BBA Aviation

BBA Aviation – Final Results interview with Simon Pryce, CEO and Mike Powell, Group FD

2015 Performance – Simon Pryce, CEO

Q: 2015 was a transformational year for the business with the acquisition of Landmark Aviation. What does this development mean for you?

A: Well, it's a really exciting and exceptional year for the Group. The acquisition of Landmark Aviation is really the next stage in our strategy of continuing to drive long-term value creation from this Group.

If you look at what the combination of Landmark and Signature does, it creates significant increase in scale in one of our best businesses. It has a track record of excellent delivery. It gives us access to accelerated value creation opportunities through cost reductions that arise through the combination, but also from the increasingly apparent revenue synergies that we think we can generate over time. And it positions the Group really well in a market that has long-term structural growth drivers for an extended and exceptionally exciting future.

Q: You say this acquisition builds on a year of underlying growth for the business, within this context talk us through BBA Aviation's 2015 performance?

A: The Group as a whole delivered growth in a broadly flat market which actually is tantamount to the hard work of everybody in the businesses. I think we should start with Signature which had yet another exceptional year.

If you look at what Signature has done, it's outperformed its market in each of the last five years and 2015 was no exception, even though that market was relatively flat. We saw very strong conversion of that volume growth into EBITDA, which is tantamount to Signature's network strengths, its cost management, its efficiency and increasingly to the way it approaches revenue management.

The team at Signature has a done a really good job and has delivered strongly over the last couple of years and that gives us great confidence that they'll be able to integrate the Landmark acquisition just as effectively as they've delivered over the last few years.

Q: And what about ASIG?

A: So ASIG has had a slightly more difficult year. The ASIG management team have had to deal with a number of issues within the business. As you know it's a very competitive environment, but they dealt effectively and in a very economically rational way with both the loss-making contract that we had to deal with in Singapore - admittedly at some cost - and also importantly, they've dealt well with costs against a background of a net contract loss position which we saw in the first half of 2015, particularly the loss of the JFK T1 contract.

But as they continue to focus on their inter-plane business which is a much higher quality service and also as they focused on service delivery and improved service quality, we've seen a much improved operational performance from ASIG in the second half of 2015 and good net contract wins towards the end of the year.

Q: Are you going to sell the business?

A: So I think as a public company, we always have to keep an eye on value creation. The announcement of the Landmark transaction did result in a couple of parties making formal approaches to us and we're obligated to look at those as part of our desire to maximise value for our shareholders.

So we are going to look at the potential strategic opportunities for ASIG which may or may not lead to the sale of some or all of the business. It will be all done on the basis of value. But in the meantime, ASIG continues to improve and I look forward to a good year for ASIG in 2016.

Q: And a disappointing performance from ERO. What's the plan there?

A: ERO has had another challenging year. As you know, we're about halfway through a programme to reduce our footprint and to make ourselves the lowest cost and highest quality provider of heavy overhauls to small thrust capacity engines. That restructuring programme has been delayed by weather in Texas, so we're about six months behind where we needed to be. And as part of that programme, as we started to move lines in the first half of this year, we did experience greater than anticipated production inefficiencies.

We addressed that well and quickly into the second half and I'm really pleased with the turn times we're seeing on virtually every engine model that we've moved. But what we didn't see in the second half which we anticipated was a pick-up in volume. Markets are broadly flat and a combination of the actions of competitors (it's a pretty tough market out there) and the OEs meant that we didn't see the volume increase that we anticipated.

So all in all, it's been a pretty tough year in ERO and as a result of that we are going to have to look further at how to simplify and reduce the costs in ERO more and we'll be undertaking that action in 2016.

Q: And what about your key markets, how have they performed over the year?

A: We saw growth, albeit slow in North America. Movements were up about 1% which is probably a bit less than we thought at the beginning of the year and we did see a slight decrease in industry confidence towards the end of 2016. I think a lot to do with the global uncertainty that there is out there today. But actually the fact that we did continue to see growth is evidence of how robust B&GA flying is at these levels.

In Europe, it was somewhat weaker than North America. The market was down about 3% and clearly deteriorated post the tragic incidents in Paris in November. Commercial markets were about where we thought they'd be as was our defence business.

So broadly, the year was a little lower market growth than we anticipated but still market growth and the businesses and particularly Signature performed really well in that environment.

Operational review – Mike Powell, Group FD

Q: Take us through the headline numbers you're reporting today.

A: 2015 was a good year for the Group. We set up and funded the acquisition of Landmark as well as delivering a satisfactory set of numbers. Within those numbers, we had Flight Support up significantly, to about $160m and in Aftermarket a decline to something around $60m of profit.

Within those divisions, Signature had an excellent performance and whilst ERO was disappointing, our Legacy business delivered another solid set of results.

The Group overall had very good free cash generation and that allowed us to set up a really good platform as we move forward with integration of Landmark.

With EPS up a touch, the Board have increased the dividend a further 5% and that really reflects the ongoing momentum that I've just discussed.

Q: And what impact has the rights issue had on these results and on the shape of the balance sheet?

A: As you know we had a very successful and well supported rights issue which we executed in quarter four. So the money has come in, in quarter four and the number of shares in issue have also gone up. But of course we didn't actually deploy that money until February when we closed the transaction. And therefore in the year end numbers that affects a number of the key metrics, such as earnings per share, any dividend ratios and also the net debt.

So what I've tried to do with this set of numbers in 2015 is provide those on both a historical basis as though that capital hadn't come in, but also on a statutory basis so the readers of the accounts can see both. And that also provides a clean edge as we look forward into 2016, so that people can get their models correct as we look forward with the new larger business.

Q: Let's take a closer look at divisional performances beginning with Flight Support and Signature's contribution.

A: Flight Support is around just over 75% of the Group's operating profit in 2015 and it will be somewhat more as we move forward with the acquisition of Landmark. Within Flight Support, Signature represents more than 95% of the division's operating profit. Signature had an excellent performance all the way through the year, outperforming the markets it operates in and that outperformance dropping through into good operating leverage.

That was somewhat offset by the contract losses in our ASIG business though we did see operational improvements in the second half of the year in the ASIG business. And all that led to very strong cash generation, mainly driven by the Signature business and that stands us in really good shape to both integrate and then grow the business post the Landmark integration.

Q: And it has been another weak performance from Aftermarket Services, ongoing underperformance in ERO. Walk us through what's happening here.

A: So the aftermarket division is around 25% of the Group's operating profit in 2015 and it will be somewhat lower in the enlarged Group as we look forward. Within that our Legacy business had a good solid performance. They had a number of new licenses coming into the business and the core business preformed really well against what was actually a very strong comparator year of the prior year.

Within the ERO business particularly in the first half of the year, we had some disruption to our factory caused by moving the engine lines around. That's now fixed. And in the second half of the year we expected to see some market share gains. Those didn't come through. The market was very competitive and pricing was also competitive and therefore profits fell again in the second half of the year.

I think as we look forward, we don't see a significant change in that marketplace and therefore we're also announcing today to the marketplace that we will put through a cash exceptional charge of $5m to further reduce the costs in that business.

Q: With the Landmark Aviation acquisition cash generation will be enhanced, wit the Landmark Aviation acquisition, but you are starting from a higher leveraged balance sheet.

A: Yes, we are starting from a proforma 2015 leverage of around 3.5x and that's the leverage point, assuming that the transaction had happened right at the end of the year and we'd disposed of the FPOs that we have to dispose of. So at 3.5x we're very comfortable and that's based on the good cash generation that this Group currently delivers which will be enhanced, as you say, as we move forward.

We still plan to invest capex to depreciation and associated amortisation of about 1.3x as we go into 2016, really finishing off the major projects in Signature at San Jose and Luton. And then we will also invest about $44m which we've already announced in terms of delivering the synergies, $19m of capex and $25m that will go through the income statement.

And with that and the cash generation of the Group, that will allow us to de-lever through 2016 while still investing and we'll probably approach something like 3x net debt/EBITDA at the end of 2016 and then continue to de-leverage through 2017.

Outlook – Simon Pryce, CEO

Q: What are your first impressions of the Landmark Aviation business and how is the integration process going?

A: So we've been looking at Landmark Aviation on and off for a number of years, so we already know the asset pretty well. We're now four weeks in, we completed on 5th February. We're four weeks into integration. We've got over 40 people in the Signature team and a significant number of Landmark folks working together through the integration plans that we put in place prior to the acquisitions and those guys are actually slightly ahead of where we anticipated they'd be a month in and we're really pleased with what we're seeing.

No surprises and everywhere we look, we see interesting opportunity and potentially greater opportunity than we originally thought in bringing the two businesses together and combining the capabilities of both of those businesses, taking best practice and applying that across the largest network of FBOs in the world.

Q: So what are your aspirations for 2016?

A: Well, I think firstly, the US in the B&GA market we probably think we will see a continuation of the relatively low growth environment that we saw in 2015. But against that background we already know how strongly Signature performs even in a low growth environment.

And then of course we'll be executing the integration of Landmark. As I've said that's got a lot of people focused hard on generating a run rate of $35m of annualised synergies by the end of 2016 and we're already ahead of where we thought we'd be in that programme.

If you look at the management actions that we've undertaken in some of our other businesses, in ERO we will be going through some further simplification work. That will leave that business in a much better place by the end of 2016.

And in ASIG of course we've done a lot of work in the second half of 2015 which means that 2016 will be a much better year for them.

And then finally, and not least, Legacy which has had a great track record over the last five years and we expect to see that continue in 2016. They're continuing to adopt a number of new licenses that they've taken on board and they've got a really strong pipeline which I expect to see them realise some of.

So all in all I think we're well positioned for a good 2016, even in a slightly less high growth environment than we might have originally anticipated. So I feel really good about the year.

Q: Now the Landmark Aviation transaction materially increases your exposure to the B&GA market. What are the medium and long term growth prospects for B&GA?

A: So B&GA is a market that benefits from structural growth drivers. It is cyclical and within a cycle, it's driven principally by company confidence. People are out growing and building, they want to get on private jets, because private jets are productivity and efficiency tools.

It's undoubtedly true that the world today is a bit more volatile and a bit more unstable than perhaps it was a year ago, but despite that we've seen pretty robust short term flying. And the markets are still up which is a positive.

Given that it's an election year, given that that uncertainty is still out there, I don't think we're planning for anything other than a continuation of the slow growth that we saw in 2015 into 2016. But the medium-term indicators for our business remain very strong. We have OEs continuing to develop and build new planes. We see strong demand for second hand planes. We see stable pricing.

And over the long term, the thing that drives GDP++ growth in this business across the cycle, there's no change in those. The demographics of the US, the lack of intermodal alternatives, the increasing money value of time, and of course the fact that the commercial airlines continue to focus on hub-and-spoke because economically that's the right thing for them to do means that there's a very exciting long-term growth story in business and general aviation. And we as the largest player in it in the best space in it, will see more than our fair share of that growth. So we're very excited about where we are and the longer term growth prospects that have been enhanced by the Landmark acquisition for BBA.

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