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EOS 2022 Full Year Unaudited Results

Canberra, 28 February 2023

SUMMARY

Electro Optic Systems Holdings Limited (EOS or Company) has filed its consolidated Preliminary Final Report on Appendix 4E for the full year ended 31 December 2022. These results are unaudited.

1. RESULTS FOR FULL YEAR ENDED 31 DECEMBER 2022

For the consolidated entity ("EOS") or ("Company"), Revenue from Continuing Operations activities was $137.9m, representing a $74.4m or 35% decrease on the prior comparative period (31 December 2021: $212.3m)

The Loss After Tax, from Continuing Operations, was $53.6m (including charges for impairment provisions), compared to a profit of $6.7m in the prior comparative period.

Underlying EBITDA from Continuing Operations (prior to charges for impairment provisions and foreign exchange gains) was a loss of $42.9m, compared to an Underlying EBITDA profit from Continuing Operations of $22.8m in the prior comparative period.

The activities of a subsidiary, SpaceLink Corporation ("SpaceLink"), were discontinued during the period and a Loss After Tax from Discontinued Operations of $62.0m was recorded. This included a loss for the period of $34.5m and impairment charges of $47.2m, as reported at 30 June 2022. This was partially offset by a gain of $19.7m on the effective disposal of SpaceLink.

Including the results of SpaceLink's Discontinued Operations, EOS reported an operating Loss After Tax of $115.6m for the year ended 31 December 2022 (31 December 2021: operating Loss After Tax of $13.8m.)

The consolidated entity reported Net Cash Used by Operations for the year totalling $51.6m (31 December 2021: $0.2m Net Cash Generated by Operations). This included $15.3m relating to Discontinued Operations in 2022. In addition, the consolidated entity reported $28.3m of Net Cash Outflows on Investing Activities (31 December 2021: $37.7m). This included $11.3m relating to Discontinued Operations in 2022.

At 31 December 2022, the consolidated entity held cash totalling $21.7m (31 December 2021: $59.3m).

Key elements of financial performance are summarised below.

Revenue from Continuing Operations

For the year ended 31 December 2022 the Consolidated Entity recorded Revenue from Continuing Operations of $137.9m (31 December 2021: $212.3m), representing a decrease of $74.4m or 35%.

The decrease in Revenue was driven by lower Defence Systems segment Revenue, down from $184.5m in 2021 to $105.9m in 2022, a decrease of $78.6m. More detailed information is provided in Section 5 below.

Revenue in the Space segment increased on prior year to $32.0m (2021: $27.8m). This included growth in the EM Solutions business. More detailed information is provided in Section 6 below.

At 31 December 2022, the Group had a backlog of contracted future work of over $300m. This represents work secured under customer contracts, mainly in Defence Systems and EM Solutions. This work is currently expected to be undertaken principally in 2023 and 2024.

Expenses from Continuing Operations

Expenses in Continuing Operations increased from $207.1m in the prior period to $215.3m in this period. This increase of $8.2m was driven by an increase in administration expenses of $7.5m (including advisory costs associated with addressing funding and related matters), increased finance costs of $7.7m, an impairment charge of $7.3m, and increases in other items totalling $15.4m, and a reduction in raw material costs by $29.7m.

During the third and fourth quarters of the year a Restructuring Program was commenced to reduce costs, improve efficiency and align resources more closely with activity levels at the end of the year. Total annual savings of $25.0m are expected to be achieved. As part of this, over 100 roles were made redundant during the year. Costs of $3.5m were incurred during the year in implementing this Restructuring Program.

Underlying EBITDA from Continuing Operations

Underlying EBITDA from Continuing Operations (prior to charges for impairment provisions and foreign exchange gains) was a loss of $42.9m, compared to an EBITDA profit from Continuing Operations of $22.8m in the prior comparative period.

Impairments

The Group recognised an impairment charge of $54.5m during the period. This included a charge of $7.3m relating to Continuing Operations and a charge of $47.2m relating to Discontinued Operations (recognised in the half year report to 30 June 2022).

Foreign Exchange

The results included a foreign exchange gain in the year of $12.7m (2021: gain of $9.8m), which predominantly arose on the translation of US$ assets in into Australian Dollars.

Discontinued Operations

During the year, the Company sought strategic funding partners to support continued investment in SpaceLink. The Company did not succeed in securing investment, and as a result the Company ceased investment in SpaceLink during the year. Accordingly, on 16 November 2022, EOS announced that SpaceLink had ceased normal operations and that an orderly wind-up process had been initiated in the United States, by way of an Assignment for the Benefit of Creditors ("ABC").

Under the ABC process, at 31 December 2022, SpaceLink was controlled by an Assignee, and the Assignee acts in the interests of creditors. As a result of the decision to cease investment, and the ABC process, EOS expects that future EOS cash outflows related to SpaceLink will be approximately nil.

SpaceLink has been treated as a Discontinued Operation. The results of Discontinued Operations include:

- Operating expenses of $34.5m arising during the year
- An impairment provision of $47.2m
- A gain arising on the Assignment and effective disposal of SpaceLink, of $19.7m, which arose when SpaceLink, with net liabilities, was put into the ABC process noted above.

Cashflow Used in Operating Activities

During the year, the Group had cash used in operating activities of $51.6m. Of this, $15.3m was represented by cash used by the Discontinued Operations of SpaceLink.

Net cash used in operating activities was impacted by a reduction in Receipts from Customers from $233.9m in the prior year to $145.9m this year. The reduction was caused by projects ending and lower than expected receipts on continuing projects. In particular, due to delays in achieving contract milestones, receipts from a significant overseas customer in the Middle East were lower than expected. Payments to Suppliers and Employees of $188.6m were down from $225.2m in the prior year.

Contract Asset

The Group recognises a Contract Asset, being revenue recognised on projects that has not yet been invoiced to customers. Revenue is recognised under Australian Accounting Standards. Amounts are invoiced to customers in accordance with legal arrangements specified in customer contracts.

At 31 December 2022, the Group had a Contract Asset totalling $164.4m, being revenue earned but not invoiced, mainly on a project with a significant overseas customer in the Middle East. The Contract Asset increased by $36.1m during the year, due to the fact more revenue was recognised during the year than was invoiced to the customer. This was because of delays in achieving contract milestones, mainly because of the impact of COVID-19 and supply chain challenges on the customer.

The Group expects to realise cash from the Contract Asset following the invoicing and collection of these amounts in future periods, in accordance with the legal arrangements specified in customer contracts.

The realisation of this asset is one of the most critical tasks for the Group. Work on this includes seeking contract amendments and other changes with customers to bring forward Cash Receipts where possible and optimising the achievement of relevant milestones.

During February 2023, a contract amendment was agreed with a significant overseas customer in the Middle East, and this is expected to help improve cash realisations in 2023 and 2024.

Contract Liabilities – Amounts Received in Advance

The Group recognises Contract Liabilities for amounts that have been received from customers as advance payments on projects. During the year, the amount of Contract Liabilities increased from $7.7m at 31 December 2021 to $22.2m at 31 December 2022.

Cashflow Used in Investing Activities

The Group used $28.3m of net cash in investing activities during the year, including $11.4m net cash used in the Discontinued Operations of SpaceLink. In Continuing Operations, the main investing cash payments were the $11.2m paid as Security Deposits for bonds, mainly required under contracts with overseas customers, and capital expenditure of $7.9m. This was partially offset by $2.6m received on the repayment of a loan from an associate entity.

Funding and Cash Balances

As a result of the funds used in Operating and Investing Cashflows, the Group was required to seek additional funding during the year.

The Group raised $14.6m in cash proceeds from the issuance of new equity share capital during the year.

The Group repaid $35.8m of Group borrowings during the year and raised $75.7m in proceeds from new borrowings. During the year, the Group established the following borrowing facilities:

- Working Capital Facility, with $20.0m principal drawn, maturing on 6 September 2023
- Working Capital Facility, with $15.0m principal drawn, maturing on 11 April 2024
- Term Loan Facility, with $35.0m principal drawn, maturing on 11 October 2025.

The total borrowings under these facilities, including capitalised initial fees and interest were $83.6m at 31 December 2022. At 31 December 2022, these facilities were fully drawn.

The facilities are secured on certain Group assets, and terms of these facilities include financial covenants and minimum earn amounts. These are disclosed in the Notes to the Financial Statements.

The cash balance fell from $59.3m at the start of the year to $21.7m at the end of the year.

The Group continues to closely monitor the Cashflow of the Group and the outlook for the business to ensure that adequate funding is in place.

The Group will continue to regularly review and, if necessary, seek to amend the EOS capital structure to allow operations to continue.

2. CHANGES IN DIRECTORS AND MANAGEMENT

During the year, Dr Ben Greene resigned as Chief Executive Officer of the Company, and on 1 August 2022, Dr Andreas Schwer was appointed as Chief Executive Officer of the Company.

On 24 November 2022, Mr Peter Leahy AC stepped down as an Independent Non-Executive Director and Chair of the Board of Directors of the Company, and Mr Garry Hounsell was appointed to both roles. Mr Robert Kaye SC was appointed as an Independent Non-Executive Director of the Company on 13 September 2022. On 31 January 2023, after the end of the year, Ms Deena Shiff stepped down from her role as an Independent Non-Executive Director of the Company. Ms Leanne Ralph was appointed Company Secretary on 25 August 2022.

In the management team, during the year, Mr Clive Cuthell was appointed as Chief Financial Officer, Mr Matt Jones was appointed Acting Executive Vice President of Defence Systems, Dr James Bennett was appointed Acting Executive Vice President of Space Systems, and Dr Ben Greene became Head of Innovation. As part of the work to reduce the size of the Executive Management Team and reduce costs, the roles of Deputy Chief Executive Officer, Chief Operating Officer and Chief Technology Officer ended during the year.

3. STRATEGIC REVIEW AND IMPLEMENTATION

During the third and fourth quarters of the year the Company commenced a Strategic Review under the leadership of new Chief Executive Officer, Dr Andreas Schwer. As part of this:

- A restructuring program was implemented, aimed at achieving annual cost savings of $25m. As part of this focus on cost reduction and improving profitability, over 100 roles were made redundant during the year.
- The Group ceased investment in SpaceLink and established an ABC process. As a result, EOS expects that future cash outflows related to SpaceLink will be approximately nil.

Further work is continuing in a number of areas, aimed at improving cashflow, profitability, funding, and returns, including:

- Strengthened focus on realising cash from the Group's Contract Asset. This includes seeking contract amendments with customers where possible, and optimising the achievement of relevant milestones
- Careful management of costs, in line with the revenue and activity levels of the business
- Initiatives to secure new customer contracts, including improving sales and marketing effectiveness
- Rationing and prioritising capital expenditure, including R&D spending, towards core defence and space businesses, using commercial investment criteria.

4. STRATEGIC GROWTH PARTNERSHIPS AND/OR CAPITAL TRANSACTIONS

EOS has received approaches from several parties in relation to potential strategic growth partnerships and/or capital transactions.

During the second half of 2022, a confidential process was commenced to develop and assess potential strategic partners, having particular regard to their ability to support diversification into new geographic markets and/or to complement our existing products in existing markets. This is expected to continue during the first half of 2023. There is no certainty that any particular outcome or transaction will result from the process.

5. DETAILED BUSINESSS UNIT UPDATE - EOS DEFENCE SYSTEMS

Defence Systems had a challenging year in 2022, with Revenue falling from $184.5m in 2021 to $105.9m in 2022, a decrease of $78.6m. The decrease was caused by the impact of supply chain constraints on continuing projects, where constraints impacted customers, third party suppliers to customers, and the Defence Systems business. In addition, new projects were secured and initiated, but the impact of these was less than the impact of projects that were completed.

The main activity during the year was the manufacture and delivery of Remote Weapon Systems ("RWS") for a large customer in the Middle East. The gross margin ratio in 2022 was lower than 2021 due to changes in project mix and other items, but consistent with levels achieved in 2020.

Market Overview and Sales Activity – Defence Systems

During 2021 and 2022, some contract awards were delayed as governments deferred program awards and announcements. This was due to a range of political, economic and global geopolitical factors, including the impact of Ukraine and ongoing global supply chain issues. This meant that some opportunities that were previously expected to be signed, and commence delivering revenue, in 2022 have been delayed by customers. These opportunities are now expected to deliver order intake and revenue in 2023 and beyond.

The global market outlook strengthened as the 2022 year progressed, as many nations announced planned increases in defence spending. This may lead to increased opportunities in future.

Work continued during the year on sales opportunities, including significant projects in Australia and overseas.

In Australia, the Commonwealth of Australia has not yet published the outcome of the Defence Strategic Review. This review is expected to clarify the Australian Defence Force's ("ADF") future plans on key projects, including some that may benefit EOS. The outcome of this review is currently expected to be published before 30 June 2023. As part of this review, the ADF's plans for some projects that may benefit EOS are now expected to be announced later than previously expected.

Regarding Ukraine, EOS continues to be in active discussions and contract negotiations on the potential provision of a significant number of RWS and related components and spares. This includes opportunities for direct supply to Ukraine, and to other countries providing support to Ukraine. These opportunities have the potential to materially improve future Revenue and Cashflow. There is no certainty that any particular outcome or transaction will result from these discussions and negotiations.

Product Development – Defence Systems

Defence Systems continued work during the year to widen its RWS product range from its longstanding successful R400 RWS product:

- Defence Systems worked to secure an initial order for the new lightweight R150 RWS product. This new product has been completed and is now entering the marketplace. An order of fourteen R150 gimbals was received in January 2023, as part of the L3Harris Vampire program, under which the US is providing support to Ukraine. The order is for less than $10m and is expected to be completed in 2023.
- Following supply in previous years, a follow-on order was secured during the fourth quarter for fourteen new heavyweight R600 RWS, plus spares, for a customer in Southeast Asia. The R600 RWS order is being manufactured in EOS US facilities in Huntsville, Alabama. The total order is for up to $15m and is expected to be completed in 2023.
- Defence Systems also supported the integration and subsequent deployment of four R400 RWS equipped uncrewed ground vehicles (UGV) for a NATO customer. This deployment in Lithuania represents the first NATO operational deployment for a UGV equipped with lethality systems.
- Defence Systems continued to develop the new R800 RWS product with evaluation by potential customers ongoing in North America.

Defence Systems worked closely with Space Systems to further develop and demonstrate Directed Energy products. This included the 'Titanis' Counter Drone Defence System, which includes both the established RWS product, as well as new Directed Energy components. The market for these products continues to develop positively. During the year, demonstrations were held with potential customers and further discussions continue. Similar to the commercialisation program for previous EOS products, it is expected to take some time for Directed Energy products to achieve significant commercial scale.

Further product development work is intended to continue on a range of opportunities. The business is focussed on obtaining third party funding for product development work.

Supply Chain, Operations and Facilities – Defence Systems

Delivery against existing contracts in 2022 continued to be impacted by supply chain constraints. The normalisation of global supply chains has taken longer to occur than previously expected and supply chain challenges continue in many markets, impacting the timing of EOS revenue recognition. Whilst in some areas supply chain challenges have started to show signs of easing, in other areas the impact of previous challenges continues to be felt, and new challenges have emerged.

In the US, the EOS facility in Huntsville, Alabama, secured a facility clearance from the US Defence Counterintelligence Security Agency. This allows the facility to compete for classified US contracts and to work with other cleared defence contractors on classified work for the US military.

Organisational Structure – Defence Systems

During the year, Mr Grant Sanderson stepped down as CEO Defence Systems, and Mr Matt Jones was appointed Acting Executive Vice President of Defence Systems.

6. DETAILED BUSINESSS UNIT UPDATE – EOS SPACE SYSTEMS

Revenue in the Space Systems segment increased on prior year (2022: $32.0m, 2021: $27.8.m). Space Systems comprises two business units, Space Technologies and EM Solutions.

Space Technologies

Space Technologies delivers space domain services (providing information on objects in space) and advanced manufacturing, (which includes the design, building and deployment of telescope and observatory equipment). Space Technologies also develops technologies that support Optical Communications (using lasers) and Space Control activities.

During 2022, Space Technologies continued to grow and commercialise its technology. This included:

- Delivering satellite laser ranging services to longstanding customers.
- The award of two contracts from the United States National Oceanic and Atmospheric Administration (NOAA) government agency's Office of Space Commerce. These new contract values are for less than $1m.
- The design and build of prototype Directed Energy gimbals for a large international customer.
- Developing technology demonstrations for space control systems under a research program funded by customers.
- Continuing to develop and demonstrate Directed Energy products and seek funding for further development activities.
- Completing the acquisition of the assets and business of KiwiStar Optics. This business produces precision optics for astronomy purposes. The total consideration for the acquisition was $318,000.

Space Technologies continues to develop sales opportunities on potentially significant future projects for Australian and overseas customers. Typically, it can take up to, and more than, twelve months for opportunities to be developed and converted to signed sales agreements.

EM Solutions

EM Solutions designs, builds, deploys and maintains on-the-move satellite communication equipment systems for defence forces. EM Solutions' main products include satellite communication terminals and antennae for naval vessels and other marine applications.

During 2022, EM Solutions continued to focus on delivering growth:

- EM Solutions continued to deliver satellite communication systems to naval customers in Australia and Europe, working closely with customers to deliver leading products and continue to deliver profitable growth.
- In addition to receiving a number of smaller orders, EM Solutions signed a $26m three-year sustainment contract with the Australian Commonwealth's Capability Acquisition and Sustainment Group (CASG) for the Royal Australian Navy's existing fleet of Cobra Maritime SATCOM terminals.

EM Solutions continues to work closely with the ADF to support the Royal Australian Navy. This includes developing proposals to support the forthcoming SEA1442 Phase 5 program, under which there is an opportunity for EM Solutions to assist in the modernisation of maritime communications for the Royal Australian Navy.

Organisational Structure – Space Systems

During the year, Mr Glen Tindall finished working with the Company and Dr James Bennett was appointed Acting Executive Vice President of Space Systems.

7. SUBSEQUENT EVENTS

There were no significant subsequent events arising after 31 December 2022 and up to the date of this report.

8. OUTLOOK

In order to improve the outlook, the Company made changes detailed above, including:

- Appointing a new CEO and management team.
- Implementing a restructuring program aimed at achieving annual cost savings of $25m.
- Ceasing investment in SpaceLink to reduce future cash outflows to approximately nil.

In addition, work is continuing on several initiatives (outlined in sections 3 to 6 above) to improve cashflow, profitability, funding, and returns.

Market and Customer Outlook

During 2022, the market outlook for EOS products continued to develop positively. This was partly due to the conflict in Ukraine and the impact on customer demand in NATO countries and other important markets.

Some contract awards that were expected in 2022 were delayed as governments deferred program awards and announcements. This was due to a range of political, economic and global geopolitical factors, including the impact of Ukraine and ongoing global supply chain issues.

EOS continues to work on potential sales opportunities, including those that were previously expected to come to fruition during 2022.

Typically, EOS operates in an industry where it can take an extended period of time (including up to, and beyond, twelve months) for opportunities to be converted into signed sales contracts.

Outlook for Revenue and Cash Receipts

The Group's activities include the sale of products under a small number of relatively large projects. Typically, both the recognition of Revenue and Cash Receipts from Customers are governed by the achievement of project milestones with legal arrangements specified in customer contracts.

Changes in project timing, and the timing of the Group's Revenue and Cash Receipts, can arise due to unplanned changes in circumstances. This can include delays at the customer, delays at the customer's other Suppliers, delays at the Group and delays at the Group's Suppliers.

As noted above, at 31 December 2022, the Group had a Contract Asset of $164.4m, representing work done but not yet invoiced to customers. Management remains focussed on the progressive realisation of this significant asset, in the form of future Cash Receipts from Customers. This is an important aspect of improving the Group's financial position.

The level of future Revenue and future Cash Receipts from Customers will depend on the achievement of product manufacturing and delivery milestones, compliance with detailed contractual requirements, ongoing customer relationships and the outcome of commercial discussions and negotiations. Historically, owing to a high level of customer concentration and specific contractual arrangements, both Revenue and Cash Receipts have been difficult to predict with certainty.

The Group intends to continue providing regular updates during the year in line with its continuous disclosure obligations.

This announcement has been authorised for release to ASX by the Board of Directors.

Dr Andreas Schwer

Group CEO
28 February 2023

Reconciliation of Loss for the year to Underlying EBITDA

Continuing Operations Year ended 31 December $m	2022	2021
Profit (Loss) for the period	**(53.6)**	**6.7**
Income tax expense (benefit)	(9.3)	9.2
Profit (Loss) before tax	**(62.9)**	**15.9**
Finance costs	14.3	6.6
Impairment of assets	7.3	-
Foreign exchange (gains)	(12.7)	(9.8)
Underlying EBIT (before impairment and foreign exchange gains)	**(54.0)**	**12.7**
Depreciation & Amortisation	11.1	10.1
Underlying EBITDA (before impairment and foreign exchange gains)	**(42.9)**	**22.8**

ABOUT ELECTRO OPTIC SYSTEMS (ASX: EOS)

EOS operates in two divisions: Defence Systems and Space Systems

- Defence Systems specialises in technology for weapon systems optimisation and integration, as well as ISR (Intelligence, Surveillance and Reconnaissance) and C4 systems for land warfare. Its key products are next-generation remote weapon systems, vehicle turrets, counter-UAS and C4 systems.

- Space Systems includes all EOS space and communications businesses, and operates as two entities – Space Technologies and EM Solutions. Space Technologies specialises in applying EOS-developed optical sensors to detect, track, classify and characterise objects in space and remains integral to research and development across the group. EM Solutions provides global satellite communications services and systems.

This announcement may contain certain "forward-looking statements" including statements regarding EOS' intent, belief or current expectations with respect to EOS' business and operations, market conditions, results of operations, financial condition, and risk management practices. The words "likely", "expect", "aim", "should", "could", "may", "anticipate", "predict", "believe", "plan" and other similar expressions are intended to identify forward-looking statements. Indications of, and guidance on, future earnings, financial position and performance, establishment costs and capital requirements are also forward-looking statements. Forward-looking statements including projections, guidance on future earnings and estimates are provided as a general guide only and should not be relied upon as an indication or guarantee of future performance. This announcement may contain such statements that are subject to risk factors associated with an investment in EOS. Forward-looking statements involve known and unknown risks, uncertainties and assumptions and other important factors that could cause the actual results, performances or achievements of EOS to be materially different from future results, performances or achievements expressed or implied by such statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this announcement.