

Leidos Holdings, Inc. (LDOS)

\$96.82 (As of 05/15/20)

Price Target (6-12 Months): **\$103.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 04/22/20)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:A

Value: B

Growth: A

Momentum: D

Summary

Leidos Holdings reported mixed first-quarter 2020 results. While its earnings missed the Zacks Consensus Estimate, revenues exceeded the mark. The company 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. However, a comparative analysis of Leidos Holdings historical EV/SALES ratio reflects a relatively gloomy picture that might be a cause for investors' concern. The company does not hold a very strong solvency position, as is evident from its sequentially deteriorating financial ratios. Due to COVID-19, new contracts have been delayed and may continue to get delayed along with scheduled deliveries, thereby adversely impacting revenues.

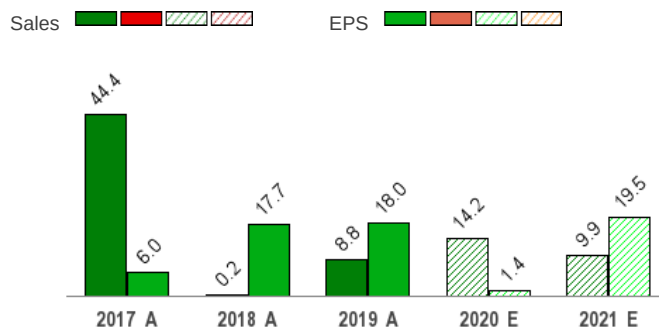
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$125.84 - \$68.00
20 Day Average Volume (sh)	1,096,997
Market Cap	\$13.8 B
YTD Price Change	-1.1%
Beta	1.15
Dividend / Div Yld	\$1.36 / 1.4%
Industry	Aerospace - Defense
Zacks Industry Rank	Bottom 30% (177 out of 254)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-4.0%
Last Sales Surprise	0.2%
EPS F1 Est- 4 week change	-5.7%
Expected Report Date	NA
Earnings ESP	0.0%
P/E TTM	18.6
P/E F1	18.5
PEG F1	2.5
P/S TTM	1.2

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	3,434 E	3,481 E	3,623 E	3,749 E	13,918 E
2020	2,889 A	3,039 E	3,277 E	3,444 E	12,668 E
2019	2,577 A	2,728 A	2,835 A	2,954 A	11,094 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.52 E	\$1.58 E	\$1.68 E	\$1.85 E	\$6.26 E
2020	\$1.19 A	\$1.08 E	\$1.33 E	\$1.51 E	\$5.24 E
2019	\$1.13 A	\$1.16 A	\$1.36 A	\$1.51 A	\$5.17 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 05/15/2020. The reports text is as of 05/18/2020.

Overview

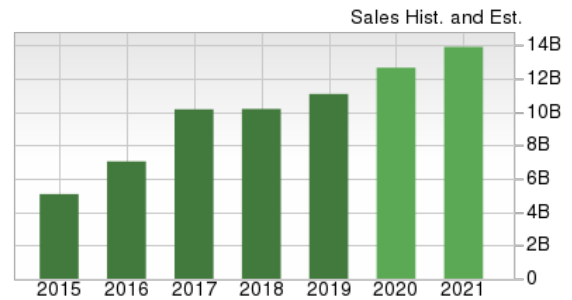
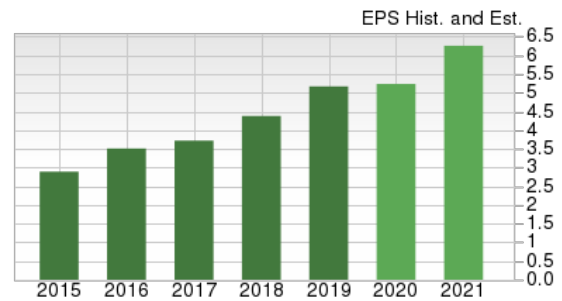
Founded in 1969, Delaware-based Leidos Holdings, Inc. is a global science and technology leader that serves the defense, intelligence, civil and health markets. Its core capabilities include providing solutions in the fields of cybersecurity; data analytics; enterprise IT modernization; operations and 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 2019, this division generated sales of \$5,367 million, contributing 48.4% 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 \$3,729 million in 2019, accounting for 33.6% 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 \$1,998 million in 2019, representing 18% of the entire business sales.



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 bolster the company's bookings and consequently its backlog count. As of Apr 3, 2020, the company's net bookings were worth \$5.5 billion compared with \$3.3 billion at 2019-end. Leidos Holdings' total backlog was \$28.3 billion compared with \$24.1 billion in the prior quarter. Such solid backlog trends indicate impressive revenue growth prospects for the company in the 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 2021 defense budget proposal reflects a 3% improvement in spending levels from fiscal 2020 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. Evidently, the company's shares have improved 27.6% in the past year against its industry's decline of 32%.

▲ While steady contract wins boost organic growth for Leidos Holdings, notable acquisitions also bolster this defense major's operating results. During the first quarter, the company closed the acquisition of Dynetics, an industry-leading applied research and national security solutions company. The integration activities are progressing per plan. Notably, Dynetics delivered approximately 30% top-line growth in the first quarter, demonstrating its businesses' strength in fast-growing strategic areas such as hypersonics, space exploration in unmanned systems.

In late April, Dynetics won one of the three prime contracts by NASA under the Artemis program to develop a human landing system through the preliminary design phase. This will add to the company's second-quarter bookings.

Favorable Budgetary revisions, solid contract inflows and strategic buyouts should keep Leidos' momentum alive

Reasons To Sell:

▼ A comparative analysis of Leidos Holdings historical EV/SALES ratio reflects a relatively gloomy picture that might be a cause for investors' concern. Evidently, the stock has a forward 12-month EV/SALES ratio of 1.54 which remained above the industry's EV/SALES ratio of 1.32. This might be concerning for this stock's investors as higher EV/SALES value indicates that the company is more leveraged when compared to its whole industry.

Unfavorable valuation and COVID-19 pandemic led impacts pose threat to this stock's growth

▼ Leidos Holdings' cash and cash equivalents were \$445 million at the end of first-quarter 2020, compared with \$668 million as of Dec 31, 2019. Its long-term debt was \$2,944 million as of Mar 31, 2020 and current debt was \$1,793 million. Therefore, both its long-term debt and current debt are much higher than its cash reserve. This reflects the fact that the company does not have a very strong solvency position, further evident from the deterioration in financial ratios. Evidently, the company's first-quarter 2020 interest coverage of 6.2 was lower than the prior-quarter figure of 7.5 and the lowest in the last four quarters.

Additionally, the company's debt-to-capital ratio of 0.59 as of Mar 31, 2020 increased sequentially from 0.49 and was the highest in the last four quarters. Its current ratio of 0.67 at the end of first-quarter 2020 declined sequentially from 1.21 and was also the lowest in the past four quarters. Such unfavorable financial ratios indicate that Leidos Holdings may face difficulty in paying off its debt obligations, at least in the near term.

▼ The COVID-19 pandemic resulted in sales volume decline for Leidos Holdings in the first quarter. New contracts have been delayed and may get further delayed for Leidos Holdings, along with scheduled deliveries, thereby adversely impacting its revenues. Moreover, the company fears that the fiscal 2021 budget cycle might get delayed as the U.S. government focuses on mitigating the impact of COVID-19, which may result in a re-evaluation of U.S. government spending levels and priorities. If that happens and the U.S. administration makes a contractionary change in budget, Leidos Holdings will be hurt.

Last Earnings Report

Leidos Holdings Q1 Earnings Miss, Revenues Rise Y/Y

Leidos Holdings' first-quarter 2020 adjusted earnings of \$1.19 per share missed the Zacks Consensus Estimate of \$1.24 by 4%. However, the bottom line grew 5.3% from \$1.13 per share registered a year ago.

Moreover, the company's GAAP earnings of 80 cents per share declined from the year-ago quarter's \$1.29.

Quarter Ending **03/2020**

Report Date	May 05, 2020
Sales Surprise	0.17%
EPS Surprise	-4.03%
Quarterly EPS	1.19
Annual EPS (TTM)	5.22

Total Revenues

Leidos Holdings generated total revenues of \$2,889 million in the quarter under consideration, which exceeded the Zacks Consensus Estimate of \$2,884 million by 0.2%. The top line also improved 12.1% year over year, backed by growth across all segments.

Backlog

At the end of the reported quarter, the company's total backlog was \$28.3 billion compared with \$24.1 billion at 2019-end. Of this total backlog, \$6.2 billion was funded.

Operational Statistics

Total cost of revenues in the quarter increased 12.3% to \$2,494 million. Operating income totaled \$192 million, in line with the year-ago quarter's figure.

Non-GAAP operating income margin for the quarter was 8.5% compared with 9.3% in the prior-year quarter, primarily attributable to higher indirect expenditures, including the impacts of the coronavirus pandemic.

Interest expenses summed \$48 million compared with \$38 million in the prior-year quarter.

Segmental Performance

Defense Solutions: Net revenues at this segment improved 14.4% to \$1,705 million from the prior-year quarter's \$1,491 million. This upside can be primarily attributed to revenues related to the acquisition of Dynetics, program wins and a net increase in program volumes.

However, the segment's operating income declined to \$95 million from the year-ago quarter's \$104 million, with the operating margin contracting 140 basis points (bps) to 5.6%.

Health: The segment recorded revenues of \$530 million in the first quarter, up 14.5% year over year. The improvement was primarily driven by a net increase in program volumes, program wins and the impact of the acquisition of IMX Medical Management Services, Inc. during the third quarter of fiscal 2019.

Operating income surged 62.2% to \$73 million, while operating margin expanded 410 bps to 13.8%.

Civil: Revenues at this segment amounted to \$654 million, up 5%. This uptick was primarily attributable to program wins and a net increase in program volumes.

While operating income rose 1.7% to \$59 million, operating margin contracted 30 bps to 9%.

Financials

Cash and cash equivalents, as of Apr 3, 2020, were \$445 million compared with \$668 million, as of Jan 3, 2020.

Long-term debt, net of current portion, amounted to \$2,444 million, as of Apr 3, 2020, compared with \$2,925 million, as of Jan 3, 2020.

Net cash provided by operating activities in the first quarter of 2020 was \$372 million compared with \$288 million a year ago.

2020 Guidance

Leidos Holdings revised its outlook for 2020. The company currently expects adjusted earnings in the \$5.00-\$5.30 range, down from \$5.30-\$5.65 per share anticipated earlier. The Zacks Consensus Estimates for 2020 earnings, pegged at \$5.49 per share, is below the company's projected view.

Leidos Holdings currently expects revenues in the range of \$12.5-\$12.9 billion this year, down from \$12.6-\$13.0 billion anticipated earlier. The Zacks Consensus Estimates for 2020 revenues, pegged at \$12.69 billion, is below the midpoint of the company-guided range.

The company's cash flow from operating activities is anticipated to be at or above \$1 billion.

Recent News

On **April 7, 2020**, Leidos was awarded a new task order by the Internal Revenue Service (IRS) to enhance, upgrade, and maintain the agency's e-Services and Integrated Customer Communications Environment (ICCE) platforms. The single award, hybrid firm-fixed price and cost-plus-fixed-fee contract has a six-month base period of performance and four one-year option years with a total value of approximately \$69 million, if all options are exercised.

On **Feb 6, 2020**, Leidos has been awarded a prime contract by the Naval Information Warfare Systems Command (NAVWAR), formerly known as the Space and Naval Warfare Systems Command (SPAWAR), to provide global network services under the Next Generation Enterprise Network Re-compete (NGEN-R) Service Management, Integration, & Transport (SMIT) contract. The single award, indefinite delivery/indefinite quantity, firm-fixed-price and cost-plus-fixed-fee contract has a five-year base period of performance followed by three one-year option periods, and an approximate value of \$7.7 billion. Work will be performed on a global scale, headquartered out of the Washington D.C. metropolitan area.

Valuation

Leidos Holdings' shares are down 0.7% in the year-to-date period and up 30.6% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Aerospace sector are down 31.7% and 37.9% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are down 32.5% and 34.5%, respectively.

The S&P 500 index is down 10.2% in the year-to-date period and up 2.8% in the past year.

The stock is currently trading at 17.2X forward 12-month earnings, which compares to 18.9X for the Zacks sub-industry, 18.5X 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 22.4X and as low as 10.7X, with a 5-year median of 15.9X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$103 price target reflects 18.3X 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	17.22	18.89	18.5	20.8
	5-Year High	22.35	22.54	20.94	20.8
	5-Year Low	10.67	14.52	14.17	15.19
	5-Year Median	15.91	17.2	17.16	17.45
P/S F12M	Current	1.05	1.14	1	3.22
	5-Year High	1.48	1.64	1.49	3.44
	5-Year Low	0.32	0.95	0.92	2.54
	5-Year Median	0.84	1.26	1.17	3.02
EV/EBITDA TTM	Current	13.68	17.63	10.56	10.32
	5-Year High	24.85	19.65	15	12.86
	5-Year Low	4.23	8.12	7.38	8.28
	5-Year Median	11.56	11.72	10.48	10.77

As of 05/15/2020

Industry Analysis Zacks Industry Rank: Bottom 30% (177 out of 254)



Top Peers

Company (Ticker)	Rec	Rank
Air Industries Group (AIRI)	Neutral	3
Bae Systems PLC (BAESY)	Neutral	3
CurtissWright Corporation (CW)	Neutral	3
Heico Corporation (HEI)	Neutral	4
L3Harris Technologies Inc (LHX)	Neutral	3
Lockheed Martin Corporation (LMT)	Neutral	3
Teledyne Technologies Incorporated (TDY)	Neutral	3
Transdigm Group Incorporated (TDG)	Underperform	5

Industry Comparison Industry: Aerospace - Defense				Industry Peers		
	LDOS	X Industry	S&P 500	AIRI	CW	LHX
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	3	3	3
VGM Score	A	-	-	B	D	C
Market Cap	13.75 B	6.90 B	18.98 B	32.06 M	3.58 B	38.16 B
# of Analysts	8	4	14	1	4	6
Dividend Yield	1.40%	0.87%	2.21%	0.00%	0.79%	1.92%
Value Score	B	-	-	C	C	C
Cash/Price	0.03	0.10	0.06	0.04	0.04	0.02
EV/EBITDA	13.06	8.41	11.60	7.71	8.43	100.50
PEG Ratio	2.51	2.17	2.58	NA	NA	NA
Price/Book (P/B)	4.09	2.85	2.59	3.07	2.14	1.73
Price/Cash Flow (P/CF)	13.78	8.79	10.28	22.64	8.84	18.40
P/E (F1)	18.82	15.62	19.01	21.00	13.35	15.62
Price/Sales (P/S)	1.21	0.86	1.92	0.59	1.43	2.42
Earnings Yield	5.41%	5.41%	5.06%	4.76%	7.49%	6.40%
Debt/Equity	0.88	0.81	0.75	0.75	0.63	0.32
Cash Flow (\$/share)	7.03	2.73	7.01	0.05	9.72	9.61
Growth Score	A	-	-	B	F	B
Hist. EPS Growth (3-5 yrs)	14.53%	12.74%	10.82%	NA	19.12%	14.53%
Proj. EPS Growth (F1/F0)	1.26%	3.61%	-10.48%	225.00%	-11.38%	12.25%
Curr. Cash Flow Growth	6.19%	6.19%	5.68%	-136.97%	7.60%	23.01%
Hist. Cash Flow Growth (3-5 yrs)	6.45%	6.62%	8.52%	-22.72%	7.51%	7.97%
Current Ratio	0.67	1.26	1.27	1.17	2.04	1.41
Debt/Capital	46.71%	46.71%	44.25%	42.81%	38.53%	24.18%
Net Margin	5.20%	5.89%	10.54%	-5.01%	12.10%	8.30%
Return on Equity	22.56%	14.41%	16.29%	-24.82%	18.48%	13.20%
Sales/Assets	1.17	0.83	0.54	1.06	0.70	0.54
Proj. Sales Growth (F1/F0)	14.19%	0.00%	-2.55%	13.61%	-4.70%	96.70%
Momentum Score	D	-	-	B	C	F
Daily Price Chg	1.03%	-0.96%	0.20%	-0.94%	0.20%	-0.60%
1 Week Price Chg	4.91%	-0.71%	3.23%	-11.11%	-1.03%	-4.49%
4 Week Price Chg	4.28%	-8.32%	0.88%	-10.26%	-5.35%	-10.82%
12 Week Price Chg	-18.82%	-33.45%	-23.26%	-29.53%	-40.62%	-21.01%
52 Week Price Chg	26.91%	-29.01%	-12.56%	-8.70%	-26.89%	-4.12%
20 Day Average Volume	1,096,997	921,329	2,553,422	33,496	244,922	1,271,089
(F1) EPS Est 1 week change	0.07%	0.00%	0.00%	0.00%	0.00%	-0.44%
(F1) EPS Est 4 week change	-5.72%	-3.77%	-5.57%	0.00%	-10.30%	-2.13%
(F1) EPS Est 12 week change	-5.99%	-12.29%	-16.22%	0.00%	-15.74%	-2.63%
(Q1) EPS Est Mthly Chg	-16.52%	-6.06%	-11.63%	0.00%	-17.13%	-5.78%

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	B
Growth Score	A
Momentum Score	D
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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