01-Nov-2023

Spirit AeroSystems Holdings, Inc. (SPR)
Q3 2023 Earnings Call
CORPORATE PARTICIPANTS

Ryan Avey  
Director-Investor Relations, Spirit AeroSystems Holdings, Inc.

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Mark J. Suchinski  
Senior Vice President & Chief Financial Officer, Spirit AeroSystems Holdings, Inc.

OTHER PARTICIPANTS

Seth M. Seifman  
Analyst, JPMorgan Securities LLC

Sheila Kahyaoglu  
Analyst, Jefferies LLC

Myles Walton  
Analyst, Wolfe Research LLC

Scott Deuschle  
Analyst, Deutsche Bank Securities, Inc.

Douglas S. Hamed  
Analyst, Sanford C. Bernstein & Company

David Strauss  
Analyst, Barclays Capital, Inc.

George David Shapiro  
Analyst, Shapiro Research LLC

Noah Poponak  
Analyst, Goldman Sachs & Co. LLC

Robert Stallard  
Analyst, Vertical Research Partners LLC

Scott Mikus  
Analyst, Melius Research LLC

Cai von Rumohr  
Analyst, TD Cowen

Gavin Parsons  
Analyst, UBS Securities LLC

Peter J. Arment  
Analyst, Robert W. Baird & Co., Inc.

Michael Ciarmoli  
Analyst, Truist Securities, Inc.

Kristine Tan Liwag  
Analyst, Morgan Stanley & Co. LLC
MANAGEMENT DISCUSSION SECTION

Operator: Good morning, everyone, and welcome to the Spirit AeroSystems Holdings, Inc. Third Quarter 2023 Earnings Conference Call. My name is Seb and I'll be the coordinator today. [Operator Instructions]

I would now like to turn the presentation over to Ryan Avey, Senior Director of Investor Relations and FP&A. Please proceed.

Ryan Avey
Director-Investor Relations, Spirit AeroSystems Holdings, Inc.

Thank you, Seb. And good morning, everyone. I'm Ryan Avey. With me today are Spirit's President and Chief Executive Officer, Pat Shanahan, and Senior Vice President, Chief Financial Officer, Mark Suchinski.

Before we begin, I need to remind you that any projections or goals we may include in our discussion today are likely to involve risks, including those detailed in our earnings release, in our SEC filings, and the forward-looking statement at the end of this web presentation. In addition, we refer you to our earnings release and presentation for disclosures and reconciliation of non-GAAP measures we use when discussing our results.

With that, I'd like to turn the call over to our Chief Executive Officer, Pat Shanahan.

Patrick M. Shanahan
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Great. Thank you, Ryan. And good morning, everyone. Welcome to Spirit's third quarter earnings call. It is a privilege to be here with you today representing Spirit AeroSystems and our global team. I want to thank the board for entrusting me with this responsibility while we search for a permanent CEO. On behalf of the entire board, we thank Tom Gentile for seven years of dedication and service with Spirit.

I'm very familiar with Spirit and its operations from my time at Boeing and as a board member for the past two years. My trips to Wichita go back to the 1990s where we tackled new programs and production rate increases together.

Now, I am the supplier, not the customer. But the dynamics are the same. Over the past several years, Spirit has expanded its portfolio of commercial and defense businesses. However, the core of the business, designing and building large scale aerostructures, has not changed.

I've been in the role for about 30 days now. To borrow a military acronym, my approach since the first day has been TACAMO, take charge and move out. Meaning, I'm with the Spirit team at all levels, deep into program and production rate plans and engaging with all our major customers.

My initial impressions are that we have a strong team and tremendous capabilities, but we need better precision in our plans, better performance and the right schedule. We are manufacturing a product we produced in large quantity at high rates before, as opposed to being in the throes of complex commercial development while concurrently ramping up production.
My focus is simultaneously stabilizing operations, delivering on our customer commitments, and strengthening Spirit financially. I want 100% alignment with our commercial and defense customers. I'm driving performance every day, and most importantly, building cohesive teams that view working together as the most effective way to perform and win.

The recent agreement with Boeing was an important step in the right direction. The strengthened partnership will support our shared goals of both companies to execute the increasing production rates, also devoting increased attention to our other major OEM commercial partnership.

Let me touch briefly on our strategy. I do not intend to wait for my replacement before moving forward. Regarding diversification, I will narrow the aperture. I don't have an appetite for next square adjacencies. We, Spirit, will build on our core defense and aftermarket success.

My principal goal is to be cash flow positive as soon as possible. Executing on programs, increasing deliveries is the most crucial lever to achieve that goal. However, we have other cash levers to pull to accelerate many of the activities previously developed along with new ones we are covering every day.

Shifting the discussion to market demand, it's incredible what a difference a couple of years make. We're witnessing unprecedented demand. I'm encouraged by the unbelievable organic growth in our core segment with a $42 billion backlog. The demand comes with challenges that we must mitigate as part of a new world that is less stable.

I recognize we have disappointed our stakeholders. We want to restore confidence in the company. I'm passionate about this industry, my customers and Spirit. I'm in Kansas most days because this is where most of the action is. The people here and, quite frankly, at all our operations have been warm and welcoming.

I'd like to provide you guidance for 2024, but I'm not prepared to at this time. My plan is to give guidance at our next earnings call, consistent with previous practices.

I'll now turn the call over to Mark to review with you our third quarter financial results.

Mark J. Suchinski
Senior Vice President & Chief Financial Officer, Spirit AeroSystems Holdings, Inc.

Thank you, Pat. And good morning, everyone. As many of you know, I've known Pat as a member of our board for a while now and I look forward to working closely with him as we navigate the path forward. I can tell you that we are aligned on our priorities and the trajectory of Spirit.

Now, turning to recent events, we are pleased to have reached a memorandum of agreement with Boeing in October, which we expect will result in improved cash flow over the next several years. I want to highlight the financial impacts of the agreement, which will be reflected in our financial results beginning in the fourth quarter.

First, the MOA established an immediate higher price in the 787 program with reductions to pricing on the 737 program beginning in 2026. We expect to record a reversal of a forward loss and material right obligations of $350 million to $370 million as a result of the 787 price increase. With this, a majority of the existing 787 forward loss liability will be reversed, and we anticipate positive margins on the program beginning in the first half of 2025 as production rates increase.
Next, the MOA provided for a broad release of existing claims and liabilities, which will include the reversal of $23 million of anticipated claims previously recorded related to the 737 vertical fin attach fitting issue.

In addition, we will receive funding for certain tooling and capital through 2025 on the 737 and 787 programs. We will repay the majority of the capital funded related to the 787 program beginning in 2025.

In October, we received an advance on the total expected CapEx funding of $100 million. Between now and 2025, there will be some timing differences between the receipt of funds and the CapEx spending, which will be reflected on the statement of cash flows.

And finally, the repayment dates were extended on the previously disclosed $100 million – $180 million advance of customer financing received in the second quarter of this year. We will now make repayments of $90 million in December of 2025 and equal repayments of $45 million in December of 2026 and 2027.

The MOA strengthens the relationships with our largest customer and further aligns the parties for future success. Broadly speaking, the agreement provides increased cash over the next several years, which will help support the production rate ramps across the different Boeing programs.

Now, let me take you through the details of our third quarter financial results which, I remind you, does not reflect any impacts of the recent Boeing MOA. So, now let’s start on slide 2.

Revenue for the quarter was $1.4 billion, up 13% from the third quarter of 2022. Year-over-year improvement was primarily due to higher production on almost all of our commercial programs, as well as the increased Defense & Space and Aftermarket revenues. Overall deliveries for the quarter increased 5% year-over-year.

The third quarter of 2023 revenue was impacted by disruption from the IAM work stoppage in early July and the Boeing 737F aft pressure bulkhead issue and continued supply chain and labor challenges, which resulted in less near-term deliveries, specifically on the 737 program. We now expect full year deliveries on the 737 program of approximately 345 units to 360 units.

Now, turning our attention to EPS. We reported an earnings per share of negative $1.94 per share compared to negative $1.22 per share in the third quarter of 2022. Excluding certain items, adjusted EPS was negative $1.42 per share compared to negative $0.15 per share in the prior year.

The operating margin was negative 9% compared to breakeven in the same period of 2022, driven by higher changes in estimates and excess capacity costs recognized during the current period.

Third quarter forward losses totaled $101 million and unfavorable cumulative catch-up adjustments were $64 million. This compared to $49 million of forward losses and $5 million of unfavorable cumulative catch-up adjustments in the third quarter of 2022.

The current quarter forward losses relate primarily to the 787 and A350 programs and were driven by higher estimates of supply chain, labor, and other related costs. The unfavorable cumulative catch-up adjustments relate primarily to the 737 and A320 programs, reflecting higher factory costs and rework costs related to the quality issue on the 737 aft pressure bulkhead.

Additionally, excess capacity costs during the third quarter of 2023 were $56 million, up from $31 million in the same period of 2022. Other income in the third quarter of this year was $7 million compared to other expense of
$42 million in the prior year. The variance was primarily due to noncash pre-tax charges of $73 million recorded in the third quarter of 2022, driven by the termination of our Pension Value Plan A as well as lower pension income during the current period.

Let's now turn to free cash flow. Free cash flow usage for the quarter was $136 million. Cash usage increased compared to the same period of 2022, largely driven by the negative impacts of working capital and costs associated with factory disruption. Working capital was impacted by the disruption and work stoppage associated with the IAM strike at the beginning of the third quarter, rework and disruption costs related to the 737 aft pressure bulkhead issue, as well as ramping to higher production rates on the 737 program.

Third quarter 2023 cash from operations also included $50 million customer advance that was previously disclosed and the payment of the ratification bonus related to the IAM contract of $23 million. We have updated our full year free cash flow to reflect the lower 737 deliveries expected for the year and the impacts of the Boeing MOA and now expect our full year free cash flow to be in the range of negative $275 million to negative $325 million.

With that, let's now turn to cash and debt balances on slide 3. We ended the quarter with $374 million of cash and $3.9 million of debt. Addressing the $1.2 billion of 2025 debt maturities is a near-term priority, and we continue to evaluate all refinancing options to address debt as well as our overall liquidity.

Next, let's discuss our segment performance, starting with the Commercial segment on slide 4. In the third quarter of 2023, Commercial revenue increased 10% over the same period of 2022 due to higher production volumes on almost all of our programs.

Quarterly operating margin decreased to negative 7% compared to positive 4% in the prior year, driven by higher unfavorable changes in estimates and excess capacity costs recorded in the current period. The changes in estimates during the third quarter, which I previously discussed, included forward losses of $87 million and unfavorable cumulative catch-up adjustments of $59 million. In comparison, during the third quarter of 2022, the segment recorded charges of $47 million of forward losses and $7 million of unfavorable cumulative catch-up adjustments.

Next, let's turn to Defense & Space segment on slide 5. Defense & Space revenue grew to $206 million or 27% higher than the third quarter of last year due to higher development program activity and increased KC-46 Tanker production.

Operating margin for the quarter decreased to 5% compared to 11% in 2022, primarily due to higher changes in estimates recorded in the current period.

The segment recorded forward loss of $15 million and unfavorable cumulative catch-up adjustments of $5 million compared to forward losses of $2 million and favorable catch-up adjustments of $2 million in the third quarter of 2022. The forward losses were primarily driven by higher production cost estimates on the Sikorsky CH-53K program and unfavorable cumulative catch-up adjustments that were primarily driven by the P-8 program.

For our aftermarket segment results, let's turn to slide 6. Aftermarket revenues were $97 million, up 21% compared to the third quarter of 2022, primarily due to higher spare parts sales. Aftermarket continues to grow along with the global air traffic recovery and is on track to meet the plan for the year. Operating margin for the quarter was 19% compared to 24% during the same period of 2022, driven by sales and model mix.
With that, we'll be happy to take your questions.

QUESTION AND ANSWER SECTION


Seth M. Seifman
Analyst, JPMorgan Securities LLC

Thanks very much. Good morning, everyone. And welcome, Pat.

Patrick M. Shanahan
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Good morning.

Seth M. Seifman
Analyst, JPMorgan Securities LLC

I've got a bunch of questions here – morning. A bunch of questions, but maybe I'll just jump. I wanted to ask you specifically, Pat, about two things that you said in your opening remarks.

One is, you talked about the other cash levers to pull to accelerate. I wonder if you could expand upon that. And you also talked about having the right schedule and, I wonder, when we think about the 737 production from here, what does the right schedule mean and what's the – what's really – what are the two or three things that you think are the most important to getting to adequate 737 profitability and not having more of these negative cum adjustments?

Patrick M. Shanahan
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Sure, Seth. Happy Wednesday. Let's maybe take the first one. The biggest – as I mentioned, the biggest lever to get to a positive free cash flow is program performance, but that's not a pass for the rest of the team to go after indirect costs, and those range from organization structure to enforcement of contracts with our suppliers to a number of the other traditional things that you might address in terms of looking at inefficiencies or belt tightening.

In addition to that, they're just things we have to stop doing. So, in parallel to the other improvement activity, we've really accelerated our focus on, hey, every dollar matters and let's bring it to the bottom line more quickly.

Your other question, I think, is really about the most important issue that we're dealing with right now. And that is the right schedule. And what I've learned over my almost 40 years in this business is, if you get the right schedule, everything else works. A schedule is a barometer for performance and, if you're on schedule, you're going to realize the appropriate costs. And if you get the right costs, you'll get the right financial results.

When I look at the schedule, and hopefully with the guidance we provided in terms of end of quarter deliveries, you did the math. And the math is, let's adjust for holidays and non-working days, our effective rate, when you look at deliveries is we're at about 37 to 42 a month in the fourth quarter, delivering to Boeing. We have a path to the 50s in 2025. And the reason I say we have a path to the 50s is we've been there before. So it's not something new. It's a question of how do we stabilize in our internal operations, so that without the effort we're using today,
we can cost effectively, with high-quality, produce the fuselages that Boeing so desperately needs. The path is through rate increases. The biggest – the two biggest levers for us are the supply chain and our own internal productivity.

When you just look at producing 737 fuselages at 42 a month, it's roughly 25,000 parts that go into one. And so, at 42, that's a million parts we need per month. And when you look at the amount of fasteners that we put in, it's something on the order of 10 million a month. And so, for us to produce, it's really about being synchronized and stable and there's just a lot of detail that goes into achieving that.

I believe that we'll be able to stabilize here and meet Boeing's demands in 2024. I'd like to walk you through the detailed schedule that we're working on. I would just tell you this, is that, we're not doing things parametrically. We're down to looking at things by the day, by the train pull, by the supplier. I've been here only a short period of time, but the readiness that we didn't have in the past is not the readiness you will see in 2024.

Seth M. Seifman
Analyst, JPMorgan Securities LLC

All right. Thank you very much.

Patrick M. Shanahan
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

You're welcome.

Operator: Our next question comes from Sheila Kahyaoglu from Jefferies. Please go ahead.

Sheila Kahyaoglu
Analyst, Jefferies LLC

Good morning, guys. And happy Wednesday to you too, Pat. So I was wondering if you guys could talk about the free cash flow revision, $275 million to $325 million of usage. How are you thinking about the change there from the prior guide? How much of it is tied to the 737? And just as we think about the step up in Q4, what really changes? First 30 days or so on the job, what have you seen that could be an immediate improvement?

Mark J. Suchinski
Senior Vice President & Chief Financial Officer, Spirit AeroSystems Holdings, Inc.

Well, Sheila, let me just take the walk on the headwinds and the tailwinds, and then I think Pat can provide some additional color. The biggest impact to free cash flow from a headwind standpoint is fewer 737 deliveries. And I think the challenge that we have here is, when we were staffed to 42 airplanes per month, we've been bringing in parts to help support 42 airplanes per month. And when we drop our deliveries from the previous forecast of [ph] $370 million to $390 million to $345 million to $360 million (00:21:18), a lot of that cost is embedded into our system. And so, by not delivering the aircrafts, we're not collecting the cash on the delivery. So I think the impact is a little bit bigger than you've put in your note as it relates to missing the deliveries.

The additional forward losses and the negative cum catch-up adjustments that we took is going to add some additional pressure to cash in the fourth quarter. And then we're seeing lower A220 deliveries in the fourth quarter, and that's primarily driven by a customer change in their schedule.
On the flip side, positiveness from the Boeing MOA, the 784 price increase, and the CapEx funding. So I think if you factor all those things in, the biggest impact I would say is that the lower 737 deliveries and us being staffed and having the working capital in place, and we’re just not going to relieve that inventory and collect the cash.

Sheila Kahyaoglu
Analyst, Jefferies LLC

Okay. Got it. Thank you.

Patrick M. Shanahan
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Thanks, Sheila.

Operator: Our next question comes from Myles Walton at Wolfe Research. Please go ahead.

Myles Walton
Analyst, Wolfe Research LLC

Thanks. Good morning. One quick clarification and then one question for you, Pat. So on the clarification, are you currently shipping to Boeing conforming fuselages at this point? I realize that you were able to recognize revenue and earnings on sort of nonconforming and then fix after the fact. But if you can update us if you're now conforming.

And then, Pat, you've made comments about diversification in your opening remarks. And just curious, I know you've been on the board for a few years. And you've only been on the job for a very short period of time. But is diversification necessary to make Spirit a great company? It had 80% concentration to Boeing just a few years ago. And obviously, the stock did quite nicely and the revenue and earnings were actually pretty good. So is diversification required?

Patrick M. Shanahan
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Sure. Maybe I'll just take the diversification one first. To the degree that Spirit has approached that in the past, I would say no. Diversification doesn’t make sense at this time. And when you look at the demand for commercial airplanes, having two of the biggest customers in the world and not being able to satisfy the demand, it should command our full attention.

Maybe the kind of the next level down, we’ve built a great defense business here and it's a more dangerous world. And I think what you would take away from some of that is we have tremendous engineering capability. And when you think about the future of large-scale aerostructures, it’s advanced materials. So, to that extent, the diversification and probably developing broader capability in advanced materials makes a lot of sense. Aftermarket is – just isn’t of the volume that we see in the other businesses.

And to your earlier question, I believe they’re conforming. We’ll make sure to get back to you on a full answer there.
Yeah, Myles. The product that we're shipping to Boeing at this point in time is being reworked and is conforming. We've put the fixes in place, so we're in good shape there.

Myles Walton  
Analyst, Wolfe Research LLC

Okay. Thank you.

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Thank you.

Operator: Our next question comes from Scott Deuschle from Deutsche Bank. Please go ahead.

Scott Deuschle  
Analyst, Deutsche Bank Securities, Inc.

Hey. Good morning.

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Hey. Good morning.

Scott Deuschle  
Analyst, Deutsche Bank Securities, Inc.

Pat, my understanding is that supplier price negotiations with Airbus these days often revolve around moving money from one year to another, but that they often fail to address the underlying long-term unit economics for suppliers. But it seems like you need a real structural fix here rather than a Band-Aid, so I'm curious if you think it's possible that you get a structural remedy from Airbus. And if not, maybe you can describe what your other alternatives might be? Thank you.

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Well, I won't describe what the alternatives are because I think we can get a remedy. And I am spending more and more time with my Airbus counterparts, and this is an item of utmost urgency for me personally, and I will be – if not leading – very deep into these conversations and discussions.

If you would indulge me for a minute just kind of talking about composites and advanced materials because, as I mentioned before, it really is the future. And when we think about the situation, we have a near-term financial problem. And when I look at the A220 or the C-Series, it was produced about the same time as the 787 and the A350, from a technical standpoint, those products are performing extremely well. The maturity of the production system, when those designs were certified, were really immature and there are inherent cost limitations and the performance that we should be realizing out of the manufacturing system just isn't there, but I think it's inherently not there.

Between us and Airbus, we have to come to some resolution to address that discontinuity. I think we'll be able to get to the place that makes sense for both parties, but it is a near-term action that I'm committed to undertaking, and my counterparts at Airbus feel the same sense of urgency.
Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Yeah.

Operator: Our next question is from Doug Harned from Bernstein. Please go ahead.

Douglas S. Harned  
Analyst, Sanford C. Bernstein & Company

Good morning. Thank you.

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Good morning, Doug.

Douglas S. Harned  
Analyst, Sanford C. Bernstein & Company

When you look at – Spirit’s been dealing with new quality escapes over the last year that have resulted from manufacturing problems that happened well before this year, such as the tail fittings, the aft bulkhead issue, 787 non-conformities. How do you make sure that there are not more issues like these still to come out and how are you thinking about changing the way you approach quality from an operational standpoint, so you can prevent this in the future?

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Well, Doug, that's probably reading my mind in terms of what's really going to change the reputation and give customers greater confidence is that we really deliver pristine quality products to our customers.

Maybe just let me frame it from this standpoint. The tone from the top internally is that my priority is the safety of our teammates, the quality of the product that we build, and productivity. Externally, the focus is quality to our customer and on-time reliable delivery.

The mindset I have is that we can be zero defects. We can eliminate all defects. We have a very robust quality management system. But every day, we have to put time and attention to that, and it isn't as though there's a silver bullet out there or a different procedure that we can implement. It's the whole organization being first and foremost focused on how we build the product.

And I think you'll see that over time because that's where my time will be in. As you know, where you put your time gets people's attention. And leadership has a long shadow, and I think you'll see us improve quite a bit in this area.
Douglas S. Hamed  
Analyst, Sanford C. Bernstein & Company

Okay. Thank you.

Operator: Our next question comes from David Strauss at Barclays. Please go ahead.

David Strauss  
Analyst, Barclays Capital, Inc.

Thanks. Good morning. Hi, Pat.

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Good morning.

David Strauss  
Analyst, Barclays Capital, Inc.

Good morning. Mark, I think before you guys have talked about getting to free cash flow positive in 2024, is there anything on the other side of the Boeing MOA as to why that still wouldn't be the case? That's my first question.

And second question, just an update, you mentioned the urgency around the refinancing. What are you looking at in terms of timing to come to market? I think previously you talked about maybe doing in two phases. So, any update there? Thank you.

Mark J. Suchinski  
Senior Vice President & Chief Financial Officer, Spirit AeroSystems Holdings, Inc.

Well, good morning, David. Good to hear from you. As it relates to 2024, I think Pat said, he's 30 days into his role here, he's making his way through. We're looking at the business holistically and really focused on completing the year, getting the business stabilized and then providing you guys a good, robust update in February.

But I'll just kind of reiterate what we said previously. We expect 2024 to be a positive cash flow year. The Boeing MOA is definitely a benefit to 2024 and beyond. And so, I'll leave it at that at this point in time and in February we'll come back and give you more specifics around our plans.

As it relates to the refinancing, it's obviously a big priority for me. The refinancing is a little more than a year out. The goal here is to assess all of our options that we have at this point in time. We've got some good plans in place. We're thinking through. We've been successful as we've gone to the markets in the past. And I think that's a – it's – as Pat talked about, his big goal working with Airbus and one of my big goals is getting through the refinancing, getting us behind us, so we can focus on the business in 2024.

And so, there's a sense of urgency there. It's a near-term priority. And we're going to be working through that as I had previously stated to make sure that we get the refinancing done before the debt becomes short term.

David Strauss  
Analyst, Barclays Capital, Inc.

Great. Thank you very much.
Mark J. Suchinski  
Senior Vice President & Chief Financial Officer, Spirit AeroSystems Holdings, Inc.

Thank you.

Operator: Our next question comes from George Shapiro from Shapiro Research. Please go ahead.

George David Shapiro  
Analyst, Shapiro Research LLC

Good morning. Welcome, Pat. It's been a while, but good to see you back in there.

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Yeah. Thank you. Good to be here.

Mark J. Suchinski  
Senior Vice President & Chief Financial Officer, Spirit AeroSystems Holdings, Inc.

Morning, George.

George David Shapiro  
Analyst, Shapiro Research LLC

And, Mark, if I looked at this quarter's free cash flow, I take out the $100 million that you're getting from Boeing and I don't – I'm not sure whether you got the – another advance for Airbus. But if you did, you're still – next year's free cash ought to be a lot better than just looking at this year's implied fourth quarter, which was like $140 million, take out the $100 million from Boeing, so at $40 million. And I don't think there was an Airbus payment there, you can correct me. But why won't next year at least be as good as the annualized rate for this year's fourth quarter?

Mark J. Suchinski  
Senior Vice President & Chief Financial Officer, Spirit AeroSystems Holdings, Inc.

Good question, George. I think as I addressed with David, as it relates to free cash flow, again, we'll stick with the fact that it's going to be positive next year. We'll provide you more specifics around that when we come back and chat with you in the first week of February when we disclose our results. We don't want to get ahead of things. Pat's got a lot of work to do here, and we're all here supporting him. We'll pull together a good plan and we'll provide you guys an update in February.

George David Shapiro  
Analyst, Shapiro Research LLC

Okay. And then, one quick one for you, Mark. The higher-than-expected excess costs, can you give us some color with that and kind of what the thinking might be when we get to the fourth quarter?

Mark J. Suchinski  
Senior Vice President & Chief Financial Officer, Spirit AeroSystems Holdings, Inc.

Sure, George. I would just say this. The third quarter was highly disrupted. When you think about our production, the number of units, our position in the factory starting the quarter, not gearing back the production line back up until around, call it, July 10 because of the IAM work stoppage and then the aft bulkhead issue.
So, I would say, for the most part, it's the IAM strike, it was the quality issue, and then just some of our own performance in the factory that ultimately added to the excess costs. And so, what I would say is it's a little bit of an anomaly because of that. And as we move into 2024, I would expect us to continue to see that – those excess costs go down as we go up in rate and absorb more of the fixed cost overhead here. So, again, I think we'll continue to see things improve in the fourth quarter and then get better in 2024 as compared to 2023.

George David Shapiro  
Analyst, Shapiro Research LLC

Okay. Thanks very much.

Mark J. Suchinski  
Senior Vice President & Chief Financial Officer, Spirit AeroSystems Holdings, Inc.

Okay. See you, George.

George David Shapiro  
Analyst, Shapiro Research LLC

See you.

Operator: Our next question is from Noah Poponak from Goldman Sachs. Please go ahead.

Noah Poponak  
Analyst, Goldman Sachs & Co. LLC

Hey. Good morning, everybody.

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Good morning.

Noah Poponak  
Analyst, Goldman Sachs & Co. LLC

Pat, is it at least in the scenario analysis that you stay in the CEO seat long term rather than it being an interim solution?

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Well, I'll tell you, Noah. My commitment to [ph] Adrianne (00:36:20), my wife and the board was that I would do this for a year, stand up the operations, so that we could put a strong replacement in place. And that remains the commitment and no change at this time.

Noah Poponak  
Analyst, Goldman Sachs & Co. LLC

Okay. Appreciate that. And then just as a follow-up on the aft pressure bulkhead challenge on the MAX, I heard you that you're now shipping conforming clean new off the line. I guess, what about the inventory rework? And just overall, what's the timeframe in which that is behind you completely?
Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

I don't have a timeframe specifically right now in the work that we've been doing. If we had this call in another week, I could probably give you a precise answer. The analysis continues to improve, and so, I can't really tell you what the final work scope is there, but it's trending towards sooner rather than later.

Noah Poponak  
Analyst, Goldman Sachs & Co. LLC

Okay. Fair enough. Thank you.

Mark J. Suchinski  
Senior Vice President & Chief Financial Officer, Spirit AeroSystems Holdings, Inc.

Thanks, Noah.

Operator: Our next question comes from Robert Stallard from Vertical Research. Please go ahead.

Robert Stallard  
Analyst, Vertical Research Partners LLC

Thanks so much. Good morning.

Mark J. Suchinski  
Senior Vice President & Chief Financial Officer, Spirit AeroSystems Holdings, Inc.

Good morning.

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Good morning.

Robert Stallard  
Analyst, Vertical Research Partners LLC

Pat, it's one for you actually. On the Airbus negotiations, I was wondering if you could give us some idea of how this differs versus the discussions you've been having with Boeing. And in conjunction with Airbus, the A220 program didn't take a charge this quarter, so I was wondering if you could give us an update on how that's going.

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Maybe Mark can talk about the charge and I can talk about the negotiation. Do you want to take that first?

Mark J. Suchinski  
Senior Vice President & Chief Financial Officer, Spirit AeroSystems Holdings, Inc.

Sure. Rob, you're right. No forward loss charge in the A220 program. It was a pretty good quarter. I think the team is doing well. We're meeting our delivery commitments to our customer. And so, a pretty quiet quarter on the A220 side.
Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Yeah. Maybe just a comment on the differences or similarities between the Boeing and Airbus negotiations. I'd say they're very similar. The nature – this is really kind of concentrated on the A220. At the end of the day, it's really about the A220. And like my earlier comment about the maturity of the production system and expectations of performance, we're not aligned. And until we can get that alignment, it makes producing at the higher rates more difficult. And I think that we will come to a reasonable outcome because it's important for Airbus, it's important for Spirit, it's important to the airplane. There's strong demand for that airplane. And we're committed to Airbus, and I think they're committed to us. And it's just something here in the short term, but I'm encouraged based on the Boeing agreement that we'll get there with Airbus.

Robert Stallard  
Analyst, Vertical Research Partners LLC

Okay. And just a quick follow-up, Pat. Hard to put a timeframe on this, do you think you'll get this done before February?

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Oh, I think so.

Robert Stallard  
Analyst, Vertical Research Partners LLC

Okay. Thank you very much.

Operator: Our next question comes from Robert Spingarn from Melius Research. Please go ahead.

Scott Mikus  
Analyst, Melius Research LLC

Scott Mikus on for Rob Spingarn. Pat, I did want to ask you, if you pursue a financial remedy on the A220 or A350, is there any concern that Spirit could potentially see a reduced role later on the A220 or A320neo if Airbus re-wings those programs?

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Yeah. That's a – I spend half my time on that question and half my time on the negotiating – not so much negotiating strategy, but the strategy process. And I think with our advanced engineering capability and the things that we do with resin transfer molding, we're a critical part. It's not so much the wing of tomorrow. It's just Airbus' long-term composite supply chain. I think we're a vital piece of that.

The issue we have is just here in the near term, how do we solve this financial disconnect? But I would bet on the team in Belfast to be a critical part of Airbus' future. We just have the overhang of some agreements that go back a long time pre-COVID that we have to kind of work our way through.

But the earlier remark I made about this company and advanced materials, the things that we're doing are really going to be the basis of the next generation of product out there on – in the defense world and commercially.
because we can do it at scale and we get reps every single day. And to go replicate some of these assets in a greenfield at scale is cost-prohibitive.

So I think it's just – you get trapped in these situations of managing quarter to quarter or that somebody should get better performance than they're actually realizing and I think just like with the Boeing agreement, we're going to get to a place that makes sense for both parties.

Scott Mikus  
Analyst, Melius Research LLC

Thanks. I'll just stick to one.

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Thank you.

Operator: Our next question comes from Cai von Rumohr from TD Cowen. Please go ahead.

Cai von Rumohr  
Analyst, TD Cowen

Yes. Thanks so much. And, Pat, welcome.

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Thank you.

Cai von Rumohr  
Analyst, TD Cowen

And so, the Boeing MOA basically – you basically get some – have to take a lower price on the 737 as you get out to 2026, and you get a much higher price on the 787 near-term. But then around the middle of 2008, you have the renegotiation of the price on the Boeing 787. And as I read, what I've read of the MOA, it looks like, basically, barring any change in the negotiation that the 787 price at that point goes back to where it currently is or relatively close? Is that your read? Or so how – should I be concerned that that's a real liability or as you get out there that the 787 could revert to going back into a modest – basically breakeven or a loss?

Mark J. Suchinski  
Senior Vice President & Chief Financial Officer, Spirit AeroSystems Holdings, Inc.

Hey, Cai. It's Mark. Let me jump in there. I would say that we came to a good conclusion on the appropriate pricing on the 787 program, essentially out through the order book. We have a commitment between the two parties to negotiate a fair and reasonable price beyond 1605 one year in advance of that delivery date. And just like we came to an appropriate conclusion, which allows Spirit to make an appropriate margin on that airplane program here shortly, that's what our expectations will be long term.

Cai von Rumohr  
Analyst, TD Cowen
Okay. And if I may, one more on the Airbus talks. Clearly, it's going to be difficult to do a refi unless that is behind you. Does that – do you feel that puts increased pressure on you to kind of come to the table more quickly or how do you deal with that timing issue of having to get that done before a refi?

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Cai, I don't think we're in a position where we're pressured to negotiate. Mark, you might comment just on the financial situation, but I think we have time to get it right, but there's no point in wasting time.

Mark J. Suchinski  
Senior Vice President & Chief Financial Officer, Spirit AeroSystems Holdings, Inc.

No. I agree with Pat. I'd just say this, Cai. I think the Boeing MOA provides a nice boost to liquidity here over the next several years. And I think we have some momentum here on that front. And so, again, when it comes to the refinancing, we're going to do what's best for us, for our company, and for our shareholders, and work through that accordingly. And as Pat said, no pressure on the Airbus side. That will happen in its due course.

Cai von Rumohr  
Analyst, TD Cowen

Thank you very much.

Operator: Our next question comes from Gavin Parsons at UBS. Please go ahead.

Gavin Parsons  
Analyst, UBS Securities LLC

Thanks. Good morning.

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Good morning.

Mark J. Suchinski  
Senior Vice President & Chief Financial Officer, Spirit AeroSystems Holdings, Inc.

Morning.

Gavin Parsons  
Analyst, UBS Securities LLC

Pat, you suggested you'll be delivering, I think, around 37 to 42 a month in the fourth quarter. Just to clarify, is your plan still that you'll be cycling and delivering at 42 starting in 2024 or is there a spread? And then could you update us on the current MAX inventory buffer?

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Let's see. No guidance on 2024. And in terms of the buffer, I don't have...
Mark J. Suchinski  
Senior Vice President & Chief Financial Officer, Spirit AeroSystems Holdings, Inc.

I've got that, Pat.

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

We've got, as you know, a mix of units in there.

Mark J. Suchinski  
Senior Vice President & Chief Financial Officer, Spirit AeroSystems Holdings, Inc.

Yeah. So we – Gavin, we have about 80 units in buffer. We’d like to categorize them in two component, units that are on hold and then units that are available to ship. So there’s around 50 units that have – that are in Boeing’s – in the buffer. Boeing owns title to those, and Boeing can pull them whenever they’re ready to pull. So buffer has increased a bit. At the end of the second quarter, it was low as we prepared for the work stoppage issue. But we’ve been able to build up that buffer to a certain degree. And as Pat said, the goal here is, as we move forward here, to sync up our production schedules. But that's an update on the buffer.

Gavin Parsons  
Analyst, UBS Securities LLC

Okay. Thank you.

Operator: Our next question comes from Peter Arment from Baird. Please go ahead.

Peter J. Arment  
Analyst, Robert W. Baird & Co., Inc.

Yeah. And good morning, Pat and Mark. Hey, the...

Patrick M. Shanahan  
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Good morning.

Peter J. Arment  
Analyst, Robert W. Baird & Co., Inc.

...the $100 million you're getting for tooling-related equipment for the 737 and 787, can you kind of give us a little more color of what the real benefit is there? Obviously, it's nice to see the cash infusion. But you've – Pat, you said, you've been at these higher rates before. So, what is actually the benefit that you're seeing here? Thanks.

Mark J. Suchinski  
Senior Vice President & Chief Financial Officer, Spirit AeroSystems Holdings, Inc.

Yeah. Sure, Peter. A couple of things. Number one, with most OEMs, if you have production rate increases or model mix or new derivatives, the OEMs always own the tooling, right? And so, that's unchanged from our previous agreements. But in this current environment, when we look at the model mixes and we have the -7s and the -8s, the -9s and the -10s, Boeing is selling more -7s, more -10s, and that has an impact on our production system.
And so, therefore, it's going to require us to make some capital investment. And so, one of the benefits of the agreement – and we appreciate this from Boeing – is they're going to pay for some capital that, normally, Spirit would have to pay and, normally, what would happen is as we built those units, we'd absorb more overhead and that would help profitability, but the big benefit here is that it's a combination of tooling and capital that Boeing is going to pay for. They've given us an advance in the fourth quarter and some funding in 2024 and a little bit in 2025, and that's going to result in us spending a higher CapEx in 2024 and 2025 to reflect the new models and the adjustments we need to make in the production system.

So, there is a benefit to Spirit. It's going to be a little lumpy when the receipts come in and when the funds go out, but we think our Boeing customer, they're making the actual capital investment themselves. And so, we appreciate that. So, really, that's – in a nutshell, it's a nice little benefit. Although it's cash neutral, it is a benefit to Spirit.

Peter J. Arment
Analyst, Robert W. Baird & Co., Inc.

Appreciate the color. Thanks, Mark.

Mark J. Suchinski
Senior Vice President & Chief Financial Officer, Spirit AeroSystems Holdings, Inc.

Sure, thanks.

Operator: Our next question comes from Michael Ciarmoli from Truist. Please go ahead.

Michael Ciarmoli
Analyst, Truist Securities, Inc.

Hey. Good morning, guys. Thanks for taking the question.

Patrick M. Shanahan
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Good morning.

Michael Ciarmoli
Analyst, Truist Securities, Inc.

Pat or Mark – good morning – just on the MOA, can you maybe help us out or give us a little bit more detail? Obviously, you kind of can triangulate where the 787 deliveries are going to be this year. You've got the $60 million revenue increase. Was that all pricing? And should we assume that's kind of roughly $2 million per unit pricing?

And then you kind of said not going to be margin positive for 2025. I guess, the reversal of the amortization looks to be an additive, but I think you're still paying back from the existing MOU, the $450,000. Can you just help us bridge some of those moving pieces so we can get a better expectation on 787?

Patrick M. Shanahan
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Yeah. Sure, Michael. I'm not going to comment specifically on what the price increase is per unit, but I think the – what you should take from the agreement is, we're reversing forward losses, where previously, in the future, our
cost was higher than our price. So when you reduce a forward loss, right, and the cost – our cost forecast is unchanged, it's a pricing benefit. So those losses or those cash losses that we would book in the future, we're reversing those because those no longer exist.

And then, when we talk about when we get to positive margins on that program, we're at 4% or 5% a month and moving to 7% a month. So, it's going to take us a little time to absorb some of that overhead and get the full benefits of the pricing agreement. And so, when we look at the early part of 2025, we're going to be at a higher rate than we are right now. And based on the price that we're getting paid per unit and what our cost projections are, we talked about being positive margins, and we expect that to be a benefit on an ongoing basis.

So, again, I don't want to get into the specifics about how much we got paid, but it's a big, big deal to Spirit. We're at the point now where we were in a loss position since, essentially, the inception of the program. And here, in short order, our cash and the – the revenue will be higher than our cost, and it'll be a cash positive program for us. And so, a good thing for us as that program starts to go up in rate here over the next 12 months to 18 months.

Michael Ciaramoli
Analyst, Truist Securities, Inc.

Got it. I'll keep it to one. Thanks, guys.

Patrick M. Shanahan
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Thank you.

Operator: Our last question today comes from Kristine Liwag from Morgan Stanley. Please go ahead.

Kristine Tan Liwag
Analyst, Morgan Stanley & Co. LLC

Hey, Pat and Mark. The MOA with Boeing clearly signaled to Spirit equity and bondholders their strategic importance to Boeing. That said, operations continue to get worse with the forward losses and the negative cumulative catch-ups even in Defense. So, from your conversations with Boeing, to what degree does Boeing's financial support extend and can Boeing step in to explicitly help underwrite the refinancing of the 2025 maturities?

Patrick M. Shanahan
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Hey. Good morning, Kristine. An interesting question. And we do thank our big customer for the agreement that we have in place and we think it's a – they deemed it as a win-win. And I wouldn't view it as charity. I think we perform a great service to our customers. I think we do a great job performing on their programs. And so, overall, they described it as a win-win and we view it as a win-win.

As it relates to refinancing strategies, as I've said before, we have access to the capital markets. We don't need Boeing to underwrite us as we think about our strategies around upcoming maturities, and I would just kind of leave it at that.
Great. And if I could do a follow-up, when we factor in the current inflation environment, the higher labor costs and the pricing step-down for the 737 come 2026, what should margins for the program be for the 737 at that point, and how would that compare to where we were around the 2019 levels?

Patrick M. Shanahan
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Yeah. Hey, Kristine. I'd just say this. Before we jump to 2026, let us get through 2023 and have a good, robust discussion with you in February about 2024. We'll have those discussions in good time.

Kristine Tan Liwag
Analyst, Morgan Stanley & Co. LLC

Great. Thank you.

Patrick M. Shanahan
President, Chief Executive Officer & Director, Spirit AeroSystems Holdings, Inc.

Thank you.

Operator: This concludes today's conference call. Thank you all very much for dialing in and have a wonderful day.