



# Huntington Ingalls Industries Inc. (HII)

Updated September 1<sup>st</sup>, 2022 by Prakash Kolli

## Key Metrics

<b>Current Price:</b>	\$227	<b>5 Year CAGR Estimate:</b>	6.0%	<b>Market Cap:</b>	\$9.20B
<b>Fair Value Price:</b>	\$213	<b>5 Year Growth Estimate:</b>	5.0%	<b>Ex-Dividend Date:</b>	08/25/22
<b>% Fair Value:</b>	107%	<b>5 Year Valuation Multiple Estimate:</b>	-1.3%	<b>Dividend Payment Date:</b>	09/09/22
<b>Dividend Yield:</b>	2.2%	<b>5 Year Price Target</b>	\$272	<b>Years Of Dividend Growth:</b>	10
<b>Dividend Risk Score:</b>	B	<b>Retirement Suitability Score:</b>	C	<b>Rating:</b>	Hold

## Overview & Current Events

Huntington Ingalls Industries was spun out of Northrop Grumman in a tax-free transaction on March 31, 2011. Shareholders received one share in the new company for every six shares of Northrop Grumman owned. Today, the company primarily builds nuclear and non-nuclear ships for the U.S. Navy. The company reports three business segments: Newport News Shipbuilding, Ingalls Shipbuilding, and Mission Technologies. Newport News builds nuclear powered aircraft carriers and submarines. Ingalls builds surface combatant ships, amphibious assault ships, and Coast Guard cutters. Mission Technologies provides fleet maintenance and modernization, IT support, nuclear management and operations, and unmanned systems. The company had approximately \$9.5B in revenue in 2021.

Huntington Ingalls reported Q2 2022 results on August 4<sup>th</sup>, 2022. Companywide revenue rose 19.3% to \$2,662M compared to \$2,231M and diluted earnings per share grew 38.8% to \$4.44 from \$3.20 on a year-over-year basis. Companywide operating margins increased 88 bps to 8.5% from 7.6%. Revenue from Ingalls Shipbuilding decreased (-1.8%) to \$658M from \$670M and operating margins rose 417 bps to 16.1% from 11.9% in the prior year driven by lower revenue in surface combatant ships offset by assault ships. Newport News revenue rose 5.1% to \$1,433M from \$1,363M in comparable periods due to higher aircraft carrier volumes offset by nuclear support services and flattish submarine volumes. Operating margins rose to 6.6% from 5.6%. Revenue for Mission Technologies increased 153.2% to \$600M from \$237M due to gains from the Alion acquisition. Operating margins decreased to 4.2% from 5.5%.

The US Navy selected the REMUS 300 as the next generation small UUV program of record.

Huntington Ingalls guided for ship building revenue of \$8.2B - \$8.5B and margins of 8.0% to 8.1%. The company guided higher for Mission Technologies revenue of ~\$2.6B and margins of ~2.5%

Huntington Ingalls' total backlog now stands at \$47.2B after about \$2.0B in contract wins of which \$24.6B is funded.

## Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
<b>EPS</b>	\$2.91	\$5.18	\$6.85	\$8.36	\$12.14	\$10.46	\$19.11	\$14.01	\$17.14	\$13.50	<b>\$15.20</b>	<b>\$19.40</b>
<b>DPS</b>	\$0.10	\$0.50	\$1.00	\$1.70	\$2.10	\$2.52	\$3.02	\$3.61	\$4.23	\$4.23	<b>\$5.10</b>	<b>\$7.49</b>
<b>Shares</b>	49.6	48.7	48.3	46.8	46.2	45.1	41.9	40.8	40.5	39.1	<b>38.9</b>	<b>35.2</b>

Huntington Ingalls' historical adjusted earnings per share has been volatile due to pension adjustments, goodwill, and divestments. But the Pentagon is spending heavily on aircraft carriers, nuclear submarines, and amphibious assault ships. The U.S. Navy has a goal of 355 ships by 2034. Huntington Ingalls should experience top and bottom line growth due to sale of ships and submarines. Huntington Ingalls' operations were impacted by COVID-19, but acceleration of aircraft carrier revenue and deferral of payroll taxes helped the second half. The company acquired Alion Science & Technology and bulked up its Technical Solution segment, but this segment is a low margin business. After 2021, we are forecasting on average 5% annual growth in earnings per share out to 2027. The share count should trend lower as well.

Huntington Ingalls has paid a growing dividend at a double-digit rate albeit off a low base since 2012. We believe that the dividend growth rate will slow to about 8% on average out to 2027. The forward payout ratio is about 34%, which leaves room for future increases.

*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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## Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	13.4	11.8	14.6	14.7	12.7	20.1	12.2	15.7	10.8	14.2	15.0	14.0
Avg. Yld.	0.3%	0.6%	0.9%	1.4%	1.2%	1.1%	1.6%	1.6%	2.1%	2.5%	2.2%	2.8%

Huntington Ingalls stock price is up since our last report on solid results. We raised our estimated earnings per share in 2022 to match consensus. The stock now trades above our fair value multiple of 14X, which is the trailing average for the past 10 years. Our current fair value estimate is now \$213. Our 5-year price target is now \$273.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

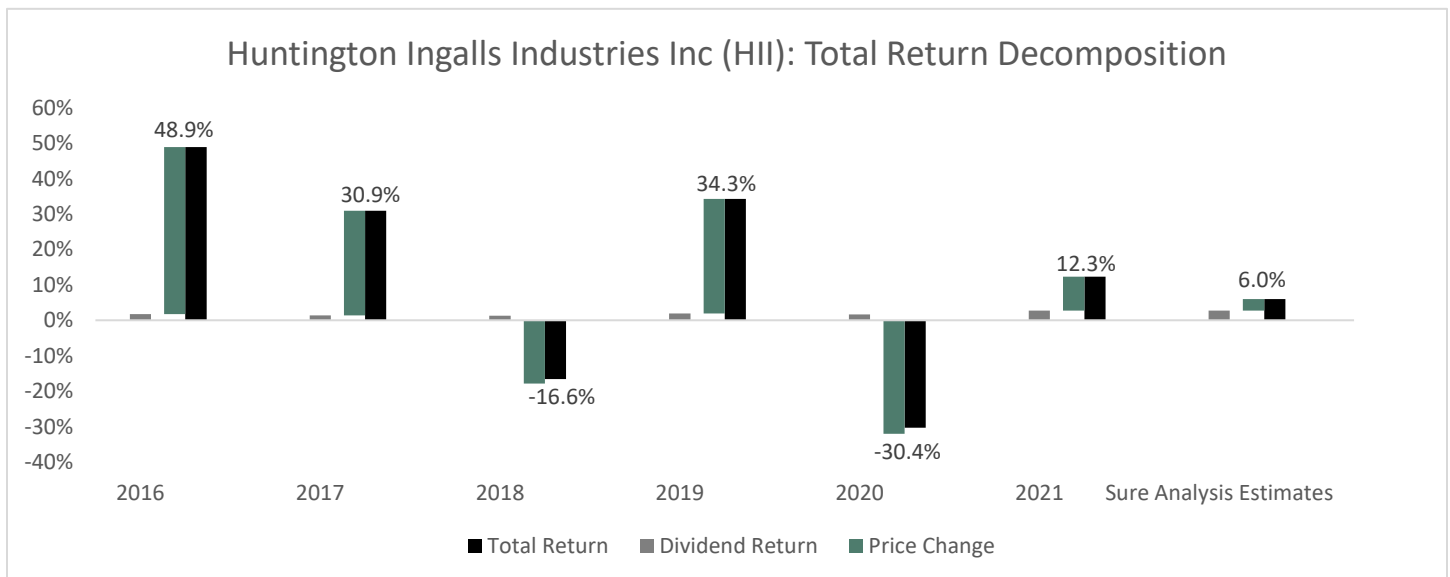
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	3%	10%	15%	20%	17%	24%	16%	26%	25%	35%	34%	39%

As a U.S. prime defense contractor, Huntington Ingalls has an entrenched position in its end markets. The company's main competitive advantage is the expertise it brings in designing and fabricating bespoke ships for the U.S. Navy. This expertise is not easy to recreate. Indeed, in the U.S., the company is the only provider of nuclear aircraft carriers, one of two providers of nuclear submarines and the only provider of amphibious assault ships. These platforms have decades long life cycles and Huntington Ingalls has expertise and experience to perform sustainment and modernization. These characteristics lead to a good degree of recession resistance. However, the company does face risks in program cuts and changes to future naval requirements. Long-term debt is \$3,102M not including pension plan liabilities. Cash and equivalents on hand is \$375M. Debt is rising as the company makes acquisitions for the Technical Solutions segment.

## Final Thoughts & Recommendation

At present we are forecasting a 6.0% annualized total return through 2027 from a dividend yield of 2.2%, 5% EPS growth, and (-1.3%) P/E multiple expansion. The company continues to grow the Technical Solutions segment through M&A and is recently winning new contracts. The shipbuilding backlog remains high. The dividend is well covered by earnings and should continue growing. At the current price, we rate this stock a hold.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	6708	6820	6957	7020	7068	7441	8176	8899	9361	9524
Gross Profit	1079	1237	1417	1503	1623	1628	1791	1531	1670	1368
Gross Margin	16.1%	18.1%	20.4%	21.4%	23.0%	21.9%	21.9%	17.2%	17.8%	14.4%
SG&A Exp.	739	739	726	669	768	759	871	788	904	898
D&A Exp.	184	226	194	180	186	205	203	227	247	293
Operating Profit	340	498	691	834	870	869	934	743	767	472
Operating Margin	5.1%	7.3%	9.9%	11.9%	12.3%	11.7%	11.4%	8.3%	8.2%	5.0%
Net Profit	146	261	338	404	573	479	836	549	696	544
Net Margin	2.2%	3.8%	4.9%	5.8%	8.1%	6.4%	10.2%	6.2%	7.4%	5.7%
Free Cash Flow	170	97	590	673	537	432	451	366	740	429
Income Tax	95	133	169	228	211	293	135	134	114	78

## Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	6392	6225	6239	6024	6352	6374	6383	7031	8157	10627
Cash & Equivalents	1057	1043	990	894	720	701	240	75	512	627
Accounts Receivable	191	171	244	236	318	442	252	318	397	433
Inventories	288	311	339	285	210	183	128	136	137	161
Goodwill & Int. Ass.	1429	1409	1573	1451	1782	1725	1755	1865	2129	3787
Total Liabilities	5725	4704	4874	4534	4699	4616	4867	5443	6256	7819
Accounts Payable	377	337	269	317	316	375	562	497	460	603
Long-Term Debt	1830	1779	1670	1273	1278	1279	1283	1286	1686	3298
Shareholder's Equity	667	1521	1365	1490	1653	1758	1516	1588	1901	2808
LTD/E Ratio	2.74	1.17	1.22	0.85	0.77	0.73	0.85	0.81	0.89	1.17

## Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	19.1%	23.9%	23.4%	28.3%	9.2%	8.2%	13.1%	7.5%	9.3%	5.8%
Return on Equity	5.6%	9.0%	10.7%	13.9%	39.9%	35.4%	51.1%	28.1%	36.5%	23.1%
ROIC	50.1	50.4	49.3	48.3	21.5%	19.4%	28.6%	16.1%	20.1%	11.2%
Shares Out.	49.6	48.7	48.3	46.8	46.2	45.1	41.9	40.8	40.0	40.3
Revenue/Share	3.39	1.92	11.97	13.93	230.57	214.95	186.67	162.47	149.75	236.33
FCF/Share	19.1%	23.9%	23.4%	28.3%	18.23	8.84	10.30	9.43	11.38	10.65

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

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