Raytheon Company (RTN)

Updated February 1st, 2019 by Nathan Parsh

Key Metrics

Current Price:	$165	**5 Year CAGR Estimate:**	9.1%	**Volatility Percentile:**	19.3%
Fair Value Price:	$173	**5 Year Growth Estimate:**	6.0%	**Momentum Percentile:**	20.9%
% Fair Value:	93%	**5 Year Valuation Multiple Estimate:**	1.0%	**Growth Percentile:**	50.9%
Dividend Yield:	2.1%	**5 Year Price Target**	$231	**Valuation Percentile:**	54.6%
Dividend Risk Score:	B	**Retirement Suitability Score:**	C	**Total Return Percentile:**	44.4%

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 five reportable divisions: Integrated Defense Systems, Intelligence Information and Services, Missile Systems, Space and Airborne Systems and Forcepoint. Raytheon has a current market cap of $47 billion.

Raytheon reported fourth quarter and full year results on January 31st. The company had earnings-per-share (EPS) of $2.93 for the quarter, which beat estimates by $0.04 and improved 117% from the prior year's quarter. Revenue grew 8.6% to $7.4 billion, though this was $90 million below consensus. EPS for the year grew 46% to $10.15, topping the company's guidance by $0.09. Revenue improved 6.7% to $27.1 billion. Operating cash flow was a company record $3.4 billion in 2018. Raytheon's backlog grew 11% to $42.4 billion by year's end.

Net sales for the Integrated Defense Systems grew 8% for the quarter and 6% for the year. Raytheon's Patriot program continue to be in high demand and was the leading contributor of growth for this segment. Intelligence, Information and Services demonstrated sales growth of 9% for the fourth quarter and 9% for 2018. This growth was primarily due to higher volumes of classified programs in the areas of cyber and space. Missile Systems' quarterly and yearly growth was 6% and 7%, respectively. Raytheon saw growth in its classified programs for both the quarter and year. Space and Airborne Systems improved 13% during the quarter with 5% growth for the year. Higher volumes of products was the main cause of growth for this division. Sales for Forcepoint, Raytheon's smallest reportable division, grew 10% in the quarter and 4% for the year. Higher demand for sales led to the year-over-year gains.

Raytheon expects EPS between $11.40-$11.60 and revenue to range from $28.6-$29.1 billion for 2019. Achieving the midpoint of the company's guidance would result in growth of 13.3% for EPS and 6.5% for revenue. Operating cash flow is expected to be ~$4 billion for the current year. Shares closed lower by 4% following the results release.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	$4.89	$4.79	$5.28	$5.65	$5.96	$6.97	$6.75	$7.44	$6.94	$10.15	***$11.50***	***$15.39***
DPS	$1.24	$1.50	$1.72	$2.00	$2.20	$2.42	$2.68	$2.93	$3.19	$3.40	***$3.47***	***$4.64***
Shares	383.2	359	339	328	314.5	307.3	299	293	288	280	***275***	***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. We maintain our 6% growth rate going forward, with much of this growth coming from revenue improvements.

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%. If the company maintains its usual schedule, investors should see a dividend increase for the May payment.

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Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	9.4	10.6	8.9	9.5	11.7	14.0	16.2	18.0	24.2	17.6	***14.3***	***15***
Avg. Yld.	2.7%	3.0%	3.7%	3.7%	3.2%	2.5%	2.5%	2.2%	1.9%	2.0%	***2.1%***	***2.0%***

Shares of Raytheon have declined $12 dollars, or 6.8%, from our October 27th update. Based off of guidance for 2019, the stock has a forward price-to-earnings ratio of 14.3. Due to company results and increases in spending on defense, we maintain our target price-to-earnings ratio 15 for 2024. If shares of Raytheon were to expand to meet our target, investors would see an additional 1% added to annual returns through 2024.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	25.4%	31.3%	32.6%	35.4%	36.9%	34.7%	39.7%	39.4%	46%	33.5%	***30.2%***	***30.1%***

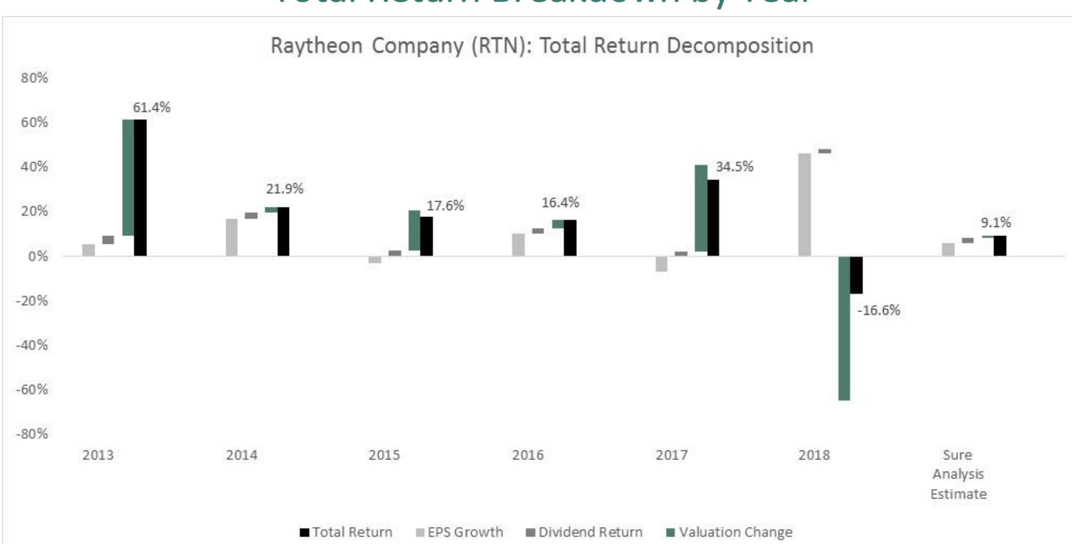
Raytheon showed earnings growth during the last recession, something few companies say. Growth should continue as long as the U.S. continues to expand its military budget. The dividend payout ratio is under 35% now, meaning the dividend is very conservative.

A key competitive advantage for Raytheon is that its expertise in the areas it operates is not easily recreated. Raytheon's contacts and contracts with the U.S. military help insulate it from competition. As such, Raytheon has competition from a limited amount of companies.

Final Thoughts & Recommendation

We estimate that Raytheon can offer a total annual return of 9.1% through 2024, up from 6.4%. Raytheon's business performed well during the fourth quarter and full year 2018. Guidance for 2019, while not received well from the market, offers solid growth rates from the prior year. Shares of Raytheon have fallen almost 7% since our last report and 17% from our August 7th report. In our last report, we recommend investors waited until Raytheon's stock traded closer to fair value. This is now the case. Though we feel that Boeing (BA) and Northrop Grumman (NOC) project a higher annual total return, the pullback in shares of Raytheon offers a solid rate of return from current levels. We have increased our 2024 price target by $29 to $231 due to EPS guidance for the current year.

Total Return Breakdown by Year



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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.

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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	24881	25150	24791	24414	23706	22826	23321	24124	25348	27058
Gross Profit	5134	4877	5127	5322	5174	5531	5713	6159	6272	7485
Gross Margin	20.6%	19.4%	20.7%	21.8%	21.8%	24.2%	24.5%	25.5%	24.7%	27.7%
SG&A Exp.	1527	1639	1847	1882	1771	1852	1940	2109	2220	2106
D&A Exp.	402	414	444	455	445	439	489	515	550	568
Operating Profit	3042	2613	2830	2989	2938	3179	3067	3295	3318	4538
Op. Margin	12.2%	10.4%	11.4%	12.2%	12.4%	13.9%	13.2%	13.7%	13.1%	16.8%
Net Profit	1935	1840	1866	1888	1996	2244	2110	2244	2024	2909
Net Margin	7.8%	7.3%	7.5%	7.7%	8.4%	9.8%	9.0%	9.3%	8.0%	10.8%
Free Cash Flow	2378	1556	1670	1542	2049	1804	1902	2227	2134	2607
Income Tax	953	590	782	878	808	790	747	873	1114	264

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	23607	24422	25854	26686	25967	27716	29281	30238	30860	31864
Cash & Equivalents	2642	3638	4000	3188	3296	3222	2328	3303	3103	3608
Acc. Receivable	4493	4414	1183	1131	1223	1042	1174	1163	1324	1648
Inventories	344	363	336	381	363	414	635	608	594	758
Goodwill & Int.	11922	12045	13192	13420	13339	13677	15725	15677	15640	14864
Total Liabilities	13668	14532	17514	18496	14770	17995	18951	20081	20897	20392
Accounts Payable	1397	1538	1507	1348	1178	1250	1402	1520	1519	1964
Long-Term Debt	2329	3610	4605	4731	4734	5325	5330	5335	5050	5055
Total Equity	9827	9754	8181	8026	11035	9525	10128	10157	9963	11472
D/E Ratio	0.24	0.37	0.56	0.59	0.43	0.56	0.53	0.53	0.51	0.44

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	8.3%	7.7%	7.4%	7.2%	7.6%	8.4%	7.4%	7.5%	6.6%	9.3%
Return on Equity	20.5%	18.8%	20.8%	23.3%	20.9%	21.8%	21.5%	22.1%	20.1%	27.1%
ROIC	16.3%	14.3%	14.1%	14.6%	13.8%	14.5%	13.7%	14.4%	13.3%	18.4%
Shares Out.	383.2	359	339	328	314.5	307.3	299	293	288	280
Revenue/Share	62.88	66.71	70.11	73.05	73.12	73.02	76.41	81.28	86.99	94.34
FCF/Share	6.01	4.13	4.72	4.61	6.32	5.77	6.23	7.50	7.32	9.09

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