

AP CAPITAL RESEARCH

# M&A Deal of The Week

## Boeing & Spirit Aerosystems



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# Executive Summary

## M&A DEAL OF THE WEEK

### Deal Summary

- On the 1st of July 2024, Boeing formally agreed to acquire Spirit AeroSystems under a definitive deal announced today. This merger has been structured as an all-stock transaction, with an equity value of approximately \$4.7 billion, or \$37.25 per Spirit AeroSystems share. Including Spirit's most recent reported net debt, the transaction value represents an enterprise value of \$8.3 billion. The reported press release did not quantify any synergetic benefits.
- Under the terms of the agreement, each of Spirit's common stock will be exchanged for several shares of Boeing's common stock equal to an exchange ratio between 0.18 and 0.25, with this dependant upon the price of Boeing's stock upon deal close. The price of \$37.25 to Spirit's closing stock price of \$28.60 represents a premium of 30%
- The agreement includes acquiring substantially all of Spirit's Boeing-related commercial operations in Wichita, Kansas, Tulsa, Oklahoma, and Dallas, Texas, as well as other commercial, defence, and aftermarket operations.
- The reintegration is expected to leverage and build on Boeing's capabilities, support supply chain stability, and integrate critical manufacturing and engineering workforces to unify Boeing's safety and quality management systems.
- Boeing believes the acquisition will position the company in a much stronger position entering 2025 by ensuring the BCA factories can ramp production in a stable fashion
- Morgan Stanley & Co. LLC is serving as lead financial advisor to Spirit, and Moelis & Company LLC is also advising. Skadden, Arps, Slate, Meagher & Flom LLP is serving as Spirit's legal counsel.
- PJT Partners is serving as lead financial advisor to Boeing, with Goldman Sachs & Co, LLC and Consello serving as additional advisors. Sullivan & Cromwell LLP is acting as outside counsel to Boeing.

### Key Figures

- |                                 |                                  |
|---------------------------------|----------------------------------|
| • Deal Premium: 30%             | • Closing date: Q2 2025          |
| • Boeing P/E: -30.2x            | • Spirit P/E: -3.3x              |
| • Boeing P/B: -5.76             | • Spirit P/B: -2.59              |
| • Boeing D/E: -320%             | • Spirit D/E: -274%              |
| • Boeing EV: \$149.4 billion    | • Spirit EV: \$7.88 billion      |
| • Boeing EV/EBITDA: 113.0x      | • Spirit EV/EBITDA: -14.9x       |
| • Boeing EV/Sales: 1.98x        | • Spirit EV/Sales: 1.21x         |
| • Boeing Market Cap: \$100.58B  | • Spirit Market Cap: \$3.94B     |
| • Boeing Revenue 3Y CAGR: 6.06% | • Spirit Revenue 3Y CAGR: 21.59% |

# Company Information

## M&A DEAL OF THE WEEK

### **Boeing(NYSE: BA)**

- First founded in 1916, Boeing is an aerospace company that designs and manufactures commercial aeroplanes, defence products, and space systems. Boeing is primarily focused in North America, where a significant portion of its operations and revenue are concentrated, with additional global operations supporting its international customer base.
- Boeing's business activities can be broken into 3 segments: Commercial aeroplanes, Defence, space & security and Global services with the main driver of revenues being its Commercial aeroplanes segment which in 2023 accounted for 45% of revenue, followed closely by its Defence, space & security segment and its Global services segment which accounted for 32% and 23% respectively.
- Regarding financials, Boeing in recent years has underperformed when looking at earnings and revenue growth with revenue peaking in 2018 at \$101 billion and a net income of \$10.5 billion. Boeing's performance in 2023 failed to meet expectations, bringing in a revenue of only \$78 billion, up 16% YOY from 2022's \$67 billion. Net income for 2023 came in at -\$2.2 billion, which was down from 2022's \$4.9 billion loss, however. This fall in profitability is due to an increase in non-operating expenses which from 2020 have totalled over \$14.7 billion, eroding Boeing's profitability.

### **Spirit AeroSystems (NYSE: SPR)**

- First founded in 2005 as a spin-off from Boeing, Spirit AeroSystems "Spirit" is a leading manufacturer of aerostructures for commercial and defence aircraft. Spirit AeroSystems is primarily focused in North America, where it produces a significant portion of the fuselage, propulsion systems, and wing components for major aerospace companies, including Boeing.
- Spirit's business can be segmented into 3 segments: Commercial, Space & defence and aftermarket services with the main driver of revenues being its Commercial segment which in 2023 accounted for 45% of revenue, followed closely by its Defence, space & security segment and its Global services segment which accounted for 32% and 23% respectively. Spirit's commercial segment was the lead driver accounting for 80% of total revenues. Space & defence and Aftermarket services made up for the remaining 13% and 7%. Their main clients are Boeing and Airbus, who account for 64% and 19% of total revenue.
- In terms of financial performance, 2023 led to revenues of \$6.05 billion, up 20% from 2022's \$5.03 billion. Net income came in for 2023 at -\$616 million, an increase of 13% from 2022's loss of \$545 million. Revenue for Spirit peaked in 2019 at \$7.86 billion, then fell to \$3.4 billion due to the lack of aerosystem-related demand caused by the Covid-19 pandemic.



# Deal Rationale and Risk

## M&A DEAL OF THE WEEK

### **Regulatory Pressure and Credit Rating Upside**

#### **Regulatory Pressure**

Pressure from US regulators and concerns about quality controls have incentivised the aviation giant, Boeing, to enter into a definitive merger agreement with Spirit AeroSystems. Spirit AeroSystems manufactures fuselage and wing parts for Boeing and its key competitor Airbus. Since the spinoff unit in Wichita, namely Spirit AeroSystems, has significantly shifted its focus towards cost-cutting strategies rather than engineering excellence, the FAA has tightened its inspection protocols. Thus, through this transaction, Boeing seeks to improve safety in its production processes following several fatal crashes involving the infamous 737 MAX. The deal marks a shift away from Boeing outsourcing most of its aircraft manufacturing and bringing Spirit back in-house in an attempt to rectify supply chain disruptions.

#### **Credit Rating Upside**

More importantly, the all-stock deal structure allows Boeing to withstand a credit downgrade and participate in the bond market in case of future funding requirements. The acquisition is subject to Spirit's \$559M divestiture of Airbus businesses, most notably the manufacturing plants in Northern Ireland, which aim to remove loss-making components and provide Boeing with exclusive fuselage production. An assured reshuffle across the management board at Boeing can further recapture shareholder trust and enable both net profit margin (currently -3%) and safety improvements.

### **Risk**

#### **Prosecution risk**

The potential of Boeing being found guilty after violating a deferred prosecution agreement in 2021, linked to fatal crashes, creates major uncertainty both within the company and the US Justice Department. The link between the US government and Boeing is complex, yet vulnerable, particularly as a criminal conviction could disqualify the aviation giant from future government defence contracts. The lack of substitutes, workplace violations, and tarnished reputation generate additional challenges across the commercial aviation industry.



# Industry Analysis

## M&A DEAL OF THE WEEK

### **The U.S. Aviation Industry**

The aerospace industry is undergoing significant growth and transformation, driven by post-pandemic recovery and rising air travel demand, which has surpassed pre-pandemic levels. Total revenues in 2024 are expected to grow 7.6% year-over-year to a record \$964 billion, underscoring this upward trend. Forecasts predict nearly 44,000 new aircraft deliveries by 2043, with single-aisle planes making up 76% of the demand for short and medium-haul routes. A key focus is sustainability, with many new deliveries aimed at replacing older, less fuel-efficient models. Advancements in digital transformation and supply chain integration are enhancing production efficiency and resilience, led by major players like Boeing through strategic acquisitions and innovations.

Boeing's acquisition of Spirit AeroSystems could significantly impact the aerospace industry, driving further consolidation as competitors adopt similar strategies. By acquiring a major supplier, Boeing would gain greater control over production and supply chains, potentially improving efficiency and reducing costs. Spirit AeroSystems, known for advanced manufacturing technologies, generated \$5 billion in revenue in 2022. This acquisition is likely to bolster Boeing's market position, prompting competitors like Airbus to pursue similar moves and leading to more consolidation. Smaller suppliers might merge with larger companies or specialize to stay competitive, creating a more integrated but challenging aerospace landscape.

### **Key Threats in the Aviation Industry and Boeing's Strategic Position**

#### **Fuel**

- Volatility in fuel prices impacts airline operational costs and can lead to higher ticket prices, potentially reducing travel demand. Additionally, supply chain disruptions from geopolitical tensions, natural disasters, or pandemics can affect aircraft production and delivery, increasing costs and delays throughout the industry.

#### **Regulatory**

- Increasing regulatory pressures for environmental sustainability, such as the EU's Green Deal aiming for a 55% reduction in greenhouse gas emissions by 2030, are pushing aerospace manufacturers towards greener technologies. Competition from emerging markets with innovative solutions threatens established players by introducing advanced technologies and flexible business models.

#### **Boeing's Position**

- Boeing's acquisition of Spirit AeroSystems is strategically aimed at addressing these threats. By integrating Spirit AeroSystems, Boeing can enhance its supply chain and production efficiency, helping mitigate risks from supply chain disruptions and cost volatility. Spirit AeroSystems' expertise in advanced manufacturing and sustainable technologies supports Boeing's efforts to develop fuel-efficient aircraft, positioning it to better navigate regulatory pressures and competitive challenges.

WRITTEN BY

Adithya Praveen

# Final Thoughts

## M&A DEAL OF THE WEEK

### **Adithya Praveen.**

With the recent arrival of Ted Colbert as CEO, Boeing enters a new era focused on restoring quality and efficiency. Under Colbert's leadership, the aggressive cost-cutting measures and quality downgrades of the past are expected to give way to a renewed emphasis on improving standards. The acquisition of Spirit AeroSystems signals the beginning of this shift, aiming to address production delays and enhance overall quality, marking a promising step toward a more robust and dependable future for the company.

### **Thomas Kinnell.**

The mounting pressure from Boeing's European competitor, coupled with the fragmented reputation has severely stifled the possibility of Boeing undergoing a trend reversal to the upside. Focusing on operation optimisation and restoring public confidence rather than pursuing a grandiose transformation will have the effect of spurring the aviation giant to swifter margin expansions. Based on NASDAQ estimates, Boeing's share price is currently trading at a 25% discount, reflecting significant growth potential.

### **Genendra Gurung.**

The combination of Boeing and Spirit AeroSystems is poised to deliver significant benefits both in the short and long term. By acquiring crucial manufacturing capabilities, Boeing can improve the supply chain and quality, achieving cost savings through economies of scale and improved efficiency by integrating Spirit's production capabilities directly into its operations allowing it to compete more effectively in the global aerospace market.

### **Samuel Thompson.**

Boeing's acquisition of Spirit AeroSystems represents a good opportunity to consolidate market share and reposition Boeing back on the top of the US Aviation industry. This deal also represents an opportunity to improve Boeing's financial performance, with some synergies being realised, leading to Boeing not making any further operating losses as it has been since 2019.



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