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CAE

(NYSE): CAE

Elevating While Simulating



CAE

| | |
|-------------------------|------------------------|
| Market Cap | \$6.8 B |
| 3/28 Close | \$21.29 |
| 52 Week Range | \$15.23-\$27.95 |
| NTM EV/EBIT | 18.5x |
| Operating Margin | 9.5% |

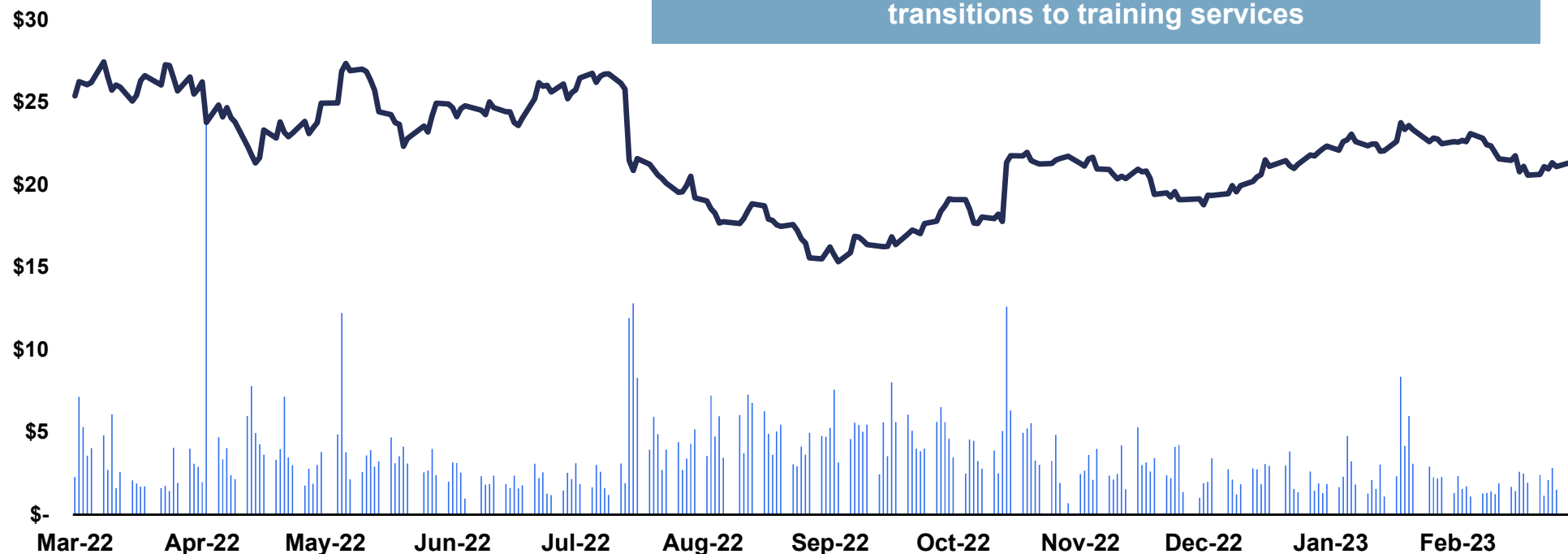
Company Overview

- CAE is a high-technology company that provides simulation training and critical operations support solutions to the civil aviation, defence and security, and healthcare markets globally.
 - Recommendation: BUY with a Price Target of **\$29.83**, representing an upside of **40.0%** from 3/28 close

Investment Thesis Overview

1. CAE **monopolized** 3rd party pilot **training** amid travel demand recovery and a **structural shortage of pilots**
2. As airlines face challenging headwinds, CAE provides **cost savings** and flexibility through outsourced training

CAE will see increased margins as more of their revenue transitions to training services



Company Overview



CAE Reports Revenue in 3 Main Segments:

Civil Aviation

Leading provider of aviation simulation and training solutions



47% of Revenue in FY 22
71% of EBIT in FY 22

Defence & Security

Only global, pure-play and platform-agnostic training and simulation company across all 5 domains



47% of Revenue in FY 22
27% of EBIT in FY 22

Healthcare

Second largest provider of healthcare simulation equipment



6% of Revenue in FY 22
2% of EBIT in FY 22

CAE History and Acquisition Morphed into Industry Behemoth ⁽¹⁾



CAE founded by Ken Patrick

1947



CAE enters defence market with NATO contracts

1950s

1960s

1970s

CAE expands product offerings, including ATC systems

CAE cements reputation throughout international markets

1980s

A pivotal decade that saw CAE become the world leader in flight and systems sim tech

1990s

CAE rapidly introduces and grows global training network

2000s



Positioned to accelerate vision in Post-COVID environment

2010s

CAE secures position as leading provider of training services

2023



(1) Company Filings

Industry Overview



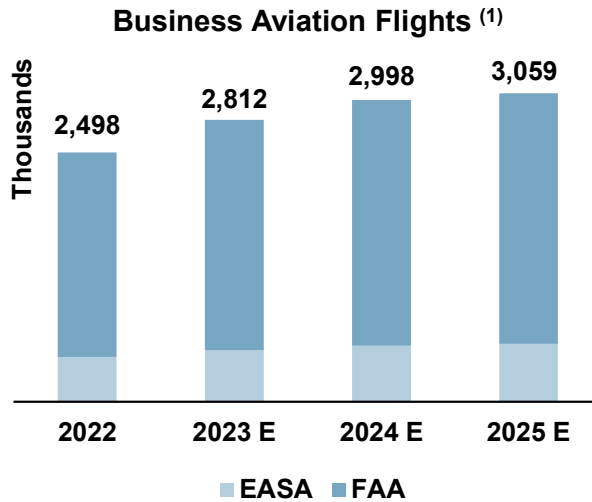
1. Civil Aviation

Business Jet

~ 7% CAGR in business related aviation flights



50% increase in business flights FY22 vs FY21

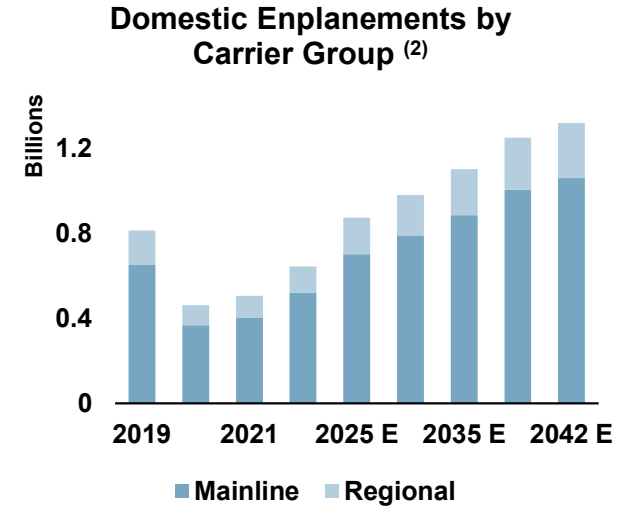


Commercial

~ 8% CAGR in commercial related aviation flights



63% increase in commercial flights FY22 vs FY21

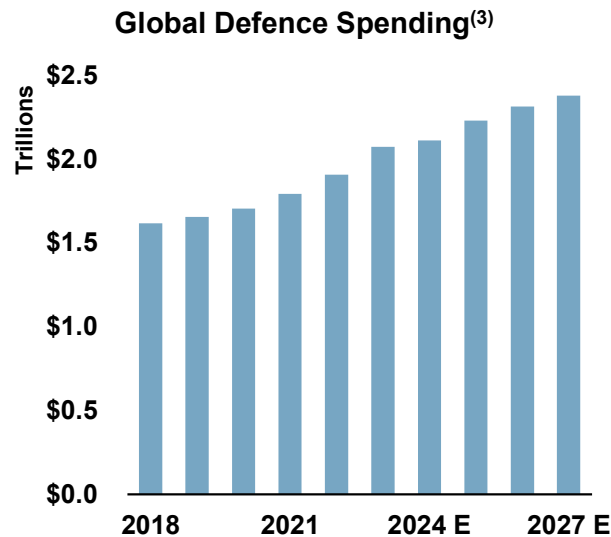


2. Defence & Security

~4% CAGR allied global defence budget



CAE has ~14% market share, 2% less than Lockheed Martin

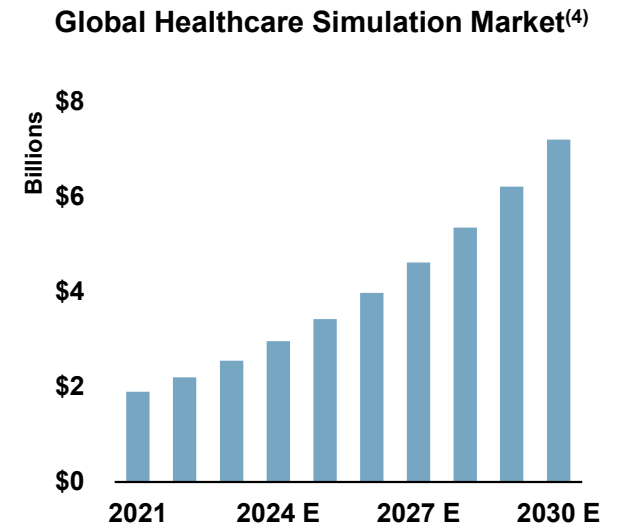


3. Healthcare

~16.1% CAGR in global healthcare simulation market



27.1% turnover rate for RN's leading to record demand for training new nurses



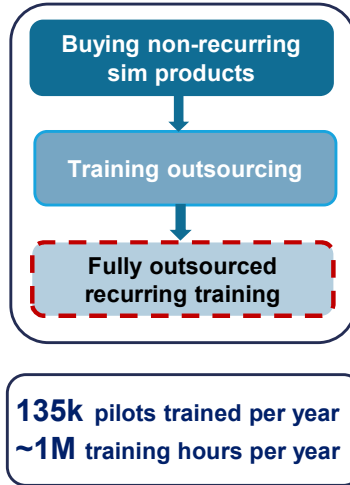
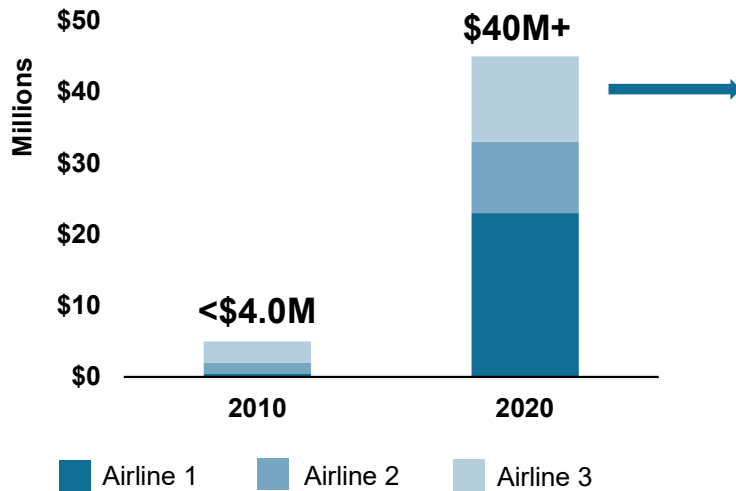
(1) JetNet IQ (2) FAA Aerospace Forecast (3) Forecast International (4) Precedence Research
Culverhouse Investment Management Group



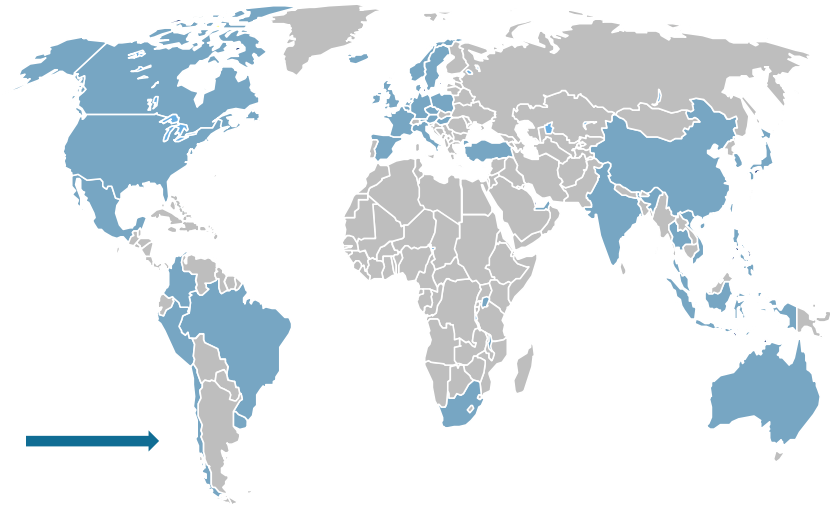
Understanding the Civil Aviation Industry - CAE's Strong Suit

CAE Is The #1 Civil Aviation Training Company In The World

Annual Training Billings From Airline Partners (1)



70 Training Centers Globally In Over 40 Countries



CAE's Flexible Partnership Style Creates Lasting Customer Relationships



Full Flight Simulators

CAE sells simulator to airlines and carriers

- \$15-25 m per simulator
- One-time Sale
- Lowest margin
- \$6 bn in backlog



Dry Training

Airlines rent CAE simulators

- Higher margin
- Recurring revenue
- Airline controls content
- Popular for bigger airlines



Joint Ventures

CAE handles portion of training hours

- JVs with 40+ airlines
- CAE builds client trust
- Sticky customer relationship



Wet Training

Full outsourcing using CAE instructors and facilities

- Highest margin
- Stickiest relationship
- Popular for Private and LC Carriers

(1) FY 22 Annual General Meeting of Shareholders

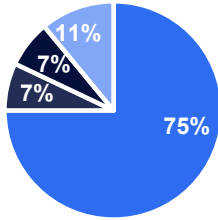


Understanding the Defence Industry

CAE Defence & Security: Advancing Legacy Business Through Strategic Repositioning

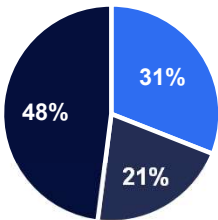
CAE Addressable Markets In D&S

~\$14B
CORE Market
Military Training
& Simulation
Market



- Air
- Land
- Naval
- Space & Cyber

~\$24B
Adjacent Market
Operations Support
Market



- Analytics & Systems Engineering
- Mission Planning & Support Services
- Mission Operations

Competitive Landscape in CORE Market

| | |
|---|--|
| OEM Est. Market Share ~35% | OEMs transitioning away from vertical integration and seeking training & simulation partnerships |
| Mid Tier / Other Est. Market Share ~29% | The demand for Multi-Domain Solutions hurts ability to compete and reach customers worldwide |
| Small Business Est. Market Share ~22% | Difficult to offer the complex solutions and high-level technological capabilities of the bigger players |

CAE Advantage

- 14% Market Share in Core Market
- Presence in 50+ countries
- Capabilities fully aligned with customer priorities
- The only global pure-play, platform-agnostic training and simulation company in the world

L3Harris Technologies' Military Training Acquisition



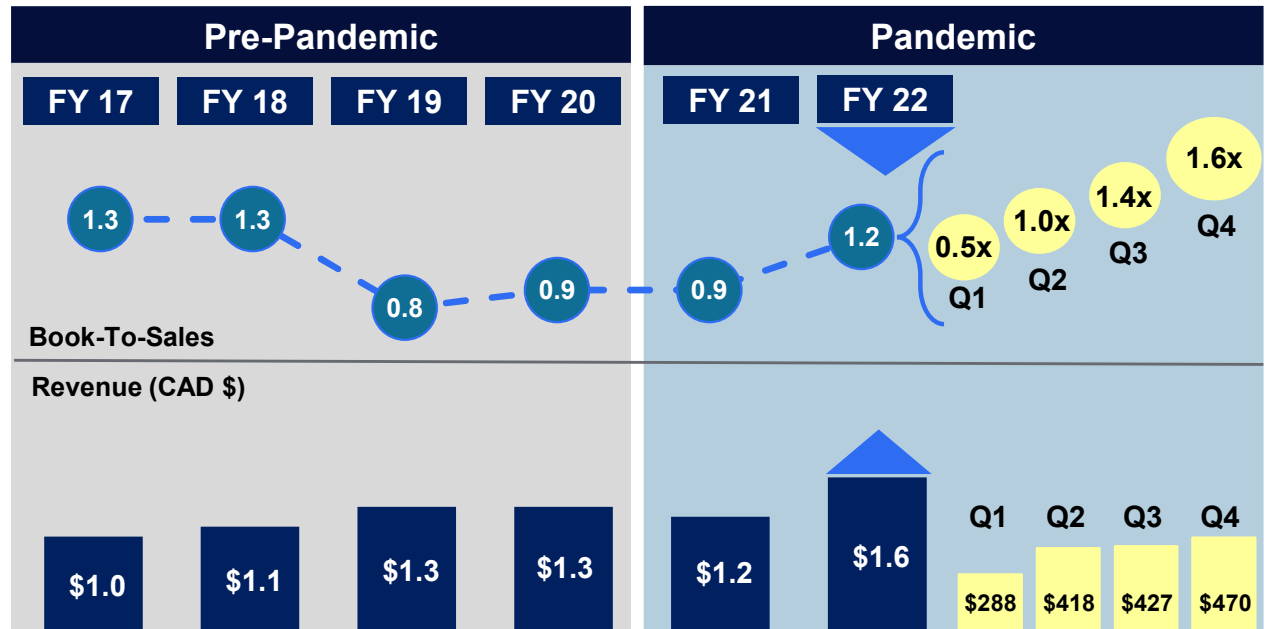
All- cash purchase price of US \$1.05B

~13.5x L3H Military Technologies' Adjusted 2020 EBITDA

EPS increased from (.42) to .25 one year post-acquisition close

3 Founding Fathers of Military Simulation Training Now Under One Roof in CAE

Key L3H MT Platforms: Link Simulation & Training, Doss Aviation, and AMI



(1) FY 22 Annual General Meeting of Shareholders

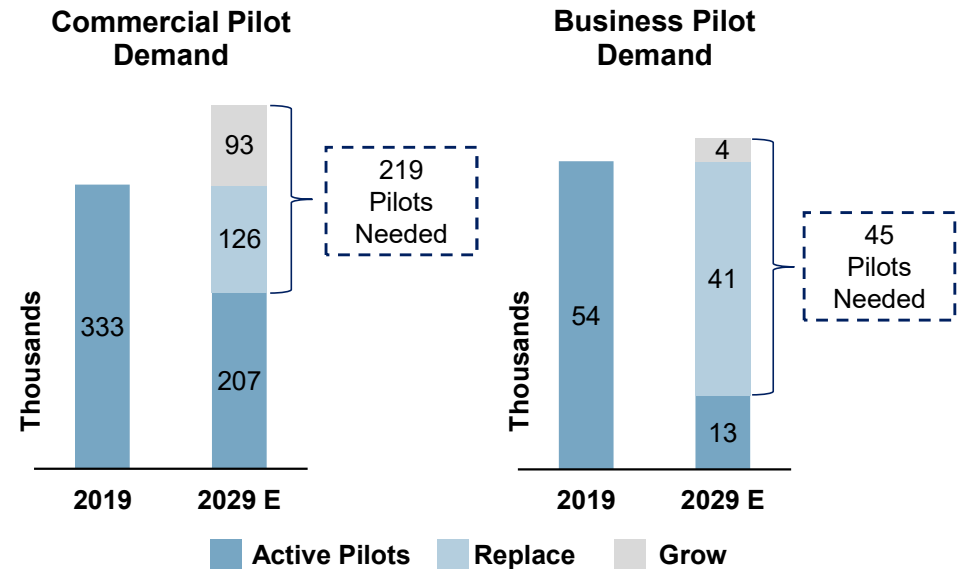


Pilot Shortage Yields High Training Demand Within Changing Environment

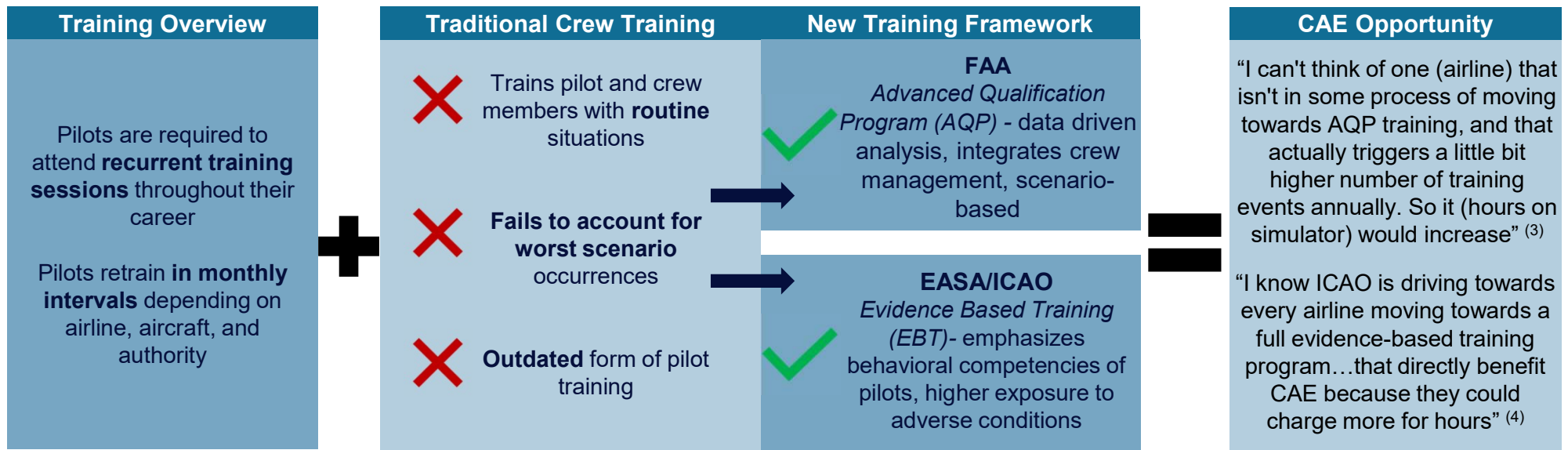
The effects from COVID-19...

| | Concern | CAE Opportunity |
|--|--|--|
| | COVID-19 encouraged early retirements from pilots leading to shortage | Estimated ~264K airline and business pilots needed over next decade ⁽¹⁾ |
| | Vacancy bidding due to 2020 furloughing means returning pilots lose previous positions | Pilots entering new positions requires extensive training and new type-ratings ⁽¹⁾ |
| | ~40% of current pilots are expected to retire by 2029 ⁽²⁾ | New pilots will need to be trained ab initio starting with Level A FFS |

...created an excess demand for pilot training ⁽²⁾



Stricter Regulatory Requirements Fortifying Recurring Revenue



(1) CAE Investor Day 2022 (2) CAE Pilot Demand Outlook (3) Former CAE Training Program Consultant (4) Emirates Type Rating Instructor



CAE's Portfolio Convinces Airlines to Outsource and Transition to JV

All-Encompassing Portfolio

1 Training Operations Solutions

2 Flight Simulation Training Devices

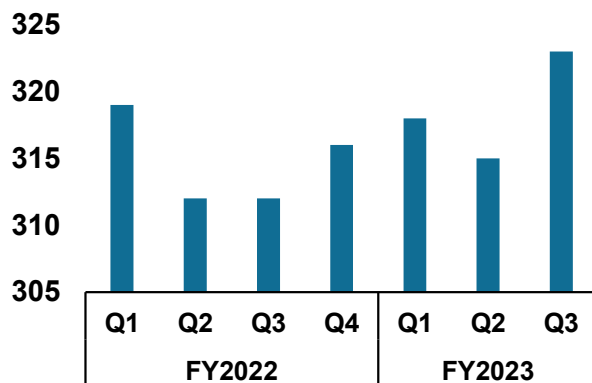
3 Ab Initio Pilot Training & Crew Sourcing Systems

4 End-to-End Digitally-Enabled Crew Management

5 Optimization Software

CAE Network Scope

FFSs In CAE Network



16 Joint Ventures

40+ Civil Aviation Relationships

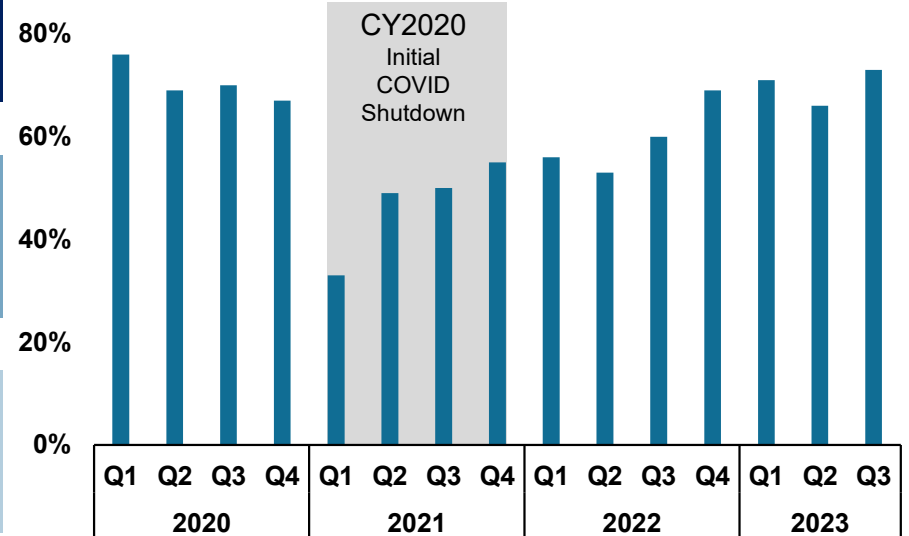
Outsourcing with CAE is Cheaper and Utilization Rates Rebounding (1)

20%-30% Airline Cost savings with CAE JV

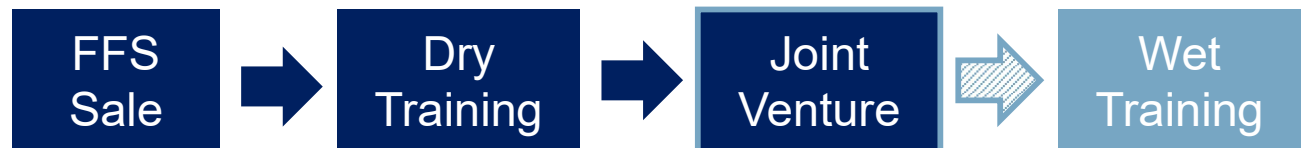
0.75% Fuel Savings with CAE Flight Management

25-year-life of CAE Full Flight Simulators

CAE Civil Aviation Training Center Utilization Rates



Evolution of CAE Customer Relationships (2)



2000s

Equipment and service sales

2011

JV agreement

2017

Full outsourcing from AirAsia Training for 20 years

2018

Announces launch of CAE Rise to be employed with AirAsia

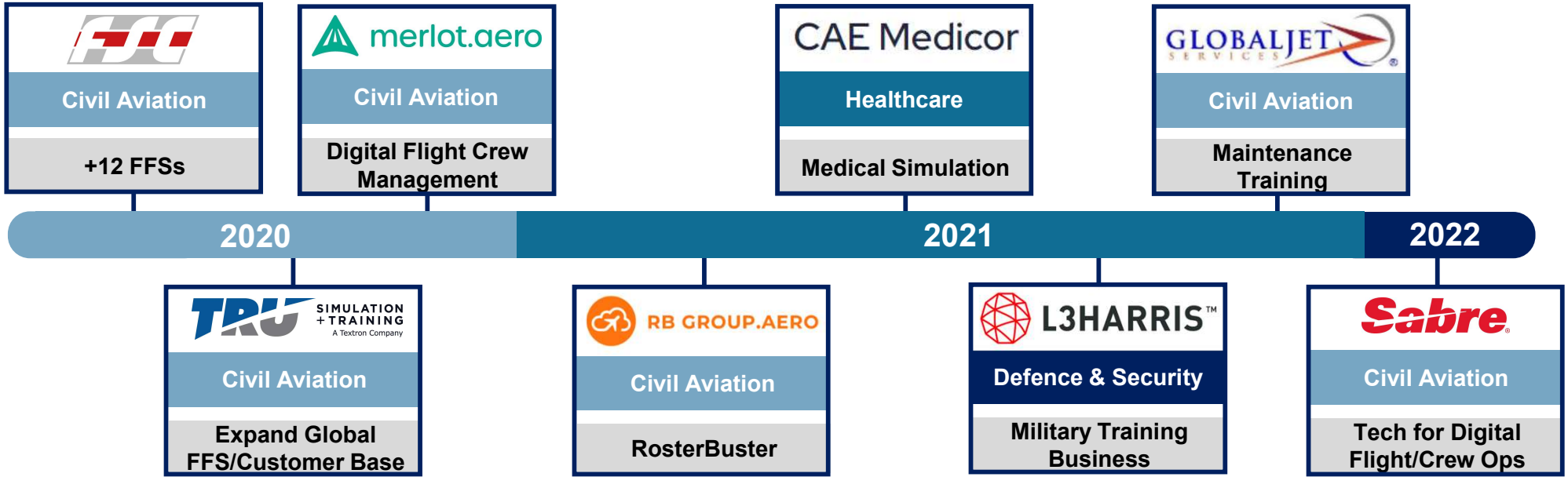
2022

AirAsia India first airline to adopt CAE Rise Training System

(1) CAE Investor Day Presentation (2) Forbes

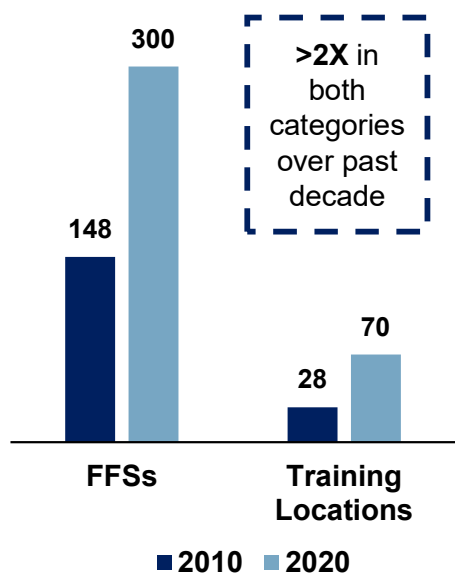


Heightened Inorganic Growth Since 2020

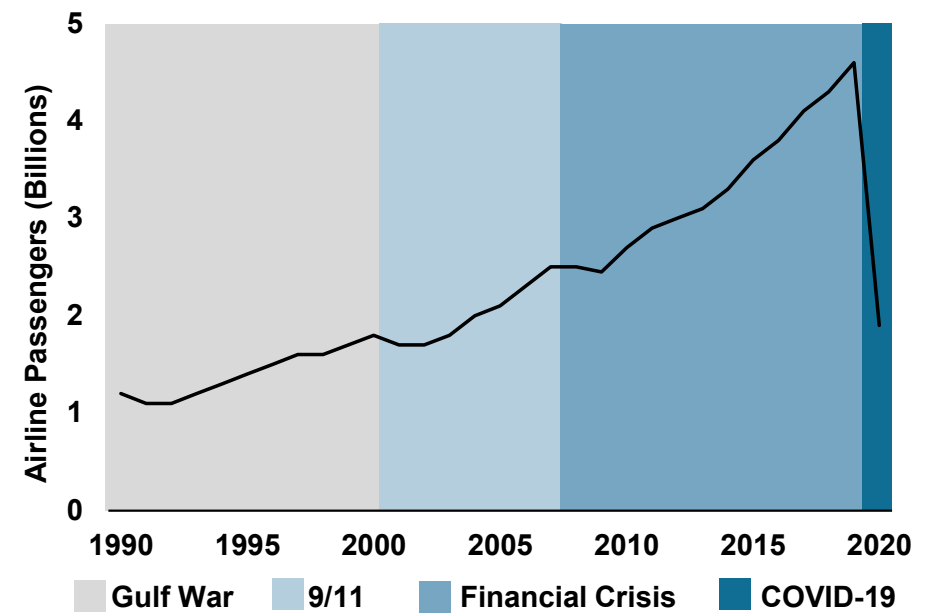


Strategic CapEx + R&D Increasing Global Presence...

- \$480+ million deployed on CapEx and R&D over past 2 years
- 21 FFS network deployments in past 2 years
- 50 FFSs relocated since start of pandemic
- 48 FFSs sold in FY22 (including first eVTOL* FFS sale)



...Prepares Portfolio for Near-Term Demand Upswing

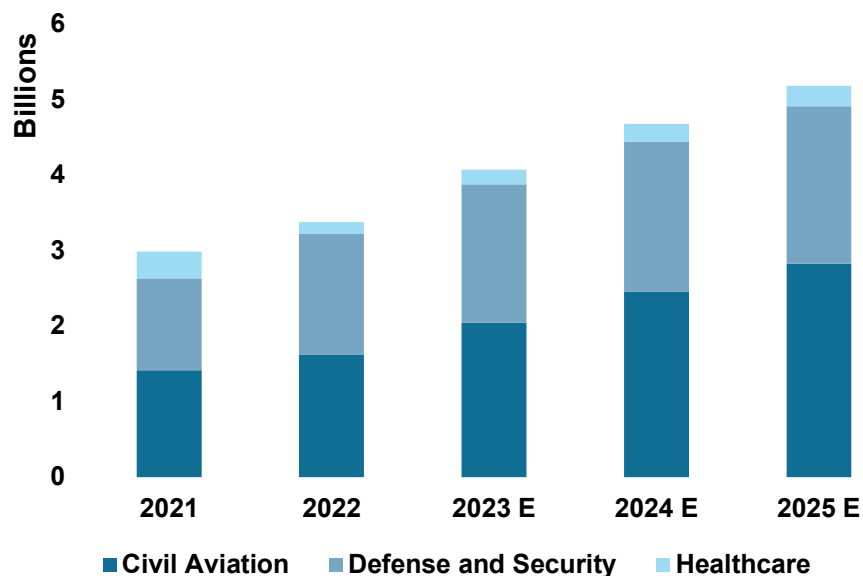


(1) IEA World Air Passenger Traffic Evolution (2) Company Filings

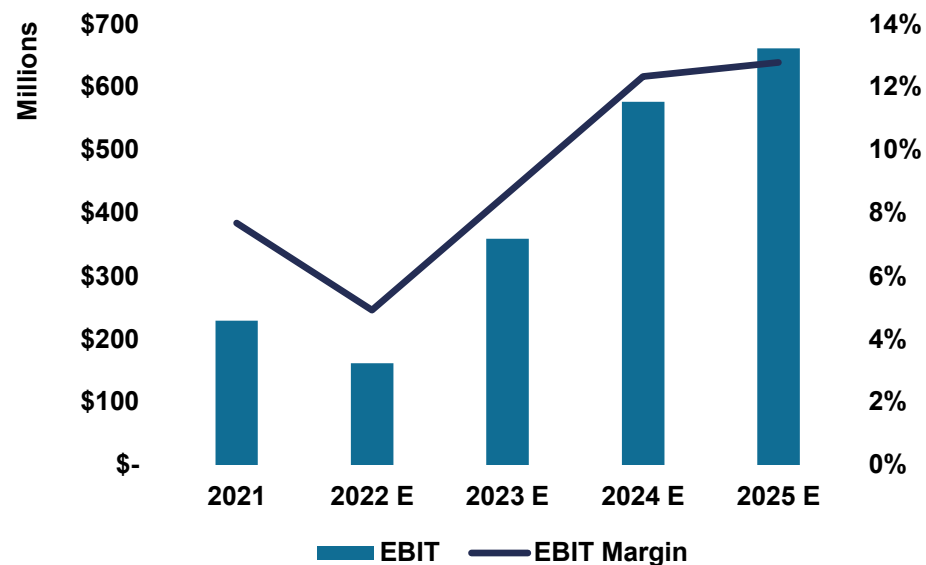


Our Thesis in the Model & Risks

Revenue Segment Mix



EBIT and EBIT Margins



CAE's Bear Case

- ✗ Airlines elect to **train pilots in-house**, particularly larger, American players
- ✗ CAE fails to transition relationships from **dry to wet training**
- ✗ Airlines prioritize **efficient capacity initiatives** that decrease aircraft usage and pilot demand
- ✗ Prolonged **air traffic weakness** from pandemic and recessionary environment
- ✗ CAE fails to **integrate L3H** effectively and does not realize EPS accretion to extent of management guidance

Our View

- ✓ Outsourcing provides up to **20-30% of cost savings** compared to in-house training and allows airlines to transition sizable costs from fixed to variable
- ✓ Multiple partnership evolutions prove that CAE successfully transitions to wet training, especially in economic downturns
- ✓ Flight revenues have increased **70%** from 2021-2022 and pent-up demand from COVID-19 still drives travel activity¹
- ✓ CAE has made 9 accretive deals in 3 years and we have confidence in increased EPS from L3H acquisition due to cost synergies and defense exposure

(1) International Civil Aviation Organization News Release (2) Forbes

Prepare For Takeoff



Valuation

Recommendation: Buy
Price Target: \$29.83
Upside: 40.0%

Summary

- CAE monopolized 3rd party pilot training amid travel demand recovery and a structural shortage of pilots
 - As airlines face challenging headwinds, CAE provides **cost savings** and flexibility through outsourced training
 - New regulations require **increased training hours** and fewer providers, increasing CAE's moat
 - CAE will see increased margins as more of their revenue transitions to **training services**
 - CAE is well positioned to meet increased demand following **aggressive M&A and CapEx**



Culverhouse Investment Management Group Team Members: Joleigh Underwood, Audrey Stoettner, Abigail Britton, Cameron Ninneman
 CAE Inc (NYSE: CAE) Values in millions CAD
 Recommendation: BUY Except per share and share count (Final value/price in USD)

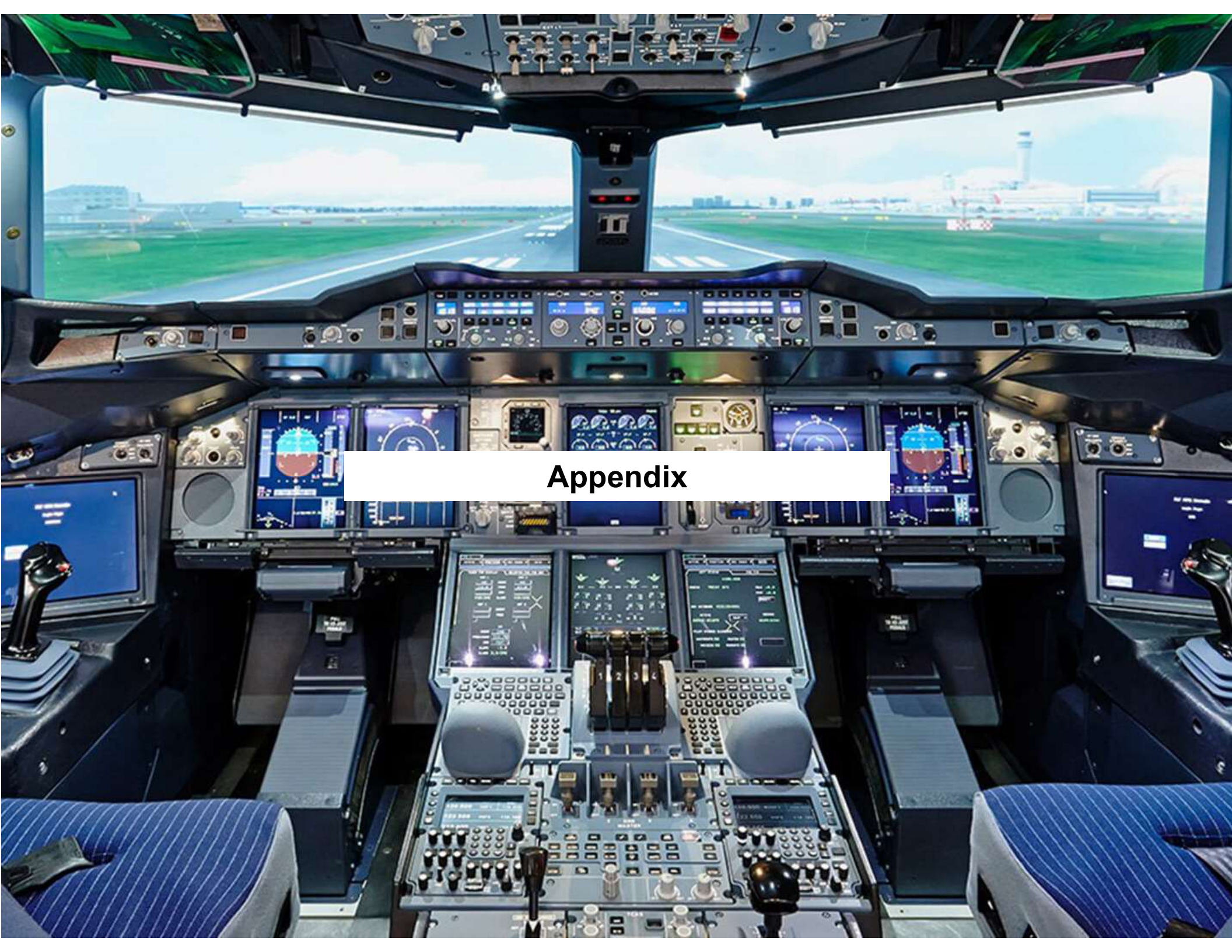
| DCF | |
|---------------------|----------|
| Discount Rate | 10.3% |
| LTGR | 2.0% |
| Sum of PV | \$6,141 |
| Terminal Value | \$10,099 |
| EV | \$16,240 |
| (+) Cash | \$192 |
| (-) Debt | \$ 3,265 |
| Equity Value | \$13,167 |
| Diluted Shares Out | 318 |
| Implied Value | \$41.42 |
| Exchange Rate | 0.72 |
| Implied Value (USD) | \$29.83 |
| Current Price | \$21.31 |
| P/V | 0.71 |
| Upside | 40.0% |

| WACC Calculation | |
|--------------------|----------|
| Risk Free Rate | 3.52% |
| Market Return | 10% |
| Equity Beta | 1.57 |
| Interest Rate | 4.9% |
| Tax Rate | 21% |
| Current Price | \$21 |
| Basic Share Count | 318 |
| Cost of Equity | 13.70% |
| Cost of Debt | 4.86% |
| Equity Amount (\$) | \$6,774 |
| Debt Amount (\$) | \$3,486 |
| Total | \$10,259 |
| WACC | 10.3% |

| Sensitivity Table | | | | | |
|-------------------|-------|-------|-------|-------|-------|
| | 2.00% | 2.25% | 2.50% | 2.75% | 3.00% |
| 9.0% | \$34 | \$35 | \$36 | \$38 | \$39 |
| 9.5% | \$32 | \$33 | \$34 | \$35 | \$37 |
| 10.0% | \$31 | \$32 | \$33 | \$33 | \$34 |
| 10.5% | \$29 | \$30 | \$31 | \$32 | \$33 |
| 11.0% | \$28 | \$29 | \$30 | \$30 | \$31 |

| Constants | |
|-----------|----------|
| Price | \$ 21.31 |
| Cash | \$ 192 |
| OLL | \$ 221 |
| Debt | \$ 3,265 |
| DSO | 318 |

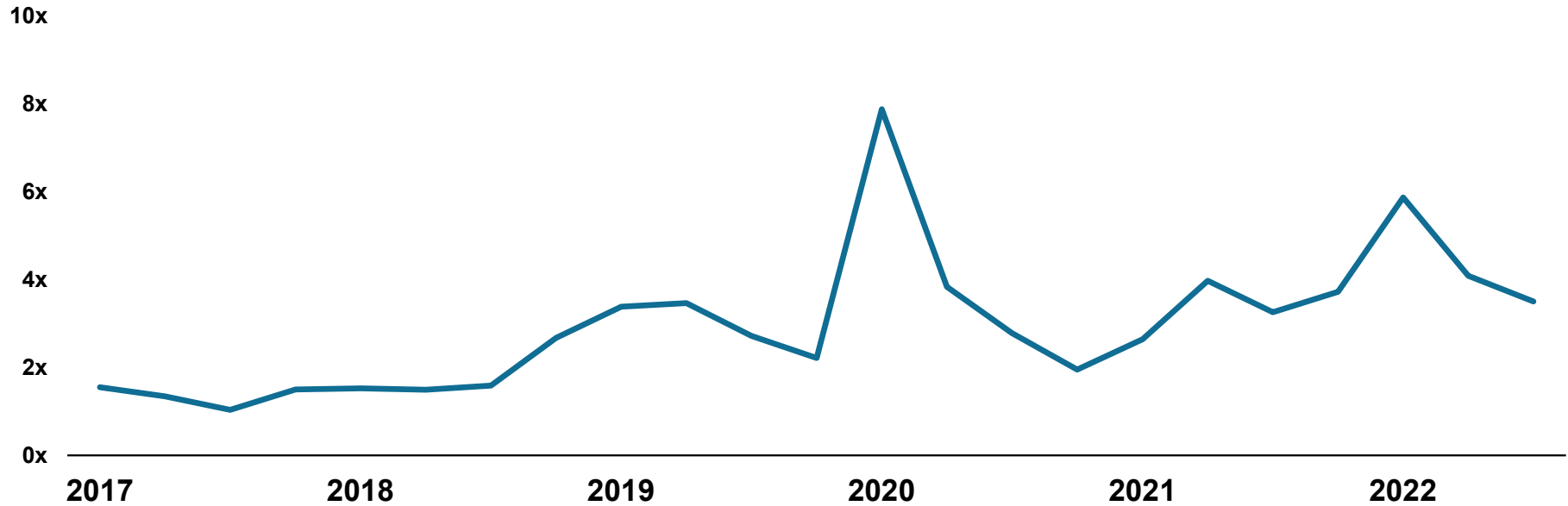
| Weighted-Average Debt Calculation | | | | | | |
|--|------------|---------|-------------|---------|---------------|----------|
| | Repay Date | Current | Non-current | Total | Rate or LIBOR | Interest |
| Unsecured senior notes | | | | | | |
| U.S. dollar, fixed rate - 3.60% to 4.90% | 2022-2034 | \$17 | \$1,177 | \$1,194 | 4.90% | \$59 |
| Canadian dollar, fixed rate - 4.15% | 2022-2027 | \$3 | \$24 | \$27 | 4.15% | \$1 |
| Term loans | | | | | | |
| U.S. dollar, variable rate | 2022-2025 | \$70 | \$443 | \$513 | 4.80% | \$25 |
| Canadian dollar, variable rate | 2022-2028 | \$6 | \$29 | \$35 | 4.80% | \$2 |
| Other | 2022-2026 | \$14 | \$58 | \$73 | 4.80% | \$3 |
| Total Actual Debt | | | | \$1,841 | | \$89 |
| Weighted Average Interest Rate | | | | | | 4.9% |



Appendix



Net Debt/EBITDA



Management guiding to **<3x Net Debt/EBITDA** by mid CY2023

Diluted EPS

