

Due Diligence Review

Extra Aircraft, LP

As Related To A Proposed Transaction To Establish
A Production Facility In Montrose County, Colorado

Prepared for

Montrose County, Colorado

Note:

This document is prepared for the exclusive use of Montrose County Colorado.

The analysis contained in this document is based on documents and data provided by Montrose County, and by Extra Aircraft, LP, as well as readily available published information, and the industry experience and informed judgment of Boyd Group International staff.

The conclusions and recommendations contained herein are based on analysis of data from sources deemed reliable as of September 2010, but not guaranteed. Moreover, due to the dynamic nature of the aviation industry, including associated risk factors, actual operational and/or financial results are not guaranteed.

This document is intended as a market overview in regard to a specific economic development proposal under consideration by Montrose County, and is not, nor is it to be considered in any way, a financial or investment recommendation regarding any segment of the aviation industry.

BoydGroup

INTERNATIONAL

Aviation Forecasting & Strategic Solutions

78 Beaver Brook Canyon Road
Evergreen, Colorado 80439
Tel: (303) 674-2000 Fax: (303) 674-9995

www.AviationPlanning.com

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I. Overview

Project Scope

Boyd Group International was retained by Montrose County, Colorado to review the viability of Extra Aircraft, LP, specifically and only in regard to a proposal to establish an assembly facility adjacent to Montrose County Airport.

In the short timeframe of this project, and utilizing data that was provided or could be gleaned from public sources, the following is the understanding of Boyd Group International in regard to this matter:



EA 330 LT

The current production in Germany is focused mostly on aerobatic aircraft, which are greatly respected in their class.



EA 500

The aircraft for which the Montrose facility is initially intended represents entry into a market segment materially different than the EA-330.

Two of these have been built, with a third in production.

- Extra Aircraft, LP is the U.S. presence of Extra Flugzeugproduktions- und Vertriebs-GmbH of Germany. It has a proposal to establish a facility to assemble and accomplish the final-build of the EA 500, a 6-seat single-engine turboprop business aircraft.
- As envisioned, the aircraft fuselages, wings, empennage, and landing gear would be shipped to Montrose from the Extra factory located in Germany. The Montrose facility would complete the construction including installation of avionics and the U.S.-produced Rolls-Royce engine.
- The proposed Montrose facility, as expressed by Extra Aircraft to Montrose County officials, would be intended to eventually produce over 40 finished aircraft per year, and eventually employ over 200 people. Extra Aircraft advised the County that their plan was to scale assembly from approximately 12 units in the first full calendar year, ramping production up to over 40 in five plus years.
- In exchange for the establishment of this facility, the County has been asked to agree to an arrangement that, as currently structured, would entail the County to spend approximately \$2.19 million.¹

The purpose of this analysis is to provide an independent overview of the portions of the proposal made by the Montrose Economic Development Corporation (MEDC) to Extra that specifically involve the

¹ This figure is based on the appraised value (\$675,000) of a parcel of land that the County would buy as a part of the transaction. The actual purchase price that is in the proposal submitted by the MEDC to Extra Aircraft was listed at \$2.3 million. The County has advised that legal considerations limit the amount the County can pay for this property to the fair market value. Therefore the dollar value used in this document is the appraised value - \$675,000.

County. Based on the data and information available, recommendations regarding the risk and benefits it may represent to Montrose will be made in this document.

Project Limitations

This project is not, and must not be construed as, a due diligence of Extra Aircraft, LP per se. It is a due diligence review only of the proposed transaction between that company and Montrose (as defined as the County and the MEDC which are jointly involved in the Extra proposal) as it affects Montrose County.

It is specifically noted that this matter was accomplished based on a number of assumptions, including:

- It was assumed within this document that the aircraft involved, the Extra Aircraft 500, would be fully operational with respect to governmental approvals.²
- The performance of the aircraft was assumed to be as expressed by Extra Aircraft and that the sales and distribution system as represented by Extra's management was or would be shortly in place.

Data Sources

Boyd Group International relied upon the following sources of data for completion of this analysis:

- Publicly-available information on Extra Aircraft, LP and Extra Flugzeugproduktions- und Vertriebs-GmbH including its product lines, history, management, and sales;
- Confidential documents were reviewed by Boyd Group International staff in the offices of the attorney for Extra Aircraft in Montrose. These included what were represented to be three years of audited financials for the current German operation. It is not clear – nor was the matter pursued – whether such data is publicly-available under German law. For the purposes of this project it is assumed that any specifics in such documents are not public knowledge and are not revealed in this document.³

² The EA 500 does not as yet have certification from the US Federal Aviation Administration. Because the aircraft does have European certification, getting FAA certification will not likely be difficult, and is for the purposes of this analysis not considered a challenge to the market viability of the EA 500.

³ To be clear, there were no data in the confidential information that revealed anything negative regarding Extra Aircraft, LP. The recommendations and conclusions in this report are based on data and information entirely in the public sector as they relate specifically to the Montrose County involvement.

Extra advised the County that it planned to assemble 12 aircraft in the first full year of operation, ramping up to 36-40 in subsequent years.

The company noted that the facility could eventually support 200 jobs.

- Additional data and information were supplied during discussions with Mr. Ken Keith, the primary shareholder of Extra Aircraft, and Mr. Errol Bader, the head of Corporate Development for the company, held at the offices of Boyd Group International on August 26, 2010.
 - A second meeting was held with these officials on September 8, 2010, where they provided additional information. This additional information was provided at a point when initial drafts of this document were being compiled. However, such information provided at that meeting did not have any effect on the initial and the final conclusions of this document.
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Disclaimer

Boyd Group International, its principals and staff, have no interests, financial or otherwise, in Extra Aircraft, LP, any of its competitors or potential competitors, or any other party to this matter.

II. Overview

It is understood that the expenditures that the County would be required to make under the terms of the MEDC proposal to Extra Aircraft would be in addition to other sources involved in the proposal. It is again noted that the scope of this report is focused only on the financial contribution of Montrose County, and the risks involved to the County.

The full mechanics of the MEDC offer to Extra are complex.

Extra Aircraft, LP

The project at hand is to provide input regarding the exposure to the County based on the financial support it would need to contribute.

As a result of the research and analyses discussed below, Boyd Group International has made the following observations regarding Extra Aircraft, LP and the transaction as proposed by the Montrose Economic Development Corporation.

- The company in Germany was purchased out of bankruptcy in 2002 by its current owner. It is represented that the bankruptcy was due primarily to debt incurred in the development of the EA 400, a piston-engined predecessor to the EA 500, which is the aircraft intended to be final-assembled at Montrose.
- A bankruptcy eight years ago should be considered as "ancient history" and in light of the company being profitable since then indicates that the bankruptcy event itself is not particularly germane to analysis of the current company. It has continued to have a market for its niche aerobatic aircraft. In addition, approximately 27 E 400 aircraft were sold. (That particular airplane is no longer marketed.)
- The EA 500 is an aircraft that was first put on the market in approximately 2005. Management then decided to take it off the market, citing poor economic conditions. Active marketing of the aircraft was not re-initiated until the fall of 2009. During the intervening years, it was represented that the company made a number of upgrades to the aircraft, particularly in avionics, but did not actively attempt to market it.
- The company advised that at one point subsequent to 2005, it had over 20 hard orders for EA 500s, but financial conditions caused them to cancel these, returning the deposits. This is a telling point: Extra Aircraft properly accounted for these funds and did not use them for working capital. That would tend to speak for the integrity of the company.
- Extra Aircraft has not had, and does not currently have, a significant market presence in the sector in which the EA 500

fits. It intends to build such market share with the EA 500, and has established a distribution system in the US, using distributors in regions of the nation.

- Maintenance support of the aircraft is not yet fully established in the US. This is logical in that there are no US-registered EA 500s in the United States. While the engine and the avionics of the EA 500 are essentially well known, maintenance of any aircraft involves on-going familiarity with the specific model to allow mechanics to efficiently trouble-shoot both current and potential maintenance issues. It is accepted that this part of the support for the EA 500 would easily be established, and would not represent any challenge to the market viability of the aircraft.
- The EA 500 itself today has only approximately five orders. Furthermore, only two examples have been constructed, and another is being built in Germany. Therefore, as a "player" in its category, it has just in the past year re-entered into the arena, and unlike other larger aircraft companies such as Cessna and Piper, does not have an already-installed base of brand customers for this category of aircraft.
- The factory in Germany appears from all information available to be efficiently managed. The main reason for the company's interest in a final assembly operation in the US was stated as being disadvantaged in the currency exchange between the Euro and the US dollar. It was represented that the German facility would continue to produce variants of the EA 330 aircraft platform.
- The depth of management available at Extra Aircraft – specific to the proposed Montrose facility - was reviewed with respect to necessary skills and expertise in production line management and supply chain logistics. At this time, no key plant management staff has been hired.
- To the extent possible a review of the suppliers – such as Rolls Royce, which is supplying the engine for the EA 500 – and their relationship with Extra Aircraft was investigated. This was to get some determination of the company's relationship with critical suppliers. To its credit, Extra apparently has strong relationships with its suppliers.
- To the extent possible, reviews were made of the dependence of the production on, and vulnerability to, sole-sourced components. Other than the engine and the avionics, there is

only one component that is clearly dependent on a single supplier, which is the unique landing gear.

- While this document is not a full financial review, the main revenue stream of Extra, appears to be based on the EA 330 aerobatic platform. This is a highly niched market. The EA 500 market, however, is very different, and, unlike the EA 330, is attempting to establish presence in a very wide market with extensive established competition.

The Transaction

The proposed structure of the Montrose deal is somewhat complex. However, the remit of this due diligence is to ascertain the risk that directly involves Montrose County.

Initial Land Purchase Is To Provide Working Capital. The transaction being considered involves the MEDC providing two parcels of land to Extra for the purpose of establishing an aircraft assembly facility. Montrose County would then purchase the parcels from Extra for a price of approximately \$2.3 million.

This, along with additional funds that would be added from other sources, would then essentially be the working capital for the Montrose-based Extra Aircraft assembly facility. *This is a critical part of the transaction that must be made clear to the public so that there are no misunderstandings regarding its intent.*

According to data and information provided to the County, the plant would final-assemble the EA 500 aircraft and later the EA 330.⁴

Note: There Is Available Alternative Land On The Airport. The land purchase in the MEDC transaction is proposed with the full understanding that the Montrose County Airport does not need to purchase more land to accommodate aviation-related industries, such as Extra Aircraft. The Airport already has 126 acres within the existing perimeter on which the Extra facility could be constructed.

The only purpose for purchasing the two additional parcels (which are not necessary to the on-going operations or future expansion of the Airport itself), is to provide a mechanism to provide working capital to Extra Aircraft, LP.

⁴ It was represented by Extra officials that the company does not currently have substantial lines of credit, and has not been able to obtain such. This is not a pejorative factor regarding the company itself. It is currently a general reality for small companies in the aviation industry – including ones with a profitable track record and strong management, both of which are apparently in place at Extra Aircraft's German factory operations.

To restate for clarity: In its current proposed form, the MEDC gives the land to Extra, the County buys it from Extra, and that gives the company a major part of the working capital it needs to establish the plant.

This arrangement is intended to address the fact that, according to company officials, Extra Aircraft has no current access to substantial lines of credit or capital to establish this facility in Montrose. The land-transfer-then-sell plan is innovative in that it is the modality from which Extra can get the cash it needs for the Montrose start-up. This does not, however, change the fact that Montrose County is taking the risk, not Extra Aircraft.

Once established, should the sales and/or revenue expectations not be met, Extra Aircraft at this time represents that it has no additional or contingency back-up financing, or credit lines for emergency funds should unforeseen circumstances arise in the establishment of the assembly operation.

Site Modification Costs. Because of the location of the specific parcels, at an appropriate time the airport must also expend funds to build a roadway, and to fence the new airport perimeter that would be created by the addition of the Extra-occupied land. These modifications are absolutely necessary to make the MEDC-provided parcels viable as an assembly facility, and to meet FAA and security requirements. They are also necessary so as not to cut off another parcel of land from road access.

The exposure to the County, not including the cost of appraisals, studies and other activities taken to date regarding this transaction, is approximately initially \$1.63 million, and subsequently another \$550,000, for a total of \$2.19 million.

This is lower than the funding exposure in the current MEDC proposal, but it is still very substantial.

Appraised Value v Proposal Value. The County has notified both the MEDC and Extra that the proposed purchase of the parcels for \$2.3 million is not possible. The specific parcels involved in this transaction have been appraised for \$675,000, well under the \$2.3 million that was a critical part of the MEDC proposal to Extra. The County has advised that legal consideration limit the County to paying fair market value for the property. Since the \$2.3 million purchase price in the MEDC proposal was a major part of the working capital that Extra would have, it is uncertain whether the lesser amount would be enough for Extra to proceed with the deal.

Extra Aircraft Exposure

Extra Aircraft has very little capital financial exposure in this transaction.

Extra Aircraft has noted that in setting up the facility, it will be moving tooling and parts worth \$3 million from the German factory. This is not an "investment" per se, nor is it truly any new expenditure for the company.

The transaction is intended to provide a facility for assembly of the EA 500s. It is of-course expected that the company would provide the necessary parts to accomplish assembly. Therefore, having those items on-site is not truly an "investment" on the part of Extra. The exposure to Extra is primarily in shipping these parts and tooling to Montrose.

Montrose County Exposure

As of September 8, 2010, the financial contributions/costs to the County of Montrose are estimated to be as follow:

Estimated Financial Risk	
Purchase of Parcels	\$675,000
Construct Road	\$750,000
Perimeter Fence	\$213,000
Phase II Build 10K Sq. Ft. Production Facility	\$550,000
Total	\$2,188,000

Land Purchase. The parcels in this transaction have been recently appraised at \$675,000. The transaction proposed by MEDC to Extra priced the land to the County at \$2.3 million – which would reduce the funding to Extra by approximately \$1.6 million.

As noted earlier, no determination has been made regarding whether this lower amount represents sufficient value to accomplish other parts of the deal. This subsequent component of the transaction does not directly involve Montrose County. The County, however, is limited to paying only fair market value for the land. Therefore, under any scenario, this portion of the deal exposes the County to \$675,000. Additional funds would be required if and when this land would be developed.

Access Road Construction. The existing location of other businesses adjacent to the Montrose County Airport now access their property across a taxiway that Extra would use for access to the Airport operations area. This would be blocked due to the establishment of the Extra Aircraft facility on Lots 3A and 4A. A new access road will need to be constructed at an estimated cost of \$750,000. Depending on soil and topographical issues, this cost could be much higher.

Perimeter Fence. Fencing the property to comply with Federal Aviation Administration (FAA) and other governmental agency requirements will entail an estimated \$213,000.⁵

Construction. Finally, the deal as currently structured commits the County to eventually construct another 10,000 square foot building for Extra, at an estimated cost of \$550,000. The total exposure to the County, based on these data, is estimated to be approximately \$2.19 million.

⁵ This figure is based on an actual estimate from a vendor.

III. Background

The Company

Extra Aircraft is an established aircraft manufacturer, well known for its core products the EA 200/300 aircraft, which are small sports/aerobatic airplanes.

These are powerful, technologically-advanced aircraft are currently built at an established factory in Germany with an output of between 27 and 32 units annually. These aircraft are well-respected in their niche.

Prior Bankruptcy

In the early part of the last decade, the company reportedly built up substantial debt that ultimately could not be serviced, and filed bankruptcy

In 2002, the current ownership, led by Mr. Ken Keith, took over. Since that time, the company has continued production of the aerobatic model and has been profitable.

As explained to Boyd Group International, one of the factors that put Extra Aircraft into bankruptcy was the debt incurred during development of a six-passenger general aviation aircraft. This was first the piston-driven EA 400, and later a turboprop version dubbed the EA 500.

The company produced approximately 27 of the EA 400, and has completed only two of the turboprop versions.⁶ The company related that at one time it had over 20 EA 500s on hard order, but an economic downturn led to cancellations, with deposit funds being returned.

The bankruptcy was eight years ago. Since that time the German operation has been profitable. Therefore the bankruptcy is not germane to the proposal under consideration by the County, and did not factor into the conclusions and recommendations in this document.

⁶ A third EA 500 was represented to be in production at the current time.

Extra Aircraft History & Products

Extra Aircraft builds a line of aerobatic aircraft that are well-known and well-respected in that sector of the aviation industry.

The EA 400 was a foray into an entirely different segment, from sport aircraft and into the mainstream of general aviation. It did not sell in large numbers.

This is a market segment that has entirely different characteristics from the sport-recreational sector and is also one where Extra faces much stronger competition, has limited market identity, and requires substantial financial resources required for marketing against established producers. In effect, the decision to design and build the EA 400, and later the upgraded EA 500, the company diversified into an entirely different business from that of its successful sport plane sector.

The EA 500 – Market Potential

It is represented by Extra Aircraft that the EA 500 (which is the aircraft that would be assembled at the proposed Montrose facility) is superior to similar aircraft in current production. While the aircraft is slower, the company represented that the EA 500 can fly farther and with more payload than its most direct competitor, the Piper Meridian. For the purposes of this project, these claims are stipulated, but they have not been verified by Boyd Group International. Other findings include:

- It is recognized that the EA 500 has been in existence for several years. Initial marketing and sales efforts ceased in 2005 and were only revived in the latter part of 2009.
- At this time, the aircraft today has less than five hard orders. This means that the Montrose facility would be built with the expectation of orders to keep assembly going. It is not being constructed as a result of strong existing orders.
- The aircraft was put back on to the market less than one year ago. It is accurate that current economic conditions are not entirely conducive to business aviation. It is also noted that there are no hard data to reliably project a rebound in this marketplace.
- The production of each EA 500 is financed, effectively, by the customer. As deposits and progress payments are made, the materials for the aircraft are purchased and production

progresses. This is a very efficient and risk-averse approach for a small aircraft manufacturer.

A gap in the progress payments, however, can delay or stop production of a specifically-ordered unit. This has not been a problem in the past for two reasons. The first is the simple fact that buyers of \$1.65 million aircraft are suitable and sophisticated individuals, and do not order such items on a whim. The second is that the company has advised that it has arranged to have buyer financing if necessary.

- There is no backstop financing or lines of credit in place for the proposed Montrose operation. This is factor that raises the core risks to the funding that the County is being asked to provide.

German Operation

The factory and operation in Germany are well-established. The company owns property and equipment at its German production facility, including the following details:

- The land leases for the facility are long term and in-place.
- Technical equipment, molds for aircraft parts, and other factory and office equipment are owned by the company.
- Buildings and land owned by the company was purchased out of the 2003 bankruptcy, reportedly at a cost substantially below the fair market value.

Profitability

Since the current management purchased Extra out of bankruptcy, it has apparently been profitable. Data is not provided here due to confidentiality agreements. However, based on this factor, and the reality that Extra is booking orders for the EA 330 to be built at the German plant, it would be logical to believe this situation will remain stable for the foreseeable future.

The company built 27 aircraft in 2009, 29 in 2008, and 32 in 2007. All were apparently the aerobatic EA 200/300 series.

Inventory levels, hourly direct labor rates, and other production related information was not made available for this project. Therefore, a more in depth evaluation of the company's manufacturing and inventory management efficiency could not be completed.

For the Montrose facility, Boyd Group International would recommend that these points – manufacturing and inventory management efficiency – are critical data that is foundational to any decision to go ahead with financial support for the company.

Capital Availability

The company made it clear to the County that it does not at this time have a significant line of credit or access to significant capital markets. The deal with MEDC has Montrose County as the source for most of the working capital in regard to the proposed facility.

Extra Aircraft's management indicated that it has attempted, but without substantial success, to secure additional financing. The main source of operating capital for the company continues to be from customer's deposits and progress payments, which are applied directly to the aircraft ordered.

The lack of extensive working capital has inhibited Extra Aircraft's ability to expand production to include the EA 500 aircraft. Moreover, the source of funding for current production requires that management carefully align receipt of customer payments with expenditures on materials and components.

Again, this is natural to a small niche manufacturer. But it does not change the fact that there is very high risk for Montrose County in this proposed transaction.

Suppliers

Extra Aircraft currently builds all aircraft at their German facility using materials and components acquired through a network of suppliers. Materials and components are acquired on an as needed basis with deliveries being closely coordinated with each stage of aircraft production, thereby allowing the company to closely manage inventory levels and trade payables.

Based on aircraft design, Extra Aircraft has developed multiple sources for most materials, including carbon fabric, and has limited the number of critical or single source suppliers to the following:

- Rolls-Royce Civil Aerospace: Single source for the EA 500's, the Rolls-Royce model 250-B17F/2 turboprop. The chances of this company going out of business or ceasing production of the RR-250 are exceedingly remote.
- Avidyne Corporation: Single source for the EA 500's integrated flight display system, the Entergra R9. This is not a marginal company, and there is essentially no danger of it ceasing production, leaving Extra in jeopardy.
- Gomolzig: A German engineering firm and the single source supplier of landing gears for Extra Aircraft. Since this is indeed a critical component there could be vulnerability should this firm choose to no longer produce landing gear or decided not to do business with Extra Aircraft. There are absolutely no such indications.

Extra represented to Boyd Group International that it maintains a good working relationship with all suppliers and, as needed, for "large ticket" items like engines, the supplier will extend payment terms. As of August 2010, Extra Aircraft advised that it is current with all suppliers.

Extra Aircraft US Operations

Extra Aircraft has been looking to locate a facility in the U.S. allowing it to be more competitive for aircraft sales in the large North American general aviation aircraft market. This facility is the focus of the discussions between Montrose County and Extra Aircraft, LP.

The company's initial plans, as expressed to the County for the U.S. operation, are limited to the final assembly of the EA 500 business aircraft, and later the EA 330 aerobatic aircraft.⁷ Production of the

⁷ It was not made clear how this would affect the German factory. If that facility continued to produce the EA 330, production of that aircraft in the US would logically

aircraft fuselage and wing assembly (i.e., composite layup processing) will remain in Germany with finished aircraft parts shipped to the U.S. assembly plant. Engines, avionics, landing gear and other components are to be shipped to the U.S. plant direct from third-party suppliers.

A newly established marketing and sales department is to be located at the U.S. facility, as will a pilot training center and North American parts distribution center. A maintenance and overhaul operation is envisioned for a later date.

Competing Aircraft Market

According to General Aviation Manufacturers Association (GAMA) general aviation shipment report for calendar year 2009, worldwide shipments for general aviation aircraft were down in all categories. The global economic down turn, credit constraints, and (no doubt) Washington's negative view of corporate aircraft, contributed to the reversal of a five year double-digit growth trend. There are no guarantees that strong growth will return to this industry in the near or even distant future.

Overall, 2009 general aviation aircraft shipments were down 43% relative to 2008, with piston aircraft declining by 55% and turboprops by 18%. Within the turboprop group the Piper 500 Meridian, most likely to be the EA 500's top competitor, total shipments for 2009 dropped to 29 aircraft from 52 aircraft for the prior year, a 44% decline.

Looking ahead, the outlook for turboprop sales remains questionable. During the first half of 2010, worldwide turboprop sales were down 44% compared to the same period during 2009. Sales of the Piper Meridian – the most direct competitor to the EA 500 - declined by 42% during the same period. This cannot but raise the question as to whether Montrose County should assume the role as a funding mechanism for a new airplane assembly plant.

be the result of strong increases in market demand. There is no data to support such a projection.

Demand Estimates

Based on representations made to the County, Extra would produce one aircraft in the immediate six to eight months period subsequent to opening the North American facility. In each full year thereafter, production (and, inherent in that projection, sales) of the Extra 500 would increase from one aircraft per month in the first full year, growing to three per month in the fourth year.

In this analysis, subsequent to the production of the first unit, the assumption was made for production of EA 500 one per month in the first full year, ramping to 36 per year by the beginning of the fifth year.

But that assumes the company can sell these numbers of aircraft. There is no market-forecast data to support these projections. Based on the nature of this sector of the industry, this is not abnormal.⁸

If the Extra 500 attained the eventual 40+ annual units as expressed to the County, it would nearly equal the best year for the Piper Meridian.

Turboprop Aircraft Worldwide Shipments						
Aircraft	2005	2006	2007	2008	2009	2010 1Q-2Q
Turboprops	375	412	549	535	411	107
Turboprop 5-Year Rolling Avg. Annual Sales	342	334	332	385	438	--
Piper 46-500 Meridian	40	49	53	52	29	8
Piper Meridian 5-Year Rolling Avg. Annual Sales	38	43	33	38	44	--
Meridian Avg Market Share	11%	13%	10%	10%	10%	--

Source: GAMA 2009 GA Statistical Databook & Industry Outlook

Table 6A

If we compare the independently-estimated sales for the EA 500 for the first five full years of production, it would indicate 130 units. This would compare to 223 Piper Meridians produced in the five year period ending in 2009. That would indicate sales of the EA 500 equaling over 58% of Meridian sales.⁹

Production Year	Yr. 1	Yr. 2	Yr.3	Yr. 4	Yr. 5	Yr. 6
Extra Aircraft 500	12	18	24	36	40+	40+

Table 6B

⁸ Indeed, it is very difficult to forecast such demand for any general aviation manufacturer. This is another risk factor that Montrose County must consider.

⁹ The year-by-year sales projections for Extra are based on independent estimates of potential based on Extra's representation of 12 in the first full year, ramping to over 36 after five full years.

For an aircraft that has only been put back on to the market for less than one year, and by a company that has very low market and brand penetration in this category, gaining this much share over the timeframe noted is highly questionable.

Another ominous market note is that sales of the Piper Meridian – the closest competitor to the EA 500 – have plummeted in 2010. According to available data, Piper has sold only 8 through the first half of the year. The exact reasons for this are unclear. Nevertheless, it does further indicate caution for a County being asked to invest \$2.19 million in this assembly facility.

Employee count, based on those sales assumptions, is projected by Extra Aircraft to total over 200 in the fifth year of production. There is no concise breakdown of specific class and craft distribution of these employees.

General aviation was down for 2009, and prospects for 2010 are cloudy.

The market can turn around, but there are no market data to indicate that it would be in such a manner to meet the production estimates.

Concerns Regarding Sales Estimates

The message is that the sales projections may be optimistic, and would again point to caution on the part of Montrose County in investing in this project as currently structured.

Boyd Group International has concerns about the likelihood of these projections being achieved:

- The EA 500 was put back onto the market in late 2009, and while this is a limited time period, it has experienced no indications of market demand at the levels projected. Only two are flying today, and there are very few hard orders. While eventual FAA certification of the EA 500 would tend to make North American sales prospects more likely, it must be noted that building an assembly facility at Montrose will not directly cause market interest to spike in the EA 500.¹⁰
- A projection of a sales demand for 40+ EA 500s subsequent to year five represents a number nearly equal to the best post-9/11 year for the Piper Meridian. While it may have better performance than the Meridian, Boyd Group International has seen no business case to support a sudden increase in market demand for the EA 500. Put another way, while the EA 500 might be an improvement over current market options, it is not a breakthrough (at least the market would support this view), and it does not create a new product category or customer base.

¹⁰ It is noted that the price of the aircraft may come down due to US production. This assumes currency gains with US production.

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- While it is clear that the Extra facility in Germany is building high-quality aerobatic airplanes, and it is apparent that the company has strong senior management skills there, details regarding how the Montrose facility will be established and who will manage it are not clear.
 - The company noted it intends to hire locally and send staff to Germany for training. That is sound. However, operating an assembly plant requires strong management background in production techniques and logistics. This would be a key position that would most likely need to be filled from outside Montrose, and with an individual with strong experience in these areas.¹⁴
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¹⁴ This was one of the key reasons for the failure of Eclipse, which had strong backing from Wall Street and the State of New Mexico. Lack of skilled production management led to high defect rates and reduced production.

III. Conclusion & Recommendations

Summary Points

Any proposal – particularly one from a company that has an established operation, as does Extra Aircraft – offering to create 200 jobs should be considered.

In reviewing the situation, however, it is the conclusion of Boyd Group International that the specific proposal on the table is one that needs revision before Montrose County should consider any expenditure as large as that required by the Extra Aircraft project.

As the transaction is structured, the proposal at hand is based on projections of EA 500 demand that by the nature of this sector of the aviation industry are very tenuous. This means that the projection of 200 new jobs is also tenuous.

This conclusion is based on the following key points:

- The intent is not to move existing production of aircraft to Montrose. Extra is seeking to have the County invest in establishing an assembly facility for an aircraft that only has two examples flying, currently has no large order book, has been on the active market for less than a year, and faces a general aviation industry that is currently in a downturn. When and to what extent this downturn may end is not clear.
- The majority of working capital dollars for the Montrose facility will come from the County and from other public sources. Extra has made clear that it does not have back-up financing should sales not meet expectations or should it encounter unforeseen problems or delays in getting the plant in operation.

These represent a situation that is separate and distinct from the status of the how the company is operating in Germany. Regardless of the profitability of that operation, or any other such data and information, the above two points remain, and reflect the risk that the County would face in this transaction.

Risk Is High

The County has exposure to expenditures of \$1.63 million initially, and a total of \$2.19 million. Theoretically, this is an investment in the future economic foundation of Montrose County. Estimates expressed to the County by Extra Aircraft, LP forecast a facility eventually producing over 40 aircraft a year, and employing over 200 people.

These projections, however, are speculative in nature and the transaction does not - in its current form - involve collateral or other financial resources from Extra Aircraft, LP that would provide any sort of meaningful protection to Montrose County.

Risks are always assumed in transactions of this nature and the determination that Montrose County must make is whether the risk in this case is advisable. Boyd Group International offers the following for consideration:

1. There are no guarantees – and, to be fair, Extra Aircraft is not attempting to posture its projections as such – that the demand for the EA 500 will meet projections. This is not anything pejorative about Extra Aircraft. It is simply a reality in the general aviation market. Without a substantial order book (which does not exist today) for the EA 500, it is difficult to recommend the County commit to over \$2 million to facilitate the establishment of a plant to assemble an aircraft where production will be entirely based on projected sales volumes, with no historical market demand data for the aircraft involved.
2. There is no financial safety net for Extra Aircraft LP. The information given by management was clear and forthright: there are no back-up lines of credit at this time. This should be a baseline requirement, as otherwise the County is effectively going into the investment business with the current deal.
3. The plan for the assembly plant itself needs to be further developed, particularly in regard to hiring professional, production-line, resume-in-place senior leadership. Having hundreds of resumes from local job applicants does not by itself satisfy this requirement.
4. In the near term, the number of jobs to be created will be far less than 200, and Extra Aircraft has been very open regarding this point.

Conclusions

There is no question that the management of Extra Aircraft has good intentions to bring quality manufacturing jobs to Montrose County. The problem is rooted in the fact that the company involved may not have adequate capital to support its operations at Montrose should projections not be met, and review of the market data completed by Boyd Group International shows no certainty of such targets being attained.

The Montrose County Airport does have sufficient land to offer Extra Aircraft on-airport operating facilities. The County has the ability to assist the company in that regard, but it is our view that it would be risky to purchase additional off-airport land and assume other associated risks given the lack of corporate financing for Extra Aircraft, LP at the present point in time.

It is recommended that the proposal be restructured to include additional safeguards for the County's risk. This would of necessity include Extra Aircraft having some reasonable lines of credit as a fallback. As the deal is now structured, the majority of working capital will come from the County's purchase of land that is donated to Extra Aircraft, with no apparent fallback funding on which Extra can turn should its projections not be met.

Owning the land itself is no real collateral, particularly in light of the facts that a) extensive additional expenditures are needed to modify access to the parcels, and b) the County Airport already has significant land for industrial development.

This project was a due diligence of Extra Aircraft only as it relates to the MEDC proposal and the role that the County would play in it.

The questions and data and information regarding this objective were fully responded to. Extra Aircraft was open and forthright in this regard.

Additional meetings and discussions will not alter the fact that the two points on which the project's conclusions are based.

Data Collected Are Sufficient To Formulate Conclusions

In a September 8, 2010 meeting with Extra management and their attorney, it was implied that there was insufficient contact between Boyd Group International and the company to formulate determinations to pass on to the client, Montrose County.

With due respect to Extra Aircraft, the core factors that lead to our recommendation that the transaction needs to be extensively revised are not any that would be changed by further discussions with Extra.

- The demand for Extra Aircraft products is predominantly driven by outside economic factors that are difficult to accurately forecast. As a result, the production goals expressed by Extra to the County for the EA 500 cannot be tied back to any hard economic or market-demand data.

Furthermore, there simply are no such data available that can predict with any reliability how the EA 500 will fare in the marketplace subsequent to the investment by Montrose County.

Extra Aircraft has made what are good-faith sales projections, but given the marketplace, and the current position of the EA 500 in the market (two examples flying, and approximately five on order) they are a weak foundation on which to base a \$2+ million investment. This is clearly a risk for the County. Additional

meetings and discussions with Extra Aircraft will not change this situation.

- The key issue here is that the investment is to facilitate the construction and establishment of a product for which demand has been and will continue to be uncertain. Additional meetings and discussions with Extra Aircraft will not change this fact.
 - The deal is structured as a one-shot injection of working capital for the Montrose facility. There is not a financial Plan B in place. Additional meetings will not alter that fact.
-

EXTRA Aircraft

PO Box 6573
Avon, CO 81620

September 27, 2010

Sent by email

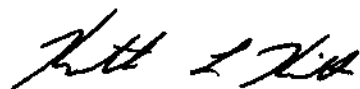
Jesse Smith
Montrose County Manager
161 South Townsend Ave.
Montrose, CO 81401

Dear Jesse

Please find attached Extra Aircraft's response to the Boyd Report.

I can be reached by phone or email for further questions.

Sincerely



Ken Keith
CEO
615-364-4040

cc: Ron Henderson
David White
Gary Ellis
Bob Hill

To: Montrose County Commissioners

From: Extra Aircraft

Re: Response to Boyd Group Due Diligence Report

As you are aware, Extra Aircraft has been in discussions with the Montrose Economic Development Corporation, elected and appointed county and city officials, the airport executive and various other state and local executives with the goal of establishing a United States based assembly factory at Montrose. Extra Aircraft ceased its search of other locations in North America in late July and announced that it had chosen Montrose as its factory site. This decision was based on the available facilities, a qualified workforce and the specific proposal of a package of incentives offered jointly by the Montrose County Commission, the MEDC, Region 10, the City of Montrose and the State Of Colorado. This incentive package had been approved in a publicly held vote by the Board of County Commissioners on July 1, 2010. It was agreed and understood by all parties that final approval of the package of incentives was dependent upon the successful conclusion of a due diligence process. Extra Aircraft publicly announced its location choice at the EAA Air Venture air show in Oshkosh, WI and in a public gathering at Montrose Airport on July 23, 2010 based on these commitments and with the knowledge that it had truthfully and appropriately supplied all required company financial and product information to the County under a confidentiality agreement.

The Boyd Group Due Diligence report

The County chose to outsource the due diligence process to The Boyd Group, a well-regarded aviation consultant. The Boyd Group is well known in aviation circles for its focus and expertise in strategy consulting and research for airports, commercial airlines and large commercial aircraft manufacturers. However, the company is not perceived by the aviation industry as a consultant which would be selected to conduct due diligence on a small general aviation manufacturer such as Extra Aircraft. Also, the County unilaterally decided on a substantially reduced incentive package from the one approved in the July 1, 2010 vote and instructed the Boyd Group to use that in its calculations and considerations. Extra Aircraft supplied all of the requested information to the Boyd Group and met with them on August 26, 2010 to answer questions related to their due diligence task. Being surprised at the choice of the Boyd Group to perform the due diligence, Extra Aircraft, on numerous occasions communicated to the appropriate parties, including The Boyd Group, that it wanted the opportunity to review the report before it was submitted in final form to be certain that it was accurate in its statements of facts. Extra Aircraft was first able to review the Boyd Group report on Sept. 21, 2010 after it had been submitted to the County. This review revealed several errors and omissions that need to be addressed.

Capital Exposure Risk

The Boyd report repeatedly states that Extra Aircraft is taking little or no risk because it is bringing no resources to the Montrose endeavor. It also states that the County Commission is the majority source of capital and financial support for Extra's US operations. These statements are erroneous.

Extra Aircraft has made it clear that it has approximately \$3,000,000 in unencumbered Extra 500 composite airframes, tooling, equipment, parts and intellectual rights that will be transferred to the Montrose facility as a capital contribution to the North American facility. Without this contribution of necessary assets, funding in addition to the current request would be required. The Boyd Group does not give this contribution any value in its report because the assets already exist. The fact that Extra's own capital has created these resources is totally ignored. In a follow-up meeting, Ken Keith, the owner of Extra Aircraft with prior experience as a CFO and a CPA, explained that this lack of recognition totally disregards generally accepted accounting principles (GAAP) that do treat such contributions as contributions to capital. With the Extra contribution to capital properly considered, the County would be injecting 39% of the total capital, not a majority, based on the original incentive package. With the reduced incentive package, the County's capital contribution is 10%. Either way, the financial risk taken by the County and Extra Aircraft is much more balanced than presented in the Boyd group report.

The Boyd Group report also overlooks the fact that Extra Aircraft's business plan shifts a substantial financial burden of marketing to its dealers. Four dealers have already signed agreements to sell the Extra 500 which means they have agreed to purchase a demonstrator aircraft (\$1,650,000) and commit other necessary staff and resources to this process. While this cannot be included in capital under accounting rules, this was intentionally included in the design of the US business to spread the risk of entering the market by finding the best marketing partners. If the Boyd report had taken into account the dealers investments in Extra Aircraft's North American operations of close to \$8,000,000, the percentage of investment by the County would have dropped from 39% to 18% under the original incentive and 5% of the reduced incentive. Clearly, the Boyd Group report overstates the financial risk to the County.

Market Risk Analysis

The second major concern expressed in the Boyd report is the attainability of sales projections. First, the report states that there is no substantial order book in existence. The fact that Extra Aircraft has worldwide orders for the Extra 500 through the third quarter of 2011, 5 of the 12 aircraft to be produced in the first 18 months of operations, is not considered significant by the Boyd Group. The reality is that production of these aircraft can begin immediately due to the transfer of airframes, parts, equipment etc. to the US from Germany. Also as stated in the business plan submitted by Extra Aircraft, experienced factory managers from Germany will oversee the US operations. This

addresses Boyd's concern about the lack of experienced personnel to successfully meet production goals.

Next, the Boyd report observes that the General Aviation market place is in bad shape and without prospects for recovery in the predictable future. The report ignores the fact stated on page 18 that the turboprop sector suffered significantly less decline (18% vs 55%) than other sectors. This is the sector where the Extra 500 will compete. As stated above, a group of dealers has already agreed to sell the Extra 500. On the whole, this dealer group has 152 years of combined experience in general aviation as a basis for their decision to make a large investment in the product. Such an investment would only be made with confidence that Extra Aircraft and the dealers themselves can be successful. ~~These dealers are in the market every day and know what is happening versus reading~~ historical sales reports and making projections based on historical information which always lags a recovery. Extra's dealer partners have each sent letters to MEDC outlining why they believe in Extra Aircraft and why the Extra 500 is competitive and will perform well in the current market. The risk of the General Aviation market was not clearly portrayed in the Boyd Group report.

Conclusion

Extra Aircraft has serious issues with the Boyd Report as stated above and as well as with other lesser issues in the report. However, the Boyd Group report repeatedly states that there is no need for further discussions with Extra Aircraft as there is nothing of further value to be gained that would change the conclusions reached in its report. Releasing the report in this flawed state will cause financial harm to Extra Aircraft and serious harm to all other parties relying on it to be accurate. Therefore, Extra Aircraft insists that the County commission not release the Boyd Group Due Diligence report until and unless all the issues that Extra has and will raise about the report are addressed and corrected.