

AerSale Corporation

NASDAQ: ASLE

PRICE TARGET: \$47

Prescience Point issues a Buy recommendation on AerSale Corporation (“ASLE” or the “Company”), a leading provider of aftermarket aircraft services and equipment, with a near-term price target of >\$47. ASLE offers immediate upside as several imminent catalysts, including FAA approval and an initial order for AerAware, the Company’s game-changing wearable heads up display (“HUD”) product, as well as a large upward revision to FY 2021 guidance, will drive its share price significantly higher.

Prescience Point is long AerSale Corporation. ASLE is one of the most obvious and attractive investments that we have ever seen. We project the Company will grow its adjusted, fully-diluted EPS from \$0.17 in FY 2020 to \$1.08 in FY 2021 to \$1.89 in FY 2022, representing a robust CAGR of 231%. These earnings projections are not optimistic but instead are actually fairly conservative, as most of this projected growth is already “locked in.” Yet, despite the Company’s parabolic growth trajectory, its shares are trading at just 10x FY 2022 earnings, while its peers are trading at 25x – 30x.

So, how can such an extreme mispricing exist in the current, frothy market environment? We believe it is primarily due to the following:

1. ASLE went public in December 2020 via a SPAC and has been negatively impacted by the weakness in the SPAC market throughout most of 2021;
2. Despite reporting record revenues and profits in FY 2020 and again in YTD 2021, the Company has been unfairly lumped together with other airline and airline services and equipment companies who have largely struggled during the pandemic; and
3. The Company has very little sell-side coverage with just one analyst from Cowen currently covering the stock.

We believe now is an ideal time to invest in ASLE as there are three major and imminent catalysts which will likely dissipate this temporary market inefficiency and could result in a more than doubling of the Company’s share price within a month.

These imminent catalysts are as follows:

DATE OF REPORT
10/27/2021

SHARE PRICE
\$19.12

52-WK HI / LOW
\$8.68 / \$19.79

AVG DAILY VOL
107.9K

FULLY-DILUTED
MARKET CAP
\$1,164.7M

Catalyst #1: FAA Approval of AerAware

AerAware is a wearable HUD, adopted from military-grade fighter jet technology, which enables commercial airline pilots to see through inclement weather such as snow, rain, sleet and fog. The product was developed in partnership with Universal Avionics, a division of Israel-based Elbit Systems, who is providing the hardware for the system, while ASLE is leading the engineering, design, modification, installations & certification flights.

For almost two years, ASLE has been working toward securing FAA approval for the product for use on the Boeing 737. Based on recent comments by ASLE management, securing FAA approval appears to be a near certainty. In support, consider our recent conversation with CFO Martin Garmendia, who told us that he believes it is "a matter of when and not if" AerAware will receive FAA approval. In further support, consider the following comments by ASLE management from its virtual presentation at the 2021 Cowen Aerospace/Defense and Industrials conference:

The system has amazed our FAA designated test pilot engineers and the pilots and engineers from potential customers who have flown our test aircraft...It's better than any of the pilots that initially flew the airplane thought it would be once we got all the bugs worked out. The clarity, the vision, seeing through clouds, seeing through smoke, seeing through rain, seeing through snow. It does all that. Our FAA designated test pilot is amazed by it...He says this industry's been waiting for (this technology) for over 20 years. So, he's amazed.

Based on flight data from FlightAware.com of ASLE's [AerAware test plane](#), at the end of September, the Company reached a major milestone by completing its final round of FAA flight tests. This means that, after conducting more than 100 hours of flight tests and making a number of revisions to the system at the FAA's request, ASLE's certification work is now essentially finished. ASLE management has indicated that a final decision by the FAA should come within a couple to a few weeks after final flight testing, so we expect FAA approval should be granted by, and likely well before, mid-November.

Catalyst #2: Launch Customer Order for AerAware

AerAware is a game-changer for the commercial airline industry. An employee from Universal Avionics told us that he believes AerAware is the next big thing in the industry, and that he left his previous job to join Universal in large part because of this product. He also told us that the product is best-in-class and is far ahead of competing products on the market today:

I see this as really a game-changing future technology. I plan to retire off this technology...I have decades of experience in this space. We are just at the beginning of this commercialization process, but we are really are at just the tip of the spear. When I say retirement, I should be able to get a good ten years out of this, and still be in the heyday of just building systems. That's my personal opinion. That's why I'm at this company. I saw what was going on...we are at the beginning of a very exciting product...I'm banking my future on it.

When you look at the technology, we are best-in-class. Our camera performance is better and higher than any other out there. We're the only ones doing a wearable HUD solution that is physically certified today....If you are at a trade show, and you went and looked at the technology, by far we are leading the industry in this segment.

AerAware is a game-changing product because it will save operators hundreds-of-millions of dollars per year by significantly reducing or perhaps even eliminating flight delays and diversions caused by inclement weather. The operational savings created by this product are so substantial that, according to industry sources that we spoke with, the payback period for AerAware is less than two years. Given this substantial ROI, it is not surprising that **several major airlines have already expressed interest in and have flown test flights with the product. Based on flight data of ASLE's AerAware test plane, this includes United Airlines, Alaska Airlines and Southwest Airlines.**

The strong interest that AerAware has attracted from several airlines was confirmed by ASLE management during its Q2 2021 earnings call:

Prescience Point: Are you seeing interest for AerAware from other airlines besides this one launch customer?

ASLE Management: Yes, let's be careful potential launch customer and the answer is yes.

The strong interest AerAware has attracted was further confirmed by the Universal Avionics employee that we spoke with:

There's healthy interest and discussions going on with multiple airlines. Keep in mind, we are at the very tip of the spear here...There are a number of conversations that are in work now, or as I would say, pursuits and opportunities and those are moving along quite well.

Based on ASLE management's public comments over the past year, some of which are provided in the table below, it appears to be a near certainty that the Company will receive an initial large order from a major airline – whom we believe to be United Airlines given the substantial number of AerAware test flights United appears to have conducted – soon before or immediately after receiving FAA approval, which, as just mentioned, we expect to happen before mid-November.

ASLE Management Comments Regarding The Potential AerAware Launch Customer

Event	Management Comments
Q1 2021 Earnings Call	<i>I believe we'll get a contingent order for AerAware subject to having this approved by the FAA in advance.</i>
Cowen February 2021 Presentation	<i>Our potential launch customer has been flying with us for almost half the test flights and we'll continue to demonstrate that aircraft to their senior management because we think they're as excited about it as we are. (they) love it...We're not just demonstrating it to our potential launch customer, but we're also showing it to multiple other airlines...and our expectation is, while that's going on, we'll have interested customers that will sign-up...my suspicion is, is that <u>if we continue on track with our potential launch customer, they'll want it as fast as we can deliver it.</u></i>
October 2020 SPACInsider Fireside Chat	<i>We have in our projections kind of starting for next year forward very small numbers for the AerAware, we greatly expect to exceed those numbers. Just to give you a reference, <u>for 2021 we only have 18 kits being sold in our 2nd half projections. We are talking to a launch customer right now that just threw out a potential order, we will exceed that by multiples.</u></i>
September 2020 Investor Presentation	<i>Our greatest opportunity lies with AerAware, a wearable heads-up display that enables a pilot to see through adverse weather while viewing necessary flight instrumentation in his visor. We are developing this system for multiple aircraft platforms, and our first Company-owned aircraft fitted with AerAware, a 737NG, has just begun flight testing. This is an exciting development for AerSale, and we expect to receive final FAA certification for this offering before year-end. <u>We have received initial interest from a potential launch customer, a major domestic airline</u></i>

Our diligence indicates that the initial order from United Airlines, the apparent launch customer, is likely to be >500 units. In support, consider that 1) ASLE management has stated that the FAA will likely require that an operator must equip its entire fleet of a specific aircraft type with AerAware in order to use the product, and 2) United currently owns 384 737s and will add more than 200 737s over the next two or three years, which will increase the total amount of 737s in its fleet to almost 600.

According to a March 2021 Cowen report on ASLE, AerAware will sell for ~\$400K per unit with gross margins of 60% - 70%. During a recent conversation, ASLE management confirmed to us that these estimates are reasonable and fairly accurate.

From March 2021 Cowen Report on AerSale:

AerAware Certification Potential In H1 - ASLE expects that AerAware will be certified by the FAA in H1 following test flights (with the FAA) that begin in late March and FAA review of the AerAware's software code (will be provided by subcontractor, Elbit Systems, in a few months). This should allow for commercial AerAware sales in Q3 or Q4. For context, we est. that AerAware will sell for approx. \$400K/each at 60-70% gross margin. To be fair, mgmt's expected certification timing for AerAware has slipped a few times in the past, so timing remains a risk.

Given these extremely attractive unit economics, a single launch customer order, just by itself, will be transformative for the Company's financial performance. For example, as shown in the table below, assuming

an order size of 500 units delivered over two years, we project that the AerAware launch customer order will add an additional \$0.80 to the Company's annual fully-diluted EPS in FY 2022.

PP-Estimated FY 2022 EPS Contribution from Initial AerAware Order

(\$ in millions, except unit and per share amounts)

	FY 2022
# of Units Delivered	250
(*) Average Selling Price	\$0.4
Revenue Contribution	\$100.0
Gross Profit Contribution	\$65.0
% Margin	65.0%
Less: Incremental SG&A Expenses	(\$3.0)
Net Income b/f Taxes	\$62.0
Less: Taxes	(\$13.0)
Net Income b/f Taxes	\$49.0
(÷) Fully-Diluted Shares Outstanding ⁽¹⁾	60.9
PP-Estimated EPS Contribution From AerAware	\$0.80

Source: Prescience Point estimates, sell-side reports, and public comments by ASLE management.

(1) Includes 17.25m public warrants and 0.718m private warrants.

Catalyst #3: Large Upward Revision to FY 2021 Guidance

Based on the Company's strong YTD performance, it is a near certainty that the Company will have to substantially raise its FY 2021 adjusted EBITDA guidance, which currently stands at \$60m - \$70m, when it reports Q3 earnings in late October / early November. ASLE has already generated \$46.9m of adjusted EBITDA through the first two quarters of the year, including \$30.4m in Q2, and only needs to generate an additional \$23.1m in Q3 and Q4 to exceed the top-end of its current guidance target.

As strong as the Company's financial performance was in the first half of the year, we believe it will be even stronger in the second half. The significant growth in the Company's adjusted EBITDA from Q1 2021 to Q2 2021 was primarily driven by the sale of 3 aircrafts, including 2 of the 24 Boeing 757s that the Company purchased last year to take advantage of the strong demand for cargo conversion aircraft. During its Q2 2021 earnings call, ASLE management disclosed that it already had sale commitments for 11 additional converted 757s, and that it expected to sell the majority of its available 757s by the end of 2021. Based on these disclosures, we expect the Company's aircraft sales in both Q3 and Q4 will be double what it was in Q2.

Assuming a doubling of quarterly aircraft sales at an average gross margin of 35%, and conservatively assuming zero growth for the remaining business lines relative to Q2, we model that ASLE will generate \$62.4m of adjusted EBITDA in the second half of FY 2021, and \$109.4m for the full year. This is 56% higher than the top-end of the Company's current adjusted EBITDA guidance range. As shown in the table below, based on our projected FY 2021 adjusted EBITDA of \$109.4m, we project that the Company will generate \$1.08 of adjusted, fully-diluted EPS in FY 2021.

PP-Estimated FY 2021 Adjusted, Fully-Diluted EPS

(\$ in millions, except per share amounts)

	Q1'21	Q2'21	Q3'21	Q4'21	FY 2021
Adjusted EBITDA	\$16.5	\$30.4	\$31.2	\$31.2	\$109.4
Less: D&A	(\$3.5)	(\$3.2)	(\$3.2)	(\$3.2)	(\$13.1)
Less: Interest Expense	(\$0.3)	(\$0.3)	(\$0.3)	(\$0.3)	(\$1.0)
Plus: Other Income (Expenses)	\$0.1	\$0.2	\$0.0	\$0.0	\$0.2
Less: Change in FV of Warrant Liabilities	(\$0.2)	(\$0.4)	\$0.0	\$0.0	(\$0.6)
Less: CARES Act Proceeds	(\$6.4)	(\$8.4)	\$0.0	\$0.0	(\$14.8)
Plus: Inventory Writedown	\$0.0	\$4.8	\$0.0	\$0.0	\$4.8
Plus: Stock-Based Compensation	\$0.1	\$0.1	\$0.1	\$0.1	\$0.3
Adjusted Income b/f Taxes	\$6.4	\$23.1	\$27.8	\$27.8	\$85.2
Less: Taxes	(\$2.5)	(\$5.1)	(\$5.8)	(\$5.8)	(\$19.3)
Adjusted Net Income	\$3.9	\$18.0	\$22.0	\$22.0	\$65.9
(÷) Fully-Diluted Shares Outstanding ⁽¹⁾	60.9	60.9	60.9	60.9	60.9
PP-Estimated Adjusted, Fully-Diluted EPS	\$0.06	\$0.30	\$0.36	\$0.36	\$1.08

Source: Prescience Point estimates and ASLE filings with the SEC.

(1) Includes 17.25m public warrants and 0.718m private warrants.

Valuation

Driven by the catalysts detailed above, **we expect ASLE shares to more than double over the near-term from the current share price of \$19.12.**

In FY 2022, we project that ASLE's core business will remain flat YoY and generate adjusted, fully-diluted EPS of \$1.08. We also project that the Company will generate an additional \$0.80 of fully-diluted EPS from delivering 250 AerAware units to its launch customer in FY 2022, and that the Company will not receive any additional AerAware orders beyond this initial order. **Based on these very conservative projections, we estimate that ASLE will generate \$1.89 of adjusted, fully-diluted EPS in FY 2022.**

ASLE's peers in the aviation equipment and services market trade at a multiple of around 25x – 30x forward year earnings. Given that ASLE generates higher margins and is growing at a much faster rate than its peers, most of whom have actually experienced a significant decline in financial performance due to the pandemic, we believe that ASLE shares should, at the very least, trade at a multiple that is in-line with its comparables.

Based on our projection that ASLE will generate \$1.89 of adjusted, fully-diluted EPS in FY 2022 and assuming a very conservative multiple of 25x, **we value ASLE shares at \$47.13 today (25x earnings multiple * \$1.89 of adjusted, fully-diluted EPS).** This represents a 146.5% premium to the current share price of \$19.12.

ASLE Valuation	
PP-Estimated FY 2022 Adj. Fully-Diluted EPS	\$1.89
(*) Forward Year PE Multiple	25.0x
PP Target Price	\$47.13

Source: Prescience Point estimates

Over the longer-term, we believe that ASLE shares have a good chance of reaching and perhaps even exceeding \$100 within the next two to three years. Given the massive addressable market and limited competition for AerAware for the foreseeable future, the Company is likely to receive large orders from several airlines for this product beyond its initial launch customer. During a conversation earlier this year, CEO Nicolas Finazzo expressed confidence to us that the Company's annual sales of AerAware could eventually amount to around 1,000 units. In addition to the bullish long-term outlook for AerAware, the Company's core asset management business should greatly benefit from what is expected to be the greatest re-equipment "super-cycle" in the airline industry's history as a record number aircraft are projected to be retired over the coming 18-24 months.

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