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Parts suppliers brace for aircraft orders boom

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At the recent Paris Air Show aircraft manufacturers added hundreds more orders to their swollen backlogs, but the supply chain is already showing signs of stress, prompting leading executives to worry whether they will be able to meet surging demand.

Already Boeing Co. (BA-N 72.67 -0.22 -0.30%) and Airbus SAS are dramatically increasing the production rates of their existing single-aisle aircraft even as they bring online capacity to build new models and new competitors enter the fray.

Over the next five years analysts at Forecast International expect production of commercial and military aircraft to jump more than 50 per cent to 4,870 units in 2016, as the global economy recovers and travellers return to the skies.

For individual suppliers to specific programes the jump in production is likely to be even more dramatic. Analysts with RBC Capital Markets expect Boeing to deliver six 787 aircraft this year but 33 aircraft next year and 108 in 2015.

"We are ramping up all our programs and so is the competition and the new entrants," Tom Enders, chief executive of Airbus, told the Financial Times. "We watch this carefully … because one bad supplier can stop the entire production line."

For Boeing the stakes are particularly high. In 1997, the company tried to double production of its 737 family in 18 months and failed. Parts and material shortages forced Boeing to shut down production for a month and take more than $1.5-billion (U.S.) in charges.

"There are a lot of scars in the Boeing company," Jim Albaugh, head of Boeing's commercial aircraft unit, admitted recently. "We got in trouble because we hadn't verified that the supply chain was ready."

This time round, Mr. Albaugh says the company is doing just that, spending time talking with suppliers to make sure that they have "the people, the processes, the tools" they need – what one executive describes as "homework checking".

For now the preparation seems to be paying off. Craig Arnold, vice-chairman of Eaton, which makes hoses, couplings and other parts for aircraft such as the 787, says that his company is well able to handle a 15 per cent annual increase in production within its existing footprint.

Mr. Arnold argues that there is sufficient spacing between major programs to allow the supply chain to respond to the production increases. "Too many of them are late quite frankly but the pacing is different," he says.

Indeed, long cycles and production delays have given companies such as Allegheny Technologies, which makes metals for the aerospace industry, plenty of time to expand its capacity.

After heavy investments over the past few years, by the end of 2011 the company will be able to churn out about 47 per cent more titanium products compared to the prior peak in 2007 and 13 per cent more nickel alloys, says Dan Greenfield, head of investor relations.

Productivity improvements and innovations in material science should give the company even more flexibility, Mr. Greenfield says, because new alloys and pressing techniques lead to less waste.

Erik Paulhardt, vice-president of aerospace and defence for The Timken Co., which makes bearings and other components, has also expanded capacity.

But he argues that improved communication between customers and suppliers will be even more crucial in preventing shortages, by reducing the uncertainty that leads some companies to over-order.

"Historically, we haven’t done a good job of working collaboratively, but if you eliminate the noise [from double ordering, and so on] then there should be enough capacity to meet demand."

Elsewhere in the supply chain early signs of stress are showing. Lead time for delivering components made from titanium and nickel alloys, crucial for jet engines, have more than doubled over the past year or so because of heavy demand for raw materials.

"It’s a Catch-22," Mark Donegan, chief executive of Precision Castparts, a key supplier of forged components, told investors at the end of May. "On one hand we’re getting shorter cycles from our customers and [on the other hand] the lead times are going out."

While PCP has the bricks and mortars in place, Mr. Donegan warns that getting hold of the right people is more difficult. "As strange as it is and as much as you see the unemployment rates, there's not people standing at the door … So what we've been really trying to reinforce to our customers is you've got to give us some time to step up."

Rob Stallard of RBC Capital Markets says that despite the efforts to work together, suppliers and their customers are often at odds over when to hire or build up stocks. "No one wants to be the one left holding the inventory hot potato. You are always trying to keep it with someone else."

As production rates exceed previous peaks, Mr. Stallard expects manufacturers to find things tougher. "The industry will cross the line in the next 12 months and then it goes into uncharted territory pretty soon after that."

And in spite of all of the preparation, Mr. Arnold notes that typically it is "what you don't know that bites you. The stuff that we can think through, we are putting plans in place. If you get in trouble it is likely to be something that you didn't anticipate."

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