

OEM Capital – Defense Electronics Technology MARKET FOCUS

January 2011

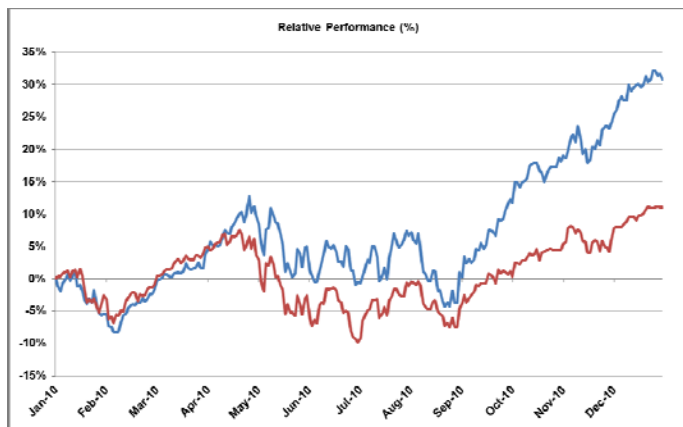
MONTHLY MARKET PERFORMANCE:

Closing Prices as of December 31, 2010

Current Company Name	Market Cap ¹	Revenue ¹	% Price Change [30 day]	% Price Change [YTD]	P/E
Advanced Photonix Inc.	42.2	23.0	42.1 ▲	118.9 ▲	NM
AeroVironment, Inc.	585.5	262.2	8.7 ▲	(9.4) ▼	40.9
AML Communications Inc.	14.5	16.0	5.5 ▲	(9.5) ▼	12.1
Anaren Inc.	311.1	175.4	4.9 ▲	38.6 ▲	21.3
Astronics Corp.	230.9	189.5	0.6 ▲	127.3 ▲	22.9
Dynamics Research Corp.	134.5	268.1	(0.4) ▼	25.9 ▲	10.9
EMS Technologies Inc.	302.9	342.1	6.6 ▲	39.3 ▲	30.7
Endw ave Corp.	22.3	16.2	(14.0) ▼	(4.2) ▼	NM
Espey Manufacturing & Electronics Corp.	55.2	28.1	0.3 ▲	21.2 ▲	16.2
Giga-tronics Inc.	13.2	19.3	2.3 ▲	(20.1) ▼	43.7
Frequency Electronics Inc.	55.4	50.2	8.9 ▲	32.1 ▲	35.0
Global Defense Technology & Systems, Inc.	154.2	206.3	23.0 ▲	3.0 ▲	36.9
Herley Industries Inc.	243.2	189.4	5.0 ▲	22.8 ▲	16.0
Hittite Microwave Corporation	1,880.8	222.3	3.6 ▲	49.5 ▲	27.6
Kratos Defense & Security Solutions, Inc.	244.4	362.9	24.1 ▲	21.9 ▲	130.6
KVH Industries Inc.	181.5	111.5	(11.0) ▼	(20.5) ▼	31.2
LaBarge Inc.	248.3	324.0	9.5 ▲	29.5 ▲	13.5
Mercury Computer Systems, Inc.	447.6	214.9	(3.4) ▼	57.6 ▲	29.5
Micronetics Inc.	20.6	35.1	(2.2) ▼	39.1 ▲	8.2
Orbit International Corp.	17.8	27.3	3.7 ▲	3.7 ▲	77.0
Sparton Corp.	84.2	171.6	5.2 ▲	43.5 ▲	23.8
Spectrum Control Inc.	194.3	163.9	(3.2) ▼	56.0 ▲	13.8

¹ (\$ millions)

OEM DEFENSE ELECTRONICS TECHNOLOGY INDEX:



■ OEM Defense Technology Index ■ S&P 500 Index

SELECTED STATISTICS FOR INDEX COMPANIES:

Trading Multiples	CY2007	CY2008	CY2009	Latest
TEV/Total Revenue	1.6x	1.4x	1.3x	1.4x
TEV/EBITDA	12.1x	10.2x	10.3x	8.9x
TEV/EBIT	15.5x	13.1x	14.4x	11.4x
Profitability				
Return on Assets %	6.4%	6.9%	5.4%	7.0%
Return on Capital %	12.4%	13.6%	10.6%	8.5%
Return on Equity %	9.2%	3.0%	3.1%	9.3%
Margin Analysis				
Gross Margin %	28.7%	28.7%	27.7%	28.8%
SG&A Margin %	14.7%	14.4%	14.6%	13.2%
EBITDA Margin %	13.1%	14.0%	12.7%	15.5%
EBIT Margin %	10.1%	10.8%	9.1%	12.1%
Net Income Margin %	5.8%	1.7%	2.4%	6.4%
Growth Rates				
Total Revenue, 1 Yr Growth %	20.4%	11.8%	(0.7%)	14.5%
Total Revenue, 2 Yr CAGR %	17.5%	15.7%	5.4%	9.1%
Total Revenue, 3 Yr CAGR %	16.6%	15.3%	9.8%	10.2%

Source of financial data: Standard & Poor's, CapitalIQ, FT and Thomson Financial

MARKET COMMENTARY:

The OEM Defense Technology Index is up 31.7% over the last twelve months, compared to 11.2% for the S&P 500 Index during the same period. The Index is comprised of publicly traded US defense electronics companies with annual revenues under \$400 million.

COMMENTARY

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Take a look at the relatively high price-to-earnings multiples in the chart to the left. They have a median valuation of 23.7x the trailing twelve months earnings. Compare this to the low teen multiples for Tier 1 and 2 defense contractors. Scarcity with the prospect of a buyout seems to be driving them higher since September 2010 because it is not the prospect of a defense budget growing 5% per year over the last decade.

Private Equity Group (PEG) deals in all industries rebounded in 2010. Buyout shops closed 3,380 transactions valued at \$225 billion, almost twice the volume of 2009 (Thompson Reuters) but it was the worst year since 2004 for fundraising. 484 funds reported raising a total of just \$225 billion. There is over \$600 billion in dry powder. If the IPO market heats up in 2011 we expect opportunistic PEG exits.

NOTABLE RECENT TRANSACTIONS:

Raytheon Space & Airborne Systems, a subsidiary of **Raytheon Co. (NYSE:RTN)** agreed to acquire all of the outstanding shares of **Applied Signal Technology, Inc. (NasdaqGS:APSG)** for \$510 million in cash. **Applied Signal Technology** is a provider of intelligence, surveillance, and reconnaissance capabilities to companies in the defense, intelligence, and homeland security markets.

TeleCommunication Systems, Inc. (NasdaqGS:TSYS) agreed to acquire **Trident Space & Defense, LLC** from private equity firm Admiralty Partners. Financial terms of this transaction were not disclosed. **Trident Space & Defense**, based in Torrance, California, is a supplier of electronic products and services to the military, aerospace, and industrial markets.

CDI-Aerospace, LLC, a subsidiary of **CDI Corp. (NYSE:CDI)** agreed to acquire Bridgewater, New Jersey based **DSPCon, Inc.** Terms of the transaction were not disclosed. **DSPCon** is a provider of data acquisition and analysis products used in military, government, aerospace, and commercial applications.

OEM Capital

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