

HEICO Corporation

Aftermarket winning with Wencor; Reiterate Buy; PO: \$220

Reiterate Rating: BUY | PO: 220.00 USD | Price: 188.91 USD

Continued gains from the wobbly Aero OEM ramp

We continue to see opportunities for growth in Flight Support Group (FSG) supported by sustained higher shop-visit volumes due to the [GTF metal powdered AOG](#) as well as the [Boeing 737MAX production cap](#). We estimate strong demand in the comm'l aftermarket will result in robust growth for FSG (up 15% Y/Y organically). In the near-term for Electronics Technology Group (ETG) we expect depressed margins on higher R&D expenses. However, innovation for long-term gains is necessary and we look at the R&D as a positive investment for future wins. With the strong aftermarket environment offsetting near term headwinds in ETG, we reiterate our Buy rating and maintain our PO.

Wencor outperforming expectations

We continue to view the Wencor acquisition favorably. With ~7,000 complimentary parts (with minimal overlap) added to HEI's existing portfolio (See Exhibit 1) and strong aftermarket demand, we see further upside for Wencor. Notably, Wencor is already outperforming initial expectations. In FSG, 1Q margins were 22%, despite a 200bps headwind from Wencor acquisition related costs. We view the strong margin performance a signal pricing and volumes meaningfully offset the added expenses. We anticipate Wencor will add ~\$840mn of revenue for FY2024.

Differentiating defense products for long term gains

To remain competitive and well positioned for future programs ETG is increasing R&D investments. ETG reported op. margins of 19.3% (the first time margins were <20% since 2013) driven by the increased R&D expense and acquisition costs. While at face value the low margins appear alarming, the R&D expenses are necessary for sustainable growth. ETG's portfolio remains well positioned to capture growth as the DoD prioritizes missile/munition replenishment, aircraft fleet readiness, and new opportunities in Space. We expect margins to return to >20% by FY2025.

The power of pricing and penetration

To ensure customer retention and attract new customers, HEI choose to maintain lower prices. This pricing model is in stark contrast to the aggressive price hikes touted by peers. The strategy has worked and attracted new customers. Now a new opportunity is present. The post-pandemic supply and quality issues and defense unique requirements have allowed HEI to further penetrate the aftermarket world not just as the best pricing option, but as a reliable high-quality partner.

Estimates (Oct) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	2.55	2.91	3.45	4.20	5.05
EPS Change (YoY)	15.4%	14.1%	18.6%	21.7%	20.2%
Consensus EPS (Bloomberg)			3.54	4.21	4.49
DPS	0.18	0.20	0.21	0.24	0.26
Valuation (Oct)					
P/E	74.1x	64.9x	54.8x	45.0x	37.4x
Dividend Yield	0.1%	0.1%	0.1%	0.1%	0.1%
EV / EBITDA*	49.0x	38.4x	29.0x	25.3x	22.8x
Free Cash Flow Yield*	1.7%	1.5%	1.8%	2.2%	3.1%

* For full definitions of *IQmethod*SM measures, see page 5.

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06 March 2024

Equity

Key Changes

(US\$)	Previous	Current
2024E Rev (m)	3,936.2	3,942.3
2025E Rev (m)	4,291.0	4,310.4
2026E Rev (m)	4,624.0	4,686.4
2025E EPS	4.10	4.20

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Stock Data

Price	188.91 USD
Price Objective	220.00 USD
Date Established	13-Jun-2023
Investment Opinion	B-1-7
52-Week Range	153.63 USD - 200.64 USD
Mrkt Val (mn) / Shares Out (mn)	26,179 USD / 138.6
Free Float	77.1%
Average Daily Value (mn)	79.75 USD
BofA Ticker / Exchange	HEI / NYS
Bloomberg / Reuters	HEI US / HEI.N
ROE (2024E)	14.0%
Net Dbt to Eqty (Oct-2023A)	64.8%
ESGMeter TM	Medium

ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BofA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to "BofA ESGMeter Methodology".

AOG: Aircraft on ground

Comm'l: Commercial

iQprofileSM HEICO Corporation

iQmethodSM – Bus Performance*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Return on Capital Employed	11.5%	9.8%	9.7%	10.4%	10.6%
Return on Equity	14.2%	13.8%	14.0%	14.7%	15.1%
Operating Margin	22.5%	21.1%	21.0%	22.1%	22.8%
Free Cash Flow	436	399	477	581	814

iQmethodSM – Quality of Earnings*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash Realization Ratio	1.3x	1.1x	1.2x	1.1x	1.2x
Asset Replacement Ratio	0.3x	0.4x	0.5x	0.4x	0.3x
Tax Rate	20.4%	20.0%	20.5%	20.5%	20.5%
Net Debt-to-Equity Ratio	5.1%	64.8%	47.5%	29.5%	11.2%
Interest Cover	NM	8.6x	5.2x	5.2x	5.9x

Income Statement Data (Oct)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Sales	2,208	2,968	3,942	4,310	4,686
% Change	18.4%	34.4%	32.8%	9.3%	8.7%
Gross Profit	1,672	2,296	3,067	3,310	3,569
% Change	16.4%	37.3%	33.6%	7.9%	7.8%
EBITDA	593	755	1,002	1,147	1,271
% Change	22.1%	27.3%	32.7%	14.5%	10.8%
Net Interest & Other Income	(6)	(70)	(156)	(131)	(77)
Net Income (Adjusted)	352	404	483	592	715
% Change	15.6%	14.8%	19.8%	22.5%	20.8%

Free Cash Flow Data (Oct)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Income from Cont Operations (GAAP)	391	444	534	654	789
Depreciation & Amortization	96	130	174	194	201
Change in Working Capital	(61)	(117)	(177)	(225)	(135)
Deferred Taxation Charge	9	(27)	(4)	12	12
Other Adjustments, Net	33	18	29	15	15
Capital Expenditure	(32)	(49)	(79)	(69)	(70)
Free Cash Flow	436	399	477	581	814
% Change	6.9%	-8.4%	19.5%	21.8%	39.9%
Share / Issue Repurchase	0	0	0	0	0
Cost of Dividends Paid	(24)	(27)	(29)	(34)	(37)
Change in Debt	50	975	(129)	0	0

Balance Sheet Data (Oct)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash & Equivalents	140	171	411	958	1,735
Trade Receivables	295	509	555	626	668
Other Current Assets	718	1,175	1,312	1,467	1,588
Property, Plant & Equipment	226	322	356	349	324
Other Non-Current Assets	2,717	5,018	5,002	4,885	4,779
Total Assets	4,095	7,195	7,637	8,285	9,094
Short-Term Debt	2	18	5	5	5
Other Current Liabilities	419	648	645	646	674
Long-Term Debt	289	2,460	2,346	2,346	2,346
Other Non-Current Liabilities	410	511	554	566	578
Total Liabilities	1,120	3,637	3,550	3,562	3,603
Total Equity	2,976	3,558	4,087	4,723	5,491
Total Equity & Liabilities	4,095	7,195	7,637	8,285	9,094

* For full definitions of iQmethodSM measures, see page 5.

Company Sector

Aerospace

Company Description

HEICO is a leading manufacturer of FAA approved jet engine and aircraft component replacement parts. The company is organized into two reporting segments: Flight Support Group (FSG) and Electronic Technologies Group (ETG). In FY21, 39% of sales came from the commercial aviation industry, 44% from defense and space, and the remaining 17% from other industrial markets including medical, electronics and telecommunications.

Investment Rationale

HEI stands to benefit as 1) a recovery in air traffic demand fuels better than anticipated growth in aftermarket producers, 2) slower than expected OEM deliveries, and 3) recent GTF/ BA MAX-9 groundings pressuring existing aircraft supply.

Stock Data

Average Daily Volume 422,136

Quarterly Earnings Estimates

	2023	2024
Q1	0.67A	NAA
Q2	0.76A	NAE
Q3	0.74A	NAE
Q4	0.74A	NAE

Exhibit 1: HEI's PMA Portfolio now consistence of nearly 20,000 parts

2023 reflects the ~7,000 additional PMA parts added from the Wencor Portfolio

	2016A	2017A	2018A	2019A	2020A	2021A	2022A	2023A
New DER Parts per year	300 - 400	300 - 400	300 - 400	300 - 400	300 - 400	300 - 400	300 - 400	300 - 400
New PMA Parts per year	300 - 500	300 - 500	300 - 500	300 - 500	300 - 500	300 - 500	300 - 500	350 - 550
Total PMA	10,000	10,000	11,000	11,200	11,500	12,000	12,200	19,550
Change in PMA Parts		-	1,000	200	300	500	200	7,350

Source: BofA Global Research, Company Filings

BofA GLOBAL RESEARCH

FSG – Green shoots continue with aftermarket demand

We outlined in our: [2024 Year Ahead: Butterflies and Bullets](#), we were wary of the notion that 2024 would be the year commercial OEM production would normalize. With that perspective, we noted a preference for Aftermarket over OEM and concerns of a massive aftermarket deceleration were overdone. Only a few weeks into the year, the thesis appears correct, so far, and we maintain our view the aftermarket hasn't run out of steam. We continue to expect HEI to capture new demand and growth from the current aftermarket environment. For FY2024, we anticipate ~15% organic growth, and 50% Y/Y growth driven by an increase in expectations Wencor. With the higher volumes leading to better than expected performance from Wencor, we are raising our FSG margin expectations to 22.5% for FY2024 from 21%.

ETG – Growth story intact, near-term margins lower

In defense, we expect ETG to see significant benefits from its strategy focusing on niche products at the subcomponent level. We continue to see long-term growth opportunities for ETG. HEI investing heavily in R&D should ensure positions on existing platforms are maintained while new opportunities are won. While we expect margins to be lower in the near-term as new products are developed, we expect a return >20% margins by FY2025E. We are approaching near-term margin step-ups more conservatively, however we see upside opportunity to realize higher margins on increased pricing on the new products. Additionally, we see upside risk for a reaccelerating of revenue driven by the new products, and appetite for M&A in the defense space.

Estimates mostly unchanged due to diversified portfolio

While we do expect a slightly longer margin recovery in ETG on the higher R&D expense, we expect the headwind to be offset by FSG and Wencor growth in the near term. The stronger than expected performance inflects in 2025, as we expect OE to achieve a less volatile and steadier ramp. The puts and takes across each segment leave our estimates mostly unchanged. For FY2024E we expect EPS of \$3.45 (vs. prior \$3.45), FY2025E: \$4.20 (vs. prior \$4.10), FY2026E: \$5.05 (vs. prior \$5.05), FY2027E: \$5.70 (vs. prior \$5.70).

Reiterate Buy and PO: \$220 on comm'l recovery

We maintain our PO, unchanged at \$220. Our PO is based on a 2.4x relative P/FCF multiple to the S&P 500 on CY25 estimates. Historically, HEI has traded between 0.9x and 2.6x (excluding some 2013 exceptions). Starting in 2018, HEI has traded above average on strong commercial aero growth expectations. We view the 2.4x multiple (vs. last 5 year average of 1.92x) as fairly valuing the upside from both Wencor and commercial aftermarket.



Price objective basis & risk

HEICO Corporation (HEI)

Our PO of \$220 is based on a 2.4x relative P/FCF multiple to the S&P 500 on CY25 estimates. Historically, HEI has traded between 0.9x and 2.6x NTM relative P/FCF multiple (excluding outlier period in 2013). In our view, a relative multiple above HEI's 5-year 1.92x average, fairly factors in HEI's unique market positioning, strong management execution and a sound balance sheet.

Downside risks are a longer-than-expected economic slowdown, which would likely lower original equipment manufacturer (OEM) production rates and demand for air travel, higher oil prices, which would likely derail air traffic growth and, therefore, aircraft demand, less acceptance of PMAs from the airline community, a change in acquisition strategy and integration.

Upside risks are increased M&A due to the company's acquisitive history, faster growth in sales, a stronger-than-expected commercial aero recovery, better-than-expected margins, a greater acceptance of parts manufacturer approval (PMA) parts by airlines and lessors.

Analyst Certification

I, Ronald J. Epstein, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Aerospace and Defense Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	AerCap Holdings N.V.	AER	AER US	Ronald J. Epstein
	Air Lease Corporation	AL	AL US	Ronald J. Epstein
	Booz Allen Hamilton	BAH	BAH US	Mariana Perez Mora
	BWX Technologies, Inc.	BWXT	BWXT US	Ronald J. Epstein
	CACI International	CACI	CACI US	Mariana Perez Mora
	Cadre Holdings Inc	CDRE	CDRE US	Ronald J. Epstein
	Crane Co.	CR	CR US	Ronald J. Epstein
	Embraer	ERJ	ERJ US	Ronald J. Epstein
	General Dynamics	GD	GD US	Ronald J. Epstein
	HEICO Corporation	HEI	HEI US	Ronald J. Epstein
	Howmet Aerospace Inc.	HWM	HWM US	Ronald J. Epstein
	KBR	KBR	KBR US	Mariana Perez Mora
	Leidos Holdings	LDOS	LDOS US	Mariana Perez Mora
	Leonardo DRS, Inc.	DRS	DRS US	Ronald J. Epstein
	Northrop Grumman	NOC	NOC US	Ronald J. Epstein
	Palantir Technologies	PLTR	PLTR US	Mariana Perez Mora
	Parsons Corporation	PSN	PSN US	Mariana Perez Mora
	RBC Bearings Inc	RBC	RBC US	Ronald J. Epstein
	Rocket Lab	RKLB	RKLB US	Ronald J. Epstein
	Teledyne Technologies Inc	TDY	TDY US	Ronald J. Epstein
	TransDigm Group Inc.	TDG	TDG US	Ronald J. Epstein
	Triumph Group	TGI	TGI US	Ronald J. Epstein
NEUTRAL				
	Albany International	AIN	AIN US	Ronald J. Epstein
	Boeing	BA	BA US	Ronald J. Epstein
	Garmin	GRMN	GRMN US	Ronald J. Epstein
	Hexcel Corporation	HXL	HXL US	Ronald J. Epstein
	L3Harris	LHX	LHX US	Ronald J. Epstein
	Lockheed Martin	LMT	LMT US	Ronald J. Epstein
	RTX Corp	RTX	RTX US	Ronald J. Epstein
	Textron	TXT	TXT US	Ronald J. Epstein

US - Aerospace and Defense Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
UNDERPERFORM				
	Bombardier	BDRBF	BDRBF US	Ronald J. Epstein
	Bombardier Inc.	YBBD B	BBD/B CN	Ronald J. Epstein
	CAE Inc.	YCAE	CAE CN	Ronald J. Epstein
	CAE Inc.	CAE	CAE US	Ronald J. Epstein
	Huntington Ingalls Industries	HII	HII US	Ronald J. Epstein
	Mercury Systems	MRCY	MRCY US	Ronald J. Epstein

iQmethodSM Measures Definitions**Business Performance**

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

EV / EBITDA

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Numerator

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

EV = Current Share Price × Current Shares + Minority Equity + Net Debt +

Other LT Liabilities

Enterprise Value

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill

Amortization

Shareholders' Equity

Sales

N/A

N/A

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Denominator

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

Sales

Basic EBIT + Depreciation + Amortization

iQmethodSM is the set of BofA Global Research standard measures that serve to maintain global consistency under three broad headings: Business Performance, Quality of Earnings, and validations. The key features of iQmethod are: A consistently structured, detailed, and transparent methodology. Guidelines to maximize the effectiveness of the comparative valuation process, and to identify some common pitfalls.

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HEICO (HEI) Price Chart



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Equity Investment Rating Distribution: Aerospace/Defense Electronics Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	31	62.00%	Buy	23	74.19%
Hold	11	22.00%	Hold	9	81.82%
Sell	8	16.00%	Sell	6	75.00%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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