



## Aug. 15, 2018 Podcast Transcript

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**Announcer:** Welcome to HII Talking Points, a Huntington Ingalls Industries podcast. Twice a quarter, we'll sit down with HII leaders to discuss topics of interest about company and industry.

**Phoebe Richards:** I'm Phoebe Richards and today I'm talking with Dwayne Blake, HII corporate vice president of investor relations. Thanks for joining Talking Points. It's great to have you.

**Dwayne Blake:** Thanks for having me.

**Phoebe Richards:** So, investor relations is a broad topic and a job function that our listeners might not know the ins and outs of. So today, I'd like to explore investor relations and your role in the company. So, to start, let's talk a little bit about the investor relations department and what it does for the company. What does a typical day look like for you?

**Dwayne Blake:** So, now is a great time to ask that question because we just finished our second quarter earnings process. And a typical day getting ready for that's been pretty hectic over the last several – I guess last six to eight weeks. It takes a fair amount of planning and lots of activities to prepare for that one hour call. Right?

It's a small staff. We're a team of two. And right now, I'm actually using one of the guys over at Newport News because I'm in the process of hiring a replacement for my director. So I give a shout out to Eric Udovich who's done a great job helping fill the void here for the last couple of quarters and been a really helpful add to the team.

So basically, as we prepare for the earnings process, it's again, pretty comprehensive. And as I mentioned, it's a one-hour call. But we've got basically a couple of documents that we really prepare to get ready for that. One being the press release, that press release that gets prepared – it's what? Twelve or thirteen pages. But the work that goes into getting ready for that, you never imagine. But just to make sure that everything is 100 percent accurate and complete.

So, we make sure that everything that goes into that document is correct. Similarly, with regard to the scripts for the CEO and the CFO, we are very keen on the content, the messaging, and making sure that everything in those documents and in their statements, their opening remarks, is accurate, complete, consistent, not misleading, consistent with the messaging, et cetera. It's all that and then as well as a presentation that gets posted along with that. So, all a part of that process to get ready for the big earnings call.

In addition to that, we go through a very comprehensive question and answer deck. We've got a couple – I want to say like 30-some pages and tons of questions. One of the things that we try to do – and Mike [Petters] is an advocate of this – that we want to make sure that analysts aren't asking us a question that we haven't already asked ourselves. Right? So you don't want to get caught flat-footed. You want to have thought and have a good clean answer that you can put forth. So, when I go through the Q&A prep, it's a very disciplined process. We get all of the information from the segments as well as from the corporate office. We get – you name it. You name the subject and we've got a prepared question and answer on it.

So all that's been going on, as I mentioned, about six to eight weeks to get ready for the one-hour call. Then, the fun that I have is right after the call. Usually starts about 10:30 AM. So the call's from 9 a.m. to 10 a.m. Then, I get on the calls with the sell-side analyst. All the guys that are trying to prepare their reports so that they can issue them shortly after the call. So I'm on the 30-minute calls with them. This most recent process, we had 10 out of my 12 analysts – I had 30-minute calls. I was on a call, on the phone from 10:30 a.m. until 4 p.m. non-stop for the most part.

But it's good. Because you want to make sure they understood what was heard. And if they got clarification and they want to get some additional information for building their models, which is really what they're focus is. That's what it's all about. So this is kind of the typical six-week – not a typical day -- but this is a typical six-week process to get ready for that.

It's pretty intense. But it's a lot of fun, too. It gives you the full insight in terms of what's going on within the company. So you know everything that's going on. Because if there's information out in the press, for example, what's going on with the budgets, what's going on with the programs, where are we investing our money from a capital perspective.

I mean, we have got to know everything about all that stuff. So we really, really cue in on all of that to make sure that we can share that insight with the Street. And also be careful because we have to be in compliance with our regulation FT from a fair disclosures perspective and making sure that we're not providing information to these guys on these one-on-one calls that I mentioned that's not available to the general public. So that's also something that we're keenly aware of, keenly focused on.

**Phoebe Richards:** So, you talk with analysts about earnings. Then, you also talk with them on a regular basis. So, how do we, as a company, ensure that analysts are up to date on what's happening at HII year-round? Then, how do you manage their expectations?

**Dwayne Blake:** Yeah. So, year-round, it's an ongoing process. When there are press releases that go out, communications team, whatever they're sending out, I'm always prepared to field a question on those types of things. But from a proactive perspective, we have the interaction with these guys after the earnings calls. Then, we also have the opportunity to meet with both investors and analysts during a couple of opportunities.

One, the sell-side analysts host conferences. We tend to participate in several of those during the year. We get a chance to meet with the sell-side analysts. Then, they'll have folks from the buy side, the

investment community, that will participate. So we get a chance to meet with those individuals in one-on-one meetings which typically run 30 to 45 minute sessions.

We get a chance to talk about business, what's going on from a strategic perspective, where the financial performance has been, kind of the high level outlook for the company. We're always talking about where the company is and where it's headed. All within the construct of as we put out the "Path to 2020" strategy, which gave the community a five year look ahead in terms of where we're going and making sure that what we're talking about and how we're updating them is consistent with that messaging. So we try to manage that and make sure that we're on point with that.

In terms of managing expectations, it's all about execution and delivering on what you put out there. So, we put the "Path to 2020" strategy out there and we – basically trying to make sure, from an execution standpoint, Ingalls, Newport News, Technical Solutions are meeting those expectations that we put out there. Each quarter, we basically get a report card. We get a chance to see and report out to the Street how we were performing. If we don't make the mark, guess what? Stock doesn't perform well.

If we exceed, then the stock does perform well. It's kind of interesting where you get kind of real-time grading, if you will, on your performance. The other thing that's kind of interesting about it is, sometimes your stock performance isn't necessarily a direct result of the things you control. It's market influences, things that are going on in the broader economy, geopolitical issues, what's going on in Washington, politics. All of that can affect the market. Sometimes we have absolutely nothing to do with that. But yet, it causes our stock to either go up or down. That's just another factor as I'm having to explain the way the stock performs the way that it does sometimes. Then sometimes that answer is, it's outside of the specific things that we're doing.

**Phoebe Richards:** So let's take a step back. Who owns HII stock?

**Dwayne Blake:** We've got over 600 institutional investors. When you look at the composition, the top three investors are Vanguard, State Street, and Fidelity. Those three firms own about 25 percent of our shares. Those are typical top shareholders in a lot of companies across the country. When you look at the makeup of the styles of investors, we've got about 37 percent of the investors that are index funds, which are the Vanguards, State Streets, BlackRocks, those types.

We've got 17 percent that are labeled as growth at reasonable prices or GARP. Then, you've got another 11 percent that are true growth investors. Another 12 percent are value investors. Then, we've got another 23 percent that are hedge funds and other styles. So that's kind of the composition.

One other point that I would like to make to the listeners is that they may not realize this but the shareholders of Huntington Ingalls that are the most important ones in our book are the employees. They are actually somewhere in the top three or four. They hold about 2.2 million shares. So we really want to make sure that employees realize that they are, in fact, key shareholders.

And that the decisions that they make on a day-to-day basis in terms of their work and their execution of their responsibilities has an influence on the stock that they are owning. So it's something that people don't think about. But I try to make that point so that people can realize that they do have skin in the game. They're part of the ownership of the company.

**Phoebe Richards:** Certainly. Would you say Vanguard, Fidelity, our own employees, is that a healthy mix for HII in terms of who's owning stock?

**Dwayne Blake:** It is. We look at benchmarking. We look at the makeup. As I walk through those different styles of investors, they're all relatively consistent with our peer group. Because that's what we tend to do is kind of look at how we stack up against our peer group. When we look at each of those categories, they're relatively consistent. That gives me some comfort that we're not out of the box in terms of being a fair distribution of the ownership.

**Phoebe Richards:** Right. In terms of shareholders and analysts, what are some of the most common questions you field?

**Dwayne Blake:** It's interesting that a lot of the questions – and I'll reference this most recent earnings call because it's all fresh in our mind. You look at the things that folks are trying to use to help build their models, trying to understand where the business is going. So we talked about the fact that – we mentioned this on the Q4 call, where we introduced for the first time growth in shipbuilding. We talked about how we were expecting three percent compound annually growth rate over the next five years. So between 2018 and 2022.

Now, people are wanting to understand, okay is that three percent now more than three percent, given some of the things that are happening? Some of the things that they're hearing in terms of budgets in Washington and this commitment from the Navy in terms of the 355-ship Navy and all of that? We have to remind them that, okay, yes, there's some positive developments out there. But this is a risk adjusted number. So, we tend to take into consideration things like continued resolutions, programmatic delays, and things of that nature that can cause all the perfect plans to be just a little bit off.

Kind of give them a little bit of push back on that from – that's one of the key questions that they always ask. What's the sales forecast? What's the top lines? Where are margins going? We've introduced – on the Q1 call, we reset expectations in terms of where margins are going to be for shipbuilding.

The historical margins for shipbuilding – and we talk about this and have been talking about this since we spun – was that kind of the healthy range is like nine to ten percent. What we did in the Q1 call was reset those expectations to be more like seven to nine percent for 2018 and 2019, mainly because the mix of work at Newport News is more weighted towards early production, which tends to be booked at a lower margin.

So we put that out there. So now, everybody wants to know, okay, we had one quarter where shipbuilding was higher than that. Now, everybody wants to say, "Are you going to reset that?" No. We put this out there. So we field those questions. They're always asking about free cash flow, pension contributions.

CVN-79 is another hot topic. They want to understand how that progress is going, what's the performance looking like. We actually added a little extra color commentary in Mike's script this quarter to provide some insights in terms of how the units are coming together and the focus of the team in terms of their March launch by the end of next year, which is their goal. We wanted to make sure that the community understood where we stand and the fact that so far so good, things are progressing along well. But, we still have a lot of hard work ahead of us. Those are the – I guess if you want to put them as the top questions, things that folks are focusing on.

**Phoebe Richards:** Right. How do you balance investors' needs with our long-term company goals?

**Dwayne Blake:** As a company that has probably the longest horizon of most companies, and you look at investors' horizons, which tend not to be very long, are much shorter in nature. It's a matter of laying out the expectations. We've done that in the form of our "Path to 2020" strategy. We basically said, "Okay, here's what we're going to do over the next five years. We're going to invest \$1.5, now \$1.8 billion of capital into our facilities.

"We're going to return substantially all free cash flow to our shareholders through share repurchases and dividend increases of at least 10 percent each year. Then, we're going to optimize and expand our services business. And we'll do that in a very disciplined and very focused way, if we find targets that are out there that make sense."

So, we laid that out. It's not a matter of basically delivering on those expectations. Investors, they expect folks to, when they put expectations out there and they put an outlook out there, they expect you to meet it. In many cases they expect you to exceed it because they know that, from a planning perspective, people tend to be conservative. But it's a matter of execution, execution, execution. The more that the shipbuilding guys can deliver on their schedules, that they can deliver on the – negotiate good contracts, allow us to execute with reasonable sales and margin expectations – so that's really what it boils down to. Laying out the expectations and then executing.

**Phoebe Richards:** We read in the news stories about activist investors. Can you talk a little bit about what an activist investor is and if HII would ever be at risk for one?

**Dwayne Blake:** Yeah. Basically, when you think about an activist, they're in essence, agitating for change. They see, in their view, opportunity for better returns from their perspective. So, they tend to begin to acquire stock in a particular company that would give them the ability to have their views have more prominence over other people's views. As they are putting their views out there, it's a matter of the company responding or not responding or choosing how to respond and dealing with that view point.

For us, the fact that we do have such a long horizon, we've got a key partnership with the Navy. The risk of activism for us is relatively low. We actually have monitoring services out there. We have information out there that I can pull today to see how we're stacking up on key metrics that flag you for the activism risk. So I'm always watching for that. Then, we also have a preset activism plan in place with an activism plans and basically, a lot of activities all pre-staged and ready to go if in fact something were to come our way.

I don't really see it as a key risk. But it's better to be prepared just in case. I really – it's something that's in the news a lot. They tend to be high visibility folks that get involved in that. But I'm hopeful that we'll stay under the radar and continue to keep our heads down and keep executing and keep delivering the long term shareholder value that our shareholders deserve.

**Phoebe Richards:** Definitely. Last question. HII was recently selected to be on the Standard and Poor's 500, S&P 500. What are the attributes that the S&P 500 uses to select companies? And what does HII have to do to stay on the list?

**Dwayne Blake:** It's a committee, the S&P 500 committee. They've got several criteria that they focus on market capitalization, liquidity metrics, U.S. domicile obviously, sector classification, financial viability, length of time publicly traded. So, those types of things. When you look at the evolution of Huntington Ingalls since we spun in 2011, you look our credit profile and the financial strength and stability. It was kind of a natural evolution that we kind of marched in.

We kind of satisfied all of those requirements. And the door was opened and we were able to come in. Now, as a matter again, it's keeping our balance sheet in a place where it continues to support those metrics, continue to execute and do the things that we need to do long term to maintain the financial health of the business. And that's really what it's all about.

**Phoebe Richards:** Great. Well, great discussion. Mr. Blake, thank you for opening the world of investor relations for us today.

**Dwayne Blake:** Thoroughly enjoyed it. Thanks for having me.

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