

Industry consolidation or bar brawl?

By Steve Townes
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Not long ago, I was on the phone with Paul Richfield, *Pro Pilot's* executive editor. We were talking about consolidation in the aviation services industry and Paul wondered if it meant new opportunities for smaller companies.

I don't think so. Industry consolidation rewards aggressive, testosterone-fueled behavior—just like a bar brawl, where a good big man beats a great little man almost every time. The fact is, size matters. Scale matters. Deep vertical capabilities are important. Having a wide variety of those capabilities helps, too. Consolidation, over time, tends to lock out the smaller companies at the bottom.

Look at each segment of the aerospace and aviation industries—you'll see consolidation in progress. Consultants, watching safely from the sidelines, and those in the thick of the fight, divide the process into 4 stages. During Stage 1, everybody crowds around the bar, jockeying for position and throwing the occasional elbow.

Drinks, courtesy of the capital markets, flow freely. This stage is becoming a dim memory for the aviation services industry, as is Stage 2, when consolidators make their move, cutting in on the dance floor and waltzing off with key customers.

Now we're in the opening days of Stage 3, marked by blockbuster deals and large-scale consolidation in many aviation segments. The big boys and the chains have taken over the place. They sit at the best tables and discuss how to divvy up the take, while their smaller rivals squabble over who gets the folding chair behind the column next to the men's room. During this time, savvy patrons should be gearing up for Stage 4.

In Stage 4, consolidation has left the bar with fewer and larger players. The marquee merger opportunities are gone and the strategic options are limited. So what happens next? The handful of oversized bruisers still in business toast their success, then maximize cash flow, build walls around market share and pursue incremental improvement.

Some experts list 3 strategies for coping with consolidation—be a buyer, be a seller or develop an incredibly defensible, tightly-defined niche. If that last choice is driven by pride more than differentiation, it won't buy you much besides a little time. My advice? Buy until you can't buy any more and then sell. Or just sell and then either start something new or head for the door.

If you plan to buy, keep in mind that consolidating companies and running them are 2 different things—and we've all seen how easy it is for bean counters to screw up perfectly good acquisitions. You'll need to be skilled at combining corporate cultures and reassuring jittery customers.

People take mergers personally, which means their foremost concern is how it will affect them. How you handle the inevitable personnel challenges can deter-

mine the stability of your customer relationships. Doing it right is a delicate leadership task. You'll also need access to capital, whether you go to the public or private equity markets, the bond market or a bank. Regardless of which option you choose, you'll be dealing with another constituency.

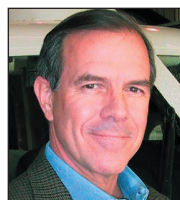
It could be venture capitalists looking for a liquidity event or bankers eyeballing quarterly results, but you'll be held accountable whatever way you go. If you have the right combination of value-adding management and capital resources, buying is a proven way to build long-term value. Just be prepared for non-stop financial second-guessing.

Most companies in this industry don't have access to the resources it takes to be a buyer. Their best choice may be divestiture. If you're looking to sell, the bad news is that you missed the best time to do it, which was Stage 2, when competition between buyers drove acquisition multiples higher. There are still opportunities, but with more buyers intent on absorbing earlier acquisitions, those multiples are dropping.

If you sell, expect extremely thorough due diligence—painfully thorough. Think of it as "corporate proctoscopy." If your valuation doesn't sync up with the analysis, you'll have another conversation about price but with less leverage. Make sure your valuation is based on an honest, objective assessment. This isn't a job for you or anyone in your organization. You need experienced CPAs and expert advisors—professionals immune to institutional optimism.

If you do decide to stay independent, odds are you'll be outfought. Large, well-capitalized companies will be coming for your market share, armed with the equivalent of ice picks and pool cues. You'll be up against sheer mass, economies of scale and value-added services. Stay close to your customers. They may actually prefer to deal one-on-one with the owner of a highly-specialized operation. Make sure your employees are content. Chances are they'll be nervous about their own job security.

So what happens after Stage 4? This is a gigantic industry, so vast and far-flung that, on any given day, one end consolidates while the other fragments. About every 5 to 10 years, those poles reverse. Big players spin off subsidiaries, move into other segments and start the process again. If you're running an aero services company, pick a fight you can win or head for the fire exit. Judging from the number of guys still in there swinging or lights-out on the floor, it's a wild time to be in the business. Just remember, don't hesitate if somebody yells, "Duck!" ✈



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