

Brazil's Global Player

Embraer Sets Sights on Growth in Defense Sector

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LONDON - Take a regional flight from an airport in the U.S., Europe or Asia and there's a good chance you will be flying on a jet developed and built by Embraer.

In little more than a decade, the Brazilian company has grown from a state-owned aerospace also-ran into a privatized global player in the regional and business jet markets.

Now Embraer is turning its attention to defense and security. It has high hopes for growth in the business unit it created last year to pursue its ambitions in the sector, Luiz Carlos Aguiar, the first president of the new Embraer Defense and Security operation, said at the recent Latin American Aerospace and Defense (LAAD) show in Rio de Janeiro.

"By the end of the decade, we want to grow business in the sector to represent 20 percent of total Embraer revenues, taking into account our other businesses are going to also grow," Aguiar said.

In 2010, defense accounted for revenues of \$670 million, 12.5 percent of the company's \$5.5 billion in annual sales.

On top of sales, Embraer reckons its aviation support services business last year earned military revenues of \$150 million. Much of that came in Embraer's traditional military markets involving the Super Tucano trainer and light attack aircraft and various adaptations of civil jet airliners into specialist platforms for airborne early warning and other tasks.

The company also is heavily involved in modernizing Brazilian military aircraft, including A-4 fighter jets for the Navy and AMX and F-5 fighters for the Air Force.

Still, company officials said, the traditional airframe business will continue to provide the core of Embraer's defense and security business for the foreseeable future.

The company is developing the KC-390, a jet-powered rival to Lockheed Martin's C-130 Hercules airlifter, and will also assemble a new fighter jet if the Brazilian government ever gets around to picking a winner.

The KC-390 is being built for the Brazilian and other air forces; first flight is scheduled for 2014.

The company also is expecting a decision from the U.S. Air Force (USAF), which is choosing between the Super Tucano and Hawker Beechcraft's AT-6 for a light attack requirement.

That could mark Embraer's long-sought foothold in the U.S. defense market. Company officials thought they had one when the U.S. ordered the ERJ-145 in 2006 as a surveillance aircraft, but that deal was canceled through no fault of the Brazilian company.

Now its U.S. priority is the light attack requirement.

"It's very important to win this campaign," Aguiar said. "We did a great job in the U.S. when we demonstrated our capability, and it's very well rated by the USAF. Better relations following [U.S. President] Barack Obama's visit here will help the process a lot."

If it wins, Embraer has a deal with contractor Sierra Nevada, an aerospace company based in Sparks, Nev., to build the aircraft.

Embraer also is transforming more generally under the government's 2008 national defense strategy to bolster local industries.

The first four months of operation at Embraer Defense and Security has seen the business already signal the intended direction of travel with moves to acquire radar, unmanned air systems and C4I and systems integration capabilities.

Much of that change became evident at the LAAD show, where in the space of two days, Aguiar announced the he had struck a deal with Elbit Systems' local subsidiary AEL Sistemas to jointly develop tactical UAVs, and then acquired 50 percent of local systems integration and C4I provider Atech Negocios em Tecnologias.

Part of the deal with Elbit, an Israeli company, involves Embraer becoming a minority stakeholder in AEL itself.

A few weeks earlier, Aguiar, who had previously been Embraer's chief financial officer, made the new business unit's first acquisition when it took a 64.7 percent stake in the radar division of Orbisat.

The UAVs, radar and particularly Atech's capabilities all reinforce a key Embraer objective to secure the lead position on a pair of massive Brazilian land border and maritime surveillance programs.

Together worth around \$10 billion, the first of those programs could kick off next year and run for the next decade.

Uncertainties There are some uncertainties about the timing of these and other defense programs with the new government of Brazilian President Dilma Rousseff reviewing major requirements here, including the long-running scrap between Boeing, Dassault Aviation and Saab for the fighter deal.

This year's defense budget has taken a big hit, and although the cut is said not to be directed at programs, executives at LAAD were nervous about the collateral damage the cutback could cause.

Rebecca Barrett, Forecast International's Latin American military markets analyst, said that Brazil needs to protect its strategic interests.

"This should be reflected in the defense budget and government's spending pattern during the Rousseff administration," Barrett said. "In that regard, programs that will be used for surveillance and the protection of Brazil's borders and off-shore oil assets will be top priority."

The analyst said the Brazilian defense budget for next year is set at 60.2 billion real (\$38.4 billion). Forecast International says that figure will rise moderately to 64 billion real by 2015.

Aguiar told reporters at LAAD that, for the short term at least, Embraer's main focus would be on building the business at home rather than buying foreign assets.

"Acquisition has not traditionally been how Embraer has grown," Aguiar said. "Acquisition in country is a good way of learning as it is easier to do something close to us. We have a small team looking [at M&A opportunities], and not only in Brazil, but there is nothing in the short term."

Embraer

Headquarters: São Paulo, Brazil

Employees: 17,000

2010 revenue: \$5.5 billion total; \$670 million in defense revenue, including \$150 million from military aviation support services.

Source: Defense News research

<http://www.defensenews.com/story.php?i=6315481&c=FEA&s=BUS>