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# The Boeing Co. (BA)

**Morgan Stanley Laguna Conference** 

## CORPORATE PARTICIPANTS

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

### OTHER PARTICIPANTS

**Kristine Tan Liwag** 

Analyst, Morgan Stanley & Co. LLC

## MANAGEMENT DISCUSSION SECTION

### Kristine Tan Liwag

Analyst, Morgan Stanley & Co. LLC

Great. Good morning, everyone. I'm Kristine Liwag, Head of Aerospace Defense Research at Morgan Stanley. Thank you for joining our next panel. We have Boeing with CFO, Brian West. Brian, welcome.

#### Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

Thank you. Good to be here.

### Kristine Tan Liwag

Analyst, Morgan Stanley & Co. LLC

Great. And I'll start with our disclosures. For important disclosures, please see the Morgan Stanley Research Disclosure website at www.morganstanley.com/researchdisclosures. If you have any questions, please reach out to your Morgan Stanley representative.

So, with that, Brian, thank you for joining us here at lovely Laguna.

#### Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

Great to be here. Thanks for having us.

## QUESTION AND ANSWER SECTION

#### **Kristine Tan Liwag**

Analyst, Morgan Stanley & Co. LLC

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So maybe starting off with some questions, you've had some recent successes with the 787 and the Starliner. How would you characterize where the company is in its turnaround?

#### Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

Yeah. So with the turnaround, make no mistake about it, some things are going well and some things are in front of us. We feel pretty good about some things that have gone in our favor. Good momentum, starts off with the 737 MAX. It's – can't forget about where we were and where we are - that airplane at over 99% reliability is performing very well, awesome in fact.

You mentioned Starliner, so very proud that that mission was accomplished. Proud of that team. 787, in August, we were given permission to begin delivery again and we started those deliveries. So that was a big one. And then in the second quarter, we did generate operating cash flow. So all that is just nice momentum and that's important sequentially. Now, we're not done and turnarounds don't go from – up into the right. We have some things that we're working to mitigate risk around. Top of that list is the 737 and 787 inventory liquidation. That's critical to our working capital and cash trajectory. The supply chain constraints, which I'm sure everyone's heard a lot about, they're very real, they're persistent and we're dealing with them.

And the next one is around our defense fixed-price development contracts, which because of those supply chain constraints, volatility, in addition to inflation, in addition to labor availability, they're pressured and they're going to get knocked around. So we got to keep our eye on that for sure. The -7, -10, 777X certification, so certifications for our commercial airplane lineup, that's very important to get done.

And then finally, China return to service. So we've got some things that are behind us and feel good and there's things in front of us. So if I were to call out one bright spot, it would be demand. So, overall demand pretty robust. It's holding up. It's resilient. And that's good for our customers. That's good for our industry. And we see that continuing. So this is not a demand question. This is much more of a supply.

#### **Kristine Tan Liwag**

Analyst, Morgan Stanley & Co. LLC

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Thanks. And actually looking at the room today, we have a fairly full room. Laguna this year we've got record attendees from both management and investors. And that was inconceivable two years ago that we would have a conference like this back in person, really largely no masks. So that really show – and most of us probably flew in here, statistically 50% on the 737.

#### Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

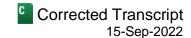
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I hope business class.

**Kristine Tan Liwag** 

Analyst, Morgan Stanley & Co. LLC

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And so, with that, you mentioned demand. We're seeing also firsthand people are here, but what are you hearing from your airline customers, because we are facing some macro uncertainty and so – but at the same time, availability of aircraft is pretty tight. So when you talk to the incremental order, are they looking at placing new airplane orders or potentially deferring...

Brian J. West Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.	A
Yeah.	
Kristine Tan Liwag  Analyst, Morgan Stanley & Co. LLC	Q
some? How do they balance these two things?	
Brian J. West Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.	A
Not deferring. See no sign of that.	
Kristine Tan Liwag  Analyst, Morgan Stanley & Co. LLC	Q
Or cancellation?	
Brian J. West	Δ
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So – yeah, so, no. In fact, because of the demand that I mentioned, the bright spot, they want to take airplanes and I am doing our very best to get them as fast as I can. But as I mentioned, we're supply constrained in some regard. No, there's not deferral. On the – your broader question around the economic backdrop and slowdown, recessionary environment, in general, historically if you look at traffic compared to economic pullback, economy might pull back a little bit, traffic will pull back little, then it'll reset and that's happened before. What's unique is where traffic is right now. So traffic is – passenger traffic is 75% what it was in 2019, about mid-80s for domestic and high-60s for international. So that – closing that gap is still a pretty big opportunity regardless of whether there's a pullback or not and getting that traffic momentum and it still got legs, I think that's what gives people little bit more confidence that they might be able to see through some economic clouds to focus on how we can continue to get back to where we were and that's a pretty big deal and it's good for our customers and it's good for the industry. So, I think – overall, I think we're a bit fortunate in that regard and keep flying.

#### **Kristine Tan Liwag**

Analyst, Morgan Stanley & Co. LLC

Great. And following up on your comment on international traffic, we're seeing it two-thirds recovered. You had some positive news this summer with the 787 approval for redelivery again – to restart deliveries. What are customers saying about the 787? Do they want the aircraft?

#### Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

Absolutely. August was a big a big moment for us, and I just got to call out our team in Charleston, who have done – who did some amazing work. I've never seen anything more disciplined. They kept their composure. They were calm. They worked with the regulator and they got it done. And they deserve a lot of that credit.

Now, in terms of the question on do clients – customers want it, consider that the 787 is the most utilized wide-body out there right now. It's being worked hard, because it's got operational systems efficiencies for clients, customers and it's got flexibility. So they like what they see and we also in – recently have welcomed China Airlines to the 787 family. So there's orders.

So that all feels pretty good. Now, long-haul international traffic has lagged, as you mentioned. It's got more to recover. Wide-body was always going to recover after narrow-body, in our view, and this is going to be a 2023-2024 kind of window. But we think that sets us up very well with the 787 because as that long-haul traffic wants to recover with traffic, the wide-body demand looks a little bit better, that's going to be a great spot for the 787 because we'll have worked on stabilizing the production line and we'll be able to be positioned well.

And remember that 787 is going to be around for a long time, a very long time and customer – voice of the customers, they really like it. So I think they're confident. We're confident. And again, getting that milestone behind us in August, now we got room to run. So, it feels pretty good.

**Kristine Tan Liwag** 

Analyst, Morgan Stanley & Co. LLC

Yeah. That's great to hear. And on the resumption of deliveries for the 787, can you give us an idea of the key moving pieces of what's been done, what's left to do and how quickly you can burn down the inventory of fully built 787?

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

Sure. So that really starts with the inventory. So as of the end of August – July, end of August, not July or I guess August, we have 118 inventory. And right now we have an expectation that we will burn more down as we close this year. We're going to get a bulk done next year and some will hang over into 2024. And that's pretty much what our expectations were. And that's really dictated by the amount of required rework that we have to go perform in order for us to satisfy what was agreed upon with the FAA. So that's – nothing's new on that front. At the same time, we are at low production rates and we have an expectation that we will get back to what we consider normal production rates, which when we hit around five a month.

And again, that is expected to be as we exit 2023. So all this has been expressed in the financial sense around our "abnormal treatment." And we've said that our abnormal cost treatment will largely be behind us as we exit 2023, because we'll have a lot of that rework behind us and we'll have that production rate going from low to that five objective. And then, beyond that, we'll worry about that in a bit. But yeah, no real changes and every day that goes by, the team feels more confident.

Kristine Tan Liwag

Analyst, Morgan Stanley & Co. LLC

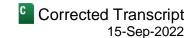
And I think for what you mentioned beyond the five per month, we're seeing – we saw at Farnborough orders for the 787. I mean, that's phenomenal. We haven't seen that for a few years. And then we have the potential replacement for wide-bodies eventually coming when you look at the age of the fleet. So what would make you comfortable to raise 787 production rates beyond five per month? What would you have to see to get you there?

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

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It's all going to be about stability. We're not really worried about the demand side of it. It's just about our own ability to be stable and have a supply chain that supports it. So I, long term, feel very confident in that product.

**Kristine Tan Liwag** 

Analyst, Morgan Stanley & Co. LLC

Great. And earlier you mentioned supply chain. So pivoting to the 737 MAX, it's been challenging to maintain 31 per month. Can you talk about what supply chain issues you're facing today and what mitigating actions you've taken to be able to produce at 31 per month and stabilize the program?

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

Yeah. So we're not – we are – the schedule is firing at 31. But we are not delivering at 31 for some of those reasons that you mentioned. Now, July and August, both light. We still are aiming at our full year target. There's risk in that. But the risk if we didn't quite get there, is more with disappointing our customers. Cash flow will be fine either way. But there are persistent supply chain constraints which has got us into position that we're in. You mentioned the electrical issue we talked about. We've got to work our way through that. Labor is real and it's not attracting labor as much as the experience curve. So we bring a lot of new labor into the factory. They have to learn. And that experience curve is real for many of us. And it takes time.

The real gating item though that we're focused on are the engines on the 737. The engines are behind. CFM has been very collaborative. The teams are working hard together. We've got senior leadership across Boeing and Safran and GE all looking very transparently of how we navigate our way through these persistent supply chain constraints that everyone is dealing with, both parts and labor, etcetera.

So that's real and that is likely going to extend into next year. And I promise you a lot of resources are looking at it and trying to work our way to a better spot, but we have to stabilize around 31. We have to stabilize at 31 and we're going to do that. And we talked about when you're going to ramp the rate. Well, when we stabilize on 31 and when there is a moment when we can sit together with our CFM partners and get confidence that we have a delivery schedule that is attainable, then you might have that discussion, but we're not there yet and we got to keep on focusing on that stability.

And then there is the inventory liquidation side of that, which we've got 290 737s in inventory as of the end of the second quarter. Bunch of those are earmarked for Chinese customers. There's a lot more we're working our way to get through and we're getting better at reliably getting them out of inventory, but there is work that's required there as well. So you're trying to do both.

**Kristine Tan Liwag** 

Analyst, Morgan Stanley & Co. LLC

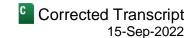
And Brian, you mentioned the Chinese customers. Maybe that's a great segue way to ask you for an update for CAAC. What are you hearing from China and the regulators and when would you anticipate the first 737 MAX to return to service in China?

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

So as we exited last year and gotten to February, both the customers in China and the regulators did exactly what they said they were going to do. And then February came – and in February, we actually had customers doing

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flight tests and then everything stopped. And they paused because they had to deal with their COVID lockdown restriction, etcetera.

So, right now, we are constantly communicating with our customers and the regulators, and we stand ready. When they're ready to pick up where they left off to finish that work, we are ready. I can't dictate the timing, only they can. But I will tell you, more broadly, we have deferred decisions on those planes for a long time. We can't defer that decision forever. So we will begin to remarket some of those airplanes that were otherwise earmarked for our Chinese customers. And we don't do that lightly. These customers are incredibly important. We're celebrating 50 years in China. It's important market. But we've deferred this decision long and now, we have to think about investors where time to start to look to reposition. And the good news is we've got confidence and conviction that we can remarket them. So we've got to navigate our way through that.

#### **Kristine Tan Liwag**

Analyst, Morgan Stanley & Co. LLC

And what are the key obstacles for these airplanes to resume deliveries in China? I mean, they already had the airworthiness in December. What's left to do?

#### Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

They literally just have to get the regulator to say you're ready to fly it again and return to service. So there's a whole set of protocols, pilot – making sure the pilots are updated on training, etcetera, and go through certain specifications. And all that work is things that we expect. And we don't see any "gotchas". We just got to work through it when the regulator and the customer are ready and we stand ready.

#### **Kristine Tan Liwag**

Analyst, Morgan Stanley & Co. LLC

Great. That's helpful color. And maybe pivoting to the 737 MAX 10, can you give us an update on where you are in terms of the certification process? And what are your plans for certification if the airplane doesn't get certified by year end as you got to add the new flight crew?

#### Brian J. West

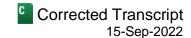
Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

Yeah, so there are lot of resources that are working very hard to get the Dash 7 and the Dash 10 certified. Answering the questions from the regulators, there's good, constructive collaboration with the FAA. There's a lot of energy around that. Make no mistake about it. I can't dictate the time. Only the FAA can do that and we were disciplined on that with the 787. We will continue to do that with proceedings through the certification for the Dash 7, Dash 10.

Now, everyone is aware of the statutory deadline at the end of December. And we're making sure everyone is informed about what exactly that means in the context because what's important is that this exemption was always intended to include the Dash 7 and the Dash 10. No mistake about it. And if you think about the customer view and our view is that the commonality of the 737 family is important and it enhances safety. It doesn't take away from it. It enhances safety. So, as long as we continue to work close with FAA and remind people of the context, we believe we have paths to work through it. But we will see that unfold as we exit this year and move into next year. But it's a real deal. And it's top of the list of things that we're trying to mitigate risk around.



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#### **Kristine Tan Liwag**

Analyst, Morgan Stanley & Co. LLC

Great. And pivoting to the defense business, geopolitically we've seen heightened tensions with Russia and Ukraine and also the Asia Pacific. How should we think about the opportunities for Boeing defense both domestically and internationally? And can you provide more details on your progress for the fixed-price development contracts that you have with BDS?

Brian J. West

Chief Financial Officer & Executive Vice President-Finance. The Boeing Co.

Sure. So I'm very encouraged by what we hear both domestically and internationally on this front on defense spending. Our – the NATO members, our partners and allies are all enthusiastically talking about the requirement for security and increasing their defense budgets. We've seen evidence with the Apache in Poland and in the Chinook in Germany, both proud of those announcements. And we believe that the portfolio matches up pretty well for where they want to spend those dollars, so encouraging. Now, the specifics in terms of all the details and the budgetary processes, etcetera, have yet to unfold, but generally positive.

On the fixed-price development side, as I mentioned, a global constraint in the supply chain and inflation and labor availability are all exacerbated by these fixed-price development contracts. The VC-25B and the tanker, they were done a long time ago, right? And they have been challenged from the beginning financially. And I know it's frustrating everybody. I will tell you that, as you work your way through the ramifications of our environment through those contracts, we had to deal with it. And there's pressure there. But I will also tell you that on the VC-25B, we will deliver two phenomenal airplanes to the customer and it will come to an end. And this will all be behind us.

On the tanker, we have a lot more airplanes to deliver. If you ask the customer, and we hear from the customer all the time, they are very complimentary of the capability and the mission and they really are applauding the tanker. And we got to start to think about international opportunities. It won't take away from the economics that has been burned on that program. And unfortunately that is what it is. But we do believe in the airplane.

On the MQ-25 and the T-7, those are really more development in nature. Those were always going to be investments. Unfortunately, investment is getting higher. The same constraints that knock around our tanker and VC-25B contracts will knock around those contracts with the added risk of – there is some discovery in engineering here that's new capabilities. So we got to work our way through all that.

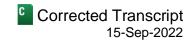
And those two though, we always look at the long-term view, and yet those will always be investments in these programs because there will be thousands of airplanes across MQ-25 and T-7 that will get delivered over time. And we got to make sure we never take our eye off that ball and we have to get through what these development contracts are. Look, these were done a while ago. Lessons learned for sure going forward but we have to work through them and meet the customer requirements.

Kristine Tan Liwag

Analyst, Morgan Stanley & Co. LLC

And pivoting to BGS, we've seen positive trajectory in revenue and also margin. How should we think about the services business going forward, especially as air traffic as you mentioned is only 75%? At some point, we'll get full recovery and growth on that. So how should we think about services?

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#### Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

Yeah. I forgot. Another bright spot. I should have mentioned that one. I love the services business. I spent lot of time there. These products last a long time and they need service and we've got real differentiated capabilities. The business is growing really well on the heels of a commercial recovery that's going at a very nice clip. Really like that revenue profile. The margins, they're accretive. They've done a very good job of managing the footprint and the cash conversion is very high. We have a new CEO. She is knocking out of the park. So everything about that business we love and really intentionally trying to go at a service business with a more asset-light model. Sometimes you can go in the service businesses and get too much into the assets. You end up paying for that over time. They've done a really nice balance and they are really getting more comfortable with the digital side of it and how do we differentiate on the digital side both in the cockpit and around the cockpit? And there are opportunities around that space as long as my arm. So, they'll be really balanced. It's a great franchise, really proud of that team and it's bright spot.

#### **Kristine Tan Liwag**

Analyst, Morgan Stanley & Co. LLC

So maybe we could talk cash. You've been steadfast in the outlook for 2022 of free cash flow breakeven. Now that we're approaching 4Q 2022, is that target still an achievable target? And can you give us some sort of puts and takes in how to think about it?

#### Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

Sure. We will – we expect to be free cash flow positive this year. Nothing's changed on that front. The levers, stronger deliveries is the biggest thing that'll underwrite that. And then we'll have expected favorability across things like expenditures, receipts, and taxes. So those are things that we got our eyes on and we believe that we will fulfill what we've said all year long.

I will tell you, as we think about next year and beyond, we expect to generate free cash flow for next year and we expect to continue to generate free cash flow and get to a point where we have a set of financials, centerpiece of cash flow that the investors recognize again. It looks more normal. Now, from where I sit today to that point, the quantum and the timing of what that looks like, it's hard to predict given the environment that we sit in, but we believe that it's still there. And if it takes a little bit longer, it takes a bit longer. We've got quite a few list of things that we've got to work our way through. I talked about those where we try to mitigate the risks. And we expect that will happen. But again, in the turnaround, sometimes it takes a little bit longer. But we still do have confidence in that endpoint and we still feel optimistic over the long term.

#### **Kristine Tan Liwag**

Analyst, Morgan Stanley & Co. LLC

And net-net, you sound really positive on free cash flow for 2022. I just want to...

#### Brian J. West

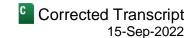
Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

We will generate positive free cash flow in 2022.

#### **Kristine Tan Liwag**

Analyst, Morgan Stanley & Co. LLC

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That's wonderful to hear. So maybe talking about the balance sheet, you've got a high debt level on the balance sheet. How do you think about – as you generate cash, how do you think about rolling that debt or paying it down versus potentially raising equity?

Brian J. West

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Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

Yeah, so first of all, we believe we have sufficient liquidity, combination of cash on hand and available revolver capacity which is in the \$12 billion range. So sufficient liquidity. I also – I know that the investment grade rating is important to us. It's a priority for sure. And then, we have maturities that are coming at us, but manageable. There's \$5 billion next year and there's \$5 billion in 2024. As we think about our trajectory and our momentum, we believe that the natural underwriting of the business and the cash flows driven by deliveries and execution will satisfy those maturities. So that one feels fine.

Our playbook on capital structure is very straightforward. We deliver airplanes. We generate cash flow. We invest in the organic priorities for the program development and we pay down debt. It doesn't get any more complicated. We have to go execute, right? We have to execute in a world that is bumpy, right, we've got to execute and we believe that, as we've gone through this year, we've gotten sequential improvement and we expect that sequential improvement to keep going. And we believe that, over time, we'll get back to that point that you all know looks more normal.

**Kristine Tan Liwag** 

Analyst, Morgan Stanley & Co. LLC

Yeah. And following up on that, do you have a target leverage that you want to get to? And can you give us a little bit more detail on how you get there?

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

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As I think about what normal looks like, for all of you, that would include what we used to have as a credit rating, which was – which is A-ish range. And there's nothing to suggest that we can't get there. Again, it's going to be the timeline. And this, if we execute well and actually delever, that will be opportunity to discuss. Other alternatives later, but right now it's focused on delivering that game plan I mentioned and delevering. And then the credit rating will take care of itself. And again, we can't wait till we get back to a day that you all remember.

**Kristine Tan Liwag** 

Analyst, Morgan Stanley & Co. LLC

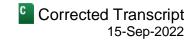
So if we fast forward to that period in the enterprise is generating normalized free cash flow, and at that point the balance sheet would have – be in better shape. What are your capital deployment priorities when you get there? What do you want to do with that cash?

Brian J. West
Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

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I'd like to get through my turnaround first. No, I - it's - let's have that discussion at the right time. I think a wonderful time to have that conversation is just it's really hard to think about it versus where we stand. So we got a lot more execution to get under our belt, but I can't wait to have that conversation.

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#### Kristine Tan Liwag

Analyst, Morgan Stanley & Co. LLC

Great. And, Brian, thinking about what are you most excited about right now?

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#### Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

I guess there's one bright spot that I didn't mention. I'm really proud of our people. I don't say that as a throwaway comment. It's just our people went a lot – though a lot the last several years, and we're not done yet. But the way they show up day in and day out and the way they bounce back, it's pretty – they're resilient. And I'm proud to be associated with a team that has that within them and has a passion for our mission. So that's the part that I mostly get excited about. And then watch us move this trajectory forward and getting better and better and better. Because if you step way back and you look at the long term prospect of The Boeing Company, there – in the next decade or two, there are lots of growth opportunities for us to go seize. I think we'll be well positioned. We do design, make and service great products. The marketplace recognizes it, customers recognize it and you can never lose sight of that real differentiating capabilities out there.

Now, we're not there yet. We – pragmatically speaking, we are in a turnaround. We have more work to do. It is not lost on anybody. Tends to take a little bit more time given the environment that we sit in. But I tend to want to be optimistic long term, and whenever I have a down day, I just walk out in the factory and I see the 787 or go to St. Louis and see the fighters or go out to Seattle. The products that we make are pretty incredible. And like I said, pretty proud of the team that I have the privilege of working with. So that's what makes me optimistic.

### **Kristine Tan Liwag**

Analyst, Morgan Stanley & Co. LLC

Well, great. Well, thank you very much, Brian. Thank you for joining us today. And this concludes our Boeing session.

#### Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

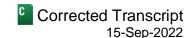
Thank you. Thanks, Kristine.

### Kristine Tan Liwag

Analyst, Morgan Stanley & Co. LLC

Thank you.

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