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CORPORATE FINANCE

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Industrials

Sector update

Aerospace & Defence

Autumn 2017



“Global aerospace M&A activity is expected to recover as political uncertainty in the US dissipates. More importantly, we expect Aerospace & Defence companies to continue to rationalise their product portfolios to match changing customer requirements and to fulfil a record aircraft order backlog.”

Jeremy Harrison
Partner
Catalyst Corporate Finance

Increasing defence budgets and consolidation are supporting M&A

The Aerospace & Defence (A&D) industry is undergoing major structural change driven by consolidation and pricing pressure. Furthermore, heightened geopolitical uncertainty is poised to drive increased defence spending globally, as evidenced by the \$696bn US Department of Defense bill for managing the US military in 2018.

The number of A&D deals involving a UK company remains at record levels. Component manufacturing transactions continue to be driven by momentum in commercial aerospace, the internationalisation of supply chains and private equity (PE) investment. Given the strength of the industry's long-term outlook and favourable funding landscape, both strategic and financial buyers will remain active while high margin businesses will continue to attract premium valuations.

Post-Brexit, the relationship between the UK and other countries, especially the US, will be imperative. This, coupled with the renegotiation of trade agreements, may introduce potential challenges and opportunities for the UK's A&D industry.

Key observations

Underlying market strength challenging existing supply chains

The aerospace sector is enjoying its second golden era marked by burgeoning order backlogs. Around \$75bn of deals were secured on day three of the Dubai Airshow by the Boeing-Airbus duopoly. Increased order volumes and price pressures are beginning to deliver a modernisation of the supply chain, which is driving elevated M&A volumes as Tier 1 and other suppliers look to expand manufacturing capabilities.

Mid-market in demand from traditional buyers and new entrants

Acquirers are targeting companies demonstrating high levels of organic growth from new generation platforms and proprietary design capabilities and system integration. Many of these firms are in the mid-market space.

PE continues to enable consolidation

PE is attracted to the potential for ongoing consolidation with platform investments and bolt-ons its underlying focus. With a number of highly successful PE investments in the sector recently, appetite and interest will be sustained.

Printing your plane

Additive manufacturing (3D-Printing) is set to disrupt the industry. Both military and commercial airline manufacturers are considering the potential of printing spare parts in-theatre to reduce costs and increase availability, a development that will define the relationship between contractors and manufacturers.

Pressure to deliver backlog of aircraft is supporting strategic M&A



“It’s an exciting time for the UK Aerospace & Defence mid-market. Both financial investors and strategic acquirers are highly active and valuations are at record highs, as evidenced by United Technologies’ recent acquisition of Rockwell Collins. Capitalising on this by understanding buyers’ criteria and tailoring our engagement with them should generate premium value for vendors.”

Richard Benyahia
Catalyst Corporate Finance

Production backlogs and the rapidly changing way aircraft are manufactured (increasing use of electronic components) has changed the basis of competition between the OEMs. They are now competing to ramp up production to meet customer commitments. The need to increase production rates is challenging suppliers to expand their offering to make themselves more attractive and important to OEMs, as well as gain leverage over pricing. Many are pursuing acquisition strategies to achieve this position.

- United Technologies Corporation’s (UTC) proposed \$30bn acquisition of Rockwell Collins occurs amid a quickening pace of consolidation among the biggest aircraft suppliers. The proposed deal will help UTC to build out its commercial business while remaining a key player in the defence industry.
- Italian aerospace provider Advanced Logistics for Aerospace (ALA) has acquired UK-based STAG Group. ALA’s expansion in Europe and the US brings it into the top five aerospace distribution and solutions providers globally.
- TT Electronics’ £42m acquisition of Tier 2 electronic components specialist Aero Stanhew increases its A&D exposure. Aero Stanhew has a similar blue chip customer base including GE Aviation, UTC and Rolls-Royce, and

supports new platforms including the 777(X), A350, A380 and F-35, thereby offering cross-selling opportunities and potential synergies.

- Tier 1 manufacturer MB Aerospace, acquired by Blackstone Group in 2015, acquired turbine parts producer Centrax Turbine Components, illustrating buyer interest in acquiring niche engine component providers serving both commercial and military markets.

Support services in demand

Strategic acquirers are targeting the fragmented airport services market to take advantage of growing fleets, increasing air freight volumes, the rise of low cost carriers and airlines’ desire to work with fewer services providers.

Examples include Dubai-based dnata’s acquisition of Air Dispatch, the provider of centralised load control planning services that calculates the weight and balance conditions for aircraft, as dnata seeks to expand its offering beyond traditional airlines; France’s Groupe CRIT’s acquisition of Cobalt, the third largest handler at London Heathrow which gives it access to the UK; and Menzies Aviation’s £165m acquisition of Aircraft Service International Group (ASIG) which expands its service offering to include fueling services.

The rising challenge from the East

Boeing and Airbus are keeping a watchful eye on new entrants into the market and customer interest in alternative platforms. While the introduction of Asian platforms like MRJ, ARJ, Comac and CJ series of high bypass turbofans are relatively recent, sooner or later we may see China as a genuine contender to challenge OEMs and key Tier 1 engine suppliers.

Furthermore, recent M&A activity points to a trend of Chinese investment into the European supply chain in an effort to build expertise and capability. Examples include China Loncin Motor’s \$44m acquisition of Italy’s Costruzioni Motori Diesel to expand its aviation engine business, Aviation Industry Corporation of China’s acquisition of Thompson Aero Seating, Shaanxi Ligeance Mineral Resources’ £326m acquisition of Gardner Aerospace, and Zhejiang Tiacheng Controls’ £55m acquisition of aircraft seat manufacturer Acro Aircraft Seating.

Private equity continues to facilitate investment and consolidation

PE remains an important investor. While specialist investors like US-based Liberty Hall continue to develop a buy & build strategy, new entrants are attracted to forecasts of strong market growth, long-term contracts and consolidation opportunities.

- Platinum Equity's acquisition of global A&D supply chain provider Pattonair from Exponent Private Equity gives them exposure to the aftermarket with a range of blue-chip engine, airframe and MRO customers.
- Liberty Hall's acquisition of Dunlop Aircraft Tyres, its fourth UK investment, follows on from its acquisition of Bromford Industries, a supplier of complex, close tolerance engine components.
- Graphite Capital's 2015 investment in Aero Technics served as a foundation asset to build a civil aircraft maintenance business. Two acquisitions have been made since – Servcorp, a manufacturer of lightweight life vest pouches, and Airbase Interiors, specialists in the repair and dry cleaning of aircraft seats.
- Silverfleet Capital acquired aero engine pipes and tubing manufacturer Sigma Components, whose customers include Rolls-Royce, Safran, Airbus, Bombardier and BAE Systems.

- EQT's acquisition of CHEP Aerospace Solutions, the global leader in pooling, management, maintenance and repair of unit load devices from Brambles, will support its plan to increase its blue-chip customer base and expand into adjacent business areas.

PE is increasingly establishing a successful record exiting investments. Most exits have been to strategic acquirers which can use projected synergies, access to new markets and product expansion to support high valuations.

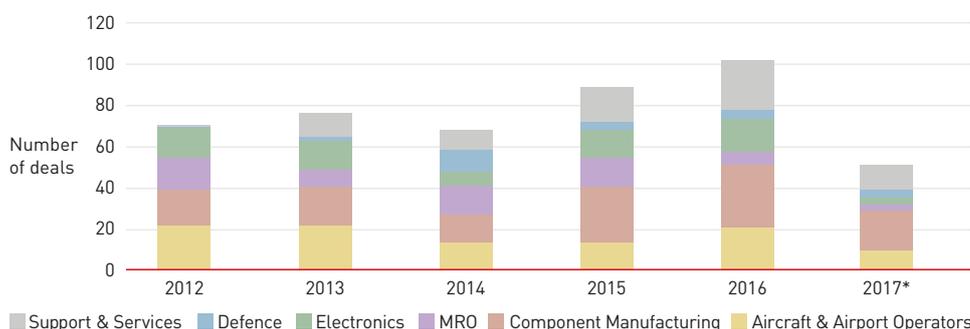
- Better Capital's highly successful investment in Gardner Aerospace generated 7x return following its sale to Shaanxi Ligeance Mineral Resources.
- Growth Capital Partners sold aviation records management software specialist FLYdocs to Lufthansa Technik, having held the asset for little more than a year.
- WestBridge Capital's sale of Aero Stanrew to TT Electronics achieved a return of 4.3x.
- Inflexion and Auctus Industries acquisition of Shimtech, the global market leader in specialist gap management components, delivered a successful return to Bridgepoint Development Capital.



"Favourable market dynamics including promises of higher defence spending, relatively low commodity prices and strong demand for passenger travel (especially in the Middle East and Asia) have all generated renewed enthusiasm from financial sponsors for technically differentiated, quality manufacturing businesses."

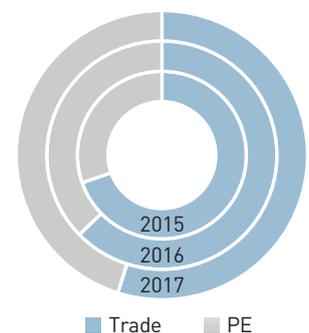
Wade Aust
Partner
Alantra US

Figure 1: M&A volume by sector



Source: S&P Capital IQ. *To end September 2017

Figure 2: M&A activity by buyer type



Selected transactions

Date	Company	Country	Target description	Acquirer	Country	Deal value (£m)
Sep-17	Acro Aircraft Seating	UK	Specialise in designing aircraft seating for various types of aircraft	Zhejiang Tiacheng Controls	China	55.0
Sep-17	Orbital ATK	US	Produces aerospace, defense, and aviation-related products - Flight Systems Group, Defense Systems Group, and Space Systems Group	Northrop Grumman Corporation	US	6,944.8
Sep-17	Doss Aviation	US	Provides flight training, aircraft maintenance, maintenance training, air traffic control and aviation logistics services	L3 Technologies	US	n/d
Sep-17	Rockwell Collins	US	Designs, produces and supports communications and aviation systems worldwide	United Technologies Corporation	US	23,874.9
Aug-17	Pattonair Ltd	UK	Provides supply chain solutions for aerospace and defense industries	Platinum Equity	US	n/d
Jun-17	Aero Components	US	Designs, manufactures, and supplies aircraft components and parts	P4G Capital Management	US	n/d
Jun-17	Halo Industries, Inc.	US	Engages in manufacturing of precision machined components for the aerospace industry	Elite Aerospace Group	US	n/d
Apr-17	Whitcraft LLC	US	Manufactures formed, machined, and fabricated sheet metal aerospace components and assemblies	Greenbriar Equity Group	US	n/d
Apr-17	Gardner Group Limited	UK	Manufactures and supplies metallic aerospace detailed parts	Chengdu Aerospace Superalloy Technology	China	326.0
Mar-17	Aerospace Holdings, Inc.	US	Engages in the design, engineering, fabrication, and machining of complex, high-precision, and close-tolerance parts, assemblies, and tooling	Harlow Aerostructures	US	12.8
Feb-17	OAG Aviation	UK	Provides real-time flight status and schedules data	Vitruvian Partners	UK	165.0
Dec-16	Air Dispatch International	UK	Aviation support services	dnata	UAE	n/d
Nov-16	Cobalt Ground Solutions	UK	Ground handling solutions	Group CIRT	France	n/d
Nov-16	Industria de Turbo Propulsores	Spain	Manufacture and testing of aeronautical engines and gas turbines	Rolls Royce	UK	612.3
Oct-16	B/E Aerospace	UK	Manufacturers and services cabin interior products	Rockwell Collins	US	6,847.0
Apr-16	Centrax Turbine	UK	Manufacturer of compressor and turbine aerofoil discs, shafts and casings	MB Aerospace	UK	n/d
Mar-16	Bromford Industries	UK	Manufactures precision machining and specialist fabrications	Liberty Hall Capital Partners	US	n/d
Nov-15	Aero technics	UK	Civil aircraft maintenance, interiors and kitting services	Graphite Capital	UK	n/d
Oct-15	MB Aerospace Holdings	UK	Engineering solutions to aerospace and defense market	The Blackstone Group	US	n/d
May-15	Shimtech Industries	UK	Manufactures composite structures, assemblies and shim solutions	Inflexion Private Equity, Auctus Industries	UK	141.0

Source: S&P Capital IQ

Selected Catalyst Aerospace sector deals

 Centralised Load Control Sale to 	 Development capital 	 Acquisition of 	 INDUSTRIES LIMITED Sale to  	 TURBINE COMPONENTS Sale to 
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Contact us

If you would like to discuss this report in more detail or the opportunities for your business, please email our Head of Industrials Jeremy Harrison at jeremyharrison@catalystcf.co.uk or call +44 (0) 121 654 5000.

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