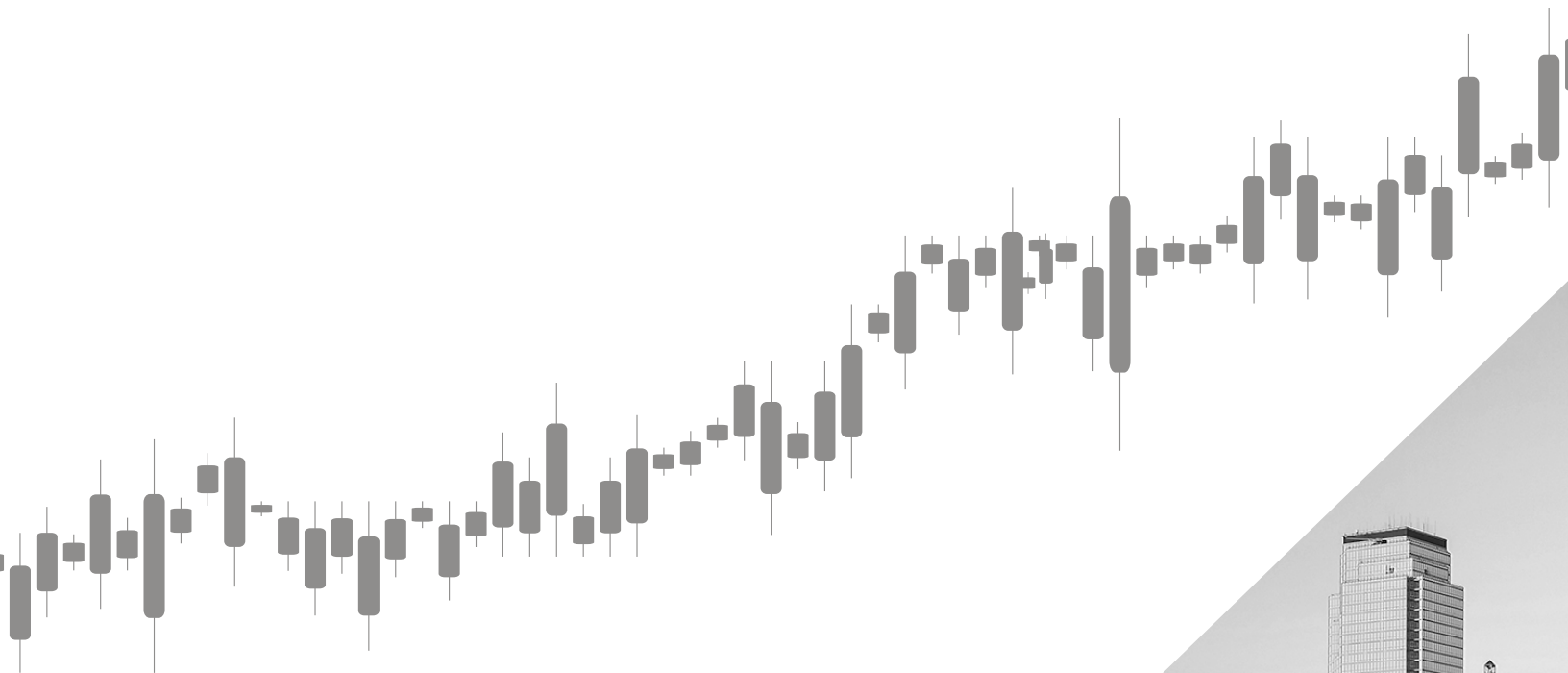


FAIRMONT
CONSULTING GROUP

MRO AMERICAS 2022
AFTERMARKET UPDATE



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MRO AMERICAS 2022 -AFTERMARKET UPDATE

“Business is very good” was the primary sentiment from parts providers and MROs at last week’s MRO Americas conference in Dallas. The aftermarket is enjoying surging demand on the heels of a Macro-recovery, but as a whole is wrestling to efficiently meet that ramp amid supply chain challenges. Widespread issues related to the consistent supply of new or used parts, maintaining labor, and costs & inflation are particularly pronounced in the labor-intensive aftermarket. Geopolitical risks (i.e. Russian invasion of Ukraine, COVID lockdowns in China) have caused major disruptions to service for Russian and Chinese carriers, as well as disruptions to the supply chain (i.e. Russian sourced Titanium).

But still, business is the best it’s been in years – with some MROs expecting to exceed 2019 levels by a fair margin this year. A wave of MRO requirements and shop visits driven by rapid return of air travel has been amplified by a continued stream of deferred maintenance – multi-million-dollar shop visits that were avoided during the cash-strapped COVID period. A record backlog of Cargo Conversions globally is expected to boost MRO demand further.

Green time engines and components played a key role in serving portions of these requirements during the lean times of COVID, but the availability of those assets has dwindled. As a result, **the aftermarket is just beginning to see the full scale of true repair and spare component demand**, placing extra pressure on the OEMs and the MRO community to efficiently serve it.

Fairmont posits that the current environment will continue to favor well-positioned independent aftermarket providers, and may accelerate the onboarding of new suppliers and the adoption of alternative solutions to maintain fleets.



KEY CONSIDERATIONS

As demand has roared back, the ability for many MROs to meet it as efficiently as in past years has eroded. Labor intensive Airframe and Component MROs are grappling with skilled labor shortages. Engine MROs - which require a steady stream of spare parts from OEMs – are beginning to lack just that. All of this is occurring in the midst of the long-awaited aftermarket recovery – many are nearing 2019 levels in the last year of business, and a few have exceeded it.

The question is, can the aftermarket capitalize on the strong fundamentals of this recovery?

Slowing component repair turn-times and emerging subcomponent delays across the market are driving a temporary “flattening” of the market, where top-tier demand typically served by OEMs or leading independents is flowing down to the secondary aftermarket. “Who actually has this part or has the means to quickly fix it?”. Overall, it is an interesting convergence of factors that we think will drive major changes in the aftermarket. **Alternative repairs (DERs), alternative parts (PMAs), Used Serviceable Material, and a more flexible independent aftermarket as a whole are likely to be an increasing area of focus for the market – and also pose compelling investment strategies.**



MUCH ADO ABOUT LABOR

Thousands of skilled MRO technicians were laid off during COVID or exited the field – often to greener pastures that are proving hard to pull talent back from. Only so much of future requirements can be addressed by training up new talent. Automation surely has an important role to play currently and in the future of Aerospace, but there are practical challenges in MRO that preclude any real near-term impact.

The end result is that Airlines, OEMs, Repair Centers and others are having to do more with less – which has proven challenging after many highly experienced AMTs and back-office supply chain employees departed the industry permanently. TATs continue to be impacted - MRO technicians and mechanics that remain in the industry or have been recently hired are significantly less efficient vs. seasoned techs (Southwest estimates seasoned techs are 4X more efficient vs. new techs). Outsourcing from operators with in-house maintenance is likely to continue - and with OEMs and Tier-1 MROs at capacity, independent providers stand to benefit.



PARTS ARE THE OTHER PART OF THE EQUATION

Meaningful disruptions in the supply of OEM spare parts and subcomponents are already apparent (four of the largest global Engine MROs described the Engine repair network as “creaky”). Both Airframe and Engine replacement components are difficult to procure in a timely manner, stretching lead times and disrupting maintenance plans. Engine OEMs are drawing the ire of repair shops and operators that are unable to secure LLPs used in overhauls. Many airlines feel that the OEMs are not adequately supporting in-service aircraft, and that they have shifted virtually all of their attention to new-build work.

This present broad opportunities across the independent MRO supply chain for agile providers that are able to address these pain points and capitalize on OEM shortfalls. In fact, many operators are now focused on

qualifying new sources of supply for both parts and services to reduce their dependence on OEMs. In some cases, this may be as simple as broadening the distributor base for more common parts, but in others we will see accelerating acceptance of alternative parts and repairs.



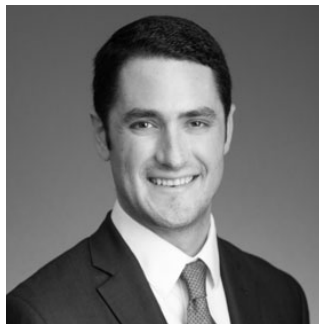
WHAT DOES THIS MEAN FOR END USERS?

COVID disruptions and the ongoing supply chain challenges in the Aftermarket are accelerating a search for more flexible solutions and cost-effective support - **MROs and End Users are turning to the independent aftermarket.** Faced with a strained parts aftermarket and many of the same labor force issues as MROs, Airlines are beginning to have trouble efficiently maintaining their current generation aircraft, such as the 737NG, A320ceo, and 777. To tackle this, airlines such as Southwest and others have been qualifying new suppliers in order to streamline repair processes where delays have been primarily caused by a lack of parts. Others are developing new repairs (DERs) and qualifying new components (e.g. PMAs).

The calculus between selecting OEM-approved/executed repairs versus alternative solutions has fundamentally changed. In several areas, the “cheaper way” may become the “only” practical or timely way for many operators to keep their aircraft airworthy. This appears to already be playing out in the market, with several PMA and DER suppliers indicating that their businesses have grown substantially since 2019 – growth they attribute in part to OEM shortages and disruptions. Retention of these components in the long term remains an open question, however it is difficult to imagine broader adoption of lower cost solutions that prove effective will be excluded wholesale even after the crisis eases.

So what does this tell us about the current market landscape? The ability to actually meet turn times is far and away the most important buying criteria right now. Other factors such as price, “tag reputation”, and vendor agreements are less important currently – this is materializing as a net benefit for the independent aftermarket (even if they themselves are not immune from the labor challenges affecting the rest of the market).

The aftermarket is rapidly changing as it grapples with a surge in demand and constrained supply, driven in large part by changing buying behaviors by operators and MROs. The most flexible and innovative independent providers have the opportunity to capitalize on this shift.



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