Raytheon Technologies Corp. (RTX)

Updated April 9th, 2020 by Eli Inkrot

Key Metrics

Current Price:	$67	**5 Year CAGR Estimate:**	8.0%	**Market Cap:**	$101.9 B
Fair Value Price:	$67	**5 Year Growth Estimate:**	6.0%	**Ex-Dividend Date[1]:**	05/16/20
% Fair Value:	101%	**5 Year Valuation Multiple Estimate:**	-0.2%	**Dividend Payment Date[1]:**	06/10/20
Dividend Yield:	2.5%	**5 Year Price Target**	$89	**Years Of Dividend Growth:**	26
Dividend Risk Score:	C	**Retirement Suitability Score:**	B	**Last Dividend Increase:**	5.0%

Overview & Current Events

Raytheon Technologies ("RTN") was created on April 3rd, 2020 after the completion of the merger between Raytheon (previous ticker: RTN) and United Technologies (previous ticker: UTX), following United Technologies' spin-offs of its Carrier ("CARR") and Otis ("OTIS") businesses. The combined business, trading with a $102 billion market cap and headquartered in Waltham, MA, is one the largest aerospace and defense companies in the world with $74 billion in pro forma 2019 sales and a global team of 195,000 employees, including 60,000 engineers and scientists. The company has four segments: Collins Aerospace Systems, Pratt & Whitney, Raytheon Intelligence & Space, and Raytheon Missiles & Defense, which generated 2019 net sales of $26 billion, $21 billion, $15 billion and $16 billion respectively.

On January 28th, 2020 United Technologies reported earnings results for the fourth quarter and full year. Adjusted earnings-per-share totaled $1.94, $0.10 above estimates, but $0.01 below the previous year. Revenue grew 8.4% to $19.6 billion, $200 million higher than expected. For the full year, adjusted earnings-per-share grew 9% to $8.26, $0.16 above the midpoint of the company's guidance. Revenue improved 16% to $77 billion. Top and bottom-line totals for the year were a record. The company had organic growth of 1% for the quarter and 5% for 2019.

Collins Aerospace grew 32% for the quarter and 1% organically. Pratt & Whitney had organic growth of 2%.

On January 30th, 2020 Raytheon reported Q4 2019 earnings. Companywide net sales increased 6.5% to $7.842 billion and diluted EPS from continuing operations increased 7.8% to $3.16 from $2.93 on year-over-year basis. The company had $12.058 billion in bookings and the backlog grew to a record $48.752 billion.

All five business segments showed growth. Integrated Defense Systems net sales increased 18% to $1.981 billion from $1.684 billion due to higher international sales. Revenue for the Intelligence, Information and Services segment increased 6% to $1.742 billion from $1.711 billion driven by higher sales in classified cyber and space programs. Revenue for Missile Systems increased 1% to $2.345 billion from $2.317 billion due to higher sales in classified programs and other programs. Revenue for Space and Airborne Systems increased 10% to $2.018 billion from $1.880 billion from strength in classified programs and the Next Generation Overhead Persistent Infrared program. Forcepoint revenue grew 3% to $177 million from $172 million in the prior year. For the year, Raytheon's sales increased 16% to $36.340 billion from $32.162 billion in 2018 and diluted earnings per share increased 17.4% to $11.92 from $10.15 in 2018.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	$4.74	$5.49	$5.34	$6.21	$6.82	$6.29	$6.61	$6.60	$7.61	$8.26	***$4.16***	***$5.57***
DPS	$1.70	$1.87	$2.03	$2.20	$2.36	$2.56	$2.62	$2.72	$2.84	$2.94	***$1.66***	***$2.22***
Shares[2]	921	907	919	917	909	838	809	799	861	864	***1,515***	***1,500***

Note that we have elected to show United Technologies' history in the table above, as 57% of the new business is now owned by legacy UTX shareholders. However, the company is much different today with the merger and spin-offs. With that being said, both United Technologies and Raytheon have put together solid operating records. In the last decade

[1] Estimate.

[2] 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.

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United Technologies grew earnings-per-share by an average rate of 7.2%, while increasing its dividend for over 25 years. Meanwhile, Raytheon grew earnings-per-share by 9.3% annually while increasing its dividend for 15 consecutive years.

Moving forward we anticipate solid growth to continue, forecasting 6% growth over the intermediate term. This takes into account the strong history of the underlying operating businesses, along with the idea of grow becoming more difficult given the size of the business along with the recent uncertainty related to the worldwide coronavirus pandemic.

We are forecasting just over $4 in earnings-per-share for this year, based on $70 billion in sales and a 9% net profit margin (in-line with the companies' past) to go along with an increased share count. This could be too ambitious if a global recession comes about, but we are enthused by the company's backlog and resiliency in lesser times. While the quarterly dividend has not yet been declared, we are expecting a ~40% payout ratio.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	15.0	14.6	14.7	16	16.4	17.0	15.3	17.7	15.7	18.1	***16.2***	***16.0***
Avg. Yld.	2.4%	2.3%	2.6%	2.2%	2.1%	2.4%	2.6%	2.3%	2.5%	2.0%	***2.5%***	***2.5%***

Once again note that we are using the history of United Technologies, which has traded with an average P/E ratio of about 16 times earnings over the past decade. We believe this is a fair starting multiple, considering the quality and growth prospects of the firm. With shares trading around this mark, this implies little influence from this component.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	36%	34%	38%	35%	35%	41%	40%	41%	37%	36%	***40%***	***40%***

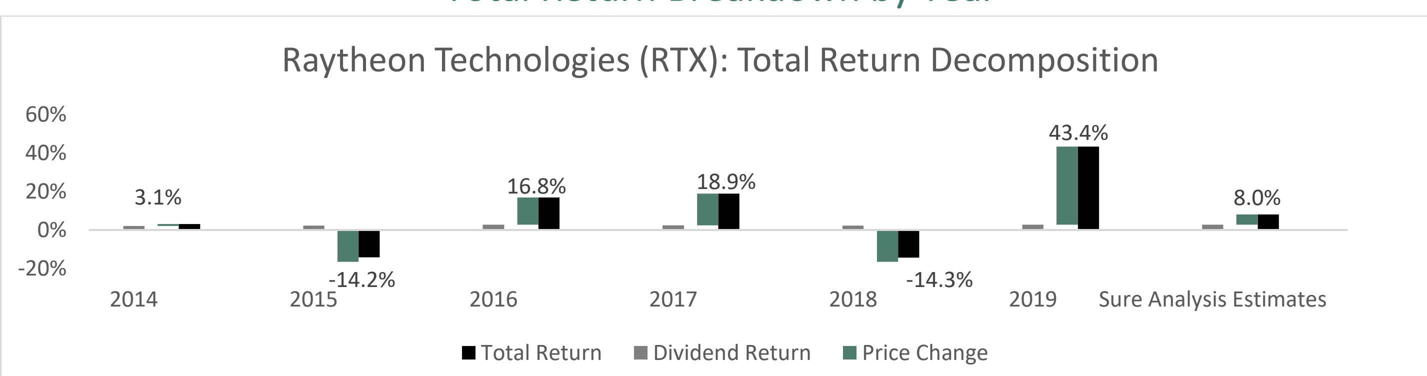
Both United Technologies and Raytheon showed tremendous resiliency during the last recession, with UTX posting $4.90, $4.12, $4.74 and $5.49 in earnings-per-share during the 2008 through 2011 timeframe, while Raytheon increased earnings every year during the recession. Moreover, both companies kept increasing their dividends during this period.

Raytheon Technologies CEO Greg Hayes has said that the current slowdown in commercial aerospace may be a two-year problem, but also notes that the company has $7 billion of cash on hand, $5 billion in financing and a $70 billion backlog.

Final Thoughts & Recommendation

There is uncertainty surrounding the new RTX, related to how the merged company will operate and the global pandemic. However, we are enthused on a number of fronts, including the storied histories of the companies, the resilient businesses and tremendous backlog. With shares trading near our estimate of fair value, we are forecasting 8.0% annual return potential stemming from 6% growth and a 2.5% dividend yield. We rate shares as a hold.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	52,275	55,754	57,708	56,600	57,900	56,098	57,244	59,837	66,501	77,046
Gross Profit	14,321	15,385	15,555	16,132	17,002	15,667	15,773	15,636	16,516	19,981
Gross Margin	27.4%	27.6%	27.0%	28.5%	29.4%	27.9%	27.6%	26.1%	24.8%	25.9%
SG&A Exp.	5,798	6,161	6,452	6,364	6,172	5,886	5,958	6,429	7,066	8,521
D&A Exp.	1,300	1,263	1,524	1,735	1,820	1,863	1,962	2,140	2,433	3,783
Operating Profit	6,898	7,846	7,684	8,549	9,593	7,291	8,221	8,138	8,553	8,966
Op. Margin	13.2%	14.1%	13.3%	15.1%	16.6%	13.0%	14.4%	13.6%	12.9%	11.6%
Net Profit	4,373	4,979	5,130	5,721	6,220	7,608	5,055	4,552	5,269	5537
Net Margin	8.4%	8.9%	8.9%	10.1%	10.7%	13.6%	8.8%	7.6%	7.9%	7.2%
Free Cash Flow	5,068	5,661	3,714	4,586	5,134	4,294	1,793	3,237	4,020	6,276
Income Tax	1,725	2,134	1,711	1,999	2,244	2,111	1,697	2,843	2,626	2,295

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets ($B)	58,493	61,452	89,409	90,594	91,206	87,484	89,706	96,920	134,211	139,716
Cash & Equivalents	4,083	5,960	4,819	4,619	5,229	7,075	7,157	8,985	6,152	7,378
Acc. Receivable	8,925	9,546	11,099	11,458	10,448	10,653	11,481	12,595	14,271	13,524
Inventories	7,766	7,797	9,537	10,330	7,642	8,135	8,704	9,881	10,083	10,950
Goodwill & Int.	21,781	21,861	42,990	43,689	42,976	42,904	42,743	43,793	74,536	74,109
Total Liabilities	35,844	38,632	62,340	57,375	58,642	58,640	60,537	65,499	93,601	95,485
Accounts Payable	5,206	5,570	6,431	6,965	6,250	6,875	7,483	9,579	11,080	10,809
Long-Term Debt	10,289	10,260	23,221	20,241	19,701	20,425	23,901	27,485	45,537	43,648
Total Equity	21,385	21,880	25,914	31,866	31,213	27,358	27,579	29,610	38,446	41,774
D/E Ratio	0.48	0.47	0.90	0.64	0.63	0.75	0.87	0.93	1.18	1.04

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	7.7%	8.3%	6.8%	6.4%	6.8%	8.5%	5.7%	4.9%	4.6%	4.0%
Return on Equity	21.1%	23.0%	21.5%	19.8%	19.7%	26.0%	18.4%	15.9%	15.5%	13.8%
ROIC	13.7%	15.1%	12.3%	11.0%	11.8%	15.0%	9.9%	8.1%	7.3%	6.4%
Shares Out.	921	907	919	917	909	838	809	799	795	864
Revenue/Share	56.65	61.48	63.65	61.85	63.51	63.52	69.29	74.88	82.09	89.18
FCF/Share	5.49	6.24	4.10	5.01	5.63	4.86	2.17	4.05	4.96	7.26

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