

## Q1 2010: Inside this Issue

Welcome to the most recent issue of Lincoln International's Aerospace and Defense ("A&D") Deal Reader, a newsletter focused on market dynamics, merger and acquisition trends and events of interest to owners and managers of global A&D businesses and their advisors.

Lincoln's Aerospace and Defense group is one of the largest and most active in the middle market - *and the only truly global team.*

In this issue, we are pleased to present an interview with Amit Yoran, CEO of NetWitness Corporation, that highlights the growing cyber security threat and the steps that both federal agencies and corporations around the globe need to take to ensure the safety of their information technology infrastructures.

Other topics covered in this issue include an article on the current trends in Washington D.C. by Lincoln Advisory Director Brig-

dier General Bob Edmonds, a review of current trends in the industry by Director Alyssa Morrisroe, and recent M&A news involving A&D companies.

We hope you find this newsletter a useful tool, and welcome any comments.

**Lincoln International**

## The Growing Cyber Security Threat: Interview with Amit Yoran, CEO of NetWitness Corporation

Conducted by Lincoln International's Scott Hebbeler

*NetWitness Corporation, based in Herndon, Virginia, provides network security monitoring software products for commercial and government organizations. Amit Yoran has been serving as CEO of NetWitness since November of 2006. Prior to NetWitness, he was appointed as Director of the US-CERT and National Cyber Security Division of the Department of Homeland Security, and as CEO and advisor to In-Q-Tel, the venture capital arm of the CIA. Formerly Yoran served as the Vice President of Worldwide Managed Security Services at Symantec Corporation. Yoran was the co-founder of Riptech, a market leading IT security company, and served as its CEO until the company was acquired by Symantec in 2002. He served as an officer in the United States Air Force in the Department of Defense's Computer Emergency Response Team.*

**Q: In a previous DealReader, we discussed the asymmetric nature of cyber attacks and their various sources (isolated hackers, terrorist cells, organized criminals, state-sponsored cyber professionals, etc.). Which of these sources do you view as the greatest threat going forward?**

Amit Yoran: Like many cyber security challenges, "greatest" is an unclear unit of measure. Ultimately, the greatest challenges come from our dynamic use of technology. That force multiplier, if not properly managed, can also turn into a strategic vulnerability. Who the threat actors are is ultimately less interesting to our defensive activities than how they are



evolving. Today's criminal elements are operating with a level of sophistication that in many instances looks like state actors. It's this evolution of the threat environment that we need to adjust to.

**Q: You and your company, NetWitness, were recently featured in the Wall Street Journal as having identified one of the largest and most sophisticated cyber attacks discovered to date. Can you tell us a bit more about the nature of this attack?**

AY: The attack involved more than 75,000 computer systems at nearly 2,500 companies in the United States and around the world. The attack, which began in late 2008, targeted proprietary corporate data, e-mails, credit-card transaction data and login credentials at companies in the health and technology industries in 196 countries. The real value in our discovery was in gaining accurate insight into a month in the life of a fairly large scale, fairly sophisticated "bot" (a type of malware which allows an attacker to gain control over the affected

computer) and its associated activities.

**Q: What can companies and government agencies do to prevent similar attacks in the future?**

AY: I don't know that such exploits can be prevented in today's computing environments – certainly not for any large scale enterprise network, in the private sector or government. Smart organizations realize that modern threats are designed to bypass their antivirus products, firewalls and intrusion detection systems, which are largely signature-based in having to know what an attack looks like in order to protect against it. If your IT security team hasn't detected or responded to a sophisticated incident in the last week, month, quarter, year or longer, I would venture to say that you're probably missing things or that your team is uniquely resourced, gifted and lucky. In my experience, it's the missing things that is the more likely scenario.

**Q: How do these organizations view the cost vs. risk tradeoff associated**

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## Growing Cyber Security Threat: Interview with Amit Yoran of NetWitness Corp.

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### with implementing a cyber security plan?

AY: In candor, it's pretty much all over the map. Some invest in "expert opinions" of what needs to get done, some follow the herd mentality of doing what other organizations are doing, some ignorantly view compliance as their objective instead of the effectiveness of their security programs, and some simply bury their head in the sand claiming that "security is not a problem" or that "my organization is not a target."

### Q: As networked-based technology becomes increasingly prevalent and cyber attacks become more malicious, the risk of consumers / end users unknowingly triggering a cyber event grows. What steps should be taken to better educate and train the end user?

AY: I'm all in favor of raising awareness of security challenges and training end users to increase their vigilance. I'm also pessimistic that the net effect of these awareness programs will lead to meaningful improvements in an organization's security posture. Ultimately, if the effectiveness of your security program requires good decisions to be made by end users, you are guaranteed to fail. Experience has taught us without exception that users will do what they can to bypass the protective measures we put in place for them. This game theory approach will yield better results than most awareness programs.

### Q: Given your previous role at the Department of Homeland Security (DHS), some have called you the "first U.S. Cyber Czar." From your experience in both the government and private sectors, what role should the government play in cyber security and how should it best partner with the private sector?

AY: The government can't do security for the entire nation, it simply doesn't work that way. It can help increase cyber security by providing some of the attributes required for free markets to succeed – specifically in the areas of transparency. For instance, the declassification and education of the market as to the true nature of the threat environment; an explanation of what security functionality and requirements are necessary to succeed; forcing transparency around breach notifications and gaining market visibility into the true cost of security failures; and identifying gaps in requirements where new focus can have meaningful impact. If greater transparency is applied to the market versus the fear, uncertainty and doubt of today, I believe rapid improvement can happen.

### Q: How do you view the various roles and missions between Cyber Command, DHS, Office of the Director of National Intelligence, etc. as it relates to protecting the .mil, .gov, and .com domains?

AY: These are very important topics that currently lack transparency and debate by an appropriately informed public.

There's enough work to go around, that's for sure. Until more is known about who is doing what and expectations are properly set, and what gaps still exist, it's hard to take great confidence in the federal government's cyber efforts.

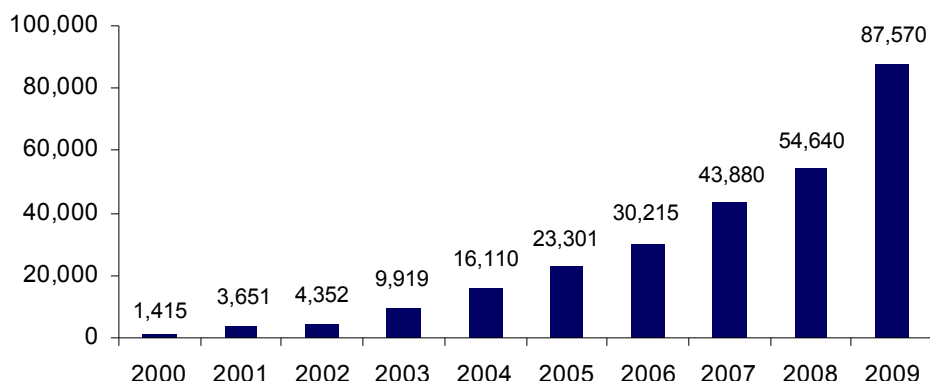
### Q: Having founded and managed your own cyber security businesses, what advice do you have for entrepreneurs seeking to grow their business in the sector?

AY: In cyber security, nuance matters. Make sure your technology is founded in solid engineering, your business plan doesn't require the ocean to be boiled all at once, and that the value you deliver to your customers is compelling. When you align those, and if the stuff really works, you've got a chance.

### Q: NetWitness recently partnered with a leading private equity fund, Summit Partners; how do you envision this partnership benefiting the company going forward?

AY: We've been growing at over 100% per year for the past three years and have been profitable for six quarters now. The investment by Summit allows us to continue our rapid growth and feel confident that we have the capital to sustain us as the numbers moving across our balance sheet get larger and larger. It also allows us to look at some related technology sets and consider expansion of our portfolio.

## Department of Defense Reported Incidents of Malicious Cyber Activity, 2000 - 2009



- Reported incidents of malicious cyber activity against the Department of Defense (DoD) increased by 24% in 2008 over 2007
- Although the figure has yet to be finalized for 2009, the DoD announced preliminary estimates that attacks would climb to 87,570 (based on actual incidents through June 2009), a 60% increase over 2008
- The U.S. Government has responded by creating the U.S. Cyber Command, an organization designed to coordinate the defense, protection, and operation of the DoD networks

Source: The U.S. - China Economic and Security Review Commission

# A New Season: Developments in the Aerospace and Defense Markets

Commentary by Lincoln International's Alyssa Morrisroe

The defense market has seen a significant shift in priorities, with numerous major programs in flux and / or killed in the recent budget. The F-22 went from being a key element of American military dominance to a dead program. The A400's future existence remains uncertain. The C-17, a platform which elicits extremely divergent views from various stakeholders, has received what may be a final blow, although Boeing is attempting to extend the program life by recently slowing its production line by a third and looking for foreign sales. The Future Combat System, which represented an anticipated major move forward in technology, has been dismantled, although certain areas will continue to be funded. Finally, there is still uncertainty over the future of the tanker program. Northrop recently removed themselves from the competition, and it is unclear whether EADS might pursue a challenge to Boeing on its own (see General's Mission Briefing Article below).

Two of the greatest beneficiaries of shifting priorities have been suppliers to Unmanned Aerial Systems and Cyber Security / Warfare participants, who have seen strong growth, and are likely to



continue to grow in future budgets.

In the commercial sector, the 787 test program appears to be gaining momentum, which is a welcome development for all industry participants. Despite widespread anticipation of cuts in aircraft build rates, Boeing and Airbus have signaled that they are planning to raise production rates in 2011.

## Implications for M&A

Major policy shifts generally create an environment of increased M&A activity, and that is already occurring, with recent headliner deals including:

- Triumph's acquisition of Vought Aircraft Industries

- Babcock International's agreement to acquire VT Group
- AAR's acquisition of Aviation Worldwide Services

After a 2009 characterized by a near freeze in acquisition activities, strategics across the A&D landscape are now pursuing acquisitions, with key demand drivers including:

- More real estate on growth platforms such as UAVs, the F-35, B787 and A380
- Enhanced technological capabilities, particularly in areas such as C4ISR, optics and composites

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## General's Mission Briefing



Brigadier General Bob Edmonds  
USAF, retired

Brigadier General Bob Edmonds is an Advisory Director in Lincoln International's Aerospace and Defense Group. He retired in 2007 from the United States Air Force after 28 years of service, including as an F-15 pilot and commander. His experience also includes leading the U.S. Air Force's Senate Liaison office on Capitol Hill after September 11, 2001 and serving as a White House Fellow.

### What to Watch: Federal Budget and Beyond

#### Freeze on discretionary spending announced in State of the Union

- National Security / DoD are exempt and, thus, defense spending will not be impacted, for now...
- Other agencies were part of the freeze...sounded good in the speech, but the reality is 10 of 15 cabinet departments saw their budgets increased in the FY2011 budget

#### Move to ban "earmarks" in the federal budget

- Much advertised effort by the House of Representatives...not supported in the Senate
- The status quo on adding budget line items used by members of Congress will not change

#### The DoD budget did not see a cut for FY2011, but many predict major challenges in FY2012 and certainly the FY2013 budget

- \$548.9 billion in the base budget
- \$159.3 billion for Iraq / Afghanistan
- \$17.0 billion for nuclear programs (primarily Department of Energy)
- 3.4% increase over FY2010 budget, but only 1.8% when adjusted for inflation; 4.7% of GDP

Implications of the Quadrennial Defense Review (QDR) on the budget: not really noticeable since most items had already been factored in over the last year; major issue will be the QDR's general theme calling for a "do it all" military (more emphasis on non-traditional defense missions and tasks)

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## General's Mission Briefing

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- Three main spending areas remain:
  - ▶ **Cyber**; some points to consider:
    - Are we moving into a Cyber Cold War – with multiple, non-state players? Is it cyber crime or cyber war? Who protects what?
    - Stand-up of Cyber Command slowed by debate on roles and missions...no commander confirmed yet (hearing scheduled for April 15th)
  - ▶ **Intelligence, Surveillance and Reconnaissance (ISR)**
    - Anything to do with Unmanned Aerial Systems, UAS (and new phrase Remotely Piloted Aircraft, RPA) will continue to be a growth area
  - ▶ **Global Supply Chain / Logistics**

### **New Obama Administration priorities in 2010 and beyond**

- FY2011 – First real Obama budget, but fiscal realities have yet to sink it with the Administration
- Post Scott Brown election and healthcare passage – where and how much domestic spending on priorities and which priorities? The American public is increasingly becoming concerned with Federal spending leading to huge debt.

***The national debt is, right now, the biggest threat to national***

### **security, and our way of life**

- How do we handle China in the future? Buyers of debt, beholden to China, do we change national security policy / declarations to assuage them?
- With the threat of interest rate increases, inflation, and a stagnating world economy, how do we pay for this debt and who pays?
- February 2010 – record monthly debt; some predict the debt will be 100% of GDP by 2019....that is not very far off

### **Issues to Keep in Mind Related to the DoD Budget**

1. Right after the Cold War was over, we took a procurement holiday on recapitalizing and buying new defense equipment; we are still in a holiday paying for the current conflicts
2. The current fiscal situation is not going to get any better with a \$1.3 trillion debt and baby boomers entering the peak years for retirement; personnel and health costs will continue to squeeze the procurement dollars out of the budget
3. We are having the wrong debate on security – terrorism is not the only and maybe not the major security threat, but we have allowed the nation to think of security in that myopic, narrow way

### **Implication of Northrop Grumman's "No Bid"**

### **Decision on the KC-X Tanker Program**

Northrop Grumman (NG) made the decision based primarily on financial reasons. Specifically, NG decided the U.S. Air Force requirements did not favor their offering, an Airbus A330-based tanker, making it more difficult to win the deal. Additionally, their EADS teammate's financial position is much different now than when they originally bid on the program. Implications from this decision include:

- Industrial base concerns, particularly for large aircraft programs
- No competition with only one bidder; difficult to ensure the DoD gets the best possible deal for the taxpayer
- Future teaming with NG – will other companies be more hesitant or was EADS really the driver in the NG decision not to bid? Insight to this question will be provided if EADS goes it alone and bids as the prime
- Trans-Atlantic defense cooperation – Future European involvement in U.S. defense procurements, which has certainly now been raised to the head of state level; President Sarkozy will be sure to raise the issue when he visits. The United States has traditionally sold more defense goods to Europe than vice versa (In 2008, the U.S. exported \$5 billion, and imported only \$2.2 billion of defense material from the EU); this no bid action comes on the heels of the U.S. cancellation of the Presidential Helicopter program, where Lockheed teamed with Finmeccanica / Augusta- Westland

## KC-X Tanker: Recent Developments



Illustration of KC-X Tanker

- **December 1, 2009:** Northrop Grumman threatened to boycott the KC-X tanker contest, claiming that the DoD showed a preference for an aircraft smaller than the A330-based tanker it had previously offered with Europe's EADS
- **March 8, 2010:** Northrop Grumman officially withdrew from competition
- **Result:** Boeing stands as the only confirmed bidder for the program and plans to offer 767-based tankers; the Pentagon has extended the bid deadline to July 9 (60 days past the original deadline) with the goal of eliciting a competing bid from EADS

## Public Comparable Trading Statistics

	Stock Price	52 Week		Enterprise Value	1-Year Growth		EV / LTM	
		High	Low		Revenue	EBITDA	Revenue	EBITDA
<b>Large Cap</b>								
BAE Systems plc	\$5.64	\$6.08	\$4.47	\$18,993	22.2%	(16.2%)	0.6x	6.6x
Boeing Co.	72.61	74.53	34.21	56,762	12.1%	(31.9%)	0.8x	16.0x
Bombardier, Inc.	6.16	6.17	2.87	14,210	(1.8%)	(17.5%)	0.7x	8.9x
Finmeccanica SpA	13.32	17.28	12.16	13,130	20.9%	13.9%	0.5x	5.2x
General Dynamics Corp.	77.20	78.62	40.78	31,284	9.2%	3.3%	1.0x	7.4x
Goodrich Corp.	70.52	72.80	35.69	10,042	(5.3%)	(11.8%)	1.5x	8.4x
Honeywell International Inc.	45.27	45.78	27.44	39,546	(15.5%)	(2.1%)	1.3x	9.1x
L-3 Communications Holdings Inc.	91.63	94.87	63.57	13,801	4.8%	4.5%	0.9x	7.4x
Lockheed Martin Corporation	83.22	87.19	65.21	33,558	5.8%	(9.3%)	0.7x	6.6x
Northrop Grumman Corporation	65.57	66.06	42.51	20,687	4.5%	(8.9%)	0.6x	6.4x
Precision Castparts Corp.	126.71	128.07	57.09	18,026	(18.7%)	(7.6%)	3.2x	11.2x
Raytheon Co.	57.12	58.30	38.00	21,452	7.4%	14.6%	0.9x	6.4x
Rolls Royce Group plc	9.05	9.33	4.38	15,191	14.7%	21.8%	1.0x	8.3x
Safran SA	26.01	27.01	9.19	12,018	2.6%	16.2%	0.8x	7.2x
United Technologies Corp.	73.61	74.85	42.06	75,546	(11.2%)	(7.0%)	1.4x	8.9x
<b>Mid Cap</b>								
CAE Inc.	\$9.81	\$10.03	\$6.54	\$2,784	(1.3%)	2.2%	1.8x	7.5x
Cobham plc	3.90	4.04	2.49	5,109	28.2%	36.5%	1.8x	9.1x
EADS	20.08	22.33	11.60	7,814	(1.0%)	(73.9%)	0.1x	5.5x
Elbit Systems Ltd.	64.07	74.23	51.53	2,862	7.4%	1.7%	1.0x	7.4x
GKN plc	2.10	2.16	0.69	3,737	(3.5%)	(11.0%)	0.6x	7.4x
Meggitt plc	4.64	4.82	1.89	4,458	(1.0%)	29.4%	2.6x	9.2x
Rheinmetall AG	71.10	72.13	33.39	2,738	(16.1%)	(54.9%)	0.6x	11.6x
Singapore Technologies Engineering Ltd.	2.28	2.41	1.61	6,746	3.8%	(3.0%)	1.7x	14.3x
Thales	40.06	48.52	36.92	8,127	1.7%	(56.9%)	0.5x	10.6x
Zodiac Aerospace SA	49.09	51.34	25.27	3,619	21.4%	(2.3%)	1.1x	9.6x
<b>Small Cap</b>								
Cohort PLC	\$1.39	\$2.79	\$1.14	\$52	17.0%	(19.8%)	0.4x	5.0x
LMI Aerospace Inc.	18.58	19.31	5.40	235	0.7%	(17.6%)	1.0x	8.2x
Magellan Aerospace Corp.	1.80	2.72	0.33	262	0.0%	5.7%	0.4x	3.6x
OHB Technology AG	20.39	24.71	8.90	315	34.0%	37.3%	0.7x	7.9x
QinetiQ Group Plc	2.04	2.72	1.84	2,047	16.6%	(7.8%)	0.8x	8.1x
Senior plc	1.68	1.68	0.42	827	(4.1%)	(6.9%)	1.0x	7.2x
Teledyne Technologies Inc.	41.27	42.87	26.00	1,721	(6.8%)	(10.8%)	1.0x	8.2x
Triumph Group, Inc.	70.09	74.73	34.36	1,528	0.3%	(1.1%)	1.2x	7.7x
Ultra Electronics Holdings plc	22.80	23.50	16.07	1,606	26.3%	31.4%	1.6x	9.7x

Notes:

1. Multiples for Boeing Co. reflect a one-time charge associated with the 787 program of \$2.5 billion. The charge reflects a reclassification of funds from inventory to R&D expense.

2. Data as of market close on 3/31/2010

3. All figures: USD in millions

## Select Recent Industry Transactions

- 3/29/2010: **Microsemi Corp. (NasdaqGS:MSSC)** announces the acquisition of **White Electronics Designs Corp. (NasdaqGM:WEDC)**, a manufacturer of defense electronic components and systems.
- 3/26/2010: **Diehl Stiftung & Co. KG** announces the acquisition of **Dasell Cabin Interior GmbH**, a developer and manufacturer of interior components and lavatories for aircrafts.
- 3/25/2010: **AAR Corp. (NYSE:AIR)** announces the acquisition of **Aviation Worldwide Services LLC**, a provider of expeditionary airlift services and aircraft modifications to the U.S. and other government customers..
- 3/23/2010: **Triumph Group, Inc. (NYSE:TGI)** announces the acquisition of **Vought Aircraft Holdings, Inc.**, a manufacturer of aero structure products for commercial, military, and business jet aircrafts.
- 3/16/2010: **Vought Defense Systems Corp. (OTCPK:VDSC)** announces the acquisition of **Cyber Aerospace, LLC**, a designer and manufacturer of Unmanned Aerial Systems for law enforcement, military, and commercial operations globally.
- 3/5/2010: **Sun Capital Partners, Inc.** completed the acquisition of **Protective Products of America, Inc.**, a manufacturer of ballistic protection for personnel and vehicles in the military and law enforcement markets
- 3/4/2010: **Orbital Sciences Corp. (NYSE:ORB)** announces the acquisitions of **General Dynamics Advanced Information Systems, Inc.**, a developer, manufacturer, and integrator or mission systems for defense, space, intelligence, surveillance, and homeland security.
- 3/2/2010: **RUAG Switzerland Ltd.** announces the acquisition of the **Helicopter Maintenance Division of Linth Air Service AG**, a provider of MRO services for helicopters throughout Europe
- 2/26/2010: **Bell Helicopter Textron Inc.** completed the acquisition of **Aviation Service Inc.**, a manufacturer and distributor of avionics systems to commercial and military aviation markets
- 2/19/2010: **L-3 Communications Holdings Inc. (NYSE:LLL)** announces the acquisition of **Insight Technology Incorporated**, a provider of night vision and electro-optical systems

# A New Season: Developments in the Aerospace and Defense Markets

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- Diversification of customer base, for defense contractors in particular

While significant questions remain on the future trajectory of defense spending and commercial demand, there is a general sense of relief in the marketplace at the relatively greater clarity in comparison to previous quarters. This is compelling

buyers, frequently those with large acquisition "war chests" and pent up demand, back into the market looking for high quality acquisitions.

The easing of tight credit markets, particularly for middle market deals, has also led to private equity firms' return to activity in the space. A&D has received strong attention from sponsors, given the tendency for companies in the industry to have strong visibility of revenue and cash flows. This trend is likely to increase as

credit markets continue to thaw.

In summary, the window of opportunity for sellers is once again open. We believe that there will be significant additional M&A activity over the coming twelve to twenty four months. For many acquirers, the deals done in this time period will shape their profiles and growth potential for decades to come.



## About Lincoln International

Lincoln International specializes in merger and acquisition advisory services, private capital raising and restructuring advice on mid-market transactions. Lincoln International also provides fairness opinions, valuations and pension advisory services on a wide range of transaction sizes. With ten offices in Asia, Europe and North America, and strategic partnerships with leading institutions in China and India, Lincoln International has strong local knowledge and contacts in the key global economies. The organization provides clients with senior-level attention, in-depth industry expertise and integrated resources. By being focused and independent, Lincoln International serves its clients without conflicts of interest. More information about Lincoln International can be obtained at [www.lincolninternational.com](http://www.lincolninternational.com).

## Industry Groups

Lincoln International dedicates teams headed by senior professionals in each of its global offices to the following industries:

- Aerospace and Defense
- Automotive and Truck
- Building and Infrastructure
- Business Services
- Chemicals
- Consumer
- Food and Beverage
- Healthcare
- Industrials
- Paper & Packaging
- Renewable Energy
- Transportation and Logistics

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