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ORB - Orbital Sciences Corporation Conference Call To Discuss Antares
Rocket Launch Failure

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PRESENTATION

Operator

Good afternoon, my name is Chris and I will be a conference operator today. At this time I would like to welcome everyone to the discussion regarding the Antares rocket launch failure.

(Operator Instructions)

David Thompson, President and CEO of Orbital Sciences, you may begin your conference.

David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

Okay, good afternoon, everyone. Thank you for joining us for the call today covering last night's Antares launch failure. I am Dave Thompson and with me on the phone is Garrett Pierce.

Before we get started I would like to ask everyone to note that some of the comments that we will make during the call may be considered forward-looking statements. As I think you all know such statements are subject to a variety of risk and uncertainties that may cause the Company's actual operational and financial results to differ materially from our current outlook. Additional information concerning the main factors that could cause such actual results to differ are contained in the reports filed with the SEC.

Here's what we're going to discuss today. I'm going to lead off with a brief description of what happened during yesterday's Antares launch attempt and what short-term actions the Company is taking to collect information about the launch failure to help us in determining the cause of the accident and to identify the appropriate corrective actions to be implemented.

Next Garret is going to comment on the financial impacts of the incident as they are currently known. And then finally I will discuss our preliminary thinking about how we may move forward to continue to maintain the Antares-Cygnus cargo supply line to the international space station for NASA. And then at that point we will be happy to take your questions.

As many of you know we intended to launch the fifth Antares rocket carrying our fourth Cygnus spacecraft to the space station last night from our launch base at Wallops Island, Virginia. Following a smooth countdown Antares lifted off at about 6:22 PM Eastern time but experienced a catastrophic failure approximately 15 seconds into the flight, which ultimately destroyed the rocket as well as the Cygnus spacecraft attached to it.



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Fortunately no one was injured as a result of the accident and based on the preliminary inspections that were conducted this morning at Wallops Island it appears that the launchpad complex itself was spared from any major damage. In addition the Antares vehicle assembly building and related Cygnus spacecraft processing facilities at other locations within the Wallops area were not affected by the failure in any way.

At Orbital we are certainly disappointed by this failure but in no way are we discouraged or dissuaded from our objectives to expand the Antares rocket well into the medium launch class. Our short-term actions have centered around the formation of an Accident Investigation Board that together with NASA, the Mid-Atlantic Regional Spaceport and the National Transportation Safety Board, will carry out the failure review and recommend corrective actions.

At this time it is too soon to know exactly how long this process will take or whether Antares and Cygnus missions that are scheduled for next year including our next flight which had been set for early April will be affected. In the days ahead our number one priority is to do all we can to meet Orbital's commitments to NASA to keep open the cargo supply line to the space station of which Antares and Cygnus play an important part.

We are considering several options in determining the best way to achieve this overarching goal. And I will comment on those in a few minutes.

Before that though I would like to ask Garrett to briefly discuss what is currently known about the financial implications of the launch failure. Garrett?

Garrett Pierce - *Orbital Sciences Corporation - Vice Chairman & CFO*

Thanks, Dave. From a financial standpoint it will take some time to assess the precise impacts; however, I can tell you that Orbital's view for 2014 remains unchanged. That our exposure to the mission success payment holdbacks on the CRS contract is covered by insurance and that the cost of any necessary facility repairs is also reimbursable by insurance.

As Dave said, early indications are that the MARS Launch Complex came through without any major damage. So hopefully repairs will not be extensive.

As to the downstream impacts of the failure in 2015 it is too soon to estimate what those could be. The largest variable likely be the length of time required to return Antares to flight status, which Dave will discuss shortly, is not known. Dave?

David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

Okay, thanks Garrett. Well, we still have a lot of work to do in the days ahead to analyze all of the telemetry and video data, to review the recollections and notes of the participants in the operation and to collect all other available information about the flight.

This investigation may or may not lead us to the conclusion that the failure was caused by a problem with the Antares first-stage main propulsion system. As most of you know the AJ-26 rocket engines used in that system have presented us with some serious technical and supply challenges in the past. So notwithstanding the previous successful flights of Antares before yesterday, Orbital has been reviewing alternatives since the middle of last year and recently selected a different main propulsion system for future use by Antares.

It is possible that we may decide to accelerate this change if the AJ-26 turns out to be implicated in the failure. But this has not yet been decided.

On this and other matters that Garrett and I are discussing today I went to again emphasize that the information that we currently have is preliminary and could change substantially as more data is collected and analyzed and as our alternative plans are refined. We are only some 18 hours into this process and sometimes reviews like this can take unexpected turns, days or weeks after the event itself occurs.

Before we open up the call for questions I would like to make a few additional observations. First, although they are increasingly infrequent in our business, rocket and satellite failures do still occur. Building and launching vehicles into space are among the most challenging and demanding things that government organizations and private companies do.



Despite the diligent efforts of some of the aerospace industry's best and brightest people, sometimes things do go wrong. We work really really hard to prevent this from happening and Orbital's record, which I believe is one of the best in the world, reflects that emphasis.

In our case we've conducted a total of 284 launches of major rockets with a 95% overall success rate over the past 3-plus decades. And we have achieved an even stronger 96%-plus success rate on 106 major launches that we have carried out in the past 10 years.

Second, and more generally, Orbital has experienced adversity in the past some of which was more difficult than this and the Company has always emerged stronger as a result. I am determined that we will do so again this time. In fact, I think the true test of an organization is not whether it experiences infrequent failure but how it responds to, learns from and moves forward after such an event takes place.

Finally, in the early 1960s President Kennedy said that Americans explore and operate in space not because it is easy because it is hard. That was true 50 years ago and it remains true today.

It might at first seem strange that I would want to highlight some of the difficulties with which our Company must contend in the business that we have chosen. But over time I think it provides the basis for a very strong strategy, one that despite occasional setbacks, generates tremendous value to our customers and also makes it very hard for all but a very few other companies to compete in our markets.

Okay, I think we are now ready to take your questions. I expect to have more of them than we will have immediate answers but we will do our best.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Howard Rubel, Jefferies & Co.

Howard Rubel - Jefferies & Company - Analyst

Thank you very much, David and Garrett for this time. I'm going to just do two.

One is to address the merger for a moment, if you don't mind. I've had a number of questions from people about how the merger agreement contemplates an event like this. Could you provide me with some color?

David Thompson - Orbital Sciences Corporation - Chairman, President & CEO

Howard, I would say in general there is no specific provision in the agreement for a launch failure. As I mentioned that is an infrequent but still not altogether unavoidable occurrence in our business and I think that is generally appreciated all around. So as far as I know I think things will continue.

Howard Rubel - Jefferies & Company - Analyst

And then you have seen both big successes and a couple of challenges. And I know you have sort of offered a very be cautious about how long something like this could take. But as you have looked in the past, is there any sort of timeframe or any sort of steps that we should look for outside looking in to see how you are progressing at resolving and coming to a conclusion?



David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

In this case I would say first that it appears that we have a very rich record of telemetry and video data and other sources of information. That is often but not always true in the cases of launch problems. I also think although this is subject to additional work that it will not likely take very long, I think a period measured in days not weeks, for the investigation team to define the handful of most likely causes of the accident.

It may take a little longer than that to zero in on the final root cause. From our experience in the past, which is not altogether transferable to this situation, I would anticipate that there will be some delay in the next scheduled Antares launch, which as I mentioned earlier, was currently set for early April.

I think a reasonable best-case estimate would bound that at three months but it could certainly be considerably longer than that depending on what we find in the review. I would hope it would be not more than a year.

Howard Rubel - *Jefferies & Company - Analyst*

Thank you very much.

Operator

Sam Pearlstein, Wells Fargo.

Sam Pearlstein - *Wells Fargo - Analyst*

Good afternoon. Can you talk, and I guess Garrett, more on the financial side is you have recently raised the booking rate on the CRS program to date. And I guess from this point forward should we be thinking about it as likely not increasing certainly until this is resolved, or should we be thinking about it actually moving back down a little bit from here?

Garrett Pierce - *Orbital Sciences Corporation - Vice Chairman & CFO*

I do not see it moving back down from here based upon everything I am aware of.

Sam Pearlstein - *Wells Fargo - Analyst*

Okay.

David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

I would just add to that we think we have a ample and conservative management reserve in our contract estimates. And within any reasonable recovery period that reserve should cover any incremental costs to be incurred in the investigation and getting back into flight status. And as Garrett indicated, any repair work that may be required on the facilities, which currently appears to be in fairly good shape, should be covered separately by insurance proceeds.

Sam Pearlstein - *Wells Fargo - Analyst*

And is the same true in terms of the receivables and the ability for you to continue to receive the milestone awards and the cash flow profile? Obviously outside the investigation and then with other costs, but does that change at all in terms of what is potentially able to be earned?



David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

I would answer that in two parts. The very near-term receivables that would have been collectible upon the completion of a successful mission a month or so from now will be covered instead by mission insurance.

We had not anticipated the collection of that receivable until January in any case, so it should have no effect one way or the other on the final quarter of the year. Receivables on other missions beyond the ill-fated one from yesterday do depend on progress both in building the Cygnus spacecraft as well as in completing milestones on the launch vehicles.

Some of those milestones could be affected as a function of delays that may be incurred for launches currently scheduled in 2015. At this point we don't have a precise estimate on the magnitude of how that might vary but we will be working to put one of those together in the next couple of days.

Sam Pearlstein - *Wells Fargo - Analyst*

Okay, thanks. If I can ask one last one, is the CRS-2 the follow-on contract where I think you were going to put in a bid later this year. Does this end up affecting that in any way?

David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

We are still on track to submit our proposal in a couple of weeks. We intend to as quickly as we can bounce back from this failure and continue both under the current contract and hopefully a future contract as well to provide an important part of the cargo bridge from Earth to space in support of NASA's human spaceflight program. So we will have to wait and see how that all comes together but we are still full speed ahead on our pursuit of future business.

Sam Pearlstein - *Wells Fargo - Analyst*

Okay. Thank you very much.

Operator

Joe DeNardi, Stifel Nicolaus.

Joe DeNardi - *Stifel Nicolaus - Analyst*

Good afternoon. David, I am wondering just given your background and your experience here, is there anything you can see from looking at the video or the telemetry data that would kind of point one way or the other that makes you feel more comfortable that or gives you a sense as to how long this is going to take to resolve and understand what happened? Or is it still too early to tell?

David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

I think the short answer is it is still a little too early to tell. There are certain specific elements of data that have been preliminarily analyzed to date that point in a particular direction but my experience also suggests that sometimes first impressions are not correct ones. And it is very important not to focus too early on what may at first appear to be the cause of an accident like this.

It is important to do a very comprehensive review and consider things that may at first not appear to be likely causes of failure just to be sure that you don't fixate early on on what initially appears to observers to be the likely cause and end up missing the real root cause. So I think we will be substantially smarter on this over the course of the -- again the coming days, not weeks -- I may be surprised. It may turn out to take longer but my best guess right now is again assuming we proceed in a very diligent and open-minded way that we will be zeroing in within a week or so to where the problem is likely to be found.

Joe DeNardi - *Stifel Nicolaus - Analyst*

Okay. That is helpful. And then if you do decide to use your the alternative to the AJ-26, what is the timeframe for when that would be ready?

David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

Under the original plan we were, as of now, about two years away from conducting the first launch of an Antares with the second-generation propulsion system. We are currently looking at the prospects for accelerating the introduction of that system and I do not at this point have a firm estimate for how much of that two-year period could be compressed. I certainly think we can shorten that interval but at this point I don't know by how much.

Joe DeNardi - *Stifel Nicolaus - Analyst*

Okay. And then Garrett, just this last one for me. Can you just -- I assume that there's not going to be any revenue booked on the program until the investigation is resolved and can you just maybe help us understand if you're not doing any work on Antares can you still do work on Cygnus and book revenue and work down the receivables balance through that and maybe what the breakdown is?

Garrett Pierce - *Orbital Sciences Corporation - Vice Chairman & CFO*

Yes, I don't have the details but we will continue to recognize revenue on a percent complete basis as we have over the life of this program. And there will be activity going and milestones will be met and payments will be made. So we have no reason to suspend recognition of revenue, none whatsoever.

David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

Joe, I think you were beginning to draw a distinction, which I think will be helpful and that is, the work on the Cygnus spacecraft will continue apace and that will generate incremental revenue and where the milestones are tied to Cygnus-related items, those milestones should still be accomplished. On the launch vehicle side, Antares, there may be a bit of a slowdown there for a period.

Again, that all depends on what comes out of the investigation. But the Cygnus component of the contract, which is the larger part of the contract, will continue without interruption.

Joe DeNardi - *Stifel Nicolaus - Analyst*

Okay. But NASA hasn't, or you haven't decided to stop work on the Antares at this point?

David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

No. No we haven't.



Joe DeNardi - *Stifel Nicolaus - Analyst*

Okay, thank you.

Operator

Michael Ciarmoli, KeyBanc Capital Markets.

Michael Ciarmoli - *KeyBanc Capital Markets - Analyst*

Hey, good afternoon guys. Thanks for taking questions.

Maybe just Dave or Garrett, just to stay on that. If the problem or failure was due to the AJ-26 and you did presumably have to accelerate that engine development, would that still enable you to recognize revenue? Because I'm assuming that wouldn't be an engine swap wouldn't be covered under the program. So has that been contemplated into the revenue recognition if that is the case?

David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

It is a good question. I think it's an astute observation. We don't know the full answer to that just yet.

It will, like many other things, it will depend on the conclusions that are drawn in the coming days and weeks from the investigation. And in turn the path we decide is the best one to follow for returning Antares and Cygnus to flight status. There may be minimal impact, there may be a gap of revenue on the launch vehicle side, or potentially there could even be an acceleration depending on the details of how we go forward.

Michael Ciarmoli - *KeyBanc Capital Markets - Analyst*

Okay. And then can you just remind us -- I believe you had -- this was going to be the first launch with some newer content. I believe the upgraded ATK motors, that was the only new wrinkle in this launch, if I am correct?

David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

Yes, you are correct. This represented a second-stage propulsion system upgrade on Antares. We have absolutely no reason at this point to have any concerns about that new -- the performance of that new second stage.

Of course we didn't get far enough along in the ascent trajectory to exercise that new propulsion system. But there is nothing that has been seen so far that would suggest that was a contributor in any way to the failure.

Michael Ciarmoli - *KeyBanc Capital Markets - Analyst*

Okay. And then just the last one I guess for me, on the merger it is probably -- you guys are keeping the guidance this year, probably too early to even discuss the implications on everything for the pro forma you have laid out there. Again barring engine changes or I am assuming everything on the pro forma merger assumptions are still intact?



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David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

I think you're right. It is just too early. It is too early to really be able to provide much insight into that.

Michael Ciarmoli - *KeyBanc Capital Markets - Analyst*

Okay. And then maybe I will just sneak one last one in. Your experience failures do happen.

You have obviously been trying to market Antares to other commercial military customers. What is the mindset, again maybe drawing on past experiences? How does this impact the potential sales process for Antares?

David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

I think there's some cross currents in that area. Certainly a failure like this for a launch vehicle still relatively early in its lifecycle is not helpful in a general sense.

On the other hand the possibility of an earlier introduction of the new main propulsion system may actually be a positive development. How those two factors net out is too early to tell and may vary depending on the circumstances of different customers.

Michael Ciarmoli - *KeyBanc Capital Markets - Analyst*

Got it. Thank you very much, guys. That's all I have.

Operator

Tyler Hojo, Sidoti & Company.

Tyler Hojo - *Sidoti & Company - Analyst*

Good afternoon. I just wanted to follow up on one of Mike's questions.

So totally understand that it is too early to ascertain some of the long-term earnings projections that you had out there for the combination of orbital and ATK. But since that is the case and since you basically don't really know when the outcome of this investigation is going to take place, are you considering perhaps delaying the shareholder vote in regards to the merger of equals?

David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

I think -- Tyler, I hate to sound like a little broken record but I think it's too early to tell on that too.

Tyler Hojo - *Sidoti & Company - Analyst*

Okay. All right. Okay, thanks.

And just in regards to kind of the no change to the 2014 guidance, I could be mistaken but my thought was that the updated guidance that you gave in Q3 anticipated a margin step-up on CRS close to 7%. I am assuming that is not going to happen, so why wouldn't at least the top end of your guidance come down?



Garrett Pierce - *Orbital Sciences Corporation - Vice Chairman & CFO*

The guidance we gave we did not indicate that we were going to take a step up. We said it is possible. But whether we took it or not we would be in the range that we have provided.

Tyler Hojo - *Sidoti & Company - Analyst*

Okay. All right, thanks. And just one last one, if I may.

So in the prepared remarks, David, you mentioned you were considering several options in terms of keeping the supply lines open to NASA. I think one of them was potentially swapping out AJ-26. Is there something else that is kind of on the table right now?

David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

There could be but I would prefer not to comment on it just yet. But again I would just go back and stress that our number one priority at this stage and always is to meet our commitments to the Company's customers and in this case NASA, which was our first customer and is our longest-standing customer.

So if we love to build rockets and satellites but more importantly than that we love to have happy customers. So we want to make sure that we look at alternatives to minimize any disruption at all, if that is possible to the cargo delivery schedules that NASA is counting on us to do.

So we are going to consider several possibilities and I would guess some time maybe into -- sometime in the month of November, we will largely have settled on a course forward. It may be staying on with the current configuration. It may be accelerating the transition to a new configuration and there may be a few variations on one or more of those themes.

Tyler Hojo - *Sidoti & Company - Analyst*

This may be a silly question, but is one of the things that you are batting around is maybe outsourcing this work to somebody else, or is that not on the table?

David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

I would say at this point I will just pass on that one and let us develop some of these options a little farther.

Tyler Hojo - *Sidoti & Company - Analyst*

Fair enough. Thanks so much. I appreciate it.

Operator

Chris Quilty, Raymond James.



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Chris Quilty - *Raymond James & Associates - Analyst*

Thank you. David, a question, do you currently have enough AJ-26s in inventory to complete the CRS-1 even with this launch failure? If you were to contemplate going forward?

David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

Yes, there are adequate CRS -- sorry, adequate AJ-26 engines in inventory, which subject to ground testing and flight worthiness determinations would fulfill all of our commitments under the current contract.

Chris Quilty - *Raymond James & Associates - Analyst*

Got you. And the clarification. Is it fair to assume that your bid for the CRS-1 extension as well as the CRS-2 contract were both going to be based upon the re-engined Antares?

David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

Yes.

Chris Quilty - *Raymond James & Associates - Analyst*

Okay. And likewise, any of the commercial contracts you were discussing up to this point were based on a re-engined Antares?

David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

A little less -- I think on that one I will be a little less clear-cut and probably not respond completely on that part, Chris.

Chris Quilty - *Raymond James & Associates - Analyst*

Okay. Fair enough then. Thank you.

David Thompson - *Orbital Sciences Corporation - Chairman, President & CEO*

Okay, thank you Chris and thanks to everyone for joining the call this afternoon. We appreciate your interest in the Company and we look forward to sharing more information as it develops in the days ahead. Thank you all.

Operator

Ladies and gentlemen, this concludes today's conference call. You may now disconnect.



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