

## L3Harris Technology (LHX)

**\$176.40** (As of 09/10/20)

Price Target (6-12 Months): **\$187.00**

Long Term: 6-12 Months

**Zacks Recommendation:**
**Neutral**

(Since: 09/09/19)

Prior Recommendation:

Short Term: 1-3 Months

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

**3-Hold**

Zacks Style Scores:

VGM:B

Value: C

Growth: B

Momentum: A

### Summary

L3Harris second quarter of 2020 earnings surpassed the Zacks Consensus Estimate but revenues missed the mark. The company follows a disciplined divestment strategy, which is expected to boost its cash flow account. The company made net synergy savings of \$60 million in the second quarter. L3Harris delivered \$60 million of net synergies in second quarter. The company's shares have outperformed its industry in the past year. However, the expanded tariff on import of aluminum by the U.S. administration may increase the input cost of aerospace and defense stocks like L3Harris. COVID-19 and its persistent effect on the commercial aviation market are concerns for the company's commercial business. Also, the pandemic impacts are pushing up its operating expenses that might weigh on its bottom line.

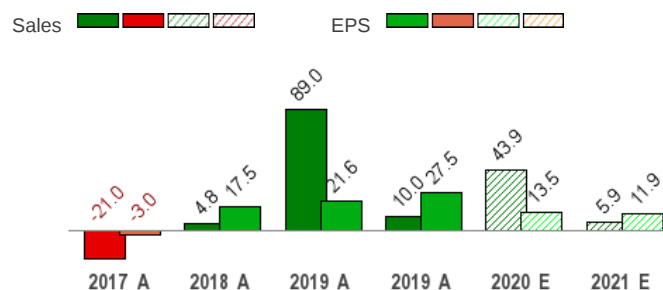
### Price, Consensus & Surprise



### Data Overview

|                                |                            |
|--------------------------------|----------------------------|
| 52-Week High-Low               | \$230.99 - \$142.01        |
| 20-Day Average Volume (Shares) | 1,234,510                  |
| Market Cap                     | \$38.1 B                   |
| Year-To-Date Price Change      | -10.9%                     |
| Beta                           | 0.69                       |
| Dividend / Dividend Yield      | \$3.40 / 1.9%              |
| Industry                       | Aerospace - Defense        |
| Zacks Industry Rank            | Bottom 8% (230 out of 251) |

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



|                               |       |
|-------------------------------|-------|
| Last EPS Surprise             | 8.0%  |
| Last Sales Surprise           | -0.4% |
| EPS F1 Estimate 4-Week Change | 0.5%  |
| Expected Report Date          | NA    |
| Earnings ESP                  | 0.4%  |
| P/E TTM                       | 16.0  |
| P/E F1                        | 15.4  |
| PEG F1                        | 1.9   |
| P/S TTM                       | 2.1   |

### Sales Estimates (millions of \$)

|      | Q1      | Q2      | Q3      | Q4      | Annual*  |
|------|---------|---------|---------|---------|----------|
| 2021 | 4,850 E | 4,770 E | 4,779 E | 5,286 E | 19,593 E |
| 2020 | 4,626 A | 4,445 A | 4,511 E | 4,912 E | 18,494 E |
| 2019 | 1,728 A | 1,865 A | 4,431 A | 4,832 A | 12,856 A |

### EPS Estimates

|      | Q1       | Q2       | Q3       | Q4       | Annual*   |
|------|----------|----------|----------|----------|-----------|
| 2021 | \$3.07 E | \$3.12 E | \$3.17 E | \$3.58 E | \$12.80 E |
| 2020 | \$2.80 A | \$2.83 A | \$2.72 E | \$3.12 E | \$11.44 E |
| 2019 | \$2.11 A | \$2.44 A | \$2.58 A | \$2.85 A | \$10.08 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 09/10/2020. The reports text is as of 09/11/2020.

## Overview

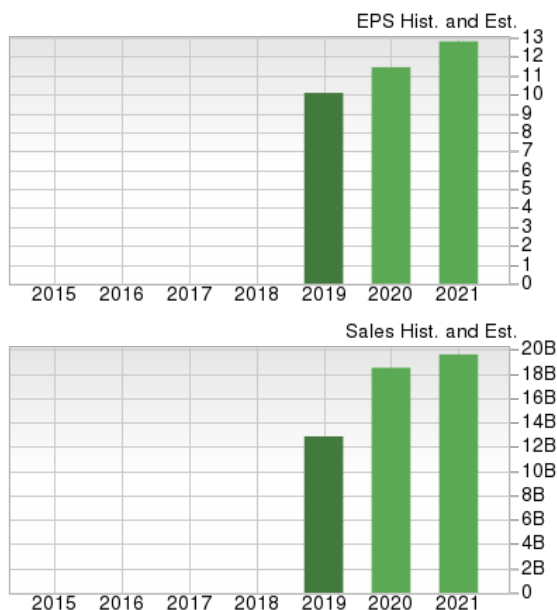
L3Harris Technologies, Inc. was formed following the merger of L3 Technologies and Harris Corporation on Jun 29, 2019. The company is a technology-oriented aerospace and defense player that delivers advanced defense and commercial technologies across air, land, sea, space and cyber domains. It currently 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 2019, this segment contributed 21.8% 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 2019, this segment contributed 33.7% 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 2019, this segment contributed 26% 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 2019, this segment contributed 18.4% to the company's total revenues. The total revenues for 2019 consisted of \$0.09 million of corporate eliminations and \$0.1 million of other non-reportable business segments' revenues.



Source: Zacks Investment Research

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## 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.

**Disciplined divestment strategy, solid capital deployment policy and strong cash position to boost L3Harris' growth**

As of July 3, 2020, the integration is progressing ahead of plan. L3Harris made net synergy savings of \$60 million in the second quarter and \$115 million yeartodate. Offsetting COVID-19 impacts, the company currently expects to deliver \$185 million in net savings by 2020-end, up \$20 million from its prior estimate, largely driven a steady ramp in savings from the supply chain, shared services and benefits. It targets \$300 million net savings, \$500 million in total, in 2021, a year ahead of plan. 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.

- ▲ Coming to quarterly highlights, U.S. Department of Defense (DoD) tactical modernization momentum continued for L3Harris, as the company won a \$95 million award for an additional low rate production contract on the U.S. army's HMS Manpack. After completion of the operational testing early next year, management projects to clinch a full rate production award against the previously announced IDIQ of nearly \$13 billion. It also won a \$900 million contract to develop and manage simulator requirements and standards across the Air Force's training portfolio. Moreover, in July, L3Harris was selected as the prime contractor for the medium unmanned surface vehicle for the U.S. Navy. Further, the company is in the process of finalizing its position on the U.S navy's frigate program as a system integrator, withan initial 10-ship contractof over \$300 million. These awards indicate solid revenue generation prospects for this defense major over the long run.
- ▲ Post its formation, L3Harris 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, it is imperative to mention that on Jul 31, L3Harris complete the divestment of its EOTech business for \$42 million. On May 15, the company completed the divestiture of its Applied Kilovolts and Analytical Instrumentation business for net cash proceeds of \$12 million. On May 4, L3Harris completed thesale of its airport security business for \$1 billion to Leidos Holdings. In July 2020, the company decided to divest another business from its Aviation Systems segment, which is expected to be completed by 2020-end. Such divestment strategies are expected to boost the company's cash flow account, thereby driving operations and allowing it to make notable share repurchases.
- ▲ L3Harris' cash and cash equivalents were \$1,947 million as of Jul 3, 2020, compared with \$663 million as of Apr 3, 2020. While its cash reserve improved significantly on a sequential basis, its long-term debt of\$7.1 billion remained well above the cash balance. Nevertheless, its current debt of\$668 million, as of Jul 3, 2020, remained well below its cash reserve. This reflects a strong solvency position, at least in the short term.

Moreover, the company's current ratio of 1.51, as of Jul 3, 2020, improved sequentially from 1.41. Also, this ratio being more than 1 indicates the company's ability to pay off its debt obligation. Its strong performance along with divestiture proceeds will enable it to achieve its prior commitment to return capital to shareholders in the third quarter. In the longer term, L3Harris targets to generate \$3 billion of free cash flow in 2022, driven in part by continued improvement in working capital. Such impressive financial stability may have boosted investors' confidence in this stock. In the past year, L3Harris has dropped 15.8% compared to the industry's 34.5% decline.

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## Reasons To Sell:

▼ In January 2020, the Trump administration announced plans to expand its existing tariffs on imports of steel and aluminum from Feb 8. Steel and aluminum derivatives now come under the tariff mandate. This tariff expansion is expected to deal a heavy blow to the U.S. aerospace and defense industry, which relies heavily on imported aluminum. In 2018, when the initial tariff was imposed, the AIA had expressed concern by saying that such a tariff will raise cost and disrupt the supply chain. Now that tariffs are being imposed on derivatives as well, input costs are expected to rise even more, thereby hurting the growth prospects of aerospace and defense stocks like L3Harris.

Impact of increased tariff on import of aluminum and COVID-19 impact on its commercial business might mar the stock's growth

▼ A comparative analysis of the company's historical EV/EBITDA TTM ratio reflects a relatively gloomy picture, which might be a cause for investors' concern. Evidently, the stock has a current trailing 12-month EV/EBITDA ratio of 18.64. This level lies near the high end of its past year range. Moreover, the company's EV/EBITDA TTM ratio remained above the industry's EV/EBITDA TTM ratio of 11.72 in a year.

▼ The novel coronavirus outbreak and its persistent effect on the commercial aviation market remains a cause of concern for the company's commercial business growth. Notably, the pandemic has significantly reduced demand for flight training, flight simulators and commercial avionics products in L3Harris' Commercial Aviation Solutions sector within its Aviation Systems segment. As a result, the company had to temporarily close some of its flight training facilities in Europe and several other locations. During the second quarter, L3Harris incurred \$14 million of restructuring charges, including workforce reductions and other exit costs within its Aviation Systems segment associated with the COVID-19-related downturn in Commercial Aviation Solutions.

It also recorded \$69 million of charges for impairment of goodwill and other assets and other COVID-19-related impacts, within the commercial market. With commercial training representing roughly 40% of L3Harris' total sales, the COVID-19 impacts are expected to hurt the company's results. Notably, the company expects revenues in its Commercial Aviation Solutions sector to decrease approximately \$300 million in 2020.

▼ In the wake of the ongoing pandemic, L3Harris' management is focused on mitigating the effects of COVID-19, which has required and will continue to require, a large investment of time and resources across its enterprise. While this will increase cost of operations for the company, it also will delay other value-added services or initiatives. Evidently, during the second quarter, the company witnessed a 160% hike in both cost of product sales and services as well as engineering, selling and administrative expenses. Such rising expenses will weigh on its bottom line growth. Additionally, many of its employees are currently working remotely. The company fears that an extended period of remote work arrangements could strain business continuity plans, introduce operational risk, including but not limited to cyber security risks, and impair its ability to manage business.

## Last Earnings Report

### L3Harris Technologies Beats on Q2 Earnings, Tweaks View

L3Harris Technologies second-quarter 2020 adjusted earnings came in at \$2.83 per share, which surpassed the Zacks Consensus Estimate of \$2.62 by 8%. The bottom line also increased 13% from the year-ago quarter's \$2.51.

Including one-time items, the company reported GAAP earnings of \$1.30 per share compared with \$2.21 in the year-ago quarter.

The year-over-year downside in GAAP earnings can be attributed to divestiture-related charges, COVID-19-related impacts and amortization of merger-related intangibles.

#### Total Revenues

In the quarter under review, the company's revenues came in at \$4,445 million, lagging the Zacks Consensus Estimate of \$4,460 million by 0.4%. However, revenues surged 138% on a year-over-year basis, driven by post-merger inclusion of L3 operations.

#### Segmental Performance

**Integrated Mission Systems:** Net sales at the segment came in at \$1,331 million. On a pro forma basis, revenues were up 7.3%, driven by growth in Electro Optical and Maritime units.

Operating income, on a pro-forma basis, came in at \$224 million compared with \$162 million in the year-ago quarter. Moreover, operating margin expanded 370 basis points (bps) to 16.8%.

**Space and Airborne Systems:** The segment recorded net sales of \$1,249 million in the second quarter, up 23% year over year. On a pro-forma basis, revenues increased 4.1% year over year driven by a ramp up in modernization on the F-35 platform in Avionics and classified growth in Intel and Cyber.

Operating income increased to \$235 million from \$228 million in the year-ago quarter. Operating margin contracted 20 bps to 18.8%.

**Communication Systems:** Net sales at the segment rose 83% to \$1,112 million. On a pro-forma basis, revenues increased 2.4% year over year due to ramp up in U.S. DoD modernization programs in Tactical Communications and Integrated Vision Systems.

Operating income increased to \$265 million from \$239 million in the year-ago quarter. Operating margin expanded 180 bps to 23.8%.

**Aviation Systems:** Net sales at the segment came in at \$800 million down 17% on a pro-forma basis, on account of COVID-19-related impacts in the commercial aviation business.

Operating income decreased to \$31 million from \$109 million. Operating margin contracted a huge 740 bps to 3.9%.

#### Financial Position

As of Jul 3, 2020, L3Harris had \$1,947 million in cash and cash equivalents compared with \$824 million as of Jan 3, 2020.

Long-term debt as of Jul 3, 2020 was \$6,273 million compared with \$6,694 million as of Jan 3, 2020.

Net cash inflow from operating activities amounted to \$1,335 million at the end of second-quarter 2020 compared with the year-ago cash inflow of \$716 million.

#### 2020 View

L3Harris made some changes to its 2020 guidance. The company continues to expect organic revenues to grow in the range of 3-5% and projects revenues in the range of \$18.2-\$18.6 billion. The Zacks Consensus Estimate for revenues of \$18.6 billion is in line with the higher end of the company provided range.

Adjusted earnings per share for 2020 are still projected in the range of \$11.15-\$11.55. The Zacks Consensus Estimate for earnings of \$11.28 lies below the midpoint of the company's guidance.

However, the company has decreased its GAAP EPS guidance to the range of \$6.03-\$6.43 from the previous guidance of \$6.95-\$7.35.

Operating cash flow and adjusted free cash flow are still expected in the range of \$2.8-\$2.9 billion and \$2.6-\$2.7 billion, respectively.

| Quarter Ending   | 06/2020      |
|------------------|--------------|
| Report Date      | Jul 31, 2020 |
| Sales Surprise   | -0.36%       |
| EPS Surprise     | 8.02%        |
| Quarterly EPS    | 2.83         |
| Annual EPS (TTM) | 11.06        |

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## Recent News

On **June 17, 2020**, L3Harris Technologies announced its new man-portable Iver4 580 unmanned undersea vehicle (UUV). The new Iver4 580 is the second vehicle in the Iver4 family of next-generation UUVs to address a wide variety of customer missions, including survey; multi-domain intelligence, surveillance and reconnaissance; anti-submarine warfare; seabed warfare and mine warfare. Built with Iver4 advanced technology, the Iver4 580 features a full suite of sensors in a portable size (5.8-inch diameter and 82-inch length) and small mission footprint for rapid deployment from any vessel.

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## Valuation

L3Harris' shares are down 10.9% in the year to date period and 15.8% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Aerospace sector are down 26% and 35.1% in the year to date period, respectively. Over the past year, the Zacks sub-industry is down 34.5% and the Zacks Aerospace sector witnessed a 38.3% decline.

The S&P 500 index is up 3.8% in the year to date period and 11.5% in the past year.

The stock is currently trading at 14.3X forward 12-month earnings, which compares to 19.7X for the Zacks sub-industry, 20.3X for the Zacks sector and 22.3X for the S&P 500 index.

Over the past five years, the stock has traded as high as 25.9X and as low as 11.6X, with a 5-year median of 18.3X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$187 price target reflects 15.1X 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       | 14.28 | 19.69        | 20.27  | 22.17   |
|                           | 5-Year High   | 25.9  | 22.54        | 21.04  | 23.44   |
|                           | 5-Year Low    | 11.55 | 14.52        | 14.17  | 15.26   |
|                           | 5-Year Median | 18.25 | 17.85        | 17.33  | 17.63   |
| P/S F12M                  | Current       | 1.97  | 1.23         | 1.64   | 4.08    |
|                           | 5-Year High   | 6.11  | 1.64         | 1.69   | 4.29    |
|                           | 5-Year Low    | 1.11  | 0.95         | 0.92   | 3.11    |
|                           | 5-Year Median | 2.31  | 1.28         | 1.23   | 3.66    |
| EV/EBITDA TTM             | Current       | 15.41 | 30.47        | 15.95  | 14.42   |
|                           | 5-Year High   | 30.49 | 32.29        | 16.69  | 15.6    |
|                           | 5-Year Low    | 9.59  | 8.16         | 7.38   | 9.51    |
|                           | 5-Year Median | 18.06 | 11.83        | 10.61  | 13      |

As of 09/10/2020 Source: Zacks Investment Research

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## Industry Analysis Zacks Industry Rank: Bottom 8% (230 out of 251)



Source: Zacks Investment Research

## Top Peers

| Company (Ticker)                         | Rec     | Rank |
|------------------------------------------|---------|------|
| General Dynamics Corporation (GD)        | Neutral | 3    |
| Heico Corporation (HEI)                  | Neutral | 3    |
| Leidos Holdings, Inc. (LDOS)             | Neutral | 3    |
| Lockheed Martin Corporation (LMT)        | Neutral | 3    |
| Northrop Grumman Corporation (NOC)       | Neutral | 3    |
| Transdigm Group Incorporated (TDG)       | Neutral | 3    |
| Teledyne Technologies Incorporated (TDY) | Neutral | 2    |
| Textron Inc. (TXT)                       | Neutral | 3    |

The positions listed should not be deemed a recommendation to buy, hold or sell.

| Industry Comparison Industry: Aerospace - Defense |           |            |           | Industry Peers |          |         |
|---------------------------------------------------|-----------|------------|-----------|----------------|----------|---------|
|                                                   | LHX       | X Industry | S&P 500   | LDOS           | LMT      | NOC     |
| Zacks Recommendation (Long Term)                  | Neutral   | -          | -         | Neutral        | Neutral  | Neutral |
| Zacks Rank (Short Term)                           | 3         | -          | -         | 3              | 3        | 3       |
| VGM Score                                         | B         | -          | -         | A              | B        | A       |
| Market Cap                                        | 38.14 B   | 11.00 B    | 22.97 B   | 12.21 B        | 105.98 B | 55.02 B |
| # of Analysts                                     | 9         | 6          | 14        | 9              | 9        | 8       |
| Dividend Yield                                    | 1.93%     | 0.01%      | 1.65%     | 1.58%          | 2.53%    | 1.76%   |
| Value Score                                       | C         | -          | -         | B              | B        | B       |
| Cash/Price                                        | 0.05      | 0.09       | 0.07      | 0.05           | 0.03     | 0.07    |
| EV/EBITDA                                         | 95.85     | 9.53       | 12.97     | 12.68          | 12.69    | 15.90   |
| PEG F1                                            | 1.97      | 2.27       | 2.92      | 1.47           | 2.27     | NA      |
| P/B                                               | 1.71      | 3.14       | 3.16      | 3.44           | 27.99    | 5.67    |
| P/CF                                              | 18.36     | 10.40      | 12.49     | 12.22          | 14.41    | 11.96   |
| P/E F1                                            | 15.77     | 15.71      | 21.20     | 15.79          | 15.71    | 14.69   |
| P/S TTM                                           | 2.08      | 1.05       | 2.39      | 1.05           | 1.68     | 1.59    |
| Earnings Yield                                    | 6.49%     | 3.95%      | 4.55%     | 6.33%          | 6.36%    | 6.81%   |
| Debt/Equity                                       | 0.28      | 0.75       | 0.70      | 1.17           | 3.22     | 1.47    |
| Cash Flow (\$/share)                              | 9.61      | 2.73       | 6.93      | 7.03           | 26.30    | 27.58   |
| Growth Score                                      | B         | -          | -         | A              | A        | A       |
| Historical EPS Growth (3-5 Years)                 | 16.25%    | 14.85%     | 10.41%    | 14.85%         | 18.30%   | 23.60%  |
| Projected EPS Growth (F1/F0)                      | 38.01%    | -7.43%     | -4.75%    | 5.20%          | 9.91%    | 5.89%   |
| Current Cash Flow Growth                          | 23.01%    | 11.64%     | 5.26%     | 6.19%          | 18.08%   | 2.21%   |
| Historical Cash Flow Growth (3-5 Years)           | 7.97%     | 7.38%      | 8.49%     | 6.45%          | 9.70%    | 14.43%  |
| Current Ratio                                     | 1.51      | 1.31       | 1.35      | 0.89           | 1.31     | 1.35    |
| Debt/Capital                                      | 22.01%    | 42.98%     | 42.95%    | 53.90%         | 76.28%   | 59.48%  |
| Net Margin                                        | 7.21%     | 5.59%      | 10.25%    | 5.26%          | 10.25%   | 6.91%   |
| Return on Equity                                  | 10.92%    | 10.92%     | 14.59%    | 23.81%         | 182.05%  | 40.24%  |
| Sales/Assets                                      | 0.48      | 0.79       | 0.50      | 1.11           | 1.29     | 0.82    |
| Projected Sales Growth (F1/F0)                    | 48.29%    | 0.00%      | -1.42%    | 11.78%         | 8.28%    | 4.91%   |
| Momentum Score                                    | A         | -          | -         | C              | F        | F       |
| Daily Price Change                                | -2.46%    | -1.53%     | -1.51%    | -1.46%         | -1.59%   | -2.77%  |
| 1-Week Price Change                               | 1.02%     | -2.18%     | -1.28%    | -3.09%         | -2.67%   | -1.66%  |
| 4-Week Price Change                               | -2.53%    | -6.24%     | -2.05%    | -8.99%         | -2.60%   | -2.54%  |
| 12-Week Price Change                              | -6.29%    | -4.64%     | 4.48%     | -13.52%        | 0.19%    | 3.84%   |
| 52-Week Price Change                              | -15.77%   | -23.42%    | -1.95%    | -0.52%         | -1.95%   | -9.64%  |
| 20-Day Average Volume (Shares)                    | 1,234,510 | 491,368    | 1,834,261 | 850,574        | 908,156  | 520,750 |
| EPS F1 Estimate 1-Week Change                     | 0.17%     | 0.00%      | 0.00%     | 0.00%          | 0.02%    | -0.10%  |
| EPS F1 Estimate 4-Week Change                     | 0.46%     | 0.00%      | 0.00%     | 0.49%          | 0.02%    | 0.19%   |
| EPS F1 Estimate 12-Week Change                    | 1.20%     | 0.00%      | 4.05%     | 4.59%          | 2.03%    | 1.54%   |
| EPS Q1 Estimate Monthly Change                    | -0.01%    | -0.01%     | 0.00%     | -2.04%         | -0.28%   | -0.71%  |

Source: Zacks Investment Research

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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 maintain a 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    | C |
| Growth Score   | B |
| Momentum Score | A |
| VGM Score      | 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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## Disclosures

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Investing involves risk; principal loss is possible. There is no guarantee that companies that can issue dividends will declare, continue to pay or increase dividends.

## Glossary of Terms and Definitions

**52-Week High-Low:** The range of the highest and lowest prices at which a stock has traded during the past year. This range is determined based on the stock's daily closing price which may differ from the intra-day high or low. Many investors use it as a technical indicator to determine a stock's current value and future price movement. The idea here is that if price breaks out from the 52-week range, in either direction, the momentum may continue in the same direction.

**20-Day Average Volume (Shares):** The average number of shares of a company traded in a day over the last 20 days. It is a direct indication of a security's overall liquidity. The higher the average daily trading volume, the easier it is to enter or exit the stock at a desired price with more buyers and sellers being available.

**Daily Price Change:** This is the percentage difference between a trading day's closing price and the prior trading day's closing price. This item is updated at 9 p.m. EST each day.

**1-Week Price Change:** This is the percentage change in a stock's closing price over the last 5 trading days. This change reflects the collective buying and selling sentiment over the 1-week period.

A strong weekly price increase for the stock, especially when accompanied by increased volume, is an indication of it gaining momentum.

**4-Week Price Change:** This is the percentage change in a stock's closing price over the last 20 trading days or past 4 weeks. This is a medium-term price change metric and an indication of the stock gaining momentum.

**12-Week Price Change:** This is the percentage change of a stock's closing price over the last 60 trading days or past 12 weeks. Similar to 4-week price change, this is a medium-term price change metric. It shows whether a stock has been enjoying strong investor demand, or if it has been in consolidation, or distress over this period.

**52-Week Price Change:** This is the percentage change in a stock's closing price over the last 260 trading days or past 52 weeks. This long-term price change metric is a good reference point for investors. Some investors seek stocks with the best percentage price change over the last 52 weeks, expecting the momentum to continue.

**Market Cap:** The number of outstanding common shares of a company times its latest price per share. This figure represents a company's size, which indicates various characteristics, including price stability and risk, in which investors could be interested.

**Year-To-Date Price Change:** Change in a stock's daily closing price in the period of time beginning the first day of the current calendar year through to the previous trading day.

**# of Analysts:** Number of EPS estimates used in calculating the current-quarter consensus. These estimates come from the brokerage analysts tracking this stock. However, the number of such analysts tracking this stock may not match the number of estimates, as all brokerage analysts may not come up with an estimate or provide it to us.

**Beta:** A measure of risk commonly used to compare the volatility of a stock to the overall market. The S&P 500 Index is the base for calculating beta and carries a value of 1. A stock with beta below 1 is less risky than the market as a whole. And a stock with beta above 1 is riskier.

**Dividend:** The portion of earnings a company is expected to distribute to its common shareholders in the next 12 months for each share they own. Dividends are usually paid quarterly. Dividend payments reflect positively on a company and help maintain investors' trust. Investors typically find dividend-paying stocks appealing because the dividend adds to any market price appreciation to result in higher return on investment (ROI). Moreover, a steady or increasing dividend payment provides investors a cushion in a down market.

**Dividend Yield:** The ratio of a company's annual dividend to its share price. The annual dividend used in the ratio is calculated based on the most recent dividend paid by the company. Dividend yield is an estimate of the dividend-only return from a stock in the next 12 months. Since dividend itself doesn't change frequently, dividend yield usually changes with a stock's price movement. As a result, often an unusually high dividend yield is a result of weak stock price.

**S&P 500 Index:** The Standard & Poor's 500 (S&P 500) Index is an unmanaged group of securities considered to be representative of the stock market in general. It is a market-capitalization-weighted index of stocks of the 500 largest U.S. companies. Each stock's weight in the index is proportionate to its market value.

**Industry:** One of the 250+ groups that Zacks classifies all stocks into based on the nature of business. These groups are termed as expanded (aka "X") industries and map to their respective (economic) sectors; Zacks has 16 sectors.

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**Zacks Industry Rank:** The Zacks Industry Rank is determined by calculating the average Zacks Rank for all stocks in the industry and then assigning an ordinal rank to it. For example, an industry with an average Zacks Rank of 1.6 is better than an industry with an average Zacks Rank of 2.3. So, the industry with the better average Zacks Rank would get a better Zacks Industry Rank. If an industry has the best average Zacks Rank, it would be considered the top industry (1 out of 250+), which would place it at the top 1% of Zacks-ranked industries. Studies have shown that roughly half of a stock's price movement can be attributed to the industry group it belongs to. In fact, the top 50% of Zacks-ranked industries outperforms the bottom 50% by a factor of more than 2 to 1.

**Last EPS Surprise:** The percentage deviation of a company's last reported earnings per share from the Zacks Consensus Estimate. Companies with a positive earnings surprise are more likely to surprise again in the future (or miss again if they recently missed).

**Last Sales Surprise:** The percentage deviation of a company's last reported sales from the Zacks Consensus Estimate.

**Expected Report Date:** This is an estimated date of a company's next earnings release. The information originated or gathered by Zacks Investment Research from its information providers or publicly available sources is the basis of this estimate.

**Earnings ESP:** The Zacks Earnings ESP compares the Most Accurate Estimate to the Zacks Consensus Estimate for the yet-to-be reported quarter. The Most Accurate Estimate is the most recent version of the Zacks Consensus EPS Estimate. The idea here is that analysts revising their estimates closer to an earnings release have the latest information, which could potentially be more accurate than what they and others contributing to the consensus had predicted earlier. Thus, a positive or negative Earnings ESP reading theoretically indicates the likely deviation of the actual earnings from the consensus estimate. However, the model's predictive power is significant for positive ESP readings only. A positive Earnings ESP is a strong predictor of an earnings beat, particularly when combined with a Zacks Rank #1 (Strong Buy), #2 (Buy) or #3 (Hold). Our research shows that stocks with this combination produce a positive surprise nearly 70% of the time.

**Periods:**

**TTM:** Trailing 12 months. Using TTM figures is an effective way of analyzing the most-recent financial data in an annualized format that helps neutralize the effects of seasonality and other quarter-to-quarter variation.

**F1:** Current fiscal year. This period is used to analyze the estimates for the ongoing full fiscal year.

**F2:** Next fiscal year. This period is used to analyze the estimates for the next full fiscal year.

**F12M:** Forward 12 months. Using F12M figures is an effective way of analyzing the near-term (the following four unreported quarters) estimates in an annualized manner. Instead of typically representing estimates for the full fiscal year, which may not represent the nitty-gritty of each quarter, F12M figures suggest an all-inclusive annualized estimate for the following four quarters. The annualization helps neutralize the potential effects of seasonality and other quarter-to-quarter variations.

**P/E Ratio:** The price-to-earnings ratio measures a company's current market price per share relative to its earnings per share (EPS). Usually, the trailing-12-month (TTM) EPS, current-fiscal-year (F1) EPS estimate, or forward-12-month (F12M) EPS estimate is used as the denominator. In essence, this ratio shows what the market is willing to pay today for each dollar of EPS. In other words, this ratio gives a sense of what the relative value of the company is at the already reported level of earnings or at a future level of earnings.

It is one of the most widely-used multiples for determining the value of a company and helps comparing its valuation with that of a competitor, the industry group or a benchmark.

**PEG Ratio:** The price/earnings to growth ratio is a stock's P/E ratio using current fiscal year (F1) EPS estimate divided by its expected EPS growth rate over the coming 3 to 5 years. This ratio essentially determines a stock's value by factoring in the company's expected earnings growth and is thus believed to provide a more complete picture than just the P/E ratio, particularly for faster-growing companies.

**P/S Ratio:** The price-to-sales ratio is calculated as a company's current price per share divided by trailing 12 months (TTM) sales or revenues per share. This ratio shows what the market is willing to pay today for each dollar of TTM sales per share. The P/S ratio is at times the only valuation metric when the company has yet to become profitable.

**Cash/Price Ratio:** The cash-to-price ratio or Cash Yield is calculated as cash and marketable securities per share divided by the company's current share price. Like the earnings yield, which shows the anticipated yield (or return) on a stock from earnings for each dollar invested, the cash yield does the same, with cash being the source of return instead of earnings. For example, a cash/price ratio of 0.08 suggests a return of 8% or 8 cents for every \$1 investment.

**EV/EBITDA Ratio:** The EV/EBITDA ratio, also known as Enterprise Multiple, is calculated as a company's enterprise value (market capitalization + value of total long-term debt + book value of preferred shares - cash and marketable securities) divided by EBITDA (earnings before interest, taxes, depreciation and amortization). Usually, trailing-12-month (TTM) or forward-12-month (F12M) EBITDA is used as the denominator.

**EV/Sales Ratio:** The enterprise value-to-sales ratio is calculated as a company's enterprise value (market capitalization + value of total long-term debt + book value of preferred shares - cash and marketable securities) divided by annual sales. It is an expansion of the P/S valuation, which uses market value instead of enterprise value. The EV/Sales ratio is perceived as more accurate than P/S, in part, because the market capitalization does not take a company's debt into account when valuing it.

**EV/CF Ratio:** The enterprise value-to-cash flow ratio is calculated as a company's enterprise value (market capitalization + value of total long-term debt + book value of preferred shares - cash and marketable securities) divided by the trailing-12-month (TTM) operating cash flow. It's a measure of how long it would take to buy the entire business if you were able to use all the company's operating cash flow.

The EV/CF ratio is perceived as more accurate than the P/CF ratio, in part, because the market price does not take a company's debt into account when valuing it.

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**EV/FCF Ratio:** The enterprise value-to-free cash flow metric compares a company's enterprise value to its trailing-12-month (TTM) free cash flow (FCF). This metric is very similar to the EV/CF ratio, but is considered a more exact measure owing to the fact that it uses free cash flow, which subtracts capital expenditures (CAPEX) from a company's total operating cash flow, thereby reflecting the actual cash flow available for funding growth activities and payments to shareholders.

**P/EBITDA Ratio:** The P/EBITDA ratio is calculated as a company's per share market value divided by EBITDA (earnings before interest, taxes, depreciation, and amortization). This metric is very similar to the EV/EBITDA ratio, but is considered a little less exact measure as it uses market price, which does not take a company's debt into account. However, since EBITDA is often considered a proxy for cash income, the metric is used as a measure of what the market is willing to pay today for each dollar of the company's cash profitability in the trailing 12 months (TTM) or forward 12 months (F12M).

**P/B Ratio:** The price-to-book ratio is calculated as a company's current price per share divided by its book value (total assets – liabilities – preferred stocks) per share. In short, the book value is how much a company is worth. In other words, it reflects the total value of a company's assets that its common shareholders would receive if it were to be liquidated. So, the P/B ratio indicates whether you're paying higher or lower than what would remain if the company went bankrupt immediately. Investors typically use this metric to determine how a company's stock price stacks up to its intrinsic value.

**P/TB Ratio:** The price-to-tangible-book value ratio is calculated as the per share market value of a company divided by the value of its tangible assets (total assets – liabilities – preferred stocks – intangible assets) per share. Tangible book value is the same thing as book value except it excludes the value of intangible assets to get a step closer to the baseline value of the company.

**P/CF Ratio:** The price-to-cash flow ratio measures a company's per share market price relative to its trailing-12-month (TTM) operating cash flow per share. This metric is used to determine whether a company is undervalued or overvalued relative to another stock, industry or sector. And like the P/E ratio, a lower number is typically considered better from the value perspective.

One of the reasons why P/CF ratio is often preferred over P/E ratio is the fact that operating cash flow adds back non-cash expenses such as depreciation and amortization to net income. This feature helps valuing stocks that have positive cash flow but are not profitable because of large noncash charges.

**P/FCF Ratio:** The price-to-free cash flow ratio is an extension of P/CF ratio, which uses trailing-12-month (TTM) free cash flow per share instead of operating cash flow per share. This metric is considered a more exact measure than P/CF ratio, as free cash flow subtracts capital expenditures (CAPEX) from a company's total operating cash flow, thereby reflecting the actual cash flow available for funding activities that generate additional revenues.

**Earnings Yield:** The earnings yield is calculated as current fiscal year (F1) EPS estimate divided by the company's current share price. The ratio, which is the inverse of the P/E ratio, measures the anticipated yield (or return) from earnings for each dollar invested in a stock today.

For example, earnings yield for a stock, which is trading at \$35 and expected to earn \$3 per share in the current fiscal year (F1), would be 0.0857 ( $3/35 = 0.0857$ ) or 8.57%. In other words, for \$1 invested in the stock today, the yield from earnings is anticipated to be 8.57 cents.

Investors most commonly compare the earnings yield of a stock to that of a broad market index (such as the S&P 500) and prevailing interest rates, such as the current 10-year Treasury yield. Since bonds and stocks compete for investors' dollars, stock investors typically demand a higher yield for the extra risk they assume compared to investors of U.S. Treasury-backed securities that offer virtually risk-free returns. This additional return is referred to as the risk premium.

**Debt/Equity Ratio:** The debt-to-equity ratio is calculated as a company's total liabilities divided by its shareholder equity. This metric is used to gauge a company's financial leverage. In other words, it is a measure of the degree to which a company is financing its operations through debt versus its own funds. The higher the ratio, the higher the risk for shareholders.

However, this ratio is difficult to compare across industry groups where ideal amounts of debt vary. Some businesses are more capital intensive than others and typically require higher debt to finance their operations. So, a company's debt-to-equity ratio should be compared with other companies in the same industry.

**Cash Flow (\$/share):** Cash flow per share is calculated as operating cash flow (after-tax earnings + depreciation + other non-cash charges) divided by common shares outstanding. It is used by many investors as a measure of a company's financial strength. Since cash flow per share takes into consideration a company's ability to generate cash by adding back non-cash expenses, it is regarded by some as a more accurate measure of a company's financial situation than earnings per share, which could be artificially deflated.

**Current Ratio:** The current ratio or liquidity ratio is a company's current assets divided by its current liabilities. It measures a company's ability to pay short-term obligations. A current ratio that is in line with the industry average or slightly higher is generally considered acceptable. A current ratio that is lower than the industry average would indicate a higher risk of distress or default. A higher number is usually better. However, a very high current ratio compared to the industry average could be an indication of inefficient use of assets by management.

**Debt/Capital Ratio:** Debt-to-capital ratio is a company's total debt (interest-bearing debt + both short- and long-term liabilities) divided its total capital (interest-bearing debt + shareholders' equity). It is a measure of a company's financial leverage. All else being equal, the higher the debt-to-capital ratio, the riskier the stock.

However, this ratio can vary widely from industry to industry, the ideal amount of required debt being different. Some businesses are more capital intensive than others and typically require higher debt to finance their operations. So, a company's debt-to-capital ratio should be compared with the same for its industry.

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**Net Margin:** Net margin is calculated as net income divided by sales. It shows how much of each dollar in sales generated by a company translates into profit. For example, if a company's net margin is 15%, its net income is 15 cents for every \$1 of sales it makes.

A change in margin can reflect either a change in business conditions, or a company's cost controls, or both. If a company's expenses are growing faster than sales, its net margin will decline. However, different net margin rates are considered good for different industries, so it's better to compare net margin rates of companies in the same industry group.

**Return on Equity:** Return on equity (ROE) is calculated as trailing-12-month net income divided by trailing-12-month average shareholder equity (including reinvested earnings). This metric is considered a measure of how effectively management is using a company's assets to generate profits. For example, if a company's ROE is 10%, it creates 10 cents profits for every \$1 shareholder equity, which is basically the company's assets minus debt. A company's ROE deemed good or bad depends on what's normal for its peers or industry group.

**Sales/Assets Ratio:** The sales-to-assets ratio or asset utilization ratio or asset turnover ratio is calculated as a company's annual sales divided by average assets (average of assets at the beginning of the year and at the year's end). This metric helps investors understand how effectively a company is using its assets to generate sales. For example, a sales-to-assets ratio of 2.5 indicates that the company generated \$2.50 in sales for every \$1 of assets on its books.

The higher the sales-to-assets ratio, the better the company is performing. However, similar to many other ratios, the asset turnover ratio tends to be higher for companies in certain industries/sectors than in others. So, a company's sales-to-assets ratio should be compared with the same for its industry/sector.

**Historical EPS Growth (3-5 Years):** This is the average annual (trailing-12-month) EPS growth rate over the last 3-5 years. This metric helps investors see how a company's EPS has grown from a long-term perspective.

Note: There are many factors that can influence short-term numbers — a recession will reduce this number, while a recovery will inflate it. The longterm perspective helps smooth out short-term events.

**Projected EPS Growth (F1/F0):** This is the estimated EPS growth rate for the current financial year. It is calculated as the consensus estimate for the current fiscal year (F1) divided by the reported EPS for the last completed fiscal year (F0).

**Current Cash Flow Growth:** It measures the latest year-over-year change in operating cash flow. Cash flow growth tells an investor how quickly a company is generating inflows of cash from operations. A positive change in the cash flow is desired and shows that more 'cash' is coming in than going out.

**Historical Cash Flow Growth (3-5 Years):** This is the annualized change in cash flow over the last 3-5 years. The change in a longer period helps put the current reading into proper perspective. By looking at the rate, rather than the actual dollar value, the comparison across the industry and peers becomes easier.

**Projected Sales Growth (F1/F0):** This metric looks at the estimated sales growth for the current year. It is calculated as sales estimate for the current fiscal year (F1) divided by the reported sales for the last completed fiscal year (F0).

Like EPS growth, a higher rate is better for sales growth. A look at a company's projected sales growth instantly tells you what the outlook is for their products and services. However, different sales growth rates are considered good for different industries, so it's better to compare sales growth rates of companies in the same industry group.

**EPS F1 Estimate 1-Week Change:** The percentage change in the Zacks Consensus EPS estimate for the current fiscal year over the past week. The change in a company's consensus EPS estimate (or earnings estimate revision) has proven to be strongly correlated with the near-term price movement of its shares. It is an integral part of the Zacks Rank.

If a stock's consensus EPS estimate is \$1.10 now versus \$1.00 a week ago, that will be reflected as a 10% upward revision. If, on the other hand, it went from \$1.00 to 90 cents, that would be a 10% downward revision.

**EPS F1 Estimate 4-Week Change:** The percentage change in the Zacks Consensus EPS estimate for the current fiscal year over the past four weeks.

A stock's earnings estimate revision in a 1-week period is important. But it's more meaningful to look at the longer-term revision. And, of course, the 4-week change helps put the 1-week change into proper perspective.

**EPS F1 Estimate 12-Week Change:** The percentage change in the Zacks Consensus EPS estimate for the current fiscal year over the past 12 weeks.

This metric essentially shows how the consensus EPS estimate has changed over a period longer than 1 week or 4 weeks.

**EPS Q1 Estimate Monthly Change:** The percentage change in the Zacks Consensus EPS estimate for the current fiscal quarter over the past four weeks.

While the revision in consensus EPS estimate for the current fiscal year is strongly correlated with the near-term price movement of its shares, the estimate revision for the current fiscal quarter is an important metric as well, especially over the short term, and particularly as a stock approaches its earnings date. If a stock's Q1 EPS estimate decreases ahead of its earnings release, it's usually a negative sign, whereas an increase is a positive sign.