



Aerospace/Defense & Government Services 2018 M&A Survey



KippsDeSanto is pleased to share its first annual survey of mergers and acquisition (M&A) activity and sentiment in the Aerospace/Defense and Government Services sectors.

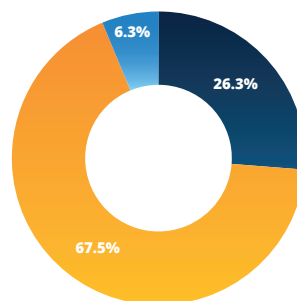
In this study, we asked key dealmakers from relevant sectors to share their predictions about M&A deal activity and valuations over the next year. We also asked them to share their insights on strategic drivers of M&A activity and the impact of recent events, including 2017's tax law changes and the Trump administration.

Respondents are very optimistic about the overall economy and M&A activity in the near- to medium-term. They expect activity levels and valuations to increase in 2018 due in part to the December 2017 tax law changes and greater budget visibility.

Overall, 168 dealmakers who are interested in the Aerospace/Defense and Government Services sectors participated in the survey. This includes 103 CEOs, Presidents, CFOs and Corporate Development executives from corporate/strategic buyers, and 65 partners and senior professionals from private equity groups. Nearly 50% of the strategic buyer participants represent public companies — including most of the largest and most active industry buyers, with more than half of respondents coming from strategic buyers with more than \$500 million in annual revenue. Approximately 90% of the participants are based in the U.S.

Dealmakers Predict Economic Growth in 2018

Respondents have very positive predictions for the U.S. economy, with 94% expecting moderate to strong economic growth in 2018. No respondents expect economic contraction, and just 6% expect the economy to remain flat.



Expectations for the U.S. Economy in 2018

- Strong economic growth
- Moderate economic growth
- Flat/no economic growth
- Moderate economic contraction
- Strong economic contraction/recession

IN RESPONSE TO: Which of the following best describes your expectation for U.S. economic growth in 2018?



"We have witnessed strong M&A activity in the Aerospace/Defense and Government Services sectors over the past four years, totaling over 300 transactions annually during this period. We have a unique position to understand the dynamics driving this volume of activity, but wanted to present the market with a broader view of the underlying factors that drive the decision-making of dealmakers in these sectors. KippsDeSanto is proud to provide this survey report with insight into the drivers of the continued momentum of M&A activity in Aerospace/Defense and Government Services sectors in 2018."

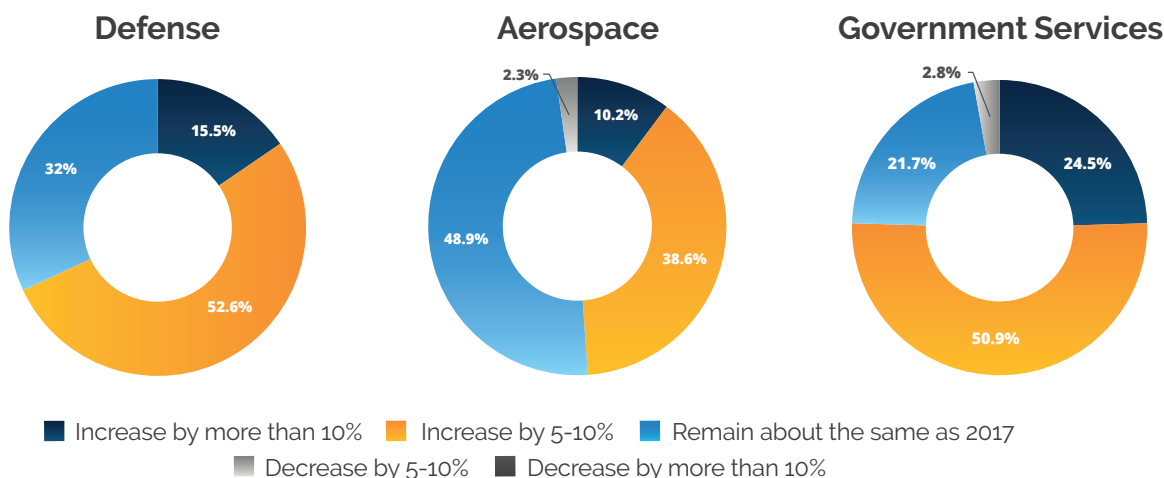
– BOB KIPPS, CO-FOUNDER AND MANAGING DIRECTOR, KIPPSDESANTO & CO.

M&A Activity Expected to Increase in Aerospace, Defense and Govt. Services

As expected, respondents also have positive expectations for M&A activity in the Aerospace, Defense and Government Services sectors in 2018. Predictions are most positive for the Government Services sector, where 75% of respondents expect the number of deals to increase by 5% or more, and 25% of respondents believe the number of deals will increase by more than 10%. This expected increase continues a growth trend in Government Services deals, which led to 102 deals announced in 2017 up from 88 in 2016.

Similarly, over two thirds of respondents (68%) think defense sector deals will be up by 5% or more in 2018, predicting an uptick in deals compared to two flat to down years since 2016. Dealmakers we surveyed also expect activity in the Aerospace sector may be stabilizing or increasing in 2018 after three consecutive years of reduced activity levels. Specifically, survey respondents predict that Aerospace deals will increase by 5% or more (49% of respondents) or will remain the same (49%).

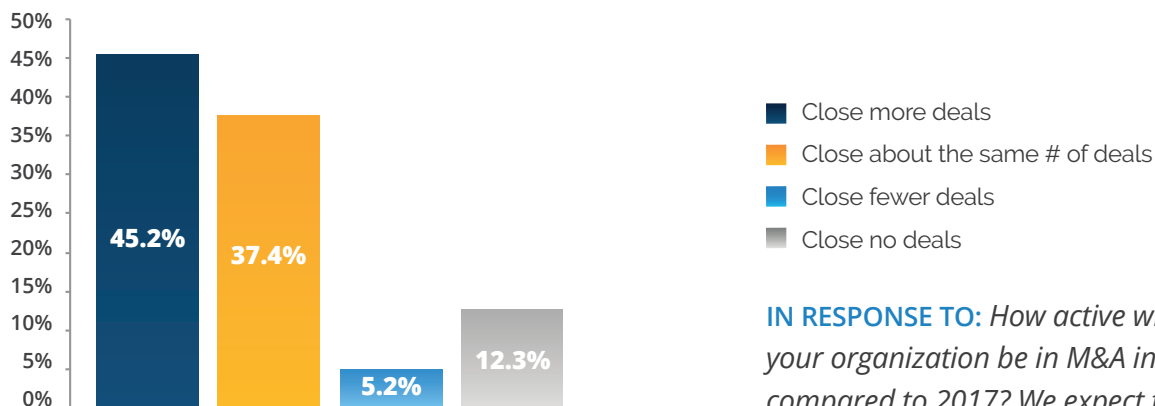
Sector Deals



IN RESPONSE TO: *In your opinion, how will overall M&A activity in 2018 compare to 2017 in each sector? The number of deals closed in 2018 will...*

Across all sectors, nearly 50% of dealmakers we surveyed expect their own organizations to close more deals in 2018 than in 2017, while only 17% expect to close fewer deals or no deals in 2018. Thirty-eight percent of respondents expect to close the same number of deals.

M&A Deals at Dealmaker's Own Organization

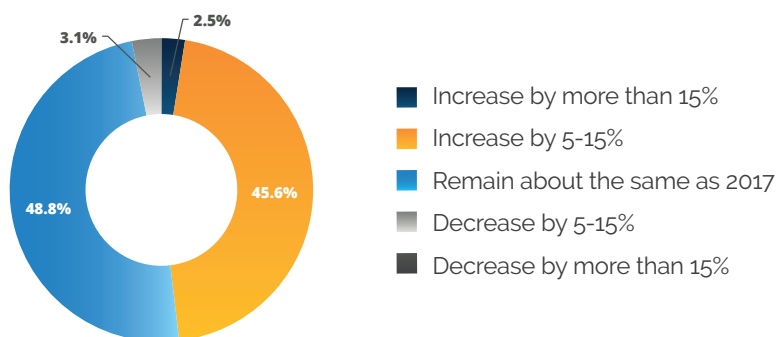


IN RESPONSE TO: *How active will your organization be in M&A in 2018 compared to 2017? We expect to...*

Valuations Predicted to be Positive to Neutral

The dealmakers we surveyed are neutral to positive about valuations in 2018. Respondents are nearly evenly split with 46% expecting valuations to be up 5-15% from 2017, and 49% expecting valuations to remain the same as 2017. Only 6% expect valuations to decline in 2018 compared to 2017.

Valuation Predictions



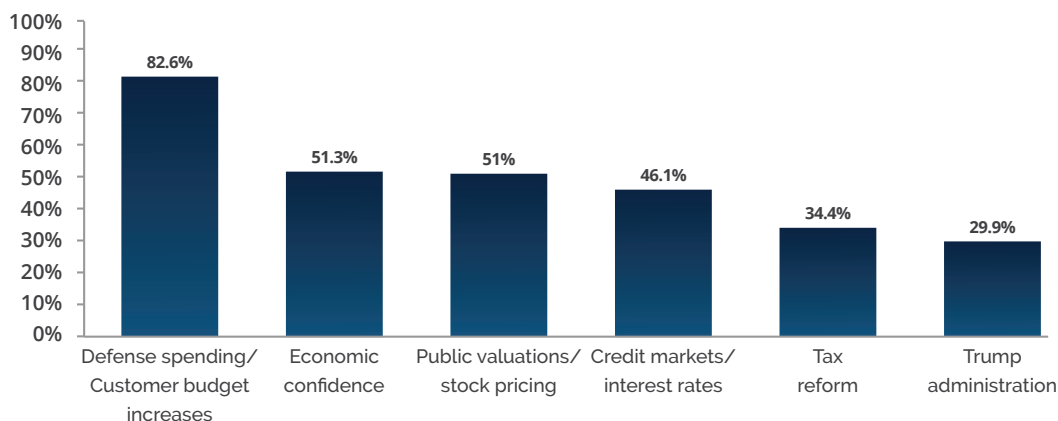
IN RESPONSE TO: *In your opinion, how will the overall valuations of U.S. based M&A targets in 2018 compare to 2017? In 2018, valuations will likely...*

Drivers of M&A Momentum

Dealmakers we surveyed note that defense spending plays a critical role in driving the number of M&A deals and their valuations. Not surprisingly, defense spending is by far the most influential factor, with 83% of respondents saying it is extremely or very influential to M&A activity and valuations. Public valuations/stock pricing, economic confidence, and credit markets/interest rates are also important factors in deal activity and valuations with between 46-51% of respondents saying they are extremely or very influential. Approximately 35% of respondents say the 2017 tax reform and 30% say the Trump administration are extremely or very influential. The Trump administration is slightly more influential for dealmakers interested in the Aerospace sector.

Drivers of M&A Momentum

(% saying factor is extremely or very influential)

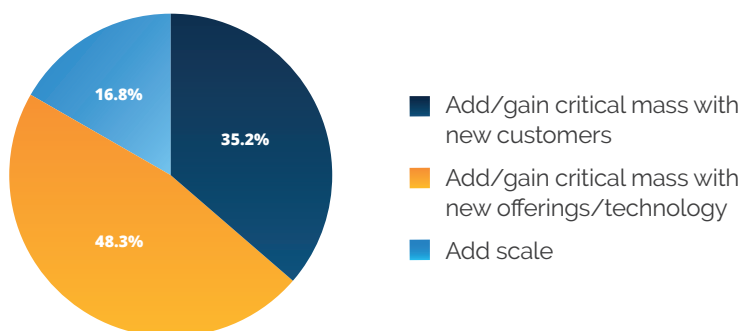


IN RESPONSE TO: *Rate the following factors based on how much influence they have on overall deal activity and target valuations in the U.S.*

Main Buyer Goals of M&A

As expected, when asked about the primary goals that drive their M&A strategy, 48% of dealmakers say adding new capabilities, products or technologies is their first priority. This is followed by adding new customers, which is the top priority for 35%. Just 17% of respondents say adding scale is their first priority in selecting M&A deals.

M&A Strategy Goals - First Priority

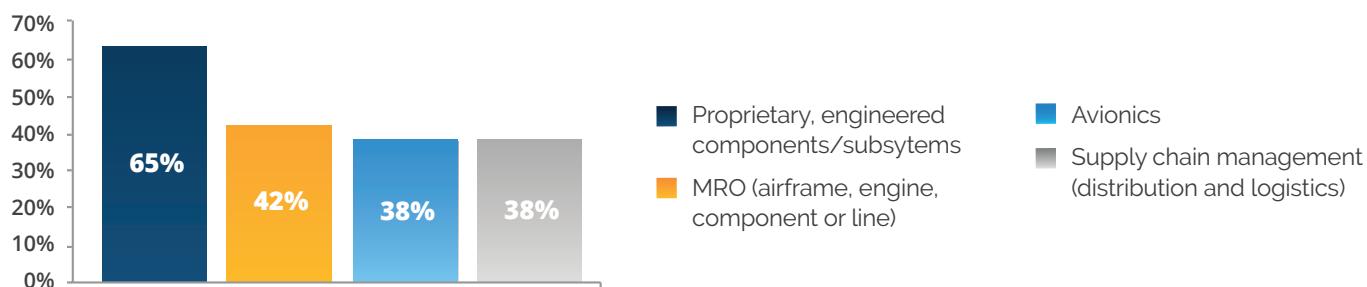


IN RESPONSE TO: Please rank how important the following goals are in your organization's M&A strategy.

Top M&A Interest Areas by Industry Sector

We also asked dealmakers which capabilities or target areas are their top priorities for M&A activity.

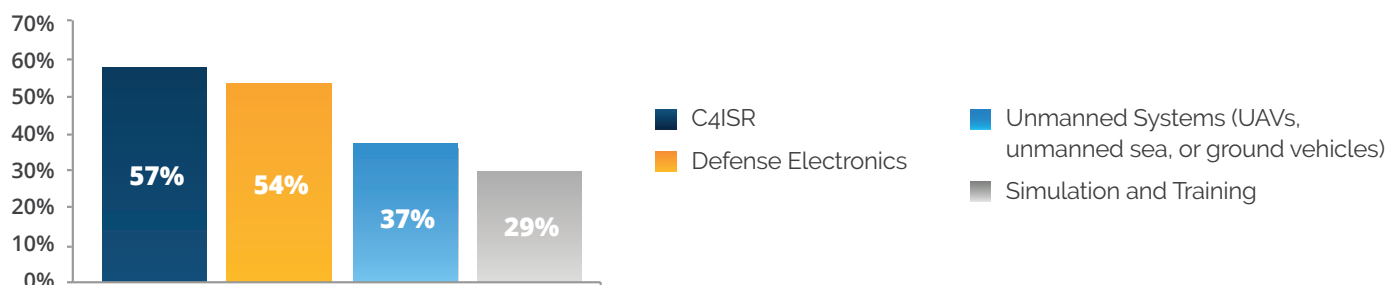
Aerospace Priority Interest Areas (% chosen as a priority area)



In the Aerospace sector, 65% of respondents say Engineered Components/Subsystems is one of their top focus areas for M&A.

IN RESPONSE TO: Based on the following list, choose and rank which M&A target areas are the top three priorities for your organization in the Aerospace sector over the next 12-24 months. You may only choose and rank three target areas.

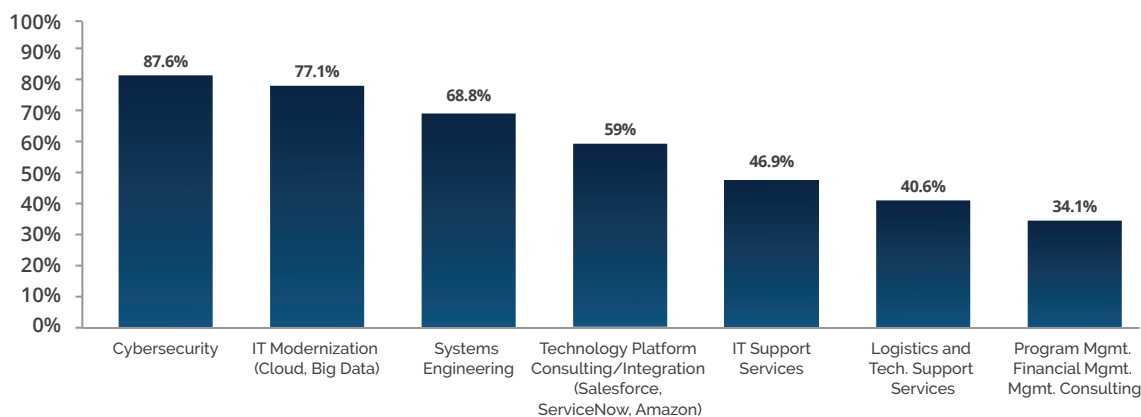
Defense – Priority Interest Areas (% chosen as a priority area)



In the defense sector, 57% of respondents say C4ISR is a top focus area, followed by 54% who say Defense Electronics is a top focus area.

IN RESPONSE TO: Based on the following list, choose and rank which M&A target areas are the top three priorities for your organization in the Defense Technology and Products sector over the next 12-24 months. You may only choose and rank three target areas.

Government Services – Priority Interest Areas (% chosen as a priority area)



In the Government Services sector, 88% of respondents say Cybersecurity is a priority area for M&A, while 77% say IT Modernization is a priority area.

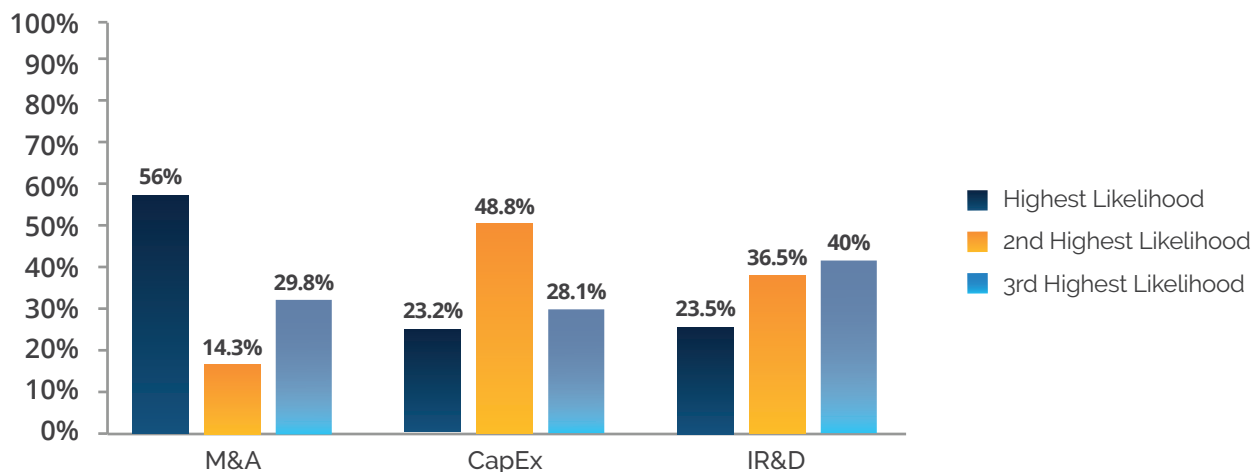
IN RESPONSE TO: Rate the following capabilities based on their importance for your organization's M&A strategy in the Government Technology and Professional Services sector over the next 12-24 months. Rate each area as highest priority, middle priority, lowest priority or no interest.

2017 Tax Law Expected to Have Positive Impacts on M&A Activity

The 2017 tax reform bill was intended to reduce corporate taxes and free up cash flow for other investments. Our survey suggests it will also impact M&A deal activity and possibly valuations. Fifty-six percent of respondents say M&A activity is the area within their organization that is most

likely to receive increased funding as a result of the 2017 tax law changes. This is double the percentage of respondents who believe that either CapEx (23%) or IR&D (23%) is most likely to receive additional funding.

Internal Funding Reallocations Based on Tax Law Changes

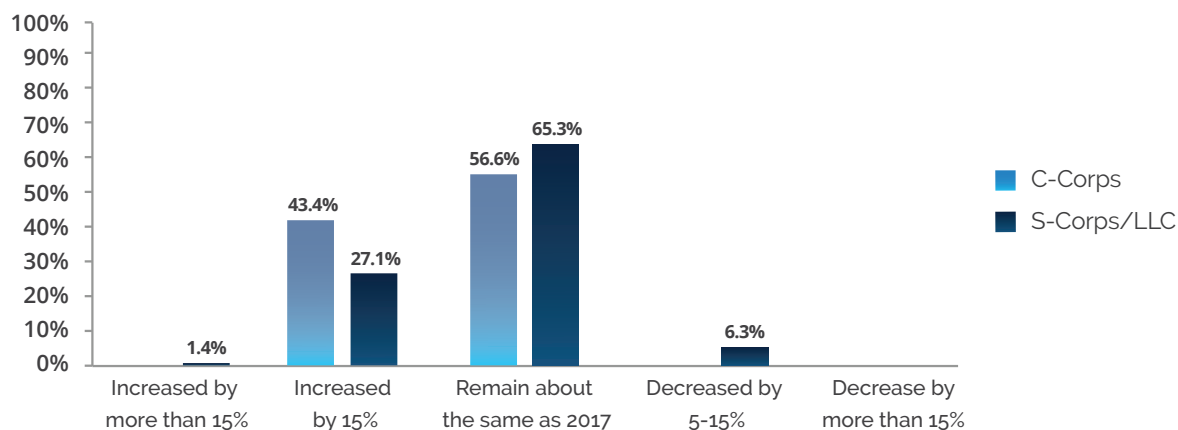


IN RESPONSE TO: Rank the following areas based on the likelihood your organization will increase funding allocations to that area as a result of the new U.S. tax law.

Tax Law Changes Likely to Help C-Corp Valuations More Than Pass-Thru Entities

According to the dealmakers we surveyed, the 2017 tax law changes will have a positive or neutral to positive impact on C-Corp values, with 43% predicting it will drive C-Corp values up 15% and no respondents predicting C-Corp values will decrease due to the new tax law. Nearly two-thirds of respondents (65%) believe S-Corp and LLC values will remain the same, but 27% of dealmakers surveyed believe that values for these business types will increase by 15%.

Tax Law Impacts on C-Corp vs. S-Corp/LLC Values

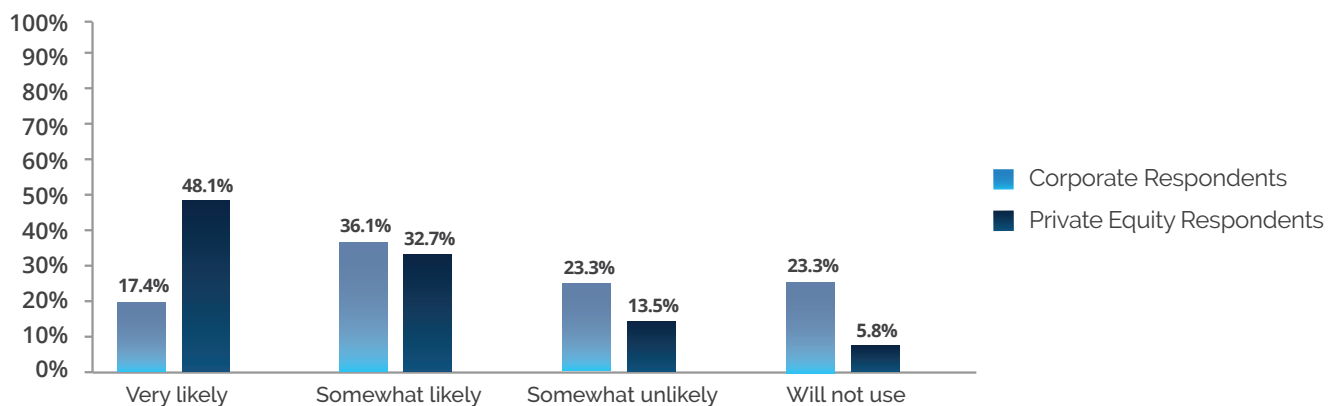


IN RESPONSE TO: How will the recently passed U.S. federal tax law affect your valuation of potential U.S. C-Corporation and S-Corporation/LLC targets? Valuations will...

Use of RWI Continues to Gain Broader Adoption

We also asked dealmakers a range of questions about their deal-making processes and preferences. As expected, private equity groups continue to use Representations and Warranties Insurance (RWI) more than strategic buyers. Over 80% of private equity respondents say they are somewhat likely to use RWI compared with just 53% of corporate respondents.

Use of Representations and Warranties Insurance Corporate vs. Private Equity Respondents



IN RESPONSE TO: *How likely are you to use Representations and Warranties Insurance in 2018?*

Select Recent KippsDeSanto & Co. Advised Transactions

<p>Pending</p>  <p>has agreed to be acquired by</p> 	<p>May 2018</p>  <p>has been acquired by</p> 	<p>April 2018</p> <p>STRATEGIC RESOURCES INTERNATIONAL</p> <p>has been acquired by</p>  <p>a portfolio company of</p> 	<p>February 2018</p>  <p>has been acquired by</p> 	<p>January 2018</p>  <p>a portfolio company of</p> <p>CM EQUITY PARTNERS</p> <p>has been acquired by</p> 
<p>January 2018</p>  <p>has been acquired by</p> 	<p>January 2018</p>  <p>has been acquired by</p> 	<p>November 2017</p>  <p>has been acquired by</p>  <p>supported by</p> <p>CLAIRVEST</p>	<p>October 2017</p>  <p>a portfolio company of</p>  <p>has been acquired by</p> 	<p>October 2017</p>  <p>has merged with</p> 
<p>September 2017</p>  <p>has been acquired by</p> 	<p>July 2017</p>  <p>has been acquired by</p> 	<p>April 2017</p> <p>BEI PRECISION SYSTEMS & SPACE COMPANY</p> <p>a subsidiary of</p>  <p>a portfolio company of</p> <p>THE CARLYLE GROUP</p> <p>PAI and Schneider Electric</p> <p>has been acquired by</p> <p>J.F. Lehman & Company</p>	<p>April 2017</p>  <p>has been acquired by</p> 	<p>February 2017</p>  <p>a portfolio company of</p> <p>DFW CAPITAL PARTNERS</p> <p>has been acquired by</p>  <p>a portfolio company of</p> <p>BRIDGE GROWTH PARTNERS & Fronkenac</p>
<p>January 2017</p>  <p>has been acquired by</p>  <p>a portfolio company of</p> 	<p>December 2016</p>  <p>has been acquired by</p> 	<p>December 2016</p>  <p>has been acquired by</p> 	<p>December 2016</p>  <p>has been acquired by</p> 	<p>December 2016</p>  <p>has been acquired by</p> 

About KippsDeSanto & Co.

KippsDeSanto is an investment banking firm focused on delivering M&A and financing expertise. Our solutions are focused on the sectors we know — aerospace/defense and government technology solutions. We are recognized for our depth of industry experience, knowledge of sector-specific transaction drivers, and long-standing relationships with industry participants.

We welcome the opportunity to have a more detailed discussion of developments in our focus industries.

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