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Top-Performing Companies

## Top-Performing Companies Prove Their Business Prowess

*Aviation Week & Space Technology Apr 24, 2015 , p. 42*

*Michael Bruno Washington*

*Utilitarian Excellence*



**Honeywell**

A funny thing happened on the way to the aerospace and defense industry's maturation. The companies became good businesses—maybe too good.

Twenty years ago when Aviation Week started its annual review of Top-Performing Companies, the concern was that Western A&D companies did not operate well as businesses, at least not compared with other sectors and Wall Street benchmarks. While they provided amazing weaponry, airliners and spacecraft, when it came to operating performance, A&D enterprises seemed to lag by decades automotive, oil and gas, and other industries in basic business prowess.

A look at this year's TPC rankings and results indicates they have learned their lessons well. Not only did A&D as a whole post record revenue for 2014, but many companies simply became operationally better. What is more, this change came about despite two years of so-called sequestration spending restraints, the historical halving of the price of a barrel of oil, the dramatic strengthening of the U.S. dollar, airliner disasters and international volatility such as in Ukraine.

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“The core of the big primes and the U.S. defense industry continue to do really well despite all the angst and observable trauma,” says TPC adviser Jacob Markish, principal at Renaissance Strategic Advisors. “Another measure that was unsurprising is that the well-focused and disciplined mid-tier, whether in electronics or in one of the commercial parts of the components sector, continues to do very well.”

Above all, the record up-cycle in commercial aerospace, led by the now nine-year backlog of large airliner orders, continues to drive up the whole sector. “The story last year, in 2014, was commercial,” says Tom Captain, vice chairman and global A&D sector leader for Deloitte and a TPC adviser. “The story will be the same in 2015. There is no bubble.”

TPC rankings of publicly traded A&D contractors are the result of composite scoring of four equally weighted performance categories that place significant emphasis on operating excellence. They are: return on invested capital (ROIC), measuring investment decisions; earnings performance, i.e., revenue quality and expansion; asset management, or how efficiently a company employs its resources; and financial health, as in a company’s strength, including overall solvency.

In turn, the TPC council of advisers this year identified several common attributes among companies that can claim success in the rankings. For starters, A&D companies appear better managed from the top down; even defense units are run as much like commercial operations as possible. Next, companies are increasingly focusing on areas of expertise, becoming dominant players in niches and shedding non-core operations.

“The thing that keeps coming back at me, year after year, is the companies that do well have a proprietary position; they know what business they’re in,” says Harlan Irvine, a TPC adviser and Deloitte principal. “The folks that have a defensible position, either they own a program of record or they own intellectual property that they can lever. They do a decent job of running the business according to the levers that are relevant.”

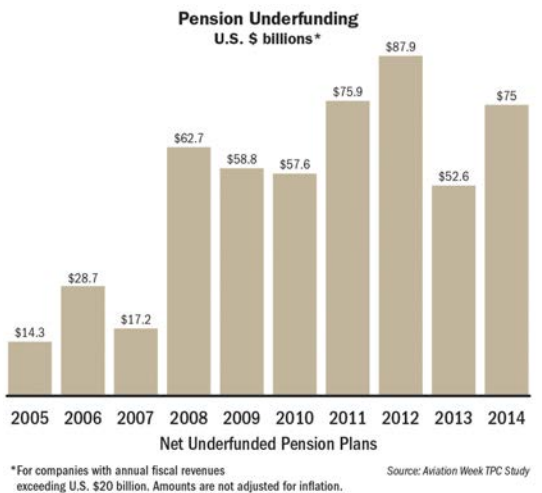
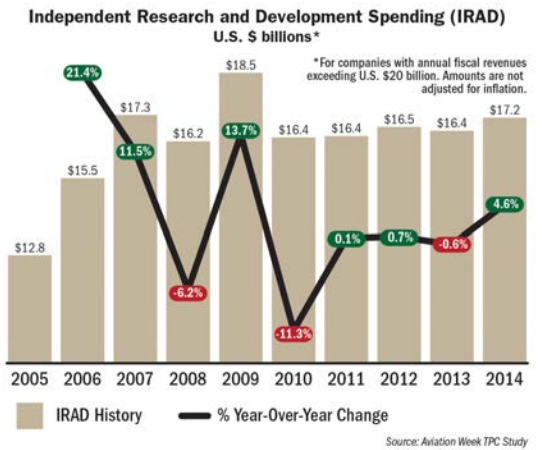
In defense, companies are trying to develop or harness commercial technology—like [Rockwell Collins](#) and its Pro Line Fusion avionics—to the extent possible rather than the Cold War approach of government-first. And, paradoxically, when focusing a company, Top-Performing Companies are buttressing revenue by diversifying customer types and sources, such as by boosting international sales, finding new clients for current offerings, and even tiptoeing into adjacent markets.

Surpassing these trends, however, is the idea that the companies in general are leaner, more efficient and more productive, per worker. If possible, major assets and inventories are placed or left in the hands of others, e.g., shipyards with the government instead of defense shipbuilders, or Tier 1 aerostructure providers instead of the nameplate original equipment manufacturers (OEMs). [Liabilities such as pensions](#), once proverbial albatrosses around the neck of industry, are being optimized. Finally, [free cash flow](#), the money generated and left over after assets are dealt with, is maximized and most of it is returned to shareholders and investors.

“It has to do with the treatment of assets,” says Steven Grundman, a TPC adviser, George Lund Fellow at the Atlantic Council, and former assistant secretary of defense for industrial affairs and installations. “Utility-style companies that manage assets well and generate cash succeed in this model. That does not tend to be a thing we all celebrate.”

For John Stack, managing director and aerospace leader at the McLean Group, and other advisers, the true measure of a company is in what it makes beyond the financial reports. What the numbers show and what industry executives and analysts can point to can be different and worthy of consideration. “It should be about value creation,” he says.

Take [Boeing](#), which won both its TPC category (\$20 billion or more in annual revenue) and scored the best among all companies (97 this year, and a five-year average of 93). Captain points out that the leading OEM looks to be on the verge of reaching \$100 billion



a year in revenue in a couple of years, and maybe even next year when the company marks its 100th anniversary. If no new airliners were ordered this year due to a cataclysmic event—think a 9/11-type terrorist attack or pandemic flu, which shuts down air travel—the backlog would slip to just an eight-year wait-list.

“Boeing is a fundamentally unique company,” Markish says. “Their commercial operations . . . effectively constitute half of a hugely valuable duopoly and [it] has consistently known how to make money.” -Results from 2014 do not represent a new era or new direction “It is -business as usual at a macro level.”

Yet while the OEM and Pentagon prime is eyeing or pursuing new programs like a “middle-of-the-market” 757-replacement airliner or the U.S. Air Force Long-range Strike Bomber, these are seen more as derivative innovations. Boeing Chairman and CEO Jim McNerney last year famously declared no more “Moonshots” when it comes to development efforts, and the company has been reaping the benefit of its steady market dominance for years.

TPC advisers recognize that it took Boeing a lot of investment and innovation—as well as some course corrections—to reach this point. Five to six years ago, the company’s problems with major programs and customers were headline news, and TPC advisers at the time criticized both management execution and program performance. Now it is “smooth sailing,” one adviser says.

The company is not only reaping the benefit of earlier investments and corrective actions, the learning curve is being extended into other programs. In February a reorganization of **Boeing Defense, Space and Security** was announced that resulted in a new entity—the BDS Development office. Modeled after a similar unit in **Boeing Commercial Airplanes**, the office “will address development risks and affordability.” Six programs now managed elsewhere in BDS will be the first to be overseen by BDS Development, including the **USAFKC-46** aerial refueling tanker and **NASA** Space Launch System rocket.

Still, for an industry that can claim hypersonic vehicles, landing humans on the Moon, and helping to build—here in the U.S.—what is arguably the most powerful military on Earth, the emphasis on shareholder value maximization and relatively lower independent research and development are less inspiring to many observers. It also comes as Pentagon officials are pushing their so-called Third Offset strategy for technology development, with a soon-to-be-unveiled Long-range R&D Plan crafted with industry in mind.

TPC advisers such as Byron Callan, a director at Capital Alpha Partners, say they see potential changes coming to industry’s makeup as managers and directors shift their focus to longer-term positioning. In 2016-18, the “overwhelming” investor focus on defense contractor capital deployment could give way to accommodation of the Pentagon’s changing acquisition practices and emerging competition.

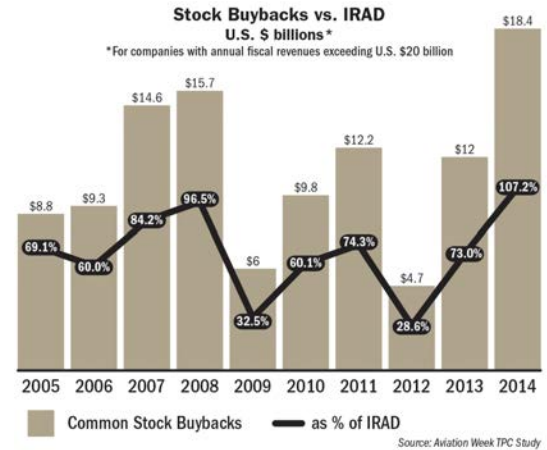
“Managements that do not make strategic decisions on their participation in defense but overwhelmingly deploy capital in favor of shareholders could be caught flat-footed by these changes,” Callan cautions.

Stock agrees: “You can only lever to pay buybacks and dividends and everything else for so long. You can’t save your way to greatness.”

### Top Performing Companies Extras

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- Rankings of A&D companies with revenues between \$250 million and \$1 billion
  - Detailed interactive charts of TPC-ranked companies with links to spreadsheets
  - Rankings of more than 100 A&D business segments in 14 categories
- [AWIN.AviationWeek.com/TPC](http://AWIN.AviationWeek.com/TPC)



### 2015 Aerospace & Defense Rankings

RANK	Company	Results Ending	2014 Revenue (\$ millions)	Total Score
<b>REVENUES GREATER THAN \$20 BILLION</b>				
1	Boeing	Dec. 14	\$90,762	97
2	Lockheed Martin	Dec. 14	45,600	96
3	Honeywell International	Dec. 14	40,306	88
4	Raytheon	Dec. 14	22,826	77
5	BAE Systems	Dec. 14	24,029	74
6	Northrop Grumman	Dec. 14	23,979	73
7	General Dynamics	Dec. 14	30,852	73
8	United Technologies	Dec. 14	65,100	64
9	Airbus Group	Dec. 14	73,445	56
10	Rolls-Royce	Dec. 14	21,391	51
11	Bombardier	Dec. 14	20,111	9
<b>REVENUES BETWEEN \$5-20 BILLION</b>				
1	Thales	Dec. 14	\$15,694	69
2	Rockwell Collins	Dec. 14	5,164	69
3	Precision Castparts	Dec. 14	10,039	65
4	Spirit AeroSystems	Dec. 14	6,799	65
5	Textron	Dec. 14	13,878	62
6	Fimmeccanica	Dec. 14	17,738	54
7	Huntington Ingalls	Dec. 14	6,957	54
8	Safran	Dec. 14	18,199	54
9	GKN	Dec. 14	10,873	52
10	Orbital ATK	Dec. 14	5,146	51
11	Zodiac Aerospace	Aug. 14	5,482	49
12	Embraer	Dec. 14	5,621	45
13	L-3 Communications	Dec. 14	12,124	44
14	Rheinmetall	Dec. 14	5,671	42
15	Babcock International Group	Sep. 14	6,042	38
16	Sercos Group	Dec. 14	6,159	1

# 2015 Aerospace & Defense Rankings

RANK	Company	Results Ending	2014 Revenue (\$ millions)	Total Score
<b>REVENUES BETWEEN \$1-5 BILLION</b>				
1	<b>Teledyne Technologies</b>	Dec. 14	<b>\$2,394</b>	<b>67</b>
2	Dassault Aviation	Dec. 14	4,452	64
3	FLIR Systems	Dec. 14	1,531	62
4	Harris	Dec. 14	4,959	62
5	Hexcel	Dec. 14	1,856	56
6	Helco	Oct. 14	1,132	51
7	Woodward	Dec. 14	2,060	49
8	OHB	Sep. 14	1,030	46
9	Exelis	Dec. 14	3,277	46
10	Ultra Electronics	Dec. 14	1,112	46
11	Cubic	Sep. 14	1,398	45
12	Elbit Systems	Sep. 14	2,919	43
13	Senior	Dec. 14	1,278	43
14	CAE	Dec. 14	1,975	41
15	Kaman	Dec. 14	1,795	40
16	MTU Aero Engines	Dec. 14	4,735	39
17	Moog	Dec. 14	2,636	39
18	Esterline	Oct. 14	2,051	39
19	Barnes Group	Dec. 14	1,262	39
20	B/E Aerospace	Dec. 14	2,599	39
21	Curtiss-Wright	Dec. 14	2,243	39
22	TransDigm Group	Dec. 14	2,430	37
23	Saab	Dec. 14	3,018	36
24	Meggitt	Dec. 14	2,420	35
25	Triumph Group	Dec. 14	3,745	32
26	GenCorp	Nov. 14	1,597	32
27	BBA Aviation	Dec. 14	2,290	32
28	AAR	Nov. 14	1,939	30
29	Cobham	Dec. 14	2,884	26
30	Kennametal	Dec. 14	2,898	25
31	Wesco Aircraft Holdings	Dec. 14	1,505	24
32	Allegheny Technologies	Dec. 14	4,223	23
33	Indra Sistemas	Sep. 14	4,064	15
<b>REVENUES BETWEEN \$250 MILLION-\$1 BILLION</b>				
1	<b>AeroVironment</b>	Apr. 14	<b>\$252</b>	<b>97</b>
2	Astronics	Dec. 14	661	92
3	e2v Technologies	Mar. 14	363	90
4	Motor Sich	Sep. 14	863	85
5	National Presto	Dec. 14	412	77
6	Esco Technologies	Sep. 14	531	75
7	Sparton	Jun. 14	336	64
8	RTI International Metals	Dec. 14	794	63
9	Magellan Aerospace	Dec. 14	726	60
10	Jamco	Mar. 14	629	59
11	Chemring Group	Oct. 14	645	51
12	Sypris Solutions	Dec. 14	355	47
13	Sumitomo Precision Products	Mar. 14	436	44
14	KeyW Holding	Dec. 14	291	42
15	S&T Dynamics	Dec. 14	511	40
16	Erickson	Dec. 14	347	38
17	Ducommun	Sep. 13	742	36
18	DigitalGlobe	Dec. 14	655	30
19	LMI Aerospace	Dec. 14	388	29
20	Kratos Defense & Security	Dec. 14	868	21

## Business Segment Winners – Fiscal 2014

RANK	Category	Company Business Segment
<b>REVENUES GREATER THAN \$500 MILLION</b> <small>Multiple Units Within a Single Category Are Aggregated</small>		
1	<b>Avionics/Flight Management/Control Systems</b>	<b>Woodward Aerospace/Energy</b>
2	Business Aircraft	Embraer Executive Jets
3	Subsystems/Subassemblies	Eaton Aerospace
4	Missile & Weapons Systems	Lockheed Martin Missiles & Fire Control
5	Military Aircraft	Lockheed Martin Aeronautics
6	Naval Systems	General Dynamics Marine Systems
7	Commercial Aircraft	Embraer Commercial
7	Rotorcraft	Textron Bell Helicopter
8	Forgings/Castings/Precision Components	Curtiss-Wright Commercial Industrial
8	Civil & Military Training & Support Services	Northrop Technical Services
9	Radars/Sensors/Electronic Warfare/C4ISR	FLIR Surveillance/Instruments/OEM/Maritime/Security
9	Propulsion	Safran Aerospace Propulsion
10	Space Systems	Lockheed Martin Space Systems
11	Land Systems	Oshkosh Defense

Note: Ranked by fiscal 2014 median category scores.

# Average 5-Year Ranking

RANK	Company	Average 5-Year Score
<b>REVENUES GREATER THAN \$20 BILLION</b>		
<b>1</b>	<b>Boeing</b>	<b>93</b>
2	Lockheed Martin	90
3	BAE Systems	80
4	Rolls-Royce	79
5	Honeywell International	75
6	Raytheon	75
7	Northrop Grumman	73
8	General Dynamics	68
9	United Technologies	65
10	Airbus Group	54
11	Bombardier	30
<b>REVENUES BETWEEN \$5-20 BILLION</b>		
<b>1</b>	<b>Rockwell Collins</b>	<b>82</b>
2	Precision Castparts	73
3	GKN	64
4	Thales	62
5	Safran	61
6	Rheinmetall	59
7	Orbital ATK	53
8	Textron	51
9	Embraer	49
10	Zodiac Aerospace	49
11	L-3 Communications	46
12	Babcock International Group	45
13	Finmeccanica	45
14	Spirit AeroSystems	38
15	Serco Group	34
<b>REVENUES BETWEEN \$1-5 BILLION</b>		
<b>1</b>	<b>Teledyne Technologies</b>	<b>71</b>
2	FLIR Systems	66
3	Harris	60
4	Cubic	58
5	Ultra Electronics	57
6	Dassault Aviation	54
7	OHB	52
8	Heico	52
9	Hexcel	50
10	Woodward	50
11	MTU Aero Engines	48
12	Saab	46
13	Senior	46
14	GenCorp	45
15	Elbit Systems	43
16	TransDigm Group	43
17	CAE	42
18	Triumph Group	41
19	Cobham	40
20	B/E Aerospace	39
21	Meggitt	39
22	Moog	37
23	Kaman	36
24	Esterline	36
25	Kennametal	36
26	Wesco Aircraft Holdings	35
27	Indra Sistemas	35
28	Curtiss-Wright	34
29	BBA Aviation	31
30	Barnes Group	30
31	AAR	29
32	Allegheny Technologies	27

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