Driving forces of M&As in Aerospace

In the first half of 2017, aerospace and defense M&A volume remained well above the historical 10-year average despite slowing order activity and continued cost pressures on the supply chain.

During the first six months of 2017, aerospace and defense transaction volume was down slightly from the second half of 2016, with 199 transactions compared to 227. However, year-over-year, transaction volume was up 43 percent compared to the first half of 2016. Strong activity across IT services and software, commercial components and subsystems, and composites segments served as transaction drivers.

Near term M&A activity in the industry will likely benefit from the positive momentum established during the Paris Air Show, where order activity for both narrow body commercial and defense aircraft was stronger than expected.

Against this backdrop, in addition to strong long-term air traffic and build rate forecasts, we expect several trends to drive continued industry consolidation in the second half of 2017.

OEM Build Rate Increases Continue to Stress Supply Chain

Both Boeing and Airbus continue to look for ways to aggressively cut costs and increase build rates on key platforms. The price and order competition on comparable platforms such as the 737 vs A320 and 787 vs A350 remains fierce. After several years of embracing an expanded supplier base, both OEMs are driving their respective supply chains to consolidate so they can regain control over technological capabilities, cost, and capacity.

As a result, suppliers are faced with the challenge of substantially building production capacity while simultaneously providing near-term price reductions. This is driving key suppliers to make significant investments in equipment, systems, and acquisitions to expand capabilities and/or enhance automation.

While large Tier I suppliers such as Spirit, Safran, and Triumph have the resources to support these demands, the competitive dynamic presents a challenge for small to mid-sized Tier I and Tier II suppliers.

“Investors are aggressively seeking opportunities that offer proprietary content, an MRO offering, or unique manufacturing capabilities.”

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M&A Interest Focused on Proprietary Content and Cross Border Activity

Key strategic investors and industry focused private equity firms continue to demonstrate a strong M&A appetite. In particular, as the commercial build-to-print market has become increasingly competitive, investors are aggressively seeking opportunities that offer proprietary content, an MRO offering, or unique manufacturing capabilities.

Additionally, several well-established Tier I Airbus suppliers based in Europe and Asia are seeking US acquisitions with direct relationships with North American OEMs.

These investment rationales, coupled with the pricing and build-rate pressures outlined above, are likely to lead to continued industry consolidation over the next 12 months.

Boeing’s Impact on the MRO Market

Boeing used the Paris Air Show to further set the stage for the planned launch of its new Global Services business that aims to capture a much larger share of the global maintenance, repair, and overhaul market. Specifically, Boeing is aggressively targeting to reach $50 billion in MRO revenue within the next 10 years.

Historically, the MRO market has been highly fragmented with airlines valuing characteristics such as flexibility, responsiveness, and competitive pricing often associated with smaller, independent companies. Boeing intends to address these customer needs through an internal reorganization as well as through selective acquisitions.

Boeing’s rejuvenated commitment to the MRO market will likely drive consolidation at all levels as companies look to position themselves to protect market share and expand differentiated capabilities.