

Transcript of
Materion Corp.
Materion First Quarter 2024 Earnings Conference Call
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Participants

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Presentation

Operator

Greetings. Welcome to the Materion First 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, Investor Relations and Corporate FP&A. You may begin.

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

Good morning and thank you for joining us on our first 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 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 conference 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 remainder 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.

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 of the press release. The adjustments are made in the prior year period for comparative purposes and remove special items, noncash charges and certain discrete income tax adjustments.

And now, I'll turn over the call 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 first quarter performance as well as our current outlook for 2024. Our results for the first quarter fell far short of our expectations. While we were expecting to be roughly in line with Q1 of '23, some operational challenges, mainly in our Performance Materials business and some pockets of slowing and market demand, led to lower sales and earnings. I'm proud of our team's quick actions to mitigate these short-term headwinds, delivering roughly flat EBITDA margins year-over-year, despite a nearly \$40 million sales decline.

We've taken a number of targeted cost actions that are benefiting not only our short-term results, but are providing longer-term structural improvements that will enhance profitability as key markets recover. Looking more closely at the sales performance, continued semiconductor weakness represented roughly half of the year-over-year decline. In addition, the expected inventory restocking of our beryllium nickel product used in nonresidential construction had a meaningful impact.

Our results were further limited by delayed shipments due to the operational challenges mainly in Performance Materials. While we had anticipated the softness in some of our end markets, demand in commercial aerospace and automotive was softer than we expected due to reduced aircraft build rates and slowing growth for electric vehicles.

Airplane deliveries were down significantly year-over-year in the first quarter and are expected to be depressed for the year. Offsetting these declines, we saw strong growth across space and defense, where we are providing critical materials for space propulsion systems and on a growing number of defense platforms. Short-term operational challenges further impacted sales on a temporary basis in the quarter. Addressing some yield and equipment issues, our operations team responded quickly to address the issues and return our assets to normal output levels.

Operational excellence initiatives have been core to our performance as we deal with market headwinds and other short-term challenges. We have taken multiple targeted actions to adjust our cost structure while continuing to invest in these areas that drive organic growth for our business. These important moves have helped to deliver strong margin performance in a softer end market environment.

Despite the decline in sales, our overall EBITDA margin for Q1 was roughly flat on a year-over-year basis, representing a strong 20% decremental margin. Our laser focus on driving margin improvement in Electronic Materials delivered EBITDA expansion of approximately 500 basis points in the quarter even with a 25% VA sales decline. This strong performance leaves us extremely well positioned to drive even higher levels of performance as markets recover.

Our focus on managing the business through some short-term headwinds is complemented by our relentless efforts to invest for the future as we continue to see the pipeline for long-term organic growth. We remain confident in our strategy and believe that our robust organic pipeline and portfolio of cost improvement initiatives will help drive earnings growth for the balance of the year.

We expect to see continued strength in the space and defense markets as we move through the year. Many of our advanced materials are engineered to perform in the harshest environments, making them an ideal fit for these demanding applications. New defense business wins in addition to the previously announced R&D partnerships for various government funded projects further solidify our position as a key supplier for advanced materials across aerospace, defense and new energy markets.

In the semi market, near-term growth in memory and logic chips used in high performance computing is expected to drive the rebound in our sales this year with the demand for power and industrial chips coming back later in the cycle. We believe Q1 was the bottom of the downturn for us, as we see order rates picking up coming into the second quarter, giving us confidence that our top line will continue to improve as we move through the year.

The industry is continuing to prepare for the global shift toward a broader AI adoption and Materion is a vital part of that supply chain. We continue to advance our broad portfolio of semiconductor products and are investing to increase capacity in key production areas to ensure we are ready to support that increased demand.

The Precision Clad Strip project continues to be a significant driver of organic growth for us, and our partnership with our customer is strong. The expansion of our new facility remains on track to start up late this year. As the customer's global rollout progresses and our teams have driven higher levels of output and performance at our new facility, we will now begin to ramp down production at our legacy facility.

Our customer indicated an adjustment to their inventory levels for the second half of the year, which will impact our shipments. This adjustment does not correlate to weaker end product sales as the customer's global rollout remains on track and their projections support a robust long-term outlook for our business.

Our team has done an exceptional job of steering the company through some short-term challenges while maintaining a longer-term focus that will further position Materion for sustainable growth and value creation. With the start of the recovery in semi and improved operational performance, we expect to deliver a much stronger Q2 with additional step ups in the third and fourth quarter, resulting in another record year for Materion in 2024.

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 last night starting on Slide 9. In the first quarter, value added sales, which exclude the impact of pass-through precious metal costs, were \$257.8 million down 14% from prior year. Despite strength in aerospace and defense and consumer electronics, our sales were negatively impacted by declines in semiconductor and automotive, plus the expected inventory correction for our nonresidential construction material.

Additionally, as Jugal commented, some temporary operational challenges limited our shipments, particularly in Performance Materials. Our teams have made meaningful progress in mitigating these challenges and expect more normal levels of output in the second quarter. When looking at earnings per share, we delivered adjusted earnings of \$0.96 in the first quarter, down 28% from prior year.

Moving to Slide 10. Adjusted EBITDA in the quarter was \$45.2 million, 17.5% of value-added sales, down 15% from the prior year with roughly flat margins. Despite the significant sales decline, the strong margin performance was driven by positive price and the benefit of our cost improvement initiatives partially offsetting the volume decline.

Moving to Slide 11. Let me now review first quarter performance by business segment. Starting with Performance Materials, value-added sales were \$155.6 million, down 7% from prior year. This year-over-year sales drop was driven by lower demand in automotive, commercial aerospace and the nonresidential construction application within industrial. Space and defense remains a bright spot with significant contribution from the emerging space market and strong defense demand more than offsetting declines in commercial aerospace.

EBITDA, excluding special items, was \$35.7 million or 22.9% of value-added sales, down 17% from the prior year period. This decrease was driven by the lower volume, partially offset by targeted cost improvement initiatives.

Moving to the outlook. We expect space and defense to remain strong throughout the balance of 2024 and again, expect the operational challenges to improve as we move into the second quarter.

Next, turning to Electronic Materials on Slide 12. Value-added sales were \$77.6 million, down 25% compared to the prior year as a result of continued weakness in the semiconductor market. EBITDA, excluding special items was \$14.5 million or 18.7% of value-added sales in the quarter. Despite significantly lower volume, operational performance and cost improvement initiatives helped mitigate the semiconductor slowdown, which drove approximately 500 basis points of margin expansion year-on-year.

As we look out to the rest of the year, we expect a gradual semiconductor recovery from Q1 with sequential improvement as we move through the balance of the year.

Finally, turning to Precision Optics segment on Slide 13. Value-added sales were \$24.6 million, down 8% compared to the prior year. This year-on-year decrease was mainly driven by reduced demand in industrial and automotive, partially offset by strength in space and defense. Precision Optics also saw some operational challenges, which delayed some shipments out of Q1. EBITDA, excluding special items, was \$0.4 million or 1.8% of value-added sales. The decrease in volume was a significant driver of this year-over-year decline in addition to unfavorable product mix. Looking out over the next few quarters, we expect a meaningful step-up in margin performance in Q2 with stronger demand and continued focus on cost improvement initiatives.

Moving now to cash, debt and liquidity on Slide 14. We ended the quarter with a net debt position of approximately \$462 million and approximately \$130 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.

Lastly, let me transition to Slide 15 and address the full-year outlook. Despite the slow start to the year, we expect to deliver another year of record results with our organic and operational initiatives more than offsetting some market softness. Since our initial guide for 2024, the outlook for commercial aerospace and electric vehicles have softened. And as Jugul mentioned,

we are expecting some inventory correction from our Precision Clad Strip customer in the back half of the year.

We also expect slightly higher interest expense based on the current rate outlook. While we will work to mitigate much of these headwinds, we are adjusting our full-year guide to a wider range of \$5.60 to \$6.20 adjusted earnings per share, a 5% increase from the midpoint versus the prior year. Despite the mixed market environment, Materion remains poised to deliver another year of strong execution and record results in 2024.

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]. Our first question is coming from Phil Gibbs from KeyBanc. Phil, your line is live. You may proceed.

Q: Thank you. Good morning.

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

Good morning, Phil.

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

Good morning.

Q: Can you please up the message here a little bit? I hear you talking about inventory reductions at the customer and ramping down of the legacy facility, but you're also saying nothing changed on long-term demand and you still plan on Phase 2 being a meaningful contributor in the future. So can you just help maybe lay out the land a little bit better here for us? It seems to have some things moving in different directions?

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

Yes. Well, Phil, as you know, this program has been really a great success for us over the last couple of years. I mean, our team has just done a fantastic job of driving yield improvement, operational improvements in our new facility, while we continue to deliver from our legacy facility. I think what we're talking about is really a short-term issue, where the customer has continued to look at if they've gone through the launch phase, how do they make sure that they've got the right levels of inventory to support their global rollout.

So that's one part of it. I think the second part of it is just the great improvement that frankly, our team has made on our new facility that has allowed us to deliver at a rate that I think is very, very satisfactory to the customer. So a combination of that, I mean they're just looking at the back half of the year and looking at making some adjustments to make sure that they're properly positioned. And then we would expect that in the new year, come 2025, because their demand will continue to be robust, and we will continue to support them in a meaningful way.

So I think all of these things actually tie together, and that's why we say the Phase 2 is on track. It's going to contribute into the 2025. We've been saying that, I think, all along that it would be late '24, really nothing of substance or meaningful deliveries here at the end of the year, but really contributing into 2025, and at the same time, making sure that we can continue to support from the Phase 1. And then we've talked, of course, over the last year, 1.5 years because I think the questions have been there about, okay, when are you going to stop producing from the legacy facility.

And I think considering the – some of the adjustments that the customer is looking at for the back half of the year it's about the right time to be able to start doing that and in support, of course, of the yield and performance improvements at our new facility. So I think it's just a natural sort of evolution of where the program is at with some corrections here for a couple of quarters, but continued success on a long-term basis.

Q: Thank you, Jugal. And then on the commercial aerospace side, you talked about some slowing and builds down. I mean, I think the only meaningful place where we've seen builds down, at least our knowledge is on the MAX program, but I know you also have a lot of maintenance exposure to the commercial side as well and maintenance has been strong.

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

Yes.

Q: Is this – does this or should this suggest to us that you just have more exposure to Boeing at this point? Or are you seeing other program adjustments?

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

Phil, as we look at commercial aerospace, I mean there – we see really a build challenge across both of the major customers, both Airbus and Boeing. I mean, if you look at some of the data, for example, that we track for build rates. If you go back to Q1 of last year, the build rate combined was around 250, 260 planes. This Q1, it was around 225. If you look at Q4, Q4 build rate on a combined basis was over 350. So the number is probably around 370, I think, for build rate. So substantial decrease here in Q1 across actually both.

There's a number of supply chain issues that, frankly, Airbus has talked about very openly that they are facing, so more of a supply chain issue on the Airbus side. And of course, we know the

challenges that Boeing is facing not only in the 737 MAX, but I think in general, I would say that they have really, really looked at their production processes to ensure that quality is at the forefront and are really taking steps, I think to adjust their build schedule as necessary. So significant down in the Q1 for commercial aerospace, which I would say is more than what we had anticipated.

And then as we think about the recovery for the rest of the year, I would expect that the build rates are going to improve. But certainly, those build rates are not going to get to that – at least we don't think that they're going to, get to the levels that they were over the last year or so. So I do expect commercial aerospace in general, to be challenged. This is absolutely not a share issue at all. As you know, we have been gaining content across both -- multiple materials and products that we have on both single-aisle and widebody planes. So our content growth is there. Our share is there. We just need these two mega companies to increase their build rates as we go forward. So we'll just -- we'll monitor the situation, but we do see this as a caution for the full-year.

Q: And then lastly for me, the operational challenges that you cited several weeks ago and then talked a little bit about today. Can you maybe pinpoint some major issues when they started to occur, what gives you confidence that they're behind you?

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

Hey Phil, I'll take that one. So as we mentioned, the majority of that issue was in Performance Materials. And really what we saw there was some yield challenges coming out of an early production process that impacts many of our downstream product lines in Performance Materials. That started really early-ish in the quarter, if you would.

And we started to see that we weren't going to be able to service all of the demand, all of the orders that we had on the books, which is when we reevaluated and then came out with a bit of the early caution. That is getting better. The issues are being addressed. I think the team got together quickly to make sure that we could get those yields back up to be able to service the full order book. There were a couple of other items. We had some delays at an outside tolling partner that were an impact and then some small yield challenges in Precision Optics. So we just had a

few things that kind of fell under the bucket of operational challenges that we think we've got addressed. But they were big enough to talk about.

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

Yes, and Phil I would add that as we look at our Q2 and as we've indicated, we expect Q2 to be a step-up -- a significant step-up from Q1. Getting those operational challenges behind us is core to that. And based on how we have been running here in the month of April and how we expect to run the rest of the quarter, I would expect that we're -- we've made a marked improvement in those operational challenges.

Q: Thank you.

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

Thanks, Phil.

Operator

Thank you. Your next question is coming from Daniel Moore from CJS Securities. Daniel, your line is live. Please go ahead.

Q: Thank you, Jugal, Shelly, good morning. In the prepared remarks -- thank you, you mentioned the start of the recovery in semi. Maybe just elaborate on conversations, dialogs with customers, in your confidence that demand should continue to improve sequentially beyond Q2 for the next few quarters?

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

Yes. Well, as you know, this market has been a very challenging market, not only for us, but for the entire industry, right? And there have been some starts and stops in thinking when is the bottom. We do believe, based on orders and based on conversations with our customers that Q1 was the low point for us. We see improvements going into Q2. We see improvements here in the first few weeks of the quarter as well as, I think, what we see for the next couple of months as well.

Our discussions with the customers as well as I think what we hear externally continues to indicate that logic and memory, in particular, is starting to lead the recovery, and I think it will continue to lead the recovery in Q3 and Q4. There are some challenges on the power side, those challenges being, frankly, the EV, the slowing growth of the EV. I think that's going to take a little bit more time for the power side. But logic and memory, I think are making -- are starting to make more of a recovery.

When I look at our order backlog, our order backlog has continued to improve over the last couple of months. We see probably from about three months ago to where we are today, approximately, I'm going to say, double-digit order backlog improvement for the semi business, which gives us confidence not only for Q2, but I think it gives us confidence for the back half of the year. So I would say, if I look at the last few quarters, it's the first time that I can sense a little bit more data that gives us confidence for the recovery to start to happen here in Q2, with Q1 being the low point and then continuing in Q3 and Q4.

Q: Very helpful. And just pulling on that string as we think about '25 and beyond and I guess it's probably more into '26, but the build rates expected for a lot of the fabs that are expected to come online. Just talk about your confidence, when do you expect a more meaningful inflection in that sort of core end market as far as when we might see the uptick to longer-term high single-digit type growth.

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

Yes. So I think when you look at the build rates in terms of the fabs and some of the investments that are being made, we certainly saw some of the investment slowdown commentary over the last 12, 18 months, as the overall market started to become more challenged. However, what we are seeing now, I think, is starting to have some more positive discussions around the investments.

We're seeing some of the investments in the U.S., for example, some of the government investments coming into play, some recent announcements at large companies. With the aid, the government is providing, I think, we're starting to see kind of almost starting back up of the investment activity in Asia as well. So we -- if the investments are happening, but perhaps a slight delay, right, from what they were talking about maybe two years ago. So probably a one to two year delay, but the investments are clearly getting back on track.

When I look at the levels that we had in the '22 time frame, I mean that was really a peak of the semi side. The thought was that those levels will start to come into play probably in the back half of '25. Perhaps now the -- perhaps now those peaks would be maybe the front half of '26. So a slight delay, a couple of quarter delay from some of the overall recovery that's happened. But I do continue to see over the next 24 to 36 months, I think a steady improvement and recovery in the semi market, again, led by logic and memory, but then followed by the other areas as well.

Q: Perfect and then last for me, and I'll jump back. The incremental capacity that you would have from shifting production from the legacy facility to the new clad strip facility, is that something that you can think about actively selling to alternative potential customers? Or is it more likely to be shuttered? Thanks.

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

Yes. So as we indicated, we would be looking at starting to slow down, certainly not stopping production. So the incremental capacity is absolutely something that I think is very usable because it's capacity that we were using, right, prior to starting this program. And so we will

simply shift that capacity to other activities in the commercial sector or consumer sector or the automotive sector. So we will make sure that, that capacity is being utilized appropriately. If for some reason, we have issues with that, we'll take appropriate action to adjust the cost structure.

Q: Okay.

Operator

Thank you. Your next question is coming from Mike Harrison from Seaport Research Partners. Mike, your line is live. You may proceed.

Q: Hi, good morning.

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

Good morning, Mike.

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

Good morning, Mike.

Q: I was wondering -- I appreciate all the detail you provided on the semi outlook, but just was hoping that maybe we could focus on the performance in the first quarter, particularly on the margin side. I know you called out the nice year-on-year improvement, but I think what was more interesting was the improvement sequentially on essentially the same level of value-added sales. Can you talk about what led the margin to be so much better in Q1 than it was in Q4 even though that value-added sales level was pretty similar?

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

Yes. Let me start with that, and then certainly, Shelly can add to that. As you know, EM has been a focus area for us for margin improvement, right? We have talked about how we need all of our businesses to contribute so that the overall company is able to get to 20% EBITDA margins or better. As the semi decline started to happen, and I'm going to go back to probably Q1 of last year, right, Q1 was almost kind of a peak quarter for us in sales.

Our margins started to frankly get impacted. We started to make significant cost improvement initiatives starting in the second quarter, but more importantly, I would say, in the back half of the year. And as you know, sometimes as you're making those plant improvements and operational improvements, they take a little bit of time to get into play. And so we're starting to see the benefits of that. And so I'm really, really proud of, I think, what the team has been able to do and to drive that improvement, I would expect that some of these improvements are going to continue. And I can assure you, we're not going to back off on that.

Some of these improvements are going to continue, and we're going to hopefully be able to drive margin enhancement as the market recovery happens. So that's a big part of it. Now certainly, there's always -- sometimes there's a little bit of onetime issues or sometimes there are little bit of mix issues. Those things go back and forth every quarter. But I think fundamentally, it's really the core improvements and the operational improvements that our teams have been driving over the last six, nine months that are starting to bear fruit and starting to deliver here in Q1, and I would expect that we continue to keep a focus on that. We need our EM business to deliver and contribute towards the 20% objective of EBITDA margins that we have.

Q: All right. Thank you for that. And then I was also wondering if you can lay out where we are in this inventory correction that's going on in the industrial business. These were really on nickel springs, I believe, for commercial sprinkler systems. Can you just kind of help us understand, I mean, we've seen destocking in a lot of different pockets of the economy, but this seems to be one that kind of cropped up later. And just curious if you feel like things are improving or if it's going to be something that's weak for the remainder of the year?

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

Yes. This is one that is kind of a fairly unique product, right, in the industrial sector, and it's hard to correlate it to a PMI index or some other type of an index that's kind of a unique product and used for this nonresidential construction. We are obviously the provider of these for the market. There was a significant growth that happened coming out of COVID. And I think the channel, frankly got a little flushed with the inventory.

As the interest rates and some of the inflation activities and some of the -- just the general downturn, I think, that we all know that's happening in the overall commercial construction and occupancy. As a result of that, we are just going through that inventory correction. It started to happen late last year, so maybe let's say, in Q4, but I would expect that the first half of this year is going to be a meaningful inventory correction that's going to happen in this business, and we would expect to start picking back up in the back half of the year, but I would expect the pick up to be, let's say, slight but then more meaningful pick up in '25 as that inventory is worked through.

So again, I want to emphasize, I think that this is not a share loss issue. This is simply just an inventory correction on a more specific element of what we consider in the industrial sector. And we would expect a small turnaround in the back half, but then a meaningful turnaround in '25.

Q: All right. very helpful. And then last question for me is just with your balance sheet, you mentioned just below the midpoint of your target leverage range. Curious if you can give us an update on your acquisition pipeline, what you're seeing in the M&A marketplace and maybe talk about the potential for some acquisition activity later in the year.

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

Yes, Mike. So I'll take that one. Yes. As you mentioned, our leverage right now sits about 2.2x, which is half between our 1.5x to 3x targeted range. So we feel comfortable where we are. As you know, we're doing a lot of organic investing, which is really what's kind of keeping that propped up after the acquisition we did of HCS Electronic Materials. We've not focused on debt paydown, but rather on organic growth. Given that we've got capacity, certainly, we still can do an acquisition, and we're always looking, kind of evaluating options, and seeing where there might be targets that would add either to our product portfolio to build that out, or something that's geographically desirable that would build out our footprint.

But it's not -- I wouldn't say today it's a must do. So I wouldn't say that we're out there saying we've got to get an acquisition done this year, but we certainly want to be opportunistic there and could do that if the right thing comes along.

Q: All right. Thanks very much.

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

Thanks, Mike.

Operator

Thank you. Your next question is coming from David Silver from CL King. David, your line is live. You may proceed.

Q: Yes, hi. Good morning.

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

Good morning, David.

Q: So it's a true statement that all of my top questions have been asked. However, that's never stopped me before. But just giving you a warning this might be a little scattershot, I mean I do have several issues I wanted to touch on. First would just be a clarification to some of Jugal's earlier comments, has to do with Precision Clad Strip and the transition, I guess, from Phase 1 in the back half of 2024 to Phase 2 maybe beginning early 2025.

So Jugal, I believe you talked about kind of inventory drawdowns at the customer, back half of this year and then the ramp-up of production from the new facility. Can you just clarify, is there a qualitatively or structurally different product that you're supplying from the new Precision Clad Strip unit. In other words, why would -- if the products were relatively similar, why would the customer need to adjust the legacy, I guess, inventory levels later in this year. Just -- maybe I'm missing something, but if you could just maybe discuss that transition as you discussed earlier. Thank you.

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

Yes. David, going back actually to about, I'm going to say, almost three years ago, probably when we started talking about this program, what we've indicated is that the customer has had, at that time, a product that they had in the marketplace. It used a technology that was not ours. We were not involved in that. The customer introduced a next-generation product. When they introduced the next-generation product then our technology.

So our Precision Clad we provide is what is used with that customer. So they have been, let's say, phasing out the older generation and phasing in the newer generation, right, and rolling that out around the world. And so as that ramp-up has happened and as they have continued to build inventory and continued to put a product in the marketplace, we have supplied to them. We have supplied to them from the legacy facility, and we've supplied to them from our new facility. And I think the -- and I'm really proud of our team for that. I mean, I think the fantastic work that our

team has done on the new facility in particular, for driving yield improvements, driving output improvements, I think has been a great support to the customer's launch and the rollout that they've been able to do.

I think all of that combined with just how are they managing it, the global rollout, they are really making sure that they've got the right levels of inventory now to support their rollout. And that's really kind of where it is, David. And so short term, a couple of quarter type of adjustments, but nothing of concern to us because this is a program that, as far as we know from the customer and we meet with the customer on a very frequent basis. They see this as a very successful program and one that will continue to be successful for the upcoming years.

Q: Okay, thank you for that. Very clear. I appreciate the longer-term perspective. Maybe a couple for Shelly here. But I was hoping you could just give us the final kind of determination from Materion's perspective on the production tax credit, I believe, or manufacturing credit that you're in line to receive as part of your participation, I guess, with critical materials. But you did kind of make a judgment earlier in 2023 that you reduced later in the year upon further clarification, I believe, from treasury on the particular details of how the credit would be calculated. So just level set us there, though, but are you at a point now where you can kind of confidently talk about the final, I guess expectations for that credit? And is there kind of a ballpark estimate for what that could add on an annual basis?

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

Yes. Thanks for that question, David. It's good to kind of give an update there. As you know, we're really excited about that credit as it gives us a reduction in our overall cost to produce high-purity beryllium products. When the act was first announced, the definition of production costs was a bit more broad and maybe less defined but did include material -- raw material costs. The update that came from the Treasury Department late last year used a different definition of production costs that would take raw materials out.

As you might recall, there was then a comment period and hearings and a number of other items that were being discussed before final guidance is given. We have not gotten any updates since

then. We did kind of look at what was said at these hearings and the different papers that were written on it, but we don't expect final guidance until later this year. So we have adjusted our approach really for that material item and are accruing at a more conservative rate. In fact, if you think about Q1, last year, we would have recorded about \$1 million more of a credit than what we recorded this year just based on a more conservative methodology. But we still believe we've taken a pretty middle-of-the-road approach and look forward to getting more clarity as the year progresses.

Q: Okay, thank you. And then maybe one more on the beryllium side, but I'm looking at the full-year 2024 guidance in -- sorry, Slide 15. And in particular, on the right-hand column, the mine development-new pit opening \$13 million. There's always been a smaller moderate amount in that column. But I was wondering, the new pit opening, is that designed to expand your capacity for the mineral that you require for your beryllium production? Or is this really a replacement? In other words, is the -- are you investing to prepare for anticipated growth? Or just is this maybe just the normal transition from a played-out portion of the mine to a new part of the mine?

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

Yes. Thanks for that. I'll start on that one. So as you know, we've got a mine out in Utah that we have dug various pits at really to obtain our raw material. So you've heard Jugal explain this process before. It's basically we have an open pit. We dig dirt and process it to get the beryllium products out of the ground. When we do that, we have to capitalize that really from an accounting treatment.

So I like to think of mine development as really raw material costs that are amortized over the period in which we use the raw material. So it's -- I wouldn't think of it as this is a different capital investment, but really, it is the size and the amount of the dig and the cost of that, which may be amortized over a different period or certainly more -- a higher quantity. We do see an uptick in our beryllium processing and our beryllium related sales and opportunities. So we're making sure that we're digging enough to have the products to support that demand. But really, what you see there is just something that goes on the balance sheet and amortizes off with production.

Q: Okay, very good. And last one for me, and I'll apologize in advance if I misquote Jugal on this. But the topic would be your expansions on the Electronic Materials side at Newton and Milwaukee. But one or two quarters ago, I believe, Jugal, you talked about -- I asked you about the timing of completion. Has it changed or whatnot. And again, I'm paraphrasing, but I believe you said, well, the slowdown in Electronic Materials demand that was happening then you thought it would jive very nicely with your planned expansions.

In other words, you wouldn't have to accelerate or anything, you could complete the expansions and upgrades at a desired pace. Based on your comments today about maybe a more drawn out recovery or rebound in the core Electronic Materials portfolio. How are you thinking about that, completing that expansion and the timing of the startup with customer demand? Any shift in that thinking?

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

No, I would say in whole, there is no shift in our thinking on that. We are continuing to progress on those expansions. We want to make sure that we're properly positioned from a capacity standpoint as the market recovery happens. And I think we'll just continue to work that, David, and make sure that all of our equipment is being installed, is being qualified with our various customers and then we're fully prepared to support them as the recovery happens in the various types of the segments of the semi market. So we -- I would say we're on track and continuing down that path.

Q: Okay, great. That's it for me. Appreciate all the color. Thank you.

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

Thanks, David.

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

Thanks, David.

Operator

Thank you. Your next question is coming from Dave Storms from Stonegate Capital Markets. Dave, your line is live. You may proceed.

Q: Good morning.

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

Good morning, Dave.

Q: Just hoping to get a feel for pacing. Last call, it was estimated that your added sales would be split roughly 45:55 between first half and second half. Does the anticipated step-up in Q2 maintain that ratio? Or should we adjust those expectations?

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

Yes. That's a good question. We spend a lot of time thinking about that and really look more at I guess think the cadence of our earnings. And we did talk last time about that being kind of a 45:55 split as we move through the year. With our soft Q1, of course, we had to kind of take

another look at what that might look like. We do see the significant step-up in Q2, but it will affect the balance of earnings where we'll probably be a little better than 40% in the first half.

When we think about Q2, we'll probably do a little bit better than Q2 of last year, but we're going to really see the meaningful step up in Q3 and Q4 to kind of hit the midpoint of our guide. So if you think 40:60, maybe 41:59, something like that, we're kind of in that zip code right now, at least how we're thinking about it.

Q: That's very helpful. Thank you. And Jugal, you mentioned with shares coming down -- excuse me, with volumes coming down, you're not really seeing share losses. Has that been because you've had to compete on price? Is there any upside to compete on price to maybe get some share gains? Basically, just how are you thinking about your pricing environment given the softer volumes?

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

Yes. Well, when I talk about the share situation, there's a number of different programs that we spoke about, beryllium and nickel is one of them, for example, and making sure that everyone understands that this is not a share issue, it's just simply an inventory destocking issue, right? And I think that's the case for a number of different things. Some of the declines that we have in Q1 in sales was simply due to operational launches. It wasn't due to order rates. It was -- we just weren't able to get the product out the door.

So I think it's a combination of things between those various items. Now when you look at pricing in general, certainly, there's always pricing pressure. I mean there's no doubt, right? Customers are always looking for ways that we can do things more efficiently and then pass on those benefits to them. So we continue to work that. We continue to drive operational excellence initiatives on our side so that any type of price down that we have to give to our customers, we're offsetting those with cost outs.

But in general, what I will tell you is if you look at our business over the last several years, we tend to be price positive. So what I mean by that is we tend to be more, I would say, on the price up than on the price downs across the board. And so -- and we'll continue to keep a focus on that. Our sales teams know very well as they work with our product teams on what the cost structure is that we have in our various businesses and how to properly price the product and making sure that we're looking at appropriate value-based pricing.

So pricing has been a key important enabler for us. I expect it to continue to be a key important enabler for us. And we're always, as I said, managing between what the pricing is and what the share is and how can we make sure that we're properly balancing both of those items.

Q: That's very helpful. Thank you for taking my questions and good luck for Q2.

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

Thank you.

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

Okay, thanks.

Operator

Thank you. We have reached the end of the question-and-answer session, and I will now turn the call over to Kyle Kelleher for closing remarks.

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

Thank you. This concludes our first quarter 2024 earnings call. A 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.