

Company Name: Aerovironment Inc  
Company Ticker: AVAV US  
Date: 2016-08-10  
Event Description: Jefferies Industrials Conference

Market Cap: 672.17  
Current PX: 28.78  
YTD Change(\$): -.69  
YTD Change(%): -2.341

Bloomberg Estimates - EPS  
Current Quarter: -0.148  
Current Year: 0.295  
Bloomberg Estimates - Sales  
Current Quarter: 38.117  
Current Year: 271.333

## Jefferies Industrials Conference

### Company Participants

- Wahid Nawabi
- Steven A. Gitlin

### Other Participants

- Howard Alan Rubel

## MANAGEMENT DISCUSSION SECTION

### Howard Alan Rubel

Good morning. Hi, I'm Howard Rubel with Jefferies. I'm the – I'm a Managing Director in the equity research department covering aerospace companies along with the rest of my team. And today it's great pleasure to have with us Wahid Nawabi, who is the Chief Executive Officer of AeroVironment. And AVAV is actually the third of our AAA line up today.

We have, as you know, Astronics earlier, AVAV, and then later in the day ATI. So the combination sort of makes for a very good show here, I think, of some very capable companies.

Wahid became a CEO and a member of the board in earlier this year. And prior to joining AeroVironment, which was – when he joined in 2011, he had been with American Power Conversion. And he originally joined AeroVironment to run the EES business, and he's now got a great command of both of the business units. And frankly, I've spent some time with him, and I think he's got some great ideas in terms of how to take the technology of the company forward.

And Wahid?

### Wahid Nawabi

Thank you.

### Howard Alan Rubel

Thank you very much.

### Wahid Nawabi

Thank you. Good morning to all. And thank you, Howard, for the introduction. And thank you for inviting us to be part of this conference in this venue. So I have a presentation, I'm going to try to walk through this few slides and we'll leave some, 10 minutes roughly, Howard, for Q&A at the end.

This is a presentation that is actually on our website and we gave this presentation and released it at our fourth quarter earnings which was in June. So if you like to go back to this and look at the slides at your own leisure later, you can access it directly from our website.

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This is our Safe Harbor Statement, of course you know we're in a quiet period now and essentially you're familiar with this and if you'd like to read this of course it is available as part of the package on the website as well.

So there is basically three things I wanted to talk to you about. First and foremost, give you a overview of who is AeroVironment, what do we do and why should you care and why should our customers care; and then secondly is, talk to you little bit about our specific new growth ventures or opportunities that strategically we believe that has a large long-term value creation opportunity for stakeholders; and then, of course, lastly, share with you the financials as of fourth quarter of last earning that we released to the market.

Company, so who are we? Really, we exist and we – our business is all about helping our customers succeed in their missions, whether we deal with defense customers in the security space, the Army, Marine Corps, Navy or with electric efficient energy systems designing battery pads for electric vehicles or charging systems, we provide what I call reliable, innovative, disruptive technologies that help our customers in their day-to-day operations and activities and missions to succeed and proceed with certainty.

And so, historically, that business has been for 45 years an innovation-based organization in a culture and company. Going after large, just large markets with an innovative, differentiated, disruptive solution and we have an IP portfolio and a track record that we have deployed this, what I call recipe and strategy to implementation with successful outcomes. And we continue to pursue the same strategy as we go forward.

Pretty much, very – historically, we've been very adaptable to change and we have selectively chosen, based on our interactions with specific customers, markets that make sense that we see value and value creation in solving customer's problems. And, historically, also, all of our solution has been what I call highly differentiated, highly innovative and technology based. So although we play in the aerospace and defense space and we also play in the, what I call, electric vehicle charging infrastructure business, we're also a technology company. Really, we bring to the table a differentiated technology capability which I am going to briefly talk to you about in the next few slides.

We have a very strong position in the core markets that we play, for small unmanned aircraft systems as well as in electric vehicle charging and we have a very clean and solid balance sheet, which enables us to judiciously apply our investments and our resources to opportunities that we believe that have the highest return based on risk adjusted probabilities of success on those opportunities, and I'll share some of that with you as we go forward. And then, of course, our solutions have been differentiated. We pioneered the markets and the products and capabilities that we have developed for the customers that we're engaged with.

Been around since 1971, about \$635 million in market cap, you could read some of the specifics there. Our fiscal year 2016 which ended in May was \$264 million in revenue, and we have since 2004 to 2016 about a 15% CAGR on our sales. And although we represent about 85% of the U.S. DoD's inventory of unmanned UAVs, its relatively small amounts in terms of dollars, about 3% or [indiscernible] (06:44) 3%. So it's about 86% to 85% of the DoD's unmanned systems is really our inventory, about 30,000 plus airplanes out there flying within the U.S. domestic market as well as now we have 30 plus international customers that are in different phases of adoption of the same capability and technology. And of course in the EV charging business, we have established a leadership position, market position, both in industrial electric vehicle charging as well as the on-road electric vehicle charging.

Brief history, all I could tell you that when I joined the company about five years ago, this was quite an impressive track record and background of the company that I realized quickly that I was very excited about and wanted to be part of. So many world records, seven vehicles in the Smithsonian Institute, records of highest altitude, flights for unmanned aircraft, solar-powered aircraft.

Some interesting points; 1989 General Motors contracted with AeroVironment to develop the first, what they referred to as the modern electric vehicle today. And it was called the General Motors Impact. It was a prototype to the production version of it, was called EV1 by General Motors. And so, see the picture of the Nano, what we call Hummingbird on the cover of TIME Magazine that was in 2011.

And there are many other ones that you could see here, and of course on the website if you have [ph] ready (08:23) time, in your leisure, you could read. But essentially the track record shows a consistent and relentless pursuit of –

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taken on very difficult technology and customer challenges that has never been done before sort of and then proving that in certain cases of course commercializing it into a real business, profitable business for our shareholders. And that's been the history of the company in all the markets that we played in.

We operate in primarily two domains or segments Unmanned Aircraft Systems and Efficient Energy Systems. And then on the Efficient Energy Systems is primarily in terms of industrial charging of electric forklifts and airport tugs, as well as test equipment to design battery packs and drivetrains for hybrid electric plug-in vehicles, as well as on the UAS side, it's primarily small unmanned aircrafts. These are hand launched, back packable, small force-based capabilities that AeroVironment innovated and essentially took to the market, to the customer, and then became a very successful, profitable business for us as our core business.

And then, of course, that has expanded into Tactical Missile Systems that we refer to or its also referred to lower ammunitions which is essentially when you see a bad guy and you have identified a target over a hill or over a mountain in dangerous environments, then you actually – you can prosecute that target, with very precise capabilities and differentiated features and performance characteristics, that's part of that capability.

And so on both of those two markets, we [ph] off (10:20) those domains we have established strong positions as a core business that offers growth by itself. And in addition to that, we have additional strategic growth initiatives that we pursue on these three fronts, primarily three fronts that also have very large long-term prospects for growth and return for stakeholders.

First one being Tactical Missile Systems, that's what I described to you earlier. You might have heard the word Switchblade, which is one of our products names, and that's the picture on the top left of the right hand side of the half of the screen. And essentially if you're a soldier out in the field, and you see the identify the back target or somebody is firing at you, that you don't know where it's at, you can fly this UAV, take off the backpack, put it on the ground launch it and go see what's going on, identify a target and then if you decide don't want to take it out, then you get prosecuted as you wish, as you see fit.

And then, of course, the other capability is that it has the ability to – for you to wave it off. So if a good person, many of you probably seen the movie called Eye in the Sky. This capability essentially allows you to wave off and change your decision at the last few seconds or minutes of the mission, and so that's a capability that our customers see a tremendous value in, specifically. And now we have multiple variants of that, that we have described in the market, one of which that our customer chose to publicly talk about and that's Blackwing, the picture next to it, which essentially is a flying periscope for us for submarine or any other underwater vehicles.

And so this market referred to as Tactical Missile Systems or application is again an area that we have innovated, we have brought products to the market with customers and innovated over time and has led to a business now which has multiple variants and we see a tremendous potential long-term for the business, for the customer and markets.

Commercial UAS, I'm sure you've heard of a lot of this in the news quite lately. We're focused on that market and I'll share with you some details on that. And we – and then of course the other category of our strategic growth initiative is what's referred to as atmospheric or stratospheric satellites. This is an airplane that we – on the left side you see, it's called the Global Observer, think of a airplane – unmanned airplane, the wingspan of a Boeing 767 flying and going at almost twice the three times the altitude of a passenger airline. Passenger airplanes fly in about 30,000 feet or 40,000 feet; this goes 50,000 feet to 60,000 feet way above that.

And it's – atmosphere is really thin, flying is really challenging and difficult, temperatures are really extreme and it could stay there for days and if you had to pair this, essentially you have a atmospheric satellite that can operate and do multiple different what I call missions, whether its communications, ISR and other things and carry different payloads and it can do it in that type of a model where you can also bring it down a lot easier and upgrade the payload and change the payload and do different things, which you can't really do with satellites in general.

So that's an area that we got customer-funded investments many years ago, and we developed the airplane, the capability, and we're engaged in pursuing specific potential customer opportunities for contracts in business. Again, I mentioned 89% of the total fiscal 2016 company revenue was on the UAS side of the segment. We've had 15% CAGR

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and a fairly strong position on our core business, as I mentioned.

And then similarly on the EES side, three primarily business applications or markets that we're going after. The test equipment was actually developed for – the development of our first modern EV, the GM Impact; and it's a business now that we provide and many automakers, engineering labs and test facilities use this and we have a leading position in that space.

Industrial charging is a technology that we innovated and developed and disrupted the market with, and now we have a strong leadership position in that. And, of course, the on-road electric vehicle market is a fairly new market application that we've gone after and we provide charging solutions for both residential and trunk and public charging, workplace charging for the electric vehicle market, which of course is a new and growing market in general.

So let's talk briefly about our three growth initiatives, Tactical Missile Systems, right. This is a specific capability that we developed many years ago, maybe about seven years or 10 years ago that we first started with this. And now we have multiple variants of it, and the capability itself is tremendous, in my opinion of course. And we have a strong position in this space already. The – one of our customers, the U.S. Army has publicly spoken about a program of record, the timing of which is still not determined specifically, but it represents a significant long-term potential opportunity for us in the market and competitors. And we believe that we're positioned quite well in that space with our progress so far and our capabilities year-to-date. And we also have multiple variants of this developed, in different phases of adoption. So – and one of which that we've talked publicly about, specifically.

This is an interesting market, of course, and very attractive in terms of our capabilities and the applications that we have been engaged with early adopter customers. We are targeting specifically four market or industries, primarily precision agriculture, energy, so think of it is an oil and gas and different infrastructure that goes into energy infrastructure, transportation. And you see a picture of a railroad, and then obviously electric utilities.

And we have intentionally chosen these select applications and industries for a number of reasons. And our approach is to provide, what I refer to as a, total solution to customer's problems. At the end of the day, if you're a farmer, operating a UAV is the – probably the furthest away from your core competency as a farmer. And so, what you really want to do is, someone who could come in and help you, make the right decisions and the take the right actions as a result of a whole bunch of different things, including a UAV that flies, the payload that goes with it, the sensors and the data you collect. And then the analytics that you do with the data to tell the farmer or the railroad company or the utility as to what to do with that information and what actions to take.

So I'll show you some specific examples of this, so you can get a flavor of this briefly. Here is an example of utility that we're working with an early adopter, that we fly our fixed-wing Puma, which we've used actually in the defense applications and this can go for miles and miles and provide – take – we can fly different type of sensors to pickup different type of data information from the critical asset.

And this one is the V12 version, in this case the customer would like us to get close to that structure, whether, it's a transmission tower or a specific cabling and inspect specific parts of this structure for structural integrity, the isolators on the power lines and essentially from those missions, those flights, you collect data and you build these very precise data models that then the customer can do – we can do and the customer can benefit from the analytics that goes along with it.

In this case, of course, this is a substation. You could see specifically, how the data is now loaded up to our e-commerce cloud that we operate and we manage. And then we analyze that data and then we provide the customer with the data products and the information they asked – for them to take specific actions. And again, this is in an early – we're in early phases of developing the solution and working with early adopter customers in order to get this right solution to the market so we can have a long-term business that could be successful in this space.

This is actually even interesting one. It's a railroad working with another early adopter customer, major railroad company in North America. This actually is not a really a visual video. It's – we flew two different flights, payloads a LiDAR sensor as well as a multispectral – I'm sorry EO, which is – it is electro-optical, visual payload sensor on it. And then we took those two data points and geo-rectified it, put it together and built this real life, what I call, precise –

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what I call a spatial image and video of the critical asset. And the beauty of that is that the customer then can look at this asset and the data at different layers and different levels, in different ways.

So if you wanted to see the distances between the tracks or if you wanted to see the tolerances as to how much variation there was within the elevations of the tracks are along the track line. All of these other new, what I call analytical computations is now doable once we collect this data and we compile it and then we analyze it different ways, means, depending on the specific requirements and expectations or the needs of the customer, okay? And then, you have LEXAN image, which is what I call a digital reality image of that specific asset or track of railway tracks.

This example is the precision agriculture, and in this case you'll see a farmer could be log-in into our portal, web portal coming in and wanted to go see their specific farm. In this case, it's actually a almond farm, an almond grower, that is somewhere in a specific geography, this I believe tend – was in California. As you know, California is a predominant supplier of almonds around the world. And in this case we've identified the almond trees, the dots that you see are the actual almond trees that are planted, the different colors represent different varieties of almonds and farmers do that. In this particular case, I believe there is three different varieties of almonds. And farmers do that for harvest seasoning and pollination reasons. There is specific reasons why they do that. And we can tell the size of the almond trees, the type of almond trees, the canopy of that almond farm in terms of the canopy, the growth rates. And the other thing you could see also is, for example, the different spots that are not – does not show trees on it.

And in this case, we can run different sensors again, LiDAR sensors, multispectral camera payload sensors. And look at a variety of different things within this farm. And the farmer can then look at this what I call data in different layers of the cake, okay, as to whether – why is this particular tree has not matured or grown as expected or why is this particular area of the farm is undernourished in terms of either water or fertilizer or whatever the case might be.

And so what the farmer does in this case is, we have developed this entire portal, and we're in the process of developing it further. And you come in, log in with your access – specific access, protected, and then you get onto our cloud and you go to specific assets that you have and you can also contrast this data from historical collections of this data, maybe last season, maybe last quarter, last month. And look, for example, as to why there are these orange spots that shows lack of vegetation, lack of growth. And so this – I'm trying to give you a flavor of what this is all about, and how this becomes really powerful in terms of our customers operations and what they do in everyday.

So I've been told that this is going to work, it did work, second click. So that's an – so this particular market, we're still in the development of our solution, and we have publicly mentioned that we're going to be launching products in this space, in the market this year, and we believe that this provides a very large long-term growth opportunity for our stockholders and to other stakeholders.

And then, of course, large airplane, I spoke to you about this one, specifically Global Observer, and then also in the past AV has developed a solar high-altitude airplane, which also broke the world record. And this is a, obviously, a very large yes or no or zero or one in terms of its probability, and we're – we have been pursuing this in years and we've got customer funded R&D that we've done this work as well.

Lastly, last but not least, our footprint internationally is growing. We have a 30 plus countries now internationally that are in different phases of adoption of a small UAS, and we believe this represents a significant opportunity short- and long-term for the company, and we're focused on increasing this footprint, as well as growing our footprint within these customer base, as we grow in terms of family of systems.

And this is, of course, about electric vehicle adoption. This is a market that we really don't have a lot of influence in terms of the adoption rate itself. It's really the electric, the OEMs, the automakers, and the policymakers that can affect this, but we have a fairly strong position and when and if the adoptions take place, we're positioned really well to take sort of take advantage of the opportunity that would come to fruition for us.

Financial overview, so as I mentioned to you before in summary, basically, we have a strong core business that is profitable and offers its own growth opportunities. Okay? In addition to that we have growth – what I call, growth pieces within the core business whether it's international or Tactical Missile Systems or domestic DoD customers, we can sell new products to existing customers and in fact grow our product portfolio and customer base to new customers.

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Primarily, we've done business with the Army and the Marine Corps and special operations and there is opportunities for us within the Navy as you've seen from our public disclosures and announcements and other customers similar to that.

And obviously internationally, it's another market in new programs, new capabilities is our other sources of growth for that as well. In addition to that, we have the strategic growth – three strategic growth initiatives that we believe represent significant long-term growth opportunities for us that we are focused on and there are different levels of investment that we manage on a regular basis on those markets, and our balance sheet and our cash position gives us the ability to sort of pursue those and make the right decisions judiciously as the opportunities progress.

Gives you a flavor of our products and service revenue mix for fiscal 2016, which we announced publicly and as part of our filings. And we do get about in the last year, for example, we received about 23% of our revenue as customer-funded R&D. And that, historically, we've always had a portion of our revenue that comes from customer funding of developing some of these capabilities and demonstrating these capabilities, and we like that model a lot better because it gives us the – a stronger assurance that the customer is serious about this solution and the capability to help them solve their problem.

The chart on our financials and our revenue performance, so we took a dip on the sequestration time 2013, 2014, as you could see their 2012 to 2013 fiscal year for us, and our EBITDA as you could see, historically we've had strong EBITDA and we intentionally decided to invest incrementally more on R&D last two years – previous years and we've since then have curtailed that slowly ramping it back down and we've mentioned in our call, last earnings release, that we've gone from 16% of revenue on R&D spend in fiscal 2016 and our expectation this year is to 12%. And we intend to get back to our historical levels eventually as the time goes by.

And here is a quick snapshot of our revenue and financials for the last fiscal year, and year-to-date means the cumulative of the four quarters combined which we released this – in June. And then, of course, the profits in our last, this is our balance sheet, about \$261 million in cash as well as zero debt, and so the board looks at this on a very regular basis with management and primarily this is to help us on our growth initiatives. Once adoption accelerates, we believe we need significant capital to capitalize on that in terms of building the factories, automating, tooling, fixtures and service capabilities, so that it also gives us a very strong base with our customers and our suppliers in terms of confidence of a small business that we have a sound, financial, historical performance as well as balance sheet.

Okay. So in summary, strong core business, strong positions with growth opportunities there, as well as additional strategic growth initiatives what offers additional potential growth that we were pursuing very judiciously in the market that we play in and we're pursuing.

With that, if you have any further questions, Steve Gitlin who is sitting here with me, who has been doing this for a long time is – will be glad to also, you can contact him in the future, and I guess we'll take some questions now.

## Q&A

**<Q - Howard Alan Rubel>**: Wahid, just join me for a couple of minutes we have left and then we'll start and we could talk for a lot more than a few minutes but let's talk two things. One is the FAA it's in the process of allowing for operations of UAVs and drones and it's a big market and we've seen some very sophisticated, large companies consider using UAVs in some fashion so that they're operating outside of line of sight. So could you explain your approach to the market and explain that this is not – this is a business to business opportunity and maybe define in some terms what you think the market size could be?

**<A - Wahid Nawabi>**: Sure. So FAA, we've been involved with FAA for a long time and we've been working with them actively for a very long time on many fronts. So the latest developments in rules that you've seen from FAA, obviously is encouraging. It's the steps in the right direction. However, they are predominantly focused on the consumer, what I call, space in applications of UAVs, which we don't play and we don't intend to play in.

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As I mentioned earlier, we're primarily focused on those four verticals on a B2B market applications, majority of the customer base there will be large enterprises that require that type of capability and sophisticated differentiations that we offer as a profile with our defense business, safety management systems, processes and all that. So that's where we're focused on. And what really matters in that space is, one – a few things but one of which is the ability for beyond visual line of sight operation of UAVs.

So you saw some examples that I showed on, for example, the railroad tracks or utility power lines. It would be very beneficial to our business and to the industry, to our customers primarily that FAA comes up with rules and regulations that allows to fly [indiscernible] (32:32) the assets that can fly those kinds of missions with all the necessary precautionary capabilities beyond visual line of sight. And that has not been announced, we're working with FAA, with many others, and we're very actively involved and that is still to come in the future. And once that happens, then this market really will open up in terms of its market size opportunities.

In terms of size, if you look at it historically, these markets are very large and very hard to predict in terms of size for us. And there is so many experts out there that do this for a living. And so, we refrain from making public predictions on that. We study those, we keep track of those and we have our own models, of course, as well to inform our decisions. All I could tell you and we've been telling you is that, they are very large. So for a business our size, it's a game changer.

**<Q - Howard Alan Rubel>**: That's what I see and that's why I brought it up and I recognize it is important of focus on, we'll call it sophisticated solutions as opposed to toys, because I think – and that's just a bedrock and what you're trying to do is change people's behavior in terms of enterprise, so that they use your solutions to either grow their business, reduce cost, or to be more, I guess, [ph] lot (34:00) quicker to the market would be the way to...

**<A - Wahid Nawabi>**: Yep.

**<Q - Howard Alan Rubel>**: Last thing, because we are out of time, which is [indiscernible] (34:07) is LMAMS or Switchblade and so I'm going through the reprogramming announcements by the Department of Defense and that's a bit more money and where are we in that process? I mean, they stepped it up, I think its \$30 million, it's pretty meaningful. I can't remember the exact number, maybe it's not \$30 million, but it was a meaningful step-up and where are we in it in and is this just the beginning of more to come?

**<A - Wahid Nawabi>**: Yes. So, I know, if you look at the historical track record of ours, Tactical Missile Systems and LMAMS. LMAMS is of course a expected program that the Army has publically announced and mentioned and we believe we're positioned well on for that, however the timing of that is not determined right now and so it could be – it's based on what the Army plans and we're engaged with them on that and feel confident about our position. And I won't speculate on that or comment on that specifically.

In terms of the budget that you mentioned, historically our Tactical Missile Systems business has been funded and we have generated revenue based on the same exact – or similar process, a similar model where there is no program of record. Therefore there's need in the active military engagements of U.S. Military, and therefore they need this capability. And so they run that up through their chain of command, and eventually get to the leaders within the different forces.

And they request funding for that through what's referred to as JUON, Joint Urgent Operational Need payments. And then the funding gets allocated and then we receive – then the proposals get submitted and we receive the award and we build the product and ship it. And so this is consistent with that and we've been saying that for the past many years and we've had that in the past as well. And that's how much I could comment on that specific – and we're – we feel pretty strong about our position and about the future of that capability.

## Howard Alan Rubel

Well, you've teased me enough but hopefully some of the rest few meetings, during the course of the day, well, and week, we'll give people some more opportunities to talk to you about some of the other details, but nice presentation

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and thank you very much.

## **Wahid Nawabi**

Thank you. Thank you very much.

## **Steven A. Gitlin**

Thank you all.

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