

Science Applications (SAIC)

\$81.66 (As of 04/30/20)

Price Target (6-12 Months): **\$86.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 09/04/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

2-Buy

Zacks Style Scores:

VGM:A

Value: B

Growth: B

Momentum: B

Summary

Science Applications is benefiting from the Engility acquisition. Strong performance of its contract portfolio is also a tailwind. Further, solid program performance and a positive impact of cost synergies are boosting EBITDA margin. Also, SAIC hopes to provide increased customer access, higher investments in competitive solutions and an improved cash flow. The stock has outperformed the industry over the last year. However, acquisition-related dis-synergies were an overhang on the top line. Competition in the emerging growth segment and an intense rivalry with CACI are concerns as well.

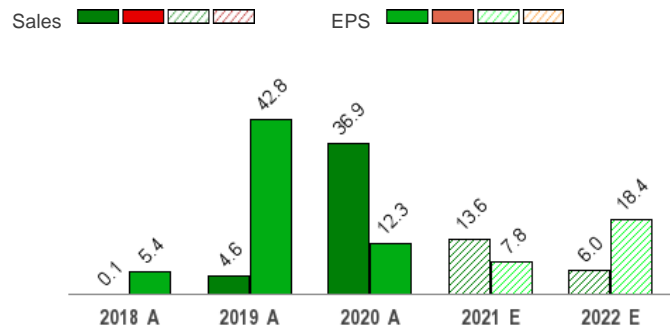
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$96.80 - \$45.45
20 Day Average Volume (sh)	604,379
Market Cap	\$4.7 B
YTD Price Change	-6.2%
Beta	1.07
Dividend / Div Yld	\$1.48 / 1.8%
Industry	Computers - IT Services
Zacks Industry Rank	Top 30% (76 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	19.7%
Last Sales Surprise	-2.1%
EPS F1 Est- 4 week change	-1.6%
Expected Report Date	06/04/2020
Earnings ESP	-3.3%

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2022					7,680 E
2021	1,727 E	1,800 E	1,874 E	1,817 E	7,245 E
2020	1,615 A	1,594 A	1,630 A	1,540 A	6,379 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2022	\$1.70 E	\$1.74 E	\$1.88 E	\$1.86 E	\$7.22 E
2021	\$1.41 E	\$1.49 E	\$1.61 E	\$1.59 E	\$6.10 E
2020	\$1.36 A	\$1.35 A	\$1.39 A	\$1.58 A	\$5.66 A

*Quarterly figures may not add up to annual.

P/E TTM	14.4
P/E F1	13.4
PEG F1	2.4
P/S TTM	0.7

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 04/30/2020. The reports text is as of 05/01/2020.

Overview

Science Applications International Corporation (SAIC) is one of the leading IT and professional services provider, primarily to the U.S. government. Founded in 1969, the company's headquarter is located at Reston, VA.

Science Applications offers transaction, technical, engineering and enterprise IT services primarily to the U.S. government. Its offerings include technology and equipment platform integration; engineering; logistics; operation and program support services; maintenance of ground and maritime systems; and training and simulation. Apart from this, Science Applications provides end-to-end services like design, development, integration, deployment, management and operations, sustainment, and security of its customers' IT infrastructure.

The company's customers lists primarily includes different government agencies, including the U.S. military, comprising Army, Air Force, Navy, Marines, and Coast Guard; the U.S. Defense Logistics Agency; the National Aeronautics and Space Administration; the U.S. Department of State; and the U.S. Department of Homeland Security. The company serves its customers with more than 15,000 employees.

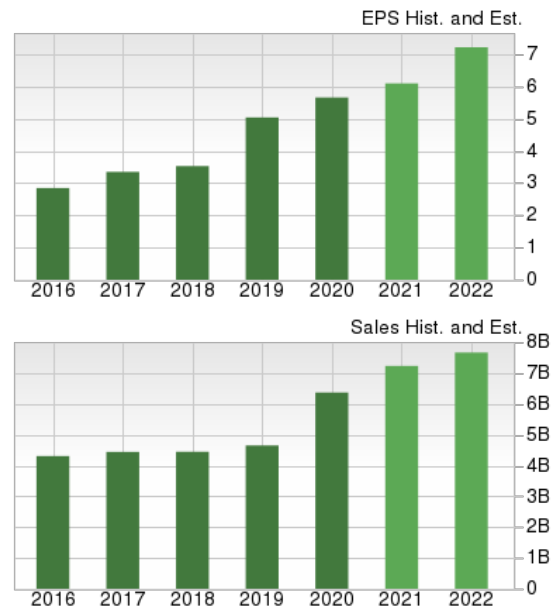
The company generated \$6.38 billion of revenues in fiscal 2020, of which more than 97% came in from the U.S. government. The company segregates its contracts in three different types:

Cost-reimbursement contracts: Under this type of contract, the company gets reimbursement for its direct and indirect allocable costs associated with the contract plus a fee (contract profit).

Time-and-materials (T&M) contracts: These contracts are based on fixed hourly rates for particular categories of direct labor, plus reimbursement for any other direct costs.

Firm-fixed price (FFP) contracts: These contracts provide for a predetermined price for specific solutions.

Its competitors include companies such as General Dynamics, Northrop Grumman, Raytheon Company, Booz Allen Hamilton, CACI International, Leidos Holdings, ManTech International, Serco Group, Perspecta, Accenture, IBM, Unisys and Agility Logistics.



Reasons To Buy:

- ▲ Science Applications remains focused on the federal government marketplace and capturing more market share. The company intends to drive operational excellence by intensively focusing on its organic and inorganic growth strategy, and strengthening existing customer relationships while building newer ones. Higher spending as proposed in the latest federal government budget is anticipated to accelerate the pace of contract awards which in turn will be beneficial for Science Applications' top-line growth.
- ▲ A leader in IT outsourcing for the U.S. government agencies, Science Applications has exposure to the rapidly growing DoD and Department of Homeland Security budgets. Its system-integration skills and intelligence expertise consume a significant portion of the funds earmarked for the Department of Homeland Security while creating systems that foster the sharing of critical information among all intelligence agencies. We believe the company is comfortably positioned, given its favored relationship with the DoD. Moreover, cyber-attacks are creating increased awareness, leading to more demand for cyber solutions.
- ▲ Having the government as a big client lends stability to the business and moderates fluctuation in revenues. Although the government generally has a lengthy approval process, the project earns money for a number of years after it is approved. Moreover, government contracts improve the visibility of future revenue streams. The company has been doing very well with a record level of awards, which reflects its disciplined business development actions, consistent operational excellence and high customer satisfaction. The company continues to execute its strategy of winning high-value contracts, delivering excellence to customers and deploying capital for growth. Its robust business model is expected to help it grow further.
- ▲ Science Applications has been aggressive in the acquisition front to boost competitive position. Notably, the spin-off from Leidos had resulted in a very little intelligence business left with the company, due to which it had been lagging to keep pace with competitors. However, the buyout of Scitor Holdings has now put it as a market leader within the intelligence community, immediately boosting its top line, bringing in approximately \$600-million additional revenues annually. The recently-completed acquisition of Engility is expected to boost the company's top-line, profitability and cash flow, consequently enhancing long-term shareholder-value creation. All this makes us optimistic about the company's growth prospects.
- ▲ Science Applications can be considered as an above-average leveraged company as its current total debt to total capital ratio of 0.57 is higher than the industry average of 0.46. Moreover, the company's total debt (including current maturities) of \$1.9 billion is way higher than the cash balance of \$188 million as of Jan 31, 2020. Nonetheless, the company's strong cash-flow generation capabilities have helped it serve financial obligations efficiently. In the trailing 12 months, Science Applications has generated operating and free cash flows of \$458 million and \$437 million, respectively. Moreover, its times interest earned ratio of 4.2 signifies the company's ability to generate enough operating income to service its financial obligations without any problems.
- ▲ Science Applications' strong operating cash flow has helped it return cash through regular quarterly dividend payment and share repurchases. Share repurchases is a good way of returning cash to investors while boosting the company's bottom-line. Moreover, consistent returns to shareholders reflect balance sheet strength and company's cash flow generating ability. During fiscal 2020, the company paid a total cash dividend of \$87 million and repurchased \$197 million worth of its common stock. Since the inception of the share-repurchase program in 2013, it has repurchased \$736 million worth of stocks.

Higher spending as proposed in the latest federal government budget is anticipated to accelerate the pace of contract awards which in turn will be beneficial for Science Applications' top-line growth.

Reasons To Sell:

- ▼ Though Science Applications has been steadily winning contracts from the federal government, but these low-margin deals have been affecting the company's profitability, which remain a major concern.
- ▼ Unfavorable contract mix is also hurting the company's profitability. The company continues to witness increase in cost reimbursement type contracts compared with fixed price contract, which is expected to be a drag on margins.
- ▼ Revenue concentration is a major risk for Science Applications. In fiscal 2019, over 95% of revenues came from sales to the U.S. federal government either as a prime contractor or subcontractor. Due to this massive dependency, changes in the government's IT spending budget is a huge deciding factor for the company's top-line growth. Moreover, these contracts are subject to extensive legal and regulatory hurdles, which are stringent, and subject to change from time to time. The government also investigates operations periodically to ensure that the terms and conditions have been properly adhered to. Deviations from the terms laid out by the government might result in huge penalties or termination.
- ▼ Science Applications competes primarily in the government IT services arena, which, like other government sectors, consists of many competitors of various sizes. Its main competitors include ManTech International Corporation, CACI, Unisys, Accenture, IBM, all of which are established players in the industry, with their respective strengths. Consequently, the company has to continuously invest in value drivers which act as a hedge against competition. These increase its operating costs and reduce its profitability.
- ▼ Moreover, seasonality is an influential factor for the top line. The fourth quarter is usually low-revenue quarter due to holidays and employee vacations. This brings down average top-line growth of the full fiscal.

Revenue concentration and increasing competition remain key concerns for SAIC.

Last Earnings Report

Science Applications Q4 Earnings Top, Revenues Miss

Science Applications reported mixed results for fourth-quarter fiscal 2020, wherein its earnings topped the Zacks Consensus Estimate but revenues missed the same. The company reported fiscal fourth-quarter adjusted earnings of \$1.58 per share, surpassing the consensus mark by 19.7% and improving 35% year over year as well.

Moreover, revenues jumped 29% from the year-ago quarter to \$1.54 billion but lagged the Zacks Consensus Estimate of \$1.57 billion. Revenues realized from the acquisition of Engility drove the top line. Solid performance of the company's contract portfolio was a tailwind.

However, adjusting for the impact of acquired revenues, the metric edged down 1.2% due to acquisition-related dis-synergies and completion of a technology contract.

Quarter in Detail

Net bookings for the fiscal fourth quarter were \$2.4 billion, reflecting a book-to-bill ratio of approximately 1.5.

Science Applications' estimated backlog of signed business deals was \$15.3 billion, of which \$2.6 billion was funded.

Adjusted operating margin expanded 20 basis points (bps) year over year to 6.8% in the reported quarter.

Adjusted EBITDA of \$134 million jumped 41%. Adjusted EBITDA margin expanded 70 bps to 8.7%.

Balance Sheet & Cash Flow

Science Applications ended the fiscal fourth quarter with cash and cash equivalents of \$188 million, down from the prior quarter's \$162 million.

Operating cash flow was \$69 million, down from the previous quarter's \$116 million. Free cash flow was \$62 million compared with \$116 million in the fiscal third quarter. During the reported quarter, Science Applications deployed \$7 million of capital, \$22 million to cash dividends and \$16 million to debt repayment.

In fiscal 2020, the company generated operating and free cash flow of \$458 million and \$437 million, respectively. During this period, Science Applications deployed \$21 million of capital, \$87 million to cash dividends and \$274 million to debt repayment.

Guidance

During the earnings conference call, Science Applications noted that it had intended to provide a formal fiscal 2021 outlook. However, citing the uncertainties due to the coronavirus pandemic, the company has decided to postpone issuing a fiscal 2021 guidance.

Nonetheless, for the investment community, the company shared its thought regarding how it had viewed fiscal 2021 before the crisis. Science Applications said it has witnessed minimal impact of coronavirus on its business.

Prior to the COVID-19 crisis, the company was expecting organic revenue growth in the range of 3% to 6% for fiscal 2021. This would include revenues from the recently-completed acquisition of Unisys Federal.

For the fiscal year, adjusted EBITDA margin is likely to be at the mid-to-upper-end of the 8-9% range.

Free cash flow is expected to be at least \$450 million for fiscal 2021.

Quarter Ending 01/2020

Report Date	Mar 26, 2020
Sales Surprise	-2.11%
EPS Surprise	19.70%
Quarterly EPS	1.58
Annual EPS (TTM)	5.68

Recent News

On Mar 12, SAIC announced that it is partnering with The Goodyear Tire & Rubber Company on a pilot project on securing customer data across supply chain with blockchain technology.

On Mar 11, SAIC received a three-year, single-award, follow-on contract worth \$45.2 million to continue supporting the Navy and Marine Corps in tactical warfare training.

On Feb 6, 2020, SAIC entered into a definitive agreement to acquire Unisys Federal, in an all-cash transaction valued at \$1.2 billion.

On Jan 10, 2020, SAIC won an application modernization contract worth \$727 million for the Department of Defense.

On Dec 11, 2019, Science Applications International announced that its Board of Directors has authorized and declared a regular quarterly cash dividend of 37 cents per share. The cash dividend is payable on Jan 31, 2020 to stockholders of record on Jan 17, 2020.

On Nov 27, 2019, Science Applications was awarded the IDIQ contract worth \$81 million by the Environmental Protection Agency. On the same day, it also received a \$582-million contract award from the space and intelligence community customers.

Valuation

Shares of SAIC have lost 6.1% so far this year while have gained 11.5% over the trailing 12-month period. Stocks in the Zacks sub-industry lost 8.3% in the year-to-date (YTD) period, while the Zacks Computer & Technology sector fell 2.3%. Over the past year, while the Zacks sub-industry has lost 10.3%, the sector rises 6.9%.

The S&P 500 Index has declined 8.8% YTD, while has gained 0.4% in the past year.

The stock is currently trading at 12.81X forward 12-month earnings, which compares to 23.77X for the Zacks sub-industry, 23.05X for the Zacks sector and 20.8X for the S&P 500 index.

Over the past five years, the stock has traded as high as 24.99X and as low as 8.18X with a 5-year median of 16.8X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$86 price target reflects 13.45X forward 12-month earnings.

The table below shows summary valuation data for SAIC

Valuation Multiples - SAIC					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	12.81	23.77	23.05	20.80
	5-Year High	24.99	32.37	23.05	20.80
	5-Year Low	8.18	15.46	16.71	15.19
	5-Year Median	16.80	22.24	19.23	17.44
P/S F12M	Current	0.64	4.66	3.51	3.30
	5-Year High	0.86	10.11	3.59	3.44
	5-Year Low	0.41	3.89	2.32	2.54
	5-Year Median	0.69	7.26	3.10	3.01
EV/Sales TTM	Current	1.00	4.49	3.79	2.91
	5-Year High	1.39	8.12	4.43	3.46
	5-Year Low	0.62	3.61	3.05	2.48
	5-Year Median	0.92	5.83	3.77	3.00

As of 04/30/2020

Industry Analysis Zacks Industry Rank: Top 30% (76 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
NCI Building Systems, Inc. (CNR)	Outperform	1
DRDGOLD Limited (DRD)	Outperform	3
Electronic Arts Inc. (EA)	Outperform	2
TPG Pace Holdings Corp. (ACEL)	Neutral	3
Cabot Microelectronics Corporation (CCMP)	Neutral	3
Jacobs Engineering Group Inc. (J)	Neutral	3
Kite Realty Group Trust (KRG)	Neutral	3
NexGen Energy Ltd. (NXE)	Neutral	3

Industry Comparison Industry: Computers - It Services				Industry Peers		
	SAIC	X Industry	S&P 500	ACEL	J	NXE
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	2	-	-	3	3	3
VGM Score	A	-	-	A	F	F
Market Cap	4.73 B	2.46 B	20.61 B	761.18 M	11.01 B	475.53 M
# of Analysts	7	4.5	14	1	8	1
Dividend Yield	1.81%	0.00%	2.11%	0.00%	0.92%	0.00%
Value Score	B	-	-	C	C	F
Cash/Price	0.04	0.06	0.06	0.20	0.06	0.08
EV/EBITDA	12.44	10.41	11.87	16.77	19.54	-582.72
PEG Ratio	2.43	2.25	2.47	NA	2.49	NA
Price/Book (P/B)	3.30	4.22	2.67	9.29	1.82	3.39
Price/Cash Flow (P/CF)	9.99	11.35	10.66	20.28	12.84	NA
P/E (F1)	13.39	23.99	19.01	NA	15.70	NA
Price/Sales (P/S)	0.74	0.88	2.10	NA	0.85	NA
Earnings Yield	7.47%	3.11%	5.05%	-0.82%	6.37%	-5.30%
Debt/Equity	1.30	0.23	0.72	3.91	0.23	0.65
Cash Flow (\$/share)	8.18	1.13	7.01	0.48	6.44	-0.03
Growth Score	B	-	-	A	F	F
Hist. EPS Growth (3-5 yrs)	17.06%	17.85%	10.88%	NA	11.23%	NA
Proj. EPS Growth (F1/F0)	7.72%	0.00%	-7.32%	11.11%	4.36%	-40.00%
Curr. Cash Flow Growth	74.09%	15.51%	5.92%	-8.32%	6.22%	-437.73%
Hist. Cash Flow Growth (3-5 yrs)	23.85%	16.83%	8.55%	NA	9.65%	NA
Current Ratio	1.27	1.35	1.23	2.76	1.55	11.17
Debt/Capital	56.47%	33.63%	43.84%	79.65%	18.92%	39.50%
Net Margin	3.54%	3.54%	11.08%	NA	7.54%	NA
Return on Equity	25.09%	11.09%	16.44%	-61.13%	12.29%	-8.23%
Sales/Assets	1.37	0.80	0.54	NA	1.08	NA
Proj. Sales Growth (F1/F0)	13.58%	4.16%	-1.42%	296.63%	-2.48%	NA
Momentum Score	B	-	-	B	C	C
Daily Price Chg	-6.14%	-1.08%	-2.39%	-1.72%	0.02%	0.76%
1 Week Price Chg	4.00%	-0.23%	-1.74%	-5.11%	-4.99%	25.23%
4 Week Price Chg	10.69%	20.40%	17.07%	31.66%	1.93%	41.92%
12 Week Price Chg	-14.88%	-15.09%	-18.53%	-22.66%	-13.82%	18.92%
52 Week Price Chg	11.45%	-24.06%	-9.82%	-5.63%	7.83%	-13.16%
20 Day Average Volume	604,379	383,559	2,641,413	136,769	878,146	769,611
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	-4.27%	0.00%
(F1) EPS Est 4 week change	-1.55%	-1.95%	-6.62%	0.00%	-4.27%	0.00%
(F1) EPS Est 12 week change	-1.34%	-12.68%	-13.28%	-112.70%	-5.76%	-16.67%
(Q1) EPS Est Mthly Chg	-4.05%	0.00%	-11.97%	0.00%	-7.31%	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	B
Growth Score	B
Momentum Score	B
VGM Score	A

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

Disclosures

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

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

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

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

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

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