



Aspen Aerogels, Inc.

Third Quarter 2017 Earnings Conference Call

November 2, 2017

C O R P O R A T E P A R T I C I P A N T S

John Fairbanks, *Vice President, Chief Financial Officer and Treasurer*

Don Young, *President and Chief Executive Officer*

C O N F E R E N C E C A L L P A R T I C I P A N T S

Eric Stine, *Craig-Hallum Capital Group, LLC*

Chip Moore, *Canaccord Genuity Group, Inc.*

Ethan Potasnick, *Needham & Company*

P R E S E N T A T I O N

Operator:

Good afternoon. My name is Jesse and I will be your conference operator today. At this time, I would like to welcome everyone to the Aspen Aerogels' Q3 2017 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. If you would like to ask a question during this time, simply press star, then the number one on your telephone keypad. If you would like to withdraw your question, press the pound key. Thank you.

John Fairbanks, you may begin your conference.

John Fairbanks:

Good afternoon. Thank you for joining us for the Aspen Aerogels' conference call. I'm John Fairbanks, Aspen's Chief Financial Officer. There are a few housekeeping items that I would like to address before turning the call over to Don Young, Aspen's President and CEO. The 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 operations, a summary balance sheet and a summary of key financial and operating statistics for the quarter ended September 30, 2017. In addition, the Investors section of Aspen's website will contain an archived version of this webcast for approximately one year.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, and such statements are subject to risks and uncertainty. 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 and 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.

The forward-looking statements made today represents the Company's views as of today, November 2nd, 2017. 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. The definitions of and reconciliations of these non-GAAP financial measures to the most directly comparable GAAP financial measures and a discussion of why we present these non-GAAP financial measures is also available in today's press release.

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

Donald Young:

Thank you, John. Good afternoon. Thank you for joining us for our Q3 2017 earnings call. I will start by providing comments about the business and our performance. Next, John will present financial details for Q3 and year-to-date 2017, and comment on our guidance for the remainder of the year. We will conclude the call with a Q&A session.

I plan to cover four topics in my prepared remarks. First, I will comment on our recent victory in our patent enforcement action that the United States International Trade Commission, the ITC. Second, I will review the three important cases related to the performance of our business that we believe will mark 2017 as a successful year. Third, I will discuss the current commercial environment, including our market outlook for the remainder of 2017. And fourth, I will reiterate our strategy and describe the longer term scope of our opportunity.

As we announced in June 2016, we took a series of legal actions to assert our rights against companies that infringe our intellectual property. We filed a complaint with the ITC alleging that two China-based companies engaged in unfair trade practices by selling Aerogel products in the United States that infringed or were manufactured by processes that infringe several of our patents.

Based on our complaint, the ITC instituted an investigation and conducted a hearing. While the ITC was deliberating, one of the defendants challenged the validity of four of our patents at the United States Patent and Trademark office. The defendants challenged to the validity of the patents were denied by the U.S. PTO, a very favorable outcome for Aspen.

Then on September 29, the judge overseeing the ITC investigation found that all patent claims that we asserted were valid and infringed by each of the two China-based companies. The judge recommended a limited exclusion order as a remedy to prevent the importation of infringing Aerogel products into the United States. We anticipate a final determination on the violation and remedy to be issued by the full ITC Commission by the end of January 2018.

This determination by the ITC validates the strength of (inaudible) portfolio protecting our Aerogel technology platform.

Our strategy is to leverage our Aerogel technology platform, and essential to that strategy are the investments in our R&D and the protection of our intellectual property. Similar to other companies that have become market leaders by creating valuable technology, we remain committed to defending our Aerogel technology platform and will continue to assert our rights, as appropriate against companies that infringe our patented technology.

We have similar actions outstanding in the German courts against the same two Chinese companies and a European distributor and expect a determination in those cases during the first part of 2018.

Our second topic today is an update of the three important indicators related to the 2017 performance of our business.

Our first indicator is focused on our goal for 2017 to build commercial momentum each consecutive quarter by gaining market share in our core end markets, principally refinery and petrochemical companies, by demographic value and growth in our adjacent markets, including LNG, district energy and power and by taking a partnered approach in the development of new markets, including building materials.

We are measuring our progress towards achieving this goal by driving increases in quarterly revenue throughout the year, with Q2 stronger than Q1, Q3 stronger than Q2 and Q4 stronger than Q3. We believe this momentum and the continued successful development of our core adjacent and new markets will position us to achieve our revenue and Adjusted EBITDA goals in years ahead. We've met this goal this year by growing revenue \$23 million in Q1 to \$25.1 million in Q2 to \$27.2 million in Q3, and as our financial guidance indicate, we expect even stronger sequence growth in Q4.

During Q3, we supplied over \$3 million of Pyrogel XTE to an important project in Brazil and saw steady revenue growth in Europe and the United States, the latter despite the initial negative impact of Hurricane Harvey. Asia was down after strong growth in 2016 and during the first part of 2017. Despite the current weakness in Asia, we believe the region is shaping up for strong performance in 2019 and 2020. In Asia, we are building on our 2016 and 2017 LNG successes and are well positioned for the next set of projects, many of which we believe will have far greater scope than our recent projects. And with respect to Hurricane Harvey in the U.S., despite the initial pause as our end users evaluate the damage, the severe flooding has created opportunity for our products.

Wet insulation in a refinery or a petrochemical plant leads to inefficient operating condition and a corrosion of their insulation, which is a significant maintenance and safety challenge. Our Hydrophobic products reduce the incidence of CIU and install rapidly, a perfect combination when you want to solve a problem and get back up and running as quickly as possible. While there may have been a pause weeks after the hurricane, the coming months and quarters will represent an opportunity for us.

As we discussed at the time of the last earnings call, we have been positively surprised during 2017 by recent levels of activity for subsea projects. The main driver of the activity centers on the attractive economics for offshore platform owners to leverage existing assets with construction of tiebacks and extended subsea timelines. Our Aerogel products are perfectly suited to guarantee flow assurance by addressing the thermal challenges associated with longer timelines. We delivered over \$5 million of subsea product during the third quarter and one additional project that will be supplied in Q4 2017 and Q1 2018.

The global energy market is not yet robust but we continue to penetrate our account and capture market share, and importantly, our revenue growth contributed to a 300 basis point increase in gross margin versus Q2 2017 to 18%. This revenue growth and gross margin improvement supported a \$2.5 million increase in Adjusted EBITDA in Q3 versus Q2 to a positive \$1.1 million. We clearly achieved our goal of building momentum during the quarter. And with current activity levels in our market, especially in subsea, we are projecting continued revenue growth in Q4.

The second indicator centers on our revenue not comprised of Subsea and the South Asia Petrochemical project. Tracking revenue other than Subsea and the South Asia Petrochemical Project permits us to gauge our day in and day out maintenance and small project work, which we believe is the base for sustained future growth. To provide context, it is important to remember that Subsea and the South Asia Petrochemical Project, together, accounted for approximately 30% of our revenue in both 2015 and 2016.

However, in 2017, we estimate (phon) that they will account for slightly less than 20% of our total revenue.

On the other hand, our base revenue not comprised of Subsea and the South Asia Petrochemical Project has grown in millions of dollars from the low 70s in 2013 and 2014 to the low 80s in 2015 and 2016. We project continued growth in this base revenue during 2017 driven by anticipated gains in market penetration in our core markets, growth in our adjacent market and by our pricing (inaudible). We are confident we will grow base revenue to a record level in 2017 and we have a keen focus on reaching \$90 million. This continued growth in base revenue is especially notable given the backdrop of lower 2017 overall market activity levels in energy infrastructure relative to the years 2014 and 2015. With strong orders already in hand for the Subsea and from our South Asia Petrochemical customer, our focus to close out the year strongly is (inaudible) base revenue.

The third indicator related to the performance of our business in 2017 is the strategic importance of diversifying into adjacent markets. We launched on schedule on July 2017 a new product, Pyrogel HPS targeting the power industry, an industry that consumes \$1.4 billion of insulation per year. Success this year will be defined by our ability to generate \$1 million to \$3 million in Pyrogel HPS revenue before the year-end, to build a portfolio of case studies and to begin the typical adoption progression for maintenance work to small scope project work and then on to larger scale project work.

Now, approximately 100 days after launch, these success indicators are well within reach. In addition, we have worked our way into the global specifications of several key players in this market, which is a critical step as we work the adoption progression. And as we have discussed in the past, the successful roll-out of Pyrogel HPS is an important demonstration of our core competency to commercialize innovation, that is, our ability to leverage our Aerogel technology platform and to develop and commercialize innovative Aerogel products into adjacent and new markets.

Our progress in the LNG and district energy market and now in power market illustrates our ability to target and penetrate diverse and high value adjacent markets to supplement our core refinery, petrochemical and subsea work. This key value driver for Aspen bodes well for future efforts as we continue to leverage our Aerogel technology platform to new and exciting markets. We will report out on these three performance indicators as we tally up the numbers upon the conclusion of Q4 2017. Again, the three indicators are building momentum each quarter, expanding our base revenue and launching Pyrogel HPS. We will also set performance indicators for 2018 and use this tool to report our progress throughout next year.

Our third topic today pertains to the current commercial environment and our market outlook for 2017. We stated early in the year that for 2017 planning purposes, we would assume that conditions in the upstream and the downstream energy end markets in 2017 will be about on par with 2016. That is to say, limited upstream activity, strained downstream spending by our refining and petrochemical end users, and that 2017 market-wide activity levels will remain below 2014 and 2015 levels. While this outlook remains mostly correct, as discussed, recent levels of activity for subsea projects have been an unexpected bonus and certain subsea projects are now technically feasible and economically attractive within today's oil price environment, we believe we are well-positioned to play an enabling role in the execution of these projects.

Overall, we remain conservative in our commercial outlook, although we are encouraged by certain market signals and by our progress in executing our strategy to leverage our Aerogel technology platform across our core adjacent and new markets. Our products are becoming increasingly mainstream in both maintenance and project work, and we are benefiting from our focus on adjacent and new markets. And as our products become more universally recognized, we believe the adoption pattern will be accelerated and become truncated in time.

Furthermore, we believe the adoption pattern that has characterized our core markets from maintenance to small scope projects to large scope projects applies to many of our end markets, most recently LNG.

We are now specified for important large scope projects in our core and adjacent markets, which are planned in 2019 and 2020 time periods. Our ability to build base revenue, to position ourselves for significant project work and to continue to exhibit strength in entering new markets gives us confidence that over a two to three-year period we can experience substantial and diverse growth even within the current energy price environment.

This narrative leads neatly to our fourth and final topic, which is the reiteration of our strategy and scope of our opportunities. Our strategy is to leverage our Aerogel technology platform. We have world-class Aerogel product and process technology. Our progress from core to adjacent and to new markets is powerful and creates the opportunity to build a large and profitable company. The core and adjacent energy infrastructure markets are over \$3 billion in size, and technical standards are moving in our direction. The building materials market for insulation is very large, over \$20 billion. Our agreements with BASF are driven at the macro level by the global trend of resource efficiency and sustainability, and of course by the need for high performance insulation that are fire resistant.

Our initial success in entering adjacent and new markets is indicative of our progress towards the goal of broadening and diversifying our end markets, creating additional growth engines and offsetting areas of cyclical weakness, such as the current energy environment.

More broadly, our partnered approach to the building materials market with BASF represents an excellent template as we evaluate additional large and high value new market opportunities in which to leverage our Aerogel technology platform. We will target markets where Aerogel elements such as low thermal conductivity, high surface area, high electrical conductivity and tunable porosity may lead to Aerogel enhanced products that could prove to be the next generation technology in important and large markets.

Each of these markets has world-class companies that are technical, commercial and financial leaders, are well-positioned to leverage new technologies and are potential partners for us.

During the downturn in the energy market, we have continued to invest in research and development, sales and marketing, and operational excellence, and believe these investments are creating strong technical and commercial positions. We will continue our strategy of leveraging our Aerogel technology platform across diverse markets to position us for long-term growth.

Overall, we are confident that the strength of our technology and the ROI that we bring to our end users across multiple markets will enable solid performance for our Company. We will maintain our commitment to grow profitably, to prudently scale up our operation and to remain financially strong. We have an experienced team of people and we are confident in our ability to execute our strategy and to realize our vision for the Company.

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

John Fairbanks:

Good afternoon. Thanks, Don. Let's start by running through our reported financial results for the third quarter and the first nine months of 2017 at a summary level. Third quarter total revenue declined 8% to \$27.2 million versus \$29.6 million in the third quarter of 2016. Third quarter net loss was \$3.1 million or \$0.13 per share in both 2017 and in 2016. Third quarter Adjusted EBITDA was \$1.1 million compared to \$1.5 million a year ago. Importantly, our third quarter Adjusted EBITDA this year represented our first quarter with positive Adjusted EBITDA since the third quarter of last year. We define Adjusted EBITDA as net income or loss before interest, taxes, depreciation, amortization, stock-based compensation expense, and any other items that we do not believe are indicative of our core operating performance.

Patent enforcement costs had a much less significant impact on our net loss and Adjusted EBITDA during the third quarter this year than in recent quarters. We incurred only \$53,000 of patent enforcement costs during the third quarter versus \$1.1 in the third quarter last year.

For the first nine months, total revenue declined 16% to \$75.3 million. Net loss was \$17.6 million or \$0.76 per share in the first nine months of 2017 versus a net loss of \$6.3 million or \$0.27 per share last year, and Adjusted EBITDA for the first nine months was negative \$5.5 million compared to positive \$6.1 million a year ago.

For the first nine months of 2017, patent enforcement costs had a disproportionate impact on both our net loss and Adjusted EBITDA. We incurred \$2.9 million of patent enforcement costs during the (audio interference)

Operator:

Ladies and gentlemen, this is the Operator. I apologize but there'll be a slight delay in today's conference. Please hold and the conference will resume momentarily. Thank you for your patience,

John Fairbanks:

Sorry, we had a line issue, and so I'll continue.

Importantly, we continue to build sequence momentum during the third quarter. Total revenue this year has improved from \$23 million in the first quarter to \$25.1 million in the second quarter and \$27.2 million in the third quarter. As we discussed during our recent conference call, our gross profit and gross margin are highly dependent on product revenue and capacity utilization levels, principally as a result of the sequence growth in revenue. Gross margin this year has improved from 10% in the first quarter to 15% in the second quarter to 18% in the third quarter. Gross profit, in turn, improved from \$2.2 million in the first quarter to \$3.7 million in the second quarter to \$4.9 million in the third quarter, and Adjusted EBITDA improved from negative \$5.1 million in the first quarter to negative \$1.4 million in the second quarter, a positive \$1.1 million in the third quarter. For future revenue and utilization growth, we would expect to continue to see the percentage growth in gross profit and Adjusted EBITDA to outpace the associated growth in product revenue.

I'll now provide additional detail on the components of our results. First, I'll discuss revenue.

Third quarter total revenue was comprised of product revenue of \$26.8 million and research services revenue of \$386,000. Total revenue for the first nine months was comprised of product revenue of \$73.7 million and research services revenue of \$1.6 million. During the third quarter, product revenue decreased by \$2.1 million, or 7% versus last year's \$28.9 million. Solid growth in our core energy and adjacent markets, the resurgence in demand in the subsea market during the quarter, was more than offset by the conclusion of shipments to the multiyear South Asia Petrochemical Project, which comprised more than 30% of revenue on last year's third quarter.

During the quarter, total shipments decreased by 27% to 8.7 million square feet of Aerogel Blanket, while our average selling price increased by 27% to a record \$3.10 per square foot, principally due to an increase in the mix of the higher priced subsea products during the quarter.

For the first nine months of 2017, product revenue decreased by \$14.6 million or 17% versus last year. Again, this decrease was driven by the conclusion of shipments to the multiyear South Asia Petrochemical Project.

For the first nine months of 2017, total shipments decreased by 24% to 25.6 million square feet, while our average selling price increased by 10% versus the year ago to \$2.88 per square foot.

Now I'll turn to our research services revenue. Our research services revenue is related to contract research performed principally for government agencies. Research services revenue decreased by 43% during the third quarter to approximately \$400,000, and by 13% to \$1.6 million during the first nine

months of 2017. This decline was due to the relative value and timing of active research contracts versus last year. For the full year, we expect research services revenue of approximately \$2.1 million, down slightly from last year. This expectation is included in our 2017 guidance.

Next, I'll discuss gross profit. Gross profit was \$4.9 million or 18% of revenue during the third quarter of 2017 versus \$6.4 million or 22% last year. This decline in gross profit and gross margin was driven by the 27% decline in shipment volume and a 31% decrease in production volume that we instituted to manage inventory growth, offset, in part, by the 27% increase in average selling price for our product, and a decrease in manufacturing and material costs during the quarter.

Gross profit was \$10.9 million, or 14% of revenue, for the first nine months of 2017, versus \$19.6 million, or 22% of revenue, last year. The decline in first nine months gross profit and gross margin was principally a result of the 24% decline in shipment volume during the period, a 30% cumulative reduction in production volume that we enacted in 2017 to manage inventory growth, offset, in part, by the increase of 10% in average selling price for our products, a decrease in manufacturing and material cost during the period. Looking forward, we anticipate improvements in gross profit and gross margin principally associated with our expectation of increasing revenue, output and capacity utilization levels.

Next, I'll discuss operating expenses. Third quarter operating expenses decreased by \$800,000, or 9% relative to last year to \$8 million. This decrease in operating expenses was driven by the \$1.1 million decrease in IP enforcement cost, offset in part by a \$300,000, a 3% increase in all other operating expenses during the quarter.

For the first nine months of 2017, operating expenses grew by \$3.3 million, or 13% relative to last year of \$28.4 million. This increase in operating expenses was the result of a \$1.2 million increase in patent enforcement costs year, an \$800,000 increase in research and development expense, a \$300,000 increase for sales personnel and programs, and a \$1 million year-over-year increase in all other operating expenses. The growth in our operating expenses during the first nine months of 2017 reflects our commitment to expand, protect and defend our Aerogel technology platform and to position Aspen for solid, long-term growth.

Next, I'll discuss our balance sheet and cash flow. Overall, our cash flow was in line with our expectations for the first nine months of 2017. Cash used in operations of \$5 million reflected our negative Adjusted EBITDA of \$5.5 million, offset in part by \$500,000 of cash generated by changes in working capital during the period. Capital expenditures during the first nine months totaled \$5.4 million, down from \$10 million last year. We ended the first nine months of 2017 with \$7.3 million of cash and minimal debt, current assets of \$39.9 million, and shareholders' equity of \$101.5 million. In addition, we had \$11.3 million available under our revolving credit facility at the end of the third quarter.

We've updated our full year financial outlook for 2017. Total revenue is expected to range between \$106 million and \$112 million, revised from prior guidance of \$104 million to \$112 million. Net loss is expected to range between \$19.3 million and \$21 million, revised from prior guidance of \$18.2 million to \$20.8 million. Adjusted EBITDA is expected to range between a loss of \$3 million and a loss of \$5 million, revised from prior guidance of a loss of \$2 million to a loss of \$5 million. EPS is expected to range between a loss of \$0.82 and a loss of \$0.90 per share, revised from prior guidance of \$0.78 to \$0.89 per share. The EPS guidance assumes a weighted average of 23.4 million shares outstanding for the year. This 2017 outlook also assumes depreciation and amortization of between \$10.7 million to \$10.8 million, stock-based compensation of between \$5.1 million and \$5.3 million, and interest expense of \$200,000. In addition, this financial outlook includes between \$3.5 million and \$3.9 million of costs and expenses associated with our patent enforcement actions for the full year.

We've also increased our projected average selling price for the full year to \$2.90 per square foot, plus or minus \$0.05. This projected average selling price reflects an increase of \$0.05 from our prior guidance, due to an expected mix of higher priced subsea products during the fourth quarter.

For the full year, we continue to expect a gross margin in the mid-teens. This gross margin expectation is unchanged from our prior 2017 outlook.

We're also reaffirming our 2017 full year capital expenditure guidance of \$6.3 million. As a reminder, the \$6.3 million projection is comprised of \$1 million of new projects initiated during 2017 and \$5.3 million of final expenditures for the pilot line, equipment in support of new products, and other projects approved and initiated during 2016.

Turning to cash at an aggregate level, we expect to generate cash during the fourth quarter due to projected improvements in operating performance, planned reduction in inventory balances, and continued constraints on capital spending during the period. Within the context of the Adjusted EBITDA range set out in our 2017 full year outlook, we expect to exit the year with between \$10 million and \$12 million of cash on hand.

As always, project work, product mix and unexpected expenses can create quarterly and annual variability in financial performance.

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

Operator:

At this time, I would like to remind everyone, in order to ask a question, please press star, then the number one on your telephone keypad. We will pause for just a moment to compile the Q&A roster.

Your first question comes from Eric Stine with Craig-Hallum. Your line is open.

Donald Young:

Hi Eric.

Eric Stine:

Hi Don. Hi John. I was wondering if we could just start with subsea. I just wanted to confirm, did you say that the 3Q business level was \$5 million. I guess confirm that first. And then you mentioned additional work. Any way you can quantify that as you're thinking about 2018?

Donald Young:

Yes, Eric. Yes, just a little over \$5 million for Q3 and what we said in our prepared remarks simply that we had orders in hand for both Q4 and for Q1. So we're going to have a strong Q4 in the subsea area as well.

Eric Stine:

Is that something where—I mean I know—well along with the refinery and petrochem you've been a little hesitant to kind of view that as sustainable. Is what you're seeing in subsea, does that make you more confident that that is something that's sustainable or are you still kind of taking a wait-and-see approach on that?

Donald Young:

If you go back, we've been doing subsea work since I'd say about 2005 and our historic average is in that space or sort of in the \$4 million to \$8 million range. When you go back to those years where we had a spike in oil prices, \$80, \$90, \$100 oil prices, those numbers our subsea numbers went up considerably—John, correct me—I think we had roughly \$15 million in 2014 and over \$20 million of subsea business in

2015, came down in 2016 to—the number's approximately \$3 million or \$4 million, if I remember correctly, and this year we've seen a nice uptick, as let's just say oil prices have stabilized and technology has improved, cost cutting has taken place, combinations have taken place of companies in the subsea and they have found a way to be more economic at projects that are economically at the same time in these areas, they're extending existing assets, our products are terrific in that longer pipeline that have greater thermal challenges.

So we continue to win a dominant amount of those more challenging opportunities and all I can tell you is we've got a good Q4 lined up, we've got a good Q1 lined up and there's a lot of—let me call it this sort of positive body language out there across 2018 as projects are being either dusted off or conceived of right now. So again, we feel better about that business. We do not expect to return to 2014 and 2015 levels, but to be solidly in our historical range feels good to us.

Eric Stine:

Yes, that's great after where it's been as of late. Okay, maybe just turning to refinery. That part of the business continue in this round of earnings releases. (Inaudible) Company's talking about the 2018 and they're seeing increased activity that they've got set up and I know to this point again you've kind of been a little conservative on that. Is this an area where you're starting to see that oil being part of it but just increased competence for market participants seeing that potentially that gets back on better footing as well?

Donald Young:

Time will tell. I've traveled a lot in the last six weeks and it's that time in the field with all of our sales people around the world and our partners and many of our end users and I would say that things do feel more positive. I'll be more quantitative with you once we get a few more purchase orders in hand. I think that these levels are still below where they were in say 2014 and even the first part of 2015. So we're still below those levels of overall market activity.

We've grown our base revenue. As I said in my comments, we will continue to here in 2017 and we'll strive to again in 2018. We know that we're taking market share. We know we're penetrating our accounts and we know that we're moving down this adoption progression that I talk about from maintenance to small scope project work to larger scope project work and we in both our core and our adjacent markets we continue to make progress moving towards some of that larger scale project work. While '18 may or may not bring any large projects, we are in a very strong position in 2019 and 2020 for some of this work that we see that has been initiated.

So again, I'll tell you more quantitatively when we have purchase orders in hand, I think, but we do feel better about that market. As I said in my remarks, we did see a little pause right after Hurricane Harvey here in the United States, but it was just pretty temporary and we feel there's nice opportunity for us here in Q4 and going into 2018 to provide solutions to some of the flooded insulation that occurred and is now evaluated. So we're in a good position to grow from there.

Eric Stine:

Okay, that's great. Thanks a lot.

Donald Young:

Thank you Eric.

Operator:

Again, if you would like to ask a question, please press star, one on your telephone keypad.

The next question comes from Chip Moore of Canaccord. Your line is open.

Chip Moore:

Thanks. Maybe just dovetail on your comments there. Obviously some short-term impacts with those storms in the Gulf, but this would seem to be a good case study I guess on the advantages of your product. Any changes in sort of discussions, customer behavior that you're seeing post those events?

Donald Young:

I think, again, you don't ever wish that kind of devastation anywhere and certainly Hurricane Harvey was devastating. We do believe that our materials really shine in resisting flooding or being able to recover from flooding relatively quickly—hydrophobic, open porous (phon)—we do not—we are not harmed by that once the flooding recedes and in replacing other materials that were on these pipes we do it quickly and we think we do it with high performance.

So it's just a nice combination of events, frankly. We are able to demonstrate that the product that was installed can withstand that kind of an event and again—so go on very rapidly and get these assets up and running quickly. We're seeing that, there's no question.

Chip Moore:

Yes, okay, good. Maybe if we switch over to the new Pyrogel product. Maybe you can elaborate a little bit more on sort of how those initial orders have been coming, and then sort of longer-term as you get spec'd in with turbines and things like that, how you see that playing out.

Donald Young:

Yes. So we came out of the gate in July, the beginning of Q3 with our launch and we've said that we will get between \$1 million and \$3 million of orders here in the tail end of 2017 and we'll be comfortably in that range. I think, very importantly, we've been to build some case studies and those are the best selling tools that we can have and so we feel that we're in a strong position.

The other thing that's so important is that we have been able to work our way to the specifications of some of these key players and without being in the specification you're always attempting to sort of crash the party, frankly, and being in the specs positions us for maintenance, small scope and we believe over a longer period of time larger scope work in those high temperature ranges that are consistent with power generation. It's a big market too. Chip, we also—the more we have begun to work that market the more convinced we are that we have a role to play in that market that consumes \$1.4 billion of insulation.

Chip Moore:

Yes, no, that's great. I will hop back in queue and let someone else in. But thank you.

Donald Young:

Thank you.

Operator:

Again, if you would like to ask a question, please press star, and then the number one on your telephone keypad.

Again, to ask a question, please press star, one on your telephone keypad.

Your next question comes from Ethan Potasnick with Ethan and Company. Your line is open.

Ethan Potasnick:

Yes, hi. This is Ethan Potasnick filling in for Sean Hannan. I was curious if you could talk about the BASF partnership now that it's about 16 to 17 months old. I'm wondering if you guys could share the degree to which it's being additive. I know you guys talked about you guys were hoping to double building materials revenue in '17 as well as '18. So could you guys provide more color on the degree this is being realized, the building materials, and what the BASF partnership is specifically contributing and perhaps when that should contribute more?

Donald Young:

Yes. Thanks Ethan. There were three elements to those agreements that occurred in the summer of 2016. The first one—or one element was around technology development. So we have a joint development agreement with them where we are developing a next-generation product for the building materials market and that work is going well. We're not quite in the position to announce the specifics of that but what I would say is it's a product that we believe will be valuable in the market, excellent thermal performance, great energy efficiency capabilities, very important in the market today, a product that has limited combustibility, non-conductibility which of course has taken heightened visibility here over the course of the past several months.

So that's one element, and a very important element, and we are working very closely with BASF at that technical level and making progress. A second element of the agreement, related—really think of it as almost kind of a consulting role in some of our operations in our plant. They are expert in several areas that are relevant to our manufacturing. Not necessarily with Aerogel specifically, but with areas around material handling, a whole host of areas where they are helping us put best practices in place and we believe that we will see the benefit of that denominated in yield and throughput improvements in our East Providence manufacturing plant. Again, working closely and I think very good productivity in the partnership (inaudible).

And then the third element was the roll-out of what we're referring to as Spaceloft A2 in our building materials effort, a first generation product that we have gone through testing and certification, particularly in the European market, and that process has taken longer than we had anticipated but we still believe that that product will contribute here in 2018 and beyond. What I would just kind of try to categorize for you is just generally speaking building materials was roughly 4% or 5% of our revenue here in 2017. We believe it can play a much larger role as we roll it out in 2018, 2019 and 2020, especially if we continue to make progress with the next-generation product here. So that will have attributes that we think will be important.

Let me just say sort of more broadly, we are working closely with BASF on some of our other—we talked about the Aerogel technology platform but there are lots of concepts that we have that we have traded ideas about with BASF around and again it's an important and strong relationship for our Company and we're confident it will pay dividends here in the short term, medium term and long term.

Ethan Potasnick:

Okay, great. On the operational side, could you describe some of your efforts to become more efficient, drive better margin, and what incremental dollars are we realizing today versus a year ago and possibly what can we potentially—you know, you guys gain further from here?

Donald Young:

Let me start and I might have John—the most important thing for us driving margin is driving volume through that plant. It's a big fixed asset and today we have the ability to generate roughly \$150 million of product through that plant. In our economics, the model underlying that plant had remained strong. Even though our gross margins are a little lower it's purely a function of volume growth through that plant. We've continued to make progress in the efficiency of that plant, again, around throughput and yield that we believe will allow us to drive those gross margins and EBITDA margins that we talked about for a long period of time as we fill that plant.

John, do you want to add to that?

John Fairbanks:

Sure. I think as Don said, we've had the time with the plant that hasn't been full over the course of the past few quarters to really focus on operational efficiency, operational excellent and those efforts really is starting to pay off. It's a combination of time spent, new process technology—actually evolving process technology and some capital expenditures over that time period, but our yields are now in our plant are at record levels. Our ability to run product through the plant, our throughput and productivity is at record levels and the product that we're producing is of the best quality that we've seen in our history.

So we've really put that—operating of the—the capacity, the excess we have, we actually have been able to use it to position ourselves that when we see the volume that Don talked about we will be more profitable than we originally anticipated. And just in rough terms, we think we could generate gross margins now of about 2 points higher than maybe what we thought we could do 12 to 15 to 18 months ago, and that would also drop right down to the bottom line. So we still need to get that volume to fill that plant but when we do we expect profitability to be even higher than we originally anticipated.

Ethan Potasnick:

Okay, great. Thank you.

Donald Young:

You're welcome.

Operator:

There are no further questions at this time. I'll turn the call back over to Don Young.

Donald Young:

Thank you Jesse; I appreciate it. Thank you for your interest in Aspen Aerogels. We look forward to reporting our fourth quarter 2017 and full year results to you in February of 2018. Have a good evening. Thank you.

Operator:

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