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“Wall Street” Perspective

Presented to: **2019 Munitions Executive Summit**
Parsippany, NJ



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Topics to Discuss

Wall St. ... what is it and why should we care?

The Defense sector and munitions segment through Wall St's eyes

Quick look back to see if we can learn from past predictions

What should a supplier (and also DOD) take away from this?

Topics to Discuss

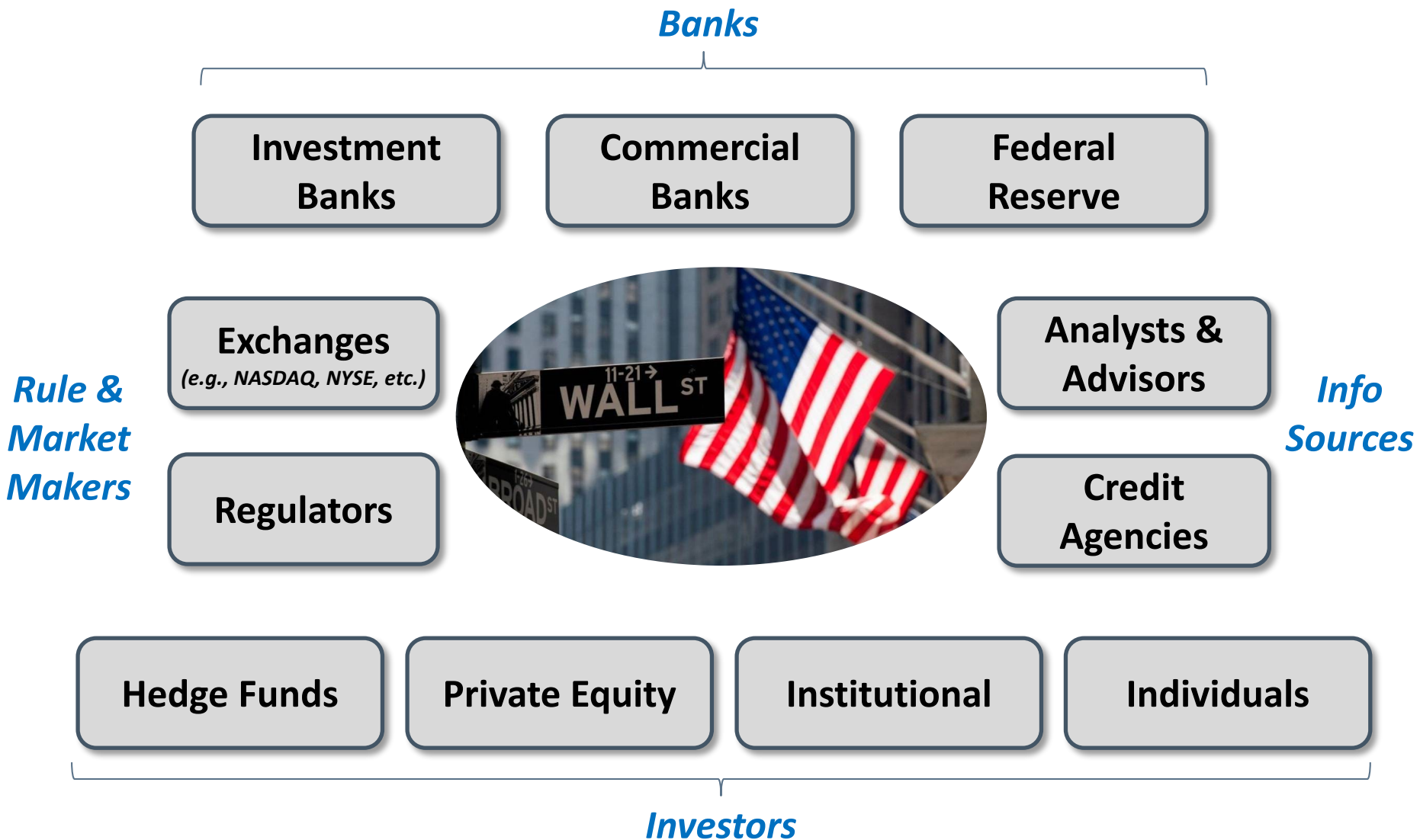
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“Wall St.” is many things, people and places in the US...



... but there are many Wall St.'s, all interconnected and trading trillions of \$\$ each day using AI and analytics

China: Shanghai Exchange



England: the "City"



Germany: Frankfurt BÖRSE

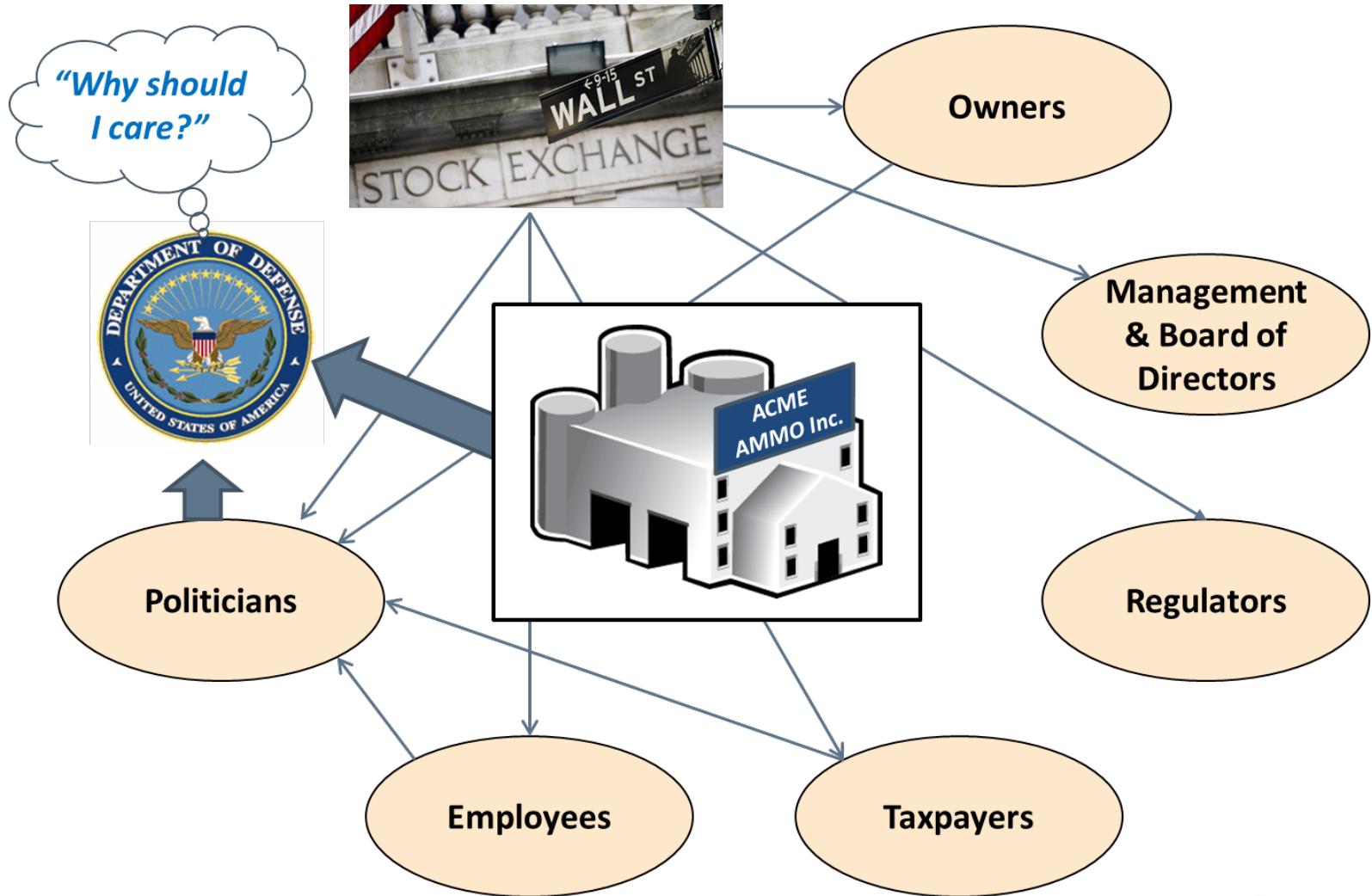


Japan: Tokyo



TOKYO
STOCK EXCHANGE

Wall St. is a key stakeholder in industry and DoD...



... that influences the Munitions sector every day

- **Directly...**

- **Provides capital** (e.g., working capital loans, equity, senior debt, bonds, etc.)
- **Creates incentives and reward system** (e.g., part of comp package, pension)
- **Sets price of capital** (e.g., share price, interest rate, covenants, etc.)
- **Shapes perception of a supplier's value** (e.g., buy/sell recommendations)
- **Change agent** (e.g., mechanism for owner exit/entry, activist shareholders, etc.)

- **Indirectly...**

- **Influences size of budgets**
- **Creates context to compare** (e.g., defense sector against other areas to invest)
- **Creates a “rule set”** (e.g., drives accountability among buyers and sellers)
- **... and many more**

Topics to Discuss

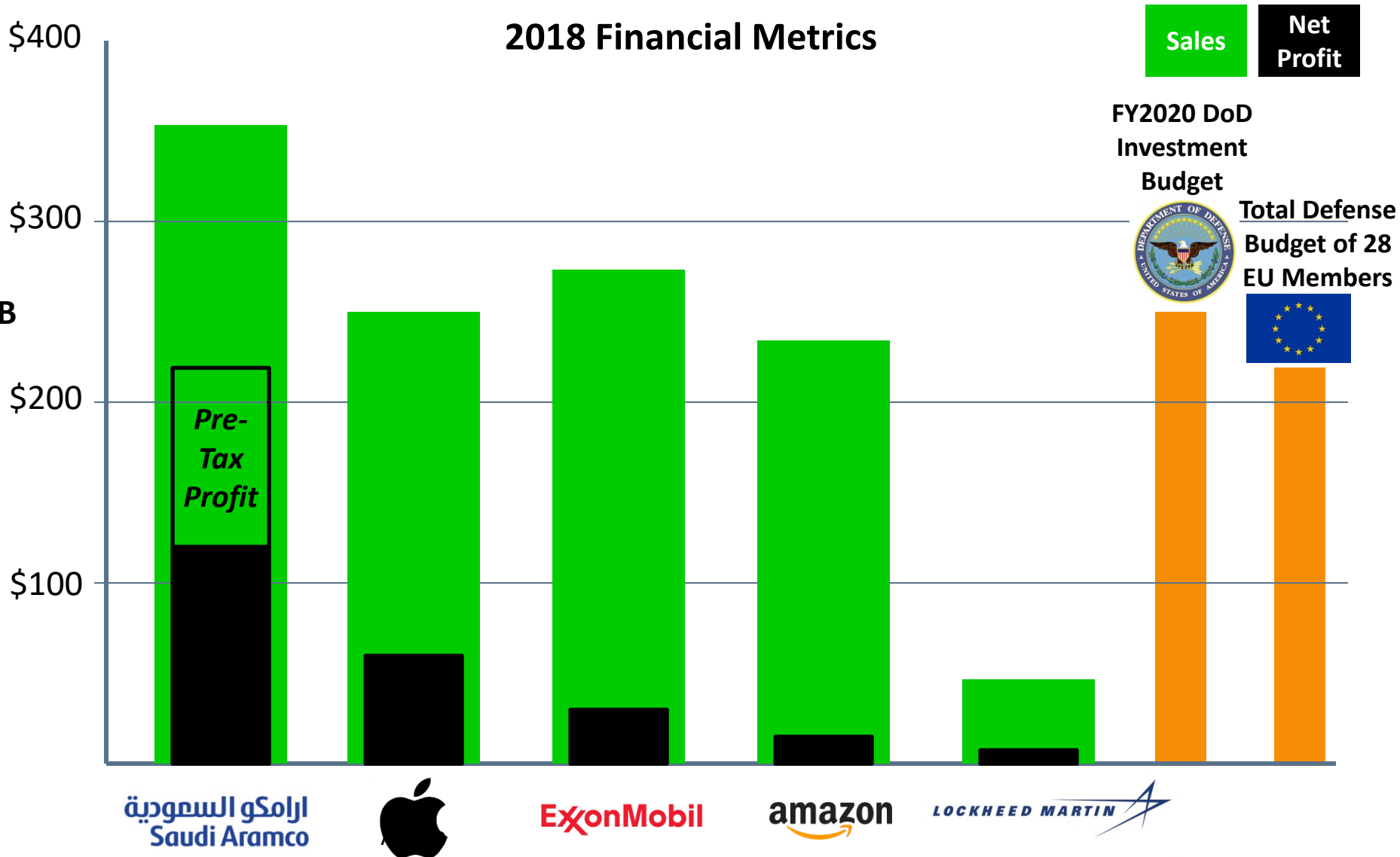
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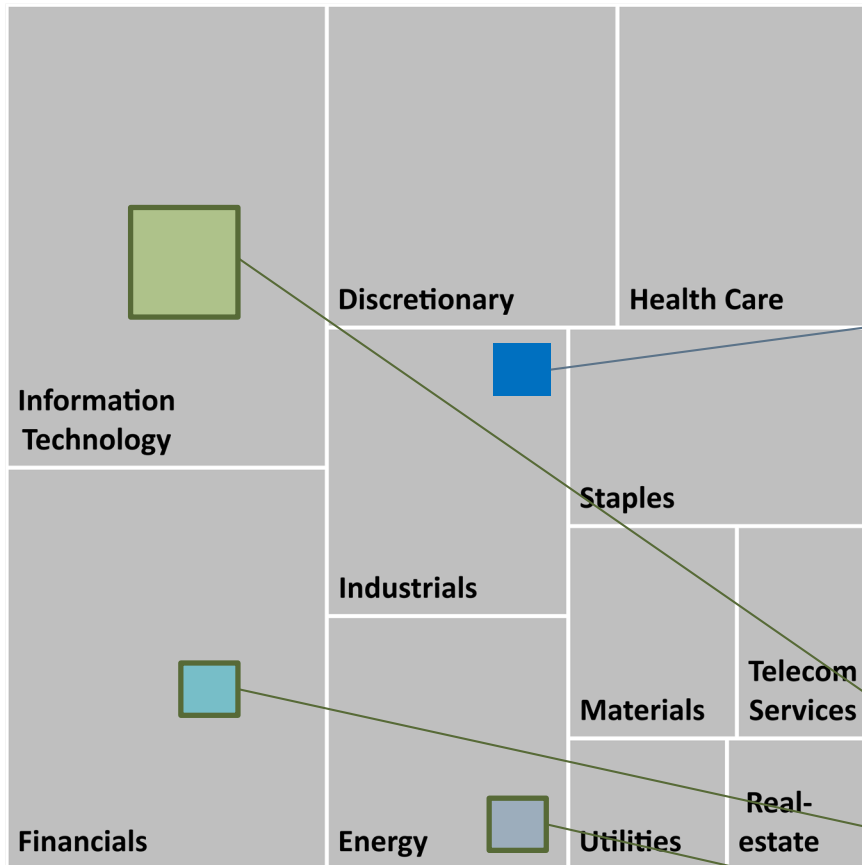
What should a supplier (and also DOD) take away from this?

First, "defense" is small scale by Wall St. standards

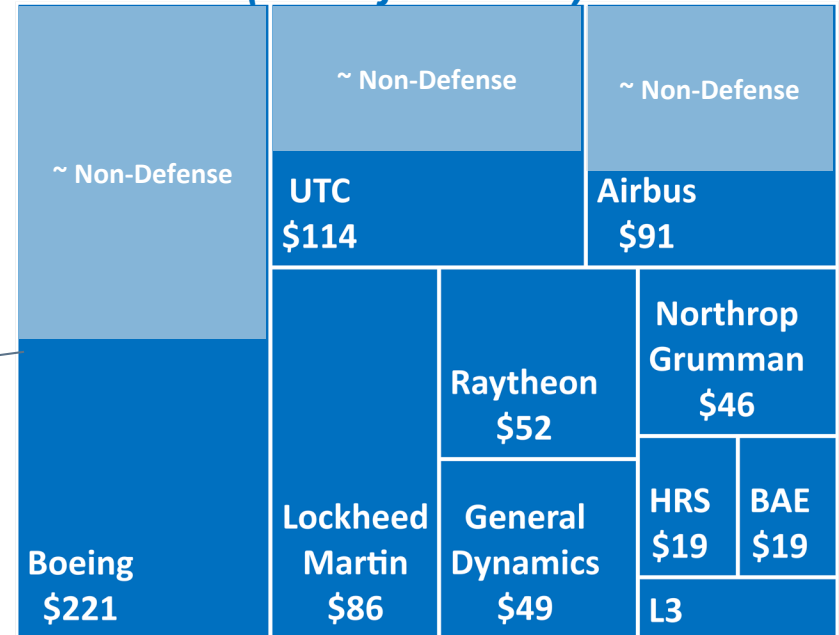


Second, defense companies don't move the market

S&P 500 Market Cap, ~\$25,000B



Defense Top 10 Market Cap, ~\$714B
(~3% of S&P 500)



Other notable firms across industries

Apple	\$915B
Microsoft	\$914B
JP Morgan	\$344B
Exxon Mobile	\$345B

Not: image not to scale; S&P 500 % allocation by industry is based on the index's industry average
Sources: S&P 500, RSAdvisors research and analysis

Third, most ordnance & munitions businesses don't move the needle for their own Companies

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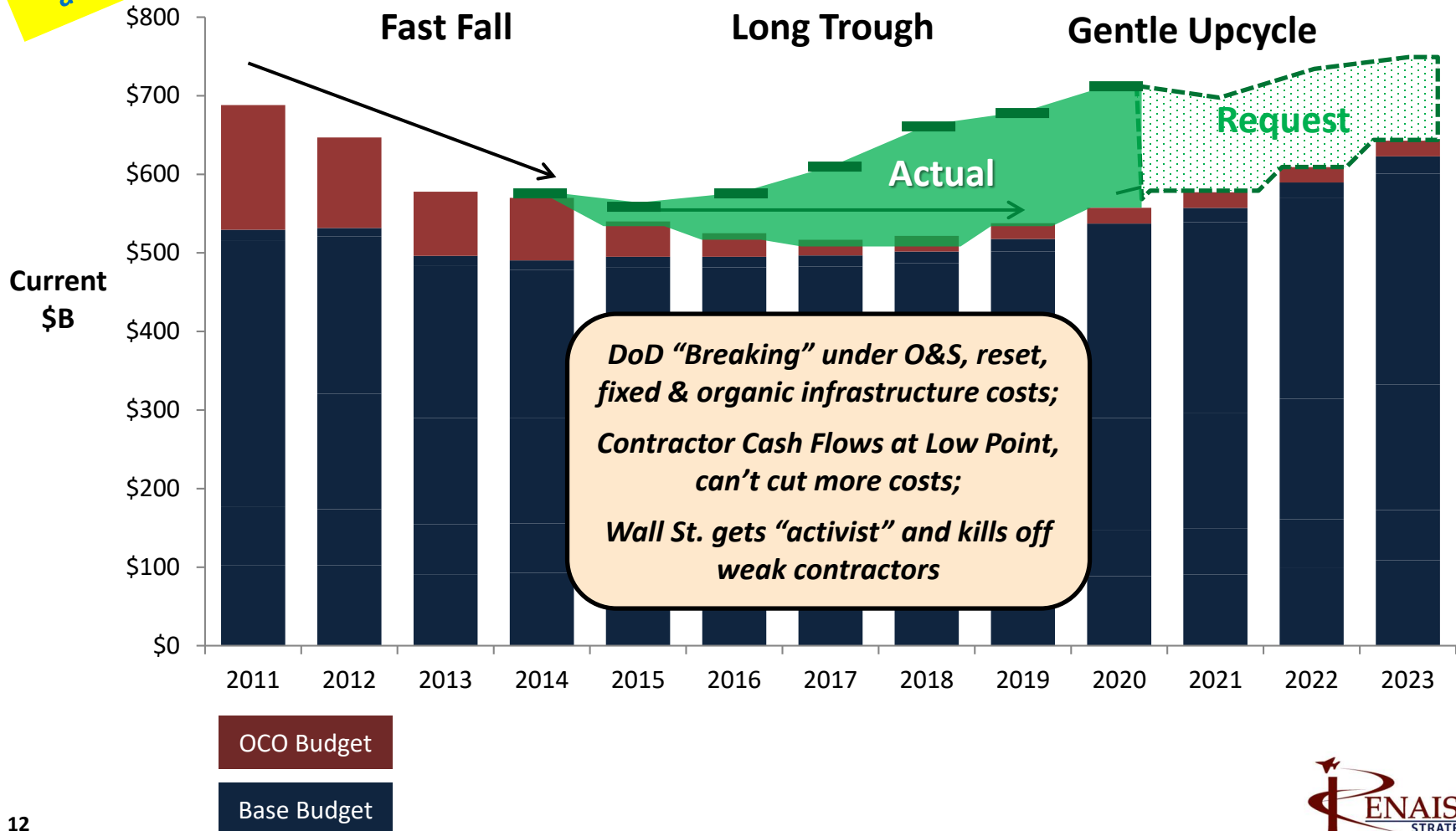
Quick look back to see if we can learn from past predictions

What should a supplier (and also DOD) take away from this?

I have spoken to you in 2014, 2015 and 2017... what did I get right / wrong and what can we learn from it?

Prediction Made at 2014 MES

Highly Plausible Scenario for DoD Total Budget Authority



I have spoken to you in 2014, 2015 and 2017... what did I get right / wrong and what can we learn from it?

Observation Made at 2015 MES

Companies Are Being Rewarded for Using Cash for M&A
(recent transactions over \$1B in enterprise value)

Announced	Acquirer	Target	Target EV as % of Acquirers EV	Stock Price 5 Day Reaction
Feb 2015	Harris	Exelis	55%	10.2% ↑
Oct 2014	Engility	TASC	125%	15.4% ↑
July 2014	AECOM	URS	136%	11.5% ↑
April 2014	Orbital	ATK	237%	7.5% ↑

Is Wall Street telling suppliers to “go big & go early” in terms of restructuring now that the budget has bottomed out?

I have spoken to you in 2014, 2015 and 2017... what did I get right / wrong and what can we learn from it?

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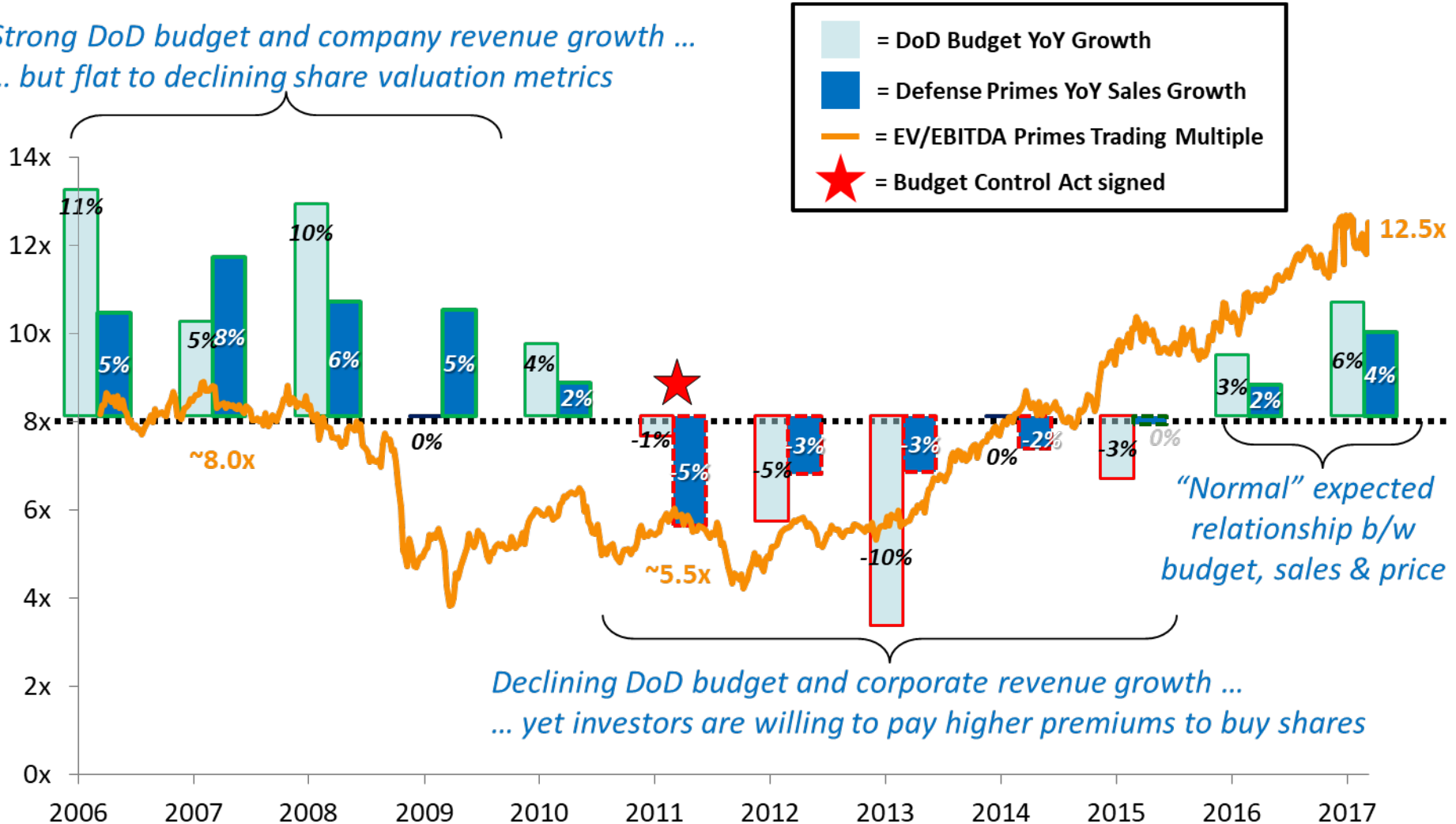
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...the pattern general has held true, but to a lesser degree

Announced	Acquirer	Target	Target EV as % of Acquirers EV	Stock Price 5 Day Reaction
Oct 2018	L-3	Harris	122%	9.9% ↑
Sept 2018	SAIC	Engility	45%	-11.5% ↓
Feb 2018	GD	CSRA	13%	7.0% ↑
Sept 2017	Northrop	Orbital ATK	18%	2.0% ↑

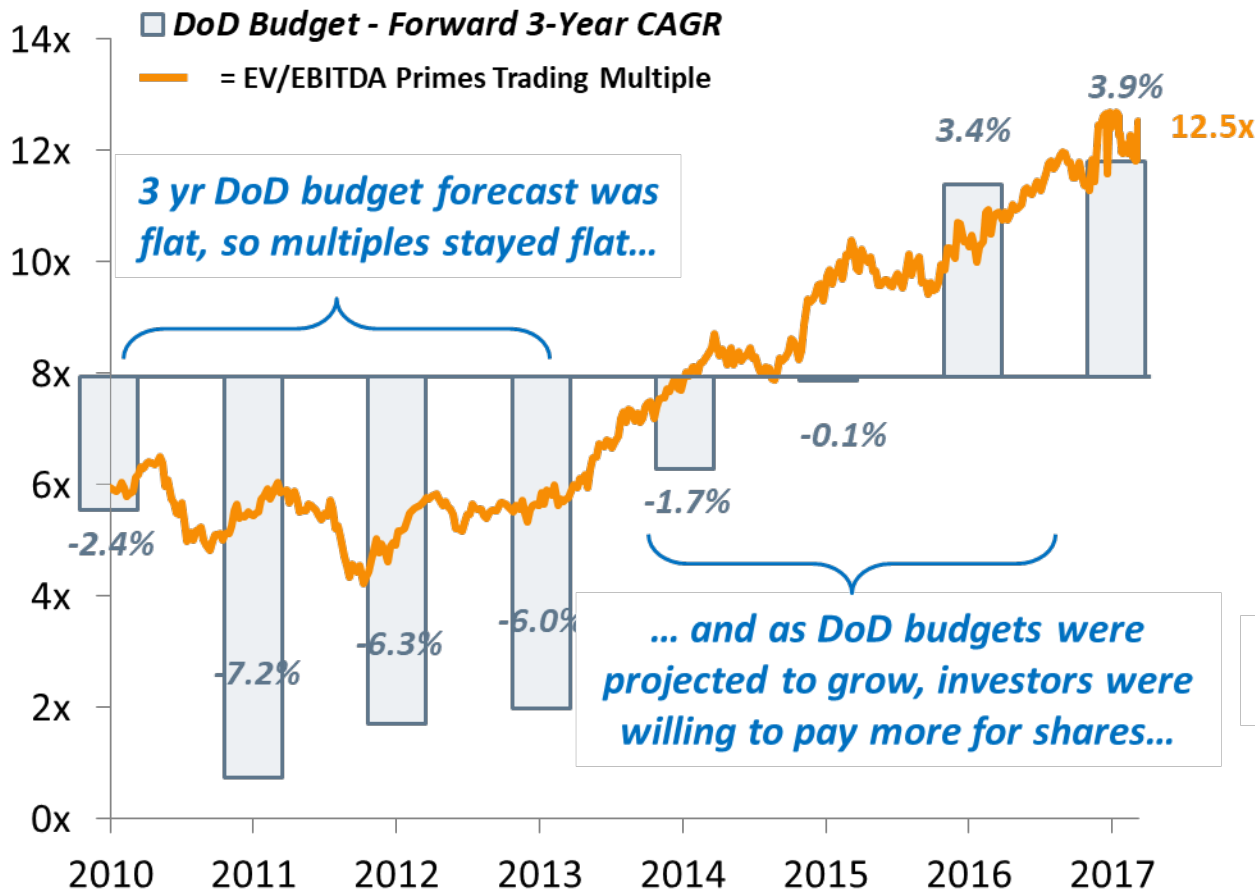
We noted valuation patterns can be counterintuitive...

*Strong DoD budget and company revenue growth ...
... but flat to declining share valuation metrics*

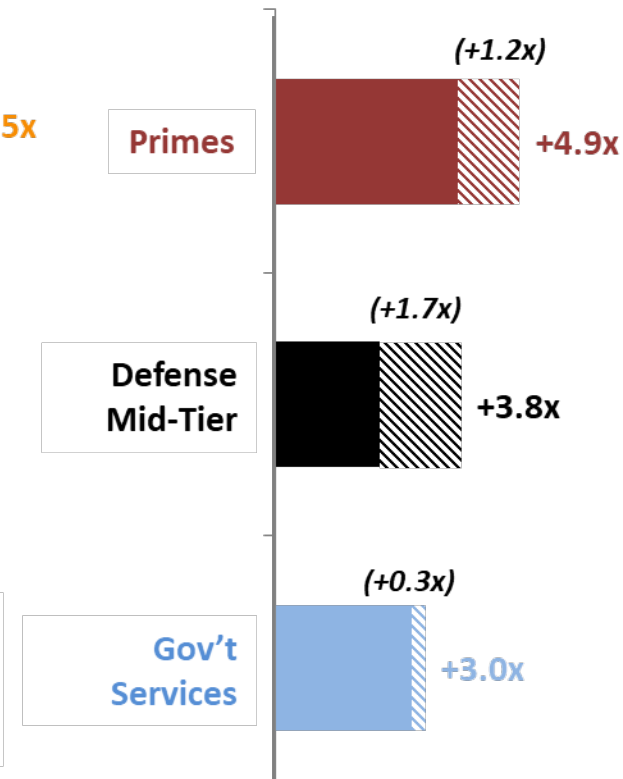


...but actually appear to predict of future trends...

Observation Made at 2017 MES



EV / EBITDA vs. 10-Year Average Post-Election Impact

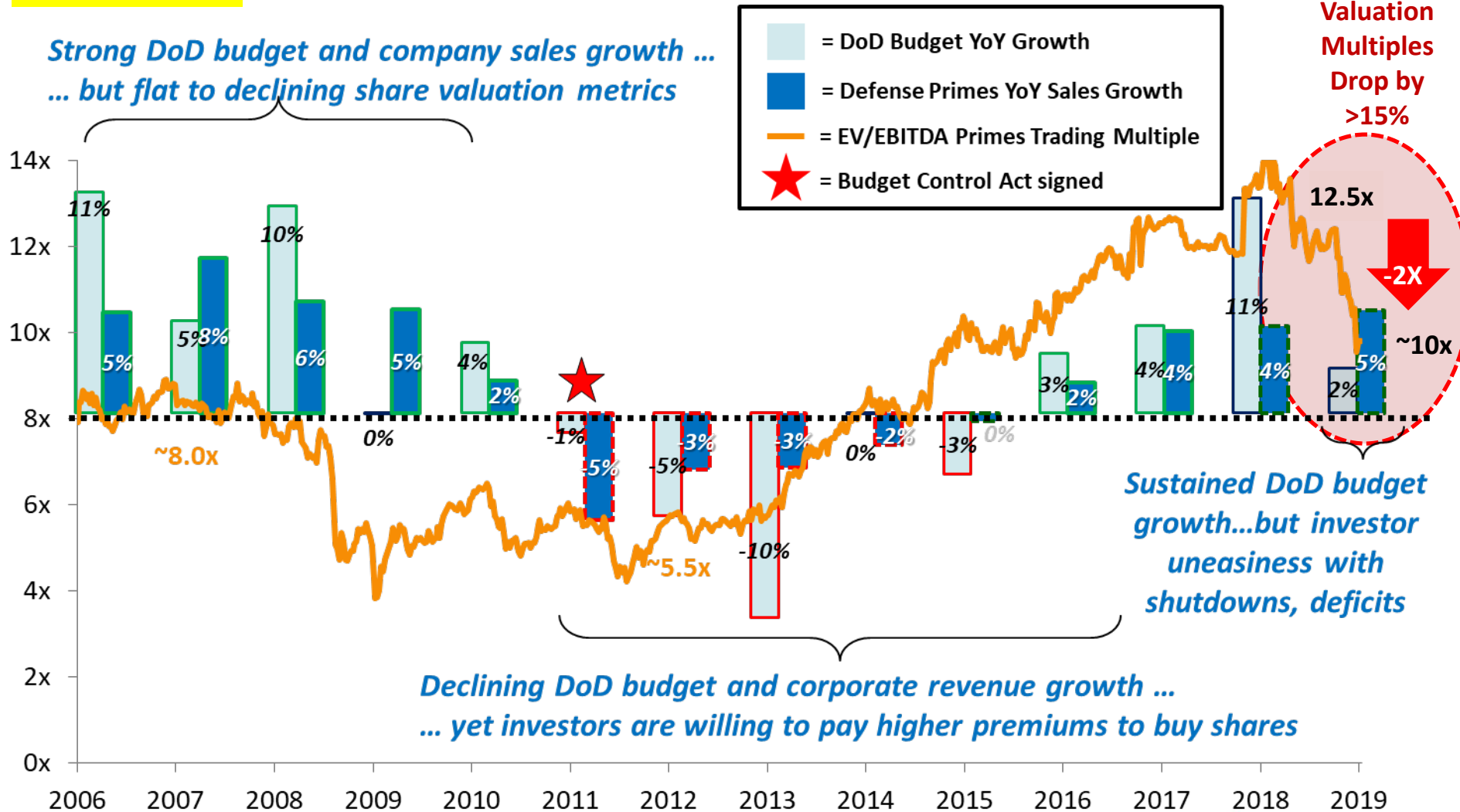


... but is Wall St. going to be disappointed with reality of DoD budgets?

... which if true, tells us that budgets will be flattening

Observation Made at 2017 MES

*Strong DoD budget and company sales growth ...
... but flat to declining share valuation metrics*



What does this look back tell us?

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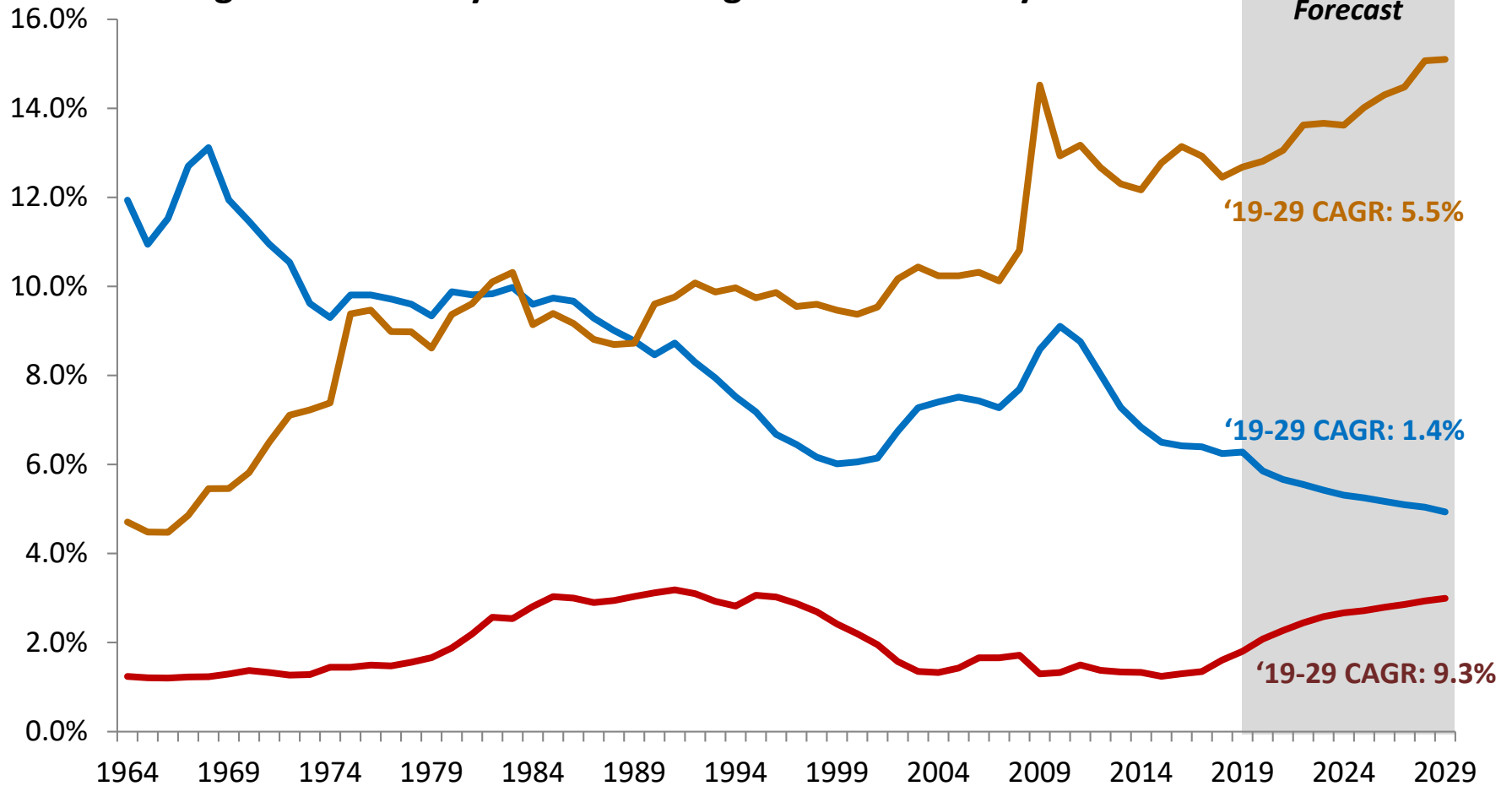
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So what is my overall message to you about Wall St.?

- For Suppliers...
 - Publicly-Traded: be mindful of the financial community, but realize that you likely won't be singled-out as a driver of share price unless they stand-out negatively
 - Small Private Companies: focus on availability of capital and interest rates and how they respond to broader market trends
 - All Companies: Focus on managing **three factors** to avoid standing-out negatively
 - **Cash**
 - » Be very efficient and a strong contributor to the total company's free cash flow / ROIC
 - **CAPEX**
 - » Invest as needed, but avoid being "drain" on parent, seek to gain customer funding if possible
 - **Capability**
 - » Success will be based on Capacity, Quality and Performance
- For DoD...
 - Understand the financial incentives and market forces your supplier partners face
 - Continue to use creative acquisition strategies (e.g., OTA) when appropriate, but be mindful that consistency of message and funding is most helpful

One last thing...

These are three types of US Government Spending... anybody guess what they are? Is this a good slide or scary slide?



If we as a country can't control this, Wall St. and its global peers will do it for us... and we will regret it

