

## Raytheon Technologies (RTX)

**\$59.87** (As of 08/07/20)

Price Target (6-12 Months): **\$65.00**

Long Term: 6-12 Months

**Zacks Recommendation:**

**Neutral**

(Since: 08/03/20)

Prior Recommendation: Underperform

Short Term: 1-3 Months

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

**3-Hold**

Zacks Style Scores:

VGM:C

Value: A

Growth: D

Momentum: D

### Summary

Raytheon Technologies ended second-quarter 2020 on a solid note, with both its earnings and revenues surpassing the Zacks Consensus Estimate. Thanks to its wide range of combat-proven defense products, the company continues to receive ample orders from the Pentagon and its foreign allies. Although the commercial part of its businesses has taken a hit lately, courtesy of the COVID-19 impact, in the military business of Collins and Pratt, Raytheon Technologies continues to see strength in sales. However, the company has underperformed its industry in the past three months. In January 2020, President Trump signed a proclamation, increasing tariffs on derivative steel products by an additional 25% and boosting duties on derivative aluminum products by an additional 10%. This might have pushed up expenses for the company.

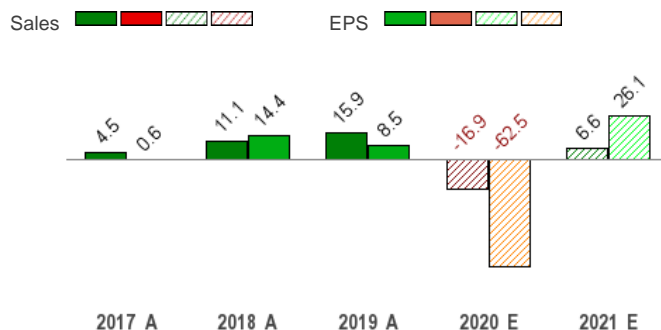
### Price, Consensus & Surprise



### Data Overview

52 Week High-Low	\$87.33 - \$38.04
20 Day Average Volume (sh)	8,669,535
Market Cap	\$53.0 B
YTD Price Change	-59.1%
Beta	0.81
Dividend / Div Yld	\$1.90 / 3.1%
Industry	<a href="#">Aerospace - Defense Equipment</a>
Zacks Industry Rank	Bottom 25% (188 out of 252)

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



Last EPS Surprise	300.0%
Last Sales Surprise	0.6%
EPS F1 Est- 4 week change	-1.9%
Expected Report Date	NA
Earnings ESP	0.0%
P/E TTM	9.7
P/E F1	19.3
PEG F1	1.6
P/S TTM	0.7

### Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	14,826 E	16,800 E	17,204 E	18,127 E	68,237 E
2020	18,210 A	14,061 A	15,372 E	16,000 E	64,002 E
2019	18,365 A	19,634 A	19,496 A	19,551 A	77,046 A

### EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.73 E	\$1.06 E	\$1.11 E	\$1.30 E	\$3.91 E
2020	\$1.78 A	\$0.40 A	\$0.66 E	\$0.66 E	\$3.10 E
2019	\$1.91 A	\$2.20 A	\$2.21 A	\$1.94 A	\$8.26 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 08/07/2020. The reports text is as of 08/10/2020.

## Overview

On Apr 3, 2020, **Raytheon Technologies** was formed following the completion of merger between United Technologies and Raytheon Company. Based in Waltham, MA, Raytheon Technologies has emerged as an aerospace and defense company, with pro-forma combined annual revenues of \$74 billion as of the end of 2019, providing advanced systems and services for commercial, military and government customers worldwide. The company currently operates through the following four business segments:

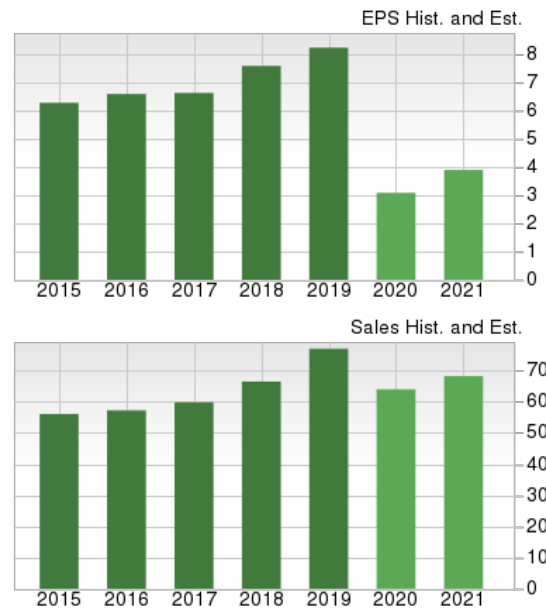
**Collins Aerospace:** It specializes in six strategic business units, namely, aerostructures, avionics, interiors, mechanical systems, mission systems, and power & control systems. It generated revenues worth \$4,202 million in the second quarter, representing 28.8% of total revenues.

**Pratt & Whitney:** It designs, manufactures and services the world's most advanced aircraft engines and auxiliary power systems for commercial, military and business aircraft. It generated revenues worth \$3,487 million in the second quarter, representing 24.6% of total revenues.

**Raytheon Intelligence & Space (RIS):** It develops advanced sensors and also offers training, and cyber and software solutions. It generated revenues worth \$3,317 million in the second quarter, representing 22.8% of total revenues.

**Raytheon Missiles and Defense (RMB):** It manufactures a broad portfolio of advanced technologies, including air and missile defense systems, precision weapons, radars, and command and control systems. It generated revenues worth \$3,590 million in the second quarter, representing 24.6% of total revenues.

Total revenues include \$532 million of intersegmental eliminations.



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## Reasons To Buy:

▲ In late 2018, legacy United Technologies acquired Rockwell Collins. During the second quarter, the Collins Aerospace unit captured positive synergies worth approximately \$30 million, bringing the year-to-date figure to \$90 million on top of the \$300 million that was realized last year. This segment remains on track to achieve a total synergy of \$600 million for Raytheon Technologies.

Merger related synergies and solid order growth to aid Raytheon Technologies

▲ Following the latest merger, Raytheon Technologies can be expected to benefit significantly from the technological upgrades in which both legacy Raytheon and United Technologies have been investing for long. Notably, at Pratt & Whitney, on the commercial aftermarket side, GTF overhaul activity continues as the company aims to upgrade engines to the latest configuration. Although the commercial part of its businesses has taken a hit lately, courtesy of the COVID-19 impact, in the military business of Collins and Pratt, Raytheon Technologies continues to see strength in sales and still expects to see mid-single-digit growth, excluding the impact of the two pending Collins divestitures.

▲ Thanks to its wide range of combat-proven defense products, Raytheon Technologies continues to receive ample orders from the Pentagon and its foreign allies. During the second quarter, the company won a handful of notable contracts. In Consequently, it witnessed record bookings of \$10.16 billion, which translated into a solid backlog of \$73.13 billion. These impressive results make us optimistic of the revenue growth prospects of the company, which, in turn, will boost its bottom line, over the long run. Notably, long-term earnings growth rate of the company is currently projected at 12% compared with its industry's rate of 6.8%. This makes it an attractive choice for investors.

▲ Its combat proven portfolio of varied missile systems remains a major growth driver for Raytheon Technologies. To this end, it is imperative to mention that at the onset of the second quarter, the company's RMB won a contract from the U.S. Air Force to develop a long-range standoff weapon, a strategic weapon that will replace the service's legacy air launch cruise missile. The company expects this franchise to be worth approximately \$10 billion over its lifetime. In June, RMB secured a \$2.3 billion U.S. Missile Defense Agency production contract for seven gallium nitride (GaN)-based AN/TPY-2 radars, as part of the Terminal High Altitude Area Defense (THAAD) system. Moreover, RMD booked an award worth approximately \$300 million for the Standard Missile-3 with the MDA and an international customer in the quarter. These indicate the rapidly increasing demand for Raytheon Technologies' missile systems.

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## Reasons To Sell:

- ▼ Rising costs of raw materials like steel are pushing up expenses of defense manufacturers like Raytheon Technologies. Moreover, the tariffs imposed by the U.S. administration on import of steel and aluminum may create or exacerbate existing materials shortages. Adding to these woes, in January 2020, President Trump signed a proclamation increasing tariffs on derivative steel products by an additional 25% and boosting duties on derivative aluminum products by an additional 10%, saying the existing tariffs had not proved as effective as he had hoped in reviving American production. This, in turn, is expected to have made it even more expensive for defense primes like Raytheon to manufacture valuable defense equipment, as America remains the world's largest steel importer. So, even if the company generates solid revenues, rising raw material cost might hurt all those gains and in turn weigh on Raytheon's bottom line. Thus, we remain skeptical as to whether the new trade tariffs will be able to aid the U.S. defense industry or remain as a prominent headwind.

Increasing tariff on imports of steel and aluminum, impact of coronavirus pandemic on commercial aerospace, delayed delivery and unfavorable financial ratios remain concerns.

- ▼ Since March 2020, the novel coronavirus outbreak started to significantly affect the U.S. and global economy, disrupted global supply chains and financial markets, and resulted in significant travel restrictions, including mandated facility closures and shelter-in-place orders in numerous jurisdictions around the world. Consequently, Raytheon Technologies began to experience issues related to COVID-19 starting from the first quarter, primarily related to a number of facility closures, less than full staffing, and disruptions in supplier deliveries, most significantly in its Aerospace businesses.

With the pandemic still looming large, continued disruption in air travel is affecting Raytheon Technologies' airline and airframer customers, and their demand for products and services of its Aerospace businesses. To tackle this crisis, the company has been incurring a number of incremental expenditures, including enhanced facility cleaning, employee temperature scanning, higher freight cost and other COVID related inefficiencies. These costs are expected to hurt its earnings by 8 cents during the second half of 2020.

- ▼ As of Apr 14, 2020, the International Air Transport Association estimated that revenue passenger miles(RPMs) for the year ended Dec 31, 2020 could decline by 48% in comparison to the prior year due to the pandemic. As a result, the company's airline customers reported significant reductions in fleet utilization, aircraft grounding and unplanned retirements, and deferred and, in some cases, cancelled new aircraft deliveries. Airlines are shifting to cash conservation behaviors such as deferring engine maintenance, requesting extended payment terms, deferring delivery of new aircraft and spare engines and requesting discounts on engine maintenance. Additionally, purchase order declines are experienced in line with publically communicated aircraft production volumes as OEM customers delay and cancel orders.

Given the significant reduction in air travel, increased numbers of planes temporarily grounded, and continued travel restrictions, Raytheon Technologies' future operating results, particularly those of its Aerospace businesses are expected to be significantly impacted during 2020. This must have caused investors to lose confidence in this stock. In the past three months, shares of Raytheon have lost 2.5% against its industry's 5.9% rise.

- ▼ Raytheon Technologies' cash and cash equivalents were \$6.98 billion as of Jun 30, 2020, compared with \$8.01 billion as of Mar 31, 2019. Its long-term debt of \$32.93 billion as of Jun 30, 2020, remained well above the cash balance. This reflects a weak solvency position for the stock, amid the ongoing economic downturn caused by the COVID-19 pandemic.

Moreover, the company's second-quarter 2020 interest coverage was 2.5%, lower than the prior-quarter level of 5.7% and the lowest in the past four quarters. Additionally, the company's current ratio of 1.20, as of Jun30, 2020, also deteriorated sequentially from 1.23. Such unfavorable financial ratios indicate that this defense major might not have sufficient capital for paying off its short-term obligations.

## Last Earnings Report

### Raytheon Technologies Q2 Earnings Beat, Sales Fall Y/Y

Raytheon Technologies second-quarter 2020 adjusted earnings per share (EPS) of 40 cents outpaced the Zacks Consensus Estimate of 10 cents by 300%.

However, the bottom-line figure declined 67.7% from the year-ago quarter's \$1.24.

Including one-time items, the company reported loss of \$2.56 against earnings of \$1.37 per share in the year-ago quarter.

The year-over-year deterioration in bottom line is attributable to charges related to the current economic environment primarily attributable to the COVID-19 pandemic.

Quarter Ending 06/2020

Report Date	Jul 28, 2020
Sales Surprise	0.56%
EPS Surprise	300.00%
Quarterly EPS	0.40
Annual EPS (TTM)	6.33

### Operational Performance

Raytheon Technologies' first-quarter sales of \$14,061 million declined 24.1% on a year-over-year basis. The top line, however, beat the Zacks Consensus Estimate of \$13,983 million by 0.6%.

Total costs and expenses increased 46.3% year over year to \$14,720 million. The company incurred operating loss of \$3,760 million against operating income of \$1,386 million in the year-ago quarter.

### Segmental Performance

**Collins Aerospace:** Adjusted sales at this segment declined 35% year over year to \$4,298 million in second-quarter 2020 due to commercial sales decline attributable to lower in-flight hours, aircraft fleet utilization and commercial OEM deliveries. Its adjusted operating income came in at \$24 million compared with the year-ago quarter's level of \$1,293 million.

**Pratt & Whitney:** Adjusted sales at this segment declined 30% year over year to \$3,607 million due to a significant reduction in shop visits and related spare part sales as well as lower commercial engine deliveries. Its adjusted operating loss was \$151million against the year-ago quarter's operating income of \$452 million.

**Raytheon Intelligence & Space:** This segment recorded second-quarter adjusted sales of \$3,314 million and recorded \$311 million of adjusted operating profit in the quarter.

**Raytheon Missiles & Defense:** This unit recorded second-quarter adjusted sales of \$3,590 million and \$397 million of adjusted operating profit in the quarter.

### Financial Update

Raytheon Technologies ended Jun 30, 2020 with cash and cash equivalents of \$6,975 million, up from \$4,937 million as of Dec 31, 2019.

Long-term debt was \$31,210 million, as of Jun 30, 2020, down from \$37,701 million as of Dec 31, 2019.

Net cash inflow from operating activities amounted to \$1,342 million at the end of second-quarter 2020 compared with \$2,769 million in the year-ago period.

Its free cash flow came in at \$559 million compared with \$2,091 million at the end of second-quarter 2019.

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## Recent News

On **Aug 3, 2020**, Raytheon Technologies announced that its business unit, Raytheon Missiles & Defense and RAFAEL Advanced Defense Systems Ltd., an Israeli-based defense technology company, have signed a joint venture to establish an Iron Dome Weapon System production facility in the United States. The new partnership, called Raytheon RAFAEL Area Protection Systems, anticipates finalizing a site location before the end of the year.

The new facility will produce both the Iron Dome Weapon System, which consists of the Tamir interceptor and launcher, and the SkyHunter missile, a U.S. derivative of Tamir. Both Tamir and SkyHunter intercept incoming cruise missiles, unmanned aerial systems and short-range targets such as rockets, artillery, mortars and other aerial threats.

On **Jun 26, 2020**, Raytheon Technologies' Missiles & Defense business received a \$2.3 billion U.S. Missile Defense Agency production contract for seven gallium nitride (GaN)-based AN/TPY-2 radars as part of the Terminal High Altitude Area Defense (THAAD) system, which is designed to protect against incoming ballistic missile threats. The contract is part of a foreign military sale to the Kingdom of Saudi Arabia.

On **Jun 15, 2020**, Raytheon Technologies announced that its Missiles & Defense business segment has completed the first guided release of a StormBreaker smart weapon from an F/A-18E/F Super Hornet, which will become the second fighter jet to add the weapon when the program reaches initial operational capability later this year.

On **May 12, 2020**, Raytheon Technologies' Intelligence & Space business won a three-year contract for value up to \$145 million, to train Afghanistan Air Force pilots.

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## Valuation

Raytheon's shares are down 2.1% in the last three months. Stocks in the Zacks sub-industry and the Zacks Aerospace sector are up 9.6% and 3%, respectively in the three months period, respectively. The S&P 500 index is up 13.9% in the said period.

The stock is currently trading at 17.1X of forward 12-month earnings, which compares to 21.7X for the Zacks sub-industry, 20.9X for the Zacks sector and 22.8X for the S&P 500 index.

Over the past three months, the stock has traded as high as 20.4X and as low as 14X, with a 5-year median of 17.3X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$65 price target reflects 18.2X forward 12-month earnings.

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## Industry Analysis Zacks Industry Rank: Bottom 25% (188 out of 252)



## Top Peers

Company (Ticker)	Rec	Rank
Bae Systems PLC ( <b>BAESY</b> )	Neutral	3
Elbit Systems Ltd. ( <b>ESLT</b> )	Neutral	3
Meggitt PLC Unsponsored ADR ( <b>MEGGY</b> )	Neutral	3
RollsRoyce Holdings PLC ( <b>RYCEY</b> )	Neutral	3
Transdigm Group Incorporated ( <b>TDG</b> )	Neutral	3
Teledyne Technologies Incorporated ( <b>TDY</b> )	Neutral	2
Moog Inc. ( <b>MOG.A</b> )	Underperform	3
Spirit Aerosystems Holdings, Inc. ( <b>SPR</b> )	Underperform	5

Industry Comparison Industry: Aerospace - Defense Equipment				Industry Peers		
	RTX	X Industry	S&P 500	BAESY	RYCEY	SPR
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Underperform
Zacks Rank (Short Term)	3	-	-	3	3	5
VGM Score	C	-	-	A	D	C
Market Cap	53.04 B	1.20 B	23.30 B	21.39 B	6.34 B	2.20 B
# of Analysts	4	4	14	2	3	6
Dividend Yield	3.10%	0.00%	1.76%	0.00%	0.00%	0.19%
Value Score	A	-	-	B	A	B
Cash/Price	0.14	0.14	0.07	0.17	0.99	0.89
EV/EBITDA	5.79	7.85	13.32	7.00	6.25	3.42
PEG Ratio	1.71	7.27	2.94	11.76	NA	NA
Price/Book (P/B)	0.77	2.09	3.19	3.01	NA	1.73
Price/Cash Flow (P/CF)	4.84	7.63	12.51	8.57	3.06	2.61
P/E (F1)	20.54	28.51	22.02	11.88	NA	NA
Price/Sales (P/S)	0.74	1.04	2.53	NA	NA	0.39
Earnings Yield	5.06%	2.87%	4.37%	8.42%	-8.43%	-19.55%
Debt/Equity	0.48	0.39	0.77	0.75	-1.46	2.43
Cash Flow (\$/share)	12.65	2.26	6.94	3.10	1.08	7.97
Growth Score	D	-	-	A	F	C
Hist. EPS Growth (3-5 yrs)	4.37%	10.59%	10.46%	NA	NA	8.47%
Proj. EPS Growth (F1/F0)	214.63%	-17.58%	-6.80%	29.23%	-104.95%	-209.20%
Curr. Cash Flow Growth	26.99%	12.73%	5.39%	8.10%	15.24%	-10.39%
Hist. Cash Flow Growth (3-5 yrs)	5.99%	5.32%	8.55%	-3.36%	-10.95%	3.45%
Current Ratio	1.20	2.71	1.33	1.01	1.07	2.71
Debt/Capital	32.37%	33.12%	44.50%	42.87%	NA	70.89%
Net Margin	-2.28%	4.46%	10.13%	NA	NA	-3.93%
Return on Equity	11.59%	8.92%	14.39%	NA	NA	-6.11%
Sales/Assets	0.49	0.73	0.51	NA	NA	0.79
Proj. Sales Growth (F1/F0)	-16.93%	-0.10%	-1.51%	16.98%	-27.46%	-54.60%
Momentum Score	D	-	-	B	F	F
Daily Price Chg	2.27%	0.42%	0.90%	-3.20%	-1.63%	-0.48%
1 Week Price Chg	-8.68%	0.00%	0.14%	5.23%	-11.82%	-11.37%
4 Week Price Chg	5.37%	6.62%	8.95%	9.94%	-0.30%	-1.84%
12 Week Price Chg	13.68%	19.13%	18.90%	9.53%	10.30%	15.99%
52 Week Price Chg	-53.43%	-21.56%	1.18%	-3.78%	-65.52%	-72.32%
20 Day Average Volume	8,669,535	162,737	2,057,775	292,782	588,581	4,550,775
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	2.75%	-5.00%	-18.99%
(F1) EPS Est 4 week change	-1.90%	0.00%	1.36%	12.85%	-127.03%	-22.45%
(F1) EPS Est 12 week change	-15.73%	-1.96%	1.57%	4.19%	-342.11%	-38.48%
(Q1) EPS Est Mthly Chg	34.60%	0.00%	0.54%	NA	NA	-32.48%

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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 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.

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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	A
Growth Score	D
Momentum Score	D
VGM Score	C

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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### Disclosures

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