

Leidos Holdings, Inc. (LDOS)

\$117.22 (As of 02/21/20)

Price Target (6-12 Months): **\$135.00**

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:C

Value: C | Growth: A | Momentum: F

Summary

Leidos Holdings ended the fourth quarter on a solid note, with both revenues and earnings surpassing the respective Zacks Consensus Estimate. It 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 in favor of increased defense spending, the macroeconomic environment in the nation aids the company's growth prospects. 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.

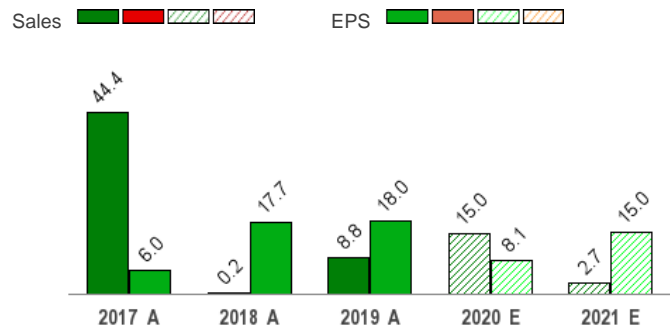
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$125.84 - \$61.74
20 Day Average Volume (sh)	902,093
Market Cap	\$16.6 B
YTD Price Change	19.8%
Beta	1.50
Dividend / Div Yld	\$1.36 / 1.2%
Industry	Aerospace - Defense
Zacks Industry Rank	Bottom 33% (170 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	11.9%
Last Sales Surprise	4.4%
EPS F1 Est- 4 week change	2.6%
Expected Report Date	NA
Earnings ESP	0.0%
P/E TTM	22.7
P/E F1	21.0
PEG F1	2.8
P/S TTM	1.5

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					13,109 E
2020	2,872 E	3,131 E	3,364 E	3,393 E	12,760 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					\$6.43 E
2020	\$1.22 E	\$1.34 E	\$1.53 E	\$1.54 E	\$5.59 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 02/21/2020. The reports text is as of 02/24/2020.

Overview

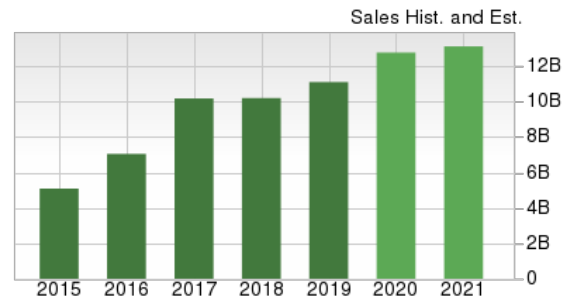
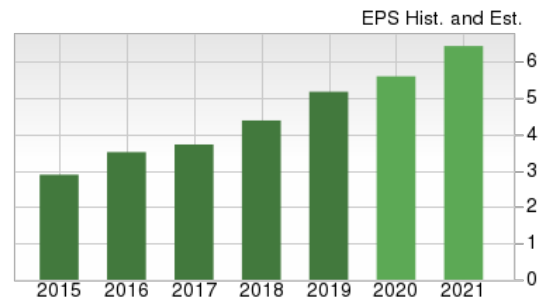
Founded in 1969, Delaware-based Leidos Holdings, Inc. is a global science and technology leader that serves the defense, intelligence, civil and health markets. Its core capabilities include providing solutions in the fields of cybersecurity; data analytics; enterprise IT modernization; operations and 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 tend to bolster the company's backlog. At the end of 2019, Leidos Holdings' total backlog stood at \$24.1 billion compared with \$20.8 billion at 2018-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. Evidently, in a year's time, shares of the company have increased 84.4% compared with the industry's 5.2% 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 2019 with \$668 million in cash and equivalents on hand compared with \$327 million as of Dec 28, 2018. It ended the year with cash flow from operating activities worth \$992 million, up from \$768 million at the end of 2018. 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

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 Jan 3, 2020, 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 Q4 Earnings Beat, Revenues Rise Y/Y

Leidos Holdings fourth-quarter 2019 adjusted earnings of \$1.51 per share surpassed the Zacks Consensus Estimate of \$1.35 by 11.9%. The bottom line also increased 37.3% from \$1.10 a year ago.

Moreover, the company's GAAP earnings of \$1.26 per share increased from \$1.25 in the year-ago quarter. This upside can be attributed to solid revenues and operating income.

For 2019, the company reported adjusted earnings of \$5.17 per share that surpassed the Zacks Consensus Estimate of \$5 by 3.4%. The bottom line increased 18% from \$4.38 a year ago.

Quarter Ending **12/2019**

Report Date	Feb 18, 2020
Sales Surprise	4.37%
EPS Surprise	11.85%
Quarterly EPS	1.51
Annual EPS (TTM)	5.16

Total Revenues

Leidos Holdings generated total revenues of \$2,954 million in the quarter, which exceeded the Zacks Consensus Estimate of \$2,830 million by 4.4%. The top line also improved 11.6% year over year, backed by growth across all segments.

For 2019, the company generated total revenues of \$11.09 billion, which exceeded the Zacks Consensus Estimate of \$10.97 billion by 1.1%. The full-year top line also improved 8.8% from the prior year.

Backlog

At the end of 2019, the company's total backlog was \$24.1 billion compared with \$20.8 billion as of Dec 28, 2018. Of this, \$5.4 billion was funded.

Operational Statistics

Total cost of revenues in the fourth quarter increased 10.9% to \$2,527 million. Operating income totaled \$261 million, compared with \$188 million in the year-ago period. The 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 7.1% in the year-ago quarter.

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Interest expenses were \$34 million, which came in line with the prior-year quarter figure.

Segmental Performance

Defense Solutions: Net revenues at this segment increased 10.7% to \$1,400 million from \$1,265 million in the prior-year quarter. This improvement can be primarily attributed to new awards and a net increase in program volumes.

Also, the segment's operating income improved 55% to \$124 million from the year-ago quarter's income of \$80 million. Operating margin expanded 260 basis points (bps) to 8.9%.

Health: The segment recorded revenues of \$526 million in the fourth quarter, up 5.8% year over year. The uptick was primarily driven by a net increase in program volumes, new awards and acquisition of IMX Medical Management Services.

Operating income increased 7.4% to \$73 million, while operating margin expanded 40 bps to 13.9%.

Civil: Revenues at this segment amounted to \$1,028 million, up 16.2% year over year. New awards and a net increase in program volumes led to the upside.

While operating income improved 54% to \$97 million, operating margin contracted 230 bps to 9.4%.

Financials

Cash and cash equivalents as of Jan 3, 2020 were \$668 million compared with \$327 million as of Dec 28, 2018. Net cash provided by operating activities at the end of 2019 amounted to \$992 million compared with \$768 million a year ago.

Guidance

Leidos Holdings issued its guidance for 2020. The company currently expects adjusted earnings in the range of \$5.30-\$5.65. The Zacks Consensus Estimate for 2020 earnings is pegged at \$5.45, below the mid-point of the company's projected range.

Moreover, the company expects 2020 revenues of \$12.6-\$13.0 billion. The Zacks Consensus Estimate for revenues stands at \$11.68 billion, lower than the company's guided range.

Management expects adjusted EBITDA margin of 10-10.2%, while cash flow from operating activities is expected to be or above \$1billion.

Recent News

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 up 40.1% in the past six months period and 84.4% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Aerospace sector are up 2.8% and 6.3% in the past six months period, respectively. Over the past year, the Zacks sub-industry and sector are up 5.2% and 10.6%, respectively.

The S&P 500 index is up 17.6% in the six months period and up 21.2% in the past year.

The stock is currently trading at 20.5X forward 12-month earnings, which compares to 22.5X for the Zacks sub-industry, 21.5X for the Zacks sector and 19.1X 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 16X. Our Outperform recommendation indicates that the stock will perform better than the market. Our \$135 price target reflects 23.6X 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	20.51	22.48	21.5	19.09
	5-Year High	22.35	22.54	21.54	19.34
	5-Year Low	10.67	14.52	14.26	15.18
	5-Year Median	15.99	17.09	16.887	17.47
P/S F12M	Current	1.31	1.58	1.39	3.51
	5-Year High	1.48	1.64	1.38	3.51
	5-Year Low	0.32	0.95	0.8	2.54
	5-Year Median	0.8	1.26	1.09	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 02/21/2020

Industry Analysis Zacks Industry Rank: Bottom 33% (170 out of 255)



Top Peers

Heico Corporation (HEI)	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
Teledyne Technologies Incorporated (TDY)	Neutral

Industry Comparison Industry: Aerospace - Defense				Industry Peers		
	LDOS Outperform	X Industry	S&P 500	CW Neutral	LHX Neutral	RTN Neutral
VGM Score	C	-	-	B	F	A
Market Cap	16.58 B	15.01 B	24.03 B	6.18 B	49.25 B	61.86 B
# of Analysts	6	4.5	13	4	8	7
Dividend Yield	1.16%	0.91%	1.76%	0.47%	1.35%	1.70%
Value Score	C	-	-	C	D	B
Cash/Price	0.04	0.04	0.04	0.05	0.02	0.07
EV/EBITDA	18.91	14.20	14.08	13.70	125.03	12.90
PEG Ratio	2.80	2.26	2.08	2.29	2.41	1.88
Price/Book (P/B)	4.85	4.43	3.29	3.63	2.15	5.06
Price/Cash Flow (P/CF)	16.68	16.47	13.42	16.43	23.19	15.68
P/E (F1)	20.97	18.48	19.00	18.90	19.25	17.62
Price/Sales (P/S)	1.49	1.39	2.64	2.49	3.83	2.12
Earnings Yield	4.77%	5.19%	5.26%	5.29%	5.19%	5.68%
Debt/Equity	0.95	0.66	0.70	0.52	0.31	0.32
Cash Flow (\$/share)	7.03	2.18	7.03	8.81	9.61	14.17
Growth Score	A	-	-	C	F	A
Hist. EPS Growth (3-5 yrs)	14.25%	13.39%	10.84%	17.93%	12.63%	13.63%
Proj. EPS Growth (F1/F0)	8.19%	13.18%	7.09%	6.02%	39.60%	5.80%
Curr. Cash Flow Growth	6.19%	4.55%	6.72%	18.64%	23.01%	9.30%
Hist. Cash Flow Growth (3-5 yrs)	37.15%	6.58%	8.25%	8.01%	7.97%	9.23%
Current Ratio	1.21	1.18	1.22	2.19	1.49	1.34
Debt/Capital	48.76%	43.17%	42.37%	34.03%	23.74%	24.65%
Net Margin	6.01%	6.01%	11.56%	12.13%	10.37%	11.46%
Return on Equity	22.51%	20.11%	16.80%	18.83%	17.71%	27.22%
Sales/Assets	1.18	0.92	0.55	0.74	0.66	0.89
Proj. Sales Growth (F1/F0)	10.13%	5.15%	3.90%	3.95%	96.83%	6.70%
Momentum Score	F	-	-	A	B	C
Daily Price Chg	-1.72%	-0.58%	-0.83%	-0.06%	-0.45%	0.79%
1 Week Price Chg	2.45%	0.67%	1.65%	-0.53%	-0.57%	-1.49%
4 Week Price Chg	14.22%	-0.73%	-0.37%	-2.20%	-0.00%	-3.50%
12 Week Price Chg	28.84%	5.00%	3.74%	4.60%	11.12%	1.67%
52 Week Price Chg	86.21%	19.74%	14.14%	19.63%	35.38%	19.85%
20 Day Average Volume	902,093	491,905	1,992,841	168,041	1,179,367	1,983,343
(F1) EPS Est 1 week change	2.63%	0.00%	0.00%	0.15%	0.00%	0.00%
(F1) EPS Est 4 week change	2.63%	0.00%	-0.02%	0.12%	1.91%	-2.34%
(F1) EPS Est 12 week change	3.84%	0.00%	-0.17%	0.18%	2.77%	-2.28%
(Q1) EPS Est Mthly Chg	-6.61%	-5.88%	-0.48%	0.00%	1.49%	-10.13%

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	C
Growth Score	A
Momentum Score	F
VGM Score	C

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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