

KAL Capital Markets Aerospace & Defense

Q2 2023



INTRODUCTION

Dear Friends,

Happy 4th of July!

We are encouraged by recent developments in both the A&D industry as well as the broader M&A market. For aerospace, we spent several days busily catching-up in-person with financial sponsors and industry participants at the Paris Air Show. The tone of those meetings was encouragingly positive as conviction around the recovery of OEM build-rates continues to grow. The consensus view is that aerospace is squarely in a strong up-cycle despite well-publicized challenges with supply-chain and availability of labor. This optimism underpins a strong M&A appetite to find opportunities to deploy capital within the supply-chain. Activity levels are picking up significantly and we expect the second half of this year to be quite busy.

For the M&A market generally, the recovery has been more mixed. Larger deals remain hampered by risk-adverse capital markets and a lending universe that is now dominated by private credit funds. The Wall Street Journal provided an accurate description of the current state of affairs when it discussed how “smaller” deals have taken over as the core of the M&A market. While total private equity deal value has declined ~50% YoY, the total number of deals is only down 4% illustrating a dramatic shift towards deals closer to \$100mm of value. The number of total deals completed year-to-date is the third highest in 30 years! We have witnessed this shift in every M&A process as buyer behavior remains strongly aggressive and larger equity groups have come down market to pursue transactions in the \$50 - \$200mm value range. This dynamic has forced multiples (at least in A&D) to remain at or above 2021 levels.

For the second quarter, we are pleased to announce two transactions. Both are described in greater detail in the subsequent pages, but they are illustrative of core sub-sectors that KAL has spent a great deal of time in. First, we represented International Water-Guard in their sale to Arcline Investment Management. IWG offers a suite of highly engineered, proprietary products to the business jet and commercial aerospace industry. Businesses that own their Intellectual Property and both the OEM and aftermarket revenue streams are commanding all-time high valuations. Secondly, we continue to grow our practice in the world of government contracting, particularly focused on those businesses sitting at the intersection of software and next-generation needs of the warfighter. We were pleased to advise Fregata Systems on their sale to Rotor Capital. Fregata offers a unique set of software-enabled services that fit into JADC-2 and its related initiatives.

Sincerely,

Trevor Bohn
Partner

Ryan Murphy
Partner

KAL
Capital



Q2 2023 TRANSACTION ANNOUNCEMENTS



Water-Guard

HAS BEEN ACQUIRED BY

ARCLINE
RISK MANAGEMENT

SALE OF COMPANY

JUNE 2023



FREGATA
SYSTEMS

HAS BEEN ACQUIRED BY

**ROTOR
CAPITAL**

SALE OF COMPANY

MAY 2023

**KAL
Capital**

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KAL CAPITAL OVERVIEW

KAL Capital is a boutique investment bank focused on providing advisory services to owners of businesses throughout the greater aerospace supply-chains.

Our services consist primarily of M&A advisory and liquidity event planning. Our clientele are generally family or partnerships that own successful, growing businesses within the aerospace/defense sector. Today's M&A environment offers business owners a wide-range of transaction alternatives, often at compelling valuations. Our role is to assist in the navigation of this process and to ensure that valuation is maximized.

SERVICES PROVIDED

- » **Sell-Side Advisory**
- » **Buy-Side Advisory**
- » **General Strategic Advisory**
- » **Debt Capital Raising**
- » **Equity Capital Raising**
- » **Merchant Banking**

Team



- » Founders have worked together for 10+ years with a combined 25+ years of A&D experience
- » Deep team of highly-seasoned support staff

A&D Sector Knowledge



- » Deep A&D sector knowledge vital to articulating unique major macro-drivers
- » KAL team understands that each business has a highly unique story and accumulation of history

Transactions



- » KAL has vast experience throughout the supply chain with a comprehensive understanding of each subsector's growth drivers and strategic buyers
- » Cross-border transaction experience

Relationships



- » KAL has long-term relationships with financial buyers as well as C-Suite executives at leading A&D public companies who prioritize KAL clients

Clients First



- » KAL is built on the belief that M&A processes should be built to maximize transaction outcomes for clients



KAL ADVISES INTERNATIONAL WATER-GUARD

INTERNATIONAL WATER-GUARD ACQUIRED BY ARCLINE



- » IWG is a leading provider and servicer of proprietary potable water systems and components for use in business and commercial jet applications, protecting both passengers and crew from the risk of waterborne illnesses
- » The Company's comprehensive product portfolio ranges from water treatment units to components and complete water systems, including control technology. IWG's products have been factory-installed or retrofitted on over 4,000 aircraft worldwide

PRODUCT PORTFOLIO

Water Treatment Units



UV-1/UV-3 UV-2 IWG-A6 NPS-A6

Water Modules



IWG-M1 IWG-M2 IWG-M3

Water Heaters



T-Series IWG-HE IWG-ES7

Water Distribution



Motorized Valve Water Transfer Pump Potable Water Pumps

KEY CAPABILITIES

Engineering & Development

- » *Full product development capability, including in-house mechanical, electrical, and software design*

Assembly

- » *In-house product assembly lines*

Testing Laboratory

- » *Full in-house testing laboratory with design verification*

Service & Repair

- » *Sole authorized maintenance & repair facility for all IWG products*

KAL ADVISES FREGATA SYSTEMS

FREGATA SYSTEMS ACQUIRED BY ROTOR CAPITAL

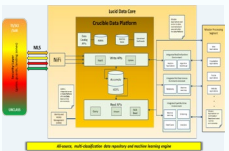


- » Fregata Systems is a Saint Louis-based provider of innovative C5ISR technologies solving vital needs of the defense and intelligence communities
- » Fregata's capabilities include multi-level secure cloud applications, communications & networking, and UAV related services which enable the warfighter to access advanced intelligence architectures

KEY CAPABILITIES

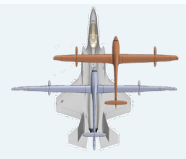
TS / SAP Multi-Level Secure Cloud

- » All source inputs with MLS outputs for advanced kill web functions
- » Time dominant focus enabling revolutionary situational awareness
- » Advanced analytics enabling machine learning



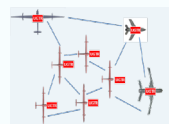
Very Long Endurance UAVs

- » Mission flexibility with minimum logistics
- » Provides huge numerical advantage
- » Enable new mesh networking methods without new radios on military platforms
- » Enduring global presence



Secure Edge Mesh Networks

- » Interconnects UAVs and other platforms
- » Cross-banding path for existing DOD links
- » Hard to detect and jam
- » Diverse WAN connections & advanced software defined networking



JADC2 INITIATIVES

Current State of Affairs

- » DOD currently performs C2 using separate segments of the battle space, primarily along the identified military domains of air, land, sea space, and cyberspace
- » Technological advances since the 1980s have enabled DOD to continue developing concepts for joint all-domain operations
- » This increased complexity is designed to offer options for military commanders to build and prosecute "Kill Webs"

Enabling Concepts for JADC2 Implementation

- ✓ **Discoverable Data**
 - » Envisions an enterprise-level methodology providing discoverable data with multi-levels of secure access across a distributed architecture
- ✓ **Intelligent Battle Management Aids**
 - » Provide a cloud-like environment using AI/ML to share ISR data to enable faster decision-making
- ✓ **DevSecOps + Open Architecture**
 - » Use agile development and software factories to speed capability delivery to the warfighter



KEY TAKEAWAYS FROM THE PARIS AIR SHOW

AIRBUS

» At the first Paris Air Show since 2019, we saw record-breaking orders booked and exciting buzz around emerging technologies including eVTOL aircraft, supersonics, and sustainability



» Indian low-cost carrier IndiGo's order of 500 A320 family aircraft was the biggest single aircraft purchase in history



» As part of its ZEROe hybrid aircraft program, Airbus announced a hydrogen fuel cell APU for the A330, with aims to reduce CO2 and NoX emissions and lower noise pollution

BOEING



» Boeing is set to lift production rates of the 737 MAX from 31 to 38 per month



» Boeing is still grappling with quality issues and a supply chain crunch. The company cited skilled labor as a "pinch point" to get to its efficiency output goals

OTHER KEY THEMES

eVTOL

» eVTOL aircraft startups took center stage with attention-grabbing new electric vehicles



Supersonic Aircraft

» Boom Aerospace announced at the Air Show that its Overture supersonic airliner remains on schedule for FAA certification by the end of this decade





COMMERCIAL ORDER PLACEMENTS & RECOVERING BUILD RATES

» While Airbus booked 821 orders during the Air Show, including a historic 500 aircraft order from IndiGo, Boeing's more muted 356 orders booked comes after booking over 1,000 orders over the last year

AIRSHOW COMMERCIAL ORDER PLACEMENTS

AIRBUS			BOEING		
Aircraft	Quantity	Customers	Aircraft	Quantity	Customers
A220	9		737 BCF	2	
A320	740	IndiGo; flynas; Air India	737 MAX	296	Avolon; Air Algeria; Air India; Luxair; Akasa Air
A330neo	20		777X	10	
A350	50	Air Mauritius; Philippine Airlines; Air India	787	48	
Total	821		Total	356	

» Despite continued supply chain uncertainty, labor shortages, raw material deficits, and skyrocketing energy prices, OEMs continue to increase monthly build rates, with full rate production across the major platforms expected by early 2025

RECOVERING COMMERCIAL BUILD RATES

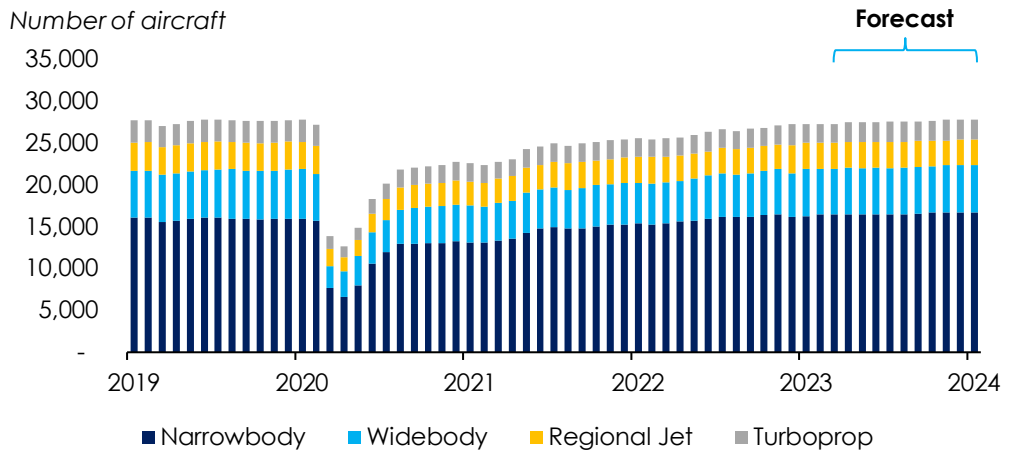
Platform	Deliveries YTD	Net Orders	Build Rate by Month	Backlog
	Through May 2023		May 2023	
B737	167	388	31 → 38	4,215
A320	199	827	45	5,983
A220	19	21	6	520
B777/ 777X	8	4	3	426
B787	25	48	3 → 5	594
A350	14	92	5	432
B747	1	0	0	0
A330	12	21	3	204



SUPPLY CHAIN CHALLENGES & FLEET RECOVERY

» In January 2023, the global commercial fleet had ~27,400 aircraft in service, just shy of the January 2020 peak of almost 28,000 set before the outbreak of the COVID pandemic. The global commercial fleet is expected to surpass its old record sometime in 2H 2023

COMMERCIAL FLEET RECOVERY IN 2023



CONTINUING SUPPLY CHAIN CHALLENGES

Key Challenges

- ✓ **Labor**
 - » Suppliers remain capacity-constrained as they work to recruit and retrain to improve productivity
- ✓ **Material Availability**
 - » Improving, but on-time delivery below growth rate
- ✓ **Rising Costs**
 - » Significant price increases across the board, particularly on raw materials and chemicals for protective coatings

Aerostructures

- » Spirit AeroSystems and its machinists union reached a tentative contract agreement on June 26th, highlighting the tight labor conditions across the A&D manufacturing sector



Aircraft Engines

- » Pratt & Whitney has faced backlash from airlines over durability issues and a shortage of spare engines on its GTF platform, with groundings peaking at 10% of the GTF-powered fleet in the first half of this year



A&D CAPITAL AND DEBT MARKETS UPDATE

A&D STOCKS RALLY IN LINE WITH BROADER MARKET

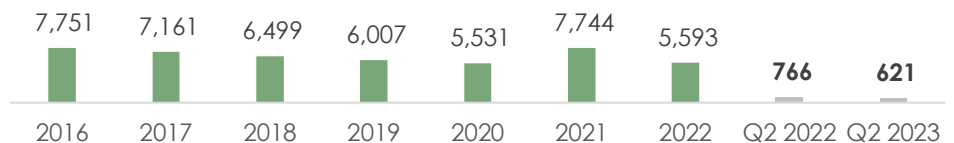
- » The overall market rebounded in Q2 2023 as fears of a banking crisis have been quelled
- » With continued expected pressure on earnings, commercial stocks are viewed as a growth play while defense stocks are viewed as an inflation hedge

iShares US Aerospace and Defense Index vs. S&P500 vs. Dow Jones IA (LTM)

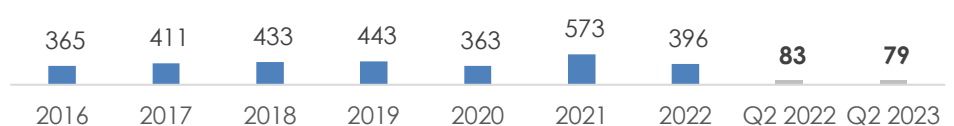


A&D M&A HOLDS AMID TIGHTENING DEBT MARKET

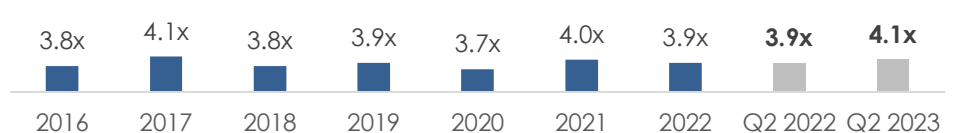
Global Middle-Market (<\$500mm) M&A Deal Volume



A&D Middle-Market (<\$500mm) M&A Deal Volume



M&A Deals DEBT / EBITDA Multiple







- » While debt markets have tightened causing a significant decline in global M&A deal activity, A&D remains a safe haven for investors looking to deploy capital with strong industry fundamentals on both the commercial (increasing production rates) and defense (increasing budget environment) side

» As the market rebounded in the Q2 of 2023, A&D stocks were buoyed by strong fundamentals of a strong commercial up-cycle and an expansionary budget environment for the foreseeable future

» A&D deal volume has remained resilient despite global M&A volume declining ~20% year-over-year

COMMERCIAL AEROSPACE SECTOR OVERVIEW

PUBLIC MARKET PERFORMANCE

Company	Share Price	52-Wk.High	Market Cap. (\$bn)	EV/Revenue		EV/EBITDA	
				NTM	LTM	NTM	LTM
 BOEING	210.9	223.9	126.9	2.1x	2.4x	n/a	n/a
AIRBUS	132.3	134	114.0	1.5x	1.7x	11.0x	14.1x
 SPIRIT	\$29.8	38.6	3.1	1.0x	1.2x	12.4x	n/a
HEICO	176.3	180.6	21.2	7.8x	8.9x	29.2x	32.0x
 MTU	237.4	245.1	13.9	2.0x	2.6x	11.7x	18.0x
TRANSDIGM <small>GROUP INC.</small>	896.5	899.6	49.2	9.7x	11.3x	19.4x	23.8x
 Parker	391.0	392.8	50.2	3.2x	3.5x	13.8x	15.8x

NOTABLE TRANSACTIONS

Target	Acquirer	Description
 WENCOR GROUP	HEICO	» Wencor is a distributor of aftermarket parts and a large independent provider of Parts Manufacturer Approval (PMA) parts to the commercial aircraft sector
 KP AVIATION	 BainCapital	» KP Aviation is a supplier of high-quality aftermarket components and assets across a broad range of aircraft and engine platforms

KKR WINS BUYOUT BATTLE FOR CIRCOR

KKR

- » **June 5, 2023**, KKR offered to acquire Circor for \$49/share, (\$1.6bn valuation)
- » **June 28, 2023**, KKR raises offer to \$52.65/share
- » **June 30, 2023**, KKR raises offer to \$56/share

 **CIRCOR**

ARCLINE

- » **June 27, 2023**, Arcline offers \$57 per share, (\$1.8bn valuation)
- » **Despite Arcline's higher bid, Circor's board has stuck with KKR, citing anti-trust concerns and KKR's full equity backstop**

The public buyout battle for Circor reveals a new normal for the private equity and highlights the high desirability of A&D flow control assets

» As commercial aerospace continues to benefit from a recovery past the previous 2019 highs, stocks have approached or surpassed their 52-week highs

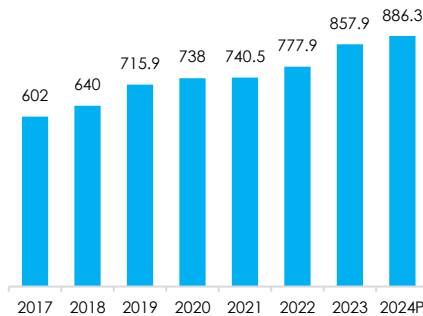
DEFENSE & GOVERNMENT SERVICES OVERVIEW

FY24 DEFENSE BUDGET REVIEW

Continued Budget Increases Amid National Security Challenges

- » Modernization of defense forces to keep pace with global challenges
- » Although an increase of 3.3% over FY2023, critics contend that this may not be enough to accommodate modernization programs
- » RDT&E spending is expected to decline as next generation programs shift from development to production, but there is a continued DoD focus on microelectronics, AI, hypersonics, and C5ISR initiatives
- » Over 40% of procurement spending is concentrated in aircraft acquisitions and shipbuilding & conversions

NDAAs Defense Budget Hist.



Source: NDAAs Executive Summaries

FY24 DoD Budget Breakdown

Department	Amount
Procurement	168.6
RDT&E	145.1
Operation & Maintenance	289.3
Military Personnel & Health	216.8
Construction & Family Housing	17.5
Defense Nuclear Programs	32.3
Total Defense Discretionary	886.3

NEXT-GENERATION AIR DOMINANCE PLATFORM

NGAD Spending (U.S. \$ Millions)

	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	Total
Next-Generation Air Dominance	-	22	283	403	873	870	1,453	1,658	1,934	2,972	3,538	3,655	4,131	21,790
Next-Generation Adaptive Propulsion	-	-	-	-	121	343	106	220	595	580	457	291	-	2,716
Collaborative Combat Aircraft	-	-	-	-	-	-	-	-	392	514	246	1,644	3,033	5,828
Air Dominance Air-to-Air Weapon	-	-	1	11	-	-	-	-	-	-	-	-	-	12
2030+ Air Dominance	33	-	-	-	-	-	-	-	-	-	-	-	-	33
Annual Total	\$ 33	\$ 22	\$ 284	\$ 414	\$ 993	\$ 1,212	\$ 1,559	\$ 1,878	\$ 2,922	\$ 4,065	\$ 4,240	\$ 5,589	\$ 7,164	\$ 30,375

Source: USAF Budget Justification documents








- » U.S. Air Force is expected to field a contract award for the NGAD in 2024
- » Boeing, Lockheed and Northrop have been preparing for this phase of the contract competition and were also awarded the Next-Generation Adaptive Propulsion contracts for integration studies

» Record procurement numbers bodes well for companies who are part of the supply chain for various platforms expected to grow in the coming years







» A significant portion of the record setting Procurement & RDT&E investments is being attributed to the NGAD platform, which brings the expected total to \$30 billion up to 2028

DEFENSE & GOVERNMENT SERVICES OVERVIEW

PUBLIC MARKET PERFORMANCE

Company	Share Price	52-Wk.High	Market Cap. (\$bn)	EV/Revenue		EV/EBITDA	
				NTM	LTM	NTM	LTM
 Raytheon Technologies	98.4	108.8	143.5	2.4x	2.6x	13.5x	14.2x
 LOCKHEED MARTIN	462.6	508.1	117.1	2.0x	2.0x	13.2x	14.4x
 NORTHROP GRUMMAN	458.2	556.3	69.6	2.1x	2.3x	15.2x	10.2x
 GENERAL DYNAMICS	215.8	256.9	59.1	1.6x	1.7x	12.6x	12.1x
 L3HARRIS™ FAST FORWARD	197.7	255.1	37.5	2.7x	2.7x	13.2x	16.3x
 BAE SYSTEMS	9.3	10.4	39.1	1.4x	1.7x	10.8x	12.5x
 leidos	88.4	110.9	12.1	1.1x	1.2x	11.1x	10.5x

NOTABLE TRANSACTIONS

Target	Acquirer	Description
 ADRANOS	 ANDURIL	» Adranos is a developer of high-performance, solid propellant for long-range missile and space launch systems
 MB AEROSPACE	 BARNES	» MB Aerospace supplies precision aero-engine components for missile systems, torpedo modules, rocket motors and other 'direct to line' sub-assemblies
 VERUS TECHNOLOGY GROUP	 BLUEHALO	» Verus is a developer and manufacturer of Counter Unmanned Aircraft Systems (CUAS) products and services

PROPRIETARY PRODUCTS SPOTLIGHT

- » The proprietary products M&A market continues to attract top A&D investors and achieve benchmark-setting multiples. Look for the proprietary A&D products market to remain active throughout 2023, as their entrenched positions and IP drive multiples higher

Notable Proprietary Products Transactions

Acquirer	Target
 ARCLINE ELECTRONIC SOLUTIONS	 VERITAS CAPITAL
 TRANSDIGM GROUP INC.	 LOARGROUP
 INTERNATIONAL Water-Guard	 Sequa CHROMALLOY
 Calspan	 DESSER Proprietary Solutions Businesses

» Public companies in the defense sector are trading near 52-week highs, bolstered by a growing 2023 defense budget

RECENT TRANSACTIONS

 HAS BEEN ACQUIRED BY ARCLINE <small>AVIATION PARTS & SUPPLY</small> SALE OF COMPANY	 HAS BEEN ACQUIRED BY ROTOR CAPITAL SALE OF COMPANY	 HAS BEEN ACQUIRED BY OMEGA MORGAN SALE OF COMPANY	 HAS BEEN ACQUIRED BY TRIVE CAPITAL SALE OF COMPANY	 HAS BEEN ACQUIRED BY Lincotek SALE OF COMPANY	 HAS BEEN ACQUIRED BY TRIVE CAPITAL SALE OF COMPANY	 HAS BEEN ACQUIRED BY INRCORE A PORTFOLIO COMPANY OF THE JORDAN COMPANY SALE OF COMPANY
 HAS BEEN ACQUIRED BY NOVARIA GROUP A PORTFOLIO COMPANY OF KKR SALE OF COMPANY	 HAS BEEN ACQUIRED BY VITESSE SYSTEMS SALE OF COMPANY	 HAS BEEN ACQUIRED BY CRESVIEW AEROSPACE A PORTFOLIO COMPANY OF AMERICAN INDUSTRIAL PARTNERS SALE OF COMPANY	 HAS BEEN ACQUIRED BY KARMAN A PORTFOLIO COMPANY OF TRIVE CAPITAL SALE OF COMPANY	 HAS BEEN ACQUIRED BY ENDEAVOUR SALE OF COMPANY	 HAS BEEN ACQUIRED BY Deloitte. SALE OF COMPANY	 HAS BEEN ACQUIRED BY AS ALLIANCE GROUP A PORTFOLIO COMPANY OF GREENBRIAR EQUITY GROUP LLC SALE OF COMPANY
 HAS BEEN ACQUIRED BY SUNVAIR AEROSPACE GROUP A PORTFOLIO COMPANY OF BLUE SEA CAPITAL SALE OF COMPANY	 HAS BEEN ACQUIRED BY CHARGER SALE OF COMPANY	 A PORTFOLIO COMPANY OF GENCAP AMERICA HAS BEEN ACQUIRED BY Calspan SALE OF COMPANY	 HAS BEEN ACQUIRED BY KROTOS SALE OF COMPANY	 HAS RECEIVED EQUITY INVESTMENT FROM GREENBRIAR EQUITY GROUP LLC EQUITY INVESTMENT	 HAS BEEN ACQUIRED BY HEROUX DEVTEK SALE OF COMPANY	 A PORTFOLIO COMPANY OF TRIVE CAPITAL HAS BEEN ACQUIRED BY MDP SALE OF COMPANY

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