

L3Harris Technology (LHX)

\$210.47 (As of 01/03/20)

Price Target (6-12 Months): **\$223.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 07/04/19)

Prior Recommendation: NA

Short Term: 1-3 Months

Zacks Rank: (1-5)

2-Buy

Zacks Style Scores:

VGM:F

Value: D

Growth: F

Momentum: B

Summary

L3Harris is a technology-oriented aerospace and defense player that delivers advanced defense and commercial technologies. On completion of its integration, L3Harris is expected to come up with \$18 billion in annualized revenues. L3Harris, post its formation, continues to follow a disciplined divestment strategy in line with both L3 Technologies and Harris' plans to efficiently focus on its core operations. In addition, management approved a new \$4 billion share repurchase authorization. Its shares have outperformed its industry in the past year. However, its huge debt level may dissuade investors from investing in the stock. Increasing costs of integration may hurt its bottom line. Further, decline in global air travel demand might impact new aircraft production and orders, and global flying hours, posing threat to L3Harris.

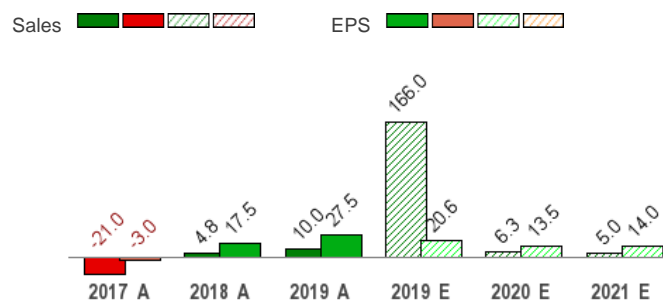
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$217.31 - \$130.14
20 Day Average Volume (sh)	1,066,388
Market Cap	\$46.5 B
YTD Price Change	6.4%
Beta	0.86
Dividend / Div Yld	\$3.00 / 1.4%
Industry	Aerospace - Defense
Zacks Industry Rank	Top 12% (31 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	6.1%
Last Sales Surprise	-0.5%
EPS F1 Est- 4 week change	0.2%
Expected Report Date	02/04/2020
Earnings ESP	-0.3%
P/E TTM	23.2
P/E F1	18.5
PEG F1	2.3
P/S TTM	4.8

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2020	4,632 E	4,741 E	4,723 E	5,110 E	19,221 E
2019	1,728 A	1,865 A	4,431 A	4,816 E	18,090 E
2018	1,568 A	1,666 A	1,542 A	1,666 A	

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2020	\$2.57 E	\$2.77 E	\$2.79 E	\$2.88 E	\$11.35 E
2019	\$2.11 A	\$2.44 A	\$2.58 A	\$2.80 E	\$10.00 E
2018	\$1.67 A	\$1.78 A	\$1.78 A	\$1.96 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 01/03/2020. The reports text is as of 01/06/2020.

Overview

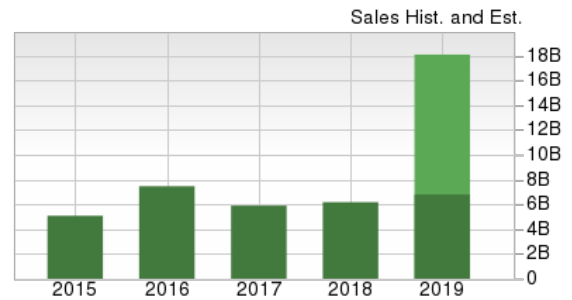
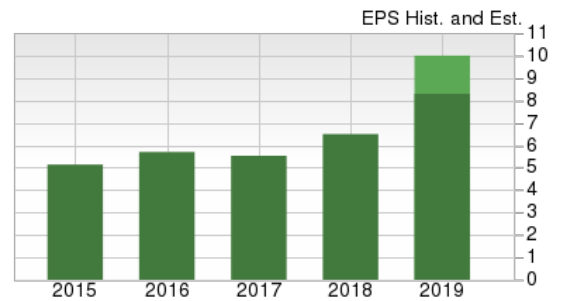
L3Harris Technologies, Inc. was formed following the merger of L3 Technologies and Harris Corporation on Jun 29, 2019. The company is a technology-oriented aerospace and defense player that delivers advanced defense and commercial technologies across air, land, sea, space and cyber domains. It currently operates through four major business segments:

Integrated Mission Systems provides complex ISR systems for large military platforms; advanced electro-optical and infrared, laser imaging and targeting sensor systems; and electrical and electronic systems and integration for maritime power and navigation solutions. In third quarter, this segment contributed 29.3% to the company's total revenues.

Space and Airborne Systems provides space payloads, sensors and full-mission solutions for classified, civil and commercial customers; situational awareness, optical networks and advanced wireless solutions; avionic sensors, hardened electronics, release systems, data links and antennas supporting fixed-wing and rotary platforms; and multi-spectral situational awareness, threat warning and countermeasures capabilities for electronic warfare solutions. In third quarter, this segment contributed 26.2% to the company's total revenues.

Communication Systems provides tactical radio communications, SATCOM terminals and battlefield management networks; broadband secured mobile networked communication equipment and integration; a full suite of helmet and weapon-mounted integrated night vision systems; and radios, applications and equipment. In third quarter, this segment contributed 23.3% to the company's total revenues.

Aviation Systems provides defense aviation products such as precision engagement sensors and systems, small UAVs, antennas and arrays, RF amplifiers and microwave electron devices; commercial aviation products such as airport security and detection solutions and airborne avionics products (for example, traffic collision avoidance and flight recorders); mission communications and networking solutions. In third quarter, this segment contributed 21.4% to the company's total revenues.



Reasons To Buy:

▲ The latest merger between L3 Technologies and Harris Corp has resulted in a global aerospace and defense technology innovator, which delivers end-to-end solutions to meet customers' mission-critical needs. The deal amalgamated L3 Technologies, a prime contractor in ISR systems, aircraft sustainment, communication, electronic and sensor systems, with technology company Harris Corp. The new company is expected to come up with \$18 billion in annualized revenue, on completion of the integration, with customers in over 130 countries. We expect the merger to offer the new company improved economies of scale, considering the optimistic investment stance adopted lately by the U.S. administration in the nation's aerospace-defense industry.

Disciplined divestment strategy, solid financial position and consolidated operational strength to boost L3Harris' growth

▲ L3Harris, post its formation, continues to follow a disciplined divestment strategy in line with both L3 Technologies and Harris' plans to efficiently focus on its core operations. To this end, in September, L3Harris completed the divestiture of the Harris Night Vision business to Elbit Systems for \$350 million in cash. The company recorded a pre-tax gain of \$229 million, following the completion of the deal. L3Harris will use the proceeds from the sale to pre-fund L3Harris pension plans and return cash to its shareholders.

▲ In July, L3Harris's management approved a 10% increase in quarterly cash dividend rate to 75 cents per share, corresponding to an increase in the annualized rate from \$2.74 to \$3.00. This represents an increase of 15% for legacy L3 shareholders. The increase has been effective from third-quarter of 2019, and the company expects to further review its annual cash dividend rate in the first quarter of 2020, as it transitions to the calendar year financial reporting. In the past year, L3Harris has moved up 59.8% compared with its industry's 25.6% growth.

In addition, management approved a new \$4 billion share repurchase authorization. During the third quarter, L3Harris returned \$922 million to shareholders including \$750 million in share repurchases, thereby keeping its track to buy back \$1.5 billion of shares in the second half of 2019. Such impressive capital deployment program is indicative of the combined company's financial flexibility in matters of incremental dividends and ongoing share repurchases. This commitment toward delivering value to shareholders should attract more investors to choose L3Harris' stocks, in the coming days.

Reasons To Sell:

- ▼ At the end of September 2019, L3Harris had \$7 billion of long-term debt outstanding and approximately \$2.1 billion of unfunded defined benefit plans liability. Management expects the unfunded defined benefit plans liability to increase substantially once the initial accounting for the transaction is calculated. Consequently, investors may get attracted to other growth stocks that bear lower debt level to avoid losses. In fact, the company has underperformed its industry in the past three months, reflecting investors' skepticism associated with its huge debt level.
- ▼ During the third quarter, L3Harris Corp incurred \$373 million of merger-related transaction and integration costs. This cost can be expected to increase as the combined company progress in the integration procedure. Such rising costs may hurt L3Harris' bottom line in initial years of integration.
- ▼ Rising crude oil prices, which are at their highest level since late 2014 and escalating labor costs along with the ongoing U.S.-China trade war are likely to remain the biggest challenges for legacy as well as low-cost airlines to maintain profitability level. This, in turn, has the potential to impact air transport, regional and business aircraft utilization rates and pilot training needs. Such factors have discouraged growth potential of the aviation industry and forced the International Air Transport Association (IATA) to downgrade its 2019 outlook for global air transport industry. Also U.S. air fares have increased significantly over the past few months.

Unfavorable debt level, rising merger related cost and rising crude oil price might mar the stock's growth

As a result of the latest merger, L3Harris' portfolio includes commercial aviation products, systems and services business. The aforementioned downturns in the global demand for air travel might impact new aircraft production and orders, and global flying hours, which pose a threat to L3Harris' growth.

Last Earnings Report

L3Harris Technologies Q3 Earnings Top, EPS View Up

L3Harris Technologies adjusted earnings from continuing operations in third-quarter 2019 came in at \$2.58 per share, which surpassed the Zacks Consensus Estimate of \$2.39 by 7.9%. The bottom line also increased 26.5% from the year-ago quarter's figure of \$2.04.

Excluding one-time items, the company reported GAAP earnings of \$1.90 compared with \$1.78 registered in the year-ago quarter.

The year-over-year uptick can be attributed to higher volume from the L3Harris merger, strong operational performance, integration savings and the gain on the sale of the Harris Night Vision business.

Total Revenues

In the quarter under review, the company's revenues came in at \$4.43 billion, falling short of the Zacks Consensus Estimate of \$4.45 billion by 0.5%.

Backlog

Backlog in the reported quarter totaled \$16.5 billion, reflecting 10% rise from the year-ago quarter.

Integrated Mission Systems: Net sales at the segment improved 10% to \$1,303 million from the prior-year quarter's \$1,186 million driven by strength in ISR missionization on the Compass Call Cross Deck program and special mission aircraft for the U.S. government. Also increased demand for Wescam turret systems boosted this segment's top line.

Operating income came in at \$180 million compared with \$145 million in the year-ago quarter. Moreover, operating margin expanded 160 basis points (bps) to 13.8%.

Space and Airborne Systems: The segment recorded net sales of \$1,162 million in the third quarter, up 20% year over year. The upside can be attributed to double-digit growth in each of this segment's businesses, Electronic Warfare (EW), Avionics, Space, and Intel and Cyber.

Operating income increased to \$226 million from \$164 million in the year-ago quarter. Operating margin expanded 250 bps to 19.4%.

Communication Systems: Net sales at the segment rose 11% to \$1,032 million on account of strong growth in Tactical Communications, Integrated Vision Systems and Public Safety businesses.

Operating income increased to \$234 million from \$199 million. Operating margin contracted 140 bps to 22.7%.

Aviation Systems: Net sales at the segment slipped 0.5% to \$948 million on account of a decline in Commercial Training Solutions and competitive loss of the USAF C-17 contract.

Operating income increased to \$127 million from \$96 million. Operating margin contracted 330 bps to 13.4%.

Financial Position

As of Sep 30, 2019, L3Harris had \$1,001 million in cash and cash equivalents compared with \$343 million as of Dec 28, 2018.

Long-term debt as of Sep 30, 2019 was \$6,307 million compared with \$3,411 million as of Dec 28, 2018.

Net cash flow from operating activities amounted to \$81 million at the end of the third quarter compared with the year-ago cash flow of \$117 million.

In the reported, L3Harris returned \$922 million to shareholders through \$750 million in share repurchases and \$172 million in dividends.

2019 View

L3Harris updated its financial guidance for 2019. The company expects to generate revenues of \$18.1 billion compared with the earlier guided range of \$18.0-\$18.1 billion. The current Zacks Consensus Estimate for the company's full-year revenues, pegged at \$18.06 billion, lies above the company guided figure.

The company increased its projection for 2019 adjusted earnings to \$10 per share from the previously guided range of \$9.60-\$9.70 per share. The current Zacks Consensus Estimate for the company's full-year earnings, pegged at \$9.67 billion, lies much below the company guided figure.

Additionally, L3Harris now expects net cash from operating activities to be \$1.95 billion compared with the prior guidance of \$2.26-\$2.31 billion. Moreover, it expects to generate adjusted free cash flow of \$2.35 billion compared with the previous range of \$2.30-\$2.35 billion.

Quarter Ending **09/2019**

Report Date	Oct 30, 2019
Sales Surprise	-0.45%
EPS Surprise	6.09%
Quarterly EPS	2.58
Annual EPS (TTM)	9.09

Valuation

L3Harris's shares are up 14.8% in the past six months period and up 59.8% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Aerospace sector are up 4.4% and 7.7% in the past six months period, respectively. Over the past year, the Zacks sub-industry and sector are up 25.6% and 32%, respectively.

The S&P 500 index is up 10.4% in the past six months period and 28.5%, respectively, in the past year.

The stock is currently trading at 18.51X forward 12-month earnings, which compares to 16.76X for the Zacks sub-industry, 17.08X for the Zacks sector and 18.71X for the S&P 500 index.

Over the past five years, the stock has traded as high as 25.9X and as low as 11.55X, with a 5-year median of 17.83X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$223 price target reflects 20.20X earnings value.

The table below shows summary valuation data for LHX

Valuation Multiples - LHX					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	18.51	16.76	17.08	18.71
	5-Year High	25.9	22.53	21.56	19.34
	5-Year Low	11.55	14.53	14.28	15.17
	5-Year Median	17.83	16.94	16.83	17.44
P/S F12M	Current	2.42	1.44	1.25	3.47
	5-Year High	6.11	1.59	1.37	3.47
	5-Year Low	1.11	0.92	0.79	2.54
	5-Year Median	2.28	1.21	1.05	3
P/B TTM	Current	2.03	12.05	9	4.41
	5-Year High	7.54	24.02	13.66	4.45
	5-Year Low	1.86	6.6	5.05	2.85
	5-Year Median	4.58	13.5	8.91	3.6

As of 01/03/2020

Industry Analysis Zacks Industry Rank: Top 12% (31 out of 252)



Top Peers

Heico Corporation (HEI)	Outperform
Leidos Holdings, Inc. (LDOS)	Outperform
Teledyne Technologies Incorporated (TDY)	Outperform
General Dynamics Corporation (GD)	Neutral
Lockheed Martin Corporation (LMT)	Neutral
Northrop Grumman Corporation (NOC)	Neutral
Raytheon Company (RTN)	Neutral
Transdigm Group Incorporated (TDG)	Neutral

Industry Comparison Industry: Aerospace - Defense				Industry Peers		
	LHX Neutral	X Industry	S&P 500	LDOS Outperform	LMT Neutral	NOC Neutral
VGM Score	F	-	-	A	B	B
Market Cap	46.53 B	10.78 B	23.66 B	14.08 B	116.70 B	63.20 B
# of Analysts	6	5	13	6	9	7
Dividend Yield	1.43%	0.87%	1.79%	1.37%	2.32%	1.41%
Value Score	D	-	-	B	C	C
Cash/Price	0.02	0.03	0.04	0.05	0.02	0.02
EV/EBITDA	118.88	14.73	13.88	16.44	16.54	15.13
PEG Ratio	2.32	2.35	1.99	2.43	2.41	1.25
Price/Book (P/B)	2.03	4.33	3.36	4.33	29.64	6.49
Price/Cash Flow (P/CF)	21.91	16.44	13.62	15.90	18.61	14.07
P/E (F1)	18.54	17.99	18.74	18.25	17.05	16.30
Price/Sales (P/S)	4.80	1.31	2.67	1.31	2.00	1.90
Earnings Yield	5.39%	5.48%	5.32%	5.48%	5.86%	6.14%
Debt/Equity	0.31	0.77	0.72	1.00	3.21	1.55
Cash Flow (\$/share)	9.61	3.73	6.94	6.26	22.24	26.65
Growth Score	F	-	-	A	A	B
Hist. EPS Growth (3-5 yrs)	10.80%	10.80%	10.56%	14.25%	14.78%	22.40%
Proj. EPS Growth (F1/F0)	36.92%	13.55%	7.41%	9.04%	12.19%	12.87%
Curr. Cash Flow Growth	23.01%	18.22%	14.83%	1.52%	24.70%	61.17%
Hist. Cash Flow Growth (3-5 yrs)	7.97%	7.64%	9.00%	37.15%	6.70%	14.12%
Current Ratio	1.49	1.22	1.23	1.16	1.28	1.29
Debt/Capital	23.74%	46.46%	42.92%	49.88%	76.27%	60.86%
Net Margin	12.02%	6.36%	11.08%	6.25%	10.26%	9.05%
Return on Equity	16.42%	16.88%	17.10%	21.12%	221.59%	39.12%
Sales/Assets	0.56	0.92	0.55	1.17	1.23	0.84
Proj. Sales Growth (F1/F0)	6.25%	5.34%	4.20%	6.47%	5.31%	5.34%
Momentum Score	B	-	-	A	C	B
Daily Price Chg	3.52%	0.43%	-0.61%	0.87%	3.60%	5.43%
1 Week Price Chg	0.86%	0.33%	0.13%	0.22%	1.84%	0.15%
4 Week Price Chg	8.83%	5.29%	2.60%	10.59%	7.20%	8.88%
12 Week Price Chg	0.26%	9.59%	8.87%	19.78%	6.94%	1.70%
52 Week Price Chg	61.84%	39.54%	29.34%	93.80%	60.32%	56.31%
20 Day Average Volume	1,066,388	458,085	1,603,615	846,506	784,596	760,707
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	0.23%	0.00%	0.00%	1.18%	0.00%	0.39%
(F1) EPS Est 12 week change	2.63%	-0.25%	-0.57%	3.19%	-3.74%	2.69%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%

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	D
Growth Score	F
Momentum Score	B
VGM Score	F

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

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