

CEO: Sikorsky 'not as attractive' as UTC siblings

Alexander Soule and Dan Freedman

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While describing Sikorsky Aircraft as having "a great future ahead," the CEO of United Technologies Corp. said on Thursday a decision to divest the Stratford-based company would be driven in part by uncertainty over future military sales and the pressure on profits exerted by the Pentagon.

On Wednesday, UTC (NYSE: UTX) announced its board is reviewing strategic alternatives for Sikorsky Aircraft, possibly to include offering its ownership interest in an initial public offering of stock or the sale of the manufacturer to another company.

Sikorsky employs more people in Stratford than any single private-sector site in Connecticut, with some 8,000 employees in Stratford, Bridgeport, Shelton and Trumbull combined, and a small lab in Stamford focused on emerging innovations. Of nearly 15,300 employees globally, about 12,470 are based in the United States.

In a Thursday meeting with investment analysts, UTC CEO Greg Hayes said Sikorsky's profile as a "platform" company results in lower margins than its sibling "systems" businesses Pratt & Whitney and UTC Aerospace. As an example, he cited the profit potential of Pratt & Whitney's PurePower, which are geared turbofan jet engines that UTC can price at a premium due to their lower noise and fuel consumption.

Last December, Louis Chenevert stepped down as CEO of UTC, with Hayes saying he would steer UTC units to higher profit margins going forward.

Sikorsky's sales totaled \$7.4 billion last year with a 2.9 percent operating margin.

Hayes noted that over the years, UTC has a record of selling off non-core businesses that no longer fit the growth portfolio the conglomerate has sought, including fuel cells, rocket engines and others.

`They ran the table'

Though "not quite as attractive" as UTC's other aerospace and building technologies businesses from a growth and margin profile, in Hayes' words, he said Sikorsky would nevertheless be ranked in the Fortune 500 as an independent company.

"Obviously, the helicopter business has its ups and downs," Hayes said. "They ran the table last year as far as contract wins."

Hayes said UTC management was mindful of the long horizon for volume production of Sikorsky's big CH-53K helicopter in development for the U.S. Marine Corps. Sikorsky is expected to start flight tests of the CH-53K this year but full production is not expected until well after 2020, with Hayes suggesting Sikorsky sales would be flat until then.

Sikorsky is also developing the high-speed S-97 Raider as a potential military helicopter prototype for a range of missions, to include armed reconnaissance and utility transport, with flight tests also expected this year.

"The question is, between now and then, how are you going to survive?" Hayes said.

`No danger'

Sen. Richard Blumenthal, D-Conn., a member of the Senate Armed Services Committee, said he was "bullish" on the future of Sikorsky and its Stratford plant.

"There should be no job impact from any possible spinoff or other change in corporate status, because there's plenty of work in combat rescue helicopters, Marine One and the Turkish helicopter deal," he said, adding he would be "deeply troubled if there are any employment consequences for this deal."

Carl Woog, deputy assistant for communications to Secretary of Defense Ashton Carter, said the Pentagon would have no comment.

Defense analysts agreed that while the U.S. military is in the midst of downsizing and the future of military rotary helicopters is uncertain, Sikorsky's Stratford plant should be able to survive.

"There's no danger that the Stratford plant will close," said Loren Thompson, a veteran analyst and CEO of the Lexington Institute in Arlington, Va. "Sikorsky is a solid business, but with limited growth prospects through the end of the decade." Unlike the Navy and Air Force, which have put much of their dwindling pile of chips into new weapons systems and technologies, the Army -- Sikorsky's main Pentagon customer -- is more focused on keeping its soldiers in uniform, Thompson said.

"The uncertainty about Sikorsky's future is traceable directly to the collapse in Army demand for helicopters," Thompson said. Nevertheless, he added, Sikorsky can survive on upgrading and refurbishing helicopters currently used by the Army and the Marine Corps.

Interesting prospects

UTC's announcement of the potential divestment of Sikorsky did not come as a surprise to analysts, with rumors cropping up from time to time over the years, according to Ray Jaworowski, senior aerospace analyst with Forecast International in Newtown. What was new Wednesday, Jaworowski said, was the suggestion that UTC would consider spinning off Sikorsky as an independent company rather than selling it to another conglomerate.

Two names he found particularly interesting as potential buyers: Lockheed Martin, which has long provided systems for Sikorsky helicopters and which already builds fighter jets in Texas; and the Bell Helicopter division of Textron, with Jaworowski saying Bell's aircraft lineup is significantly slanted toward civilian and light military applications, reducing overlap with Sikorsky's dominant military models like the Black Hawk.

There is recent precedent of a conglomerate selling off an aircraft division as an independent company, but it did not go well. In 2006, Massachusetts-based Raytheon sold Hawker Beechcraft to Goldman Sachs and other investors. With civil aviation sales plummeting following the 2008 financial crisis, Hawker Beechcraft in 2012 filed for bankruptcy and Textron acquired the business last year, combining it with its Cessna airplane division.

Andrew Philip Hunter, a fellow at the Center for Strategic & International Studies who was a senior Pentagon official in acquisitions between 2011 and 2014, said that Sikorsky's production of several brand-name helicopters -- the Black Hawk and Marine One, which carries the president -- should help it weather the storm.

He pointed to Huntington Ingalls Industries, the Virginia-based Navy shipbuilder, as a possible model for what might happen to Sikorsky if it goes the spinoff route.

Northrup Grumman spun it off in 2011 and the company has done well on its own because of its lock on construction of Navy aircraft carriers. Also, it is one of only two builders of nuclear powered submarines.

"Sikorsky is not quite as secure; it does have competition," Hunter said. "But on the other hand, the Black Hawk has been a successful system for so many years. They have a market niche that can be tough to beat."

`Huge player'

Hayes said UTC would not contemplate any spinoff of Sikorsky that would burden it with excessive debt.

A Lockheed Martin spokeswoman declined comment; Textron spokesman Dave Sylvestre said he could not speak on merger speculation, while noting Sikorsky's and Bell's competition for the future of military rotorcraft playing out within the Pentagon's walls.

"Obviously, they are a huge player in the market and a huge competitor to Bell," Sylvestre said. "We are reviewing the (announcement)."

Looming over all is continued uncertainty with regard to military spending and the energy sector, which relies on helicopter shuttles to reach offshore rigs, not to mention the prospect of any interruption in funding similar to the 2013 U.S. government sequestration on spending that had a significant impact on military suppliers.

"There are still questions on whether sequestration is going to be fully imposed in 2016," Jaworowski noted.

Sikorsky is expected to vie with Bell to produce a replacement for the Black Hawk, offering a design in partnership with Boeing based on its S-97 Raider and Bell countering with a smaller version of its Osprey tilt-rotor aircraft.

"Right now, I would put the Boeing-Sikorsky proposal slightly ahead," Jaworowski said.

Alex.Soule@scni.com; 2039642236; www.twitter.com/casoulman

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