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BWXT - Q2 2017 BWX Technologies Inc Earnings Call

EVENT DATE/TIME: AUGUST 08, 2017 / 1:00PM GMT

THOMSON REUTERS

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by, and welcome to BWX Technology, Inc. Second quarter 2017 Earnings Conference Call. (Operator Instructions) As a note, this call is also being recorded. I would now like to turn the call over to our host, Mr. Alan Nethery, BWXT's Vice President of Investor Relations and Corporate Procurement. Please go ahead, sir.

M. Alan Nethery - *BWX Technologies, Inc. - VP of IR and Corporate Procurement*

Thank you, Denise, and good morning, everyone. We appreciate your joining us to discuss our 2017 second quarter results, which we reported yesterday afternoon. A copy of our press release is available in the Investors section of our website at bwxt.com. Joining me this morning are John Fees, BWXT's Executive Chairman; Rex Geveden, President and Chief Executive Officer; and David Black, Senior Vice President and Chief Financial Officer.

As always, please understand that certain matters discussed on today's call constitute forward-looking statements under federal securities laws. Forward-looking statements involve risks and uncertainties, including those described in the safe harbor provision at the end of yesterday's press release and the Risk Factors section of our most recent 10-K and 10-Q filings. These risks and uncertainties may cause actual company results to differ materially and we undertake no obligation to update these forward-looking statements except where required by law. On today's call, we may also provide non-GAAP financial measures, such as adjusted earnings per share, that are reconciled in yesterday's earnings release and our company overview presentation, both of which are available on the Investors section of our website. BWXT believes that non-GAAP measures provide greater insight and transparency into the company's operational performance, and provides these measures to investors to help facilitate comparisons of operating results with prior periods and to assist them in understanding BWXT's ongoing operations.

And with that, I will now turn the call over to John.

John A. Fees - *BWX Technologies, Inc. - Executive Chairman*

Thank you, Alan. BWXT built on the strong momentum from the start of the year with EPS in the second quarter up almost 9% compared to the second quarter of 2016, and adjusted EPS up over 24% compared to the second quarter of last year. Our disciplined approach to executing on our long-term strategy drives stability, profitability and growth that will continue our already demonstrated excellent performance.

In the second quarter 2017, the company achieved consolidated revenue growth of 1.9% compared to the second quarter of 2016. The consolidated operating income was $92.3 million, a 4.4% increase compared to the same period, and margins increased to 22.5%. Again, compared to our second quarter of 2016, EPS grew $0.05 to $0.61, and adjusted EPS increased $0.11 to $0.56. Backlog continues to be strong, there are $3.8 billion at the end of the quarter. This strong financial performance is a result of our disciplined operational execution and our management of our costs.

We entered 2017 with an ambitious plan, and I'm happy to report that we are executing ahead of that plan. Based upon the results achieved in our first 6 months and the clarity we enjoy in our backlog, we have decided to raise EPS guidance by $0.12, and now expect adjusted earnings to be between $1.97 and $2.07 per share. There are a number of growth areas we are very excited about. Recently, Senator Roger Wicker and Representative Bob Wittman, Chairman of the Congressional Seapower Committees, that oversee America's Navy and Marine Corps, published an editorial, where they proposed the national policy that codifies 355 ship requirement and Force Structure Assessment released by the Navy in December. According to the Chairman, a 335-ship Navy would keep pace with the Navy's increasing missions and growing international competition in international seas. Regarding competition, the Chairman claimed China is on track to have twice as many submarines and 4x as many surface ships as the United States by 2030. Warships doubled with submarine patrols and expanded the top operational areas. The Chairman's editorial echoes Admiral John Richardson, Chief Naval Operations, who stated in The Future Navy white paper, that the number of ships in the Navy fleet determines where we can be and being there is a key to naval power. Admiral Harry Harris, Commander of the Pacific Command, told Congress he has only half the submarines he needs. The key tenet of the new administration was to strengthen the United States military and its Navy. The company remains confident it can support the needs of the Navy as they develop their spending plans. We have diligently aligned capital expenditures with facility expansion needs to show we have the right resources ready to support additional production volume. Our current forecast do not consider all the aforementioned opportunities. However, we do see the potential for a meaningful volume growth in excess above baseline forecasts. If the Navy moves forward with proposed plans to continue producing 2 Virginia class submarines per year, we could expect to add at least $2 billion of incremental revenue over the next 20 years. This scenario led us to provide our multiyear guidance of double -- low double-digit adjusted EPS CAGR over 3 to 5 year period following 2017. As we discussed last quarter, we hope to better understand procurement plans for the Virginia class submarines by year-end. Furthermore, if the most optimistic but unlikely scenarios are considered, which will include the faster build rate for aircraft carriers and a few more Virginia class submarines, we could see an incremental revenue of about $4 billion over the next 15 to 20 years.

Echoing the macro growth patterns we announced on May 26 that the company's Four Rivers Nuclear Partnership joint venture with lead partner CH2M and Fluor Corporation was awarded the Paducah Deactivation and Remediation Contract at the U.S. Department of Energy’s Paducah Gas Diffusion Plant in Kentucky. This is a contract valued at roughly $1.5 billion over 10 years, and it includes a 5-year base term followed by 3-year and 2-year option periods, unilaterally exercised by the Department of Energy. We're excited to add this Deactivation and Remediation Contract for our portfolio of Nuclear Management Projects.

Next, we'll elaborate on these items and other strategic initiatives that we're working on the later in the call. Before he does, let me turn the call over to David, who will discuss second quarter results and other financial matters.

David S. Black - *BWX Technologies, Inc. - CFO, SVP and Treasurer*

Thanks, John. The Nuclear Operations Group or NOG's second quarter 2017 revenues were $313 million, slightly down from Q2 2016. However, we are still on track to achieve our guidance for the year. Year-to-date, the segment's revenue was up 2.7% compared to 2016 at $638 million, and its operating income was up 14.5% to $148 million. Operating income for the quarter increased over 16% from the second quarter of 2016 to $74.8 million. NOG continued to deliver solid operating income margins. Additionally, we booked almost $170 million of work for NOG this quarter. This segment's backlog at the end of June was near to $3.3 billion. Compared to Q2 2016's revenue of $47.9 million, the Nuclear Power Group or NPG's business grew 13.8% to $54.6 million. Revenue growth in this segment was primarily due to the acquisition of BWXT Nuclear Energy Canada or NEC as well as an increase in our components business. Combined, these increases contributed more than $30 million in revenue, and more than offset timing differences for outage work. Year-to-date, the segment increased its revenue $48 million or 57.2% to $132.2 million. Operating income for NPG in the second quarter was $6.5 million as compared to $26.7 million in the second quarter of 2016. But recall that Q2 2016 included a $15-million benefit from litigation.

Furthermore, in 2016, service volume was light in the first quarter and strong during the second quarter. In 2017, the inverse was true. Net of the litigation benefit booked in the second quarter of 2016, year-to-date operating income in 2017 increased 9.2% compared to the first 6 months of 2016. Operating income margin for the second quarter of 2017 was about 12%. The segment continued to build backlog, booking $56.7 million in the second quarter, and ended the quarter with a backlog of $481 million, 25% higher than the $385 million of backlog a year ago. We are on track to meet the increased revenue and margin guidance for the year.

During the second quarter, the Nuclear Services Group or NSG segment contributed operating income of $7.8 million, including a $7.9-million benefit from -- excluding a $7.9-million benefit from a legal settlement of a contract dispute. From Q2 2016 to Q2 2017, the segment increased bookings 25.1% to $28.2 million. NSG grew revenue from $32 million in Q2 2016 to nearly $37 million this quarter, which excludes the legal settlement previously mentioned.

Capital expenditures guidance was increased from around $55 million in 2016 to about $100 million in 2017. The company's capital expenditures were $15 million in the second quarter, $6.6 million higher than the second quarter of 2016, which reflects the increased investment for the anticipated organic growth. Depreciation and amortization totaled $14.2 million for the second quarter, up $1.5 million due largely to the acquisition. The GAAP effective tax rate was 30.6% in the second quarter, better than our full year guidance due to excess tax benefits related to employee share-based payments.

As of June 30, 2017, the company's cash and short-term investments positions net of restricted cash was $152.4 million. Second quarter cash flow from operating activities generated $118.8 million compared to a generation of $85.8 million in the second quarter of 2016. As of June 30, 2017, we have $522 million of borrowing and term loans, including those made available under the September 2016 amendment, no borrowings under the revolving line of credit, and letters of credit totaling $131.3 million. As a result, the company had $268.7 million of remaining availability under our credit facility.

On August 4, 2017, our Board declared a cash dividend of $0.11 per common share payable in the third quarter of 2017. As we mentioned last quarter, we will adopt the updated pension guidance of the FASB we issued in March 2017, beginning in 2018. These income statement classification changes will not impact our EPS or net income, but will alter operating income and margins at the consolidated and segment levels, reducing what we report as operating margin in NOG by 150 to 200 basis points.

Now I'll hand the call over to Rex for a discussion of the segment operations and the outlook for the remainder of 2017. Rex?

Rex D. Geveden - *BWX Technologies, Inc. - CEO, President and Director*

Thank you, David, and good morning. John and David have already discussed our accomplishments for the first half of the year, and I will now provide some additional operating details.

As discussed, we have continued revenue momentum in the second quarter. This is due principally to strong results in our Nuclear Operations and Nuclear Power segments. We continue to experience growth in Canada, both organically and in the acquired business. As anticipated, we are realizing very good cost synergies from the acquisition of the BWXT NEC business, and we expect to see significant revenue synergies in the future. This is underscored by NPG segment operating margins, inclusive of amortization of intangibles of nearly 12% in the second quarter. Nuclear Operations delivered strong operating margins, 400 basis points above Q2 of 2016. Upon adoption of the pension accounting change in 2018 that David mentioned, we do expect margins in Nuclear Operations to drop by 150 to 200 basis points. However, we anticipate that NOG will continue to have a FAS/CAS pension benefit of 200 to 300 basis points for several more years.

We are still confident in the missile tube market, and are progressing well on the current contracts. Up to this point in time, we have 1 contract, and manufactured about half of all the missile tubes that have been awarded and continue to project the total market share of about 60%. In accordance with our prior plans, we are well capitalized for higher production rates, and are well positioned to compete for future awards.

Nuclear Services performed very well compared to prior comparable periods, both in second quarter and year-to-date. Strong operating income performance in the quarter resulted from a combination of superior outage performance in the U.S. services business, and improved contract performance at U.S. government sites where we perform management and operations and environmental remediation services. We continue to forecast growth in this segment with anticipated gains in market share. To that end, we are extremely pleased with the $1.5-billion award for Paducah, Deactivation and Remediating -- Remediation project mentioned earlier by John.

At the consolidated level, we booked approximately $255 million of new orders in the second quarter of 2017. Consolidated backlog remains high at $3.8 billion. NOG's strong backlog of nearly $3.3 billion is above the level of the prior comparable quarter and excludes approximately $800 million of negotiated but unawarded options. NPG ended the second quarter with a backlog of $481 million, almost 25% more than the prior period. As John said, we updated guidance for the full year 2017, and now expect adjusted earnings per share between $1.97 and $2.07. Adjusted earnings per share exclude any mark-to-market adjustments for pension and postretirement benefits recognized during 2017, and other items listed in the non-GAAP reconciliation tables found in Exhibit 1 of our earnings release.

Other changes for guidance for the full year 2017 include the following: Nuclear Power's segment revenue will increase to between $265 million and $275 million. Nuclear Power operating margins will approach 12% inclusive of the amortization of intangibles. R&D expenses captured mostly in our Other segment will rise to approximately $10 million to support acceleration of promising R&D efforts. Effective tax rate will decrease, and is expected to be between 31% and 33%. All other guidance remains unchanged.

As we discussed, the company performed exceptionally well with adjusted earnings per share of $1.11 in the first half. However, we will experience some expected softening in the second half of the year due to the following factors: lower production due to holidays and plant maintenance outages in the second half of the year compared to the first half and nuclear operations; lower fuel production in Canada due to a normal month-long plant shutdown for the maintenance and in addition to cyclical softening and component deliveries and lower volume outage work in both the U.S. and Canada in the second half; and we expect higher incremental R&D expenditures in the second half of the year compared to the first half of 2017.

Beyond our expected 2017 results, we continue to anticipate the adjusted earnings per share, compounded annual growth rate will be in the low double-digits for the 3-, 5-year period following 2017. This longer range forecast includes anticipated growth in missile tubes, adding the larger-size Columbia Class production and Virginia class production remaining at 2 submarines per year. As discussed, there are additional scenarios being contemplated, which would create even greater volume for BWXT, but they are not considered in our forecast or our CapEx guidance, for example, scenarios wherein the Navy procures more than 2 Virginia class submarines per year, or accelerates the pace of aircraft carrier production above the current rate of 1 vessel every 5 years, are not included in our strategic forecast or CapEx guidance. However, we've been planning for the possibility of increased production levels and best can be viewed as upside should any of these scenarios manifest positively.

We continue to emphasize 5 key dimensions of growth: growth in Navy nuclear propulsion based on higher customer demand; growth in the Canadian commercial nuclear market with the concrete opportunities and reactor servicing and refurbishment; increased profitability of the Nuclear Services business as we've recaptured market share and find new avenues for growth, such as space nuclear propulsion and power; R&D driven organic growth; and strategic acquisitions. We see significant opportunities in all of these areas, and we'll provide additional details at the appropriate time.

We have substantial balance sheet capacity, and remain committed to a balanced capital-allocation approach with a focus on investments and operational improvements that will smartly grow the business. We are confident about numerous organic growth prospects, and we'll continue to invest capital to support these opportunities. We are also actively working our M&A pipeline and see multiple opportunities that may be actionable. To ensure that we are maximizing value for our shareholders, the returns on these growth-focused investments will continue to be evaluated against share repurchases and other capital investment options. We have $193 million remaining in share repurchases authorized by the BWXT Board.

To conclude, we had a strong second quarter due to our continued focus on operational excellence and growth in our chosen markets. We are pleased with our progress and have raised our 2017 guidance. Looking beyond 2017, our strategic plan features additional growth opportunities that fit our strengths and increased options to participate in the markets we are currently serving and potentially, interesting adjacent markets. We remain very well positioned to serve our customers and address market needs, and we are prepared to face the growth challenges that lie before us.

That concludes our prepared remarks, and I will now turn the call back over to the operator, who will assist us in taking your questions. Operator?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And your first question will come from Robert Labick of CJS Securities.

Peter Lukas

It's Pete Lukas for Bob. Clearly a strong visible growth with existing platforms, Columbia being the larger missile tube, et cetera. You guys touched on it briefly, but can you talk a little bit more about how you look for additional growth organically and kind of go through the process there?

Rex D. Geveden - *BWX Technologies, Inc. - CEO, President and Director*

Sure. We've got the 5 categories of growth, Pete, that I mentioned earlier. We see growth in Technical Services part of our business based upon a steady pipeline of opportunities that are available there that we are competing for. But we have mentioned the missile tubes and the Navy demand going forward. We also -- we very much like the growth opportunities -- organic growth opportunities that are occurring in Canada. We've talked about this in some detail in past conference calls, but that market is essentially doubling from about CAD 1 billion per year that we can address to about CAD 2 billion that we can address based upon the plant refurbishment schedules. We were just in Canada for our Board meeting, we heard from both CEO utilities, Bruce Power and Ontario Power Generation are quite confident about the future of the nuclear utilities in Canada. So that's one of our largest growth opportunities. We have -- and we mentioned this last year in connection with our strategic plan and started to focus on some R&D-driven organic growth. We haven't been very specific about that yet because of competitive sensitivities, but we're very bullish on some things that can meaningfully change our portfolio going forward, add new and interesting dimensions. And then maybe the final category is that we have some interesting possibilities in what we are calling strategic nuclear materials. Again, we haven't been very specific about that, but those opportunities are becoming very concrete for us and we'll lead us in future growth. I would say -- I would tell you that from an organic growth perspective, some of what happens in our organic growth just comes out of opportunities that naturally arise with the acquisition plans of our current customers, but another dimension of it is that our strategic planning process is very rigorous and it drives out interesting ideas, and we are getting some lift in the future from strategic ideas.

Peter Lukas

Very helpful. And lastly, you mentioned significant opportunities for new opportunities in current adjacent markets. Anything you are able to elaborate on there to give us a direction to be looking?

Rex D. Geveden - *BWX Technologies, Inc. - CEO, President and Director*

Yes. We haven't disclosed anything there yet, again, Pete, because of competitive sensitivities. We hope to do so in the fairly near future, but those opportunities are shaping up in concrete ways and we'll say more about it later.

Operator

And your next question will come from Pete Skibitski of Drexel Hamilton.

Peter John Skibitski - *Drexel Hamilton, LLC, Research Division - Senior Equity Research Analyst*

Yes, I guess, maybe for David. David, just the revenue was a little bit soft in the quarter versus expectations, and I just wanted to verify, was the number of workdays this quarter the same as in 2Q '16? Just wondering if there was any differential there.

David S. Black - *BWX Technologies, Inc. - CFO, SVP and Treasurer*

Yes, I don't think there was a differential in workdays. I mean, I think, once again, revenue for us is as expected. So for the street, there was a miss, but for us, we're still looking at our revenue plan and meeting that revenue plan. So for us, it's in line.

Peter John Skibitski - *Drexel Hamilton, LLC, Research Division - Senior Equity Research Analyst*

Okay. So in the 10-Q, the [tiding] items you outlined at NOG, you mentioned just material purchases and fuel deliveries related to downblending. Those are truly just timing issues...

David S. Black - *BWX Technologies, Inc. - CFO, SVP and Treasurer*

Yes. I mean, we've got -- we've long-lead material, there's some timing issues in the fueling, there could all be small timing issues as you go through. So we see no concerns about the revenue line and where we are at today even when we look at last year.

Peter John Skibitski - *Drexel Hamilton, LLC, Research Division - Senior Equity Research Analyst*

Okay. And then the NPG, you did raise the revenue guidance there. Can you talk about -- anyways, you guys why you raised that -- the revenue guidance at NPG? And that on a total-company basis at this point, are you may be looking at close to the mid-point revenue guidance or the upper end? Just whatever color you can add on that would be great.

David S. Black - *BWX Technologies, Inc. - CFO, SVP and Treasurer*

I mean, so for NPG, obviously, we were able to get our hands more around what we acquired with NEC. And just looking at the market out there and what we are able to obtain, and if you look at our backlog also, very strong backlog at NPG. So we just relooked at the business up there, and felt that the guidance there needed to change a little as well as -- we got our hands around the margins and we feel now that we can raise the margin guidance now to, say, approaching the 12% instead of the 10% inclusive of the amortization of the intangibles. So I think from that standpoint, we are able to do that. Now when you look at NOG, you've always got to remember that as we look through the NOG revenues, as we get through the year and we find out where we're going to get our savings, a lot of times your revenue's going to look differently because you recognize less revenue on an NOG business, but you're recognizing more profit as you are taking some of those savings, you are not going to recognize revenue and profit. So you have a different way of looking at revenues through the year because of the way it goes through the contract.

Operator

Your next question will come from Robert Spingarn of Credit Suisse.

Robert Michael Spingarn - *Crédit Suisse AG, Research Division - Aerospace and Defense Analyst*

High level going back to this opportunity with the overall budget, how should we think about upside on Virginia class? Is the right way -- do you guys think about potential upside in units to perhaps 3 or 4 year in the non-Columbia funding year? So those would be 2022, 2023 and 2025, is that one way to think about that?

Rex D. Geveden - *BWX Technologies, Inc. - CEO, President and Director*

Yes, Robert, this is Rex. Yes, that's one way to think about it. From our prior guidance as we sort of hammered on in our prepared remarks, we had been assuming a continuous production of 2 Virginias regardless of whether or not Columbia procurement occurs in that year, but we've seen from the Congress now, both from the authorizers and from the appropriators, this scenario where you've got 3 Virginias in certain years to get a jump on building up the Virginia class size. I think you know the Navy's talked about taking the Virginia -- the number of Virginia boats from 48 up to 66. In order to do that in a meaningful timeframe, you'd really have to accelerate some of that on the front end. So that's not in our guidance up to this point. We haven't forecasted around that way, so you can think of those years where you built 3 Virginias as real upside to the business, and by the way, we're starting to think of that as a likely scenario. There's the mother...

Robert Michael Spingarn - *Crédit Suisse AG, Research Division - Aerospace and Defense Analyst*

Well, I was going to ask you now that just on the back of that, so if that's a likely scenario, how far in advance do you need to do any -- spend any capital -- CapEx, number one, for that third Virginia? What's the magnitude of the CapEx to get ready for that? And what kind of incremental margins would you get on a third Virginia during the periods where you're actually doing that?

Rex D. Geveden - *BWX Technologies, Inc. - CEO, President and Director*

Well, so as we've discussed in the past, when you think about the delivery of the nuclear components to the shipyards, that's considered a long-lead item for the ships, and so the orders for our components are about 2 years ahead of the ship-building schedule that you normally see. In order to capitalize for that production, we need to order large vertical mills and similar kinds of equipment to expand our capacity, and we need sort of 1 or 2 years' notice to be able to do that. So we're in a pretty active dialogue with our customers right now about the capitalization necessary to be ready for this additional production. So we're making decisions around that right now. From the standpoint of incremental revenues and incremental capital, the thing that we disclosed in the past was that we thought for the 2-Virginia scenario, there'd be perhaps $2-plus billion of incremental revenue. From a margin perspective -- incremental margins, they are not going to be substantially different than what we experienced right now, because we renegotiate these market-basket agreements every 2 or 3 years, and so any cost reductions that we may get captured in that, so you could think of incremental revenues as consistent with what we normally see out of NOG.

Robert Michael Spingarn - *Crédit Suisse AG, Research Division - Aerospace and Defense Analyst*

I just want to be clear, that $2 billion you just mentioned refers to what and over what period of time?

Rex D. Geveden - *BWX Technologies, Inc. - CEO, President and Director*

Okay, that was referring to just a 2 Virginias per year over about a 20-year period is what we had disclosed before, so if we get into this scenario of 3 Virginias in the near term, then it's more capital and it's more revenue.

Robert Michael Spingarn - *Crédit Suisse AG, Research Division - Aerospace and Defense Analyst*

Okay. And then just a housekeeping question on the tax rate. It sounds like you are guiding for slightly higher tax rate in the second half, notwithstanding the fact that you just took it down, how does that flow in Q3 and Q4?

David S. Black - *BWX Technologies, Inc. - CFO, SVP and Treasurer*

I mean it's -- the way I'm looking at it, it's going to be consistent in Q3 and Q4, but overall, the year's going to come out probably the midrange of what we're now saying, 31% to 33%.

Operator

The next question will be from Nick Chen of Alembic Global.

Nicholas Chen - *Alembic Global Advisors - Equity Research Associate*

So just looking at the quarter, obviously, came in ahead of our expectations. It seems like there was a lot of strength out of the projects going on in Canada. I was just wondering, how much ahead of your expectations is that performing?

Rex D. Geveden - *BWX Technologies, Inc. - CEO, President and Director*

So the way we kind of put it in the past, Nick, is that the cost synergies are probably better than we anticipated. The revenue synergies really are mostly going to be realized in the future, but we're starting to see some of it. We've got visibility into a -- we announced in Q2, for example, or just after the close of the quarter that we've been awarded a $34-million Canadian contract to supply large motors for the pumping systems at the Bruce Power site, and there's more opportunity behind that. That's an example of business that we wouldn't have had without the acquisition that's real strategic synergy for the business. So that's the cost synergies sort of in summary here shaping up, I think, better than we thought. You are seeing that reflected in our margins. We started the year with guiding margins at around 10%, because we had pretty high amortization hurdles with that acquisition. But you saw we've done 18% in the first quarter, thereabouts in 12% in the second quarter, so we've experienced consolidated margins at about 15% year-to-date in that business, and part of that is just better cost synergy with the acquisition, and part of that is just very good performance with our portfolio of projects. So yes, we like the business very much. The cost synergies are good, the strategic synergies are going to come, and I think we're all going to believe for years to come that this was a good, strategic acquisition for the business.

Nicholas Chen - *Alembic Global Advisors - Equity Research Associate*

That's great to hear. And then just in terms of the missile tube contracts, I was hoping we could get an update there and also just around the investments you guys are making into the Mount Vernon manufacturing facility?

Rex D. Geveden - *BWX Technologies, Inc. - CEO, President and Director*

Yes, sure. In terms of updates, we are right in the middle of manufacturing missile tubes. We hope we start delivering the first of those a little bit later in the summer, and we're doing well with our production. What we did in Mount Vernon was we took a building that was kind of in standby for the last 20 years, and we've completely refurbished it. Building 219, we call it. It's a gleaming palace ready for high production levels, and the customer seems inclined to go towards more or less continuous production scenario where they might order up to about 100 tubes per order, perhaps split among, let's say, 2 suppliers. And so we've capitalized to be able to capture the largest share of whatever gets awarded. We also have invested -- made the decision to invest in some large machining capabilities there in addition to what we already had on the Mount Vernon side, so we're spending significant amounts on machining capabilities in addition to that facility reimbursement.

Nicholas Chen - *Alembic Global Advisors - Equity Research Associate*

That's great. And then just the final question, going back to your guys' opening remarks about the potential ramp up in the submarine programs. I think you said, just to be clear, that could add an additional $4 billion of revenue?

Rex D. Geveden - *BWX Technologies, Inc. - CEO, President and Director*

No, let's be clear on that. What we disclosed before was that if we got to the 2 Virginias per year continuous production, that's what our prior guidance was about and our prior forecast strategically was about, assuming that 2 Virginias, and that's the one that gets you $2 billion plus in incremental revenue. And what we said now is if you look at all of these other possibilities, the 3 Virginias in some years and going forward, aircraft carriers and such, that kind of, what we call it the kitchen-sink scenario where it's all happening, that gets you to maybe $4 billion in incremental revenue, so we're talking about a difference between $2 billion and $4 billion compared to prior guidance.

Nicholas Chen - *Alembic Global Advisors - Equity Research Associate*

Okay. And if it were to get to that level, do you guys have the capacity to take on that sort of work? Or would that require a lot more investment into your manufacturing footprint?

Rex D. Geveden - *BWX Technologies, Inc. - CEO, President and Director*

Yes, we don't yet, but we are very sure that we could get the capacity for that. We would have to make investments. We certainly have to hire several hundred people to make that happen, but we've done the planning forward, it's been presented to our Board and we could get on that trajectory.

Operator

And the next question will come from Kristine Liwag of Bank of America Merrill Lynch.

Kristine Tan Liwag - *BofA Merrill Lynch, Research Division - VP*

I just wanted to clarify for the $4 billion incremental revenue that you guys highlighted, so what does that imply for the rate of carrier procurement? And also, how high is your expectation for Virginia class? It sounds like it's more than 2, but is that 3, is that 4? Can you provide a little bit more detail?

Rex D. Geveden - *BWX Technologies, Inc. - CEO, President and Director*

Sure. So what has been discussed and with the authorizers and with others that the possibility of -- for the aircraft carriers instead of doing 1 boat every five years, there's been some discussion around going to a 1 every 3 years, alternating with 1 every 4 years, which gets you about 1 every 3.5 years, and that's the high-volume scenario for us, of course. Each of those carriers has 2 reactors. Those reactors are large and so there's some interesting volume implications with that. We have also looked at, and what seems to be in my opinion a more serious consideration on the part of the Congress, is the idea of building perhaps 3 Virginia submarines in some of the early years, 3 of those early years. And so those are the kind of volume scenarios that we've been talking about. If you added all that stuff together, that gets you to the $4 billion plus incremental revenue guidance that we gave, and it's in, by the way, that's a pretty rough number. We certainly would have to sharpen our pencils around different scenarios, see how that impacts revenues.

John A. Fees - *BWX Technologies, Inc. - Executive Chairman*

Yes, if you take a look at it, what we were trying to provide is some view for you all between what we've been saying, which is the incremental Virginia, which is the $2-billion scenario that we talked about, but if all these things being discussed are to occur, what's sort of the other side of that. And so we're just trying to give you sort of some bookends to think about it in terms of what could potentially happen and what could potentially impact us, and what's the magnitude of that impact there.

Kristine Tan Liwag - *BofA Merrill Lynch, Research Division - VP*

That's helpful. And if you are able to capture this opportunity, how should we think about margins? Are you be able keep any sort of incremental economies of scale or anything like that? Or do you have to share that all with the Navy?

David S. Black - *BWX Technologies, Inc. - CFO, SVP and Treasurer*

Once again, I think, we repriced these market baskets into the future, so our margin picture will stay the same over time. What we state now that is that our margins will be in the high teens and that's where they will stay. Most of the future pricing, any benefit that we get will go to the government, and so...

Rex D. Geveden - *BWX Technologies, Inc. - CEO, President and Director*

And then I'm just -- I might add to that, Kristine, that part of that dynamic is our government customers have heavily incentivized us to reduce costs, obviously, and so within a market basket when we drive down cost, we can drive up margins and David talked about that earlier in the call, this dynamic between driving down your cost, and therefore, taking a little bit of a revenue sacrifice in order to get incremental margin improvements, and that's very characteristic of what happened in Nuclear Operations in Q2.

Kristine Tan Liwag - *BofA Merrill Lynch, Research Division - VP*

That's great, and maybe lastly for me. For the Columbia Class submarine, how is the missile tube procurement of that program different from the Virginia class or are they similar? And do you also expect to get 60% of that market as well?

Rex D. Geveden - *BWX Technologies, Inc. - CEO, President and Director*

Yes, we are the only contractor that's currently been awarded contracts to produce missile tubes for both the Columbia Class and also the Virginia class. Differences are that the Columbias have 16 missile tubes per boat, the Virginias will have -- after Block V, will have 4 missile tubes per boat. They're similar looking things, but they're different in function. Missile tubes for Virginia are to hold tactical missiles and Tomahawk missiles, and each of those missile tubes hold 7 Tomahawks. The Columbia Class missile tubes hold the strategic missiles, the Trident missiles, for strategic strike capabilities, so they serve very different military purposes. If you look at them in terms of scale, size, they're pretty similar, but very different in quantity and somewhat different in function.

Operator

(Operator Instructions) Your next question will be from Michael Ciarmoli of SunTrust.

Michael Frank Ciarmoli - *SunTrust Robinson Humphrey, Inc., Research Division - Research Analyst*

I think just on the Nuclear Power Group, the organic growth looked to be down pretty significantly, and I guess, that's based on timing and the outages. You raised the revenue guidance, and I understand, I see the margin guidance up to 12%, but can you maybe just talk about the back half of the year. With the revenues presumably being increased, you're still only employing maybe a 9% margin run rate to get to that 12%, I mean, are you guys -- should we expect the margins to be at that 9% or 8% in the back half of the year? I mean, is there a mix issue that is impacting the profitability? On the updated revenues, I would have thought with the higher volumes we would have seen actually, at least, maybe the 12% or better sustained in the back half of the year.

Rex D. Geveden - *BWX Technologies, Inc. - CEO, President and Director*

Michael, Rex here. Let me comment on the first half first, this -- the -- as revenue -- the serial revenue between the first quarter and the second quarter. First quarter, we had very strong revenue numbers, and there were sort of 2 components of that. One other -- one component was we did have very high-volume service outage in Canada, and service revenues in the first quarter, that's off in somewhat in the second quarter, that was completely anticipated. We also had a very large component delivery in that first quarter, that was the -- it's a system called Browns, it's the fuel handling system that we -- that got delivered out of our acquired business, with the acquired GE business. And so that roll-off between first quarter and second quarter is completely anticipated. And you'll see some of that in that business. There's -- because of some of the chunkiness in component deliveries and the service cycling, you'll see some uneven revenue there. Now in terms of the second half, we do expect to see a little bit of, let me call it, margin compression in the second half. It's due principally due to the fact that for a month of each late summer we have a fuel maintenance outage. We shut down the plants, clean out the furnaces and refurbish the robotic equipment and so on, and so we have a revenue dip -- natural revenue dip in Q3 because of the fuel plant outage that's planned and will occur on an annual basis, and that's part of the reason for our view on the second half.

Michael Frank Ciarmoli - *SunTrust Robinson Humphrey, Inc., Research Division - Research Analyst*

Got it, got it. That's helpful. And then just maybe, Rex, if you could, trying to get a handle on the Columbia Class, and I know you guys don't really disclose the revenue per ship set. You've mentioned all these scenarios, but how should we think about if the most robust scenario doesn't play out or maybe even the scenarios subsisting the Virginia class at 2 don't play out? Can you guys still grow the top line organically just with the Columbia Class progressing? I mean, if we look at the funding for nuclear propulsion on the Columbia Class versus the Virginia, I mean, it's about $1.7 billion versus the $1 billion. So is that going to be a just a natural organic growth accelerant regardless of any other scenario?

Rex D. Geveden - *BWX Technologies, Inc. - CEO, President and Director*

I mean, the Columbia is a larger boat than what we currently have in our current forecast of the Virginia, so to me, the Columbia is an organic growth avenue for us. And then, obviously, when you throw the additional Virginia on and that's when we talk about the $2 billion plus, so I think inside of the government forecast and what we're planning on, we got that organic growth in our -- as we've said in the past, all we can say about that is that it's larger than a Virginia. As we get into these growth scenarios, we always got to remember that the pricing on an incremental boat is going to be somewhat cheaper than a boat we have now because of the fact that all that fixed cost has already being absorbed, so you're only looking at the variable and the incremental cost. So you've got to remember all of those things when we're looking at this growth trajectory we're talking about for the Columbia and then the second Virginia.

Operator

Your next question will be a follow-up from Pete Skibitski of Drexel Hamilton.

Peter John Skibitski - *Drexel Hamilton, LLC, Research Division - Senior Equity Research Analyst*

I think last quarter, you said you may need to use some incremental working capital this year if you won some tech services contracts and we've got one, obviously, there. But as a result, free cash and income would be below one time. Is that likely to play out? Are you going to use some working capital and free cash should a bit depressed on that basis this year?

David S. Black - *BWX Technologies, Inc. - CFO, SVP and Treasurer*

I mean, once again, it just depends on those bids we have outstanding and those bids we win, so certain wins, whether it's in NNSA or DOE environmental management, some of those require more working capital than others just based on how the contract is structured. So it's based on which contracts we win and when, whether or not that working capital be used for that specific purpose, and as we win those in the future, we'll let you know that one is one that we'll use working capital or not. But we're forecasting wins and forecasting some use of working capital for that.

Peter John Skibitski - *Drexel Hamilton, LLC, Research Division - Senior Equity Research Analyst*

Okay, okay. So we're talking here on at least another 1 or 2 before the year is out?

David S. Black - *BWX Technologies, Inc. - CFO, SVP and Treasurer*

I hope so, but unaware. It's contingent on the government and their decision making.

Peter John Skibitski - *Drexel Hamilton, LLC, Research Division - Senior Equity Research Analyst*

Got it, okay. And then, guys, on the NASA study contract that you won, I guess, for the Mars mission, I'm just curious how big that contract could be if it went on into production? Might imagine it would be a smaller type of a reactor, but curious as to the order of magnitude of the sales opportunity there?

Rex D. Geveden - *BWX Technologies, Inc. - CEO, President and Director*

Okay, thanks for the question, Pete. Yes, that's an exciting win for us. That study contract is just short of $20 million as you know, but we're in the very, very early stages of that. We just keep looking at fuel design and core design. We've got some estimates out there, they're pretty rough at this point, but should NASA move to nuclear thermal propulsion system into their exploration architecture, and we went into a test phase and into a manufacturing and delivery phase, we estimate that the total program would be in the range of $600 million to about $1 billion, so it'd be a very substantial program for us, over a period of, let's say, 10 years. Now if this became a normal architectural element and we're producing these on a regular basis, then there is higher potential from that, but if we just delivered a one-off design, tested, manufactured, let's call it, somewhere between $600 million and $1 billion.

Peter John Skibitski - *Drexel Hamilton, LLC, Research Division - Senior Equity Research Analyst*

That's great, that's great. Okay. And then I want to ask if there's any impact to you guys from this recent Scana decision, South Carolina, to stop work on the 2 commercial nuke plants? I would guess it wouldn't be that meaningful, but I just want to check for sure.

Rex D. Geveden - *BWX Technologies, Inc. - CEO, President and Director*

No, Pete. It's -- we have very little exposure to the U.S. commercial nuclear power generation market, so no material impact on us.

Peter John Skibitski - *Drexel Hamilton, LLC, Research Division - Senior Equity Research Analyst*

Okay, right. And then last one. I just want to get a feel for -- with the new adjusted EPS guidance, guys, at the high end of the range, you're looking at approaching 20% EPS growth here in '17. Going forward that's a high bar for a low double-digit type of the EPS CAGR going forward. You guys are still comfortable despite there's high bar you set here for yourself that, that kind of 3 or year 5 target you feel is still very achievable?

David S. Black - *BWX Technologies, Inc. - CFO, SVP and Treasurer*

Yes.

Operator

And ladies and gentlemen, this will conclude our question-and-answer session. I would like to hand the conference back over to Alan Nethery for any closing comments.

M. Alan Nethery - *BWX Technologies, Inc. - VP of IR and Corporate Procurement*

Thanks, Denise, and thank you for joining us this morning. I'd like to remind everyone that our Investor and Analyst Day is October 4, and a link to the webcast throughout the day will be available on the Investors section of our website, bwxt.com. That concludes our conference call. Replay of this call will be posted on our website later today. Will be available for a limited time. If you have further questions, please call me, (980) 365-4300. Thank you.

Operator

Thank you, sir. Ladies and gentlemen, the conference has now concluded. Thank you for attending today's presentation. At this time, you may disconnect your lines.
