Raytheon Company (RTN)

Updated November 4th, 2019 by Prakash Kolli

Key Metrics

Current Price:	$216	**5 Year CAGR Estimate:**	3.7%	**Volatility Percentile:**	32.3%
Fair Value Price:	$176	**5 Year Growth Estimate:**	6.0%	**Momentum Percentile:**	64.1%
% Fair Value:	123%	**5 Year Valuation Multiple Estimate:**	-4.0%	**Growth Percentile:**	57.5%
Dividend Yield:	1.7%	**5 Year Price Target**	$236	**Valuation Percentile:**	32.4%
Dividend Risk Score:	B	**Retirement Suitability Score:**	C	**Total Return Percentile:**	26.7%

Overview & Current Events

Raytheon Company is one of the five largest U.S. defense contractors based on revenue. The company had over $27B in sales in 2018. Raytheon operates five business segments that are Integrated Defense Systems (missile defense), Intelligence and Information Systems (services, training, engineering and logistics), Missile Systems (produces munitions and missiles), Space and Airborne Systems (airborne radars and sensors) and Forcepoint (a cybersecurity business). Approximately 70% of sales are to the U.S. Department of Defense with the rest mostly from other U.S. agencies and international military sales. The company's best-known products are the Patriot missile defense system and the Tomahawk cruise missile. The company has a market capitalization of ~$60.18B.

Raytheon reported another excellent quarter for Q3 2019 on October 24, 2019. Companywide net sales increased 9.4% to $7,446M from $6,806M and diluted EPS from continuing operations increased 36.9% to $3.08 from $2.25 on year-over-year basis. The Q3 2018 results were negatively impacted by a pension plan annuity transaction. The company had $9,439M in bookings and the backlog grew to a record $44,614M. The strong quarter resulted in the company increasing sales guidance range to $29.1B - $29.4B and continuous operations EPS ranging from $11.70 to $11.80.

Four of the five business segments showed growth. Integrated Defense Systems net sales increased 18% to $1,755M from $1,493M in comparable periods due to higher international sales to Qatar. Revenue for the Intelligence, Information and Services segment increased 6% to $1,855M from $1,742M in the prior year driven by higher sales in classified cyber and space programs. Revenue for Missile Systems increased 4% to $2,165M from $2,082M in Q3 2018 due to higher sales in classified programs and other programs. Revenue for Space and Airborne Systems increased 14% to $1,939M from $1,695M in comparable periods from strength in classified programs and the Next Generation Overhead Persistent Infrared program. Forcepoint revenue declined (3%) to $167M from $173M in the prior year.

Raytheon and United Technologies have announced a merger of equals. Raytheon shareholders will own 43% and United Technologies shareholders will own 57% of the merged company. Raytheon shareholders will receive 2.3348 shares in the new company for each share of Raytheon that they own. The merger would create a new company called Raytheon Technologies with pro forma revenue of $74B making it the largest defense contractor. The merger was approved by both boards and also by shareholders. There is risk that the merger may not be completed as United Technologies must spin off the Carrier and Otis divisions and the deal must still pass regulatory and U.S. DoD approvals.

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	***$11.75***	***$15.72***
DPS	$1.24	$1.50	$1.72	$2.00	$2.20	$2.42	$2.68	$2.93	$3.19	$3.40	***$3.77***	***$5.54***
Shares[1]	383.2	359	339	328	314.5	307.3	299	293	288	280	***276***	***250***

Raytheon's earnings per share have exhibited some volatility over the past 10 years due to fluctuations in defense spending. But U.S. and international military spending is now strong, and Raytheon is a prime beneficiary with its focus on missiles and radars. We expect higher defense budgets to drive both the top and bottom lines. We are forecasting an

[1] Share count in millions.

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 November 4th, 2019 by Prakash Kolli

average increase of 6% annually in EPS. Raytheon's dividend per share was growing at a double-digit rate but has slowed, and we are now expecting an 8% average annual growth in dividend per share. Note that the payout ratio is relatively low at only ~32.8%. Hence, there is room for further increases even if defense spending slows.

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	***18.4***	***15.0***
Avg. Yld.	2.7%	3.0%	3.7%	3.7%	3.2%	2.5%	2.5%	2.2%	1.9%	2.0%	***1.7%***	***2.3%***

The stock price has increased markedly since our last report and is now trading above our fair value of $178 even after raising our 2019 EPS estimate. But Raytheon is no longer trading on fundamentals but rather on the expected merger with United Technologies. Our long-range price-to-earnings ratio multiple is 15.0. Our 5-year price target is now $236.

Safety, Quality, Competitive Advantage, & Recession Resiliency

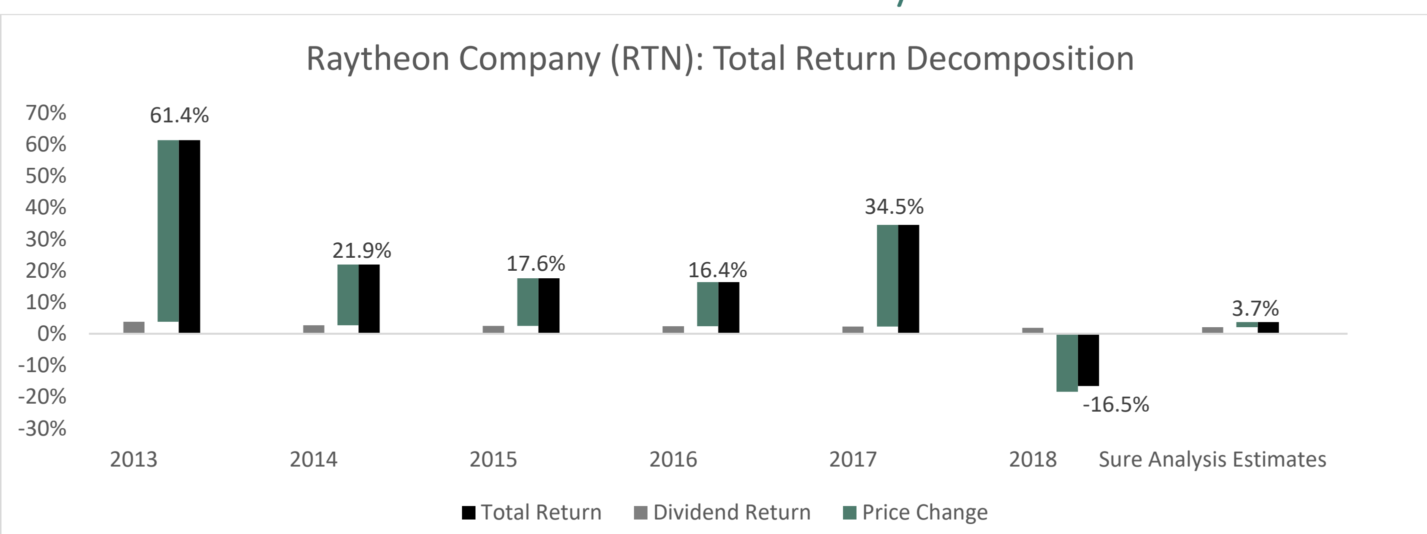
Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	25%	31%	33%	35%	37%	35%	40%	39%	46%	34%	***32%***	***35%***

As a U.S. defense contractor, Raytheon has an entrenched position in many of its end markets. Of note is the Patriot system, which has a large installed base in the U.S. and in allied militaries around the world. This system typically requires technology upgrades and also service and maintenance contracts. Raytheon also has significant strengths in naval ship missile systems, has a duopoly with Lockheed Martin in missile production and has a major presence in space and airborne radars. This gives Raytheon a competitive advantage in that they are often only one of two companies that can provide needed technologies to U.S. DoD. These characteristics lead to a good degree of recession resistance. However, the company does face risks in program cuts that could lead to revenue declines. Raytheon's balance sheet is very conservative with $500M in short-term debt, $4,258M in long-term debt and $2,646M in cash and cash equivalents.

Final Thoughts & Recommendation

At present we are forecasting a 3.7% annualized return through 2024 down from our last report due to stock price gains. Raytheon's businesses are performing extremely well, and investors are seemingly bullish on the impending merger. But the current stock price reflects this. At the current share price, we rate this stock a hold.

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 November 4th, 2019 by Prakash Kolli

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.