

General Dynamics Corp. (GD)

\$165.03 (As of 03/02/20)

Price Target (6-12 Months): **\$175.00**

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:A

Value: B

Growth: B

Momentum: B

Summary

General Dynamics 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. The budgetary amendments under the current U.S. administration tend to strongly favor the company's business line. Product innovation can be expected to expand its footprint in the business jet market. However, rising interest expenses can be a potential headwind for the company's bottom-line growth going ahead. Moreover, delayed payments related to one of its large international vehicle programs in Canada are hurting its cash flow reserve. A comparative analysis of its EV/Sales F12M ratio reflects a gloomy picture. Also, in the past year, shares of General Dynamics have underperformed the industry.

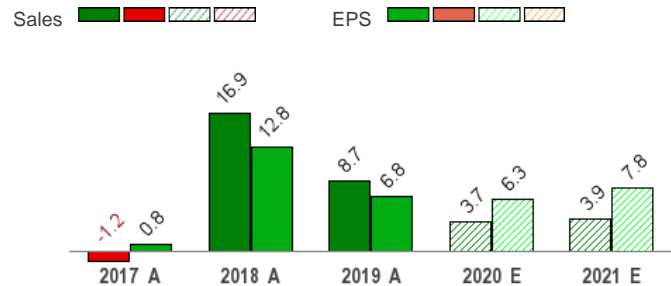
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$193.76 - \$155.47
20 Day Average Volume (sh)	1,730,862
Market Cap	\$47.8 B
YTD Price Change	-6.4%
Beta	1.15
Dividend / Div Yld	\$4.08 / 2.5%
Industry	Aerospace - Defense
Zacks Industry Rank	Bottom 30% (179 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	1.5%
Last Sales Surprise	1.6%
EPS F1 Est- 4 week change	0.5%
Expected Report Date	04/22/2020
Earnings ESP	-0.8%
P/E TTM	13.8
P/E F1	13.0
PEG F1	1.5
P/S TTM	1.2

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	9,916 E	10,344 E	10,614 E	11,744 E	42,364 E
2020	9,524 E	10,117 E	10,128 E	10,957 E	40,792 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	\$13.73 E
2020	\$2.65 E	\$3.02 E	\$3.22 E	\$3.73 E	\$12.74 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 03/02/2020. The reports text is as of 03/03/2020.

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.**

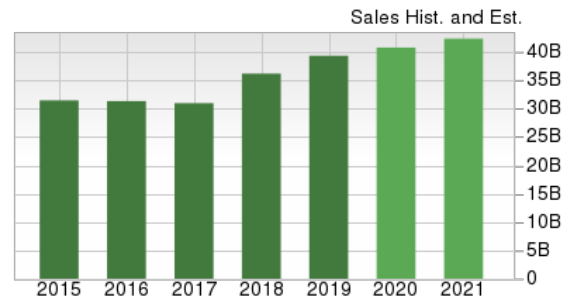
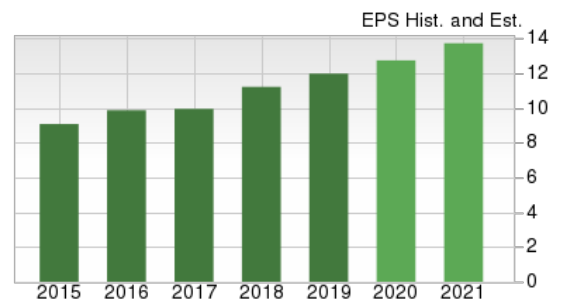
The **Aerospace** segment consists of Gulfstream Aerospace, which manufactures business jets, and Jet Aviation, which provides aircraft maintenance and spare parts. Segment revenues in 2019 summed \$9,801 million, representing 24.9% of the company's total revenues.

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:

▲ General Dynamics boasts a strong position in the U.S. defense space and overseas. The budgetary amendments under the current U.S. administration tend to strongly favor the company's business line. Notably, the proposed fiscal 2020 defense budget includes a spending provision of \$205.6 billion for the U.S. Navy, approximately 6% higher than the previous fiscal budget allotment. It includes the procurement for purchasing 11 new ships, including four submarines. General Dynamics, being one of the two contractors in the world equipped to build nuclear-powered submarines and one of the prime U.S. shipbuilders, should certainly benefit from this increased budget proposal, if approved.

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

▲ During the fourth quarter of 2019, General Dynamics witnessed strong order growth, which was in line with its usual trend. This, in turn, boosted its backlog, which grew 28.1%, year over year, to record-high \$86.9 billion. The estimated contract value, at the end of the third quarter, was \$35.64 billion, up 2.7% year over year. As a result of these order flows, the company's Aerospace unit reflected a book-to-bill ratio of 1.7 to 1, while the Marine Systems Unit enhanced its backlog in the quarter with a book-to-bill of 8.1 to 1. Notably, significant order intakes, particularly in aerospace and marine, 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.

▲ From the context of product development, General Dynamics' G600 aircraft received both type and production certification from the U.S. Federal Aviation Administration (FAA) toward the end of June 2019. Additionally, in the fourth quarter, 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. Notably, such product innovation along with the major certification approvals is projected to enhance this shipbuilder's footprint in the business jet market, going ahead.

Reasons To Sell:

- ▼ General Dynamics' interest expenses rose 29.2% year over year to \$460 million during 2019. Interestingly, the company has been witnessing an upward trend in its interest expenses over the last few years. Interest expenses witnessed a massive surge of 245.6% at the end of 2018 and a rise of 13.2% at the end of 2017. The increase in interest expenses reflects a full year of financing for the CSRA acquisition and additional commercial paper issuances. Such rising expenses can be a potential headwind for the company's bottom-line growth, going ahead. This might have discouraged investors' interest in this stock. Evidently, General Dynamics' share price has declined 1.1% in the past year compared with the industry's decline of 11.6%.

Delayed payments from a large program is hurting General Dynamics' cash flow. Rising interest expenses are likely to hurt the company's growth prospects.
 - ▼ A comparative analysis of its forward 12-month Enterprise Value/Sales (EV/Sales F12M) ratio reflects a relatively gloomy picture that might be a cause for investors' concern. General Dynamics currently has a forward 12-month EV/Sales F12M ratio of 1.4. Moreover, the company's EV/Sales F12M is higher than that of its industry's 1.37, reflecting the stock to be an overvalued one.
 - ▼ General Dynamics is carrying more commercial paper than anticipated due to delayed payments related to one of its large international vehicle programs in Canada, which is outstanding since the fourth quarter of the last year. Such payment delays affected the company's cash flow from operations. Evidently, the company witnessed a cash inflow of \$2,981 million as of Dec 31, 2019, compared to the cash inflow of \$3,148 million in the comparable year-ago period. If such payment delays persist, the General Dynamics' cash flow balance may consistently remain under pressure. This, in turn, might reduce the company's ability to reward its shareholders through dividend hikes and share repurchase programs.
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Last Earnings Report

General Dynamics Q4 Earnings Top Estimates, Sales Up Y/Y

General Dynamics Corporation reported fourth quarter and 2019 results. Fourth-quarter earnings from continuing operations of \$3.51 per share beat the Zacks Consensus Estimate of \$3.46 by 1.45%. Earnings were up 14.3% from \$3.07 in the year-ago quarter.

For 2019, earnings were \$11.98 per share, up 6.8% from \$11.22 in the year-ago quarter. Moreover, full-year earnings exceeded the Zacks Consensus Estimate of \$11.92 by 0.5%.

Quarter Ending **12/2019**

Report Date	Jan 29, 2020
Sales Surprise	1.61%
EPS Surprise	1.45%
Quarterly EPS	3.51
Annual EPS (TTM)	11.98

Total Revenues

General Dynamics' fourth-quarter revenues of \$10,773 million surpassed the Zacks Consensus Estimate of \$10,602 million by 1.6%. Further, revenues increased 3.8% from \$10,378 million in the year-ago quarter. Revenues grew year over year in four of the company's five segments.

In 2019, total revenues increased 8.7% year over year to \$39.35 billion. Full-year revenues surpassed the Zacks Consensus Estimate of \$39.19 billion by 0.4%.

Backlog

The company recorded a total backlog of \$86.95 billion, up 28.1% year over year. Funded backlog at the quarter-end was \$57.53 billion.

Segment Performance

Aerospace: The segment reported revenues of \$2,930 million, up 8.4% year over year. Operating earnings of \$480 million increased 25.7% from the prior-year quarter's \$382 million.

Combat Systems: Segment revenues increased 13.1% to \$1,972 million. Operating earnings were up 8.8% to \$284 million in the quarter.

Information Systems and Technology: The segment reported revenues of \$2,024 million, which fell 15% year over year. Operating income also declined 11.3% to \$172 million.

Marine Systems: The segment's revenues of \$2,565 million were up 11.7% from the year-ago quarter's \$2,297 million. However, operating income declined 6.6% year over year to \$199 million.

Mission Systems: The segment's revenues of \$1,282 million were up 2.5% from the year-ago quarter's \$1,251 million. Operating income grew 3.9% to \$188 million from the year-ago quarter's \$181 million.

Operational Highlights

Company-wide operating margin expanded 50 basis points (bps) to 12.3% from the year-ago quarter's 11.8%.

In the quarter under review, General Dynamics' operating costs and expenses rose 3.2% to \$9,445 million.

The company paid out \$1,152 million in dividends in 2019 compared with \$1,075 million in 2018.

Financial Condition

As of Dec 31, 2019, General Dynamics' cash and cash equivalents were \$902 million compared with \$963 million as of Dec 31, 2018.

Long-term debt as of Dec 31 was \$9,010 million compared with the 2018-end level of \$11,444 million.

As of Dec 31, the company's cash provided by operating activities was \$2,981 million compared with \$3,148 million in the year-ago period.

Free cash flow from operations at the end of the fourth quarter was \$2,013 million compared with \$1,824 million in the year-ago period.

Recent News

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 13.5% in the past six months period and down 1.1% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Aerospace sector are down 13.7% and 11% in the past six months period, respectively. Over the past year, the Zacks sub-industry is down 11.6% whereas the sector is down 6.9%.

The S&P 500 index is up 1% in the past six months period and up 4.9% in the past year.

The stock is currently trading at 12.8X forward 12-month earnings, which compares to 19.2X for the Zacks sub-industry, 18.4X for the Zacks sector and 16.9X for the S&P 500 index.

Over the past five years, the stock has traded as high as 20.9X and as low as 12.3X, with a 5-year median of 15.5X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$175 price target reflects 13.5X 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	12.75	19.17	18.4	16.87
	5-Year High	20.91	22.54	21.54	19.34
	5-Year Low	12.26	14.52	14.26	15.18
	5-Year Median	15.51	17.14	16.9	17.44
P/S F12M	Current	1.16	1.35	1.18	3.12
	5-Year High	2.05	1.64	1.39	3.43
	5-Year Low	1.12	0.95	0.8	2.54
	5-Year Median	1.44	1.27	1.09	3.01
P/B TTM	Current	3.52	30.51	13.96	3.96
	5-Year High	5.97	36.57	16.72	4.54
	5-Year Low	3.41	7.33	5.26	2.85
	5-Year Median	4.22	14.44	9.21	3.62

As of 03/02/2020

Industry Analysis Zacks Industry Rank: Bottom 30% (179 out of 255)



Top Peers

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

Industry Comparison Industry: Aerospace - Defense				Industry Peers		
	GD Neutral	X Industry	S&P 500	LDOS Outperform	LMT Neutral	NOC Neutral
VGM Score	A	-	-	B	C	A
Market Cap	47.80 B	12.41 B	22.14 B	15.56 B	107.52 B	56.32 B
# of Analysts	8	4.5	13	6	9	7
Dividend Yield	2.47%	1.05%	1.98%	1.24%	2.52%	1.57%
Value Score	B	-	-	C	C	B
Cash/Price	0.02	0.04	0.05	0.05	0.01	0.04
EV/EBITDA	10.18	12.53	12.79	14.59	12.93	16.65
PEG Ratio	1.46	2.18	1.92	2.61	2.29	NA
Price/Book (P/B)	3.52	3.89	3.00	4.56	33.92	6.39
Price/Cash Flow (P/CF)	11.08	14.47	11.97	15.66	14.50	12.18
P/E (F1)	12.95	16.61	17.43	19.59	15.79	14.49
Price/Sales (P/S)	1.21	1.20	2.48	1.40	1.80	1.66
Earnings Yield	7.72%	5.74%	5.74%	5.11%	6.33%	6.90%
Debt/Equity	0.66	0.66	0.70	0.95	3.60	1.60
Cash Flow (\$/share)	14.89	2.18	6.94	7.03	26.30	27.58
Growth Score	B	-	-	A	C	A
Hist. EPS Growth (3-5 yrs)	7.05%	13.39%	10.85%	14.53%	16.29%	23.28%
Proj. EPS Growth (F1/F0)	6.38%	13.18%	6.48%	8.67%	10.04%	9.35%
Curr. Cash Flow Growth	3.16%	3.16%	6.03%	6.19%	18.08%	2.21%
Hist. Cash Flow Growth (3-5 yrs)	6.36%	6.40%	8.52%	6.45%	9.70%	14.43%
Current Ratio	1.18	1.21	1.23	1.21	1.22	1.13
Debt/Capital	39.89%	43.17%	42.57%	48.76%	78.24%	61.48%
Net Margin	8.85%	6.01%	11.57%	6.01%	10.42%	6.64%
Return on Equity	26.70%	16.94%	16.66%	22.51%	198.95%	39.51%
Sales/Assets	0.81	0.92	0.54	1.18	1.24	0.84
Proj. Sales Growth (F1/F0)	3.66%	4.84%	4.07%	14.01%	6.11%	5.46%
Momentum Score	B	-	-	B	B	C
Daily Price Chg	3.34%	2.18%	3.82%	7.22%	3.10%	2.17%
1 Week Price Chg	-14.88%	-14.08%	-12.06%	-12.43%	-13.54%	-9.91%
4 Week Price Chg	-6.56%	-9.15%	-6.43%	7.42%	-10.03%	-7.63%
12 Week Price Chg	-9.90%	-9.54%	-5.15%	22.15%	-0.52%	-2.06%
52 Week Price Chg	-1.03%	1.67%	4.77%	71.70%	25.16%	18.68%
20 Day Average Volume	1,730,862	667,163	2,363,047	1,158,332	1,264,682	1,040,885
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.15%	0.00%	0.00%
(F1) EPS Est 4 week change	0.48%	0.00%	-0.04%	3.09%	-0.02%	-0.23%
(F1) EPS Est 12 week change	-1.50%	0.00%	-0.33%	4.30%	-0.44%	0.67%
(Q1) EPS Est Mthly Chg	-0.81%	-1.20%	-0.38%	-1.59%	-2.05%	1.06%

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	B
Growth Score	B
Momentum Score	B
VGM Score	A

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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