

Aerospace & Defense



M&A Review and Outlook

Mergers and Acquisitions (M&A) activity in the Aerospace and Defense (A&D) industry significantly increased in 2010 from more subdued levels of the previous two years. Globally, 212 deals with an average transaction size of US\$194 million were closed in 2010 versus 153 deals with an average transaction value of US\$272 million in 2009. Of the deals completed in 2010, 26 were greater than US\$100 million (deals with disclosed financial terms), up from 23 in 2009. Of the 26 deals in the US\$100 million-plus category, the average transaction value of US\$528 million increased 9 percent from the prior year's average transaction value of US\$483 million.¹

Average EBITDA acquisition multiples increased to 9.6x in 2010 from 8.4x in 2009 (deals with disclosed financial terms only). Although EBITDA acquisition multiples have risen as the economy continues to recover, they remain considerably off the high of 13.2x achieved in 2007. Transaction valuations for large-sized companies with established technologies and compelling

growth opportunities remain robust—many at double digit EBITDA multiples. For deals over US\$500 million in 2010, acquisition multiples averaged 1.7x revenue and 12.8x EBITDA.¹

Some of the sub-sectors within A&D of strong M&A interest continued to be unmanned aerial vehicles (UAVs); command, control, communications, computers, intelligence, surveillance and reconnaissance (C4ISR); cyber security; rotorcraft; and simulation & training.

Large-cap A&D companies continued to participate in sizable M&A deals in 2010. Boeing, L3 Communications, TransDigm and Triumph Group all completed acquisitions which ranked within the top 10 largest A&D deals by transaction value in 2010. Triumph Group acquired Vought Aircraft Holdings, Inc., a manufacturer of aero structures for commercial, military, and business jet aircraft manufacturers, for US\$1.6 billion in March.² Boeing acquired Argon ST, a provider of systems engineering, development, and C4ISR, for US\$799 million in June,³ and TransDigm acquired McKechnie Aerospace, which engages

in the design, manufacture, and logistic support of structural components, systems, and assemblies for the commercial, regional, business, and military aerospace industries, for US\$1.4 billion in September.⁴

A further highlight in 2010 has been the continued emergence of high-tech defense technology deals. Landmark deals by CGI Federal and L-3 Communications highlight the broader trend from “big guns” to smaller high-tech procurements by the Department of Defense. CGI Federal acquired Stanley, Inc., a provider of information technology (IT) services and solutions to the United States defense, intelligence, and federal civilian government agencies, for US\$1.1 billion in May. The combination of CGI's U.S. federal business unit and Stanley brings additional resources and capabilities to the U.S. Government market and marks CGI Federal's expansion into the U.S. defense and intelligence markets. With this acquisition, CGI Federal joins a select list of Federal IT contractors with more than US\$1 billion in revenue⁵. L-3 Communications acquired Insight Technology, which develops and produces night vision and electro-optical systems, for US\$613 million in February. Insight expands and broadens L-3's warrior systems capabilities. Warrior systems include high-tech mission critical night vision and electro-optical equipment such as laser aiming and illumination devices, laser rangefinders, laser markers and designators, night vision goggles and monoculars, and thermal imaging systems.⁶

¹ Capital IQ and company filings, February 4, 2011.

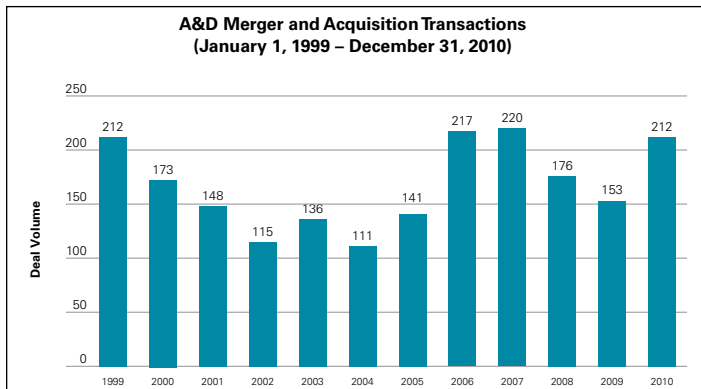
² Triumph Group, Inc., press release, March 23, 2010.

³ Boeing, Inc., press release, June 30, 2010.

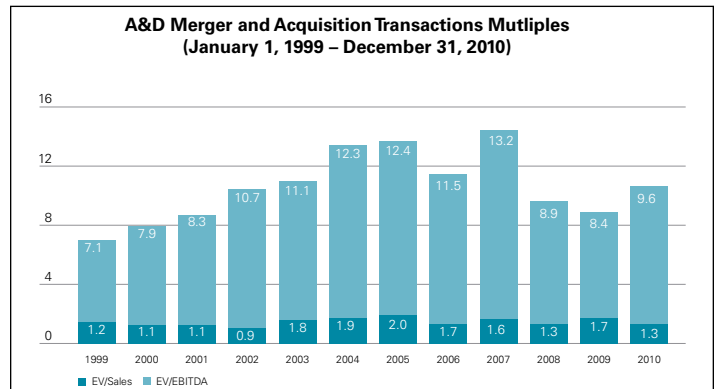
⁴ TransDigm Group Incorporated, press release, September 27, 2010.

⁵ CGI Group Inc., press release, May 7, 2010.

⁶ L-3 Communications, press release, February 19, 2010.



Source: Capital IQ and Company Filings, February 4, 2011.



Source: Capital IQ and Company Filings, February 4, 2011.

2011 Industry Outlook

According to Fitch, Inc., the global A&D industry in 2011 is expected to be stable, with projected growth in most end-markets.⁷ Fitch projects large commercial aircraft deliveries from the major manufacturers to grow as Airbus and Boeing are projected to increase deliveries by approximately 6.5 percent in 2011 and a further increase 13 to 14 percent in 2012. The commercial aftermarket is expected to grow in the mid-to-high single digits as analysts believe jet revenues and profits could begin to rise in 2011. However, regional aircraft deliveries are expected to decline 5 percent in 2011. Conversely, suppliers are expected to see the highest revenue increases in the sector as they benefit from the robust aftermarket demand and the buildup to higher production rates in 2012.⁷ In terms of commercial aviation traffic, developing markets such as China, India, and the Middle East are projected to continue exhibiting much higher growth than those of the developed markets such as the United States and Europe.

On the defense side, while the current impasse over the fiscal 2011 defense budget is expected to be resolved in the coming months, overall U.S. defense spending is expected to decrease in fiscal 2012 due to current political pressures to reduce government spending, including elimination or reduction of a number of military programs. Supplemental funds for operations in Iraq and Afghanistan are also expected to continue trending down in the next few years due to gradual withdrawal of U.S. troops in the Middle East. Risks to the U.S. defense outlook include margin pressures from tougher contract terms and pressure on spending after fiscal 2012 due to fiscal challenges and growing support in Congress for reduced defense spending.⁷

Foreign military sales are expected to play a larger role in the defense industry and will potentially act as an offsetting factor against defense spending reductions in the United States. Despite declines in the overall worldwide defense markets, defense budgets for a number of foreign markets in the short – medium term are not expected to fall at the same rate as overall defense spending, thus mitigating the revenue downside risk for those defense companies, both European and U.S. based, supplying to the international markets.⁸

Overall, industry analysts collectively have a positive outlook on the A&D sector with expectations for substantial cash deployment, and increased M&A activity. The A&D industry will continue to adjust to the recovering economic environment and the shift in priorities by using M&A as a way to expand or maintain market share and broaden capabilities.

The wave of consolidation over the last two decades has ceased with M&A now trending towards an increasingly strategic nature. Companies are seeking to reposition their businesses, selling off units that pose potential conflicts of interest or are not core to a company's operations, and seeking businesses in growth sectors such as cyber-security and other defense-related information technology areas. A recent example is Lockheed Martin's decision to divest its Enterprise Integration Group, which provided systems engineering and integration services, in order to avoid conflict of interest. Another recent example is AAI Corporation, whose corporate parent Textron Inc. has opted to split the company into three businesses: an unmanned aircraft unit; a testing, training and simulation business;

and a technical services group in order to add efficiency to its decision-making process for each unit.⁹

Furthermore, foreign A&D contractors, especially those from Europe, are expected to continue to have acquisition interest in the United States due to their desire to enter or deepen their presence in the large U.S. defense market. Finally, U.S. private equity firms are expected to continue pursuing acquisitions of all sizes in the A&D and government services markets.⁹

Conclusion

The A&D industry is showing signs of improvement as the global economy continues its recovery. With 2010 M&A volumes approaching the 2007 highs, all indications are that the A&D industry is poised to continue its growth, both in revenue and M&A volume, into 2011 and beyond. With these positive indicators also come uncertainties. Despite the A&D market's projected CAGR of over 5 percent through 2014, the projected decrease of U.S. defense budget and globalization of commercial aerospace are presenting opportunities and challenges to participants across the global supply chain.¹⁰

⁷ Fitch, Inc. "Aerospace & Defense 2011 Outlook – Growth Offsets Risks from Cash Deployment and Program Execution," press release, January, 24, 2011.

⁸ Hodge, Nathan. "International Call to (Buy) Arms," *The Wall Street Journal*, July 20, 2010.

⁹ Censor, Marjorie. "Mergers and spinoffs shake up the defense industry," *The Washington Post*, February 7, 2011.

¹⁰ Datamonitor Global Aerospace and Defense Report, October 2010.

Top Ten Global Deals by Transaction Value in 2010 (\$USD millions)¹

Date	Target	Buyer	Transaction Value	Enterprise Value ²	EV ² /Sales	EV ² /EBITDA ³
Mar-10	Vought Aircraft Holdings, Inc.	Triumph Group, Inc. (NYSE:TGI)	1,587.0	1,587.0	0.8x	–
Apr-10	DynCorp International Inc.	Cerberus Capital Management, L.P.	1,561.6	1,439.2	0.4x	5.6x
Sep-10	McKechnie Aerospace DE, Inc.	TransDigm Inc.	1,411.4	1,345.0	4.2x	14.3x
Nov-10	Swissport International AG	PAI Partners	1,234.9	1,234.9	0.8x	10.9x
May-10	Stanley, Inc.	CGI Federal Inc.	1,063.8	1,059.9	1.2x	11.6x
Nov-10	Ladish Co. Inc. (NasdaqGS:LDSH)	Allegheny Technologies Inc. (NYSE:ATI)	833.2	806.5	2.1x	14.7x
Oct-10	Lockheed Martin EIG Unit	Veritas Capital	815.0	774.7	1.3x	–
Jun-10	Argon ST, Inc.	Boeing Co. (NYSE:BA)	799.2	774.7	2.3x	18.1x
Feb-10	Insight Technology Incorporated	L3 Communications Holdings Inc. (NYSE:LLL)	613.0	613.0	–	–
Oct-10	Seven Aviation Mechanical Businesses	Hubei Aviation (SZSE:002013)	609.0	609.0	–	–

Source: Capital IQ and company filings, February 4, 2011.

¹ Includes announced, closed, and effective transaction agreements, February 4, 2011.

² Enterprise Value (EV) equals Market Capitalization plus Debt, Preferred Equity, and Minority Interest, minus Cash and Cash Equivalents, February 4, 2011.

³ EBITDA equals Earnings before Interest, Taxes, Depreciation, and Amortization, February 4, 2011.

Market Snapshot											
Company	Market Cap ¹	Share Price ¹	52-Week Low	52-Week High	Price % Change 1 Mo	Price % Change 1 Yr	Debt to TC	Price to BV	EV(2)/ Sales	EV ² / EBITDA ³	
S&P 500											
Boeing Co.	50,878.1	69.1	59.5	76.0	-3.2%	-2.5%	81.3%	18.4	0.8	8.2	
General Dynamics Corp.	27,721.8	74.4	55.5	79.0	-4.2%	-1.1%	19.4%	2.1	0.9	6.3	
Goodrich Corp.	10,455.6	83.5	63.2	94.1	-8.6%	19.0%	41.0%	3.1	1.7	9.5	
Honeywell International Inc.	43,854.3	55.9	37.9	58.2	-2.6%	28.6%	38.1%	4.1	1.4	11.5	
Lockheed Martin Corporation	27,986.0	80.5	67.7	87.2	-1.2%	-6.3%	57.5%	7.5	0.7	5.9	
Northrop Grumman Corporation	19,503.4	67.0	53.5	72.5	-3.2%	2.9%	26.3%	1.4	0.6	5.4	
Raytheon Co.	17,887.6	49.7	42.7	60.1	-2.1%	-12.5%	26.7%	1.8	0.7	6.1	
Rockwell Collins Inc.	9,736.2	62.8	51.9	68.0	-5.0%	2.6%	26.2%	6.6	2.1	10.3	
United Technologies Corp.	73,842.9	80.2	62.9	85.5	-5.6%	10.6%	31.2%	3.5	1.5	9.0	
S&P 500 Mean					-4.0%	4.6%	39%	5.4	1.2	8.0	
S&P 500 Median					-3.2%	2.6%	31%	3.5	0.9	8.2	
Other Primes/Systems Suppliers											
BAE Systems plc	17,609.7	5.2	4.7	6.3	-8.8%	-10.1%	61.9%	2.0	0.5	4.3	
Bombardier, Inc.	11,225.2	6.5	4.3	6.9	4.9%	14.0%	53.9%	2.9	0.7	9.1	
European Aeronautic Defence and Space Company EADS N.V.	22,262.0	27.3	18.8	31.5	-7.6%	36.4%	32.4%	1.8	0.2	3.5	
EMBRAER - Empresa Brasileira de Aeronáutica S.A.	6,145.7	34.0	19.9	35.4	-1.3%	44.9%	38.6%	2.1	1.2	13.9	
Finmeccanica SpA	7,102.7	12.3	10.9	15.0	-5.6%	-38.2%	30.6%	0.7	0.5	3.9	
Thales	7,498.5	37.7	35.4	42.9	1.5%	-6.1%	32.2%	1.4	0.5	9.5	
Other Primes/Systems Suppliers Mean					-2.8%	6.8%	42%	1.8	0.6	7.4	
Other Primes/Systems Suppliers Median					-3.5%	3.9%	35%	1.9	0.5	6.7	
Avionics/Electronics											
Alliant Techsystems Inc.	2,318.4	69.4	60.1	84.0	-4.0%	-13.9%	59.5%	2.1	0.7	5.4	
DRS Data & Research Services plc	10.6	0.3	0.2	0.4	-4.3%	63.6%	32.0%	1.3	0.3	3.5	
Harris Corp.	5,951.5	46.5	40.2	54.5	-4.7%	-1.6%	44.4%	2.5	1.3	5.8	
Herley Industries Inc.	267.3	19.0	12.5	19.0	0.1%	36.7%	6.3%	1.6	1.3	7.6	
L3 Communications Holdings Inc.	8,489.4	78.5	66.1	97.8	-1.9%	-16.6%	37.7%	1.3	0.8	6.1	
CAE Inc.	3,287.6	12.8	9.1	13.6	-1.0%	38.0%	27.9%	2.6	2.3	10.2	
Ultra Electronics Holdings plc	1,850.4	26.8	24.0	30.9	-8.1%	16.5%	17.1%	4.7	1.6	9.5	
Avionics/Electronics Mean					-3.4%	17.5%	32%	2.3	1.2	6.9	
Avionics/Electronics Median					-4.0%	16.5%	32%	2.1	1.3	6.1	
Components (Large Cap)											
Cobham plc	4,155.7	3.6	3.1	4.5	1.0%	-6.8%	42.2%	2.4	1.5	7.8	
Curtiss-Wright Corp.	1,552.0	33.5	26.1	38.9	-8.1%	-5.3%	25.5%	1.3	1.0	7.1	
Esterline Technologies Corp.	2,121.4	69.6	43.6	73.5	-1.9%	43.5%	29.8%	1.5	1.5	8.5	
Meggitt plc	4,146.7	5.4	2.0	6.3	-6.7%	16.2%	35.0%	1.6	2.8	10.7	
Moog Inc.	1,955.3	43.1	30.0	46.3	-4.0%	136.8%	38.4%	1.7	1.2	8.5	
Precision Castparts Corp.	20,117.6	140.2	101.0	152.0	-7.2%	630.8%	3.4%	3.0	3.3	11.9	
Rolls Royce Group plc	17,553.3	9.4	8.6	10.9	-9.2%	-53.5%	31.8%	2.7	0.8	6.8	
Smiths Group plc	8,339.4	21.3	16.3	23.5	-5.7%	0.6%	47.9%	4.7	2.2	10.8	
Textron Inc.	7,042.1	25.5	15.9	28.9	-7.6%	14.9%	67.9%	2.4	1.2	13.2	
Zodiac Aerospace SA	3,664.4	69.1	50.3	81.0	-2.6%	40.9%	30.5%	1.7	1.4	10.5	
Components (Large Cap) Mean					-5.2%	81.8%	35%	2.3	1.7	9.6	
Components (Large Cap) Median					-6.2%	15.6%	33%	2.0	1.5	9.5	
Components (Mid Cap)											
Ducommun Inc.	234.6	22.3	16.0	24.3	1.5%	10.1%	1.3%	0.9	0.6	5.7	
Heroux-Devtek Inc.	244.7	8.1	5.0	8.6	2.6%	66.3%	31.4%	1.1	0.9	6.2	
Magellan Aerospace Corp.	75.0	4.1	1.8	5.0	-9.6%	120.6%	49.3%	0.3	0.4	4.4	
Triumph Group, Inc.	2,061.8	85.1	60.1	97.3	-4.7%	40.5%	47.5%	1.4	1.4	9.8	
Components (Mid Cap) Mean					-2.5%	59.4%	32%	0.9	0.8	6.5	
Components (Mid Cap) Median					-1.6%	53.4%	39%	1.0	0.7	6.0	
MRO/Aftermarket Services											
AAR Corp.	1,071.8	27.0	14.9	29.1	-5.5%	9.1%	35.7%	2.6	0.9	8.2	
HEICO Corp.	1,609.4	58.0	34.6	59.4	1.8%	47.9%	3.6%	7.9	2.7	13.0	
MRO/Aftermarket Services Mean					-1.8%	28.5%	20%	5.2	1.8	10.6	
MRO/Aftermarket Services Median					-1.8%	28.5%	20%	5.2	1.8	10.6	
Total Aerospace Industry Mean					-3.7%	34.7%	35%	3.0	1.2	8.1	
Total Aerospace Industry Median					-4.1%	12.3%	32%	2.1	1.1	8.2	

Source: Capital IQ and company filings, March 18, 2011

¹ Market Capitalization amounts are in millions, based on closing share prices as of March 18, 2011

² Enterprise Value (EV) equals Market Capitalization plus Debt, Preferred Equity, and Minority Interest, minus Cash and Cash Equivalents

³ EBITDA equals Earnings before Interest, Taxes, Depreciation, and Amortization

⁴ Market Capitalization and Share Prices are based on foreign exchange listed securities and converted to US\$

Select Aerospace & Defense M&A Transactions

- February 7, 2011 – **Kratos Defense & Security Solutions, Inc.** (NASDAQ: KTOS), a provider of engineering, information technology (IT) services, and warfighter solutions, acquired **Herley Industries Inc.** (NASDAQ: HRLY), a developer of microwave technology solutions for the defense, aerospace, and medical industries, for \$287 million. The transaction implies a valuation multiple of 1.4x revenue and 8.6x EBITDA based on LTM November 2010 results.
- January 16, 2011 – **Lockheed Martin Corporation** (NYSE: LMT), a developer of aerospace and defense technologies, acquired **Advanced Military Maintenance, Repair and Overhaul Center LLC**, a provider of military maintenance, repair and overhaul (MRO), for an undisclosed amount.
- January 7, 2011 – **Curtiss-Wright Corp.** (NYSE: CW), a provider of overhauling precision components and systems, acquired **Predator Systems, Inc.**, a provider of hydraulic fuses, hydraulic manifolds, flow meters, valves, dampers, and dashpots, as well as pumps, hydraulic motors, and intensifiers, for \$13 million. The transaction implies a valuation multiple of 1.7x revenue based on LTM September 2010 results.
- January 3, 2011 – **HEICO Corp.** (NYSE: HEI), a developer of aerospace, defense, and electronics related products, acquired **Blue Aerospace, LLC**, a distributor, repair manager, and parts provider for the military-related aerospace aftermarket, for an undisclosed amount.
- December 18, 2010 – **Raytheon Co.** (NYSE: RTN), a provider of electronics, mission systems integration, and mission support services, acquired **Applied Signal Technology, Inc.**, a provider of intelligence, surveillance, and reconnaissance solutions for defense, intelligence, and homeland security markets, for \$512 million. The transaction implies a valuation multiple of 1.8x revenue and 14.3x EBITDA based on LTM January 2011 results.
- November 29, 2010 – **BAE Systems plc** (LSE: BA.), a developer of defense and aerospace systems, acquired **stratsec.net Pty Ltd.**, a provider of information security consulting and testing firm, for \$23 million.
- November 22, 2010 – **Boeing Co.** (NYSE: BA), a manufacturer of commercial jetliners, military aircraft, satellites, missile defense, human space flight, and launch systems and services worldwide, acquired **Summit Aeronautics Group, LLC**, a provider of aerospace products and services, for an undisclosed amount.
- November 22, 2010 – **ManTech International Corporation** (NASDAQ: MANT), a provider of technologies and solutions for mission-critical national security programs, acquired **MTCS, Inc.**, a provider of Command, Control, Communications, Computers, Intelligence, Surveillance and Reconnaissance (C4ISR) systems integration, cyber security and network engineering solutions to U.S. government customers, for \$75 million.
- November 24, 2010 – **Veritas Capital**, a private equity firm, acquired **CPIT International, Inc.** (NASDAQ: CPII), a provider of microwave, radio frequency, power, and control products, for \$360 million. The transaction implies a valuation multiple of 1.5x revenue and 9.0x EBITDA based on LTM October 2010 results.

KPMG Corporate Finance LLC We Can Do a Great Deal Together.

KPMG Corporate Finance LLC provides a broad range of investment banking and advisory services to its domestic and international clients. Our professionals have the experience and depth of knowledge in global M&A and project finance to advise clients on mergers and acquisitions, sales and divestitures, buyouts, financings, debt restructurings, equity recapitalizations, infrastructure project finance, and other advisory initiatives. In addition, we remain independent of financing sources, helping to ensure that our efforts are objective and aligned with the goals of clients.

Operating in 82 countries, KPMG International's member firms' corporate finance practices (KPMG) comprise more than 2,100 professionals who are able to meet the needs of clients across the globe. In 2010, as a leading financial adviser, KPMG completed 269 deals totaling US\$16.5 billion, according to Thomson Reuters SDC's global M&A middle market league tables.

www.kpmgcorporatefinance.com

Contact Us

We welcome the opportunity to meet with you, learn more about your company's objectives, and discuss our people and capabilities.

Terence Yeh
Managing Director
Los Angeles
213-817-3128
tyeh@kpmg.com

Thomas R. Groh
Vice President
Chicago
312-665-2186
tgroh@kpmg.com

Corporate finance services, including Financing, Debt Advisory, and Valuation Services, are not performed by all KPMG member firms and are not offered by member firms in certain jurisdictions due to legal or regulatory constraints. The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

© 2011 KPMG Corporate Finance LLC, a Delaware limited liability company, is a member of FINRA and SIPC and is registered as a broker dealer with the SEC. KPMG Corporate Finance LLC is a subsidiary of KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. Printed in the U.S.A. The KPMG name, logo and "cutting through complexity" are registered trademarks or trademarks of KPMG International. 23917NSS