

KAL Capital - Aerospace & Defense

Quarter In Review

Introduction

Dear Friends,

We hope that everyone is enjoying a great start to their summer!

During the second quarter, we witnessed financial markets realize that the inflationary pressures (both labor and raw material) could no longer be dismissed as transitory and that a more restrictive monetary policy would be required to tame the price pressures exacerbated by COVID supply-chain disruptions and the war in Ukraine. This shift in policy has had a negative impact on public equity valuations, particularly on areas that had witnessed the steepest increases such as cryptocurrency and early-stage technology companies. These equity valuation declines reflect a significant risk that the US economy is now or will shortly be in a recession.

All that being said, the impact on aerospace M&A activity and valuation trends has been extremely limited. KAL Capital has witnessed that first-hand with three closed transactions in the quarter (a new record for the firm!); we dive into these great outcomes later in this report.

The reality is that the end-markets that our clients serve are the least likely to be impacted by a recession and should continue to grow despite any broader economic malaise. On the defense-side, we continue to see incredibly strong M&A appetite by the buyer community as optimism around the sustainability of growing DoD budget trends is as strong as ever. The last quarter witnessed several landmark transactions including Carlyle's acquisition of Mantech, but for us we continue to see a consistent drum beat of activity further down the supply-chain as private equity-backed strategic buyers lead the way.

Commercial aerospace activity continues to be generally positive but remains well below pre-COVID activity levels. This is primarily due to challenges in the Boeing supply-chain as MAX and B787 production continue to disappoint supply-chain participants. That said, the astounding rebound in air travel is the best leading indicator for an industry on its way to recovery. The recent, well publicized challenges with on-time performance will surely get better over time.

In summary, we continue to believe the aerospace/defense M&A markets will be insulated from broader economic pressures assuming the financing market remains somewhat normalized.

We are headed to the Farnborough Airshow and would love to meet-up in-person!

Sincerely,



Trevor Bohn
Partner



Ryan Murphy
Partner

Table of Contents

I. KAL Capital Overview

II. KAL Advises Systems Vanguard Electronics

III. KAL Advises Systems Hitemco

IV. Q2 2022 M&A Update

V. Defense and Government Services Overview

VI. Defense Focus: Resilient Amid Uncertainty

VII. Commercial Focus: Quarter in Review

VIII. Commercial Aerospace Market Overview



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 Vanguard Electronics

Vanguard Electronics Acquired by iNCORE, LLC



- Vanguard Electronics is a leader in the design and manufacture of inductors and transformers with a reputation for reliability in demanding environments
- KAL Capital announced the sale of Vanguard Electronics to iNCORE, a portfolio company of The Jordan Company, where KAL served as the sell-side advisor on the transaction
- Vanguard offers a complete line of RF and Power components ranging from milliwatt chip inductors to 10kVA power transformers

Focused on High-Performance RF and Power Components

RF & Microwave Products



Fixed Chip Inductors



Air Core Inductors



Wideband Transformers



Torodial Inductors

Power Magnetics



Pulse & Data Bus



Custom Products

- *Nearly 6 decades of successful custom inductors and transformers production*

Investment Highlights

Vertically-Integrated with In-House Engineering, Design, and Fabrication

Blue Chip Defense Electronics Customer Base

Positioned on Key, High Growth Missile Programs

Unique Suite of Approvals and Processing Capabilities

Focused on High-Performance RF and Power Components

❖ By adding Vanguard's product suite, iNCORE will solidify its place as the premier provider of power magnetics, RF, microwave components and custom solutions

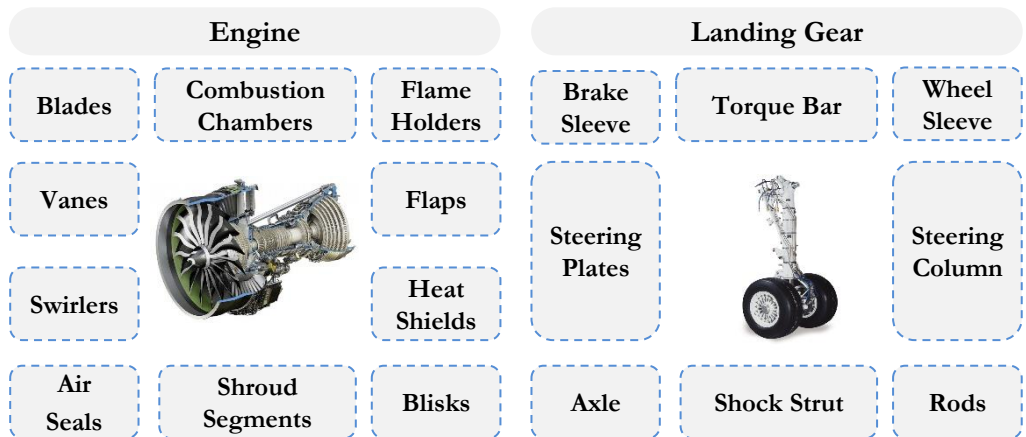
KAL Advises Hitemco

Hitemco Acquired by Lincotek



- KAL Capital announced the sale of Hitemco to Lincotek, where KAL served as the sell-side advisor on the transaction
- Hitemco is a leading independent provider of diffusion and thermal sprayed enhanced surfaces serving the aerospace, energy, minerals, and transport industries. The business has developed a particular expertise in diffusion coatings
- Headquartered in Parma, Italy, Lincotek is vertically-integrated provider of surface treatments and coatings for turbine blades and vanes

Surface Treatments for Performance-Critical, High-Value Components



Investment Highlights

Technical Leader in the Design & Engineering of Thermal Spray & Diffusion Coatings

Positioned on Key Commercial & Military Platforms at Every Stage of the Production Lifecycle

Significant Investment in Infrastructure and Capacity to Support Future Growth

State-of-the-Art In-House Thermal Spray & Diffusion Coatings Automation Capabilities

Unique Management System Focused on Fast Turnaround

❖ By adding Hitemco's capabilities, Lincotek will be uniquely positioned to offer the aerospace and IGT markets the most complete set surface treatment solutions of services to date

Q2 2022 M&A Update

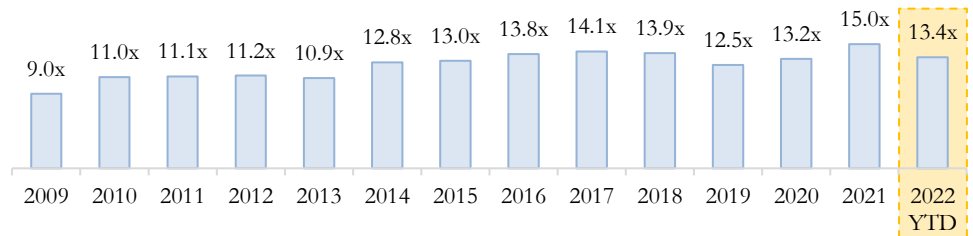
❖ Companies received unprecedented returns in the M&A market as multiples continued to climb in 2022

❖ The growth of M&A in 2021 should continue in Q2 2022 as investors continue to look to M&A for growth amid a volatile market

EBITDA Multiples on the Rise

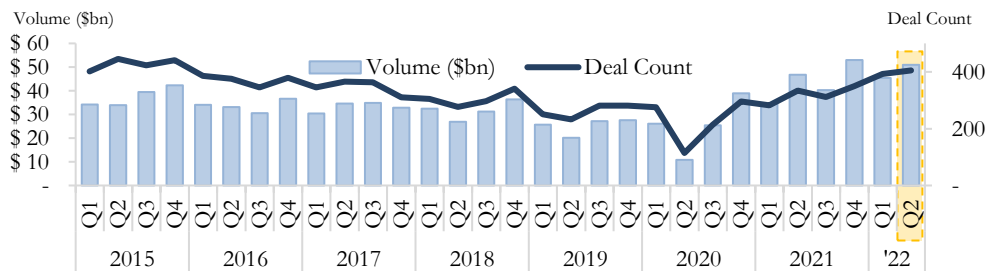
- EV/EBITDA Multiples surpassed the record highs from 2021 as buyers are ready to deploy their reserve capital throughout 2022
- The average EBITDA Multiple has increased from 9.0x in 2009 to 13.4x in 2022 YTD

Average A&D EV/EBITDA Multiples



Long Term M&A Volume

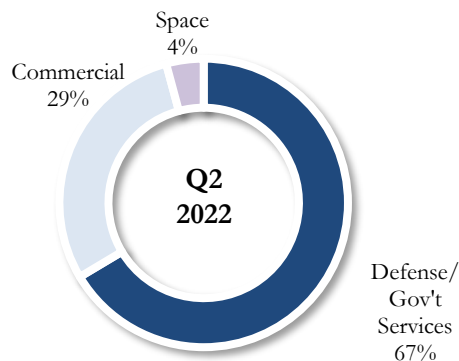
- The U.S. M&A market has remained strong following a record setting year in 2021 with many of the underlying market dynamics remaining the same in 2022
- Private equity dry powder remains near all time highs, leading experts to forecast continued high levels of M&A throughout 2022



Most major firms predict the momentum to continue well in into 2022 as demonstrated in Q1 and Q2, despite rising rates and political factors

2022 Q2 Aerospace & Defense M&A

End Market Breakdown












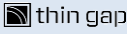


- Defense:** Defense and Gov't services transactions continue to grow at unprecedented rates
- Commercial:** The global commercial aircraft market is expected to grow from \$163bn to \$181bn in 2022 representing a CAGR of 10.2%
- Space:** 2022 space related M&A activity is expected to far surpass previous years with the second quarter showing a significant increase in deal volume over the first quarter of 2022

Defense & Government Services Overview

❖ Public companies in the defense sector are trading near 52-week highs, bolstered by a growing 2022 defense budget

Public Market Performance								
Company	Share Price	% of 52-Wk.High	Market Cap. (\$bn)		EV/Revenue		EV/EBITDA	
			06/30/22	12/31/21	2022	2021	2022	2021
 Raytheon Technologies	\$92.92	87.5%	\$ 137.81	\$ 134.95	2.7x	2.5x	14.5x	13.6x
 LOCKHEED MARTIN	415.25	86.5%	110.61	99.83	1.9x	1.7x	13.7x	12.3x
 NORTHROP GRUMMAN	464.36	94.3%	72.17	62.93	2.5x	1.9x	9.5x	7.5x
 GENERAL DYNAMICS	214.53	84.1%	59.46	59.11	1.9x	1.7x	12.8x	11.8x
 L3HARRIS™ FAST. FORWARD.	230.96	82.6%	44.59	41.99	3.1x	2.7x	14.6x	12.8x
 BAE SYSTEMS	38.87	94.5%	31.89	17.28	1.4x	1.2x	9.9x	9.0x
 leidos	99.58	89.6%	13.61	12.89	1.4x	1.2x	11.2x	9.7x
 Nasdaq	157.49	73.2%	25.94	34.97	5.5x	5.8x	15.6x	16.5x

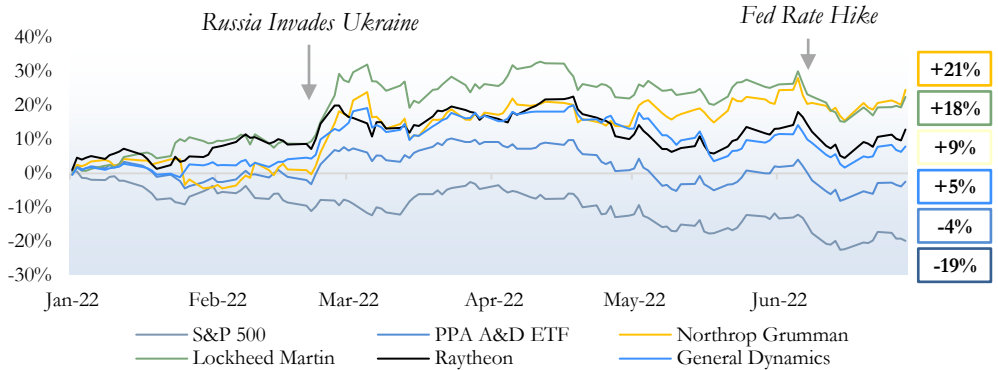
Notable Transactions		
Target	Acquirer	Description
 ManTech	 THE CARLYLE GROUP	▪ Defense contractor that offers solutions in the cyber, data collection & analytics, and software engineering fields.
 TELEPHONICS™ Specialty Technology & Services A Lockheed Company	 TTM Technologies	▪ Provider of highly sophisticated intelligence, surveillance and communications solutions deployed across a wide range of land, sea and air applications
 PVP ADVANCED EO SYSTEMS	 RAFAEL	▪ Specifies in the development, manufacturing and sustainment of EO systems for air, land, sea and critical homeland security applications.
 Xator CORPORATION	 PARSONS	▪ Federal contractor specializing in technology-focused defense, intelligence, security and infrastructure engineering

Active Buyer Highlight	
 Allied Motion	Recent Acquisitions
	 thin gap <ul style="list-style-type: none"> ▪ Leading developer and manufacturer of high performance, zero clogging slot-less motors
	 AIREX™ <ul style="list-style-type: none"> ▪ Provides precision electromagnetic components and solutions
<ul style="list-style-type: none"> ▪ Public company that produces precision and specialty motion control components and systems for aerospace and defense markets 	 FDP GROUP <ul style="list-style-type: none"> ▪ Technically advanced, reliable and cost-effective electrical drive systems and light weighting technologies

Defense Focus: Resilient Amid Uncertainty

US Commitment to Ukraine Security and Sovereignty Lifts Defense Sector

Public Market Returns



- During a time of geopolitical uncertainty, as hearts and minds are focused on the human tragedy, the economic implications of such a seismic event cannot go unnoticed
- Since Russian unleashed its war, the overall market has seen a 15% dip. The US response to Russian aggression and its unwavering commitment to support Ukraine's sovereignty and territorial integrity has buoyed the defense market countering the negative effects supply chain concerns and inflation have inflicted on the rest of the overall market

Key Program Implications for Ukraine Crisis

- The crisis has necessitated a response from the international community causing the US to provide necessary equipment to thwart the invasion and NATO allies to reassess their procurement strategies, recalculate their stance on defense spending in the face of the crisis
- Below are the key missile and aircraft programs most significantly affected:

Weapons System



Javelin/Stinger



HIMARS



NASAMS



F-35

OEM



Recipient/Country



Contract Description

Pentagon moved \$1.45bn to the Army and Marine Corps to restock Javelin anti-tank and Stinger anti-aircraft missiles that the U.S. sent to Ukraine

Lockheed Martin won a \$160mm contract to supply the M142 HIMARS to the U.S. Army and Marine Corps, of which 8 have been sent to Ukraine

U.S. is finalizing new contract with Raytheon for supply of NASAMS, having already sent 2 to Ukraine as part of latest aid package

Germany has committed to buying 35 new aircraft worth up to \$100bn; it will serve as Germany 5th gen nuclear fighter for years to come

❖ U.S. has committed to providing more than \$6.9bn in military assistance since Russia launched its brutal invasion

❖ The defense industry has remained resilient in the face of global geopolitical uncertainty and the resulting supply chain shocks and rise in inflation, outperforming the overall market

❖ The US continues to standby Ukraine in its efforts to defend itself from Russia's invasion providing advanced rocket systems and munitions while NATO allies revise their strategy investing and modernizing their fleets

Commercial Focus: Quarter in Review

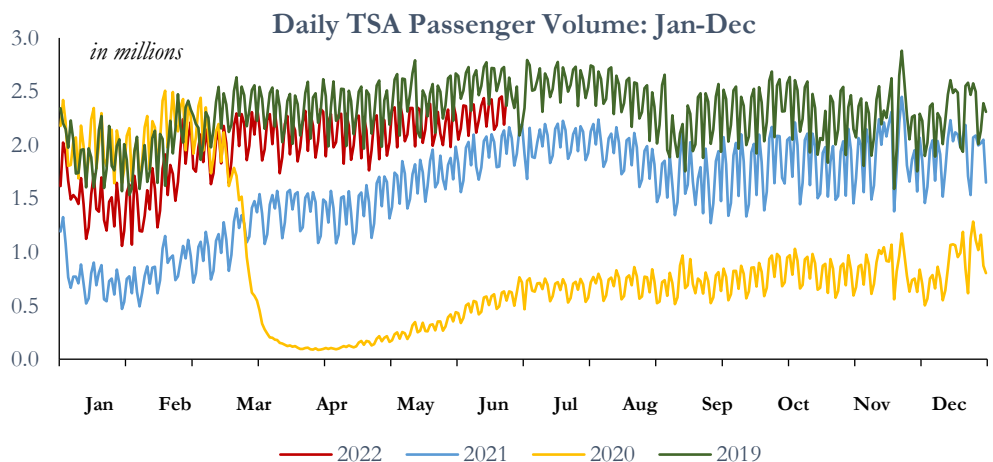
Boeing and Airbus Deliveries, Orders, Build Rates & Backlog

- Boeing and Airbus delivered 35 and 47 commercial jets in May 2022, and 165 and 237 respectively YTD through May
- Through Q1 of 2021, Boeing and Airbus delivered 156 and 297 commercial jets respectively, they are on track to beat these numbers pending June 2022

Platform	Deliveries YTD	Net Orders	Build Rate by Month	Backlog
	Through May 2022		May 2022	
B737	145	132	27	4,125
A320	183	191	45	5,847
A220	19	73	5	529
B777/ 777X	9	45	2	432
B787	0	-6	2	482
A350	24	7	5	440
B747	3	0	0.5	3
A330	11	-80	2	221






Narrow Body Aircraft Passenger Counts

- Narrowbody aircraft passenger traffic are expected to see continued strengthening as the airline industry continues along the road to recovery as pre-pandemic levels are approached and surpassed



Commercial Aerospace Market Overview

Public Market Performance								
Company	Share Price	% of 52-Wk.High	Market Cap. (\$bn)		EV/Revenue		EV/EBITDA	
			06/30/22	12/31/21	2022	2021	2022	2021
 BOEING	\$ 137.70	57.1%	\$ 81.47	\$ 125.55	2.1x	2.5x	15.4x	17.1x
AIRBUS	23.35	66.7%	76.64	94.61	1.2x	1.7x	8.2x	13.4x
 SPIRIT AEROSYSTEMS	30.41	57.0%	3.20	2.54	1.4x	1.8x	12.0x	16.4x
HEICO	130.94	82.2%	15.70	18.69	8.2x	9.7x	27.0x	35.7x
 MTU Aero Engines	83.55	65.6%	9.67	10.19	2.8x	1.9x	12.8x	18.8x
TRANSDIGM GROUP INC.	527.27	76.8%	28.78	35.58	9.0x	10.7x	20.0x	24.9x
 Parker	246.31	72.4%	31.62	41.64	2.5x	3.1x	11.4x	14.5x
 Nasdaq	157.49	73.2%	25.94	34.97	5.5x	5.8x	15.6x	16.5x

Notable Transactions		
Target	Acquirer	Description
 Parker Aerospace	 KAMAN AEROSPACE	<ul style="list-style-type: none"> Manufactures aircraft wheel and brake systems and related hydraulic products for the general aviation, business aviation, rotorcraft, and military aircraft markets
 FMI CHEMICAL	NOVARIA GROUP	<ul style="list-style-type: none"> Supplies aircraft OEMs and MRO facilities worldwide with nonmetallic aerospace sealants, compounds and coatings for aircraft manufacturing and MRO
 VELOCITY AEROSPACE	 PAG	<ul style="list-style-type: none"> Provides a broad range of aviation maintenance, repair, and overhaul services. The company's customers include a global base of commercial air transports, corporate business aircraft, regional airlines, and helicopters

HEICO– Active Buyer Highlight	
 <ul style="list-style-type: none"> Heico Corp is a publicly traded aerospace and electronics company Products are found in aircraft, spacecraft, and defense equipment 	Recent Acquisitions <ul style="list-style-type: none">  PIONEER INDUSTRIES, INC. <ul style="list-style-type: none"> Full-Service spare parts dealer serving commercial and government industries  Furukawa Microwave <ul style="list-style-type: none"> Designer & Manufacturer of high-powered passive microwave components  PACIWAVE, INC. <ul style="list-style-type: none"> Designer and manufacturer of RF and microwave components and integrated assemblies



3738 Bayer Ave
Suite 103
Long Beach, CA 90808
www.kalcap.com
P: (949) 404-4201

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Trevor Bohn
Partner
(949) 404-4203
trevor@kalcap.com



Ryan Murphy
Partner
(949) 404-4204
ryan@kalcap.com

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