

## Leidos Holdings, Inc. (LDOS)

**\$101.08** (As of 01/09/20)

Price Target (6-12 Months): **\$116.00**

Long Term: 6-12 Months

**Zacks Recommendation:**

**Outperform**

(Since: 10/16/19)

Prior Recommendation: Neutral

Short Term: 1-3 Months

**Zacks Rank:** (1-5)

**2-Buy**

Zacks Style Scores:

VGM:A

Value: B

Growth: A

Momentum: B

### Summary

Leidos Holdings has outperformed its industry in the past year. Increased contract wins from the Pentagon and other U.S. allies owing to its cost-effective defense solutions have been acting as a key catalyst for this defense major. In fact, these contract wins tend to bolster its backlog, thereby boosting its revenue growth prospects. With the current U.S. administration being in favor of increased defense spending, macroeconomic environment in the nation has been boosting the company's growth prospects. Leidos Holdings' strong balance sheet and a steady cash flow position offer it substantial financial flexibility. However, the outcome of any ongoing or future audits is unpredictable, and if future adjustments exceed the company's estimates, the company's profitability may be affected.

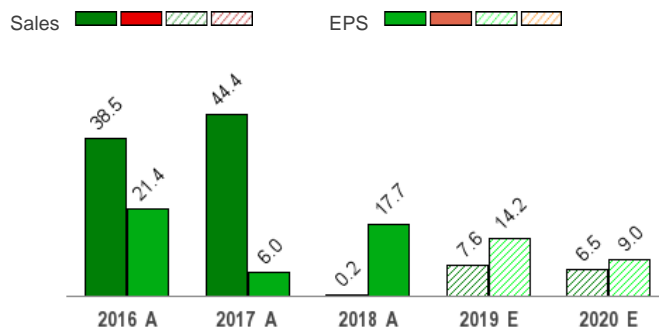
### Price, Consensus & Surprise



### Data Overview

52 Week High-Low	<b>\$101.46 - \$54.08</b>
20 Day Average Volume (sh)	<b>815,814</b>
Market Cap	<b>\$14.3 B</b>
YTD Price Change	<b>3.3%</b>
Beta	<b>1.51</b>
Dividend / Div Yld	<b>\$1.36 / 1.3%</b>
Industry	<b><a href="#">Aerospace - Defense</a></b>
Zacks Industry Rank	<b>Top 12% (31 out of 254)</b>

### Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	<b>13.3%</b>
Last Sales Surprise	<b>3.5%</b>
EPS F1 Est- 4 week change	<b>1.2%</b>
Expected Report Date	<b>02/18/2020</b>
Earnings ESP	<b>-0.9%</b>
P/E TTM	<b>21.3</b>
P/E F1	<b>18.6</b>
PEG F1	<b>2.5</b>
P/S TTM	<b>1.3</b>

### Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2020	2,666 E	2,826 E	2,928 E	2,927 E	11,681 E
2019	2,577 A	2,728 A	2,835 A	2,830 E	10,972 E
2018	2,443 A	2,529 A	2,575 A	2,647 A	10,194 A

### EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2020	\$1.26 E	\$1.38 E	\$1.38 E	\$1.36 E	\$5.45 E
2019	\$1.13 A	\$1.16 A	\$1.36 A	\$1.35 E	\$5.00 E
2018	\$1.03 A	\$1.12 A	\$1.14 A	\$1.10 A	\$4.38 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 01/09/2020. The reports text is as of 01/10/2020.

## Overview

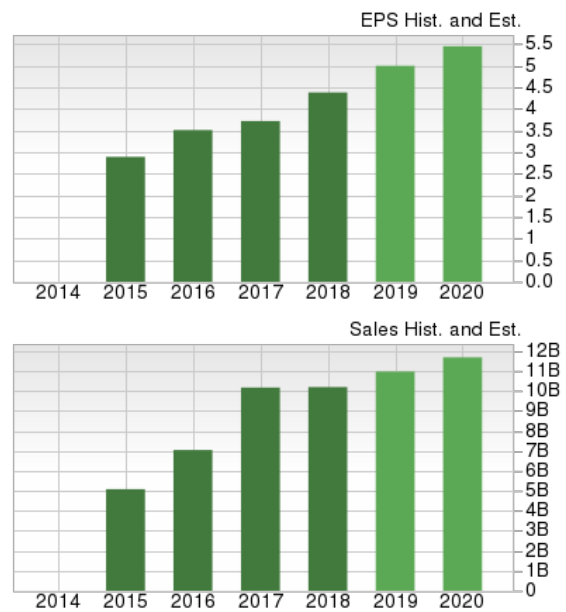
Founded in 1969, Delaware-based Leidos Holdings, Inc. is a global science and technology leader that serves the defense, intelligence, civil and health markets. Its core capabilities include providing solutions in the fields of cybersecurity; data analytics; enterprise IT modernization; operations and logistics; sensors, collection and phenomenology; software development; and systems engineering. Outside the United State, the company's international customers include foreign governments and their agencies, primarily located in the United Kingdom, the Middle East and Australia.

Leidos Holdings currently operates through three business segments namely — Defense Solutions, Civil and Health.

**Defense Solutions:** This business segment offers surveillance and reconnaissance, integrated systems solutions and global services for the U.S. Intelligence Community, military commands as well as other government and commercial customers. It provides multi-spectral, airborne, ground and maritime ISR collection as well as processing systems, advanced sensor design, command and control solutions, and training systems. In 2018, this division generated sales of \$4,948 million, contributing 49% to total business sales.

**Civil:** This segment provides aviation solutions, security products, enterprise IT services, federal environment and infrastructure solutions as well as logistics. While aviation solutions provide systems integration for Air Navigation Service Providers, including the FAA and airport operators, security products include Vehicle and Cargo Inspection System, explosive detection systems as well as radiation detection systems. The unit realized sales of \$3,429 million in 2018, accounting for 34% of total business sales.

**Health:** This unit offers affordable solutions to federal and commercial customers, which are responsible for the health and well-being of people worldwide comprising service members and veterans. Its primary capabilities include providing complex systems integration, managed health services, enterprise IT transformation and life sciences. Sales at this division totaled \$1,817 million in 2018, representing 17% of the entire business sales.



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## Reasons To Buy:

- ▲ Increased contract wins for its cost-effective defense solutions from the Pentagon as well as other U.S. allies have been serving as a primary growth driver for Leidos Holdings. In fact, these contract wins tend to bolster the company's backlog. At the end of third-quarter 2019, Leidos Holdings' total backlog stood at \$23.9 billion compared with \$21.7 billion at second-quarter end. Such solid backlog trends indicate impressive revenue growth prospects for the company in quarters ahead.
- ▲ With the current U.S. administration being in favor of increased defense spending, macroeconomic environment in the nation has been boosting the company's growth prospects. In this regard, it is imperative to mention that the fiscal 2020 defense budget reflects a 5% improvement in spending levels from the fiscal 2019's budget. Such increased spending levels are expected to drive order growth for defense players like Leidos Holdings. This has also made the company's investors optimistic about its growth trajectory. In a year's time, shares of the company have increased 87.2% compared with the industry's 25.8% rise.
- ▲ Leidos Holdings' strong balance sheet and a steady cash flow position offer it substantial financial flexibility. This, in turn, enables it to reward its shareholders with impressive dividend payouts and share repurchases. Notably, the company exited the third quarter with \$635 million in cash and equivalents on hand compared with \$327 million as of Dec 28, 2018. It ended the quarter with cash flow from operating activities worth \$349 million. Such solid cash flow reserve should allow Leidos Holdings to make future dividend hike, which, in turn, would attract investors.

Favorable Budgetary revisions, solid cash flow growth and solid contract inflows should keep Leidos' momentum alive

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## Risks

- In the United States, Leidos Holdings faces intense competition for its broad portfolio of products and services. In particular, the company competes with well-recognized companies, financial resources and a larger technical staff. This, in turn, puts Leidos Holdings in a competitively disadvantageous position. Moreover, in recent times, some mega mergers and acquisition deals have been inked in the aerospace-defense space. Such consolidations tend to boost the power of newly build defense majors, threatening the profit generation capability of other players in the market like Leidos.
  - As of Sep 27, 2019, indirect cost audits by the Defense Contract Audit Agency remain open for 2013 and subsequent years. Now, Leidos Holdings cannot predict the outcome of any ongoing or future audits. Management fears that if the future adjustments exceed the Company's estimates, its profitability may be adversely affected.
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## Last Earnings Report

### Leidos Holdings Beats on Q3 Earnings, Ups 2019 View

Leidos Holdings' third-quarter 2019 adjusted earnings of \$1.36 per share surpassed the Zacks Consensus Estimate of \$1.20 by 13.3%. The bottom line also increased 19.3% from \$1.14 a year ago. This upside can be attributed to solid revenues and operating income.

However, the company's GAAP earnings of \$1.11 per share declined from 96 cents in the year-ago quarter.

Quarter Ending **09/2019**

Report Date	Oct 29, 2019
Sales Surprise	3.52%
EPS Surprise	13.33%
Quarterly EPS	1.36
Annual EPS (TTM)	4.75

### Total Revenues

Leidos Holdings generated total revenues of \$2,835 million in the quarter, which exceeded the Zacks Consensus Estimate of \$2739 million by 3.5%. The top line also improved 10.1% year over year, backed by growth across all segments.

### Backlog

At the end of the reported quarter, the company's total backlog was \$23.9 billion compared with \$20.8 billion as of Dec 28, 2018. Of this, \$5.7 billion was funded.

### Operational Statistics

Total cost of revenues in the third quarter increased 12.7% to \$2,450 million. Operating income totaled \$249 million, compared with \$203 million in the year-ago period. This upside was driven by a decrease in selling, general and administrative expenses along with a decline in integration and restructuring costs.

As a result, operating margin expanded to 8.8% from 7.9% in the year-ago quarter.

Interest expenses were \$28 million compared with \$35 million in the prior-year quarter.

### Segmental Performance

**Defense Solutions:** Net revenues at this segment increased 8.3% to \$1,354 million from the prior-year quarter's \$1,250 million. This improvement can be primarily attributed to new awards received by the segment during the quarter under review along with a net increase in program volumes.

Also, the segment's operating income rose 4.5% to \$93 million from the year-ago quarter's income of \$89 million. Operating margin contracted 20 basis points (bps) to 6.9%.

**Health:** The segment recorded revenues of \$508 million in the third quarter, up 14.4% year over year. The uptick was primarily driven by a net increase in program volumes and new awards.

Operating income increased 21.1% to \$63 million, while operating margin expanded 70 bps to 12.4%.

**Civil:** Revenues at this segment amounted to \$973 million, up 10.4% year over year. New awards and a net increase in program volumes led to the upside.

While operating income declined 38% to \$57 million, operating margin contracted 450 bps to 5.9%.

### Financials

Cash and cash equivalents as of Sep 27, 2019, were \$635 million compared with \$327 million as of Dec 28, 2018. Net cash provided by operating activities at the end of third-quarter 2019 amounted to \$349 million compared with \$371 million a year ago.

### 2019 Guidance

Leidos Holdings raised its guidance for 2019. The company currently expects adjusted earnings of \$4.90-\$5.10, up from \$4.50-\$4.75 anticipated earlier. The Zacks Consensus Estimate for 2019 earnings is pegged at \$4.72, below the company's projected figure.

Moreover, the company expects 2019 revenues of \$10.90-\$11 billion compared with the earlier guidance of \$10.65-\$10.95 billion. The Zacks Consensus Estimate for revenues stands at \$10.82 billion, below the company's guided range.

Management expects adjusted EBITDA margin of 10.2-10.4%, up from the previous guidance of 9.9-10.1%.

Cash flow from operating activities is expected to be at or above \$875 million, up from the previous guidance of \$825 million.

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## Valuation

Leidos Holdings' shares are up 24.3% in the past six months period and 85.5% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Aerospace sector are up 8.2% and 9.9% in the past six months period, respectively. Over the past year, the Zacks sub-industry and sector are up 25.5% and 30.2%, respectively.

The S&P 500 index is up 10% in the six months period and up 27.1% in the past year.

The stock is currently trading at 18.51X forward 12-month earnings, which compares to 17.82X for the Zacks sub-industry, 17.86X for the Zacks sector and 18.94X for the S&P 500 index.

Over the past five years, the stock has traded as high as 20.78X and as low as 10.67X, with a 5-year median of 15.99X. Our Outperform recommendation indicates that the stock will perform better than the market. Our \$116 price target reflects 21.25X earnings value.

The table below shows summary valuation data for LDOS

Valuation Multiples - LDOS					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	18.51	17.82	17.86	18.94
	5-Year High	20.78	22.53	21.56	19.34
	5-Year Low	10.67	14.53	14.28	15.17
	5-Year Median	15.99	17.02	16.83	17.44
P/S F12M	Current	1.22	1.49	1.3	3.51
	5-Year High	1.27	1.59	1.37	3.51
	5-Year Low	0.32	0.92	0.79	2.54
	5-Year Median	0.79	1.21	1.05	3
P/B TTM	Current	4.4	12.66	9.29	4.47
	5-Year High	4.46	24.02	13.66	4.47
	5-Year Low	1.97	6.72	5.12	2.85
	5-Year Median	2.91	13.5	8.93	3.61

As of 01/09/2020

## Industry Analysis Zacks Industry Rank: Top 12% (31 out of 254)



## Top Peers

Heico Corporation (HEI)	Outperform
Teledyne Technologies Incorporated (TDY)	Outperform
Air Industries Group (AIRI)	Neutral
Bae Systems PLC (BAESY)	Neutral
Curtiss-Wright Corporation (CW)	Neutral
L3Harris Technologies Inc (LHX)	Neutral
Raytheon Company (RTN)	Neutral
Transdigm Group Incorporated (TDG)	Neutral

Industry Comparison Industry: Aerospace - Defense				Industry Peers		
	LDOS Outperform	X Industry	S&P 500	CW Neutral	LHX Neutral	RTN Neutral
<b>VGM Score</b>	<b>A</b>	-	-	<b>B</b>	<b>F</b>	<b>B</b>
Market Cap	14.31 B	12.80 B	23.94 B	6.24 B	46.93 B	63.67 B
# of Analysts	6	5.5	13	5	6	6
Dividend Yield	1.35%	0.87%	1.78%	0.47%	1.41%	1.65%
<b>Value Score</b>	<b>B</b>	-	-	<b>C</b>	<b>D</b>	<b>C</b>
Cash/Price	0.05	0.02	0.04	0.05	0.02	0.04
EV/EBITDA	16.66	14.40	13.97	13.82	119.79	16.92
PEG Ratio	2.47	2.34	2.03	2.31	2.33	1.66
Price/Book (P/B)	4.40	4.53	3.33	3.67	2.05	4.90
Price/Cash Flow (P/CF)	16.16	16.63	13.73	16.58	22.10	18.02
P/E (F1)	18.55	18.23	18.79	19.11	18.63	17.77
Price/Sales (P/S)	1.33	1.42	2.64	2.51	4.84	2.22
Earnings Yield	5.39%	5.39%	5.32%	5.23%	5.37%	5.63%
Debt/Equity	1.00	0.67	0.72	0.52	0.31	0.38
Cash Flow (\$/share)	6.26	5.28	6.94	8.81	9.61	12.69
<b>Growth Score</b>	<b>A</b>	-	-	<b>B</b>	<b>F</b>	<b>A</b>
Hist. EPS Growth (3-5 yrs)	14.25%	12.53%	10.56%	17.93%	10.80%	11.92%
Proj. EPS Growth (F1/F0)	9.04%	14.18%	7.49%	6.34%	37.45%	8.35%
Curr. Cash Flow Growth	1.52%	20.42%	14.83%	18.64%	23.01%	30.35%
Hist. Cash Flow Growth (3-5 yrs)	37.15%	7.81%	9.00%	8.01%	7.97%	7.51%
Current Ratio	1.16	1.16	1.23	2.19	1.49	1.54
Debt/Capital	49.88%	43.20%	42.99%	34.03%	23.74%	29.29%
Net Margin	6.25%	6.46%	11.08%	12.13%	12.02%	11.47%
Return on Equity	21.12%	19.00%	17.16%	18.83%	16.42%	27.23%
Sales/Assets	1.17	0.91	0.55	0.74	0.56	0.89
Proj. Sales Growth (F1/F0)	6.47%	5.32%	4.20%	3.68%	6.45%	6.96%
<b>Momentum Score</b>	<b>B</b>	-	-	<b>B</b>	<b>A</b>	<b>C</b>
Daily Price Chg	1.21%	1.14%	0.53%	0.72%	0.47%	0.55%
1 Week Price Chg	1.27%	1.06%	-0.30%	1.20%	4.34%	3.10%
4 Week Price Chg	10.85%	7.23%	1.92%	1.99%	8.16%	4.79%
12 Week Price Chg	23.71%	10.20%	6.54%	14.14%	5.65%	14.70%
52 Week Price Chg	84.08%	41.63%	22.58%	35.92%	57.38%	43.28%
20 Day Average Volume	815,814	493,325	1,580,816	188,769	1,164,921	1,184,935
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.39%	0.00%
(F1) EPS Est 4 week change	1.18%	0.00%	0.00%	0.00%	0.62%	0.07%
(F1) EPS Est 12 week change	3.19%	-0.25%	-0.50%	0.10%	2.30%	-1.06%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.00%	0.00%	0.49%	0.00%

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## 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.

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### 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>B</b>
Growth Score	<b>A</b>
Momentum Score	<b>B</b>
VGM Score	<b>A</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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