

## Leidos Holdings, Inc. (LDOS)

**\$91.68** (As of 08/27/20)

Price Target (6-12 Months): **\$97.00**

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 ended the second quarter of 2020 on a mixed note. While its earnings surpassed the Zacks Consensus Estimate, revenues failed to meet the mark. The company has outperformed its industry in the past year. 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. Its recent acquisitions should boost inorganic growth. However, the company does not hold a very strong solvency position, as is evident from its sequentially deteriorating financial ratios. Due to COVID-19, the company may incur increasing costs, which may not be fully recoverable, thereby impacting its profitability. Also, Leidos fears that fiscal 2021 budget cycle might get delayed with U.S. government focusing on mitigating COVID-19's impact.

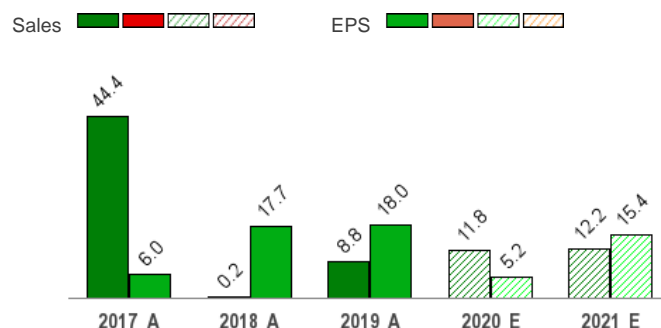
### Price, Consensus & Surprise



### Data Overview

52 Week High-Low	\$125.84 - \$68.00
20 Day Average Volume (sh)	1,080,809
Market Cap	\$13.0 B
YTD Price Change	-6.3%
Beta	1.10
Dividend / Div Yld	\$1.36 / 1.5%
Industry	<a href="#">Aerospace - Defense</a>
Zacks Industry Rank	Bottom 12% (223 out of 252)

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



Last EPS Surprise	44.9%
Last Sales Surprise	-4.2%
EPS F1 Est- 4 week change	3.7%
Expected Report Date	11/03/2020
Earnings ESP	0.0%
P/E TTM	16.3
P/E F1	16.9
PEG F1	2.3
P/S TTM	1.1

### Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	3,295 E	3,407 E	3,537 E	3,716 E	13,907 E
2020	2,889 A	2,914 A	3,176 E	3,414 E	12,400 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	\$1.46 E	\$1.54 E	\$1.67 E	\$1.78 E	\$6.28 E
2020	\$1.19 A	\$1.55 A	\$1.25 E	\$1.44 E	\$5.44 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 08/27/2020. The reports text is as of 08/28/2020.

## Overview

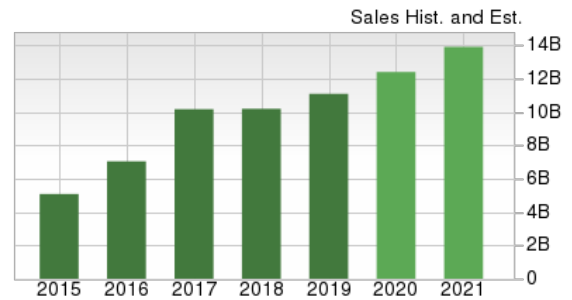
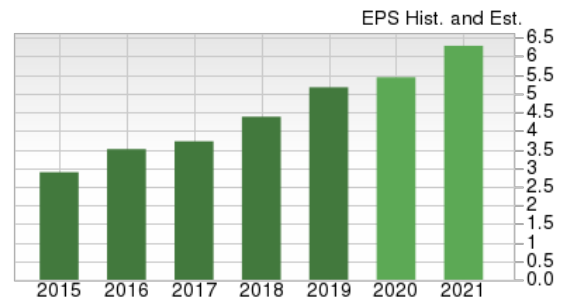
Founded in 1969, Delaware-based Leidos Holdings, Inc. is a global science and technology leader that serves the defense, intelligence, civil and health markets. Its core capabilities include providing solutions in the fields of cybersecurity; data analytics; enterprise IT modernization; operations and 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. During the second quarter of 2020, the company recorded net bookings worth \$4.6 billion compared with \$3 billion during the second quarter of 2019. Leidos Holdings' total backlog was \$30.7 billion compared with \$28.3 billion in the prior quarter. Notably, large new business wins in the defense solutions segment and the Human Lander System program contributed to the record backlog in the reported 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 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 gained 5.2% in the past year against its industry's decline of 29.7%.
- ▲ While steady contract wins boost organic growth for Leidos Holdings, notable acquisitions also bolster this defense major's operating results. During the second quarter, the company completed the acquisition of L3Harris' security detection and automation businesses for \$968 million. The addition of these businesses has expanded the scope and scale of Leidos Holdings' global security detection and automation offerings. In January, 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, during the second quarter, Leidos Holdings' revenues grew 6.8% year over year, driven by the acquisitions of Dynetics and the L3Harris security detection and automation businesses.

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

---

## Reasons To Sell:

- ▼ Leidos Holdings' cash and cash equivalents were \$588 million at the end of second- quarter 2020, compared with \$445 million as of Mar 31, 2020. Its long-term debt was \$4,677 million as of Jul 3, 2020 and current debt was \$854 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 second-quarter 2020 interest coverage of 6.1 was lower than the prior-quarter figure and the lowest in the last four quarters.

Additionally, the company's debt-to-capital ratio of 0.61 as of Jul 3, 2020 increased sequentially from 0.59 and was the highest in the last four quarters. Further, its current ratio of 0.89 at the end of second-quarter 2020 being less than 1 indicates that the firm might not be able to meet debt obligations in the near future.

- ▼ During the second quarter, COVID-19 adversely impacted Leidos Holdings' revenues by approximately \$132 million and operating income by approximately \$68 million compared with the prior-year results. The company experienced delays on certain contracts as a result of standby leave absences, which caused a portion of its contracts to be less profitable. Since the pandemic is still ongoing, these delays are expected to continue in the near future. Hence, Leidos Holdings might continue to witness such weak performance in its operational results in the next few quarters.
- ▼ 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. Even after COVID-19 subsides, the company will experience materially adverse impacts on its business as a result of the outbreak's global economic impact, including any recession that is occurring or may occur in the future. In addition, Leidos Holdings may incur increasing costs as a result of COVID-19, and these cost increases may not be fully recoverable or adequately covered by insurance, which might impact its profitability.

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

## Last Earnings Report

### Leidos Holdings Q2 Earnings Beat, 2020 EPS View Up

Leidos Holdings second-quarter 2020 adjusted earnings of \$1.55 per share beat the Zacks Consensus Estimate of \$1.07 by 44.9%. Moreover, the bottom line grew 33.6% from \$1.16 per share registered in the year-ago period.

Further, the company's GAAP earnings of \$1.06 per share improved from the year-ago quarter's 93 cents.

Quarter Ending **06/2020**

Report Date	Aug 04, 2020
Sales Surprise	-4.21%
EPS Surprise	44.86%
Quarterly EPS	1.55
Annual EPS (TTM)	5.61

### Total Revenues

Leidos Holdings generated total revenues of \$2,914 million in the quarter under consideration, which missed the Zacks Consensus Estimate of \$3,042 million by 4.2%. The top line however improved 6.8% year over year, backed by growth across all segments, except Health.

### Backlog

At the end of the reported quarter, the company's total backlog was \$30.7 billion compared with \$28.3 billion at first-quarter 2020 end. Of this total backlog, \$7 billion was funded.

### Operational Statistics

Total cost of revenues in the quarter increased 7.8% to \$2,531 million. Operating income totaled \$249 million, up 18.6% from the year-ago quarter's figure.

Adjusted operating income margin for the quarter was 11.2% compared with 9.4% in the prior-year quarter, primarily attributable to a net gain recognized upon the receipt of proceeds related to the VirnetX legal matter and program wins.

Interest expenses were \$41 million compared with \$33 million in the prior-year quarter.

### Segmental Performance

**Defense Solutions:** Net revenues at this segment improved 12.6% to \$1,757 million from the prior-year quarter's \$1,560 million. This upside can be primarily attributed to revenues related to the acquisition of Dynetics, program wins and a net increase in program volumes.

Moreover, the segment's operating income improved to \$119 million from the year-ago quarter's \$113 million while the operating margin contracted 40 basis points (bps) to 6.8%.

**Health:** The segment recorded revenues of \$399 million in the second quarter, down 20.4% 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.

Operating income slumped 98.4% to \$1 million, while operating margin contracted 1190 bps to 0.3%.

**Civil:** Revenues at this segment amounted to \$758 million, up 13.6%. This uptick was primarily attributable to program wins and a net increase in program volumes.

While operating income rose 39.3% to \$78 million, operating margin expanded 190 bps to 10.3%.

### Financials

Cash and cash equivalents, as of Jul 3, 2020, was \$588 million compared with \$668 million, as of Jan 3, 2020.

Long-term debt, net of current portion, amounted to \$4,148 million, as of Apr 3, 2020, compared with \$2,925 million, as of Jan 3, 2020.

Net cash provided by operating activities in the second quarter of 2020 was \$794 million compared with \$474 million a year ago.

### 2020 Guidance

Leidos Holdings revised its outlook for 2020. The company currently expects adjusted earnings in the \$5.25-\$5.55 range, up from \$5.00-\$5.30 per share anticipated earlier. The Zacks Consensus Estimate for 2020 earnings, pegged at \$5.24 per share, is below the company's projection.

Leidos Holdings currently expects revenues in the range of \$12.2-\$12.6 billion this year, down from \$12.5-\$12.9 billion anticipated earlier. The Zacks Consensus Estimate for 2020 revenues, pegged at \$12.67 billion, is above the company-guided range.

The company's cash flow from operating activities is now anticipated to be at or above \$1.2 billion compared with \$1 billion projected earlier.

## Recent News

On **Aug 25, 2020**, Leidos announced that it won a prime contract worth \$292 million by the Federal Aviation Administration (FAA) to design and develop a system to provide real-time access to essential weather, aeronautical, and National Airspace System (NAS) information through a common, NAS-wide Enterprise - Information Display System (E-IDS). The scalable, cloud-ready solution will replace five legacy systems as part of FAA's Next Generation Air Transportation System (NextGen) modernization project.

On **July 7, 2020**, Leidos got awarded with a new task order by the U.S. Army Contracting Command – Aberdeen Proving Ground (ACG-APG) to provide Intelligence, Electronic Warfare and Sensors (IEW&S) system and software support to the U.S. Army's Communications-Electronics Command (CECOM) Software Engineering Center (SEC), Sensors and Mission Equipment Division (SMED). The single-award, indefinite-delivery/indefinite-quantity, cost-plus-fixed-fee task order has a one-year base period of performance, followed by four one-year options, and a total approximate value of \$210 million if all options are exercised. Work will be performed primarily at Aberdeen Proving Ground, Md.

On **Jun 23, 2020**, Leidos announced that it won a prime contract by Edinburgh Airport Limited (Edinburgh Airport) to upgrade the airport's security tray return systems with antimicrobial tray technology. This is Leidos' first order of the antimicrobial security tray technology introduced to mitigate the spread of bacteria from person-to-surface contact.

Under the contract, Leidos will provide new antimicrobial security trays that prevent reproduction of a broad spectrum of bacteria, including staphylococcus aureus (staph), E. coli, and antibiotic-resistant bacteria like MRSA and VRE, by 99.99%.

## Valuation

Leidos Holdings' shares are down 6.3% in the year-to-date period and up 5.2% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Aerospace sector are down 22.2% and 31.8% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry is down 29.7% while the sector is down 34.1%.

The S&P 500 index is up 8.1% in the year-to-date period and 19.4% in the past year.

The stock is currently trading at 15.3X of forward 12-month earnings, which compares to 21.3X for the Zacks sub-industry, 21.3X for the Zacks sector and 23.4X 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 \$97 price target reflects 16.2X 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	15.33	21.32	21.29	23.36
	5-Year High	22.35	22.54	21.29	23.36
	5-Year Low	10.67	14.52	14.17	15.25
	5-Year Median	15.85	17.76	17.29	17.58
P/S F12M	Current	0.97	1.31	1.71	3.81
	5-Year High	1.48	1.64	1.71	3.81
	5-Year Low	0.32	0.95	0.92	2.53
	5-Year Median	0.86	1.28	1.18	3.05
EV/EBITDA TTM	Current	12.39	32.09	16.57	13.25
	5-Year High	24.85	32.39	16.81	13.25
	5-Year Low	4.43	8.15	7.39	8.25
	5-Year Median	11.85	11.82	10.62	10.92

As of 08/27/2020

## Industry Analysis Zacks Industry Rank: Bottom 12% (223 out of 252)



## 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	3
L3Harris Technologies Inc (LHX)	Neutral	3
Lockheed Martin Corporation (LMT)	Neutral	3
Transdigm Group Incorporated (TDG)	Neutral	3
Teledyne Technologies Incorporated (TDY)	Neutral	2

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	A	C
Market Cap	13.04 B	11.52 B	23.67 B	35.21 M	4.28 B	39.17 B
# of Analysts	9	5	14	1	4	8
Dividend Yield	1.48%	0.01%	1.64%	0.00%	0.66%	1.88%
Value Score	B	-	-	C	B	C
Cash/Price	0.05	0.09	0.07	0.05	0.04	0.05
EV/EBITDA	13.34	9.93	13.33	8.41	9.61	98.18
PEG Ratio	2.23	2.37	3.05	NA	NA	1.10
Price/Book (P/B)	3.68	3.37	3.18	3.00	2.50	1.76
Price/Cash Flow (P/CF)	13.04	10.87	12.81	24.80	10.59	18.86
P/E (F1)	16.72	16.38	21.68	NA	15.13	15.86
Price/Sales (P/S)	1.12	1.12	2.50	0.71	1.77	2.14
Earnings Yield	5.93%	3.87%	4.43%	-2.61%	6.61%	6.30%
Debt/Equity	1.17	0.75	0.74	0.75	0.57	0.28
Cash Flow (\$/share)	7.03	2.73	6.94	0.05	9.72	9.61
Growth Score	A	-	-	B	B	B
Hist. EPS Growth (3-5 yrs)	14.85%	14.85%	10.41%	NA	18.25%	16.25%
Proj. EPS Growth (F1/F0)	5.20%	-3.74%	-4.94%	66.67%	-6.43%	37.77%
Curr. Cash Flow Growth	6.19%	11.64%	5.22%	-136.97%	7.60%	23.01%
Hist. Cash Flow Growth (3-5 yrs)	6.45%	7.38%	8.50%	-22.72%	7.51%	7.97%
Current Ratio	0.89	1.31	1.35	1.26	1.91	1.51
Debt/Capital	53.90%	42.98%	43.86%	42.71%	36.20%	22.01%
Net Margin	5.26%	5.59%	10.25%	-3.25%	10.52%	7.21%
Return on Equity	23.81%	10.92%	14.66%	-12.21%	16.75%	10.92%
Sales/Assets	1.11	0.79	0.50	0.94	0.67	0.48
Proj. Sales Growth (F1/F0)	11.78%	0.00%	-1.43%	-10.32%	0.22%	89.84%
Momentum Score	D	-	-	A	C	D
Daily Price Chg	1.26%	1.10%	0.43%	-4.56%	0.82%	1.04%
1 Week Price Chg	-5.86%	-4.20%	-1.45%	-7.52%	-6.94%	-2.19%
4 Week Price Chg	-0.74%	2.94%	3.75%	-0.86%	14.39%	4.58%
12 Week Price Chg	-13.49%	-1.61%	3.95%	-3.36%	-3.19%	-9.18%
52 Week Price Chg	5.14%	-13.44%	2.75%	-5.74%	-16.21%	-15.06%
20 Day Average Volume	1,080,809	535,697	1,887,168	60,292	318,602	1,496,911
(F1) EPS Est 1 week change	0.49%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	3.71%	0.00%	0.79%	0.00%	6.62%	1.24%
(F1) EPS Est 12 week change	5.03%	0.00%	3.43%	0.00%	5.59%	1.02%
(Q1) EPS Est Mthly Chg	-6.06%	-1.70%	0.00%	0.00%	-7.77%	-0.99%

---

## 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>B</b>
Growth Score	<b>A</b>
Momentum Score	<b>D</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.

---

### Disclosures

**This report contains independent commentary to be used for informational purposes only. The analysts contributing to this report do not hold any shares of this stock. The analysts contributing to this report do not serve on the board of the company that issued this stock. The EPS and revenue forecasts are the Zacks Consensus estimates, unless indicated otherwise on the reports first page.** Additionally, the analysts contributing to this report certify that the views expressed herein accurately reflect the analysts personal views as to the subject securities and issuers. ZIR certifies that no part of the analysts compensation was, is, or will be, directly or indirectly, related to the specific recommendation or views expressed by the analyst in the report.

Additional information on the securities mentioned in this report is available upon request. This report is based on data obtained from sources we believe to be reliable, but is not guaranteed as to accuracy and does not purport to be complete. Any opinions expressed herein are subject to change.

ZIR is not an investment advisor and the report should not be construed as advice designed to meet the particular investment needs of any investor. Prior to making any investment decision, you are advised to consult with your broker, investment advisor, or other appropriate tax or financial professional to determine the suitability of any investment. This report and others like it are published regularly and not in response to episodic market activity or events affecting the securities industry.

This report is not to be construed as an offer or the solicitation of an offer to buy or sell the securities herein mentioned. ZIR or its officers, employees or customers may have a position long or short in the securities mentioned and buy or sell the securities from time to time. ZIR is not a broker-dealer. ZIR may enter into arms-length agreements with broker-dealers to provide this research to their clients. Zacks and its staff are not involved in investment banking activities for the stock issuer covered in this report.

ZIR uses the following rating system for the securities it covers. **Outperform-** ZIR expects that the subject company will outperform the broader U.S. equities markets over the next six to twelve months. **Neutral-** ZIR expects that the company will perform in line with the broader U.S. equities markets over the next six to twelve months. **Underperform-** ZIR expects the company will underperform the broader U.S. equities markets over the next six to twelve months.

No part of this report can be reprinted, republished or transmitted electronically without the prior written authorization of ZIR.