDA?

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**Kevin McDonnell** - AeroVironment Inc - Chief Financial Officer, Senior Vice President

Right. It's pretty simple. We have the \$300 million to \$320 million of EBITDA in range. CapEx should be roughly a little bit less than half of that. So in order to hit 50% cash conversion of EBITDA, the change in working capital has to be minimal. And that's what we're forecasting.

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**Operator**

(Operator Instructions) Austin Bohlig, Needham.

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**Austin Bohlig** - Needham & Company LLC - Equity Analyst

Congrats on the nice order fall through even with the government shutdown. But my question has to deal with kind of the full year guide with this anticipated funding coming from the [OBD]. Is it fair to assume that anything that flows through that you're expecting is not yet baked in to your current full year guidance?

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**Wahid Nawabi** - AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer

No, Austin, we are expecting and we're expecting multiple task orders and orders on the second half that we believe we're going to be able to convert that to revenue. In order for us to overperform, it's going to be more difficult because of the timing, how long it takes to go build those products, get them tested and accepted by the customer and then deliver to our customers.

So we're confident about our full year guidance, number one.

Number two, we do expect contract awards and task orders in the second half that will convert to revenue, and that that's part of our forecast, and we are confident that we can achieve that.

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**Austin Bohlig** - *Needham & Company LLC - Equity Analyst*

Got you. Got you. And then just kind of some specifics on kind of like where are you hoping that these new contracts come from within your product portfolio? Is this precision strike, UAS, counter UAS?

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**Wahid Nawabi** - *AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer*

So Austin, it's a very nice, nice portfolio or basket of contracts and award that we expect. It's basically the critical areas that the US DoD needs them desperately and we've been talking about. So P550, more Switchblade, more one-way attack, more counter UAS, more directed energy, more SCAR and BADGERS.

And those are the key areas that we expect more of in our second half of the year. there's obviously orders for cyber and other businesses, too, but those five or six categories make up the lion's share of the expected additional contract awards and task orders for the second half.

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**Operator**

Clarke Jeffries, Piper Sandler.

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**Clarke Jeffries** - *Piper Jaffray Inc - Analyst*

I wanted to ask, Wahid, how do the recent changes to missile technology control and the treatment of UAS affect the current AeroVironment portfolio and maybe even how your posture might change for the future product portfolio? Did any of those changes have any direct impact on the \$870 million IDIQ? It sounds like maybe there was some counter UAS focus to that contract, but curious there.

And then any other key policy changes you'd flag as crucial for growing the international business?

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**Wahid Nawabi** - *AeroVironment Inc - Chairman of the Board, President, Chief Executive Officer*

Sure. So we expect -- first of all, the comment about the change in policy, absolutely. We believe that the new policy and definition that the US Department of War and government came up with how they categorize drones and how the categories loading munitions and one we attack is very favorable to us because they're trying to lax the definitions as to how it's treated versus a true missile that goes very long, long distances, and it's categorized as a missile.

So an arm drone or on FPV is not categorized the same. That is going to help us significantly over the next two to three years. It's not really immediate, but it is over the next two, three years.

Secondly, yes, the sole source nearly \$900 million IDIQ is directly related to that because the US DoD and the Department of War expects us to ship a lot of products because of the demand that they see from different allies. Obviously, the US Department of War is in contact with those international customers, and they see the uptick in demand for our solutions.

So we do expect that to happen. But most of that is not going to happen overnight. It's still a process that takes some time, and we work it.

Overall, we feel very positive about the general demand for our solutions from international markets, including Direct Energy, Counter-UAS, one-way attack, loading munition, P550, JUMP 20.

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**Operator**

And this concludes the Q&A session. I will turn it back to Denise for final comments.

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**Denise Pacioni - AeroVironment Inc - Investor Relations**

Thank you once again for joining today's conference call and for your interest in AeroVironment. As a reminder, an archived version of this call, SEC filings, and relevant news can be found under the Investors section of our website.

We hope you enjoy the rest of your evening and we look forward to speaking with you again following next quarter's results.

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**Operator**

This concludes today's conference call. Thank you for participating. You may now disconnect.

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