

CONFLUENCE OF SUPPLY AND DEMAND DRIVES GROWTH FOR C4ISR MARKET

C4ISR SECTOR UPDATE | NOVEMBER 2024



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PARTNERS**

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C4ISR

Confluence of Supply and Demand Drives Growth for C4ISR Market

KEY SECTOR TAKEAWAYS

Capstone Partners' Aerospace, Defense, Government, & Security (ADGS) Group is pleased to share its Command, Control, Communications, Computers, Intelligence, Surveillance, & Reconnaissance (C4ISR) report, with insights and analysis on sector trends, buyer activity, and public company performance. Middle market owner-operators have benefitted from a robust funding environment supported by heightened demand for defense electronics production. This has translated to the merger and acquisition (M&A) ecosystem where transaction volume has surged. Several key takeaways are highlighted below.

1. Transaction volume in the C4ISR sector has reached 44 transactions year to date (YTD), a 12.8% rise compared to the prior year period.
2. Defense electronics production has bolstered growth among middle market businesses and public company players, leading to favorable projections for the future of the space.
3. The U.S. Department of Defense (DOD) has established the Microelectronics Commons and Secure Enclave programs to support growing demand for defense electronics products.
4. Public companies in the C4ISR sector have generated healthy returns to-date, strengthening cash flows for potential future acquisitions.

Capstone Partners has developed a full suite of corporate finance solutions, including, financial advisory services, merger and acquisition advisory, debt advisory, and equity capital financing to help privately owned businesses and private equity firms navigate through each stage of a company's lifecycle.

To learn more about Capstone's wide range of advisory services and C4ISR knowledge, please [contact us](#).

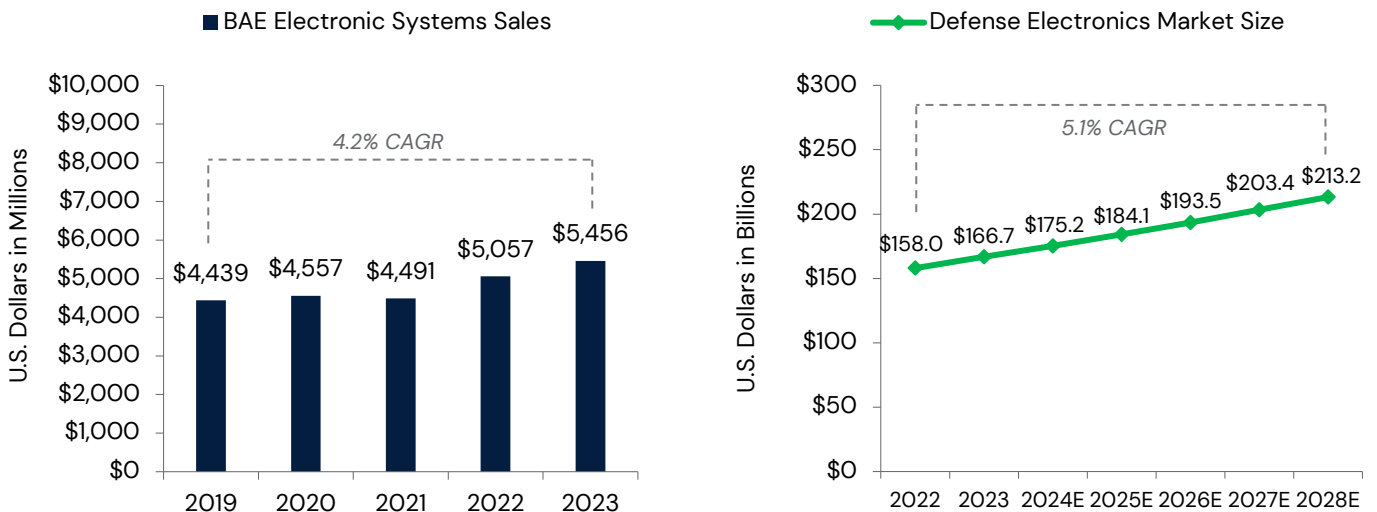
DEFENSE ELECTRONICS CREATE BASIS FOR SECTOR GROWTH

Defense electronics have served as the backbone of C4ISR sector production, connecting the space’s multiple end users and end markets through workable technology. While many large-scale DOD projects in recent years, such as the renamed Combined Joint All-Domain Command and Control (CJADC2) program and the Replicator Drone initiative, have propelled financial growth in the space, middle market players and sub-contractors have driven the bulk of sector consolidation. These businesses have continued to bolster both the supply chain for defense electronics and the subcontracting ecosystem, allowing prime contractors to maintain margin strength and allocate capital efficiently. The expected growth of the Defense Electronics market has reflected this reality.



The Defense Electronics market was valued at \$158 billion in 2022 and is expected to reach \$213.2 billion by 2028 through a compound annual growth rate (CAGR) of 5.1%, according to Markets and Markets Research.¹ This growth is likely to be supported both by capital-intensive projects such as CJADC2, and growing demand from the U.S.’ vast array of security partnerships including NATO (North Atlantic Treaty Organization), AUKUS (Australia, U.K., U.S.), Israel, Ukraine, Taiwan, and GCC (Gulf Cooperation Council) countries. Leading public players have experienced this growth including L3Harris Technologies (NYSE:LHX), which has won prime defense electronics contract awards for its Integrated Mission Systems (IMS) business segment. Notably, L3Harris’ IMS segment was awarded a five-year, \$587.4 million contract by the U.S. Navy to produce the Next Generation Jammer–Low Band (NGJ-LB) electronic warfare attack capability, according to a press release.² Public players in the sector have seen revenue increases in line with the Defense Electronics market’s projected growth. BAE Systems’ (LSE:BA.) Electronic Systems business unit has experienced revenue growth at an annual rate of 4.2% between full-year 2019 and full-year 2023, garnering \$5.5 billion in sales in 2023, according to an earnings report.³ As demand sharpens, public players in the space may turn towards consolidation to solidify market positioning and bolster competitiveness for new government contract awards.

BAE’s Electronics Systems Segment Poised to Track Defense Electronics Market Growth



Source: BAE Investor Relations, Markets and Markets, and Capstone Partners

FUNDING SPOTLIGHT: CHIPS AND SCIENCE ACT



U.S. Department of Commerce



U.S. Department of Defense

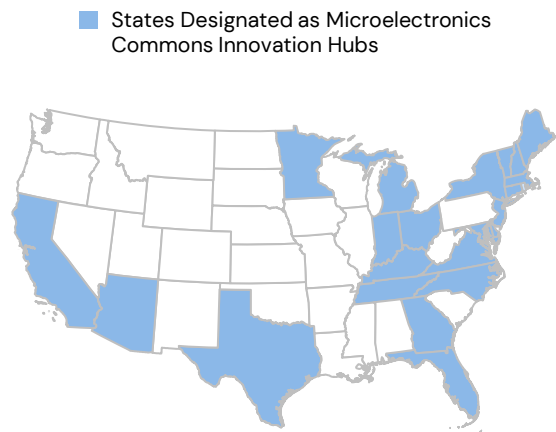


Sector Implications

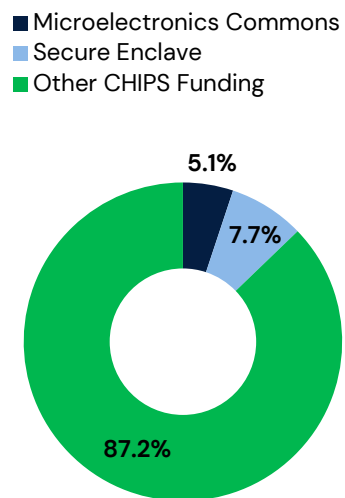
Significant funding for the Creating Helpful Incentives to Produce Semiconductors (CHIPS) and Science Act of 2022 has been routed from the U.S. Department of Commerce to the DOD for the explicit production of semiconductors and microchips for defense electronics applications. The two main DOD initiatives funded by the CHIPS act are the Microelectronics Commons program and the Secure Enclave program. These programs have been billed by the DOD as two separate functions in service of the same goal of microchip production. The Microelectronics Commons functions as the Research, Development, Test, & Evaluation (RDT&E) production arm, allocating funding to a network of universities and start-ups in order to create a “pathway to commercialization for U.S. microelectronics researchers and designers from ‘lab to fab,’” according to a DOD press release.⁴ The DOD received \$2 billion in funding from the CHIPS act for the program.

The Secure Enclave program represents the manufacturing arm of the DOD’s microchip initiative. When the CHIPS and Science act was being written, language was included to set aside funding for a “secure enclave” which would provide protection over the domestic microchip supply chain and produce chips specifically for the DOD and Intelligence Community (IC). In September, Intel (Nasdaq:INTC) was awarded a \$3 billion sole-source contract by the DOD and U.S. Department of Commerce to fulfill the “secure enclave” production of microchips for defense electronics, according to a press release.⁵ In total, funding for the Secure Enclave program constitutes 7.7% of the \$39 billion in total funds allocated for the CHIPS and Science act. While funding packages for the Secure Enclave and Microelectronics Commons programs have already been awarded, sector players are likely to benefit from fortified microchip supply chains and a faster time-to-market for defense electronics products.

Microelectronics Commons Draws Participation from Geographically Diverse Locations



CHIPS and Science Act Funding DOD Allocations vs. Total Funding

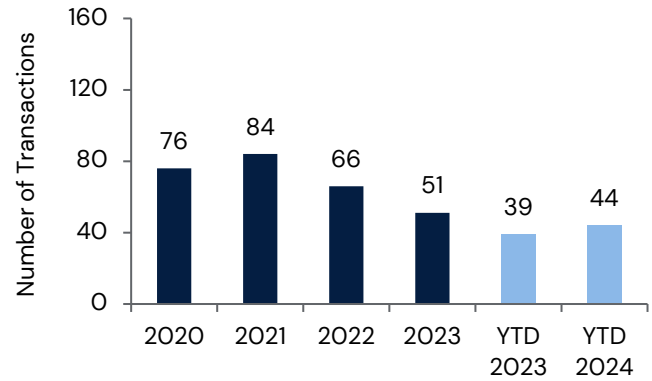


Source: U.S. Department of Commerce and Capstone Partners

C4ISR M&A VOLUME GROWS AS DEFENSE SPENDING BALLOONS

The C4ISR sector has experienced a surge in M&A activity with 44 transactions announced or completed through YTD, a 12.8% rise compared to the 39 transactions from the prior year period. Strategic competition with China and boiling geopolitical conflicts involving U.S. allies have hastened the pace of consolidation in the sector. While 2021 saw an influx of sellers looking to exit their businesses before a proposed capital gains tax was implemented, political uncertainty regarding the presidential election may again influence decision making among C4ISR owner-operators. Although political considerations for business owners may be hard to predict for M&A, robust and persistent defense spending is likely to drive continued consolidation in the space.

C4ISR M&A Transaction Volume Surges



Year to date (YTD) ended September 16
 Source: Capital IQ, FactSet, PitchBook, and Capstone Partners

Total federal spending on defense is likely to reach \$1 trillion in the near term. Although the Fiscal Responsibility Act of 2023 capped annual increases in defense spending at 1% through fiscal year (FY) 2025, the total budget for U.S. defense in FY 2024 has surpassed \$900 billion due to multiple supplemental funding packages for Israel, Ukraine, and Taiwan worth a total of \$95.3 billion, according to the House Appropriations Committee.⁶ This surge in spending, despite a cap on annual increases, has driven deal rationale for sector participants looking to move up-market in their contract acquisition pursuits. Notably, the merger between Jacobs’ (NYSE:J) Critical Mission Solutions (CMS) and Cyber & Intelligence (C&I) business units, and Amentum Holdings (NYSE:AMTM) in November 2023 (undisclosed), has provided an optimistic blueprint for contractors looking to bolster awards. The transaction, which closed in September 2024, formed Amentum Holdings as a new publicly traded company that expects to compete for large enterprise contracts in the Intelligence, Defense, and Civilian end markets of the Government Services space. The new company brings a combined contract backlog of \$47 billion and combined revenues of \$13.7 billion for FY 2024, which places the firm between Leidos (NYSE:LDOS) and Booz Allen Hamilton (NYSE:BAH) in terms of annual revenue, according to an investor presentation.⁷ This deal may signal opportunities for other sector players to gain significant market share from legacy operators through strategic consolidation and mission alignment across the Federal Government’s defense spending priorities.

C4ISR M&A Purchase Multiples Remain Healthy

Valuation Method	Average Revenue Multiple	Average EBITDA Multiple
C4ISR M&A Transactions (2021-YTD)	2.2x	13.2x
C4ISR Public Company Trading Multiples (LTM)	2.1x	17.0x

Source: Capital IQ, FactSet, PitchBook, and Capstone Partners

M&A purchase multiples in the C4ISR sector have slightly outpaced public company trading multiples on a revenue multiple basis, averaging 2.2x EV/Revenue between 2021 and YTD. Despite public companies in the sector outpacing M&A transactions on an EBITDA multiple basis, revenue may offer a more realistic valuation of middle market businesses in the space. Middle market C4ISR companies’ ability to win prime contracts and sub-contracts has often been highlighted as an important measure of a company’s growth profile and overall value. Notably, ITT (NYSE:ITT) acquired kSARIA, a radio frequency (RF) product manufacturer, in August for an enterprise value of \$475 million, equivalent to 2.7x EV/Revenue. The transaction represents the highest disclosed revenue multiple paid for a business in the C4ISR sector since TransDigm’s (NYSE:TDG) November 2023 acquisition of CPI International’s Electron Device Business (\$1.4 billion, 4.6x EV/Revenue).

NOTABLE M&A TRANSACTIONS



CACI (NYSE:CACI) announced its intent to acquire Azure Summit Technology in September for an enterprise value of \$1.3 billion. Azure is a leading designer and developer of a broad range of defense electronics products including the Switchblade family of digital signal processing cards, signal receivers, and tuning devices. These products have been primarily deployed across unmanned aerial vehicles (UAVs) in the U.S. military's arsenal. The company also produces a host of RF communication and direction finder (DF) geolocation devices.

"Azure Summit's core capabilities and technology bolster CACI's market-based strategy. When combined with more than \$400 million in share repurchases over the last six quarters, this transaction underscores CACI's flexible and opportunistic capital deployment approach, which focuses on driving free cash flow growth," said CACI CEO, John Mengucci, in a press release.⁸



Parsons (NYSE:PSN), a diversified solutions provider to the Defense and Intelligence end markets, acquired BlackSignal Technologies in July for an enterprise value of \$200 million. BlackSignal provides multiple services across the C4ISR landscape. This includes geolocation and tracking, signal detection and processing, machine learning, signal discovery, and electronics hardware manufacturing. In particular, BlackSignal is known for its signal processing products and services which detect and disrupt enemy command and control platforms.

This acquisition is expected to expand Parsons' DOD and IC customer base, while adding new counter-C4ISR capabilities. The acquisition is also consistent with Parsons' strategy of purchasing companies with greater than 10% revenue growth and EBITDA margins, according to a press release.⁹ BlackSignal is expected to be integrated into the Parsons Defense & Intelligence business unit.



Red Cat Holdings (Nasdaq:RCAT), a Puerto Rico-based drone technology company, acquired FlightWave Aerospace Systems in June for an undisclosed sum. FlightWave designs and develops unmanned Vertical Take-off and Landing (VTOL) drones, sensors, and associated software solutions. The company's main product line, the Edge 130, has been approved for sale to the U.S. military for the Pentagon's Replicator Initiative.

"Our Teal drones already bolster mission effectiveness and safeguard warfighters globally. The Edge 130 complements Teal with extended range and endurance, additional payloads and capabilities for maritime and other environments, and positions us to address the evolving requirements of the Pentagon's Replicator Initiative," said Red Cat CEO, Jeff Thompson, according to a press release.¹⁰ FlightWave's brand and product line has been integrated within Red Cat's unmanned C4ISR systems.



Sagewind Capital-backed Sigma Defense acquired Electronic Warfare Associates (EWA) in April for an undisclosed sum. EWA has been a prominent player in the field of electronic warfare and defense electronics for the past 47 years, according to a press release.¹¹ In an attempt to capitalize on funding for the Pentagon's CJADC2 program, Sigma Defense targeted EWA for acquisition due to its plethora of electronic warfare products including RF jammers and radar.

"The electromagnetic spectrum is a critical source of signature data that must be collected, analyzed, distributed, and acted on with speed, the same as all other elements of CJADC2. Understanding the full impact of electronic warfare attack and countermeasures is a critical component against a near peer adversary, so the alignment between EWA and Sigma Defense was a natural fit," said Matt Jones, Sigma Defense CEO, in the transaction press release.

SELECT M&A TRANSACTIONS

Date	Target	Acquirer	Target Business Description	Enterprise	EV/LTM	
				Value (mm)	Revenue	EBITDA
09/16/24	Azure Summit Technology	CACI (NYSE:CACI)	Operates a radio-frequency engineering company.	\$1,275.0	-	-
09/09/24	Oceaneering Intelligence Division	ShipTracks	Provides engineered services and products to the Energy, Defense, and Aerospace industries.	-	-	-
09/04/23	Tucson Embedded Systems	Precise Systems	Offers hardware and software engineering for flight-critical and safety-critical systems.	-	-	-
08/19/24	Criteria Labs	Ceramic Products Group	Provides semiconductor manufacturing services for defense and military applications.	-	-	-
08/14/24	Hera Systems	Redwire (NYSE:RDW)	Offers satellite information and analytics to perform space domain awareness missions.	-	-	-
08/07/24	Alastar	Cleartronic (OCTPK:CLRI)	Develops and operates an online situational awareness platform for public safety agencies.	-	-	-
08/01/24	kSARIA	ITT (NYSE:ITT)	Offers aerospace products, tactical products, and radio-frequency and microwave assemblies.	\$475.0	-	-
07/30/24	BlackSignal Technologies	Parsons (NYSE:PSN)	Provides C4ISR and electronic warfare solutions.	\$200.0	-	-
07/30/24	SyQwest	CTS (NYSE:CTS)	Manufactures a broad set of sonar and acoustic sensing solutions for naval applications.	\$125.0	-	-
07/16/24	LinQuest	KBR (NYSE:KBR)	Provides technical solutions to the U.S. government and Commercial industry.	\$745.0	-	-
07/11/24	FlightWave Aerospace Systems	Red Cat Holdings (Nasdaq:RCAT)	Designs and manufactures long-range sensors for VTOL drones.	-	-	-
06/27/24	High Point Aerotechnologies	Dzyne Technologies	Operates as a holding company for a group of businesses in the C4ISR sector.	-	-	-
06/20/24	Cobham Advanced Electronic Solutions	Honeywell (Nasdaq:HON)	Develops communications and sensor equipment for military and industrial uses.	\$1,900.0	-	-
06/18/24	SPYROS Information & Technology	Synergy ECP	Offers signals intelligence solutions to the Aerospace & Defense industry.	-	-	-
06/17/24	Stellar Blue	Wavestream	Provides connectivity network and electronics solutions for satellite networks.	\$245.0	-	-
06/13/24	EpiSys Science	Merlin Labs	Develops hardware and software systems for intelligence collection applications.	-	-	-
06/10/24	Par Government Systems	Booz Allen Hamilton (NYSE:BAH)	Offers geospatial C4ISR solutions for the U.S military.	\$95.0	-	-
05/28/24	Raptor Scientific	TransDigm (NYSE:TDG)	Provides electronic circuit testers for unmanned aerial vehicles and satellites.	\$655.0	-	-
05/27/24	Allegient Defense	BCS	Offers tactical communication and surveillance systems.	\$12.5	-	-

Source: Capital IQ, PitchBook, FactSet, and Capstone Partners

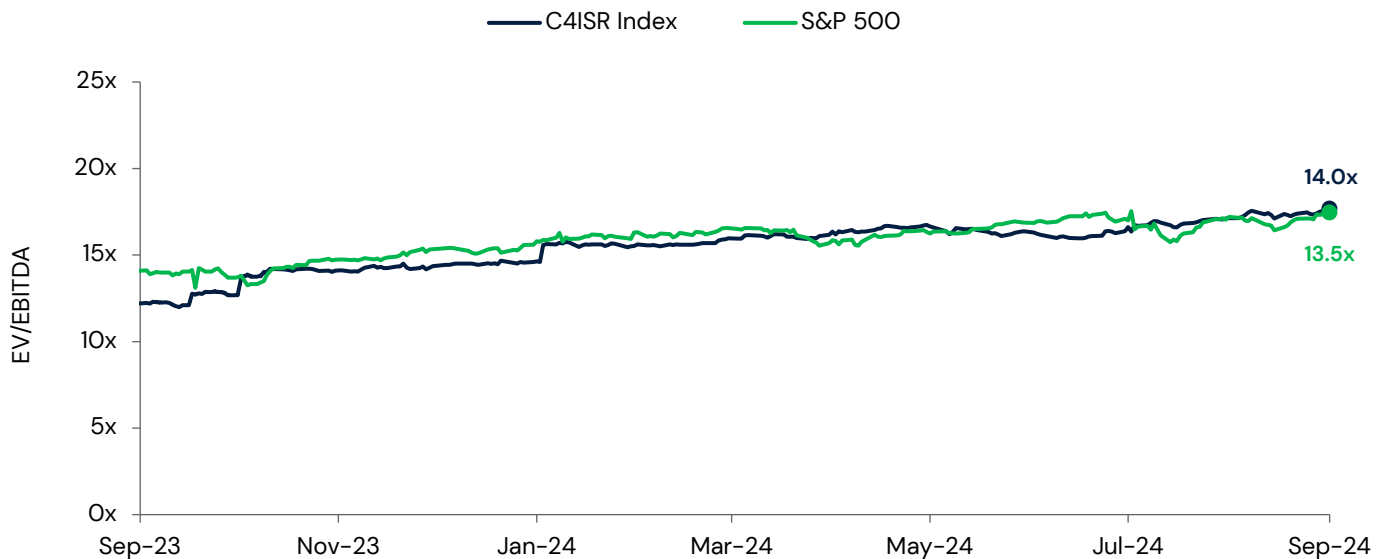
PUBLIC COMPANY DATA

Company	Price 09/24/24	% 52 Wk High	Market Cap	Enterprise Value	LTM			EV / LTM	
					Revenue	EBITDA	Margin	Revenue	EBITDA
Booz Allen Hamilton Corporation	\$159.86	97.2%	\$20,652.4	\$23,979.1	\$10,949.2	\$1,269.6	11.6%	2.2x	18.9x
CACI International, Inc	\$491.45	98.7%	\$10,961.1	\$12,746.2	\$7,659.8	\$891.3	11.6%	1.7x	14.3x
General Dynamics Corporation	\$308.09	99.4%	\$84,520.3	\$94,277.3	\$44,946.0	\$5,559.5	12.4%	2.1x	17.0x
Hexcel Corporation	\$62.22	80.7%	\$5,086.4	\$5,799.9	\$1,849.7	\$363.7	19.7%	3.1x	15.9x
Jacobs Solutions, Inc.	\$148.33	96.0%	\$18,429.8	\$21,552.0	\$16,948.6	\$1,476.3	8.7%	1.3x	14.6x
Leidos Holdings, Inc.	\$159.68	99.6%	\$21,511.1	\$25,905.1	\$16,008.0	\$1,901.0	11.9%	1.6x	13.6x
L3Harris Technologies, Inc.	\$237.73	96.8%	\$45,098.6	\$57,867.6	\$20,765.0	\$3,686.0	17.8%	2.8x	15.7x
Lockheed Martin Corporation	\$580.51	99.8%	\$138,369.2	\$155,103.2	\$71,069.0	\$10,167.0	14.3%	2.2x	15.3x
Northrop Grumman Corporation	\$533.14	99.7%	\$77,969.2	\$92,532.2	\$40,764.0	\$4,304.0	10.6%	2.3x	21.5x
RTX Corporation	\$120.27	97.2%	\$159,727.9	\$198,978.9	\$72,417.0	\$9,217.0	12.7%	2.7x	21.6x
Science Applications International Corporation	\$137.78	94.9%	\$6,822.9	\$9,063.9	\$7,297.0	\$643.0	8.8%	1.2x	14.1x
TransDigm Group Incorporated	\$1,417.98	99.6%	\$79,564.8	\$98,098.8	\$7,606.0	\$3,774.0	49.6%	NM	26.0x

Mean	15.6%	2.1x	17.0x
Median	12.4%	2.1x	15.7x
Harmonic Mean	12.8%	1.9x	16.0x

EV = enterprise value; LTM = last twelve months
 \$ in millions, except per share data
 NM = Not Meaningful

C4ISR Index Average EBITDA Trading Multiple Keeps Pace With S&P 500



C4ISR Index includes: BAH, CACI, GD, HXL, J, LDOS, LHX, LMT, NOC, RTX, SAIC, TDG; market capitalization weighted
 Source: Capital IQ and Capstone Partners as of September 24, 2024

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Tess is a Managing Director with over 30+ years of experience in the Aerospace & Defense industry, government policy arena and Financial Services sector. Tess has deep domain knowledge and transaction advisory skills, especially in the high-growth markets of Command, Control, Communications, Computers, Intelligence, Surveillance and Reconnaissance (C4ISR), and the Air, Land, Sea, & Space (ALSS) sector.

Prior to Capstone, Tess founded the Aerospace & Defense practice at a middle market boutique investment bank, focusing on private and public corporate clients with diverse products such as command and control software for aerial drones, satellite-based force tracking systems and electronic warfare devices used in Afghanistan and Iraq. She was Global Head of Equities Strategy at Lehman Brothers, responsible for strategy development leveraging competitive intelligence, market analysis and acquisitions across Americas, Europe and Asia. Transactions included investments in stock exchanges, a NYSE specialist market-maker and international broker dealers. Tess was also Director of Corporate Development and Strategy at Raytheon, with deal team transactions valued at over \$3.4 billion in sensor automation/information synthesis, geospatial mission support, network forensics, interoperable communications for homeland security, and commercial aviation/life cycle support. She holds a PhD in War Studies from Kings College London, an MA in Law & Diplomacy from Harvard's Kennedy School of Government, and a BA in International Relations from UCLA. A recognized industry expert, she was honored with deal awards, such as M&A's Most Influential Women 2021, M&A Atlas Awards for Industrials 2019, and M&A Advisor, Corporate / Strategic Deal of the Year 2018. She has also spoken at Thompson Reuters A&D Summit, Int'l AUVSI Conferences, New York Capital Roundtable and on a tv interview on ABC's Government Matters. She serves on the Board of the U.S. Navy League – CT Council.



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Hilary is a Vice President in the Aerospace and Defense group, bringing over 10 years of experience spanning investment banking and equity research. Prior to Capstone Partners, Hilary worked as a Vice President on the Textile Manufacturing team at Lehman Brothers. She has significant public company expertise with a focus on Industrials and Manufacturing M&A and carve-outs. She has also worked on numerous strategic advisory and company valuation assignments. Hilary earned a BBA in International Finance & French from Texas Christian University, M.J. Neeley School of Business. She is a Series 79 Registered Investment Banking Representative.



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FIRM TRACK RECORD

Capstone’s Aerospace, Defense, Government & Security Group has represented numerous companies that serve the needs of federal, state and local or foreign governments, as well as the needs of civilian and defense-related agencies. We understand the nuances associated with sole-sourced, multi-year or subcontracted awards, the value of partnerships, Governmentwide Acquisition Contracts (GWACs), Indefinite Delivery Indefinite Quantity (IDIQs), and General Services Administration (GSA) schedules. We have completed transactions requiring complex Committee on Foreign Investment in the U.S. (CFIUS) filings, International Traffic in Arms Regulations (ITAR) registrations and contract negotiations, and those involving classified information. Our advisory work has included multiple industries and involved companies of diverse specialties, many of which sell in both the public- and private-sector markets.



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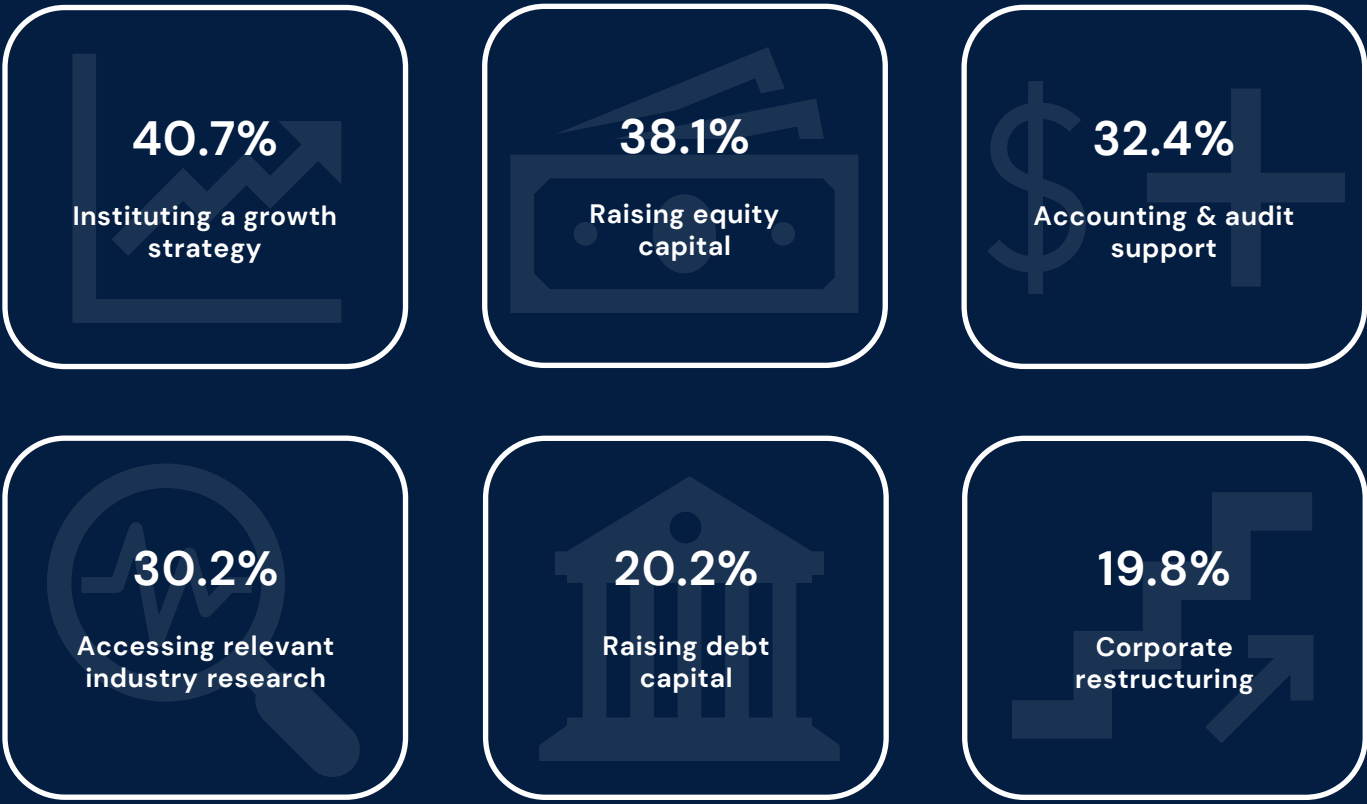


CAPSTONE’S PROPRIETARY RESEARCH REVEALS TOP SERVICES IN DEMAND

The stage and initiatives of a business often dictate which financial services are in demand. As the bulk of CEOs polled in Capstone’s 2024 Middle Market Business Owners Survey indicated growth strategies are a priority for 2025, the lion’s share (40.7%) of owners anticipate a need for growth strategy support services. Similarly, 38.1% of CEOs require equity capital advisory services to support operational initiatives and business expansion. Nearly one-third of owners require accounting and audit support to shore-up cash flows and establish financial stability. In addition, 30.2% of CEOs demonstrated an interest in accessing relevant industry research to keep up with emerging industry trends, complete competitor analyses, and track capital markets activity in their space.

Capstone has developed a full suite of [corporate finance solutions](#) to help privately owned businesses and private equity firms through each stage of the company’s lifecycle, ranging from growth to an ultimate exit transaction. In addition, we developed specialty advisory practices to provide financial performance, buy-side, employee stock ownership plan (ESOP), and equity and debt services. All of these capabilities are supported by 12 industry banking groups, an active sponsor coverage group, and a dedicated Market Intelligence Team.

Top Financial Services Required by Business Owners in 2025



*Question: Have you ever had, or do you anticipate having, a need for any of the following services?
Source: Capstone Partners’ Middle Market Business Owner Survey, Rebased Sample Size (N): 278*

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Disclosure

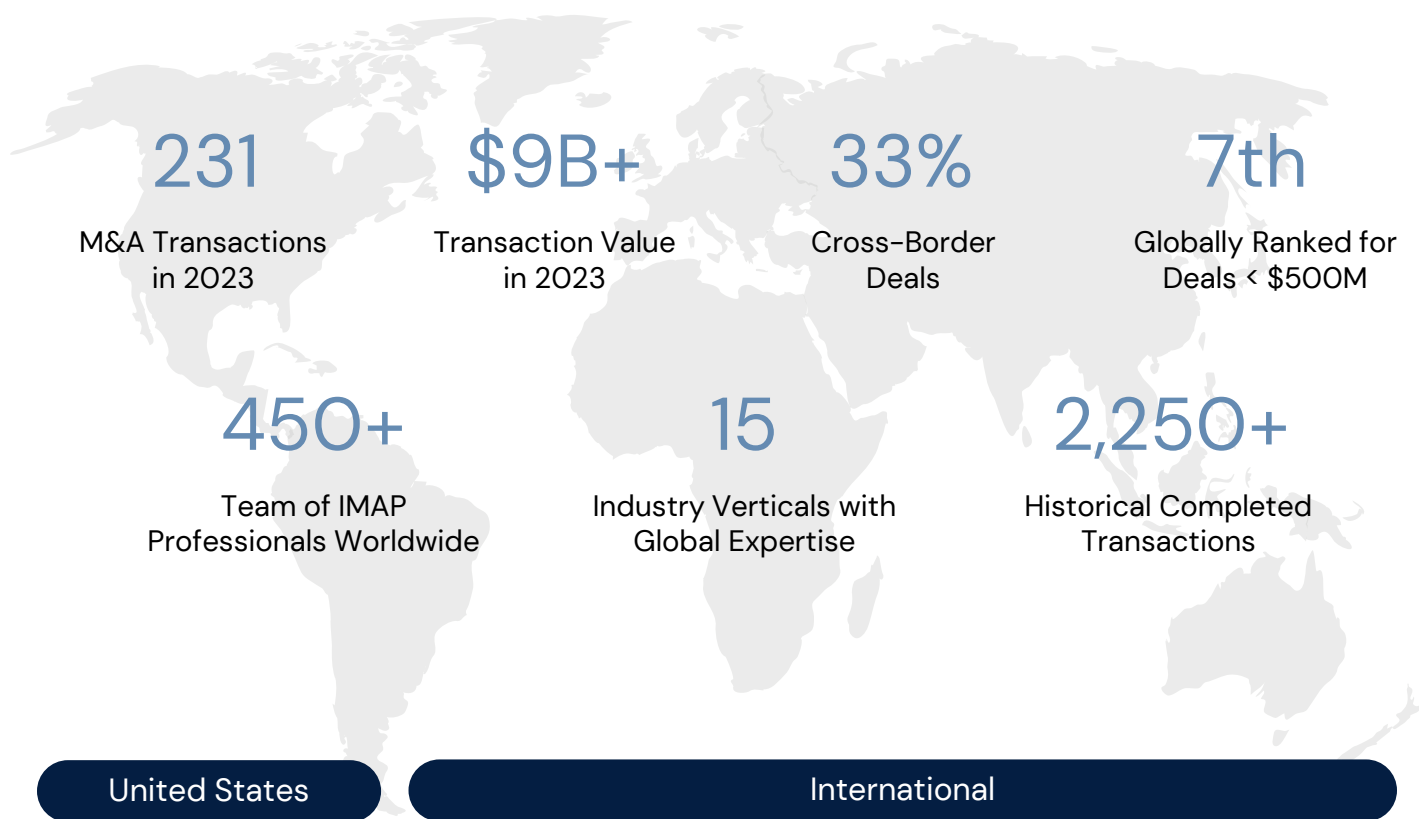
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