

Transcript of
Materion Corp.
Second Quarter 2024 Earnings Call
August 06, 2024

Participants

Kyle Kelleher – Director, Investor Relations & Corporate FP&A, Materion Corp.
Jugal Vijayvargiya - President and Chief Executive Officer, Materion Corp.
Shelly Chadwick - Vice President and Chief Financial Officer, Materion Corp.

Analysts

Daniel Moore - CJS Securities
Michael Harrison - Seaport Research Partners
David Silver - CL King
Philip Gibbs - KeyBanc Capital Markets
Dave Storms - Stonegate Capital Markets

Presentation

Operator

Greetings. Welcome to the Materion Second Quarter 2024 Earnings Conference Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. [Operator Instructions] Please note this conference is being recorded.

I will now turn the conference over to your host, Kyle Kelleher, Director of Investor Relations and Corporate FP&A. Kyle, you may begin.

Kyle Kelleher - Director of Investor Relations & Corporate FP&A, Materion Corp.

Good morning and thank you for joining us on our second quarter 2024 earnings conference call. This is Kyle Kelleher, Director of Investor Relations and Corporate FP&A. Before we begin our remarks this morning, I would like to point out that we have posted materials on the company's website that we will reference as part of today's review of the quarterly results. You can also access the materials through the download feature on the earnings call webcast link.

With me today is Jugal Vijayvargiya, President and Chief Executive Officer, and Shelly Chadwick, Vice President and Chief Financial Officer. Our format for today's call is as follows. Jugal will provide opening comments on the quarter. Following Jugal, Shelly will review the detailed financial results for the quarter in addition to discussing our expectations for the second half of 2024. We will then open up the call for questions.

Let me remind investors that any forward-looking statements made in the presentation, including those in the outlook section and during the question-and-answer portion, are based on current expectations. The company's actual performance may materially differ from that contemplated

by the forward-looking statements as a result of a variety of factors. Those factors are listed in the earnings press release we issued yesterday afternoon.

Additionally, comments regarding earnings before interest, taxes, depreciation, depletion, and amortization, net income and earnings per share reflect the adjusted GAAP numbers shown in attachments 4 through 8 in yesterday's press release. The adjustments are made in the prior year period for comparative purposes and remove special items, non-cash charges, and certain discrete income tax adjustments.

And now, I'll turn the call over to Jugal for his comments.

Jugal Vijayvargiya - President and Chief Executive Officer, Materion Corp.

Thanks Kyle, and welcome everyone. It's nice to be with you today to discuss our record second quarter performance as well as our outlook for the second half of the year. After a challenging start to the year, I'm pleased to share that Materion is back on track, delivering record results again in the second quarter.

Top line improvements, coming mainly from organic initiatives, combined with our focus on strong operational performance and cost management, led to the highest quarterly EBITDA in the history of our company. I'm especially proud of our team for achieving these strong results while continuing to secure several new business wins and customer partnerships that will seed the pipeline for long-term sustainable growth.

Value-added sales were a second quarter record, up 4% year-over-year, largely driven by strength in aerospace and defense and consumer electronics. In addition to a gradual semiconductor rebound, now starting to flow through to our order books, the operational challenges we faced in the first quarter have largely been mitigated and we're seeing the impact of the targeted cost improvement initiatives enhancing our bottom line, as we outperformed our midterm margin target of 20% for a third time in the last five quarters.

While we're seeing softer demand across select markets, including industrial and automotive, the momentum we're building across other large markets like aerospace and defense, combined with our operational initiatives and targeted cost management, continues to drive strong performance. With new partnerships and business wins in space and defense, we are demonstrating once again the ability of our products and technologies to drive solutions for some of our customers' most demanding technical challenges.

In aerospace and defense, our customers are developing new products and applications that require the highest level of performance reliability in the harshest conditions. The criticality of our materials to these applications is affirmed through rising demand for our products as well as customer investments to secure the supply of these key materials. I am pleased to announce that a leading aerospace and defense customer has agreed to invest approximately \$10 million in new capacity and capabilities at one of our existing sites in support of their growing demand.

The growth of commercial space is driving new opportunities for us, as Materion remains uniquely suited to serve the needs of this expanding market. Our reputation as an innovative and

reliable supplier for highly visible space projects like the James Webb Space Telescope have paved the way for opportunities to support the next generation of applications.

In the second quarter, we secured a \$150 million multiyear agreement to supply critical materials for space propulsion systems. This announcement follows four previously announced orders over the past 18 months, further solidifying our position as a long-term key partner to this important customer.

Defense continues to be a growing market for us, as advances in technology drive new government initiatives and modernization programs around the world. So far this year, we've received approximately \$60 million of new orders in this market, with potential for significant upside in future years as these programs gain traction. The pace of incoming orders for defense is at roughly twice the pace we saw last year.

In the second quarter, semiconductor recovery drove single-digit increases in both sequential and year-over-year comparisons for VA sales, mostly driven by growth in logic and memory applications. Although the pace of recovery for semi is looking to be slower than anticipated, we expect to see growth in the second half as we're seeing a pickup in order rates for the remainder of the year.

As the rebound occurs, we're expanding our capabilities to serve customers who are rapidly innovating advancements in support of rapid digitization and the shift toward artificial intelligence. The expansion of our portfolio to include ALD or atomic layer deposition products is allowing us to support the production of the most sophisticated semiconductor products.

This quarter, we were pleased to receive an overall excellent supplier award from a leading ALD customer. Our team has collaborated with this customer to innovate multiple ALD materials, which will see expansion, the rapid growth of AI, and the increasing demand for the most complex chips.

Another source of meaningful growth for Materion has been the important precision clad strip project that we started in 2020. Together with funding from the customer, we built the new state-of-the-art facility to produce higher volumes of product in support of the global rollout of their next generation product.

Today, we are pleased to be able to share that the customer who invested with us is Philip Morris International. Our precision clad strip is used in PMIs heat not-burn consumables for the IQOS ILUMA, a smoke-free product that heats tobacco instead of burning it. It is an alternative for adult smokers who would otherwise continue to smoke that is gaining popularity in Europe and Japan.

This business win has created a unique avenue to further diversify our portfolio, enabling us to continue to deliver strong performance even as some large markets have experienced softness in recent months. We are proud of our team's ability to work with the customer in support of this application and successfully ramp-up a new production facility to meet the customer's needs.

These many examples demonstrate the power of the Materion strategy, which is grounded in our team's ability to harness our advanced materials expertise to create solutions that enable our customers' breakthrough solutions.

Our focus on our customers' needs across our diverse portfolio is helping us to navigate short-term headwinds across some end markets, while also building our pipeline to ensure long-term organic outgrowth.

With a laser focus on operational excellence and maintaining the benefits of the structural cost improvements we've put in place, we are positioning ourselves for strong earnings growth throughout the balance of the year. While we're taking down the top end of our guidance range to reflect a softer end market environment, we are well positioned to deliver another record year for Materion.

Now, let me turn the call over to Shelly to cover more details on the financials.

Shelly Chadwick - Vice President and Chief Financial Officer, Materion Corp.

Thanks Jugal, and good morning, everyone. During my comments, I will reference the slides posted on our website yesterday afternoon starting on Slide 10. In the second quarter, value-added sales, which exclude the impact of pass-through precious metal costs, were a second quarter record at \$279.8 million, up 4% from prior year.

This increase was driven by continued strength in aerospace and defense, gradual improvement in semiconductor and growth in precision clad strip, which we have now reclassified from other to consumer electronics given today's announcement. This year-over-year increase was slightly offset by weakness in the industrial, automotive and energy end markets. When looking at earnings per share, we delivered record Q2 adjusted earnings of \$1.42, up 3% from prior year.

Moving to Slide 11, Adjusted EBITDA in the quarter was \$57.8 million, or 20.7% of value-added sales, up 4% from the prior year and a record for any quarter. As Jugal commented, we're very pleased to have once again delivered margins above our midterm target of 20%. This year-over-year increase was driven by higher volume, improving operational performance and continued cost management. These drivers help to offset some weaker price mix.

Moving to Slide 12, let me now review second quarter performance by business segment. Starting with Performance Materials, value-added sales were \$173.1 million, up 4% compared to prior year. This year-over-year increase was driven largely by strength in aerospace and defense and consumer electronics, partially offset by weakness in the industrial, automotive and energy end markets.

EBITDA, excluding special items was \$43.1 million, or 24.9% of value-added sales, down 6% compared to the prior year period. This decrease was driven largely by unfavorable price mix, the carry forward impact of the Q1 operational challenges and a lower recorded benefit from the manufacturer's production credit. Continued strong cost management partially offset the decrease.

Moving to the outlook, we expect space and defense to remain strong throughout the balance of 2024, with a slightly weaker outlook across the industrial and automotive end markets and the impact of the previously discussed second half inventory correction for precision clad strip. We also expect strong operational performance as we move past the impact of the Q1 operational challenges.

Next, turning to Electronic Materials on Slide 13, Value-added sales were \$81.1 million, up 5% year-on-year and sequentially driven by the gradual semiconductor market recovery. The energy market remains suppressed with smart glass sales down due to softness in the non-residential construction market. EBITDA, excluding special items was \$17.1 million, or 21.1% of value-added sales in the quarter, delivering the highest margin profile since the second quarter of 2022.

This increase was driven by higher volume and the impact of the cost improvement initiatives, both of which are strong contributors to the 230 basis points of margin expansion year-on-year and 240 basis points sequentially. As we look out to the rest of the year, we expect the semiconductor market recovery to continue, but at a slower pace than previously expected.

Turning to the Precision Optics segment on Slide 14, Value-added sales were \$25.6 million, up 2% compared to the prior year. This increase was driven by market strength in aerospace, life sciences and consumer electronics, slightly offset by some defense order timing. EBITDA, excluding special items was \$2.1 million, or 8.2% of value-added sales.

The decrease year-over-year was largely driven by operational challenges combined with an unfavorable mix. Despite the year-over-year decline, this business saw sequential improvement driven by higher volume and strong cost management. Looking out to the second half of 2024, we expect a step up in margin performance as we improve operational performance and continue to drive targeted cost improvement initiatives across the business.

Moving now to cash, debt and liquidity on Slide 15, we ended the quarter with a net debt position of approximately \$468 million and approximately \$106 million of available capacity on the company's existing credit facility. Our leverage at 2.2x remains just slightly below the midpoint of our target range. We expect to generate strong cash flow in the back half of the year, bringing our leverage below 2 times by year-end.

Lastly, let me transition to Slide 16 and address the full-year outlook. Since the first quarter earnings call, the outlook for semiconductor, automotive and industrial end markets has softened. Despite the lower end market demand, we remain confident in our ability to execute and deliver another year of record results by delivering on our organic initiatives and continuing to drive operational and cost improvements throughout the company.

With the softer end market demand in mind, we are lowering the top end of our guide, revising our range from \$5.60 to \$5.90 for the full-year adjusted earnings per share, an increase of 2% from prior year at the midpoint.

This concludes our prepared remarks. We will now open the line for questions.

Operator

Thank you. At this time, we will be conducting a question-and-answer session. [Operator Instructions] And the first question today is coming from Daniel Moore from CJS Securities. Daniel, your line is live.

Q: Thank you. Good morning, Jugal, good morning, Shelly. I appreciate the color.

Jugal Vijayvargiya - President and Chief Executive Officer, Materion Corp.

Good morning, Dan.

Shelly Chadwick - Vice President and Chief Financial Officer, Materion Corp.

Morning.

Q: Maybe just give you the opportunity to kind of elaborate on what you're seeing in the marketplace looking at the balance of the year. Just talk about any more color on the recovery and semi slightly slower than expected, not a surprise given what we've seen there. But any meaningful change in the outlook for, kind of, memory versus logic and where you're seeing that recovery maybe push out to the right a bit?

Jugal Vijayvargiya - President and Chief Executive Officer, Materion Corp.

Yeah. Dan, the markets have certainly been choppy as you know. We talked about the semi business in our last call, and we indicated that, we expected that Q1 to be the low point with some recovery into Q2 and then a little bit more incremental in Q3 and then a little bit more of a step up in Q4.

I would say the general trend is still there, and that's what we are seeing with our order rates. Clearly, it's led by the logic and memory devices, and we're hearing about it from all the semi customers, as well as, I think, just in the marketplace. But I would say the pace of recovery is probably a bit muted from the time that we spoke one quarter ago. So, we still expect the recovery just a bit less, I think, and going into Q3 and Q4. And that's how we've sort of revised our thinking and the guide change from the top end that we made.

When you look at the other markets, industrial continues to be challenged. Housing starts, non-res constructions continued to be challenged. So, the recovery on industrial, I would say, is a bit slower than what we had anticipated. Automotive production has been revised. In fact, if you look at the latest IHS data, it indicates about a 2% down from the beginning of the year.

Europe is expected to be, and we have a lot of business with European automakers, expected to be down 6% now year-over-year versus the 2% that I think it was at the beginning of the year. The rig count continues to be challenged, in fact less than 800 is the number for the rig count. It continues to be challenged there.

What's exciting for us is, I think, the number of new initiatives our team has been able to drive to help offset many of these choppy conditions, and I would say really tough conditions in some of the markets. When you look at the work our team has done on space, the number of initiatives that they've been able to do.

We announced today, as you know a large order for that, the number of initiatives on the defense side, the opportunities and organic opportunities there and then even in the other markets, the number of organic initiatives that I think our teams have continued to drive to help offset, I mean, delivering a 4% year-over-year growth here in Q2.

And then I would expect that we would continue to have growth going into Q3 and Q4 on a combined company basis. So certainly, a choppy situation right now I think in the markets, but very pleased with the level of effort and results our team is doing on a number of fronts organically to help offset.

Q: Helpful. I missed the first couple minutes of prepared remarks, so I apologize. But I'm wondering if you could give a little bit more detail on the new precision clad strip project, could that lead to more additional customer opportunities, maybe size, the scale of sort of the opportunity set? And what, if any capex might be needed to set up a facility? It sounds like you'd be setting up a dedicated facility, if I'm not mistaken. So, any color on that new opportunity would be really interesting and helpful.

Jugal Vijayvargiya - President and Chief Executive Officer, Materion Corp.

Yeah. So, on precision clad, I mean, as we have spoken over many quarters now, we have been in the precision clad business for a number of years. We've supported various markets. I go back to the 2020 timeframe when we announced that we had a customer that wanted to work with us to buy a lot more of the precision clad than what we were capacitated to do.

We worked with the customer to put a facility in place. And that facility, today we're mentioning is in Reading, Pennsylvania area, Leesport, Pennsylvania. We put that facility in place in combination with the customer as they invested roughly about \$120 million to help fund that facility.

We're very pleased to work with them and I think it's been a fantastic relationship. And today we announced that that customer is Philip Morris International, who is using our product in their IQOS ILUMA product. So, I would ask you and, of course, others to look at that information. It's a product that's gaining popularity in Europe and Japan and they continue to do a global rollout.

Now, with that said, we are always working on this particular product segment and trying to gain more customers in the automotive segment and consumer electronics, clean energy, and others. So, we have a number of new initiatives that we continue to work on precision clad, I mean, we're one of very few, I would say, really capable precision clad strip suppliers in the world.

So we continue to do that and we will. We will continue to pursue other customers. And if additional capacity is needed, we'll put additional capacity in either in the Leesport facility, which is the new facility, or our existing facility, where we were – where we have been doing precision clad for many years prior to this new project that's come on board.

Q: Excellent. Look forward to hearing more. And lastly, maybe just Shelly, with two quarters remaining, I appreciate the update and guide. Any sense of the cadence of revised profitability

guidance, Q1 historically is your strongest quarter. Is that how you see this year shaping up as well?

Shelly Chadwick - Vice President and Chief Financial Officer, Materion Corp.

Yeah. That is how we see it. We expect that Q3, from a profitability perspective, is probably going to look a lot like Q3 of last year. We do expect some of the markets where we've seen some inventory correction to start to come back. Jugal mentioned the non-res construction, we think that sprinkler business will start to see some orders there in Q3. Automotive, we've seen maybe an over correction there. We expect that business to start to come back in the back half.

So, we'll move past the impact of the operational challenges we saw in Q1 starting in Q3. And we do expect the volumes to be up even higher in Q4. So, you will see the strongest quarter of the year being Q4 and really by a meaningful step with the combination of kind of the higher volume, the better operational performance, and then that normal sort of seasonality we sometimes see with markets like defense.

Q: Really helpful. I'll jump back with any follow ups. Thank you.

Shelly Chadwick - Vice President and Chief Financial Officer, Materion Corp.

Thanks, Dan.

Operator

Thank you. The next question is coming from Mike Harrison from Seaport Research Partners. Mike, your line is live.

Q: Hi. Good morning.

Shelly Chadwick - Vice President and Chief Financial Officer, Materion Corp.

Hi, Mike.

Jugal Vijayvargiya - President and Chief Executive Officer, Materion Corp.

Hello Mike.

Q: I was hoping that we could talk a little bit more about the operational issues that impacted Q1 and it sounds like maybe there was still some lingering impact in both Performance Materials and Precision Optics in the second quarter. Any help you can provide on quantifying the impact of those two segments in Q2 would be appreciated. And then, I guess, I just want to understand, do you guys feel like those operational issues are completely resolved in both segments at this point, or could there be some further headwinds as we look into the second half?

Shelly Chadwick - Vice President and Chief Financial Officer, Materion Corp.

Yeah. I'll start with that one, Mike. So, in Performance Materials is where we saw the main operational issues. And as you know, a much – a big part of that business is vertically integrated and sort of see operational challenges work through that system takes a little bit of time. We are seeing marked improvement there. So, I don't think we have concerns over the operations in

Performance Materials, where you see some of that impact still coming through in Q2, it's really normal amortization of variances.

On the Optics side, we did see some continued operational challenge in Q2, but the team thinks they've really got that figured out and expect better performance in Q3 and for the back half of the year.

Q: All right. And then just in terms of the Philip Morris application, any further update on their rollout plans and how their inventory management is going to impact volumes and also the Phase 2 startup in the second half? Just trying to get a better sense of how we should think about the volume and the earnings headwind from PMI in the Performance Materials segment as we're comparing the second half to what you guys did last year?

Jugal Vijayvargiya - President and Chief Executive Officer, Materion Corp.

Yeah. So, Mike, as we indicated, I think in the last call, that second half of the year, we expected inventory correction based on the management – inventory management things that the customer is going through. And I would say it's in line with what we reviewed last time. So really, no change from our assumptions on that inventory correction on management in the back half of the year. Yeah, same as our commentary, I think, from a quarter ago.

As we look at our Phase 2, of course, we've been working on Phase 2, and our team has done a tremendous job of getting – continuing to make progress on getting the equipment qualified. We've indicated that that equipment would be ready, really at the beginning of the year, and we would expect to start using it and start to ramp that into the '25 timeframe. Of course, we will work with the customer on the level of volumes that they expect.

So, it's one thing to, of course, have the capacity for Phase 1 and Phase 2, and at the point that we can do that. And then in terms of the actual orders and deliveries, those, we will just continue to work with the customer on what level of inventory correction do they want to continue to work through, or new orders that they want to place? What level of new orders that they want to place, and I would expect that to continue to then get ramped over time.

So, I think we're very well positioned to be able to support the customer as they continue to move forward on the global rollout and we'll just – just like we have I mean, we'll follow the lead under order patterns and requirements that they have as we get closer to the end of this year and have a better understanding of the requirements for next year.

Q: All right. Thank you for that. And then on Electronic Materials, that gross margin number has moved around a little bit in the past several quarters, kind of anywhere from the mid-20s to mid-30s. Q2 was 33.5%, and as you noted, kind of a higher watermark for overall EBITDA margin for that segment. Do you see that 33% or 34% gross margin level at the sustainable level that maybe you can build on as volumes recover? Or should we think about maybe some mix factors or any other factors that could maybe lead gross margin to be a little bit softer in Electronic Materials over time?

Shelly Chadwick - Vice President and Chief Financial Officer, Materion Corp.

Yeah. No, great question. And we're really proud of the work that the team has done in Electronic Materials to kind of right size their cost structure, while they've had some softer volumes. It's given them a chance to really focus on operations and make sure that we've got the right organizational setup there.

That really has helped prop up growth margins as we kind of moved through the downturn, and now we're starting to see things pick back up slightly. There is a mixed impact within EM based on their product mix or whatnot. But we do think that the progress we've seen should be sustainable as the volumes start to come back, and that that'll be great for bottom line margins going forward.

Q: All right, very helpful. Thanks very much.

Shelly Chadwick - Vice President and Chief Financial Officer, Materion Corp.

You're welcome.

Jugal Vijayvargiva - President and Chief Executive Officer, Materion Corp.

Thanks, Mike.

Operator

Thank you. [Operator Instructions] The next question is coming from David Silver from CL King. David, your line is live.

Q: Yeah. Hi. Good morning. Thank you.

Jugal Vijayvargiva - President and Chief Executive Officer, Materion Corp.

Good morning, David.

Shelly Chadwick - Vice President and Chief Financial Officer, Materion Corp.

Good morning.

Q: Good morning. Happy Tuesday. I'm going to preface my remarks by stipulating I've been jumping around amongst three calls, so my apologies if I'm making you repeat yourself.

The first place I'd like to start would be with the new \$150 million contract for critical materials for space propulsion. I've been following your company for a few years, and I really don't recall a new piece of business of that scale. So, correct me if I'm wrong or whatnot, but how long has it been since there was an order of that size that you've disclosed?

Jugal Vijayvargiva - President and Chief Executive Officer, Materion Corp.

Yeah, I think, David, first of all, I'm very pleased with the work that the team has done. This is our 5th order actually with this customer. We've announced four orders with this customer, more of, I would say, smaller chunks of orders. This order here is a multiyear contract now.

What we had been announcing is almost, in a way you could say, almost kind of like spot orders, where we get an order for one or two quarters and we supply. This gives us, I think, a multiyear long-term sustainable revenue stream with the customer and we're very, very pleased with that.

When you put the other four orders that we have announced along with this one, it's in the neighborhood of around \$220 million of business between the last 18 months and then, of course, the go forward \$150 million contract that we announced today. Very pleased with that, I think the work our team has done.

With regard to the size of the orders, obviously, you know about the precision clad program, which today we announced that the PMI international program and that, of course, has been a very large, meaningful business for us, and we're very, very pleased with how that turned out.

But in addition to that, certainly the space contract is one that is a very meaningful program for us. So, these types of businesses for us, I think we're doing everything we can to make sure that we're getting larger, more sustainable type of contracts, so we can be – have a little more surety in our revenue stream, and I hope that we can continue to do that.

Q: Okay. And then maybe just a quick follow up on that, but. Should I assume that this large order compared to, I think, you said, the four other smaller ones, is it essentially the same, in other words, they're asking for maybe more material or they're willing to commit for a longer period, but your role or the company's role hasn't really changed much? Or is this – does this represent maybe, I don't know, an evolution where the current contract encompasses some additional, I don't know, either cross selling or bundling or technology included? So, first order to the fifth order, is there kind of a development or an evolution in your role there, or is it – should I think of it as just a larger version of the previous four orders?

Jugal Vijayvargiya - President and Chief Executive Officer, Materion Corp.

Yeah. Well, first of all, I mean, we've been a great, I think, partner, I hope, with this customer and the customer, I think, has confidence in us, and that's why they're reaching out and wanting to work with us now on a multiyear program.

It is essentially, like you said, the same product that we've been supplying in the prior four orders, it's a matter of just really cementing our relationship with them on a more longer-term basis, so that we're not looking at on a more spot order, order by order type of a situation.

It allows us to do, of course, much better planning, make sure we have the right capacity, the capability, workforce, and then continue to drive improvements, operational improvements, efficiency improvements, so that we're able to provide them with better product and better value, frankly, over time. So, I think this is just, again, a great testament to the relationship that our teams have developed with the customer.

Q: Got it. Thank you for that. I'd like to switch over to Electronic Materials for one or two. But I was happy to see that despite the, as you put it, a slower than anticipated pace of recovery in that area, the revenues grew both year-over-year and sequentially, as did the operating income and

there's been a lot of margin improvement over that time as well. I'm thinking about your expansion projects that are underway at Newton and Milwaukee.

Has the timing of when those projects would be completed and/or startup, has the timing of that changed with the change in your thinking about the pace of recovery, end market recovery in that area? Or is it the case where the customers that you had envisioned to be the major off takers for that new capacity? Are they lined up or should we push back maybe the startup or the initial contribution from those investments a little bit further to the right, I guess, as someone else said?

Jugal Vijayvargiva - President and Chief Executive Officer, Materion Corp.

Yeah. No, I think in general, as we've talked about in earlier quarters, those projects I think are on track, and in fact, as we had indicated in earlier discussions, the bit of a slowdown in the semiconductor market actually gave us an opportunity to put those projects in place in a more efficient and more meaningful way.

As you know, when the market was at its peak, I mean, we hardly had a time to get other things done. And so, I think it's allowed us to put those projects in place. I would say, by and large, I mean, the projects are on track. I think as the market recovers, which we've had kind of indicated perhaps a little bit more of a recovery in Q4 and then into '25, I think we'll be well positioned to take advantage of those projects.

In Milwaukee, as you highlighted, we mentioned it in the call earlier today, but I'm very pleased with the supplier award recognition from a leading ALD customer, which is exactly the type of capacity that that new facility is having. So, I think as ALD continues to grow, we are well positioned to be able to do that. And the fact that our team has developed this great relationship to receive this award is again, a testament of the work.

And when you look at our Newton facility and the additional projects that we have going on there, that really serves the logic and memory market, it's the main market of that area serves for the semiconductor side, and that area is the one that has started the recovery. So, we would expect that the recovery to continue and then into '25, so that the projects we have would be adding value to that ramp up.

Q: Okay. Great. Maybe just a question for Shelly, I guess, on capital expenditures. But, when I looked at the relevant slide in the deck here, and I'm sorry, I'm fiddling with it here. I think it might be 16, sorry.

Shelly Chadwick - Vice President and Chief Financial Officer, Materion Corp.

Yeah. The guide.

Q: But I was just wondering, yeah, has the total CapEx spend moved down a little bit in the last 90 days or so? And if so, or if there's been shifts in the emphasis there, what has changed, I guess, in your CapEx projections for the current year? And I guess that feeds in a little bit to what I was asking Jugal about maybe the timing of the Electronic Materials programs.

Shelly Chadwick - Vice President and Chief Financial Officer, Materion Corp.

Yeah, good question. So it is down a little bit, but I would say it's probably two different factors. I mean, one, of course, as the CFO, I'm very focused on cash generation and making sure that we're being prudent with our debt paydown while we're investing for growth.

So, we have not delayed any growth-related projects. The other side of that is a specific piece that we're working on in Performance Materials, which you used to see on this page, extrusion press, that's just been pushed out a quarter or two while we're doing more engineering to get ready for that. So that's another piece of kind of the tick down.

Q: Okay, very good. Thank you for that. And I guess the last question would be one about, I guess, the Q1 to Q2 margin progression. I mean, to me that was one of the more eye-catching developments, I guess, in your quarterly release. And I'm just wondering if, in addressing the issues that led to the inefficiencies in the first quarter, first of all, congratulations for kind of addressing that so quickly. But I'm just wondering, I mean, have your thoughts about the target level 20%, I guess, was your intermediate level you've exceeded that a few times now. I mean, should we be thinking that there's going to be some upside to that midterm target that you seem to have reached ahead of schedule?

Jugal Vijayvargiya - President and Chief Executive Officer, Materion Corp.

Well, first of all, thanks for recognizing that and we'll definitely pass that on to the team for, I think, the great work that they did in the first quarter to kind of help recover and then get us back on track here in the second quarter with record results, the highest EBITDA level of any quarter that we've had. So, we'll definitely pass that on. This is the third quarter in the last five, where we have been north of 20% EBITDA margins.

We've also highlighted in our remarks that, we expect the back half of this year to be north of 20% EBITDA margins. And then I think where we go, David, in '25, we'll obviously be talking about that later this year and early in the next year, but our goal is the same. We want to make sure that we can, on a sustainable basis, deliver north of 20% EBITDA margins. If certainly we can do more, then we'll definitely be talking about that.

Q: Okay, great. And I forgot to add that you're accomplishing this in a less than robust demand environment, as you've articulated. And that's it for me. I apologize for the scattershot nature of the questions. I'm just happy I asked the right question to the right company jumping around on too many calls this morning. Thanks very much.

Jugal Vijayvargiya - President and Chief Executive Officer, Materion Corp.

Thanks, David.

Shelly Chadwick - Vice President and Chief Financial Officer, Materion Corp.

Thanks, David.

Q: I appreciate it.

Operator

Thank you. The next question will be from Phil Gibbs from KeyBank Capital Markets. Phil, your line is live.

Q: Hey, good morning.

Jugal Vijayvargiya - President and Chief Executive Officer, Materion Corp.

Good morning, Phil.

Shelly Chadwick - Vice President and Chief Financial Officer, Materion Corp.

Hi, Phil.

Q: Noticed in your slide deck, you had some nice incremental business wins within propulsion and then also just generally defense. Are those orders expected to, to ship over the next 6 to 18 months? And how should we think about that? I wouldn't think you'd be able to cater to all those in the back half.

Jugal Vijayvargiya - President and Chief Executive Officer, Materion Corp.

Yeah. No, they're clearly not all in the back half right. So let me start with the roughly \$60 million of orders that we have had on defense. First of all, by the way, I just want to highlight what a wonderful job our team has done in terms of securing these orders.

A couple of things that I think that are important; one is, we're starting to have more and more of our defense orders from outside the US, so global, I think that's been a very important part of the work that our team has been doing. So a sizable portion of that \$60 million is actually outside.

The second is that this is \$60 million for the first two quarters of the year. All of last year, we had \$60 million of new defense orders. So, we're roughly on pace to be about two times the value of defense orders this year than what we secured last year. So, the team has done certainly a very nice job of that.

We would expect those to ship a bit of it here in the back half of this year, but then really into '25. And, typically, as you know, Phil, defense orders do tend to be in the one-to-two-year timeframe. So, we would expect that to happen. With regard to the space and the propulsion orders that we also indicated that this is our 5th order from this customer. So, the first four were these spot orders, but now this is a multiyear contract that we have.

So, this is a two, three, four-year type of a multiyear type of a contract and so, we would expect – right now, let me back up, right now we're, I'm going to say, still finishing up, delivering to the, to the orders that we had already. We're finishing those up. And this new award will go into effect once we finish delivering the last, the fourth contract that we had. Once we finish delivering that, this will go into effect and then it'll last on a multi-year basis.

Q: Thank you. And then generically on your backlog, can you give us an idea about how your overall backlog looks right now relative to the end of '23 or end of first quarter? Just so, we've got an idea of the visibility that you may have.

Jugal Vijayvargiya - President and Chief Executive Officer, Materion Corp.

Yeah. So, look, I mean, the backlog is kind of a mixed bag, as you can imagine, right? I mean, there are certain markets where the backlog is improving. I mean, we indicated, for example, on semi, our backlog is improving, because we are starting to see a bit more of an order pattern. You know, on semi, as you can imagine on space and defense, our backlog is improving.

But there are certain areas, like automotive and industrial and a couple of very challenged areas where our backlog is certainly a bit more challenging. So, it's a mixed bag of where we've got some areas where the backlog is improving quite a bit and unfortunately, other areas where it's not.

I would say on an overall basis, the backlog at a Materion level is moving in the right direction. So incremental moves from quarter to quarter. And I hope we can continue that into Q3 and then more of a larger step move in Q4 as that is a, particularly in the semi market and then beryllium nickel for industrial market, et cetera that we would expect a much more of a pickup on the backlog in the fourth quarter.

Q: Thank you. And then lastly, for me, I think the slide deck also talked about a focus on cash generation in the back half of the year. The first half carried a bit more cash than we thought, you know, three, six months ago.

Let's just say for networking capital, I know you've got a focus to let some inventory bleed down or normalize a bit as you ship on some of these projects. Is that still the case as of right now? And how should we be thinking about cash generation and net working capital in the back half and whatever you're going to say next, what gets you there? Thank you.

Shelly Chadwick - Vice President and Chief Financial Officer, Materion Corp.

Sure. So, we didn't end Q2 with the cash generation that we were looking for, and a lot of it was timing. We do have some plans to reduce inventory that are well underway, but they're being a little bit offset by some build that we have both for the space business and also clad. So, we're managing that from a timing perspective.

Same with accounts payable. If you think about controlling costs and bringing costs in and trying to manage inventory that way, it's bringing down our APU a little bit as well, which is a good guy. So, as we look out at the back half of the year, stronger earnings is certainly a help, but we expect those working capital numbers to get in line as well. So, to be able to bring down the debt to under 2 times where we think it should be at this point.

Q: Thank you.

Jugal Vijayvargiya - President and Chief Executive Officer, Materion Corp.

Thanks, Phil.

Operator

Thank you. The next question will be from Dave Storms from Stonegate. Dave, your line is live.

Q: Good morning.

Shelly Chadwick - Vice President and Chief Financial Officer, Materion Corp.

Good morning.

Jugal Vijayvargiya - President and Chief Executive Officer, Materion Corp.

Good morning, Dave.

Q: You just on the call, in the slides, you mentioned or highlighted how cost management has been a driver of the margin growth. Just curious as to how much more headroom you see here, how many more levers you have to continue having cost management be beneficial to margin expansion?

Shelly Chadwick - Vice President and Chief Financial Officer, Materion Corp.

Yeah, I'll start, and if Jugal has anything to add, he can pipe in. But I think that if we think about where we've been, we started out with some very targeted cost actions, sort of waiting to see what the markets would do, in semiconductors, in EM, Electronic Materials specifically, I think we got a little bit more holistic saying, really where do we have opportunities to improve the cost structure in this business. And so, I would say those were a bit more fulsome action. And now I would say we're kind of back to that targeted level.

There's work going on in Optics, I think we mentioned that as well. But they certainly will become more selective, as we don't – we're focused on growing the business, right. That takes investment. So, I would say we've done the lion share of what there is to do. It would be selective from here, but there'll also be investments as we look towards what's coming in the future.

Q: Very helpful. Thank you. And apologies if I missed this, has there been any more clarity on the production tax credit?

Shelly Chadwick - Vice President and Chief Financial Officer, Materion Corp.

Yeah. No, great question. Not really. We expect that there will be final guidance still this year, and there are whispers here and there of what might or might not be included. As we've said before, we think we've taken a very middle of the road approach in what we are accruing for a benefit. It's a little bit less than what we were accruing in the first half of last year, but I would say there's equal amounts, upside and downside, based on where that final guide lands. So, we look forward to hearing that sometime in the back half.

Q: Very helpful. Thank you. And then just one more for me. I know you mentioned debt pay down as part of one of your uses for the expected increase in cash flows. I'm just curious, are you seeing anything in the M&A market that piques your interest, where you think values are, just with the flow of cash expected? Just anything along that line?

Jugal Vijayvargiya - President and Chief Executive Officer, Materion Corp.

Yeah. Clearly, as we've indicated before, I mean, we're always looking at opportunities, right. I mean, our door's sort of always open, but we're very, very critical in the way we look at things.

We want to make sure that it's the right fit. We don't want to do M&A just for the sake of doing M&A. We want to make sure that it's got the right culture fit, it aligns with our mega trends, our portfolio that we have and that we can really drive significant value as we doing that.

So, we are continuously looking at that and evaluating opportunities. And certainly, if there is an opportunity for us to move forward, then we would. Even at today's levels, we have the capacity to be able to do it, but certainly we're going to continue to improve our cash position, not only for M&A, but as we've highlighted, we want to continue to make sure that we're driving organic investments. So, we'll keep doing that.

Q: Very helpful. Thank you, very much and good luck in 3Q.

Shelly Chadwick - Vice President and Chief Financial Officer, Materion Corp.

Thank you.

Jugal Vijayvargiya - President and Chief Executive Officer, Materion Corp.

Thank you.

Operator

Thank you. There were no other questions at this time. I would now like to hand the call back to Kyle Kelleher for closing remarks.

Kyle Kelleher - Director of Investor Relations & Corporate FP&A, Materion Corp.

Thank you. This concludes our second quarter 2024 earnings call. Recorded playback of this call will be available on the company's website, materion.com. I'd like to thank you for participating on this call and your interest in Materion. I will be available for any follow-up questions. My number is 216-383-4931. Thank you again.

Operator

Thank you. This concludes today's conference, and you may disconnect your lines at this time. Thank you for your participation.