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Q3 2024 AAR Corp Earnings Call

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PRESENTATION

Operator

Good afternoon, everyone. Welcome to AAR's Fiscal 2024 Third Quarter Earnings Call. We are joined today by John Holmes, Chairman, President and Chief Executive Officer; and Sean Gillen, Chief Financial Officer.

Before we begin, I would like to remind you that comments made during the call may include forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. These forward-looking statements involve risks and uncertainties that could cause actual results to differ materially from the forward-looking statements.

Accordingly, these statements are no guarantee of future performance. These risks and uncertainties are discussed in the company's earnings release and the Risk Factors section of the company's annual report on Form 10-K for the fiscal year ended May 31, 2023, and Form 10-Q for the fiscal quarter ended February 29, 2024, which we expect to then file with the SEC shortly.

In providing the forward-looking statements, the company assumes no obligation to provide updates to reflect future circumstances or anticipated or unanticipated events. Certain non-GAAP financial information will be discussed on the call today. A reconciliation of these non-GAAP measures to the most comparable GAAP measures is set forth in the company's earnings release.

A replay of this conference call will be available for on-demand listening shortly after the completion of the call on AAR's website.

At this time, I would like to turn the call over to AAR's Chairman, President and CEO, John Holmes.

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

Thank you, and good afternoon, everyone. I appreciate you joining us today to discuss our third quarter fiscal year 2024 results.

Before we discuss the results, I would like to take the opportunity here to again welcome the Triumph Product Support employees to the AAR family. The close of the acquisition and related financing transactions just subsequent to the end of our quarter, this business, which is now part of our Repair & Engineering segment, meaningfully scales our previous component repair operation, add differentiated repair capability on both current and next-generation platforms and expands our footprint into the higher-growth Asian market. Integration is off to a great start, and I am very, very excited about what we can do with this business.

Turning to the results. We delivered another strong quarter. Specifically, sales were up 9% year-over-year from $521 million to a third quarter record of $567 million. Sales to commercial customers increased 18%, more than offsetting a 7% decrease in sales to government customers.

For Parts Supply, total sales were up 6% year-over-year, driven by strong performance in our commercial distribution business.

In USM, demand remains exceptionally strong, which drove another quarter of growth. To break that down further, individual USM parts sales were up significantly year-over-year but large asset transactions such as whole aircraft and whole engine sales were down. This reflects even tighter supply in this market.

For example, opportunities like the 757 acquisition that we made from American Airlines last year are even more difficult to find. Having said that, we have the best sourcing team in the world and continue to have the balance sheet flexibility to be able to act quickly when those opportunities do arise.

I mentioned strong commercial distribution performance, and I would like to highlight that specifically. Commercial distribution had an exceptional quarter posting 27% organic growth. This was driven by growth from existing product lines as well as the early ramp of recently announced wins.

Government distribution had a lower quarter when compared to a very strong quarter a year ago. However, government bookings have been increasing, and we expect growth to return to that business moving forward.

In Repair & Engineering, sales were up 10% over the prior year quarter as we were able to drive greater volumes through our hangars. I'm proud of the efficiency gains we continue to make with our existing footprint.

In Integrated Solutions, sales were up 15% over the prior year quarter due to increased flight hours in our commercial power-by-the-hour programs and the contribution from TRAX.

Finally, in Expeditionary Services, sales were down 15% over the prior year quarter due to a decline in shipments of pallets to the U.S. Air Force. As a reminder, we have a sole-source provider of these pallets, and we expect the DoD's procurement volumes to return to more normalized levels in our FY '25.

Turning to profitability. Our adjusted operating margin was 8.3%, up from 7.6% in the prior year quarter driven by margin expansion in Parts Supply and Repair & Engineering. This represents our 12th straight quarter of year-over-year adjusted operating margin expansion, and our margins are now approximately 50% higher than they were before COVID. We are especially proud to have made this progress in an inflationary environment in which labor costs, in particular, have been rising.

Our adjusted diluted earnings per share from continuing operations were up 13% from $0.75 per share to a third quarter record of $0.85 per share. With respect to cash, we generated $20 million in cash flow from operating activities from continuing operations. Our cash flow and EBITDA growth resulted in net leverage at quarter end of just under 1x adjusted EBITDA.

As you know, we elected to finance the Product Support acquisition entirely with new debt. Pro forma for the acquisition, net leverage at the end of Q3 was 3.6x adjusted EBITDA. The decision to finance entirely with debt reflects our confidence in the continued cash flow generation and EBITDA growth and our resulting ability to delever.

Turning to new business. During the quarter, we announced a new multiyear distribution agreement with Ontic to supply certain military products to the U.S. government. We also announced a multiyear contract extension and expansion for flight hour component support services with ASL Airlines.

We also announced TRAX agreements to provide eMRO services to Singapore Airlines as well as eMRO and eMobility services to Archer Aviation. The Singapore Airline award in particular demonstrates the power of the AAR TRAX combination, as AAR was instrumental in securing that award.

Finally, just yesterday morning, we announced an agreement to provide surplus CFM56-5B engine material to Cebu Pacific. This agreement leverages our long-term supply partnership with FTAI Aviation and drives further predictability into our USM operations.

With that, I'll turn it over to our CFO, Sean Gillen, to discuss the results and the acquisition in more detail.

Sean M. Gillen ***AAR Corp. - Senior VP & CFO***

Thanks, John. Our sales in the quarter of $567.3 million were up 8.9% year-over-year. Our commercial sales were up 17.6% year-over-year, driven by commercial growth in each of Parts Supply, Repair & Engineering and Integrated Solutions.

Our commercial distribution sales were a particular standout as we continue to drive sales growth on existing product lines and expanded newly won product lines as well.

Our government sales were down 7.4% year-over-year. However, sequentially, government sales were up 5% as we have started to see a recovery in our government activities within distribution, Integrated Solutions and Expeditionary Services.

Gross profit margin in the quarter was 19.4%, up from 18.1% in the prior year quarter, driven by strong performance in Parts Supply as well as Integrated Solutions, including the high-margin TRAX offering. Gross profit margin in our commercial business was 19.8%, and gross profit margin in our government business was 18.6%.

SG&A expenses in the quarter were $77 million. This included $9.4 million of Triumph Product Support transaction expenses, $2.8 million of TRAX acquisition and amortization expenses, and $2 million of investigation costs. Excluding these items, SG&A was $62.8 million or 11.1% of sales.

Net interest expense for the quarter was $11.3 million, which included $6.1 million of costs related to the bridge financing commitment for the Product Support acquisition that will not recur going forward.

Cash flow provided by operating activities from continuing operations was $20.4 million. This is net of inventory investment in Parts Supply, specifically in commercial distribution, which, as we mentioned, had significant sales growth in the quarter.

Our net leverage at the end of Q3 was 0.95x. As John indicated, we financed the Product Support acquisition entirely with new debt consisting of $550 million of unsecured notes with an interest rate of 6.75%, and an approximately $205 million incremental draw from our revolving credit facility, which we upsized by $205 million in conjunction with the acquisition.

In Q4, we expect our net interest expense to be approximately $18.5 million, which consists of $9.3 million associated with the fixed rate notes and the balance from the floating rate revolver and the amortization of financing expenses.

Going forward and consistent with our reporting for TRAX, our adjusted operating income and adjusted EPS will exclude noncash amortization expense associated with purchase accounting. Our adjusted results will also exclude transaction expenses recognized in Q4 as well as integration costs that we expect to incur over the next 12 to 18 months.

As a reminder, we indicated that we expect to generate $10 million of run rate synergies from the Product Support acquisition and expect that it will be accretive in full year fiscal 2025. However, in Q4, we expect it to be slightly dilutive to earnings as the incremental interest expense associated with the acquisition will modestly exceed incremental operating profit.

As we also indicated previously, we will step up the tax basis, which will generate approximately $9 million of annual cash tax savings for each of the next 15 years. This will not impact our GAAP tax rate or adjusted EPS, and we expect our adjusted effective tax rate to be approximately 27.5%.

Before turning the call back to John, I would like to take this opportunity to thank our bank group for their support of the financing of the acquisition. Their additional $205 million commitment to our revolver reflects their confidence in AAR and the merits of the acquisition, and allowed us to partially finance the acquisition with flexible prepayable debt that facilitates our delevering going forward.

Thank you for your attention, and I will now turn the call back over to John.

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

Great. Thank you, Sean. Regarding the market going forward, the continued new aircraft delivery challenges as well as the GTF and other engine issues means the demand for current generation aircraft and associated maintenance and parts requirements will remain strong. This is good news for AAR.

While this means that USM supply will remain tight, we will continue to leverage our global sourcing network to secure material to meet this demand. This also means sustained high demand for our commercial distribution activities where we expect significant growth to continue coming from both existing lines as well as new contract awards.

In Repair & Engineering, I am excited to announce that we expect to break ground on our airframe MRO facility expansions in both Miami and Oklahoma City this quarter. Once complete in our FY '26, these will add approximately 15% capacity to our network. In the meantime, we will look for ways to drive growth and higher throughput, utilizing our existing footprint like we did this quarter.

In Integrated Solutions, we have a strong pipeline of both government and commercial opportunities, and we expect awards will be made this calendar year. We are also encouraged by the high level of customer interest in the TRAX eMRO suite of offerings.

Regarding Q4, we expect revenue growth in the mid- to high teens, including the contribution from the Product Support acquisition of approximately $65 million to $70 million in sales. And we expect adjusted operating margins of approximately 9% overall, which reflects the accretive contribution from the Product Support acquisition.

More generally, we are incredibly well positioned to continue our growth and margin expansion as we move into our FY '25 and beyond. The TRAX acquisition is working well and the thesis behind the combination is proving out as evidenced by the recently announced Singapore win.

We are incredibly excited about the differentiated high-margin capability that the Product Support acquisition brings, and our team is already pursuing numerous opportunities with our customers.

Overall, our end markets are extremely strong, and we remain focused on executing on our growth strategy.

With that, I'll turn it over to the operator for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question will come from the line of Robert Spingarn with Melius Research.

Robert Michael Spingarn ***Melius Research LLC - MD***

I have a few different questions here. John, first, I thought I'd go back to a couple of your comments on the business. And this concept of a slower OE ramp, leaving more older aircraft in service longer. How is that affect -- really, it's driving the Parts business. How is that affecting MRO because I'm curious if that's increasing demand or lowering it because you just can't get airplanes out of an airline schedule long enough to work on them.

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

Yes. It's a really -- that's a very great question. With respect to your first point on Parts, absolutely. The longer the current generation aircraft fleet is in operation, and obviously, you're seeing very high utilization, the more parts requirements it's going to drive. So it's good news for the Parts business.

For the heavy maintenance business, over the medium term, it will be a positive. It will drive more maintenance requirements. You've got aircraft that were expected to be retired that are now going to end up going in for another maintenance event.

However, in the immediate term, it is driving a lot of movement in the maintenance schedules at the airlines as airlines like United and Southwest, 2 of our big customers, look to move things around to adjust to the new delivery schedules that they're getting out of the OEM. So it's creating a little bit of churn for us in the immediate term. But on the balance, it will be a positive for us.

Robert Michael Spingarn ***Melius Research LLC - MD***

Okay. And then focusing on Parts Supply, I just wanted to think about sequentially through the quarter. The year-on-year growth at 6.5% was solid, but we might have expected a little bit higher, you had good margins. But just on the top line growth and then comparing to prior quarters, how do we think about that 6.5% when we look through the various months of the quarter in terms of front of quarter, back of quarter? Is there a trend?

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

I wouldn't point to much of a trend throughout the quarter. I mean it's fairly steady. But I would parse that 6.5%, right? You've got really 2 kind of major buckets in there. You've got new parts distribution and then you've got USM. And within those 2 buckets, I want to take you a level further.

So in new parts distribution, the commercial business, as we mentioned, just had an outstanding quarter. We're 27% organic growth year-over-year in new parts commercial distribution. And if you look at our peer set, that's about the best that you see out there. So we're really happy with the way commercial distribution is going.

Government distribution had a lower quarter than it did last year. Last year, we had a very strong quarter. This year, we also had a good quarter. It was just lower than last quarter. We had seen bookings, and I believe we've talked about this in prior earnings calls, we have seen government bookings decrease throughout last year. So we're feeling the effects of that now.

On the flip side, we are now seeing government bookings increasing the last several months. So we expect that will drive return to growth in the government distribution as well. So a couple of moving parts on the commercial -- on the new parts distribution side.

And then flipping over to the USM, flipping over to USM, as we mentioned, we kind of break that down into 2 buckets: large asset sales, which are whole aircraft and whole engines, and then the day-to-day parts sales.

The day-to-day part sales are at record levels. We saw double-digit growth in day-to-day part sales in USM. Those packages are the parts at this moment in time are easier to source. So we're getting our hands on those and we're repairing them and reselling them.

The whole assets, the larger dollar assets, those are harder to come by. And so we saw a decline year-over-year in large asset sales. And obviously, the focus of that team is to continue to leverage the global sourcing network to get our hands on the right assets to meet the demand.

So anyway, I wanted to take you through. You got a few different moving parts below that 6.5%. And hopefully, that gives you a little more color.

Robert Michael Spingarn ***Melius Research LLC - MD***

Yes. And just on that comment you made a moment ago, why is it that the smaller batches of components and parts or -- of USM are easier to come by than the full aircraft, et cetera? I guess the full aircraft, if you have a full aircraft somewhere, an airline doesn't want to let that go, they want to put that back in service. Is that the reason?

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

Yes, that's -- exactly. You want the aircraft in service. And then in terms of whole engine, the engine shops are full right now. The slots are full. And so if you've got a spare engine, you're going to want it on a wing and operating.

Robert Michael Spingarn ***Melius Research LLC - MD***

Okay. And then just one more on engines. Given MAX and the geared turbofan situations, with the airlines extending the lives of old aircraft and engines, we see a build-out still with Pratt and CFM on their maintenance networks for these engines, GTF and LEAP. Do you have any interest in getting into the engine MRO market?

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

That question comes up relatively frequently. At this time, our biggest customers in the trading business are the engine MROs themselves, the MTUs, Delta TechOps, et cetera. And so we're not in the business of competing with our customers. Our preference is to be the supplier to support that broadening demand across the engine MRO network.

Robert Michael Spingarn ***Melius Research LLC - MD***

Okay. And then just one quick one for Sean on margins. Just they've been doing well. Your Parts business is strong, within Repair & Engineering, strong demand for airframe MRO. And then with the Triumph asset and the TRAX acquisitions, these being accretive to margins, could you be close to double-digit operating margins at some point in fiscal '25?

Sean M. Gillen ***AAR Corp. - Senior VP & CFO***

Yes. I think that's certainly the focus. As you heard John say, in Q4, we think we'll be around 9%. And if you think about the continued mix shift of Part Supply and the impact of the Triumph Product Support acquisition as well as TRAX, all that's accretive to margins and getting towards that 10%.

Operator

And that will come from the line of Bert Subin with Stifel.

Bert William Subin ***Stifel, Nicolaus & Company, Incorporated, Research Division - Associate***

John, maybe just to follow up to one of the questions there. If we think about the guide for the fourth quarter, mid- to high-teens sales growth would seem to imply mid-single-digit organic growth versus the 9% you just did this past quarter.

It seems like you gave a pretty upbeat outlook though, on a lot of the contributors there. So what's driving the, I guess, slowdown? Is it just comps? Do you think USM is going to decline sequentially, because it sounds like government is getting better, parts distribution is still strong. Maybe there's a little bit of volatility in MRO. But if I put it all together, it seems like it's maybe a little better. So can you just help me understand that equation?

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

Yes. I'd say part of it is comps obviously had some strong performance last year. So that's certainly driving a bit of it. But your comment on government, I would say that overall, we see things improving in government, but we would not expect a meaningful improvement in this quarter.

So we see a similar dynamic in Q4 and as much as you're going to have real strong commercial performance in trading, in commercial distribution as well as in the hangars but that is offset by continued softness in the government market.

As we move through our FY '25, we expect to return to growth in government, which will be a nice match to expected continued strength in the commercial markets as well.

Bert William Subin ***Stifel, Nicolaus & Company, Incorporated, Research Division - Associate***

On the government point, like if I look at the President's budget request for FY '25, and granted, a lot of things can change, it seems to indicate a large retirement cycle. And so far, not really any indications of increased sustainment spending. Are you seeing something different than that? Because it seems like there's optimism toward government that that's going to start to get better once we get into FY '25. So I'm just curious where that's coming from.

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

Yes. We're hearing the same thing that hasn't yet translated into orders. If you look at the stated levels, inventory levels, across the platforms that we support, pretty much without exception, they are below the state of inventory levels to meet the expectations for sustainment. So at some point, we absolutely do expect a replenishment in parts and pallets in particular to meet those stated levels. We haven't seen the inflection point yet.

As I mentioned, in government distribution, we are seeing better months and better bookings which could be a leading indicator that you're starting to see that inflection. But it's not translating yet into something we would call a significant trend.

Bert William Subin ***Stifel, Nicolaus & Company, Incorporated, Research Division - Associate***

Just to clarify, is the -- I guess, the differential is more sort of weakness in parts in government, MRO is steadier and so parts is the opportunity?

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

Government MRO has been steady. The government distribution business, yes, is the opportunity, like in the parts business. For government overall at AAR, we've got opportunities to grow in the government programs business, so the supply chain program. We have a number of bids out there that have not yet been awarded. We would expect to see awards come out this calendar year. They take a while, but when they happen, they're big.

And then again, you've got the Expeditionary business, the mobility business that you'll see improvement there once the pallet awards start to come through. So we got a few different buckets in the overall AAR government business.

Bert William Subin ***Stifel, Nicolaus & Company, Incorporated, Research Division - Associate***

Got it. Okay. Just one last one for Sean. You gave some color on maybe getting closer to 10% as we think about next year. Can you just breakdown where Parts Supply falls into that? It seems like there's maybe an opportunity, USM, I assume, is sort of flattish, but maybe as parts distribution matures, there's an opportunity.

And then I guess as a follow-on to that, can you give us any color on how to think about free cash? Does that start to moderate post some of the parts distribution? Or does that start to get better post some of the parts distribution growth?

Sean M. Gillen ***AAR Corp. - Senior VP & CFO***

Yes. And I think as you think about the margin improvement for the company, Parts Supply has been a big part of that. And if you think about next year, we do think that will continue to be the highest growing part in the highest-growing segment, specifically led by commercial distribution, but also continued growth in USM and Parts Supply operating margin is close to 13%, so accretive to the overall company and will help drive that improved margin outlook next year.

And then in terms of free cash flow, good quarter, $20 million of operating cash in this quarter. If you look earlier this fiscal year, a little bit heavier on the inventory investment to help drive some of that growth. As we get into this next fiscal year, obviously, a big focus on generating cash and delevering as well as growing EBITDA, I think you'll see a little bit better free cash flow performance on that, with the caveat that the USM market, as John talked about, remains dynamic, and we continue to be in a good position to source new material to meet that demand that's growing.

Operator

And that will come from the line of Josh Sullivan with The Benchmark Company.

Joshua Ward Sullivan ***The Benchmark Company, LLC, Research Division - MD & Senior Equity Research Analyst***

John, you called out the GTF issues just in your prepared remarks. What's your sense on how long the cycle looks like on the supplemental GTF worker? When is it peak in your view at this point?

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

I think that is a very popular question to ask in the industry right now. So I don't know that I could give you better insight than anyone else. What I would say, though, is that, generally speaking, between that and the slower overall aircraft introduction, we expect the elevated demand to be measured in years.

Joshua Ward Sullivan ***The Benchmark Company, LLC, Research Division - MD & Senior Equity Research Analyst***

Got it. Got it. And then on the CFM CB relationship, should we expect additional similar relationships to follow down the pipe? Is the relationship with FTAI and maturing to a point where you're expecting an increase in volume of parts at this point?

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

The relationship with FTAI is going very, very well. They're great partners. The relationship has grown beyond the initial expectations, and both of us have expectations that it will continue to grow from here. So that is a meaningful contributor to the USM business, and we expect that to continue to grow.

Joshua Ward Sullivan ***The Benchmark Company, LLC, Research Division - MD & Senior Equity Research Analyst***

Got it. And then just as far as expansion into Asian markets, particularly with the Triumph assets, what do you think the biggest opportunity is? Is it organic? Do you think you're taking share from internal airline capabilities or third-party suppliers?

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

Yes. Great question. We -- one of the most attractive things about the Triumph acquisition was the facility they have in Asia. They've got very unique capability over there, particularly on the structure side. They are set up with next-gen capability to move into platforms like the 787, the A350. And as -- and that's where the majority of those fleets in the world are going.

So as those fleets mature, we are only -- we will be 1 of the 4 providers of structure repair capability in the region to support those large fleets. And that's organic growth as the new aircraft mature.

Furthermore, we see opportunities to expand the capability on the component and accessory side as well in that facility. We're looking at investment opportunities that we can make there to broaden the capability in the region because the competitive set there is somewhat limited as a lot of that work comes back to the west. So we see a lot of opportunity now having a very solid footprint in Asia.

Operator

And that will come from the line of Sam Struhsaker with Truist Securities.

Samuel Pope Struhsaker ***Truist Securities, Inc., Research Division - Research Analyst***

On for Mike Ciarmoli this evening. I was just curious, if you guys can maybe talk in a little more detail about kind of the trajectory of the integration costs for the acquisition moving forward. And then in addition to that, maybe cover a little bit more how thinking about the free cash flow profile in that business as well or kind of the new combined?

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

Sure. I can talk about integration and you want to -- I'm looking at Sean here. He'll take the second.

Okay. So with integration, we expect the overall integration to take 12 to 18 months. More of the costs will be in the back half of that period of time because the real work that's got to get done is setting up a couple of the Triumph facilities to take government work that we'll be transferring from some of our other sites, and that requires physical investment and reconfiguration of the Triumph site, which obviously translates to cost. So we're a few quarters away from that cash outlay.

In advance of that, though, there is work that Triumph today has near identical capability to us in certain areas, and we believe that Triumph will be able to perform the work that we do today more profitably than we do. And so we will start to realize synergy benefit by transferring volume from existing AAR sites to a higher profit environment at the Triumph site. And to transfer that volume were capability already exists requires little to no investment.

So it's a long way to say that at the beginning, not a lot of cash, and it will ramp throughout the 12- to 18-month integration period.

Sean M. Gillen ***AAR Corp. - Senior VP & CFO***

And I'd just add in terms of kind of the integration costs to expect, we've said $10 million of run rate synergies. I'd expect the onetime integration cost to be a little in excess of that over the time period that John talked about.

In terms of free cash flow trajectory, I think, nothing really notable there. There's a little bit of seasonality to our free cash flow. Q4 tends to be a stronger quarter than Q1. Other than that, I think the only real nuance is around the net working capital changes specifically to inventory to support Parts Supply. And I think what you've seen over the past 1.5 years, obviously, we've got a lot of opportunity to put money to work. We'll continue to do so, but also focused on making sure we're disciplined and generating cash to delever over the next couple of years here.

Operator

And that will come from the line of Ken Herbert with RBC Capital Markets.

Stephen Francis Strackhouse ***RBC Capital Markets, Research Division - Associate***

This is Steve Strackhouse on for Ken. So I just wanted to double click on margins one more time. I realized we kind of asked about it a couple of times, but kind of ex Triumph, it looks like margins were doing really well kind of in the quarter and just even thinking back to your Investor Day, give or take 9 months ago. It sounds like you guys are on kind of a better run rate than you might have anticipated. Is there maybe just a couple of things within Parts Supply or Repair & Engineering that's kind of driving those margins higher?

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

Yes. I would say that overall, the team is executing ahead of the plan that we originally envisioned. You're seeing a nice growth out of Parts Supply, which by definition is higher, and really, really strong execution in the Repair & Engineering group.

And I'd like to add that once those -- again, we're a little ways away, but once the facility expansions come online in the Repair & Engineering group, the expansion in Oklahoma City and Miami, we're going to take advantage of the fixed cost base that's already existing, leverage that fixed cost base. And so those expansions should drive further margin improvement in R&D as well.

Stephen Francis Strackhouse ***RBC Capital Markets, Research Division - Associate***

Great. And then just one more, maybe on the Triumph update. I realize that you guys have maybe (inaudible) headed for a full month in-house. But is there any change in how you're thinking about the growth in terms of high single digits there, or is there any change in kind of the margin profile that you're now thinking about internally?

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

No, I would say it's consistent with what we described when we announced the acquisition. The only other color I would give there is that as we've gone to know the team, as we've gotten to know the business even more since closing, we're really, really excited about where we can take this business.

There's a lot of opportunity and a lot of a lot of areas where we can cross-sell what ARR offers with what Triumph offers. So they've got a great set of capability and a great team, and we're excited that we're now together.

Operator

And that will come from the line of Louie DiPalma with William Blair.

Michael Louie D DiPalma ***William Blair & Company L.L.C., Research Division - Analyst***

John, you mentioned this a little bit in the answer to your last question, but how should we think about revenue synergies for the Triumph deal? When the deal was originally announced, there was a focus on the cost aspect. But what are the opportunities with the Triumph deal to make the sum of the part a lot better than each of the individual components?

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

Sure. I would just talk about synergies in general. The $10 million that we've described, those are hard cost synergies that come from footprint rationalization and we feel very, very good about that number at a minimum.

Over and above that, you'd have a couple of buckets. The first, before I get to revenue, the first is the opportunity to in-source repair. AAR, we spend a lot of money with other repair vendors today to support our commercial power-by-the-hour programs. We send out a lot of work that we're in charge of managing. And we also spend a lot of money, millions in repair, to repair assets that we acquire through our trading business. And most of that repair goes to repair parties that are not Triumph.

So there's a synergy opportunity to in-source those repairs, both from commercial programs as well as trading. It would be over and above the $10 million.

And then to your point on revenues in general, I really believe that we've got the best aftermarket commercial sales team in the world, and spending time in Singapore in February, in Europe, earlier this month as well as having a number of meetings here in North America. Our sales team is extremely excited to sell the higher margin, higher engineered capability that we get with Triumph to our existing customer base.

And so while we haven't quantified it yet, the early returns from our internal sales team as well as the initial conversations that we've had with some of AAR's largest customers would suggest that there'll be a lot of opportunity to put Triumph volume through our sales channels.

Michael Louie D DiPalma ***William Blair & Company L.L.C., Research Division - Analyst***

Great. And yesterday, I believe, was the 1-year anniversary of when you've acquired TRAX.

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

It was. Yes. We had a little celebration.

Michael Louie D DiPalma ***William Blair & Company L.L.C., Research Division - Analyst***

Yes, I was wondering, has the debt, has the deal met your expectations if you had to grade the deal on a report card, would it be an A+? And how were and how are the TRAX bookings and what does the pipeline look like?

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

I would say overall, it's definitely meeting or exceeding expectations as we think about the deal. The only mistake we made yesterday was not celebrating in Miami versus Chicago, where it's 28 degrees, but the TRAX deal has gone very, very well, and I highlight a couple of things.

First, the deal that we announced in Singapore, with SIAA, that's a big airline with a big complicated fleet and ultimately, we'll be a very large customer for TRAX, that deal would not have happened in the speed at which it happened if it weren't for the AAR relationships that we had with SIAA. So the thesis of putting a smaller enterprise tracks with a great product together with a bigger company AAR with great relationships, certainly played out there.

Related to that, there are a number of competitions that TRAX is in right now, with other very large carriers where I don't believe that they would be considered in the way that they are today if it weren't for the backing of AAR. So our first priority was to open doors for TRAX. And in the first year since owning it, that's absolutely proving out.

The second priority was to ultimately leverage the TRAX platform as a sales channel for AAR parts. That is something that is absolutely still a focus of ours. We've been focused more on the former and probably spending a little bit more time on the former than we might have anticipated in the first year. But the opportunity to ultimately sell parts through the TRAX network is still very much an element of the strategy that we intend to pursue.

Operator

And we do have a follow-up question from Robert Spingarn with Melius Research.

Robert Michael Spingarn ***Melius Research LLC - MD***

I actually -- I have one for each of you, and they both touched on things you already talked about. Sean, just -- we'll start with you, just quickly, you mentioned delevering the balance sheet. And I just wondered if you could give us some color on the pace of that process as we go here. And maybe how sale of Expeditionary Services would factor in and what the timing on that might be? Is that something that might be sooner rather than later?

Sean M. Gillen ***AAR Corp. - Senior VP & CFO***

Yes. Just maybe first, we have a target net leverage of 1 to 2x, obviously, on the back of this acquisition at 3.6x pro forma. So the focus is to get back down to the high end of that range to 2x, and I think that would be 18 to 24 months would be the time line we'd be looking at for there. And I'd say that's just an organic -- no divestiture associated with that. That'd just be EBITDA growth and cash flow generation across the combined business. Obviously, any divestiture would get you there a bit quicker.

Robert Michael Spingarn ***Melius Research LLC - MD***

Okay. Is that all you want to say on divesting? I mean, is there any other color we can put around that?

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

I would just say that, obviously, deleveraging is a focus of ours. And we have highlighted that Expeditionary Services is not core to the future going forward. However, where the balance sheet was a quarter ago, it wouldn't necessarily have made sense to pursue that in earnest. Obviously, our balance sheet looks a little bit differently. So we're paying a lot more attention to a potential process there.

Robert Michael Spingarn ***Melius Research LLC - MD***

Okay. Okay. That's good. And then -- so John, just -- we just talked about Triumph and some of what it brings to the table. I wanted to go back to something you said last quarter about their position in PMA relative to yours could accelerate your push a little bit.

I know it's early. I imagine this is -- it's not going to happen that quickly. But I wondered where you are in the process? Are you starting to aggregate a list of parts to PMA that might not run afoul of any parts distribution agreements you have in the other parts of your business, like with the OEM parts suppliers?

And first, is there a cost associated with putting this together? And then the last part of this somewhat lengthy question on PMA is, is the gridlock in FAA on the airplane programs impacting the PMA approval process from what you can see?

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

Yes. Great set of questions. And I'm actually very happy you asked about PMA because that is a focus of ours, an early focus of ours. So just a couple of thoughts.

First of all, for AAR's own internal PMA effort, it continues to move along well. We have several parts right now out for approval related to the last part of your question, at this point, based on the office that we deal with, we have not seen any sort of slowness, so things are moving along. Again, inside of AAR, that's a very small effort, but we're excited about the potential there.

As it relates to Triumph, I would say that on the balance, we're more excited about the potential for PMA than we were even before it closed. They've got a nice portfolio, again, a small portfolio, but generating healthy revenue and healthy margin of PMAs that is not in any way in conflict with any of our distribution agreements. So largely interior parts. So it's totally a different part of the aircraft than where we play in distribution. So that's encouraging.

The other thing that's occurred there is they really are not engaged in any meaningful marketing activities for this PMA portfolio. So the sales that they have, which again, are impressive given the small number of parts they have PMAs on, we think that we can, just by putting their PMAs through our distribution channels to market, just grow their existing portfolio of PMAs.

Third thing I mentioned is that they've got an engineering process and PMA design and approval set of procedures that is further advanced than what we have. We have a lot more data than they have in as much as we're working on a 1,000 aircraft a year in our hangars, and we are able to collect data in terms of what parts might make good PMA candidates because of the volume of aircraft that we see. So if you combine our access to data plus their, I would say, more advanced engineering and approval procedures, that's a good combination.

So again, a long answer to, I guess, a long set of questions, but we're very encouraged by the PMA growth. Having said all of that, these are relatively small revenue dollars today inside the overall AAR portfolio. But as you know, it comes with high margin and now that we're together, likely high growth.

Operator

I'm showing no further questions at this time. I would now like to turn the call back over to management for any closing remarks.

John McClain Holmes ***AAR Corp. - CEO, President & Chairman of the Board***

Well, listen, we really appreciate the time and the interest and the very thoughtful questions, everybody, and we look forward to being back here with you next quarter. Thank you.

Operator

This concludes today's program. Thank you all for participating. You may now disconnect.