

Industry Top Trends Update

# Aerospace and Defense

## Commercial aircraft are supply constrained

### What's changed?

**Commercial aerospace revenues and earnings remain below pre-pandemic levels.** Global demand for jetliners, particularly narrowbody, business, and freight aircraft, is strong. U.S. air travel volumes are approaching pre-pandemic levels, supporting aftermarket sales of parts and maintenance services. But the commercial aircraft sector has yet to recover to pre-pandemic levels.

**Commercial supply is likely to lag demand.** Boeing's ramp up of 737 MAX deliveries and production has been uneven and resumption of 787 deliveries awaits regulatory approval. Supply chain constraints, including shortages and delays for components throughout the value chain, are limiting production growth

**U.S. defense spending supports sales growth.** The 2022 U.S. defense budget is up 6% from 2021, and the 2023 request represents a 4% increase over 2022. While the Russia-Ukraine conflict may lead to increased spending by European allies, we do not expect it to result in a near-term windfall.

### What to look out for?

**Resumption of 787 deliveries and MAX deliveries in China.** Boeing is seeking FAA approval to resume 787 deliveries after quality issues required remedy, and seeking Chinese government approval to resume deliveries of 737 MAX planes to customers in China, one of its largest markets.

**How long will supply problems last?** Delays and shortages of certain components are impeding aerospace companies' ability to meet demand. Improvement in the second half of the year would free up working capital and allow companies to make progress meeting backed up orders.

**Defense companies may pay higher cash taxes in 2022.** U.S. tax rules now require research and development spending to be capitalized, resulting in temporarily higher cash taxes starting in 2022. The rule may be changed or deferred in future legislation, but we assume it stays in place in our forecasts.

### What if there's a recession?

**The recovery of air travel could falter.** Reduced demand would result in lower aftermarket sales for OEMs, component suppliers, and service providers. Orders for new aircraft would likely be less immediately affected, due to pent-up demand.

**Stretched supply chains could gain time to recover.** Less demand for commercial aerospace aftermarket products, and potential deferrals of new planes, would give suppliers time to catch up on delayed orders. A slower economy would also reduce pressure on materials and labor costs and availability.

**The effect on defense spending would be limited.** U.S. national security priorities, including heightened perception of risks and focus on modernization and readiness, would likely insulate defense orders from budgetary pressures.

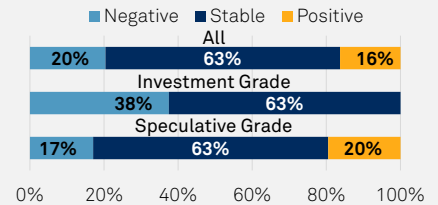
### Latest Related Research

- [Raytheon Technologies Corp. Ratings Affirmed, Outlook Negative On Uneven Recovery And Higher Tax Payments](#), June 7, 2022
- [Jazz Acquisition Inc. Upgraded To 'B-' From 'CCC+' On Improved Credit Metrics: Outlook Stable; Debt Ratings Raised](#), May 13, 2022

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### Outlook Distribution



### Ratings Statistics (YTD)\*

	IG	SG	All
<b>Ratings</b>	8	41	49
<b>Downgrades</b>	0	2	2
<b>Upgrades</b>	0	3	3

Ratings data as of end-June 2022. \* Year-to-date

### Ratings Outlook Net Bias

