Raytheon Company (RTN)

Updated October27th, 2018 by Nate Parsh

Key Metrics

Current Price:	$177	**5 Year CAGR Estimate:**	4.9%	**Volatility Percentile:**	5.5%
Fair Value Price:	$151	**5 Year Growth Estimate:**	6.0%	**Momentum Percentile:**	46.7%
% Fair Value:	117%	**5 Year Valuation Multiple Estimate:**	-3.1%	**Growth Percentile:**	47.4%
Dividend Yield:	2.0%	**5 Year Price Target**	$202	**Valuation Percentile:**	21.7%
Dividend Risk Score:	B	**Retirement Suitability Score:**	C	**Total Return Percentile:**	16.6%

Overview & Current Events

Raytheon Company was founded in 1922. The company's first product was the S gas rectifier tube, which eliminated expensive batteries found in home radios. Today, Raytheon is the fifth largest military contractor. The company provides missile, electronic, radar and communication systems to the United States and its allies. Raytheon has four divisions: Integrated Defense Systems, Intelligence Information and Services, Missile Systems and Space and Airborne Systems. Raytheon has a current market cap of $50 billion and had a company record $25.3 billion in sales in 2017.

Raytheon reported 3rd quarter earnings on October 25th. The company earned $2.25 per share, $0.30 above estimates and a 14% improvement year over year. Revenue increased 8.4% to $6.81 billion, topping estimates by $120 million.

All divisions within the company saw sales grow in the quarter. Integrated Defense Systems increased revenue 7% as Raytheon's Patriot program continues to see strong international demand. Intelligence, Information & Services climbed 13%. Higher sales for cyber and space business programs were a major contributor to revenue growth. Missile Systems was up 7% due to higher sales for the company's classified programs. Space & Airborne Systems grew 6%, due in large part to higher sales volumes for surveillance and targeting systems. Raytheon booked $8.7 billion worth of new orders, helping the company's backlog increase 14% to another company record $41.6 billion. The company did see segment operating margins contract 60 basis to 12.4%. Raytheon now expects segment margins to be in the range of 12.3%-12.4% for 2018, down from 12.5%-12.7% previously. The company did increase the midpoint for earnings-per-share guidance to $10.06, up from $9.88 previously. If achieved, this would represent 45% growth from 2017.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$3.95	$4.89	$4.79	$5.28	$5.65	$5.96	$6.97	$6.75	$7.44	$6.94	***$10.06***	***$13.46***
DPS	$1.12	$1.24	$1.50	$1.72	$2.00	$2.20	$2.42	$2.68	$2.93	$3.19	***$3.47***	***$4.64***
Shares	400.1	383.2	359	339	328	314.5	307.3	299	293	288	***280***	***250***

Raytheon's earnings per share growth rate over the past decade is almost 6% per year. The company experienced earnings growth in both 2008 and 2009, a time where many companies struggled with increasing their bottom lines.

One major catalyst for the Aerospace and Defense sector is the amount of funding the governments of the world are currently providing for defense products. The U.S. alone spent $589 billion on defense in fiscal 2017, an increase of $9 billion from the previous year. For fiscal 2018, that figure jumped to $700 billion.

Raytheon has increased its dividend for the past 14 years. Over the past decade, the annual growth rate has been 12%. The most recent raise (on March 21st) increased the dividend 8.8%.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	14.8	9.4	10.6	8.9	9.5	11.7	14.0	16.2	18.0	24.2	***17.6***	***15.0***
Avg. Yld.	1.9%	2.7%	3.0%	3.7%	3.7%	3.2%	2.5%	2.5%	2.2%	1.9%	***2.0%***	***2.3%***

Shares of Raytheon have declined $20 dollars, or 10.2%, from our August 7th update. Based off of updated guidance, the stock has a forward P/E of 17.6, down from 19.9 earlier. Due to company results and increases in spending on defense, we have raised our 2023 target P/E to 15 from 14. If shares of Raytheon were to revert to this new target, the stock could experience multiple contraction of 3.1% per year, down from an 5.5% annual contraction in our previous update.

Safety, Quality, Competitive Advantage, & Recession Resiliency

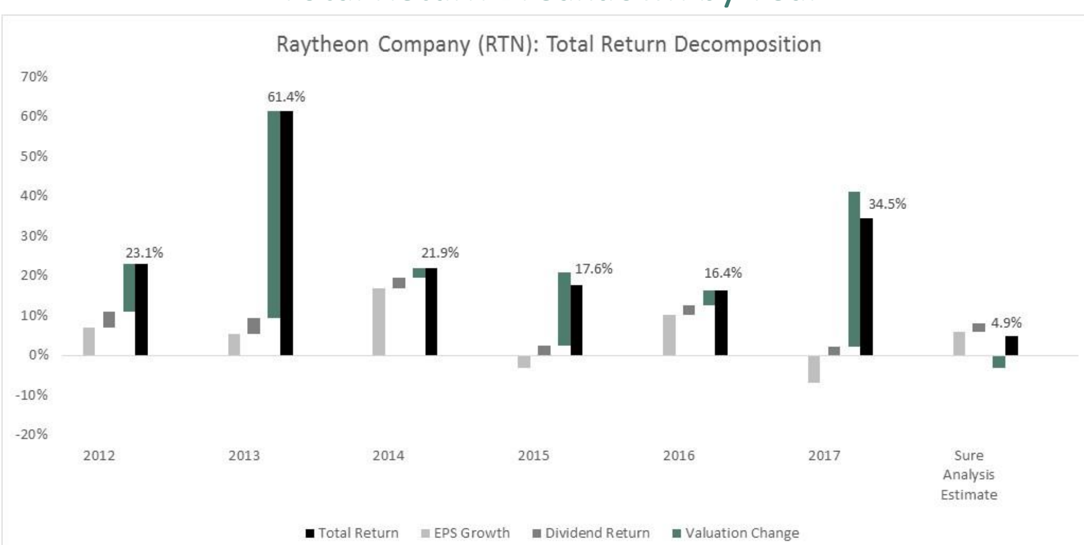
Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	20.3%	21.7%	20%	19.8%	19.9%	19.9%	20%	19.5%	20.4%	20.3%	***20.3%***	***20.3%***
Debt/A	60.3%	57.9%	59.5%	67.7%	69.3%	56.9%	64.9%	64.7%	66.4%	67.7%	***66.9%***	***63.5%***
Int. Cov.	40.8	28	22.5	17.9	15.5	15	15.7	13.8	15.4	18	***18.5***	***20.3***
Payout	28.4%	25.4%	31.3%	32.6%	35.4%	36.9%	34.7%	39.7%	39.4%	46%	***34.5%***	***34.5%***
Std. Dev.	25.5%	37.4%	17.3%	22.6%	14.4%	20.4%	14.6%	19.1%	12.3%	9.1%	***11.2%***	***19.3%***

Raytheon showed earnings growth during the last recession, something not every company can say. Given strong global demand for products, this should continue as long as the world's economies are on solid ground. Raytheon has produced a very consistent gross profit to asset ratio over the last 10 years. Given spending levels for defense, Raytheon is in a very good position to maintain their profitability, perhaps even improve upon this metric. The company has seen a rise in debt as a percentage of assets has increased slightly over the past ten years, but not yet to an unmanageable level. The dividend payout ratio has been below 40% for much of the past ten years. Even with double digit dividend growth, the payout ratio has stayed very low. This low ratio affords Raytheon a cushion if earnings enter a period of decline. Dividend growth investors should feel comfortable in Raytheon's ability to continue to grow its dividend.

Final Thoughts & Recommendation

The Aerospace and Defense sector as a whole has pulled back with the rest of the market. Raytheon has been no exception, with its stock falling more than 17% since early May. We now estimate that Raytheon can offer investors a total annual return of 4.9% through 2023, up from 2.3% previously. This forecast is based off of growth (6%), dividends (2%) and multiple contraction (3.1%). Outside of lower margins, the company produced a solid 3rd quarter. Each division saw sales growth and estimates for EPS for the year were increased. Raytheon, however, continues to offer the lowest expected total return amongst the large defense contractors. Though we have raised our 2023 price target $4 to $202 due to the increase in EPS guidance, we recommend investors wait to buy until Raytheon's stock trades closer to fair value. Raytheon continues to earn a sell recommendation from Sure Dividend at current prices.

Total Return Breakdown by Year



Click here to rate and review this research report. Your feedback is important to us.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.

Raytheon Company (RTN)

Updated October27th, 2018 by Nate Parsh

Income Statement Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Revenue	23174	24881	25150	24791	24414	23706	22826	23321	24124	25348
Gross Profit	4685	5134	4877	5127	5322	5174	5531	5713	6159	6272
Gross Margin	20.2%	20.6%	19.4%	20.7%	21.8%	21.8%	24.2%	24.5%	25.5%	24.7%
SG&A Exp.	1548	1527	1639	1847	1882	1771	1852	1940	2109	2220
D&A Exp.	390	402	414	444	455	445	439	489	515	550
Operating Profit	2620	3042	2613	2830	2989	2938	3179	3067	3295	3318
Op. Margin	11.3%	12.2%	10.4%	11.4%	12.2%	12.4%	13.9%	13.2%	13.7%	13.1%
Net Profit	1672	1935	1840	1866	1888	1996	2244	2110	2244	2024
Net Margin	7.2%	7.8%	7.3%	7.5%	7.7%	8.4%	9.8%	9.0%	9.3%	8.0%
Free Cash Flow	1637	2378	1556	1670	1542	2049	1804	1902	2227	2134
Income Tax	824	953	590	782	878	808	790	747	873	1114

Balance Sheet Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Total Assets	23134	23607	24422	25854	26686	25967	27716	29281	30238	30860
Cash & Equivalents	2259	2642	3638	4000	3188	3296	3222	2328	3303	3103
Acc. Receivable	3898	4493	4414	1183	1131	1223	1042	1174	1163	1324
Inventories	325	344	363	336	381	363	414	635	608	594
Goodwill & Int.	11662	11922	12045	13192	13420	13339	13677	15725	15677	15640
Total Liabilities	13946	13668	14532	17514	18496	14770	17995	18951	20081	20897
Accounts Payable	1201	1397	1538	1507	1348	1178	1250	1402	1520	1519
Long-Term Debt	2309	2329	3610	4605	4731	4734	5325	5330	5335	5050
Total Equity	9087	9827	9754	8181	8026	11035	9525	10128	10157	9963
D/E Ratio	0.25	0.24	0.37	0.56	0.59	0.43	0.56	0.53	0.53	0.51

Profitability & Per Share Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Return on Assets	7.2%	8.3%	7.7%	7.4%	7.2%	7.6%	8.4%	7.4%	7.5%	6.6%
Return on Equity	15.5%	20.5%	18.8%	20.8%	23.3%	20.9%	21.8%	21.5%	22.1%	20.1%
ROIC	12.6%	16.3%	14.3%	14.1%	14.6%	13.8%	14.5%	13.7%	14.4%	13.3%
Shares Out.	400.1	383.2	359	339	328	314.5	307.3	299	293	288
Revenue/Share	54.34	62.88	66.71	70.11	73.05	73.12	73.02	76.41	81.28	86.99
FCF/Share	3.84	6.01	4.13	4.72	4.61	6.32	5.77	6.23	7.50	7.32

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.