

21-Feb-2019

Aspen Aerogels, Inc. (ASPN)

Q4 2018 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good afternoon. My name is Rob, and I'll be your conference operator today. At this time, I would like to welcome everyone to the Aspen Aerogels Fourth Quarter 2018 Earnings Call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. [Operator Instructions] Thank you.

Mr. John Fairbanks, you may begin your conference.

John F. Fairbanks

Vice President, Chief Financial Officer & Treasurer, Aspen Aerogels, Inc.

Thanks, Rob. Good afternoon. Thank you for joining us for the Aspen Aerogels conference call. I'm John Fairbanks, Aspen's Chief Financial Officer. There're a few housekeeping items that I would like to address before turning the call over to Don Young, Aspen's President and CEO. Press release announcing Aspen's financial results and business developments, as well as a reconciliation of management's use of non-GAAP financial measures compared to the most applicable GAAP measures is available on the Investors Section of Aspen's website, www.aerogel.com.

Included in the press release is a summary statement of operation, a summary of balance sheet, a summary of key financial and operating statistics for the quarter and year ended December 31, 2018. In addition, the Investors Section of Aspen's website will contain an archived version of this webcast for approximately one year.

Please note that our discussion today will include forward-looking statements, including any statement regarding outlook, expectations, beliefs, projections, estimates, targets, prospects, business plans and any other statement that is not a historical fact, such statements are subject to risks and uncertainties.

Aspen Aerogels' actual results may differ materially from those expressed in these forward-looking statements. A list of factors that could affect the company's actual results can be found in Aspen's press release issued today, are discussed in more detail in the reports Aspen files with the SEC particularly in the company's most recent Annual Report on Form 10-K.

The company's press release issued today and filings with the SEC can also be found in the Investors Section of Aspen's website. Forward-looking statements made today represent the company's views as of today February 21, 2019. Aspen Aerogels disclaims any obligation to update these forward-looking statements to reflect future events or circumstances.

During this call, we will refer to non-GAAP financial measures including adjusted EBITDA. These financial measures are not prepared in accordance with U.S. generally accepted accounting principles or GAAP. These non-GAAP financial measures are not intended to be considered in isolation or as a substitute for results prepared in accordance with GAAP, definitions of and reconciliations of these non-GAAP financial measures to the most directly comparable GAAP financial measures. The discussion of why we present these non-GAAP financial measures is also available in today's press release.

I'll now turn the call over to Don Young, President and CEO of Aspen Aerogels.

Donald R. Young

President, Chief Executive Officer & Director, Aspen Aerogels, Inc.

Thank you. Good afternoon. Thank you for joining us for our Q4 2018 earnings call. I will start by providing comments about the business, our performance and our outlook. Next, John, will review our Q4 and fiscal 2018 financial performance and provide 2019 guidance. We will conclude the call with a Q&A session.

I plan to cover four topics in my prepared remarks. First, I will review Q4 and the year 2018 overall, including our three 2018 performance indicators. Second, I will describe the current commercial environment and introduce our performance indicators for 2019. Third, I will provide an update on our strategic relationship with BASF, which includes a second \$5 million prepayment that we received from BASF last month. And four, I will explain our strategy to address global opportunities for resource efficiency and sustainability through the leveraging of our aerogel technology platform.

At a summary level, our fourth quarter revenue trends were strong on a quarter-over-quarter basis. Total revenue of \$35.7 million was nearly 50% higher than Q3 and on par with a strong Q4 last year. Base revenue in Q4 grew 26% year-over-year to a record \$29.4 million. Project revenue was more than 15% of total revenue in Q4, and in line with our outlook at the time of our last earnings call. This fourth quarter project revenue was a significant improvement to the first three quarters of 2018, when projects represented less than 5% of total revenue. This Q4 momentum in both base and project revenue is key to our 2019 revenue outlook.

With respect to the full-year 2018, despite a strong finish in Q4, revenue was down 7% from 2017. Adjusted EBITDA lagged our expectations and was hampered throughout the year by repeated cost increases in our raw materials, especially in the silanes value chain. We continue to work to reduce our exposure to certain raw materials, and we have put in place an offsetting price increase for 2019, both of which we expect to help mitigate the issue.

I'll now turn to our three 2018 performance indicators. As a reminder, they are growing our base revenue, driving year-to-date growth in both revenue and adjusted EBITDA and expanding capacity through the EP20 initiative.

Base revenue is a good indicator of day-in and day-out maintenance and small scope project work, our version of a recurring revenue stream.

We initially targeted \$100 million in base revenue for 2018 from our 2017 level of \$88 million, and consistent with our goal of long-term annual growth in base revenue of more than 10%. At the time of our last earnings call, we projected that base revenue would grow between 5% and 10% in 2017 levels. Base revenue for the year grew by 6% to a record \$93 million.

The second performance indicator for 2018 relates to growth in year-to-date revenue and adjusted EBITDA as measured at the end of each quarter. During our last earnings call, we projected that we would not achieve growth in total revenue or adjusted EBITDA in 2018. However, we anticipated that solid Q4 revenue would set the stage for us to accomplish our 2019 objectives of revenue growth in excess of 20% and a return to positive adjusted EBITDA.

The strong Q4 base revenue in active and near-term project pipeline including subsea, LNG and petrochemical prospects and our 2019 price increase have strengthened our confidence in our ability to deliver on our 2019 objectives. In fact, we have already received \$12.4 million in subsea orders for delivery in 2019, which compares favorably to the \$8.2 million in subsea projects we delivered in all of 2018.

The third 2018 performance indicator relates the EP20 initiative. Our goal for EP20 remains to implement low capital cost, process technology improvements to increase the capacity in our East Providence, Rhode Island manufacturing facility by 20% by the end of 2020. The goal of EP20 translates to expanding our capacity from approximately 50 million square feet to 60 million square feet of aerogel blankets per year. Upon completing EP20, we project that our revenue capacity will approach \$200 million and adjusted EBITDA has the potential to reach the range of \$28 million to \$35 million per year.

We made significant progress in 2018. We increased our manufacturing capacity to approximately 55 million square feet or approximately \$180 million by the end of 2018, well on our way to our \$200 million EP20 target. We plan to focus our resources in 2019 on reducing product variable cost and driving profitability. We expect to complete the remaining EP20 capacity expansion projects during 2020.

My second topic today is to provide an overview of the anticipated commercial environment for 2019 and to introduce our 2019 performance indicators. We are confident that the commercial environment and our investment in sales personnel, new products, and enhanced marketing programs will support our projected revenue growth of 20% or more in 2019.

We expect to benefit from continued volume growth in our day-in and day-out maintenance work and net positive impact from our 2019 price increase, and a more robust and near-term project pipeline.

We believe that project revenue as a percentage of total revenue will continue to improve in 2019 and 2020 with anticipated project wins in the subsea, LNG and petrochemical markets. While we do not expect project work to reach historical levels in 2019, we do expect that projects will account for 20% of total revenue for the year. This change signals a strong improvement in market trends compared to recent years and is the basis for our 2019 projection for revenue growth in excess of 20% and a return to positive adjusted EBITDA for the full-year.

Our three performance indicators for 2019 will be first, 20% revenue growth and positive adjusted EBITDA; second, project revenue comprising 20% of total revenue; and third, the formation of an additional partnership

with a leading company aimed at leveraging our aerogel technology platform into a new market. We will review our progress on these three performance indicators during our quarterly earnings calls.

The third topic today relates to our partnership with BASF. In January, we announced an amendment to our supply agreement with BASF that expands our strategic relationship to include the initial commercialization of next-generation, high-performance, non-combustible building products developed under our joint development agreement. In addition, the amendment resulted in a second \$5 million prepayment that we received during January.

The enhanced supply agreement provides additional support for our commercial and technical efforts and have strengthened our financial position. Our partnership with BASF is important to Aspen and provides a model for how we might monetize our aerogel technology platform in new markets with other elite partners.

The fourth and final topic before I turn it over to John is to review our strategy which is to leverage our aerogel technology platform across our core adjacent and new markets. There are two key elements to the strategy. The first element is to grow our core and adjacent markets to fill the East Providence manufacturing facility, including the expanded capacity from the EP20 initiative in order to create a business with potential annual revenue approaching \$200 million and potential adjusted EBITDA of between \$28 million and \$35 million per year.

The second element of the strategy is to leverage our aerogel technology platform by creating additional new businesses. We have jumpstarted the process with our promise in building materials work with BASF as we begin to penetrate our first commercial market outside of energy infrastructure. Our products with BASF are high-performance and non-combustible, a perfect combination for a focus on common sense building safety and energy efficiency. As I said, we see the technical, commercial and financial partnership that we have with BASF as a template that we want to replicate with other elite partners as we leverage our aerogels technology platform into additional new markets.

We believe the key to maximizing long-term shareholder returns is to build a strong energy infrastructure business that generates cash to invest and realizing the substantial potential in our core and adjacent markets and to invest in business opportunities in new markets, which can lead to significant breakout value. The goal is to unlock that potential and to reset meaningfully the valuation of the company.

In summary, we are focused on growing revenue 20% or more in 2019, delivering positive adjusted EBITDA and having project work reemerged to comprise 20% of our total revenue in 2019. We believe that by accomplishing these objectives and by implementing profit enhancing process technology advancements, we will be in a position to generate in 2020 significant growth in adjusted EBITDA. The drive to profitability is our imperative 2019.

Now, I'll turn the call over to John for a review of our financial results.

John F. Fairbanks

Vice President, Chief Financial Officer & Treasurer, Aspen Aerogels, Inc.

Thanks, Don. Let's start by running through our reported financial results for the fourth quarter and fiscal 2018 at a summary level. Fourth quarter total revenue declined by 2% to \$35.7 million from \$36.4 million in the fourth quarter of 2017.

Fourth quarter net loss was \$14.1 million or \$0.59 per share compared to a net loss of \$1.7 million or \$0.07 per share last year. Fourth quarter adjusted EBITDA was negative \$3.2 million compared to positive \$2.2 million a year ago. We define adjusted EBITDA as net income or loss before interest, taxes, depreciation, amortization,

stock-based compensation expense and other items that we do not believe are indicative of our core operating performance.

Our net loss and adjusted EBITDA for the fourth quarter reflected a \$2.8 million reserve for uncollectable accounts receivable related to revenue we booked during 2017 for a refinery project in Brazil.

In addition, our net loss for the quarter reflected a \$7.4 million impairment charge, the write off of pre-construction costs for the Statesboro, Georgia facility. Statesboro asset write-off had no impact on adjusted EBITDA during the period.

For the full year, total revenue declined 7% to \$104.4 million. Net loss was \$34.4 million or \$1.45 per share in 2018 versus a net loss with \$19.3 million or \$0.83 per share last year.

Adjusted EBITDA for the year was negative \$11.5 million compared to negative \$3.3 million a year ago. Again, net loss for 2018 reflected both the \$2.8 million reserve for uncollectable accounts receivable, and the \$7.4 million write-off of the Statesboro assets. While adjusted EBITDA for the year only reflected the \$2.8 million accounts receivable reserve.

I'll now provide additional detail on the components of our results. First, I'll discuss revenue. Fourth quarter total revenue was comprised of product revenue of \$35.1 million and research services revenue of \$534,000. For the year, total revenue is comprised of product revenue of \$102.1 million and research services revenue of \$2.2 million.

During the fourth quarter, total revenue decreased by \$700,000 or 2% to \$35.7 million versus \$36.4 million last year. This decline in fourth quarter total revenue was driven by a \$6.7 million or 54% decrease in project revenue due principally to the conclusion of the South Asia petrochemical project. This decline was largely offset by a \$6 million or 26% increase in base revenue led by strong growth in our petrochemical and refinery markets, particularly in Asia.

During the fourth quarter, total shipments decreased by 1% to 11.8 million square feet of aerogel blankets, and our average selling price decreased by 1%, \$2.99 per square foot, principally due to a modest decrease in the mix of higher price subsea products this year.

For the full year, total revenue decreased by \$7.3 million or 7% versus 2017. This decline in total revenue was driven by \$12.4 million or 58% decrease in project revenue in the subsea market and due to the conclusion of the South Asia petrochemical project, offset in part by a \$5.4 million or 6% increase in base revenue led by growth in our Asian petrochemical and refinery markets, and in the building materials market.

For 2018, total shipments decreased by 8% to 34.4 million square feet, while our average selling price increased by 1% versus 2017 \$2.96 per square foot. This increase in ASP reflected the favorable impact of our 2018 price increase partially offset by a decrease in the mix of our higher price subsea products.

Our 2019 outlook anticipates total revenue in the range of \$126 million to \$134 million, representing growth of between 20% and 28% versus 2018. This projected growth in 2019 is based on our expectation of continued volume growth in our core petrochemical and refinery markets and in the building materials market. An increase in project revenue, particularly in the subsea and LNG markets and an increase in our average selling price.

We project that our average selling price for the year will increase by approximately 10% to \$3.25 per square foot plus or minus \$0.05. The increase in ASP is driven by the price increase we enacted in January 2019 to offset the significant increase in raw material costs experienced during 2018.

Next, I'll discuss gross profit. Gross profit was \$5.6 million or 16% of revenue during the fourth quarter of 2018 versus \$7.9 million or 22% of revenue last year. Decrease in fourth quarter gross profit of \$2.3 million and gross margin of six percentage points was driven principally by the increased cost of raw materials, and to a lesser extent the decline in shipment volume and the decrease in selling price.

As a reminder, we instituted a price increase in January 2019 that we project will increase our average selling prices by approximately 10% in 2019. We estimate that if our 2019 price increase had been in full effect for the fourth quarter of 2018, [ph] we would've (00:21:19) generated an additional \$3 million of gross profit – gross margin in the mid-20s.

For the year, gross profit was \$12.7 million or 12.1% of revenue versus \$18.7 million or 16.7% of revenue last year. Year-over-year decrease in 2018 gross profit of \$6 million and gross margin of five percentage points was driven principally by the decline in shipment volume, the increased cost of raw materials, and an unfavorable mix of products sold.

Looking forward to 2019, we expect gross margin to be approximately 20% for the full year, as in past year's quarterly gross margins could run from the [ph] mid-18s (00:22:07) to the mid-20s depending on quarterly revenue levels.

Expected increase in gross profit and gross margin is driven by the combination of a projected increase in revenue, output, and capacity utilization, and the impact of our 2019 price increase. This gross margin expectation is included in our 2019 guidance.

Next, I'll discuss operating expenses. Fourth quarter operating expenses were \$19.5 million versus \$9.4 million last year, it included the \$7.4 million impairment charge for the write-off of the pre-construction cost of the Statesboro, Georgia facility, and the \$2.8 million reserve for uncollectible accounts receivable associated with the Brazilian project. Write-off of the Statesboro cost was based principally on our determination that our manufacturing technology improvements over the past three years have made the existing engineering designs to the second manufacturing facility increasingly obsolete.

The write-off of the accounts receivable reflects the likely bankruptcy of Brazilian engineering firm that purchased material from us in 2017 for a Petrobras refinery project. Excluding the two write-offs, our fourth quarter operating expenses were flat to last year at \$9.4 million.

For the full year, operating expenses were \$46.6 million versus \$37.8 million in 2017. Again, excluding the two write-offs, operating expenses declined by \$1.4 million or 4% to \$36.4 million during the year. Looking forward, our 2019 guidance includes our expectation that operating expenses excluding the impact of the 2018 write-offs will grow by approximately 10% to slightly more than \$40 million for the year.

This projected operating expense increase reflects the annualized impact of our investment in sales and research personnel and expense during 2018 to drive growth in our energy infrastructure business and to develop breakout opportunities in new markets, and a budgeted increase in incentive compensation.

Next, I will discuss our balance sheet and cash flow for 2018. Cash used in operations is \$8.7 million reflected our negative adjusted EBITDA of \$11.5 million, partially offset by \$2.8 million of cash provided by reduced investment in working capital during the year. Capital expenditures for the year totaled \$3.6 million, down from \$6.1 million in 2017.

During the year, we also received pre-payments from BASF in the aggregate of \$5 million. We ended 2018 with \$3.3 million of cash, net current assets of \$14.2 million, \$4.2 million on our revolving credit facility and shareholders' equity of \$70.3 million. And importantly we had access to an additional \$10.3 million available under our revolving credit facility at year-end.

I'll now turn to our full year financial outlook for 2019. Total revenue is expected to range between \$126 million and \$134 million. Net loss is expected to range between \$12.7 million and \$14.7 million. Adjusted EBITDA is expected to range between breakeven and positive \$2 million. EPS is expected to range between a loss of \$0.53 and a loss of \$0.61 per share. This EPS guidance assumes a weighted average of 24.1 million shares outstanding for the year. This 2019 outlook also assumes depreciation and amortization of \$10.2 million, stock-based compensation of \$3.9 million, interest expense of \$600,000, a patent enforcement cost of \$800,000.

For the full year, we expect the gross margin of approximately 20%, an average selling price of \$3.25 per square foot plus or minus \$0.05.

During 2019, we will continue our focus on controlling capital expenditures, strengthen our balance sheet and to maintain financial flexibility. Our 2019 capital budget of \$1.5 million is comprised of \$1 million of maintenance related capital projects and \$0.5 million to complete a few EP20 projects that we initiated in 2018.

Turning to cash at an aggregate level, within the context of the adjusted EBITDA range, set out in our 2019 full year outlook, we expect to exit 2019 with between \$3 million and \$7 million of cash on hand and no outstanding borrowings under our revolving credit facility.

As Don mentioned, we've amended our supply agreement with BASF, received \$5 million in an additional pre-payment January 2019 to help support the development of next-generation building products and associated manufacturing technologies. This \$5 million pre-payment is included in our 2019 year-end cash guidance.

Although we don't plan to provide specific quarterly guidance on a routine basis, we think it's important from time-to-time to provide our investors the general view to our expectations during the year. During the first quarter of 2019, we expect to achieve double-digit volume growth in terms of square feet shift versus the first quarter of 2018. However, we expect our average selling price for the quarter to remain on par with our 2018 average of \$2.96 per square foot and fall below our \$3.25 per square foot expectations for the full-year 2019.

This first quarter price expectation reflects the impact of orders we carry from Q4 2018 into Q1 2019, both in subsea projects and in our base business, which we booked with 2018 pricing. As a result of this lower pricing, we expect that our first quarter 2019 profit profile will remain in line with 2018 levels. However, we expect to deliver strong year-over-year growth in volume, average selling price, revenue, gross profit and adjusted EBITDA over the final three quarters of the year and to achieve our full-year 2019 outlook.

I'll now turn the call back to Rob for Q&A.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] And your first question comes from the line of Eric Stine from Craig-Hallum. Your line is open.

Eric Stine

Analyst, Craig-Hallum Capital Group LLC

Hi, Don. Hi, John.

Q

John F. Fairbanks

Vice President, Chief Financial Officer & Treasurer, Aspen Aerogels, Inc.

Hi, Eric.

A

Eric Stine

Analyst, Craig-Hallum Capital Group LLC

Hey, maybe just to start with LNG, you provided some commentary there on the pipeline. Just curious, I mean, maybe some context, is that something where you're seeing more projects, are you seeing more content within projects or how does it break down between the two?

Q

Donald R. Young

President, Chief Executive Officer & Director, Aspen Aerogels, Inc.

We are – I would characterize it this way Eric, that we've had LNG projects in our pipeline, and they have become more near-term, and so we just have a variety of projects that are more near-term and we believe that one or two of them will fall into 2019 and have a big impact.

A

Eric Stine

Analyst, Craig-Hallum Capital Group LLC

Got it. And, I mean, how should we think about that, I guess in the context of this guidance, just doing the math you called out that subsea work that, I think you're at \$12.5 million for 2019 already, so you're almost half way to your project mix goal. So that doesn't – I mean you're going to get more orders in subsea, so that doesn't leave a whole lot of what needs to be filled in by LNG. I mean, is that – should we think of these as upside or are you trying to just build in the fact that the timing is very difficult to call?

Q

Donald R. Young

President, Chief Executive Officer & Director, Aspen Aerogels, Inc.

I think, we're being careful with your latter point there, and make sure that we set expectations that we can meet or beat. And so I would think of the LNG revenue as important to meeting our goals throughout the year. And some of these projects are rather large and will span from not only 2019, but into 2020 as well, and [ph] we really report (00:31:40) that year also. So these are pretty good sized projects that we're talking about, and I talked about...

A

Eric Stine

Analyst, Craig-Hallum Capital Group LLC

Got it.

Q

Donald R. Young

President, Chief Executive Officer & Director, Aspen Aerogels, Inc.

A

...we've done maintenance work for a lots of different facilities around the world, three dozen or so. And as you know, Eric, we did the three projects towards the end of 2017, \$3 million, \$5 million and \$8 million in size. And we're building on that momentum and we think that will come to fruition for us here in 2019 and 2020. But your math is basically right. We've got some more work to do to hit that 20% of total, and we've got a good shot at doing it.

Eric Stine

Analyst, Craig-Hallum Capital Group LLC

Q

Yeah. Okay. Thanks for that. And then just on subsea, in that, you gave the order number or the number you've got both for 2019, I mean when you think about the recovery that you're seeing now how does that compare to past recoveries in that market? And I mean I would assume the strength you're seeing now that's something you expect to persist throughout the year?

Donald R. Young

President, Chief Executive Officer & Director, Aspen Aerogels, Inc.

A

We think that – this is the one area where we tend to have a little visibility on our projects. We get the purchase order in advance, and then typically deliver a quarter or two later. And so for the way I would say it is, we've got solid projects in hand as the \$12.4 million number suggest, we anticipate getting another order or two for this year. But the pipeline is strong and we continue to believe that we'll continue to build on that business into 2020 and even 2021. So that market has a nice visibility for us right now and there is a reason for optimism.

Eric Stine

Analyst, Craig-Hallum Capital Group LLC

Q

Got it, okay. And maybe last one for me just turn into power gen, maybe just an update on that product. It seems like it is tracking the same as some of your other applications have in the past, so kind of where do you view that application as we sit here today?

Donald R. Young

President, Chief Executive Officer & Director, Aspen Aerogels, Inc.

A

Yeah, we have continued to win a series of smaller orders, kind of maintenance and small scope work. And as you suggested in your question that's the pattern dating all the way back to 2007, 2008, and 2009 when we introduced Pyrogel and Cryogel into refinery and petrochemical and LNG business, we started off doing smaller scope maintenance work mostly and smaller scope project work, and that of course we built into a much larger size projects over time. The power market is playing out exactly the same way. Our revenue mix there, there's no one order that's been spectacular, but there are – we're seeing green shoots all around the world.

Eric Stine

Analyst, Craig-Hallum Capital Group LLC

Q

Okay. Thank you.

Donald R. Young

President, Chief Executive Officer & Director, Aspen Aerogels, Inc.

A

Thanks Eric.

Operator: And your next question comes from the line of Chip Moore from Canaccord. Your line is open.

Chip Moore

Analyst, Canaccord Genuity LLC

Hey Don, hey John, how are you guys doing?

Donald R. Young

President, Chief Executive Officer & Director, Aspen Aerogels, Inc.

Good. How are you, Chip?

Chip Moore

Analyst, Canaccord Genuity LLC

Good. I guess following up on your commentary around the strengthening pipeline and LNG potential a little early to talk about 2020, but it sounds like your tone is a little more optimistic. [ph] As a (00:35:15) 20% growth rate something we should think about is being sustainable into 2020 when you combine that with the maintenance work?

Donald R. Young

President, Chief Executive Officer & Director, Aspen Aerogels, Inc.

Yeah. So the way I would think about the pieces of that, we've been able to grow our day-in and day-out business, really it's dating back to 2008 in good times and bad times. And I believe that we'll continue to do that in 2019 and 2020 and 2021. Those numbers have been – if you look back over time, have been double-digit percentages throughout that period of time. And so the project work what we're seeing as more diversity in project work, a lot of our project work used to be really driven frankly by sort of crude prices and that drove a lot of that early project work that we had. And we're still seeing opportunities there. So we'll continue to build on that.

But the natural gas – ample supply of natural gas is driving a different set of projects for us, which of course there's been a lot written about LNG, and we're playing really well into that trend. But I would also say we're seeing things on the petrochemical side that are using natural gas as feedstock and – low cost natural gas as feedstock. And so we're seeing broader set of projects in warm markets across our geographies, and it gives us confidence that – and this is something that's not just set up here for 2019, but we think there's nice visibility in 2019, 2020 and 2021.

And I'd just remind you that when we grew significantly from 2008 through 2015, project revenue was 40%, 45%, even 50% in any given year of our total revenue, and as I said in my commentary that number in the first three quarters of 2018 was around 5%, in Q4 it was 15%, and here in 2019 we're projecting it to be 20%. Those are relatively modest numbers from – even from – any historical sorts of – for our history at least going back to 2008. So we think we have room to grow on the project side as well. As of just marked against total revenue. So we see a lot – we see a lot of opportunity for us to grow our maintenance business and to pile projects on top of it, really put together a growth track here in the 2019, 2020 and 2021. We've...

Chip Moore

Analyst, Canaccord Genuity LLC

Got it. Got it...

Donald R. Young

President, Chief Executive Officer & Director, Aspen Aerogels, Inc.

A

...we still expect [indiscernible] (00:38:20) Chip, using EP20, and we did it with the expectation that the investments that we're making both in the facility, but also in our sales and marketing team and some of the research and development work that we've done to make those sales more profitable. Again, we think those are good investments that will pay dividends in 2019, 2020, and 2021.

Chip Moore

Analyst, Canaccord Genuity LLC

Q

Absolutely. Maybe if we turn to BASF with the prepayment we can get a little more update on commercialization and building materials and development of future products where that stands, and then you did talk about hopefully signing up someone new this year. Maybe you can expand on that a little bit in terms of progress you had in terms of negotiations already?

Donald R. Young

President, Chief Executive Officer & Director, Aspen Aerogels, Inc.

A

Sure. So BASF, again just has been a terrific partner for us, and we – I believe we've said in Q4, we received technical approvals in the European market for our first generation product which really opens the market to our sales team and much more probably BASF sales team to begin moving product of that first generation. And so we anticipate that playing a greater and greater role in 2019 and beyond.

A lot of this expanded supply agreement that we had in the second \$5 million prepayment, was around the second generation product as well, which we're very excited about, it has great application, no doubt in the building materials area. We believe it also has application in some other markets as well. It's a really interesting product form, and it's got great characteristics in terms of thermal and non-combustibility. So we're really excited with our partnership with BASF and that \$5 million obviously is a shot in the arm for us both in terms of accelerating the work and just supporting our financial position. So that's been great. Go ahead, John. Yeah.

John F. Fairbanks

Vice President, Chief Financial Officer & Treasurer, Aspen Aerogels, Inc.

A

The new product we see it's really complementary to the existing Spaceloft A2, SLENTEX product in the building materials market. I just want to emphasize the point that Don made that it will help us to open up applications within other markets for that product form as well. So we are – we and BASF are very excited about the potential of that new product.

Donald R. Young

President, Chief Executive Officer & Director, Aspen Aerogels, Inc.

A

And then in terms of new partnerships, we have a long history of working in government research programs on other forms of aerogel, and we've said before we're very focused in areas around energy storage, around filtration, and we've advanced that work, we're working with two universities right now to continue to move that work forward. There are a handful of very logical partners in these areas and we have conversations going on with them all on these topics. So, as I said in my notes that BASF model, if you will, technical, commercial, financial, monetizing our aerogel technology platform, those are all sort of the key elements that we expect to put forth later this year with one of those good companies.

Chip Moore

Analyst, Canaccord Genuity LLC

Got it. And one more on the price increase, I think you said it was in January, has that been successfully implemented, and what's your confidence that that gets pushed through?

Donald R. Young

President, Chief Executive Officer & Director, Aspen Aerogels, Inc.

Yeah, we're very confident that the 10% marker that John talked about taking our ASPs from the very, very high or just shy of \$3 to \$3.25 plus or minus nickel. We're very confident about that for the year Chip. The price increase ranged frankly across our product mix, across our geographies, et cetera, and so we're – when you boil it all down we're very confident about the 10% sticking for the year.

Chip Moore

Analyst, Canaccord Genuity LLC

Understood. And sorry, one last one on the bankruptcy in Brazil there, the [ph] AR issue (00:43:02), is that sort of one-off situation or any other outstanding collections that we should be concerned about?

John F. Fairbanks

Vice President, Chief Financial Officer & Treasurer, Aspen Aerogels, Inc.

Nothing. It was – it really was a one-off for us, highly unusual for us in our history and it was in Brazil, Brazil is a tough country at present to do business in, and we just got it, it was a Petrobras project, [ph] we felt it (00:43:30) was well capitalized, but the contractor just ran into financial difficulties. We actually won a law suit against them, any payments to Petrobras was making would be reverted to a court account on our behalf, but ultimately the agreement that this contractor have with Petrobras was terminated and we believe that they're likely to go bankrupt. So that's why we reserved it, but we have no other exposures [ph] to be coming (00:43:59).

Chip Moore

Analyst, Canaccord Genuity LLC

Great. All right. Thanks a lot guys.

Operator: And your next question comes from the line of Sean Hannan from Needham & Co. Your line is open.

Sean K. F. Hannan

Analyst, Needham & Co. LLC

Yeah. Thanks. Good evening, folks. So first question, I just want to see if we could get – maybe I missed this, just a little bit of detail on that impairment specifically what should we be thinking about, what is behind those numbers? And what should folks think about Georgia here going forward? Obviously we move forward EP20, and we've been on that whole track, and that's very clear, but is everything regarding Georgia is it completely dead and off the table now?

John F. Fairbanks

Vice President, Chief Financial Officer & Treasurer, Aspen Aerogels, Inc.

So Sean, I'll go back [indiscernible] (00:44:47) just to provide a little color. During 2016, we completed the design of that second financing...

Sean K. F. Hannan

Analyst, Needham & Co. LLC

Yeah.

Q

John F. Fairbanks

Vice President, Chief Financial Officer & Treasurer, Aspen Aerogels, Inc.

... [indiscernible] (00:44:54) Georgia, right. And we had an incentive package from a local government included free land, and back in 2016 we delayed that project, but we had – those engineering designs had cost us about \$7.4 million. And so then during the fourth quarter...

A

Sean K. F. Hannan

Analyst, Needham & Co. LLC

Okay. That's all engineering design work dollars, okay?

Q

John F. Fairbanks

Vice President, Chief Financial Officer & Treasurer, Aspen Aerogels, Inc.

...that's all it is. And since no – and essentially it's the full value. So in 2018, we decided that we would – we were unlikely to use those designs going forward. At first, the local government, our contracts with them got to the point, they had a right to terminate the incentive package unless we broke ground by February 2019, we obviously did not...

A

Sean K. F. Hannan

Analyst, Needham & Co. LLC

Right.

Q

John F. Fairbanks

Vice President, Chief Financial Officer & Treasurer, Aspen Aerogels, Inc.

... [indiscernible] (00:45:38). And so they indicated they were going to terminate the incentives and we wouldn't have rights to the land. And so some of the value and the designs was associated with the plot or land, it was on. And secondly, our EP20 related capacity gains have expanded the timeframe in which we expect demand will exceed capacity, and then pushed out the need for that second facility. And then finally...

A

Sean K. F. Hannan

Analyst, Needham & Co. LLC

Right.

Q

John F. Fairbanks

Vice President, Chief Financial Officer & Treasurer, Aspen Aerogels, Inc.

...I think probably most importantly, our cumulative manufacturing technology – process technology advancements since 2016 had been significant, and we continue to make advancements. Over the next couple of years, we expect for our technology to advance further working on it. We think we're putting quite a bit of investment into it.

A

And so from that perspective it's making the technology that underlies the old plans increasingly obsolete. And so when you look at it from those three factors, it just made us – come to the decision in the fourth quarter that we just were not going to use going forward.

Donald R. Young

President, Chief Executive Officer & Director, Aspen Aerogels, Inc.

Sean, I would just...

Sean K. F. Hannan

Analyst, Needham & Co. LLC

Okay.

Donald R. Young

President, Chief Executive Officer & Director, Aspen Aerogels, Inc.

...I would just add to that very good description. We are – and really just to build on that, we're focusing very hard on low capital process technology improvements, not only in our existing plant, but in the plants of the future as well. We've made some really interesting advancements in that area. So that's one thing.

The second thing is, and it's consistent with the low capital sort of version here is, we're really working hard in our partnerships, and so we'll see how those partnerships play out, not only in terms of product development, distribution and those sorts of ideas, but also next lines of capacity. So there's a lot on the table here, but we're very focused on being low capital and driving to profitability, that's what we're all about right now we need to do that. And so that's our focus.

Sean K. F. Hannan

Analyst, Needham & Co. LLC

[ph] Helpful (00:47:49). Okay. And actually, Don, on that note as we are looking to focus more on profitability, that brings you to another question for you and John is, as I think about the revenue opportunity for 2019, that really kind of gets you at a high number versus some historical levels. But when I look at how we flow through the EBITDA, we're certainly not realizing what we had realized say back in 2014, 2015, 2016. And I'm just kind of looking at this quickly, but it's really an OpEx factor, it is the gross margins we're looking to be tracking to a better number for this year. I recognize that sales and marketing is a conscious effort to have more dollars in that. But in the aggregate, the OpEx number seems to be a fair bit higher than I think a few of us may have – would've expected to get to for that type of a revenue number. How should we think about the OpEx here? I mean is there is this the right type of number, is the G&A number appropriate where it is? What are some opportunities we could have in order to perhaps become a little bit more driving in that EBITDA. Just wanted to get some perspective on that?

<A – [002WYB-E]John Fairbanks – Aspen Aerogels, Inc.> Yeah. Actually, Sean, this is really actually two pieces, and we acknowledge that our operating expenses are up since 2015, 2016, 2017 levels. And those are conscious investments in driving sales, because that's clearly been what's been missing from the mix over the past few years. So, you hit the nail on the head.

And we have added about \$3 million to research and development over that 2015 to 2019 time period as well. And that's once again conscious decision to invest in our aerogel technology platform, and ultimately to open up new markets. We'll take those off the tables, because those are conscious investments.

One of the other pieces though with this increase in our raw material costs, which we've taken with the price increase, taken the efforts to mitigate. It actually changed our breakeven, essentially our material costs went up by effectively 10%, our revenue went up by 10%, has changed the old dynamic that we used to talk about. We talk about our breakeven being about a hundred and N million dollars and our breakeven now is essentially 10% higher than that, about \$30 million to \$32 million – \$32.5 million depending on mix. But lot of that is because of the increase in raw material cost and increase in pricing, it's just changed the old algebra that I think that you're familiar with. But ultimately, we still will be able when we fill that East Providence plant, that \$200 million revenue, we can still generate between \$28 million, \$35 million of EBITDA, so the dollars haven't changed, but the percentage [indiscernible] (00:51:10).

Sean K. F. Hannan

Analyst, Needham & Co. LLC

Okay.

Donald R. Young

President, Chief Executive Officer & Director, Aspen Aerogels, Inc.

And I would also Sean – I would just add, I talked about the EP20, and we made good progress in our first year, and we'll complete the capacity expansion of that next year in 2020. We're very focused here in 2019 on what I was referring to as profit enhancing process technology advancements. And we believe there are efficiencies that we can bring to our manufacturing technology, to our bill of materials that drive profitability to numbers that would be, I think more satisfying to you and to us.

Sean K. F. Hannan

Analyst, Needham & Co. LLC

Okay. Last question here, if I think about the core work that you do and then the project work, and Don you would hit on this a few times in the conversation. Prior years, early years project was a really big percentage in some of those growth years, recently that had come off [ph] table your quotes has been (00:52:27) coming up a fair bit. We're now looking at about 20%-ish projects work in 2019. What should the model be, because clearly there's a lot of volatility that you can get in that project work? Can you lend us a perspective around what do you think it should be? Where are your comfort levels with – for a given range? Help us provide some perspective as you implement strategy and tactically execute in the balance of nature of your revenues?

Donald R. Young

President, Chief Executive Officer & Director, Aspen Aerogels, Inc.

Yes. So for a seven-year period we were in the 40% plus range of project revenue. And if you look at some similar companies to ours I've talked about Thermon before, not exactly our business but works to the same kinds of factors that we do.

They're roughly 50:50 between maintenance and project work themselves. I believe that we will continue to move to our historical norms in 2020 and 2021. We're already on that track here in 2019, and I also know that we need to have more consistency in our project success here. Just winning a big project and have it work through over the course of two quarters or four quarters or even six quarters that's not good enough.

We need to have consistent project wins, and so we're really doing two things about that, one is over a year ago we changed the organization to include a very dedicated team to project wins and that's about getting into the specifications very early in these – in the process and taking advantage of our \$800 million of Pyrogel and

Cryogel installed in these kinds of facilities using them as case studies and winning projects day-in and day-out. So it's a consistent part of our revenue.

And the second thing and I mentioned this earlier in the Q&A, we are pretty crude or crude oil price oriented in our early – earliest days, and I think we have more breadth now with natural gas not only on the LNG side, but also on the petrochemical side. So the opportunities we have to win projects over the course of many years is much greater. So we're targeting 20% this year. I believe that number on an ongoing basis that a third of our revenue year-in and year-out should be in that range, a third of our revenue, that makes a lot of sense to me. And, yeah, I think some years it should be. It will be a little higher than that, and some years it will be a little lower than that, but we cannot have it be 5% or 10% or 15% of our revenue, it needs to get into that. One-third of our revenue coming from projects year-in and year-out. And I believe we've got the ability to do that.

Sean K. F. Hannan

Analyst, Needham & Co. LLC

Okay. All right. Thanks so much. Thanks for addressing the questions here.

Donald R. Young

President, Chief Executive Officer & Director, Aspen Aerogels, Inc.

Thank you, Sean.

John F. Fairbanks

Vice President, Chief Financial Officer & Treasurer, Aspen Aerogels, Inc.

Thanks, Sean.

Operator: And there are no further questions at this time. I will turn the call back over to Mr. Don Young.

Donald R. Young

President, Chief Executive Officer & Director, Aspen Aerogels, Inc.

Thank you, Rob. We appreciate your interest in Aspen Aerogels. We look forward to reporting to you our first quarter 2019 results in early May 2019. Have a good evening.

Operator: This concludes today's conference call. You may now disconnect.

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