

Summer 2005

## Industry Update

### Sweet Home Alabama

After evaluating more than 70 candidates from 32 states, European Aeronautic Defence and Space Company's (EADS) North American operations announced that it selected Mobile, Alabama's Brookley Industrial Complex as the site for its KC-330 advanced tanker U.S. production facility. Airbus' KC-330 is the competing aircraft to Boeing's 767 tanker. Mobile provides a strategically located complex on the Gulf of Mexico with existing runways, a deepwater port, and a skilled aerospace workforce. An airbus engineering center will be co-located with the future production facility and is scheduled to begin operations in 2006.

Historically, breaking down the wall that separates non-U.S. companies from coveted U.S. defense contracts has been nearly impossible to do. But amid the ethics scandal at Boeing, the door has been opened for other companies to enter into the mix for a potential U.S. Air Force tanker replacement program, and EADS appears to be the next most capable candidate. With the opening

of the Brookley Industrial Complex for its KC-330 production, and potentially partnering with a U.S. aerospace company (Northrup Grumman appears to be the most likely candidate for this role), EADS appears to be taking all the right steps to make itself a viable option. However, the political hurdles may be too high for a US\$20+ billion contract to be awarded solely to a foreign-owned company, especially in light of recent legislation proposed in the U.S. House of Representatives that would deny military contracts to any foreign company, such as EADS, receiving a government subsidy in a country that is a member of the World Trade Organization. Given the circumstances, it is conceivable that a split contract could be awarded to multiple contractors, which could include EADS.

### New Aircraft Commitments Announced at the Paris Air Show

With 461 new aircraft commitments announced at this year's Paris Air Show, the commercial aircraft industry is on pace to have one of its best years of new orders

since 2000. Assuming these commitments eventually convert to firm orders, the industry will have booked more than 900 new aircraft orders in 2005.<sup>1</sup> By comparison, 1,026 total orders were recorded in 2000. At current planned production rates, this significant up-tick in orders has led to a near-term sellout of some aircraft, such as Boeing's new 787 Dreamliner, which is sold out through 2010. As a result, Airbus and Boeing are carefully considering increasing production rates of their highest demand aircraft.

Other headline events at the Air Show included Northrup Grumman's award of more than US\$300 million in contracts to European companies for work on the F-35 Joint Strike Fighter; Pratt & Whitney's relaunch of its PW6000 engine for use on narrowbody aircraft, such as the Airbus A318; and the announcement of US\$4 billion in engine support contracts to Snecma Services and General Electric from Northwest Airlines and AirAsia, respectively.

<sup>1</sup> SG Cowen, *Boeing Company Coverage Report: Upbeat Paris Inputs Outweigh Air Canada Cancellation*, June 20, 2005

New Aircraft Commitments Announced at 2005 Paris Air Show							
Boeing			Airbus			Total	
Model	Ordered		Model	Ordered			
737	104	73%	A320	202	63%		
777	38	27%	A330	17	5%		
787	0	0%	A350	95	30%		
			A380	5	2%		
<b>Total</b>	<b>142</b>	<b>100%</b>		<b>319</b>	<b>100%</b>	<b>461</b>	
<b>Aisle Configuration</b>							
Single Aisle	104	73%		202	63%	306	66%
Twin Aisle	38	27%		117	37%	155	34%
<b>Total</b>	<b>142</b>	<b>100%</b>		<b>319</b>	<b>100%</b>	<b>461</b>	<b>100%</b>
<b>Geographic Mix</b>							
EU	22	15%		18	6%	40	9%
AP	0	0%		8	3%	8	2%
India	20	14%		78	24%	98	21%
Mid East	20	14%		125	39%	145	31%
NA Airline	32	23%		0	0%	32	7%
Leasing	48	34%		10	3%	58	13%
Other	0	0%		80	25%	80	17%
<b>Total</b>	<b>142</b>	<b>100%</b>		<b>319</b>	<b>100%</b>	<b>461</b>	<b>100%</b>

Source: SG Cowen, Boeing Company Coverage Report: Upbeat Paris Inputs Outweigh Air Canada Cancellation, June 20, 2005

### M&A Update

Aerospace and defense deal flow slowed considerably in the second quarter of 2005 compared with Q1 2005. However we feel these results are a bit misleading because first-quarter transaction volume was very

strong, by historical standards. Going forward we anticipate industry M&A activity to remain robust. JPMorgan reports that industry free cash flows in 2004 increased 34 percent to US\$17.8 billion, of which only 30 percent was used for share repurchases

and dividends. With U.S. Department of Defense budgetary pressures expected to temper defense spending and thus quell organic avenues for revenue and earnings growth, many companies could look to use excess cash to make acquisitions as a means to grow. For this reason, we feel the current environment is conducive to additional acquisition activity and we anticipate deal flow to be strong for the remainder of the year.

### Stock Market Update

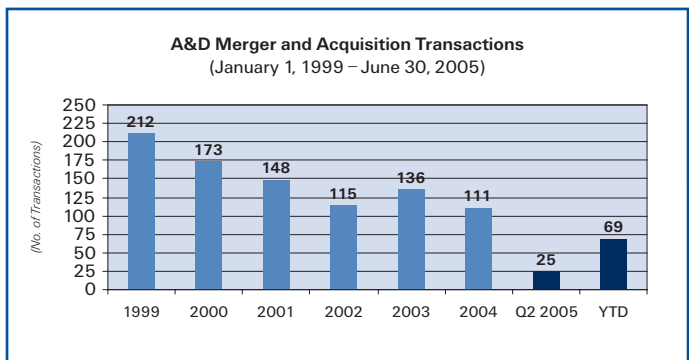
Market performance of U.S. aerospace and defense company stocks has been strong through the first six months of 2005, as the Dow Jones Aerospace and Defense Index is up 10 percent year to date through June.<sup>2</sup> This strength has been driven by positive market sentiment toward avionics, defense electronics, and airframe manufacturers.

<sup>2</sup> Bloomberg L.P. market data as of June 30, 2005

Historical Transaction Multiples (January 1, 1999 – June 30, 2005)					
Year	EV/ Sales	EV/ EBITDA	Year	EV/ Sales	EV/ EBITDA
YTD	2.55 x	11.92 x	2001	1.11 x	8.31 x
2004	1.86 x	12.26 x	2000	1.08 x	7.86 x
2003	1.76 x	11.11 x	1999	1.18 x	7.09 x
2002	0.90 x	10.67 x			

EV = Enterprise value.  
EBITDA = Earnings before interest, taxes, depreciation, and amortization.

Source: Thomson Financial, company filings YTD as of June 30, 2005



Source: Thomson Financial, company filings YTD as of June 30, 2005

### Select A&D Transactions from June 2005

- Nortel Networks Inc (NNI)**, the U.S. subsidiary of Nortel Networks Ltd, completed its acquisition of Virginia-based **PEC Solutions Inc**, a government IT services firm, and created U.S.-based Nortel PEC Solutions to provide mission-critical solutions for U.S. federal, state, and local government customers. NNI acquired PEC for an estimated US\$448 million (net of cash acquired) through a cash tender offer for all of the outstanding shares of PEC at US\$15.50 per share.
- PCA Aerospace Inc** acquired Fairchild Aerostructures Co. from Huntington Beach, CA-based **The Fairchild Corp**. The acquired business has been renamed PCA Aerostructures Co. Also making an equity investment in PCA Aerospace was private equity firm Vintage Capital Partners, L.P.
- Privately held **Advanced Products Corp** (APC) acquired a majority interest in privately held **Advanced Machine & Stretchform International Inc** (AMSI). Gardena, CA-based AMSI produces complex machined and formed aluminum and titanium structural components, such as wing panels, large fuselage sections, fuel tanks for space boosters, and helicopter hub and rotor assemblies. Terms of the deal were not disclosed.
- Esterline Corp** acquired Rancho Santa Margarita, CA-based **Palomar Products, Inc**. Palomar Products is a manufacturer of secure military communication products. Applications include airborne, shipboard, and land-vehicle solutions. Terms of the deal were not disclosed.

**Market Snapshot**  
(Closing Prices as of June 30, 2005)

Company Name	Stock Price	Market Cap (US\$ millions)	Debt to TC	Price to Earnings	Price to BV	EV to Sales	EV to EBITDA
<b>S&amp;P 500</b>							
Boeing Company	66.00	51,942.65	50.6%	30.58	4.53	1.15	18.36
General Dynamics Corp.	109.54	21,949.13	30.8%	17.02	2.97	1.23	10.36
Goodrich	40.96	4,937.45	57.5%	24.07	3.52	1.35	9.81
Honeywell International	36.63	31,246.47	34.7%	17.86	2.73	1.28	13.89
Lockheed Martin Corp.	64.87	28,801.64	40.8%	20.83	3.87	0.87	11.56
Northrop Grumman Corp.	55.25	19,861.47	24.9%	16.26	1.19	0.81	8.47
Raytheon Company	39.12	17,690.06	34.3%	21.79	1.66	1.12	11.71
Rockwell Collins	47.68	8,520.42	13.3%	23.83	6.54	2.67	14.11
United Technologies Corp.	51.35	52,564.24	23.7%	17.71	3.36	1.48	10.67
Group Median			34.3%	20.83	3.36	1.23	11.56
<b>Other Primes/Systems Suppliers</b>							
BAE Systems	5.14	15,735.96	33.5%	nmf	1.73	1.14	11.58
Bombardier Inc.	2.13	3,722.74	70.8%	22.81	1.58	0.47	7.93
EADS	31.87	25,198.67	22.6%	15.80	1.05	0.56	4.42
Embraer-Empresa Brasileira	6.16	4,433.29	37.2%	7.97	2.54	1.50	7.67
Finmeccanica SpA	0.93	7,883.18	47.7%	11.64	1.64	0.79	7.71
Thales SA	40.62	6,591.77	50.4%	34.13	2.69	0.66	9.25
Group Median			42.4%	15.80	1.68	0.73	7.82
<b>Avionics/Electronics</b>							
Alliant Techsystems	70.60	2,629.71	62.4%	17.02	3.83	1.34	10.17
DRS Technologies	51.28	1,408.79	52.1%	22.89	2.10	1.40	9.95
EDO Corp.	29.91	602.48	38.9%	21.56	2.79	1.21	9.78
Harris Corp.	31.21	4,166.54	22.3%	23.44	2.96	1.48	12.36
Herley Industries	18.24	260.41	2.9%	20.93	1.33	1.72	11.19
L-3 Communications Holdings	76.58	9,082.17	35.0%	20.68	2.23	1.51	12.05
CAE	5.37	1,328.70	52.5%	nmf	2.39	1.78	9.53
Group Median			38.9%	21.25	2.39	1.48	10.17
<b>Components (Large Cap—over US\$500 million)</b>							
Cobham Plc	25.35	2,829.68	34.4%	17.99	2.90	1.75	8.88
Curtiss Wright	53.95	1,166.09	41.6%	18.98	1.98	1.55	9.72
Esterline Technologies	40.08	1,008.18	29.2%	21.02	1.66	1.50	9.88
Meggitt Plc	5.07	2,176.65	44.5%	35.25	2.44	3.20	13.21
Moog Inc.	31.49	1,215.78	36.4%	20.54	2.37	1.46	10.46
Precision Castparts Corp.	77.90	5,153.23	32.1%	21.72	2.89	2.00	11.29
Rolls-Royce Plc	5.15	8,774.12	40.5%	24.15	1.99	0.95	9.32
Smiths Group Plc	16.47	9,240.26	38.7%	22.61	4.22	1.97	12.28
Textron Inc.	75.85	10,228.98	65.3%	20.06	2.81	1.55	13.49
Zodiac SA	53.69	2,886.38	52.0%	24.01	3.62	1.94	11.92
Group Median			39.6%	21.37	2.63	1.65	10.88
<b>Components (Mid-Cap—US\$100 – \$500 million)</b>							
Ducommun Inc.	16.91	170.06	0.3%	13.60	1.09	0.73	7.24
Heroux-Devtek	3.38	91.13	40.0%	nmf	0.86	0.82	12.10
Magellan Aerospace Corp.	2.55	231.44	41.7%	nmf	0.93	0.89	13.70
Triumph Group	34.76	552.82	23.1%	21.68	1.05	1.03	11.03
Group Median			31.5%	17.64	0.99	0.86	11.57
<b>MRO/Aftermarket Services</b>							
AAR Corp.	15.71	506.82	42.6%	38.05	1.61	0.98	12.32
Aviall Inc.	31.59	1,121.70	45.5%	24.02	3.04	1.21	14.12
HEICO Corp.	23.41	572.54	8.1%	30.41	1.86	2.67	14.36
Group Median			42.6%	30.41	1.86	1.21	14.12

Market capitalization is calculated as the number of outstanding shares multiplied by the current stock price.

TC = Total book capital.

BV = Book value of equity.

EV = Enterprise value.

EBITDA = Earnings before interest, taxes, depreciation, and amortization.

nmf = Not meaningful figure.

Note: Companies included in the above analysis derive at least 50 percent of revenue from aerospace- and defense-related products or services.

## KPMG Corporate Finance

KPMG Corporate Finance LLC provides a full suite of investment banking and strategic advisory services to its domestic and international clients. Our professionals have the experience and depth of knowledge in global M&A to advise clients on mergers and acquisitions, sales and divestitures, buyouts, financings, restructurings, fairness opinions, and other strategic initiatives. In addition, we remain independent of financing sources, helping to ensure that our efforts are objective and aligned with the goals of our firms' clients. Operating in 51 countries, KPMG's Corporate Finance practice comprises more than 1,500 professionals who are able to meet the needs of KPMG's firms' clients across the globe. In 2004, KPMG's Corporate Finance practice was ranked the number one financial adviser for completing the highest number of transactions globally (361 deals totaling US\$18.9 billion), according to Thomson Financial's global M&A league tables.

## Aerospace and Defense Experience

KPMG Corporate Finance LLC is well positioned to assist middle market aerospace and defense companies in assessing and developing a plan to implement the relevant strategic alternatives for their businesses. Whether this includes making acquisitions, divesting noncore operations, or an outright sale of the business, KPMG Corporate Finance's Aerospace & Defense team can assist you.

## KPMG Corporate Finance Is a Leading Financial Adviser Globally

2005 through June 30	No. of deals	2004	No. of deals
1. <b>KPMG Corporate Finance</b>	144	1. <b>KPMG Corporate Finance</b>	361
2. JP Morgan	139	2. JP Morgan	324
3. Citigroup	136	3. Citigroup	308
3. Goldman Sachs	136	4. Goldman Sachs	290
5. Morgan Stanley	131	5. Morgan Stanley	277
6. UBS	125	6. UBS	248
7. Rothschild	97	7. Credit Suisse First Boston	242
7. Merrill Lynch	97	8. Rothschild	226
9. PricewaterhouseCoopers	95	9. Merrill Lynch	201
10. Credit Suisse First Boston	94	10. Ernst & Young	192

2003	No. of deals	2002	No. of deals
1. <b>KPMG Corporate Finance</b>	368	1. CSFB/DLJ	344
2. Salomon Smith Barney/Citigroup	268	2. <b>KPMG Corporate Finance</b>	320
2. Goldman Sachs	268	3. Salomon Smith Barney/Citigroup	312
4. Credit Suisse First Boston	257	4. JP Morgan/Chase	290
5. JP Morgan	234	5. Morgan Stanley DW	268
6. Morgan Stanley	229	6. Goldman Sachs	252
7. UBS	226	7. Merrill Lynch	201
8. Rothschild	185	8. PricewaterhouseCoopers	199
9. Deutsche Bank	184	9. Deutsche Bank	190
10. PricewaterhouseCoopers	182	10. UBS Warburg	188

Source: Thomson Financial Securities Corporation. Each set of figures is taken from the league table press releases issued for that year.

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

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