

# Grant Thornton Corporate Finance

## mergers & acquisitions

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### Grant Thornton Corporate Finance Mergers & Acquisitions Industrials Group

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## Aerospace Components:

Structural factors, strong demand and private equity investments drive mergers and acquisitions

The Aerospace Component sector is seeing a significant increase in merger and acquisition activity fueled by:

- private equity interest in the sector;
- benefits of consolidation in a fragmented industry;
- suppliers facing increasingly demanding customers;
- private business owners approaching retirement age; and
- buoyant orders for aircraft and parts.

### Industry drivers

Strong demand is being seen in the U.S. Aerospace Components sector:

- Net new orders are expected to show a 20% increase for 2005. AIA reports that the sector is on pace for almost \$200 billion in net new orders for the year, compared with \$165 billion in 2004.<sup>1</sup>
- The backlog of unfilled orders supports continued strong demand into 2006, with almost \$230 billion in unfilled aerospace orders at the end of the first half of 2005.<sup>2</sup>
- Higher fuel costs are driving demand for more efficient, newer commercial aircraft models.
- Military spending has expanded, accounting for over 60% of aircraft spending in 2004 compared with less than 50% in 2000.<sup>3</sup>

To simplify their supply base and control costs, OEMs and their tier one suppliers are shifting preferences towards manufacturers delivering entire systems and sub-assemblies as opposed to individual components. This is encouraging suppliers to respond through consolidation and providing additional value-added outsourcing.

Many owners of component manufacturers are reaching retirement age and are looking to monetize ownership:

- private equity has proven an active buyer in the industry; and
- transitioning ownership through the use of external capital is more likely to increase value for departing shareholders.

## M&A activity

M&A activity within the Aerospace Components sub-sector has picked up considerably. (Table One illustrates 15 representative aerospace component transactions that have occurred since Q1 2004):

- Private equity players have become major participants in the sector and account for roughly half of the transactions taking place. Over the past eighteen months, they have completed numerous stand-alone acquisitions of components manufacturers.

- Strategic buyers continue to seek acquisitions that bring: proprietary technologies; achieve scale; and enhance component offerings.

Sector consolidation through M&A activity can provide tangible benefits for components suppliers through:

- driving improvements in design and manufacturing processes to enhance innovation and create production efficiencies;
- reducing customer concentration;

- creating more substantial businesses better able to support capital expenditure needs; and
- providing valuation multiple expansion through increased scale.

The components sector is highly fragmented – around 1,500 companies with combined annual revenue of \$45 billion support major OEMs.<sup>2</sup> The typical aircraft parts company has revenue of \$25 million and 150 employees.

**Table One: Recent Aerospace Components Transactions**

Ann. Date	Target	Description	Acquiror	Transaction value (\$mm)	TV / LTM Sales
<b>Private Equity</b>					
09/07/05	Precision Parts International Inc.	Manufacturer of metal components and subassemblies	First Atlantic Capital	NA	NA
08/03/05	BAE Systems Precision Aerostructures	Aerospace component machining and sheet metal manufacturing	TECT Corp.	NA	NA
12/13/04	Neuvant ASD	Supplier of structural parts and assemblies to aerospace industry	TECT Corp.	NA	NA
10/15/04	Stelllex Aerostructures, Inc.	Provider of engineered subsystems and components	Carlyle Group	NA	NA
10/15/04	K&F Industries Holdings	Aircraft wheels, brakes, brake control systems, bladder fuel tanks	Aurora Capital Group	\$1,006	2.9x
10/06/04	Tru-Circle Aerospace	Machined and sheet metal parts and assemblies manufacturer	TECT Corp.	NA	NA
04/01/04	TurboCombustor Technology, Inc.	Complex sheet metal fabrications for gas turbine engines	CAI Partners/AeroEquity	\$40	1.0x
<b>Strategic Buyers</b>					
07/06/05	FCS Control Systems	Manufacturer of high-fidelity simulation equipment	Moog Inc.	\$44	1.8x
03/01/05	Indal Technologies, Inc.	Shipboard helicopter handling systems for naval applications	Curtiss-Wright Corp.	\$63	1.6x
02/22/05	Boeing Commercial Airplanes - Wichita	Commercial airplane facilities in Kansas and Oklahoma	Onex Corporation	\$1,200	NA
01/17/05	Loud Engineering & Manufacturing Inc.	Manufacturer of landing gear systems and related components	CIRCOR International	\$36	2.1x
12/31/04	TriWestern Metals Co.	Producer of electro-galvanized and flat rolled products	Esmark, Inc.	\$15	NA
10/19/04	Integrated Aerospace Inc.	Supplier of specialist landing gear systems	Smiths Group	\$110	2.2x
11/10/04	Flowserve - Govt. Marine Bus.	Manufacturer of pumps for U.S. Navy nuclear subs and aircrafts	Curtiss-Wright Corp.	\$28	1.1x
09/02/04	Aero-Craft Co.	Manufacturer of components for gas turbines and aircraft engines	Volvo Aero	NA	NA
<b>Mean</b>					<b>1.8x</b>
<b>Median</b>					<b>1.8x</b>

Source: Company filings, press releases

### Valuation benchmarks

In 2005, acquisitions less than \$25 million in size took place at an average multiple of 5.8x EBITDA (across all sectors). This compares with a higher multiple of 8.5x EBITDA for larger transactions (between \$25 million and \$250 million).<sup>4</sup> Although terms of smaller private aerospace component company transactions tend not to be disclosed, higher multiples are paid for businesses with:

- proprietary technology & design;
- rapidly growing aftermarket business;

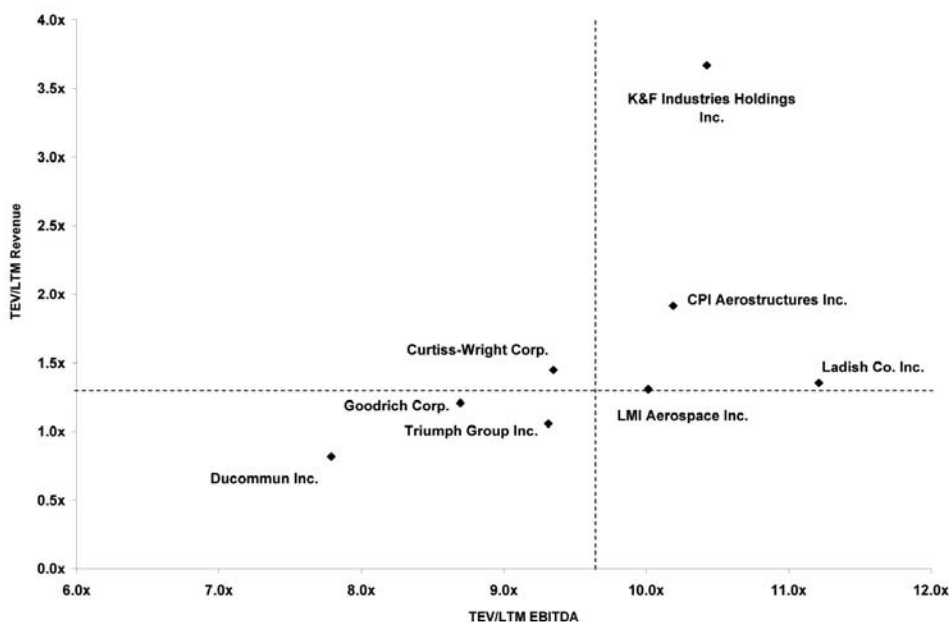
- exceptional customer position; and
- significant size.

### Public Company Trading Comparables

As with private company transactions, public market aerospace component supplier valuations tend to increase in line with the sophistication of a company's offerings. Generally, the more precision and advanced technology required for a particular component, the greater the trading valuation:

- More specialized technology and systems providers support higher market valuations between 9.0x - 11.0x EBITDA.
- Company size is an additional factor contributing to a difference in trading valuations.
- With improved earnings, not only have absolute valuations increased, but trading multiples have risen as well. Public company enterprise value market multiples for the sector have risen since 2001 from around 5.6x EBITDA to over 9.0x EBITDA.

Table Two - Aerospace Component Public Trading Multiples



Source: Capital IQ as of December 2005

### Private equity

Private equity players are being attracted to the sector by the prospect of pursuing a buy and build strategy, thereby:

- capturing the benefits of consolidation; and
- gaining price multiple expansion from subsequent demand among strategic buyers for businesses of significant size. >



Consequently, private equity is proving an attractive alternative source of additional buyers, providing sellers a greater opportunity to maximize value – particularly for those businesses which may not be critical acquisitions for strategic buyers.

- The private equity community has substantial capital seeking investment (around \$100 billion) and debt availability is high.
- The private equity market is itself highly fragmented – providing business owners a significant challenge to identify the right partner.
- Private equity transactions can prove highly favorable for ongoing management, providing management teams with the opportunity for significant ownership and independence going forward.

## Conclusion

The combination of: lengthening backlogs; strong availability of capital; an aging shareholder base; and increasing demands by OEMs should ensure continued M&A activity among aerospace component manufacturers. Private equity has become a useful source of capital for owners seeking to maximize value or to embark on acquisition strategies.

## Footnotes

- 1: AIA Update October 2005
- 2: First Research Aircraft Parts Manufacture Industry Profile
- 3: U.S. Dept. of Commerce; Department of Defense; General Aviation Manufacturers Association; AIA
- 4: Thomson Financial U.S. M&A Transactions

## About Grant Thornton Corporate Finance LLC

Grant Thornton Corporate Finance LLC provides investment banking and ownership consulting services to middle-market companies in the United States and around the world. For additional information or to discuss: ownership transition issues; acquisitions, divestitures and capital raising strategies; or how transaction planning can help to increase business value, please feel free to contact Ian Cookson on 617.848.4982 or by email at [ian.cookson@gt.com](mailto:ian.cookson@gt.com).

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