

General Dynamics Corp. (GD)

\$130.62 (As of 04/30/20)

Price Target (6-12 Months): **\$138.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 02/21/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:B

Value: A

Growth: C

Momentum: C

Summary

General Dynamics ended the first quarter of 2020 on a dismal note, with both earnings and revenues missing the Zacks Consensus Estimate. It boasts a strong position in the U.S. defense space and overseas, and continues to witness strong order growth, securing some pivotal contracts from the U.S. government and its overseas clients. Product innovation can be expected to expand its footprint in the business jet market. Also, in the past year, its shares have outperformed the industry. However, the slashing of shipbuilding investments by \$4 billion, per the recently proposed fiscal 2021 defense budget, could deal a heavy blow for the shipbuilding giant, going ahead. Moreover, it anticipates COVID-19 to continue affecting its businesses during the entire of 2020. It also faces intense competition for its broad portfolio of products and services.

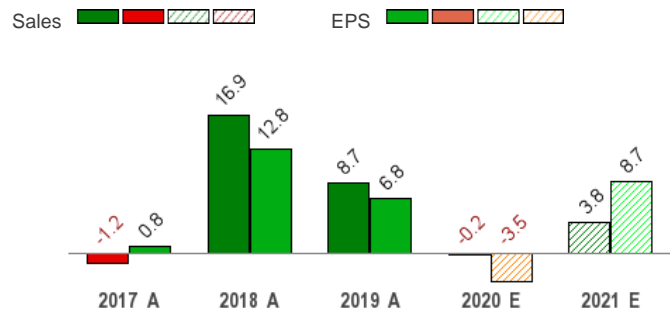
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$193.76 - \$100.55
20 Day Average Volume (sh)	1,954,554
Market Cap	\$37.5 B
YTD Price Change	-25.9%
Beta	1.01
Dividend / Div Yld	\$4.40 / 3.4%
Industry	Aerospace - Defense
Zacks Industry Rank	Bottom 32% (171 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-1.2%
Last Sales Surprise	-5.8%
EPS F1 Est- 4 week change	-11.3%
Expected Report Date	07/22/2020
Earnings ESP	-8.1%
P/E TTM	11.0
P/E F1	11.3
PEG F1	1.3
P/S TTM	1.0

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	9,916 E	10,344 E	10,614 E	11,744 E	40,765 E
2020	8,749 A	9,586 E	9,659 E	10,907 E	39,264 E
2019	9,261 A	9,555 A	9,761 A	10,773 A	39,350 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$2.87 E	\$3.15 E	\$3.62 E	\$4.16 E	\$12.57 E
2020	\$2.43 A	\$2.67 E	\$2.96 E	\$3.63 E	\$11.56 E
2019	\$2.56 A	\$2.77 A	\$3.14 A	\$3.51 A	\$11.98 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 04/30/2020. The reports text is as of 05/01/2020.

Overview

Headquartered in Falls Church, VA, **General Dynamics Corporation** engages in mission-critical information systems and technologies; land and expeditionary combat vehicles, armaments and munitions; shipbuilding and marine systems; and business aviation. The company was incorporated in February 1952.

Following CSRA acquisition, the company's Information Systems & Technology (IS&T) segment has been reorganized into Information Technology and Mission Systems segments. The company currently operates through five segments: **Aerospace, Combat Systems, Marine Systems, Mission Systems and Information Technology.**

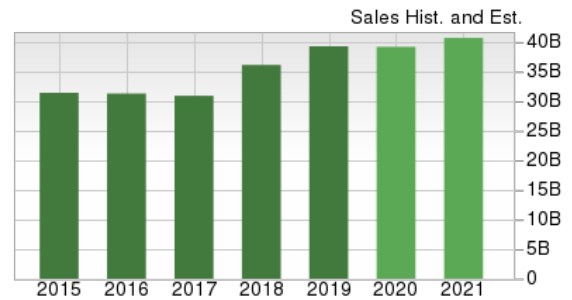
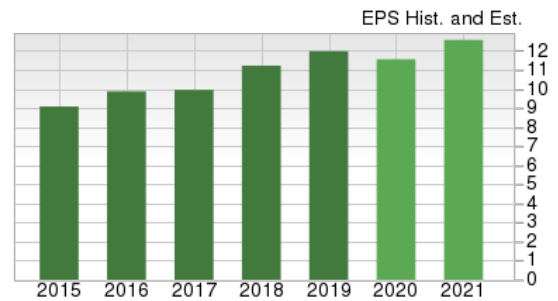
The **Aerospace** segment consists of Gulfstream Aerospace, which manufactures business jets, and Jet Aviation, which provides aircraft maintenance and spare parts. Segment revenues in 2019 summed \$9,801 million, representing 24.9% of the company's total revenues.

Combat Systems manufactures combat vehicles, medium-caliber guns, ammunition and ammunition handling systems. Revenues during 2019 came in at \$7,007 million, contributing 17.8% to the company's total revenues.

Mission Systems segment provides command, control and intelligence systems solutions. Revenues during 2019 came in at \$4,737 million, contributing 12.6% to the company's total revenues.

Marine Systems makes nuclear submarines, surface combatants and auxiliary ships. In 2019, revenues amounted to \$9,183 million, comprising 23.3% of the company's total revenues.

The **Information Technology** segment integrates secure communication systems and networks. Segment revenues in 2019 summed \$8,422 million, representing 21.4% of the company's total revenues.



Reasons To Buy:

- ▲ The company's short-term debt and current portion of long-term debt stands at \$5.05 billion, as of Mar 31, 2020, compared to \$2.92 billion, as of Dec 31, 2019. Meanwhile, the company's cash and cash equivalents were \$5.33 billion at the end of the first quarter, which is higher than its current debt level, indicating strong solvency. Additionally, General Dynamics has a current ratio of 1.34, as of Mar 31, 2020, compared to 1.18, as of Dec 31, 2019. This improved current ratio, which being more than 1, indicates this shipbuilder's ability to pay off its short-term obligations.

Further, the company's times interest earned ratio has improved sequentially. It came in at 10.2 at end of first-quarter 2020, up from the previous quarter's 10.1. The improvement in this ratio indicates that the firm will be able to meet debt obligations in the near future without any difficulties. At a time when every entity is looking forward to preserve liquidity amid uncertainties concerning the COVID-19 outbreak, improving times interest earned and current ratio are reassuring for General Dynamics' investors. Consequently, the company outperformed its industry in terms of share price performance. Notably, General Dynamics' share price has lost 25.2% in the past year compared with the industry's decline of 29.5%.

- ▲ During the first quarter of 2020, General Dynamics witnessed strong order growth, which was in line with its usual trend. This, in turn, boosted its backlog, which grew 23.9% year over year to \$85.7 billion. The estimated contract value, which combines total backlog with estimated potential contract value, was \$123.9 billion at the end of the first quarter. As a result of these order flows, the company's Aerospace unit reflected a book-to-bill ratio of 1.1 to 1, while the Information Technology Unit enhanced its backlog in the quarter with a book-to-bill ratio of 1.2 to 1. Notably, significant order intakes, particularly in the Aerospace and Information Technology segments, position the company well for 2020 and beyond. Such impressive book-to-bill ratio indicates solid demand for the company's products, thereby bolstering its revenue generation prospects significantly.
- ▲ In the fourth quarter of 2019, General Dynamics' Gulfstream G500 received certification approval from the European Aviation Safety Agency, clearing the way for European Union registrations and customer deliveries. As a result, the company successfully delivered its Gulfstream G500 to its first European customer in Georgia. In October 2019, General Dynamics introduced its flagship aircraft in the business jet industry, the Gulfstream G700, which completed its first flight in February 2020, demonstrating the program's maturity and officially launching its official flight-test program. This ultra-long-range jet is expected to commence service in 2022. Notably, such product innovation along with major certification approvals is projected to enhance this shipbuilder's footprint in the business jet market, going ahead.

General Dynamics' focus on product innovations should help maintain a steady growth momentum and drive results in the quarters ahead. Positive budgetary amendments also boost growth

Reasons To Sell:

- ▼ It is already a known fact that General Dynamics boasts a strong position in the U.S. defense space and overseas. However, the fiscal 2021 defense budget proposes to slash its shipbuilding investments by \$4 billion, as the U.S. Navy plans on securing fewer ships and submarines and direct more funding toward operations and research. The proposed spending provision includes eight ships, including three submarines, compared to the procurement for purchasing 11 new ships, including four submarines, in the previous year's budget. If approved, this might hamper growth of the company's shipbuilding business in the near term.
- ▼ Although the COVID-19 pandemic did not have a material impact on General Dynamic's operating results or business in the first quarter of 2020, its ongoing and prolonged impacts may be a cause of concern and might dent its second-quarter performance. This could be because the pandemic might have an adverse impact on the company's existing and planned operations, distribution systems and thus, increase overall expenses. Within the company's Aerospace segment, quarantine and travel restrictions in connection with the outbreak have already delayed aircraft deliveries and impacted some supply chain providers. Since the pandemic is unlikely to die out anytime soon, it might turn out to be a major growth inhibitor for this stock, going ahead.
- ▼ General Dynamics faces intense competition for its broad portfolio of products and services, both in the domestic front as well as the global market. Particularly, it faces competitive threat from various smaller competitors, particularly in some of its services businesses. Moreover, information technology procurements are increasingly focusing on price over other competitive factors.

Delayed payments from a large program is hurting General Dynamics' cash flow. Rising interest expenses are likely to hurt the company's growth prospects.

Last Earnings Report

General Dynamics Q1 Earnings & Revenues Miss Estimates

General Dynamics Corporation reported first-quarter 2020 earnings from continuing operations of \$2.43 per share, which missed the Zacks Consensus Estimate of \$2.46 by 1.2%. Moreover, earnings declined 5.1% from \$2.56 in the year-ago quarter.

Total Revenues

General Dynamics' first-quarter revenues of \$8,749 million missed the Zacks Consensus Estimate of \$9,284 million by 5.8%. Further, revenues declined 5.5% from \$9,261 million in the year-ago quarter. The decline was primarily attributable to lower sales from the Aerospace segment on a year-over-year basis.

Backlog

The company recorded a total backlog of \$85.7 billion, up 23.9% year over year. Funded backlog at the quarter-end was \$47.6 billion.

Segment Performance

Aerospace: The segment reported revenues of \$1,691 million, down 24.5% year over year. Operating earnings of \$240 million also declined 26.8% from the prior-year quarter's \$328 million.

Combat Systems: Segment revenues rose 4.4% to \$1,708 million. Moreover, operating earnings were up 8.3% to \$223 million in the quarter.

Information Systems and Technology: The segment reported revenues of \$1,988 million, which decreased 8.3% year over year. Operating earnings also declined 3.8% to \$150 million.

Marine Systems: The segment's revenues of \$2,246 million grew 9.1% from the year-ago quarter's \$2,058 million. Moreover, operating earnings rose 2.2% to \$184 million.

Mission Systems: The segment's revenues of \$1,116 million declined 3.6% from the year-ago quarter's \$1,158 million. Operating earnings remained flat at \$148 million on a year-over-year basis.

Operational Highlights

The operating margin contracted 10 basis points (bps) to 10.8% from the year-ago quarter's 10.9%.

In the quarter under review, General Dynamics' operating costs and expenses declined 5.3% to \$7,808 million.

The company repurchased 3.4 million of its outstanding shares in the first quarter of 2020. In March, the board of directors increased the quarterly dividend to \$1.10 per share. This 7.8% increase marked the company's 23rd consecutive annual dividend increase.

Financial Condition

As of Mar 31, 2020, General Dynamics' cash and cash equivalents were \$5,330 million compared with \$902 million as of Dec 31, 2019.

Long-term debt as of Mar 31, 2020, was \$12,951 million, which witnessed a rise from the 2019-end level of \$9,010 million.

As of Mar 31, 2020, the company's cash used by operating activities was \$666 million compared with \$795 million used in the year-ago period.

Free cash outflow from operations at the end of the first quarter of 2020 was \$851 million compared with \$976 million at the end of the first quarter of 2019.

Quarter Ending 03/2020

Report Date	Apr 29, 2020
Sales Surprise	-5.76%
EPS Surprise	-1.22%
Quarterly EPS	2.43
Annual EPS (TTM)	11.85

Recent News

On **April 9, 2020**, General Dynamics' Electric Boat division secured a \$55.9-million modification contract for manufacturing 18 missile tubes to support Columbia-class fleet ballistic missile submarines and the United Kingdom's Dreadnought-class submarines. The deal has been awarded by the Naval Sea Systems Command, Washington, D.C. Work related to the deal is scheduled to be completed by May 2028 and will be performed in Quonset Point, RI.

On **Mar 5, 2020**, General Dynamics announced that its board of directors has approved a 7.8% hike in its annual dividend. This has taken the annualized payout to \$4.40 per share. Notably, the revised quarterly dividend of \$1.10 per share will be paid out on May 8 2020, to stockholders on record as of Apr 10.

On **Feb 11, 2020**, General Dynamics Mission Systems announced it was awarded a contract for the Army Consolidated Product Line Management Plus (CPM Plus) Program from the Army Contracting Command in Orlando, Florida. CPM Plus is an eight year, single-award, indefinite-delivery, indefinite-quantity, cost-plus fixed-fee/firm-fixed price contract with a ceiling of \$883 million.

On **Jan 3, 2020**, General Dynamics Corp.'s business subsidiary, National Steel and Shipbuilding Co. (NASSCO), secured a \$98-million contract to execute docking phased maintenance availability for fiscal 2020. The deal was awarded by the Naval Sea Systems Command, Washington, DC.

Per the terms, General Dynamics' NASSCO unit will maintain, modernize and repair USS Harpers Ferry (LSD 49) and also provide the required facilities and human resources for the completion of the work. Work related to the deal is expected to get completed by December 2020 and will be performed in San Diego, CA.

Valuation

General Dynamics' shares are down 26% in the year-to-date period and down 25.2% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Aerospace sector are down 26.5% and 31.2% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry is down 29.5% whereas the sector is down 30.5%.

The S&P 500 index is down 8.9% in the year-to-date period and up 0.5% in the past year.

The stock is currently trading at 10.8X forward 12-month earnings, which compares to 19.1X for the Zacks sub-industry, 18.9X for the Zacks sector and 20.8X for the S&P 500 index.

Over the past five years, the stock has traded as high as 20.9X and as low as 8.3X, with a 5-year median of 15.3X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$138 price target reflects 11.5X earnings value.

The table below shows summary valuation data for GD

Valuation Multiples - GD					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	10.84	19.13	18.9	20.8
	5-Year High	20.91	22.54	20.94	20.8
	5-Year Low	8.25	14.52	14.17	15.19
	5-Year Median	15.32	17.19	17.06	17.44
P/S F12M	Current	0.94	1.26	1.1	3.3
	5-Year High	2.05	1.64	1.49	3.44
	5-Year Low	0.76	0.95	0.92	2.54
	5-Year Median	1.43	1.27	1.18	3.01
EV/EBITDA TTM	Current	9.29	13.84	10.32	10.66
	5-Year High	14.81	19.53	14.99	12.87
	5-Year Low	7.65	8.12	7.39	8.27
	5-Year Median	11.86	11.7	10.42	10.78

As of 04/30/2020

Industry Analysis Zacks Industry Rank: Bottom 32% (171 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
The Boeing Company (BA)	Neutral	3
Embraer-Empresa Brasileira de Aeronautica (ERJ)	Neutral	4
Huntington Ingalls Industries, Inc. (HII)	Neutral	3
Leidos Holdings, Inc. (LDOS)	Neutral	3
L3Harris Technologies Inc (LHX)	Neutral	3
Lockheed Martin Corporation (LMT)	Neutral	3
Northrop Grumman Corporation (NOC)	Neutral	3
Textron Inc. (TXT)	Underperform	5

Industry Comparison Industry: Aerospace - Defense				Industry Peers		
	GD	X Industry	S&P 500	LDOS	LMT	NOC
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	3	3	3
VGM Score	B	-	-	B	A	A
Market Cap	37.47 B	7.79 B	20.61 B	14.02 B	109.11 B	55.12 B
# of Analysts	8	5	14	8	8	7
Dividend Yield	3.37%	0.84%	2.11%	1.38%	2.47%	1.60%
Value Score	A	-	-	C	C	C
Cash/Price	0.02	0.08	0.06	0.05	0.02	0.04
EV/EBITDA	8.30	8.78	11.87	13.34	13.05	16.35
PEG Ratio	1.24	2.05	2.47	1.83	2.34	NA
Price/Book (P/B)	2.79	2.79	2.67	4.09	31.29	6.29
Price/Cash Flow (P/CF)	8.77	9.33	10.66	14.06	14.79	11.99
P/E (F1)	11.04	16.20	19.01	17.99	16.20	14.59
Price/Sales (P/S)	0.96	0.88	2.10	1.26	1.78	1.61
Earnings Yield	8.85%	5.56%	5.05%	5.56%	6.17%	6.85%
Debt/Equity	0.66	0.71	0.72	0.95	3.28	1.60
Cash Flow (\$/share)	14.89	2.73	7.01	7.03	26.30	27.58
Growth Score	C	-	-	A	A	A
Hist. EPS Growth (3-5 yrs)	7.05%	13.39%	10.88%	14.53%	17.30%	23.28%
Proj. EPS Growth (F1/F0)	-3.55%	8.57%	-7.32%	6.24%	9.41%	6.85%
Curr. Cash Flow Growth	3.16%	6.19%	5.92%	6.19%	18.08%	2.21%
Hist. Cash Flow Growth (3-5 yrs)	6.36%	6.62%	8.55%	6.45%	9.70%	14.43%
Current Ratio	1.18	1.20	1.23	1.21	1.23	1.13
Debt/Capital	39.89%	42.81%	43.84%	48.76%	76.64%	61.48%
Net Margin	8.87%	6.01%	11.08%	6.01%	10.21%	6.57%
Return on Equity	25.86%	16.06%	16.44%	22.51%	185.10%	39.02%
Sales/Assets	0.80	0.85	0.54	1.18	1.26	0.85
Proj. Sales Growth (F1/F0)	-0.81%	0.00%	-1.42%	14.40%	6.18%	5.29%
Momentum Score	C	-	-	B	B	C
Daily Price Chg	-4.41%	-2.13%	-2.39%	-4.03%	0.30%	-0.35%
1 Week Price Chg	-6.43%	-6.14%	-1.74%	2.69%	-4.92%	-4.77%
4 Week Price Chg	2.11%	8.82%	17.07%	11.49%	9.92%	5.21%
12 Week Price Chg	-29.82%	-27.63%	-18.53%	-10.14%	-11.37%	-9.09%
52 Week Price Chg	-25.18%	-26.01%	-9.82%	35.10%	16.99%	14.05%
20 Day Average Volume	1,954,554	1,004,916	2,641,413	1,129,011	1,491,163	880,820
(F1) EPS Est 1 week change	-6.96%	0.00%	0.00%	0.00%	0.26%	-3.62%
(F1) EPS Est 4 week change	-11.26%	-3.96%	-6.62%	-2.33%	-0.44%	-3.90%
(F1) EPS Est 12 week change	-13.76%	-13.76%	-13.28%	0.78%	-0.60%	-4.29%
(Q1) EPS Est Mthly Chg	-6.10%	-3.81%	-11.97%	-5.14%	-2.17%	-2.47%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	A
Growth Score	C
Momentum Score	C
VGM Score	B

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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