Survey

LONGBOW Research
Tactical advantage through independent research

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Industry: **INDUSTRIAL**
Sub-Sector: **AEROSPACE SUPPLY**

Aerospace Supplier Health Report

Notable Industry Trends and Data Points for 2Q19

Key Takeaways

- **Longbow's Call:** The data points and channel feedback collected from a quarterly survey of aerospace suppliers is pointing to a healthy double-digit sales growth environment and generally upbeat expectations for the rest of 2019. We maintain a high level of confidence that suppliers within our coverage group can meet/beat versus 2Q expectations. Within an undercurrent of bullishness, we are starting to lose visibility into the 737Max supply chain, with 15% of suppliers now expressing some doubt about near-term order sustainability. Ahead of next week's Paris Air Show, we highlighted the four main talking points picked up from the channel over the past two weeks.

- **Main takeaways:** (1) The average sales comp calculated for the entire aerospace channel was +11-12% y/y for 2Q19, which appears to be trending slightly above market expectations. Most of the companies in our coverage group are guiding to +HSD aero growth in 2019. The strength in the channel is more apparent for tier-4 suppliers, including the forging companies like Arconic (ARNC). (2) We are picking up a few "yellow flags" around the 737Max program. While it is not a universal view, some contacts offered relatively cautious Boeing-related commentary, including early evidence of customer order push-back and/or changes to procurement strategies. Safran was mentioned as sending our contacts negative pulses. At the same time, other key suppliers like GE are generally seen as holding near full production capacity with no planned changes to production. (3) A greater number of suppliers are talking about "pricing power" or optimism about future contracts. (4) The M&A discussion picked up considerably over the past few weeks. OEMs are starting to look at backward integration in order to better control supply.
- **OEM Index:** Contacts reported the largest sequential increase in new orders for Norfolk Grumman (NOC), Spirit Aero (SPR) and GE. Negative momentum was seen by suppliers of Bombardier, Safran, and Rolls-Royce (see pages 9-10).
- Boeing lowered the monthly delivery target on the 737 platform to 42/month (down 10). When asked, our contacts said they were running internal operations to reflect a 47-48 run-rate. The "risk" to models could revolve around lower probability the rate will move to 57/month in 2H. Hexcel (HXL) first discussed this risk last month and addressed contingency plans. Comparatively, suppliers said they were running near 56-57/month for the A320.

Investment Thesis

- We plan to revisit our demand and sales assumptions upon returning from France. However, we do not expect to make any large modeling revisions. We believe any perceived BA risks, as it relates to our coverage group, could be offset by new contract awards like the GE9x or favorable Airbus outlook.

Model Implications

- Our models are driven by 1,947 est. comm. aircraft deliveries in 2019 (+10%).

IMPORTANT DISCLOSURES ARE LOCATED IN THE APPENDIX.