

Huntington Ingalls(HII)

\$195.29 (As of 03/26/20)

Price Target (6-12 Months): **\$207.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 01/27/20)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

2-Buy

Zacks Style Scores:

VGM:A

Value: A

Growth: B

Momentum: B

Summary

Huntington Ingalls is the sole designer and manufacturer of nuclear-powered aircraft carriers in the United States. Furthermore, over 70% of the active U.S. Navy fleet consists of Huntington Ingalls ships. Being the nation's largest military shipbuilder, it boasts stable financials. The shipbuilding business outlook remains strong, given the fiscal 2020 defense budget, which in turn is benefitting this stock. Its shares have outperformed the industry in a year. However, its exposure to debt combined with its ability to incur significant amounts of debt in the future increases its vulnerability to adverse economic or industry conditions. Additionally, reduced fleet size poses a threat to its growth potential. Consequently, fewer contracts are awarded to the same fixed number of shipyards, which has resulted in work reduction in the industry.

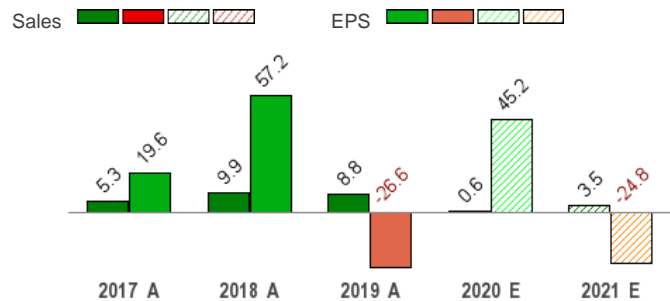
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$279.71 - \$147.14
20 Day Average Volume (sh)	580,550
Market Cap	\$8.0 B
YTD Price Change	-22.2%
Beta	1.29
Dividend / Div Yld	\$4.12 / 2.1%
Industry	Aerospace - Defense
Zacks Industry Rank	Top 35% (89 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	2.8%
Last Sales Surprise	3.1%
EPS F1 Est- 4 week change	1.6%
Expected Report Date	05/07/2020
Earnings ESP	0.0%
P/E TTM	13.9
P/E F1	9.6
PEG F1	NA
P/S TTM	0.9

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					9,265 E
2020	2,113 E	2,199 E	2,227 E	2,417 E	8,956 E
2019	2,080 A	2,188 A	2,219 A	2,412 A	8,899 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021					\$15.30 E
2020	\$4.46 E	\$4.79 E	\$4.97 E	\$6.54 E	\$20.34 E
2019	\$2.85 A	\$3.07 A	\$3.74 A	\$4.36 A	\$14.01 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 03/26/2020. The reports text is as of 03/27/2020.

Overview

Based in Newport News, VA, **Huntington Ingalls Industries** designs, builds and maintains nuclear-powered ships such as aircraft carriers and submarines, and non-nuclear ships, such as surface combatants, expeditionary warfare/amphibious assault and coastal defense surface ships for the U.S. Navy and Coast Guard and provides after-market services for military ships around the globe.

Currently, Huntington Ingalls operates through three segments: Ingalls, Newport News and Technical Solutions.

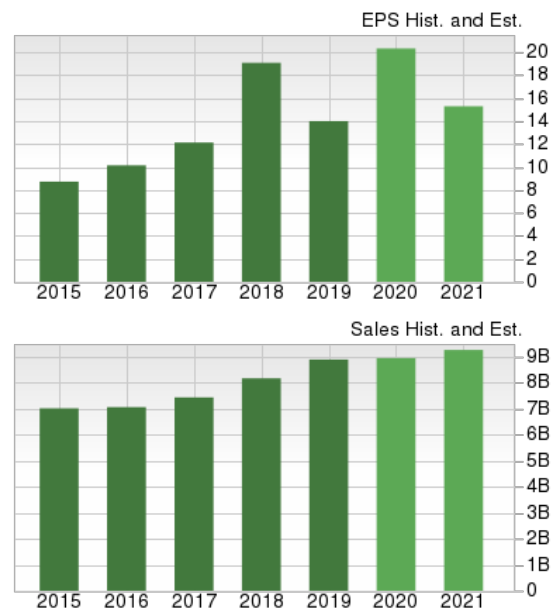
Ingalls – The segment manufactures amphibious assault and expeditionary ships for the U.S. Navy. The division is the only builder of National Security Cutters ("NSCs") for the U.S. Coast Guard and one of only two companies that builds the Navy's current fleet of DDG-51 Arleigh Burke -class destroyers. It generated revenues of \$2,555 million in 2019, representing 28.2% of total revenues.

Through its **Newport News** segment, the company is the nation's sole designer, builder and refueler of nuclear-powered aircraft carriers. It is also one of only two companies currently designing and building nuclear-powered submarines for the U.S. Navy. The segment generated revenues of \$5,186 million in 2019, representing 57.3% of total revenues.

The **Technical Solutions** segment provides a wide range of professional services through its fleet support, integrated missions solutions, nuclear and environmental, and oil and gas operations. It generated revenues of \$1,309 million in the 2019, representing 14.5% of total revenues.

Total revenues included intersegment eliminations worth \$151 million.

As of Dec 31, 2019, the company's total backlog was \$46.5 billion, significantly higher than \$23 billion at 2018 end.



Reasons To Buy:

▲ **Largest U.S. Military Shipbuilder & Recent Uptick:** The company is the prime industrial employer in Virginia. It is the sole designer and manufacturer of nuclear-powered aircraft carriers in the U.S. Over 70% of the active U.S. Navy fleet consists of Huntington Ingalls ships. Notably, Huntington Ingalls ended the fourth quarter on a solid note, generating revenues worth \$2.41 billion that reflected a year-over-year improvement of 9.7%. The growth was led by higher sales volume at all three business divisions. Coming to the quarterly updates, the company's CVN 79 Kennedy was launched in December 2019 and has successfully transitioned into its final assembly and test activities. Its CVN 73 USS George Washington has also transitioned into its final outfitting and test phase. Moreover, the refueling and complex overhaul is approximately 68% complete and the ship is scheduled for redelivery to the Navy in late 2021. At the Ingalls division, LHA 7 Tripoli is essentially complete and the team is working on its delivery in the next few weeks. LPD-28 Fort Lauderdale is approximately 70% complete and is on track for launch in the first half of 2020.

The company is the largest player of the nation's shipbuilding industry. Its stable financials, return of cash to shareholders and solid budget outlook are added positives.

On the submarine program, Huntington Ingalls' SSN 794 Montana achieved the pressure hull complete milestone in December and remains on track to deliver in the first half of 2021. SSN 796 New Jersey is on track to achieve the pressure hull complete milestone in late 2020. On successful completion, such notable programs should boost the company's top line.

▲ **Positive Budget & Backlog:** The shipbuilding business outlook remains strong, given the fiscal 2020 defense budget that represented the biggest budget request in more than 20 years for shipbuilding. The defense budget includes a solid spending plan worth \$34.7 billion on shipbuilding. No doubt, one of the prime beneficiaries of this new spending proposal will be Huntington Ingalls. For more than 100 years, this company has been building ships, aircraft carriers and submarines for the U.S. Navy at their shipyards in Virginia and Mississippi. Additionally, the fiscal 2020 budget includes funding worth \$2.2 billion for Columbia Class Submarine and \$2.6 billion for CVN-78.

The value of new contract awards at the end of fourth-quarter 2019 was approximately \$32.3 billion, which resulted in total backlog of \$46.5 billion as of Dec 31, 2019. Such significant backlog count indicates solid revenue growth for the company.

▲ **Stable Financials:** Huntington Ingalls maintains stable liquidity and capital resources to fund its operations. This in turn must have allowed Huntington Ingalls to be on with its schedule to invest \$1.8-\$1.9 billion in its shipyards, increase its dividend at least 10% annually through 2020 and utilize share buybacks to return all free cash flow to its shareholders from 2016 through 2020. Keeping up with this trend, the company raised its dividend by 19.7% to \$1.03 as well as its share repurchase program from \$2.2 billion to \$3.2 billion alongside an extension of the term of the program to October 31, 2024, in November 2019. This reflects Huntington Ingalls' solid cash generating capacity. Moreover, in 2019, the company returned \$262 million through share repurchases and paid out cash dividends worth \$149 million to its investors, as the company focuses on maximizing shareholder value.

Such solid financial position may have boosted investors' confidence in this stock. As a result, Huntington Ingalls outperformed the industry in a year's time. Shares of the company have lost 4.8% compared with the industry's 31.2% decline.

Reasons To Sell:

- ▼ **Reduced Fleet Size:** Given uncertain and unpredictable U.S. defense spending levels, any reduction in shipbuilding activity by the U.S. Navy will result in fewer contracts to the same fixed number of shipyards. Notably, the fleet size has been reduced from 566 ships in 1989 to 293 ships as of Dec 31, 2019. Consequently, fewer contracts are awarded to the same fixed number of shipyards, which has resulted in workforce reduction in the industry. Obviously, this is not an encouraging scenario for shipbuilders like Huntington Ingalls.
- ▼ **Intense Competition:** In its primary business of designing, building, overhauling, and repairing military ships, the company primarily competes with General Dynamics Corp. Among the six major private U.S. shipyards, Huntington Ingalls owns three while there are numerous smaller private shipyards that compete for contracts. Again, Huntington Ingalls' products, such as aircraft carriers, submarines, amphibious assault ships, surface combatants, and other ships, compete for funding with each other, as well as with other defense products and services. More competitive pressure is brewing up for future shipbuilding programs that might have a negative impact on the company's profit.
- ▼ **Exposure to Debt:** As of Dec 31, 2019, Huntington Ingalls had \$1.29 billion of debt, slightly higher than the figure at the end of 2018. Such rising debt levels, combined with the company's ability to incur significant amounts of debt in the future, increases its vulnerability to adverse economic or industry conditions. Moreover, it will require the company to dedicate a portion of its cash flow from operations to repayments of debt, thereby reducing the availability of cash flow to fund working capital, capital expenditures as well as strategic initiatives. In fact, such high debt levels may have pushed the debt-to-equity ratio for the company and kept it higher than that of the broader market. Notably, the company's current debt-to-equity ratio stands at 91.31, while that of the S&P 500 Index stands at 91. This might remain a concern for those investing in this stock.

Competitive pressure and extensive exposure to debt may hurt Huntington Ingalls' profit.

Last Earnings Report

Huntington Ingalls Q4 Earnings Top, Revenues Up Y/Y

Huntington Ingalls Industries, Inc.'s fourth-quarter 2019 earnings of \$4.36 per share surpassed the Zacks Consensus Estimate of \$4.24 by 2.83%. However, the reported figure declined 11.7% from \$4.94, reported a year ago.

For 2019, the company reported earnings of \$14.09 per share, which outpaced the Zacks Consensus Estimate of \$13.87 by 1.6%. However, the bottom line declined 26.6% from \$19.09 registered a year ago.

Quarter Ending **12/2019**

Report Date	Feb 13, 2020
Sales Surprise	3.10%
EPS Surprise	2.83%
Quarterly EPS	4.36
Annual EPS (TTM)	14.02

Total Revenues

Total revenues came in at \$2,412 million exceeding the Zacks Consensus Estimate of \$2,339 million by 3.1%. The top line also rose 9.7% from \$2,199 million registered in the year-ago quarter. The upside can be attributed to higher sales volume at all the three business divisions of the company.

In 2019, the company generated revenues of \$8,899 million, which once again outpaced the Zacks Consensus Estimate of \$8,830 million by 0.8% and also improved 8.8% from \$8,176 million registered in the prior year.

Segment Details

Newport News Shipbuilding: Revenues totaled \$1,390 million at this segment, up 8.8% year over year backed by higher revenues in submarine construction. Meanwhile, operating income surged 133.3% to \$133 million due to award of the VCS Block V contract, as well as contract changes for support services on Los Angeles-class submarines.

Ingalls Shipbuilding: Revenues at this segment came in at \$702 million, up 0.4% year over year, due to higher revenues on the San Antonio-class LPD program and Legend-class National Security Cutter (NSC) program. However, operating income declined 29.8% to \$59 million due to lower risk retirement on the LHA and LPD programs, as well as recoveries related to a 2018 settlement agreement.

Technical Solutions: Revenues at this segment summed \$369 million, up 38.2% year over year. The upside is primarily attributable to higher mission driven innovative solutions (MDIS) revenues as well as higher fleet support and oil and gas revenues. Operating loss amounted to \$19 million against the operating income of \$7 million in the year-ago quarter.

Backlog

Huntington Ingalls received new orders worth \$9.7 billion in the fourth quarter. As a result, the company's total backlog reached \$46.5 billion as of Dec 31, 2019.

Financial Update

Cash and cash equivalents as of Dec 31, 2019, were \$75 million, significantly down from \$240 million as of Dec 31, 2018.

Long-term debt, as of Dec 31, 2019, was \$1,286 million compared with the 2018-end level of \$1,283 million.

Cash from operating activities, at the end of 2019, grossed \$896 million compared with \$914 million at the end of 2018.

Recent News

On **Mar 27, 2020**, Huntington Ingalls announced that it has closed on the previously announced acquisition of Hydroid Inc., a leading provider of advanced marine robotics to the defense and maritime markets. In conjunction with the transaction, HII and Kongsberg Maritime have established a strategic alliance to jointly market naval and maritime products and services to the U.S. government market and potentially to global markets.

On **Feb 28, 2020**, Huntington Ingalls' Ingalls Shipbuilding division delivered amphibious assault ship Tripoli (LHA 7) to the U.S. Navy. Tripoli will be commissioned later this year before sailing to its homeport of San Diego, California.

When Tripoli enters the fleet, it will be the flagship of an Amphibious Ready Group, strategically positioning Marine Expeditionary Units ashore across a full spectrum of missions, including humanitarian, disaster relief, maritime security, antipiracy and other operations while providing air support for ground forces.

On **Feb 4, 2020**, Huntington Ingalls announced that it has entered into an agreement to acquire Hydroid Inc. a leading provider of advanced marine robotics to the defense and maritime markets and a U.S. based indirect subsidiary, wholly owned by Kongsberg Maritime. In conjunction with the transaction, Huntington and Kongsberg Maritime are also establishing a strategic alliance to jointly market naval and maritime products and services to the U.S. government market and potentially to global markets.

Valuation

Huntington Ingalls' shares are down 22.1% in the year to date period and down 4.8% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Aerospace sector are down 31.8% and 32.6% in the year to date period, respectively. Over the past year, the Zacks sub-industry is down 31.2% and the Zacks Aerospace sector witnessed a 28.3% decline.

The S&P 500 index is down 23% in the year to date period and down 12.8% in the past year.

The stock is currently trading at 10.2X forward 12-month earnings, which compares to 15.4X for the Zacks sub-industry, 14.6X for the Zacks sector and 14.9X for the S&P 500 index.

Over the past five years, the stock has traded as high as 21.3X and as low as 8.1X, with a 5-year median of 14.4X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$207 price target reflects 10.8X earnings value.

The table below shows summary valuation data for HII

Valuation Multiples - HII					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	10.2	15.41	14.62	14.92
	5-Year High	21.32	22.54	21.54	19.34
	5-Year Low	8.12	14.52	14.26	14.92
	5-Year Median	14.38	17.09	16.88	17.42
P/S F12M	Current	0.88	1.03	0.9	2.68
	5-Year High	1.6	1.64	1.39	3.43
	5-Year Low	0.71	0.95	0.8	2.54
	5-Year Median	1.11	1.26	1.09	3
EV/EBITDA TTM	Current	9.13	13.05	11.23	9.16
	5-Year High	12.76	19.47	16.89	12.88
	5-Year Low	5.33	8.12	7.15	8.27
	5-Year Median	9.04	11.64	10.05	10.78

As of 03/26/2020

Industry Analysis Zacks Industry Rank: Top 35% (89 out of 253)



Top Peers

Euronav NV (EURN)	Outperform
Leidos Holdings, Inc. (LDOS)	Outperform
Ardmore Shipping Corporation (ASC)	Neutral
Bae Systems PLC (BAESY)	Neutral
General Dynamics Corporation (GD)	Neutral
Lockheed Martin Corporation (LMT)	Neutral
Northrop Grumman Corporation (NOC)	Neutral
Hexcel Corporation (HXL)	Underperform

Industry Comparison Industry: Aerospace - Defense				Industry Peers		
	HII Neutral	X Industry	S&P 500	GD Neutral	LMT Neutral	NOC Neutral
VGM Score	A	-	-	A	C	A
Market Cap	7.95 B	8.83 B	18.50 B	38.57 B	98.69 B	53.84 B
# of Analysts	4	5	13	8	8	6
Dividend Yield	2.11%	0.82%	2.35%	3.06%	2.74%	1.64%
Value Score	A	-	-	B	D	B
Cash/Price	0.01	0.07	0.07	0.03	0.02	0.05
EV/EBITDA	9.22	8.71	11.16	8.50	11.95	16.04
PEG Ratio	NA	1.51	1.74	1.36	2.11	NA
Price/Book (P/B)	5.03	3.04	2.44	2.84	31.16	6.11
Price/Cash Flow (P/CF)	9.52	10.81	9.87	8.94	13.32	11.64
P/E (F1)	9.60	14.21	15.29	10.71	14.52	13.95
Price/Sales (P/S)	0.89	0.94	1.93	0.98	1.65	1.59
Earnings Yield	10.42%	6.49%	6.47%	9.33%	6.88%	7.17%
Debt/Equity	0.91	0.66	0.70	0.66	3.60	1.60
Cash Flow (\$/share)	20.51	2.33	7.01	14.89	26.30	27.58
Growth Score	B	-	-	B	C	A
Hist. EPS Growth (3-5 yrs)	19.95%	13.39%	10.85%	7.05%	16.29%	23.28%
Proj. EPS Growth (F1/F0)	45.18%	12.22%	2.89%	3.79%	9.89%	8.59%
Curr. Cash Flow Growth	-19.56%	4.55%	5.93%	3.16%	18.08%	2.21%
Hist. Cash Flow Growth (3-5 yrs)	6.79%	6.40%	8.55%	6.36%	9.70%	14.43%
Current Ratio	0.94	1.21	1.23	1.18	1.22	1.13
Debt/Capital	47.73%	43.17%	42.57%	39.89%	78.24%	61.48%
Net Margin	6.17%	6.01%	11.64%	8.85%	10.42%	6.64%
Return on Equity	35.78%	16.94%	16.74%	26.70%	198.95%	39.51%
Sales/Assets	1.25	0.84	0.54	0.81	1.24	0.84
Proj. Sales Growth (F1/F0)	0.64%	2.17%	2.37%	2.17%	6.64%	5.29%
Momentum Score	B	-	-	C	A	B
Daily Price Chg	10.06%	9.71%	6.21%	9.15%	9.59%	11.39%
1 Week Price Chg	-10.81%	-21.46%	-16.96%	-18.37%	-11.37%	-9.69%
4 Week Price Chg	-9.27%	-21.10%	-15.70%	-19.85%	-8.91%	-3.13%
12 Week Price Chg	-23.67%	-28.76%	-23.67%	-25.37%	-12.28%	-9.70%
52 Week Price Chg	-4.79%	-16.82%	-13.99%	-20.63%	18.51%	20.30%
20 Day Average Volume	580,550	1,597,169	4,286,768	3,188,321	2,828,017	1,701,585
(F1) EPS Est 1 week change	0.00%	0.00%	-0.15%	-2.31%	0.00%	-0.12%
(F1) EPS Est 4 week change	1.56%	-1.24%	-2.28%	-2.31%	-0.14%	-0.17%
(F1) EPS Est 12 week change	7.98%	-4.54%	-3.22%	-3.71%	-0.57%	0.11%
(Q1) EPS Est Mthly Chg	0.00%	0.02%	-1.60%	-0.82%	0.03%	0.42%

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	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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