



Northrop Grumman Corporation (NOC)

Updated November 6th, 2022 by Prakash Kolli

Key Metrics

Current Price:	\$523	5 Year CAGR Estimate:	2.5%	Market Cap:	\$80.46B
Fair Value Price:	\$372	5 Year Growth Estimate:	8.0%	Ex-Dividend Date:	11/26/22 ¹
% Fair Value:	141%	5 Year Valuation Multiple Estimate:	-6.6%	Dividend Payment Date:	12/15/22
Dividend Yield:	1.3%	5 Year Price Target	\$547	Years Of Dividend Growth:	19
Dividend Risk Score:	A	Retirement Suitability Score:	C	Rating:	Sell

Overview & Current Events

Northrop Grumman Corporation is one of the five largest US aerospace and defense contractors based on revenue. The company reports four business segments: Aeronautics Systems (aircraft and UAVs), Mission Systems (radars, sensors and systems for surveillance and targeting), Defense Systems (sustainment and modernization, directed energy, tactical weapons), and Space Systems (missile defense, space systems, hypersonics and space launchers). Northrop Grumman completed its acquisition of Orbital ATK in 2018 and divested IT Services in 2021. Northrop Grumman makes the B-2 Spirit, E-2D, E-8C, RQ-4 Global Hawk, MQ-4C Triton, and MQ-8B/C Fire Scout. The company also provides content on the F-35 and F/A-18. It won the contract for the B-21 Raider. The company had revenue of over \$35.7B in 2021.

Northrop Grumman released results for Q3 FY 2022 on October 27th, 2022. Companywide revenue increased 3% to \$8,971M from \$8,720M and diluted adjusted earnings per share decreased (-11%) to \$5.89 from \$6.63 on a year-over-year basis. Revenue for Aeronautics Systems was down (-7%) to \$2,537M from \$2,725M in the prior year due to lower volumes in Manned Aircraft and Autonomous Systems. Revenue for Defense Systems fell (-5%) to \$1,345M from \$1,409M in comparable quarters due to program completion, lower scope on an international training program, and wind down of JSTARS and the UKAWACS offset by the NATO AGS ISS. Revenue for Mission Systems increased 1% to \$2,456M in the quarter from \$2,436M in the prior year due to higher volumes on Networked Information Solutions and SEWIP offset by Navigation, Targeting and Survivability, and JCREWS. Revenue for Space Systems increased 18% to \$3,163M in Q3 2022 from \$2,681M in Q3 2021 from higher sales in Launch & Strategic Missiles, Graphite-Epoxy Motor (GEM63) for Amazon's Kuiper program, SDA programs, Commercial Resupply Services (CRS), and restricted programs.

The company won \$8.7B in contracts in Q3 with a 0.97 book-to-bill ratio including \$2.8B for restricted programs, \$1.3B for GMD, and \$0.8B for SDA Tranche 1 Tracking Layer. The total backlog is ~\$79.6B at end of the quarter of which \$32.6B is funded. The company guided for \$36,200M to \$36,600M in sales and \$24.50 to \$25.10 earnings per share in 2022.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	\$7.81	\$8.35	\$9.75	\$10.39	\$12.19	\$11.47	\$21.33	\$21.21	\$23.65	\$25.63	\$24.80	\$36.44
DPS	\$2.15	\$2.38	\$2.71	\$3.10	\$3.50	\$3.90	\$4.70	\$5.16	\$5.67	\$6.28	\$6.92	\$10.17
Shares²	237	217	198	181	175	174	171	167	167	156	153	138

Northrop Grumman's earnings have increased substantially over time driven by top line growth from contract wins, modernization and upgrades, services, and acquisitions. A significant reduction in share count has helped drive earnings per share gains as well. Looking forward, the company will achieve both revenue and EPS growth through its involvement in the F-35, B-2, E2-2D, B-21, and space platforms. We reduced our estimate of average annual EPS growth to 8% out to 2027 due to a weaker outlook and US budget uncertainties. The company retired debt early and conducted share buybacks with sale proceeds of the IT Services segment. Northrop Grumman has paid a growing dividend for 19 years. The payout ratio is currently low at approximately 28% so there is room for further increases.

¹ Estimated based on prior years. Northrop Grumman has not yet announced the next quarterly dividend.

² 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.



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Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2020	Now	2026
Avg. P/E	8.2	10.4	12.9	16.1	17.4	23.0	16.8	17.9	13.8	13.6	21.1	15.0
Avg. Yld.	3.4%	2.7%	2.1%	1.9%	1.6%	1.5%	1.7%	1.7%	1.7%	1.8%	1.3%	1.9%

Northrop Grumman's stock price is up significantly since our last report despite missing third quarter estimates. The company's outlook remains the same. The stock trades higher than our fair value multiple of 15X, near the trailing 10-year average. Our current fair value is now \$372. Our current 5-year price target is now \$547.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	28%	29%	28%	30%	29%	34%	25%	24%	24%	25%	28%	28%

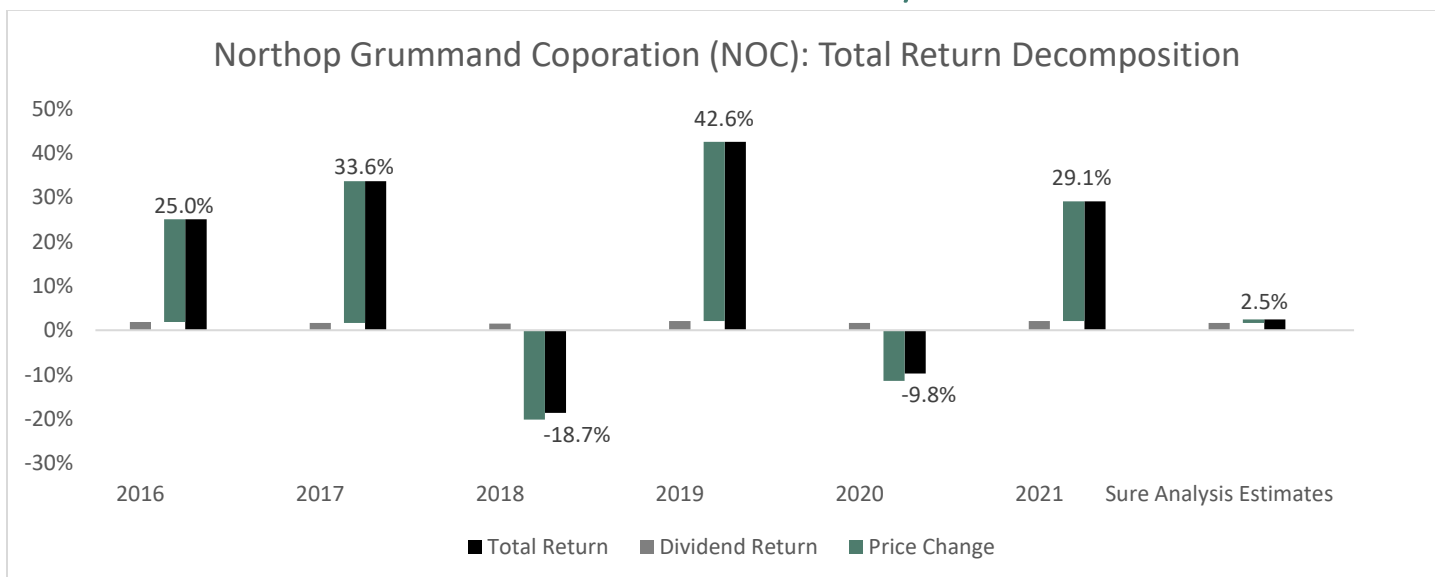
As a prime US defense contractor, Northrop Grumman has an entrenched position in many of its end markets. Of note are the B-2, B-21, E-2D, E-8C, Global Hawk and Triton platforms. Few companies have the technical expertise and classified workforce to build these platforms. In addition, these platforms have decades long life cycles and Northrop Grumman has the 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 changing administrations that could lead to revenue declines caused by new priorities to the defense budget.

Debt increased due to the Orbital ATK acquisition, which the company is paying down. Long-term debt is now at \$11,803M offset by \$1,666M in cash and equivalents. Interest coverage is 14X and the leverage ratio is down to 1.4X.

Final Thoughts & Recommendation

At present we are forecasting a 2.5% annualized total return through 2027 from a dividend yield of 1.3%, 8% EPS growth, and (-6.6%) P/E multiple contraction. Northrop Grumman maintained its forecast for 2022. The company's balance sheet is solid, and the credit rating was upgraded. The Space segment is rapidly growing. The dividend yield is low, but the dividend safety is high as illustrated by the low payout ratio and reasonable debt level. But the stock price is rich at this juncture. At the current price, we rate this high-quality stock a sell.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	25218	24661	23979	23526	24706	26004	30095	33841	36799	35667
Gross Profit	5580	5379	5601	5642	5909	5930	6791	7259	7478	7268
Gross Margin	22.1%	21.8%	23.4%	24.0%	23.9%	22.8%	22.6%	21.5%	20.3%	20.4%
SG&A Exp.	2450	2256	2405	2566	2632	2712	3011	3290	3413	3597
D&A Exp.	510	495	462	467	456	475	800	1018	1267	1239
Operating Profit	3130	3123	3196	3076	3277	3218	3780	3969	4065	3671
Op. Margin	12.4%	12.7%	13.3%	13.1%	13.3%	12.4%	12.6%	18.8%	11.0%	10.3%
Net Profit	1978	1952	2069	1990	2043	2869	3229	2248	3189	7005
Net Margin	7.8%	7.9%	8.6%	8.5%	8.3%	11.0%	10.7%	10.7%	8.7%	19.6%
Free Cash Flow	2309	2119	2032	1691	1893	1685	2578	3033	2885	2152
Income Tax	987	911	868	800	638	1360	513	300	539	1933

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	26543	26381	26572	24424	25614	35128	37653	41089	44469	42579
Cash & Equivalents	3862	5150	3863	2319	2541	11225	1579	2245	4907	3530
Acc. Receivable	2858	2685	2806	2841	3299	1054	1448	1326	1501	1467
Inventories	798	698	742	807	816	398	654	783	759	811
Goodwill & Int.	12431	12438	12466	12460	12450	12507	20044	19748	18301	18090
Total Liabilities	17029	15761	19337	18902	20355	27996	29466	32270	33890	29653
Accounts Payable	1392	1229	1305	1282	1554	1661	2182	2226	1806	2197
Long-Term Debt	3930	5928	5925	6386	7058	14399	13883	12770	14261	12777
Total Equity	9514	10620	7235	5522	5259	7132	8187	8819	10579	12930
D/E Ratio	0.41	0.56	0.82	1.16	1.34	2.02	1.70	1.45	1.3	0.99

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	7.6%	7.4%	7.8%	7.8%	8.2%	9.4%	8.9%	5.7%	7.5%	16.1%
Return on Equity	19.9%	19.4%	23.2%	31.2%	37.9%	46.3%	42.2%	26.4%	32.9%	59.6%
ROIC	14.3%	13.0%	13.9%	15.9%	16.9%	17.0%	14.8%	10.3%	13.7%	27.3%
Shares Out.	237.1	216.7	198.4	181.3	175.1	174.1	170	167	168	161
Revenue/Share	99.52	105.43	113.06	122.79	136.88	148.09	172.37	199.06	219.56	221.67
FCF/Share	9.11	9.06	9.58	8.83	10.49	9.60	14.77	17.84	17.21	13.37

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

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