L3Harris Technologies (LHX)

Updated May 16th, 2022 by Prakash Kolli

Key Metrics

Current Price:	$236	**5 Year CAGR Estimate:**	7.9%	**Market Cap:**	$45.55B
Fair Value Price:	$216	**5 Year Growth Estimate:**	8.0%	**Ex-Dividend Date:**	06/02/22
% Fair Value:	109%	**5 Year Valuation Multiple Estimate:**	-1.8%	**Dividend Payment Date:**	06/17/22
Dividend Yield:	1.9%	**5 Year Price Target**	$317	**Years Of Dividend Growth:**	21
Dividend Risk Score:	A	**Retirement Suitability Score:**	C	**Rating:**	Hold

Overview & Current Events

L3Harris Technologies (LHX) is the result of a merger between L3 Technologies and Harris Corporation completed on June 29, 2019, forming the sixth largest defense contractor. Shareholders of L3 Technologies received 1.30 shares of Harris Corporation for each of their own shares outstanding. The company now reports three business segments: Integrated Mission Systems (~42% of revenue), Communication Systems (~23% of revenue), and Space and Airborne Systems (~35% of revenue). The majority of the L3Harris' sales are to the US Government or to other defense contractors. The company had revenue of about $17.8B in 2021.

L3Harris reported weak Q1 2022 results on April 28th, 2022. Companywide revenue fell (-5%) to $4,103M from $4,299M and diluted non-GAAP EPS decreased (-2%) to $3.12 from $3.18 on year-over-year basis.

Integrated Mission Systems segment revenue fell (-2%) to $1,721M from $1,751M in the prior year due to declines in ISR offset by Maritime and Commercial Aviation. Revenue for Space & Airborne Systems decreased (-1%) to $1,450M from $1,460M. Growth came from Space offset by declines in Intel & Cyber, Mission Networks, and the F-35. Communications systems revenue decreased (-13%) to $963M from $1,112M due to lower volumes in Tactical Communications, Integrated Vision, and Public Safety.

L3Harris is facing supply chain challenges affecting its ability to source electronics components.

The funded book-to-bill ratio was 0.98 and the organic backlog grew 6% to $21.1B. The company won a $6.1B IDIQ for SINCGARS, a $3.7B IDIQ for portable radios, $750M IDIQ for vehicle radios, $300M for manpack radios, $500M for servicing Canadian CF-18, and several other large awards.

The company guided for $17.3B - $17.7B in revenue and $13.35 - $13.65 for EPS in 2022.

Growth on a Per-Share Basis[1]

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	$4.80	$4.92	$5.00	$5.14	$5.70	$5.12	$6.38	$10.08	$11.60	$12.95	***$13.50***	***$19.84***
DPS	$1.22	$1.48	$1.68	$1.88	$2.00	$2.12	$2.28	$2.87	$3.40	$4.08	***$4.48***	***$6.58***
Shares[2]	112	107	106	124	125	120	118	216	206	***199***	***193***	***166***

L3Harris has only a short operating history. But the new company is positioned for both top and bottom-line growth in high margin market segments. Increased defense spending will support top line growth. Both predecessor organizations have a history of increasing earnings and dividends. We are currently forecasting average annual earnings per share growth of 8% out to 2027. The COVID-19 pandemic impacted revenue in the commercial aviation business but is now recovering. The defense budget is increasing and the conflict in Ukraine should provide some tailwinds offset by supply chain disruptions. Bottom line growth will be driven by organic sales increases, higher margins, and robust share buybacks. L3Harris has about $2.2B left in its share repurchase authorization. We are forecasting on average 8% annual increase in the dividend out to 2027 due to the low payout ratio.

---

[1] Note that L3Harris is the successor organization to Harris and thus tabular data before 2019 is for Harris.

[2] Share count is in millions.

Disclosure: This analyst is long LHX.

L3Harris Technologies (LHX)

Updated May 16th, 2022 by Prakash Kolli

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	8.3	9.6	13.3	14.2	13.9	19.7	22.2	20.3	36.2	23.4	***17.5***	***16.0***
Avg. Yld.	3.1%	3.1%	2.5%	2.6%	2.5%	2.1%	1.6%	1.7%	1.8%	1.9%	***1.9%***	***2.1%***

L3Harris' stock price is up since our last report due to the conflict in Ukraine despite supply chain delays. We have left our earnings estimate at the mid-point of guidance for 2022. Our fair value multiple is 16X, discounting for merger uncertainties. The stock is trading below our fair value estimate of $216. Our 5-year price target is now $317.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	25%	30%	34%	37%	35%	41%	36%	28%	29%	32%	***33%***	***33%***

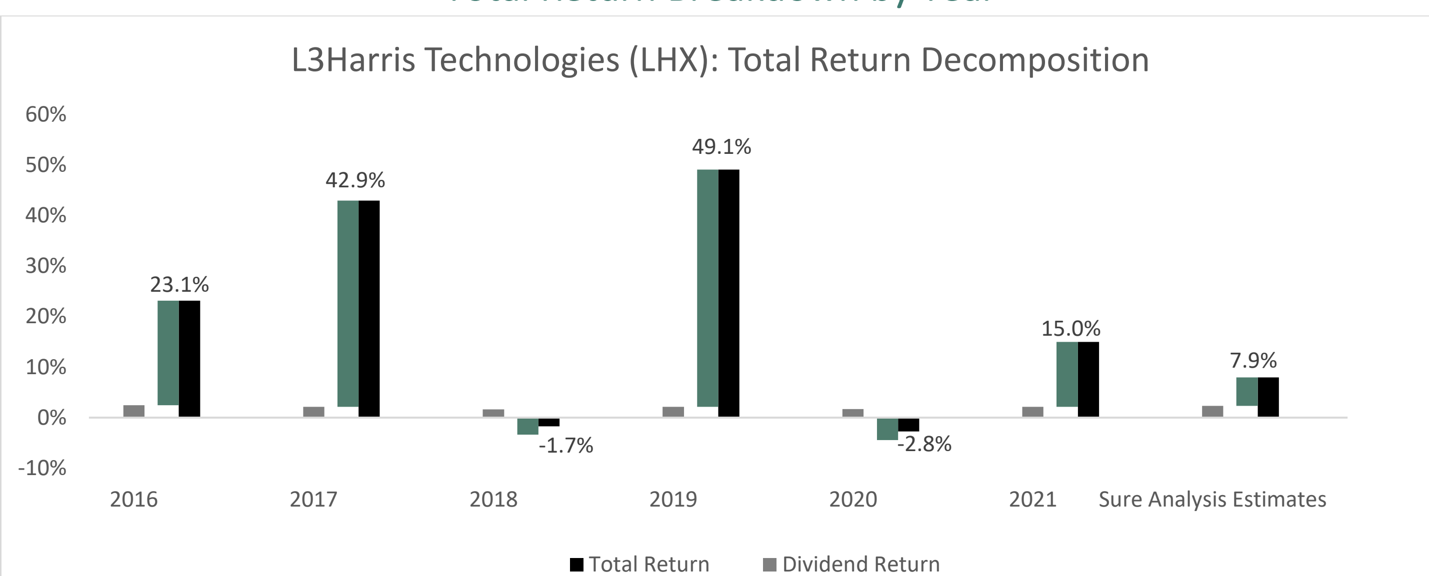
As a large defense contractor L3Harris has competitive advantages related to defense contracting, which often requires knowledge of acquisition regulations and accounting standards, particularly for large programs. The company develops and manufactures complex and bespoke systems for the DoD requiring a skilled work force with security clearances that is not easily replicated. Notably, L3Harris is the market leader in tactical communications. Furthermore, L3Harris has built long-term relationships with both the DoD and prime contractors in its areas of expertise. These attributes make it somewhat recession resistant. But the company may experience top and bottom-line declines if defense programs are cut, or the defense budget is decreased. COVID-19 was causing headwinds for commercial aviation and public safety.

L3Harris took on debt to fund the merger. Short-term debt is $3M, current long-term debt is $262M, and long-term debt is $6,795M offset by cash and equivalents of $402M. Interest coverage is 9.8X, and the leverage ratio is about 2.1X.

Final Thoughts & Recommendation

We are forecasting 7.9% annualized total return over the next five years from a dividend yield of 1.9%, 8% EPS growth, and (-1.8%) P/E multiple contraction. L3Harris is being impacted by supply chain issues and the global shortage of electronic components affecting organic revenue growth. The company is aggressively buying back shares and rapidly raising the dividend. The dividend safety is excellent. At the current stock 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 is long LHX.

L3Harris Technologies (LHX)

Updated May 16th, 2022 by Prakash Kolli

Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	5,112	5,012	3,885	5,992	5,897	6,168	6,801	9,263	18,194	17,814
Gross Profit	1,727	1,702	1,515	2,160	2,043	2,102	2,334	2,537	5,308	5,376
Gross Margin	33.8%	34.0%	39.0%	36.0%	34.6%	34.1%	34.3%	27.4%	29.2%	30.2%
SG&A Exp.	914	820	883	1,105	1,150	1,182	1,242	1,881	3,315	3,280
D&A Exp.	221	204	244	361	311	259	258	442	1,032	967
Operating Profit	813	882	632	1,055	893	920	1,092	656	1,993	2,096
Op. Margin	15.9%	17.6%	16.3%	17.6%	15.1%	14.9%	16.1%	7.1%	11.0%	11.8%
Net Profit	113	535	334	324	543	699	949	822	1,119	1,846
Net Margin	2.2%	10.7%	8.6%	5.4%	9.2%	11.3%	14.0%	8.9%	6.2%	10.4%
Free Cash Flow	655	645	706	772	450	615	1,024	766	2,422	2,352
Income Tax	203	256	109	273	261	206	160	73	234	440

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	4,858	4,919	13,127	12,009	10,090	9,851	10,117	38,336	36,960	34,709
Cash & Equivalents	321	561	481	487	484	288	530	824	1,276	941
Acc. Receivable	569	458	837	398	368	466	457	1,216	1,344	1,045
Inventories	669	619	1,015	867	841	411	360	1,219	973	982
Goodwill & Int.	2,000	1,969	8,123	6,583	6,470	6,361	6,210	28,459	26,784	24,830
Total Liabilities	3,297	3,094	9,725	8,952	7,162	6,573	6,754	15,592	16,119	15,390
Accounts Payable	340	324	581	494	540	622	525	1,261	1,406	1,767
Long-Term Debt	1,735	1,624	5,216	4,517	4,030	3,790	3,522	6,954	6,918	7,061
Total Equity	1,561	1,826	3,397	3,056	2,928	3,278	3,363	22,587	20,724	19,320
LTD/E Ratio	1.11	0.89	1.54	1.48	1.38	1.16	1.05	0.31	0.33	0.37

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	2.2%	10.9%	3.7%	2.6%	4.9%	7.0%	9.5%	3.4%	3.0%	5.2%
Return on Equity	6.5%	31.6%	12.8%	10.0%	18.1%	22.5%	28.6%	6.3%	5.2%	9.2%
ROIC	3.1%	15.9%	5.5%	4.0%	7.5%	10.0%	13.6%	4.5%	3.9%	6.8%
Shares Out.	111.2	107.3	106.8	125	124.3	121.1	120.5	223.7	215.9	203.2
Revenue/Share	45.97	46.71	36.38	47.94	47.44	50.93	56.44	41.41	84.27	87.67
FCF/Share	5.89	6.01	6.61	6.18	3.62	5.08	8.50	3.42	11.22	11.57

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