BBA Aviation

BBA Aviation Interim Results 2015

Interim performance – Simon Pryce, Group Chief Executive

Q: How do you describe these interim results?

A: As usual, it was another busy first half for BBA Aviation, but one in which we produced a good set of results. I think there are four key themes that jump out of our numbers that are important to focus on.

Firstly, Signature delivered an excellent operational and financial performance, and that's in an environment of perhaps lower growth than we anticipated at the beginning of the year, which I think is evidence of what a market leader Signature has become.

Secondly, we did have to deal with a couple of issues in ASIG and in ERO, and a couple of those issues were of our own making, but we have addressed them. We expect much-improved performance from those two businesses in the second half.

We continued to invest in the first six months of this year in the strategic development of the Group. We integrated the acquisitions that we've made in Signature to further expand its network, and we've added another eight locations to our Signature Select partner programme. In our Aftermarket business, we signed up two important new licensees with new licence awards. We've got new engine fuel service authorisations, and we've extended a number of our major authorisations with Pratt & Whitney. So half of good strategic development already.

And then finally, all of the performance in the first half from the actions that we're undertaking gives us confidence that 2015 will be a year of good growth.

Q: Growth in US B&GA flying hours was slower than expected. So what impact has that had on the Group?

A: Firstly, it's important to note that there has been growth in the first half, a strong first quarter, and a softer perhaps second quarter than we anticipated. I think it is probably in part due to some decline in business confidence in the second quarter of the year. I think as America began perhaps to recognise the impact that a stronger dollar, lower US consumption and other issues might have, that sort of dampened market expectations of growth in North America.

But I spend quite a bit of time out and about with our customers, and on the ground they're feeling pretty confident and very growth-orientated. So whilst I don't think we're planning for any acceleration into the second half, we anticipate that H2 should be a half of further market growth.

And I think importantly for us, the medium-term indicators of B&GA flying, particularly in North America, remain strong, whilst OE sales in the first half were a little softer than they were in the first half of last year. The order book remains very good. And the OE book-to-bill rates, which is a good indication of future demand, remains very strong. And importantly the second-hand market remains stable, and is even strengthening a bit with second-hand planes available for resale at or below the through-cycle norms and actually pricing pretty firm.

So what that means is this in a GDP+ growth industry like ours, with a market that is still 15% below where it was in the prior peak, even with only slow growth in 2015, there is a lot of growth to come in 2016 and beyond.

Q: The Group has continued to make good strategic progress during the period. So what were some of the highlights?

A: I think, firstly, Flight Support, and Signature, really is performing well, and that is for us evidence of how effective our strategic execution has been over the last five years. We've invested over $300m in our network. We have increased the size of our FBO portfolio by 30% over the last five years. And we spent a lot of time focusing on our customers, and that's resulting in the industry leader that Signature is today. Customers don't just tell us good things; they use us when they can because they know that Signature provides them with the things that they really care about, in a way that others don't.

In ASIG, it's dealing well with a challenging set of net contract losses that we previously announced, and we also had to take the very difficult decision, but the economically rational one, to exit Singapore, even though we only started up in October there. And the team has done a very good job of exiting that location effectively and efficiently, and continuing to support the customer right through to the end of the contract.

So in Aftermarket, we're seeing good development in Engine Repair and Overhaul on market share across most of our engine programmes. But we are in the middle of a footprint reorganisation, which is designed, when it's finished, to create an engine repair facility that can process engines more quickly, that is more flexible and is more cost-effective, all of which benefits the customer.

We did anticipate some inefficiency associated with the line moves during the course of the first half, but we probably underestimated it. And as a result of underestimating it, we incurred a number of costs associated with the slow throughput. We took some decisive action during the half to deal with this, and I'm very confident we'll see a much improved performance from Engine Repair in the second half.

Divisional performance – Mike Powell, Group Finance Director

Q: Can you talk us through the key numbers that you're reporting today?

A: These are a good set of results. We have seen our organic growth up 5%. We've seen good contribution from acquisitions, and that results in underlying operating profit up 3%, and earnings per share up about 1%.

I think from my side, what do I see in this set of results? Mainly three things around, firstly, the strategy is being delivered, particularly with the Signature results being very strong. Secondly, we've resolved a number of issues and made progress in both ERO and our ASIG businesses.

And last but not least, on cash, we continue to generate cash and reinvest that back into the business for future growth, particularly into our Signature and our Legacy businesses. And all of that gives us confidence, which you can see as we have increased the interim dividend by 5%.

Q: So let's focus on the divisional performances, starting with Flight Support. How much was the strong performance there driven by Signature?

A: Flight Support now is a very significant part of the Group, with the operating profits just over about three-quarters of the Group in its entirety, and some very strong numbers, up some 19% year on year. And all of that has been driven by Signature, and a little bit more. Signature is now more than 90% of the Flight Support division and Signature's results are driven by its acquisitions that we've made in the last 12 months, by the organic drop-through that we have made, and also by Signature's outperformance against the markets that it operates within.

Q: There's also a couple of one-offs in the Flight Support numbers. So can you tell us more about those?

A: Yes, there are two, which roughly, roughly net off against each other. One positive, one negative. The positive one is the Hong Kong. We have a facility in Hong Kong, and what we've done is we're really reflecting the economic reality through the accounts, because we do have a significant influence on that business, and it has scale. So what you see there is a write-up of just over $5m into the first half. That's offset somewhat by Singapore, which we've discussed before, we were working through the contract with the customer. We couldn't come to a conclusion on that, and therefore we have terminated that contract in late July. And therefore what you see is the trading losses for the months up to the termination going through the operating profit. So both of those numbers net off and are non-repeat items.

Q: And what can you say about Aftermarket services, where performance was weaker than anticipated?

A: Yes, Aftermarket was weaker than anticipated. Legacy was a solid performance, though down year on year. But that was expected; we have a normal churn of licenses within our Legacy business, and that will come back nicely in the second half, as we'd expect.

The main decline was due to ERO, and that was really due to the footprint rationalisation taking longer than expected.

Q: So staying with the rationalisation of the footprint in Aftermarket services, can you give us more of an update on what's been going on there?

A: Two main issues as we've reorganised and sorted the footprint out. Number one was the labour that we needed to cross-train to make it more flexible across the different types of engines. And secondly, we've had to move a number of engines across factories. Both of those issues have taken us longer than we anticipated. What that's done is lead to a number of cost increases, both in terms of overtime, in terms of customer concessions, and in terms of lease engines so that we can keep our customers planes flying.

During the quarter, what we did, the last quarter we have trained our labour to be more flexible across those engines, and we've improved our process flows within the factories. I'm pleased to say that during June and July, we've seen that in the operational metrics, and the turnaround time is improving, and that leads a much more increased confidence in our second half outlook.

Q: A large part of BBA's growth strategy has been focused on acquisitive growth. So is your balance sheet properly geared up to fund further acquisitions?

A: The business continues to generate significant amounts of cash. We've invested quite heavily over the last 18 months, and even this year our capital to depreciation will be about 1.5 times, before it normalises down to about one times depreciation in the out year.

What that's meant is our leverage has gone up to about 2.6 net debt to EBITDA, and again given the cash generation of the business in the second half, I'd expect to see that trickle down to the top end of our stated through-cycle range of 1.75 to 2.25. But what we also have is a good pipeline of M&A opportunities, and therefore we have a balance sheet that is flexible to cope with those.

So summing everything up, a good set of numbers, Signature delivering really well, issues being addressed in ERO and ASIG, a solid Legacy performance, and our good cash generation being reinvested into the business for future growth.

Strategy and outlook – Simon Pryce, Group Chief Executive

Q: How confident are you when it comes to the Group's full year outlook?

A: The performance of the Group in the first half of 2015, and the actions we've undertaken, gives us confidence that 2015 is going to be another year of good growth for us. I think if you stand back and look at the business, because there is quite a lot of moving parts in this first half, what's really going on is Flight Support, and particularly Signature, is really outperforming and is making up for Aftermarket, which had a weaker than anticipated first half.

And as we enter the second half, we have Signature performing very strongly. We've taken a number of actions to address the issues that were headwinds, for our ASIG and Engine Repair businesses in the first half, and I'm confident that those businesses will see much improved performance in the second half.

And finally, we've made some strategic investments in the first half, which will begin to contribute in the second half. And we see a good pipeline of strategic investment opportunity into H2, particularly and importantly as cash generation begins to accelerate.

So all in all, I think we're pretty well set up for a good year.

Q: As we look ahead to 2016 and beyond, what gives you confidence in the Group's continued growth prospects?

A: Firstly, I think the things that really excite me are our Flight Support business, in particular Signature. We've seen what the impact of volume can do on the Signature and how it delivers strong financial performance with the additional volume that it generates. Our major market of US Business & General Aviation fly remains 15% below its peak. There's lots more volume to come for Signature, and that's before it continues its outperformance. And that will have a very beneficial impact, particularly over a period of more normalised expenditure on both our margin development and on our return on invested capital in that business.

In our Aftermarket space, our Engine Repair business is going through a reorganisation that, when it's finished, will create Engine Repair and Overhaul facilities that can provide customers with more rapid turn times from a lower cost facility in a more flexible way. And all that will be done just as demand for Engine Repair and Overhaul, both due to increased flying, and to the cycles on specific engines, picks up.

We'll also start to see contributions from some of the strategic growth investments we're making today. Our facility in San Jose will be completed by the beginning of 2016. Our new authorisations for helicopter engines in Engine Repair and Overhaul, the facilities will be up and running, and the test cells done.

And finally we'll benefit from a record year of licence adoption within Legacy. So all of that means is, strong organic growth from our base business to come, and importantly the continued cash generation that you see from BBA Aviation, we'll be able to deploy in the strong pipeline of future investment opportunities we see. And so I'm very excited about the future of this Group.