

**LOCKHEED MARTIN**



The Frugalicious Team

# Company Overview

- LMT is a defense prime contractor that designs, develops and manufactures products and services to the US Military and Allied Military Forces
- Ticker symbol: LMT
- Current price: \$337 per share
- Market cap: \$93B
- Employees: 110K



# Aeronautics

## Aeronautics Segment:

- 40% of net sales

## Provides:

- Military aircraft
- Combat & air mobility aircraft, and unmanned air vehicles

## Programs include:

- F-35 Lightning
- C-130 Hercules
- F-16 Fighter Falcon
- F-22 Raptor



# Missile & Fire Control

## Missile & Fire Control

- 17% of net sales

## Provides:

- Missile defense systems
- Tactical missiles
- Air & ground weapon systems
- Integration services
- Manned & unmanned vehicles

## Major Programs:

- PAC-3, THAAD
- Multiple Launch Rocket System, Javelin tactical missile programs
- Hypersonics



# Rotary & Mission Systems

## Rotary & Mission Systems

- 25% of net sales

### Provides:

- Services, support and manufacturing
- Military & commercial helicopters
- Ship & submarine combat systems
- Simulation & training services
- Unmanned systems
- Supports government cyber security



# Space

## Space

- 18% of net sales

## Provides:

- Designs, develops and manufactures
- Satellites
- Space transportation systems
- Advance strike & defensive systems
- Classified systems that support national security systems

## Major Programs Include:

- The AWE, FBM, SBIRS, Orion and more



# How Do They Make Money?



# Government Contracts

- Serves as both a prime contractor and a subcontractor for the U.S. Government
- Govt. Announces Contract
  - Bidding War
- LMT is highly specialized, strong relationship with government
- Typically wins every contract it bids for



# Government Contracts

- 71% of revenue derived from the U.S. government, 64% from the Department of Defense
- Heavily interconnected and intimately familiar with the government's supply chain
- Over a century of relationships and connections built up

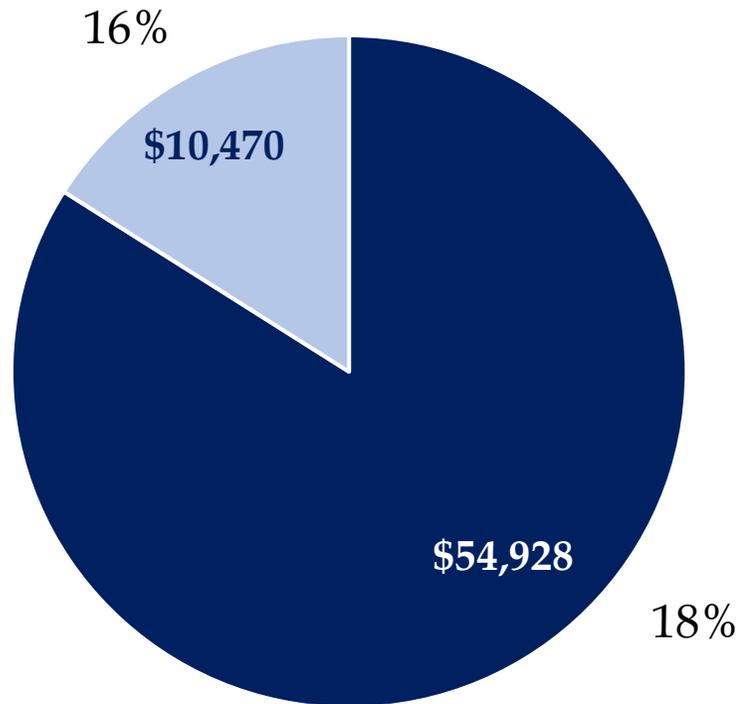


# International Customers

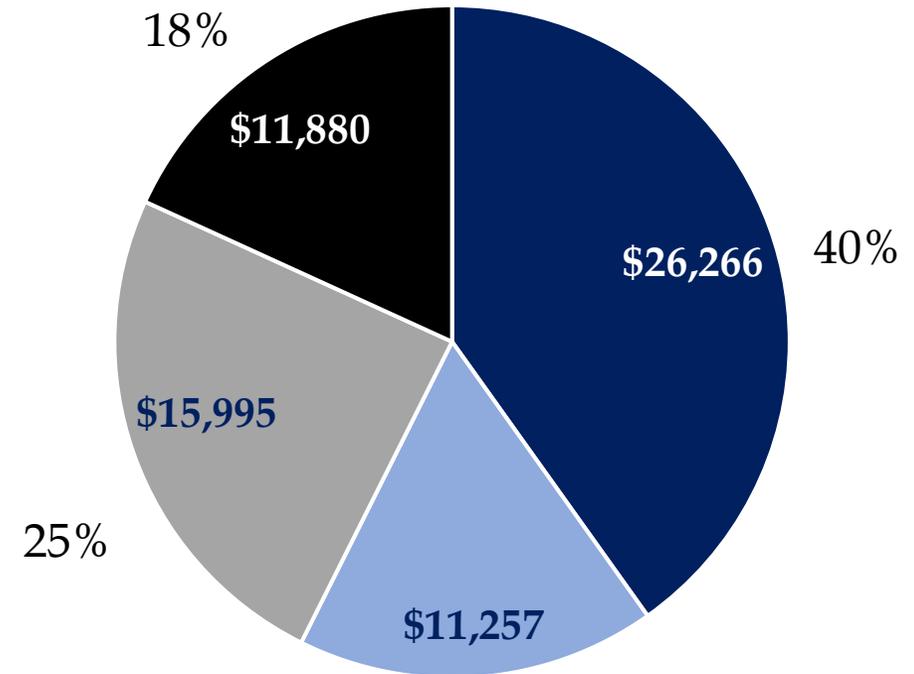
- U.S. allies
  - Government authorization required
  - Conflicts of interest
- Differing, often less stringent regulations on defense companies
- Largest customers: Australia, UK, Bahrain



# Revenue Breakdown

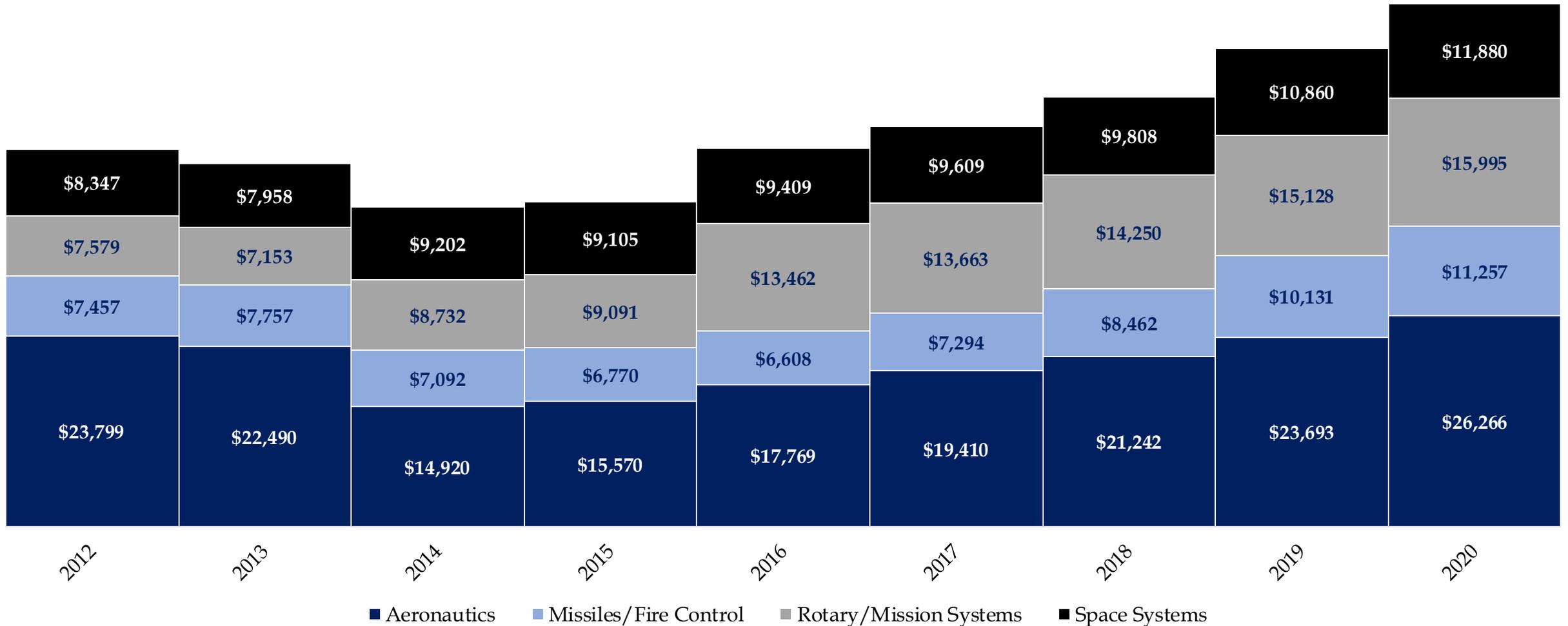


■ Products ■ Services ■ ■



■ Aeronautics ■ Missiles/Fire Control ■ Rotary/Mission Systems ■ Space

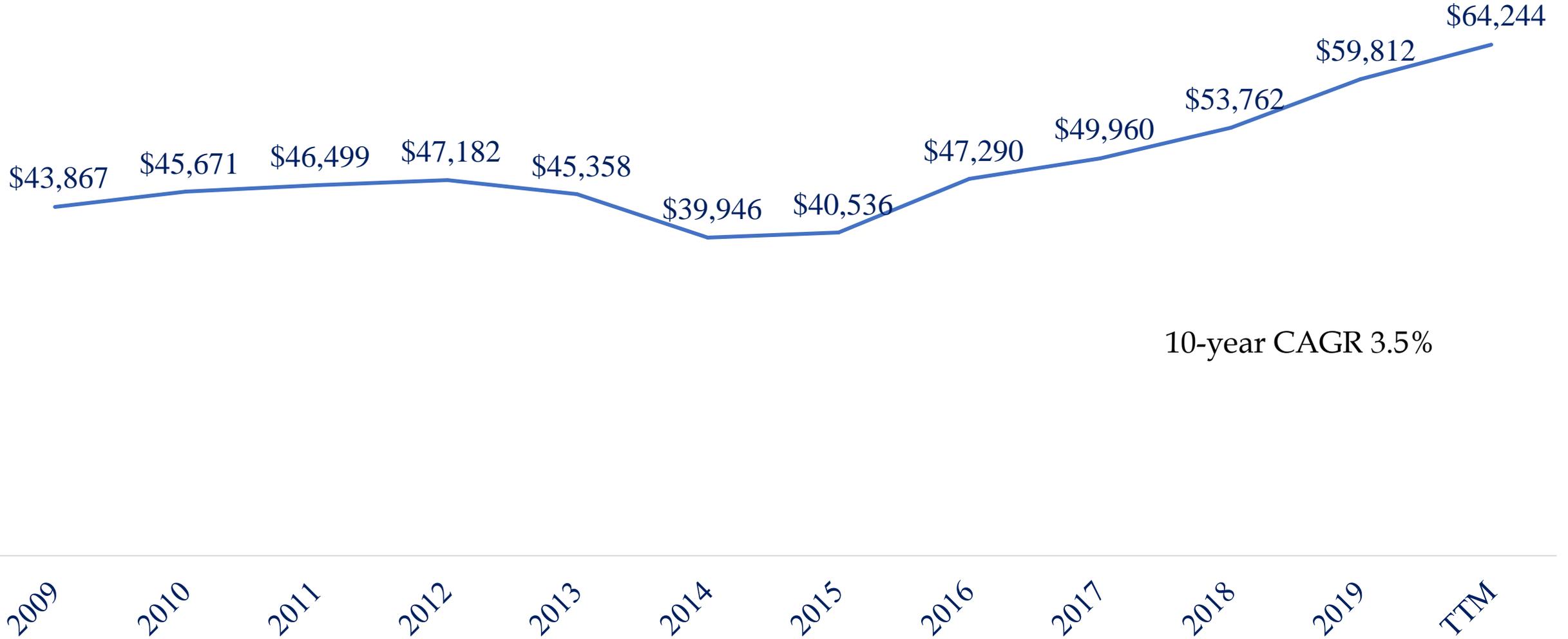
# Revenue Breakdown



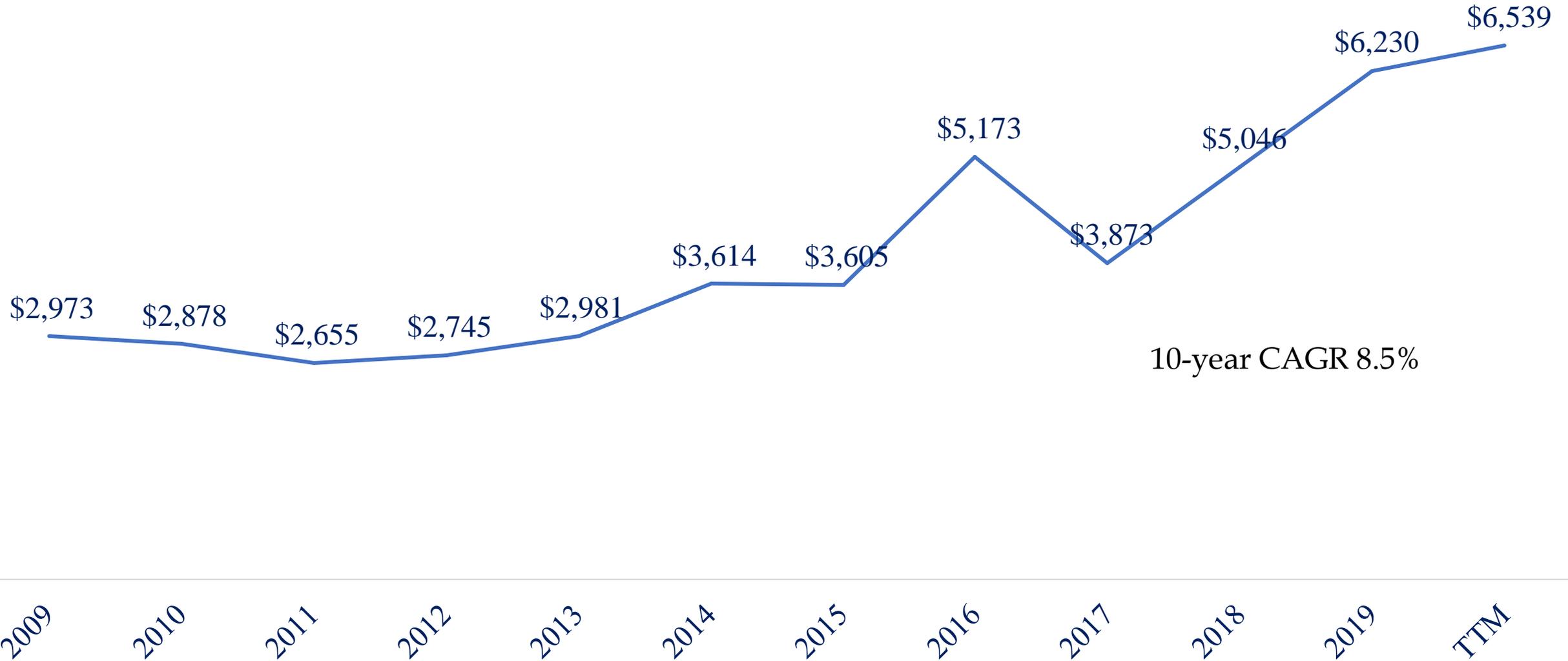
# Interpretations of Financial Statements



# Revenue



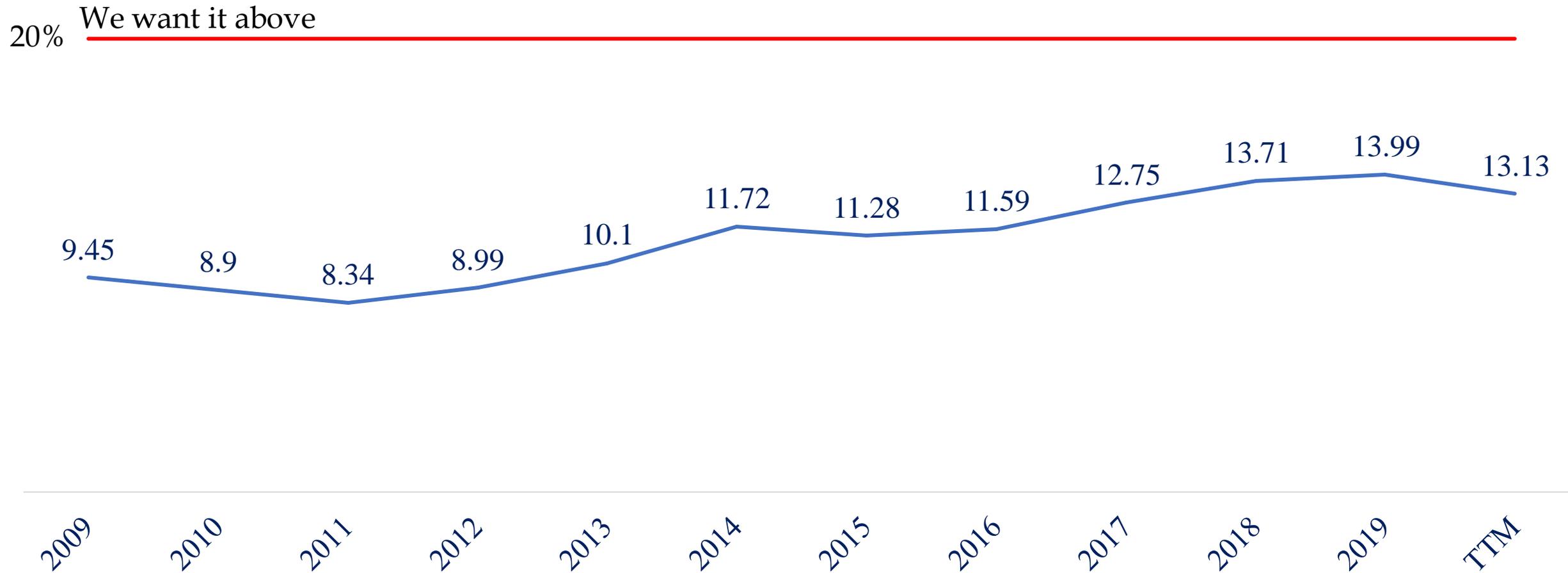
# Net Income



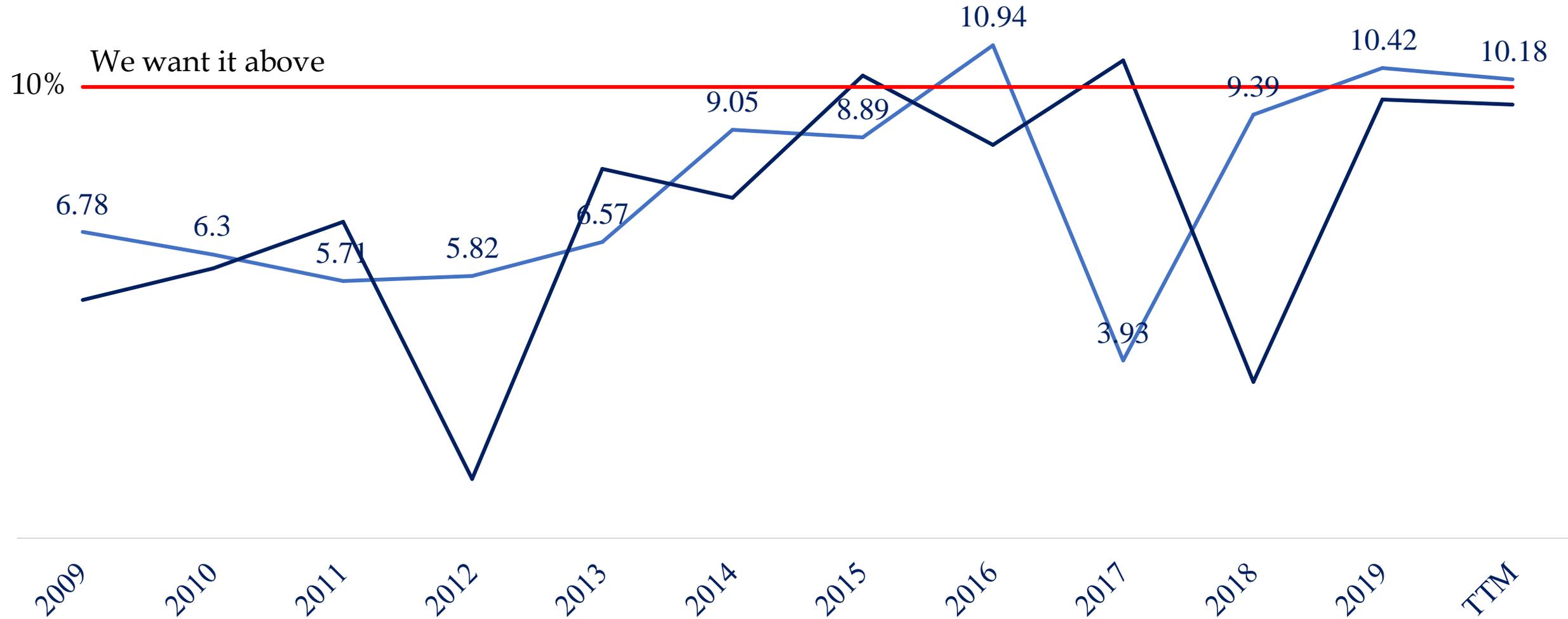
# Cash Flow From Operations



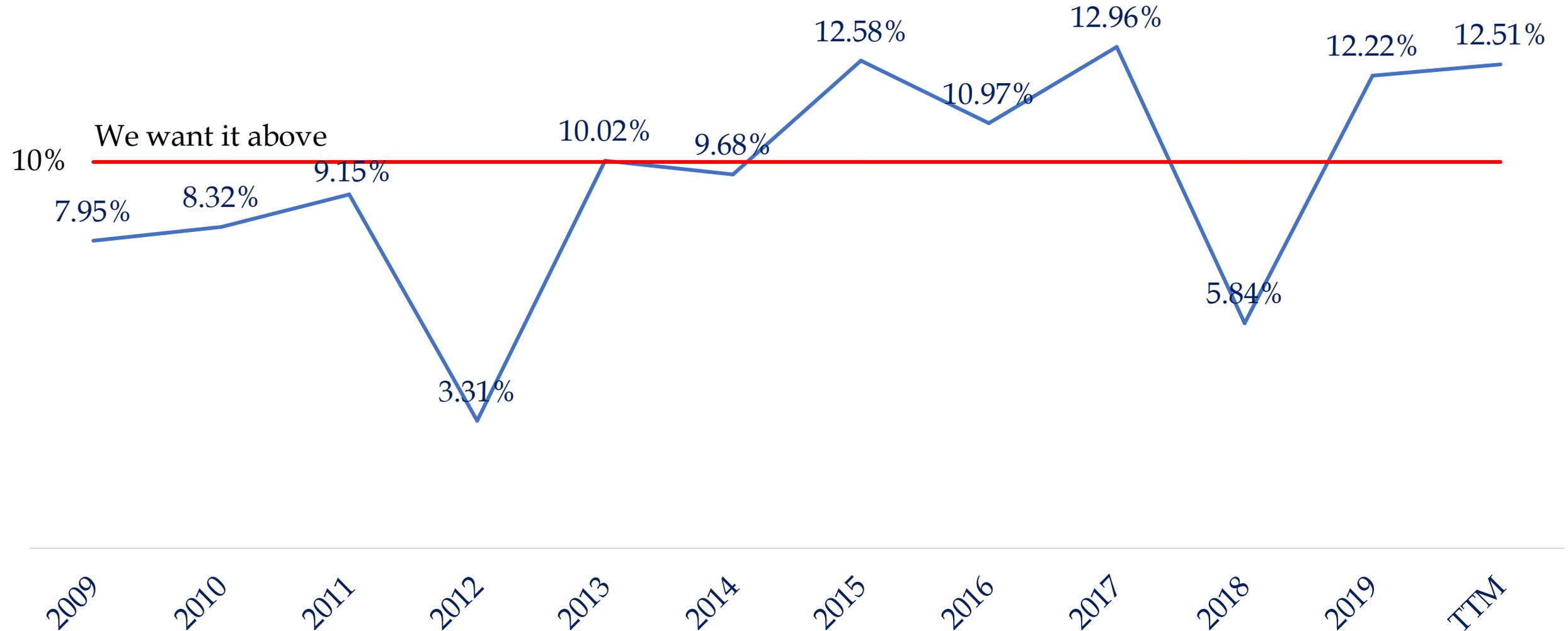
# Operating Margin



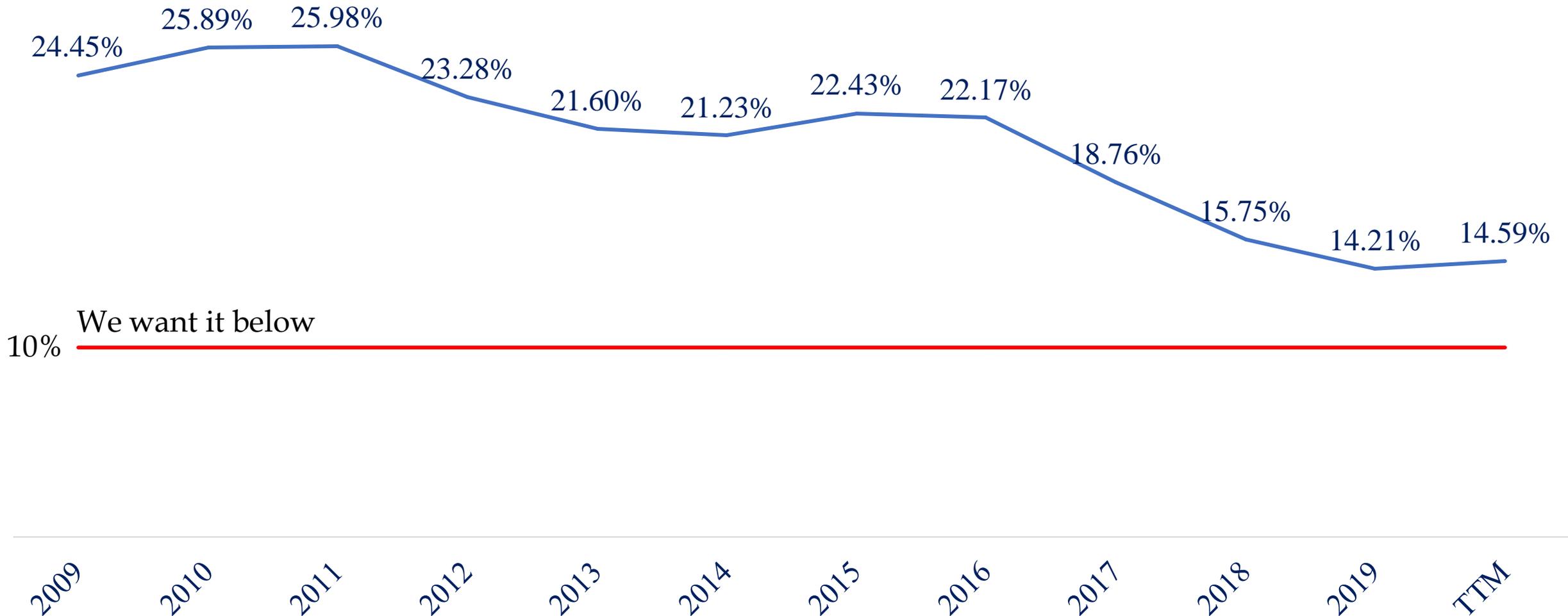
# Net Margin and FCF Margin



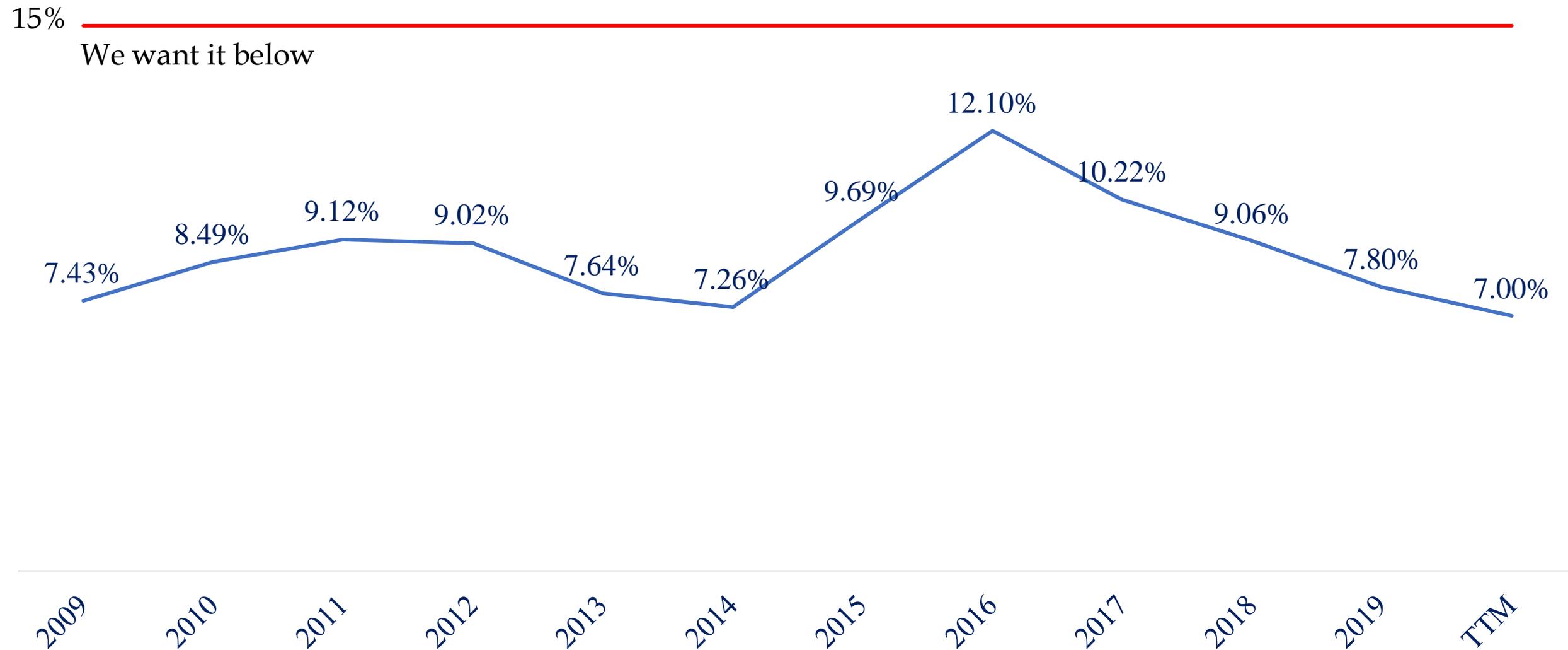
# Cash Flow From Operations Margin



# Depreciation & Amortization to GP

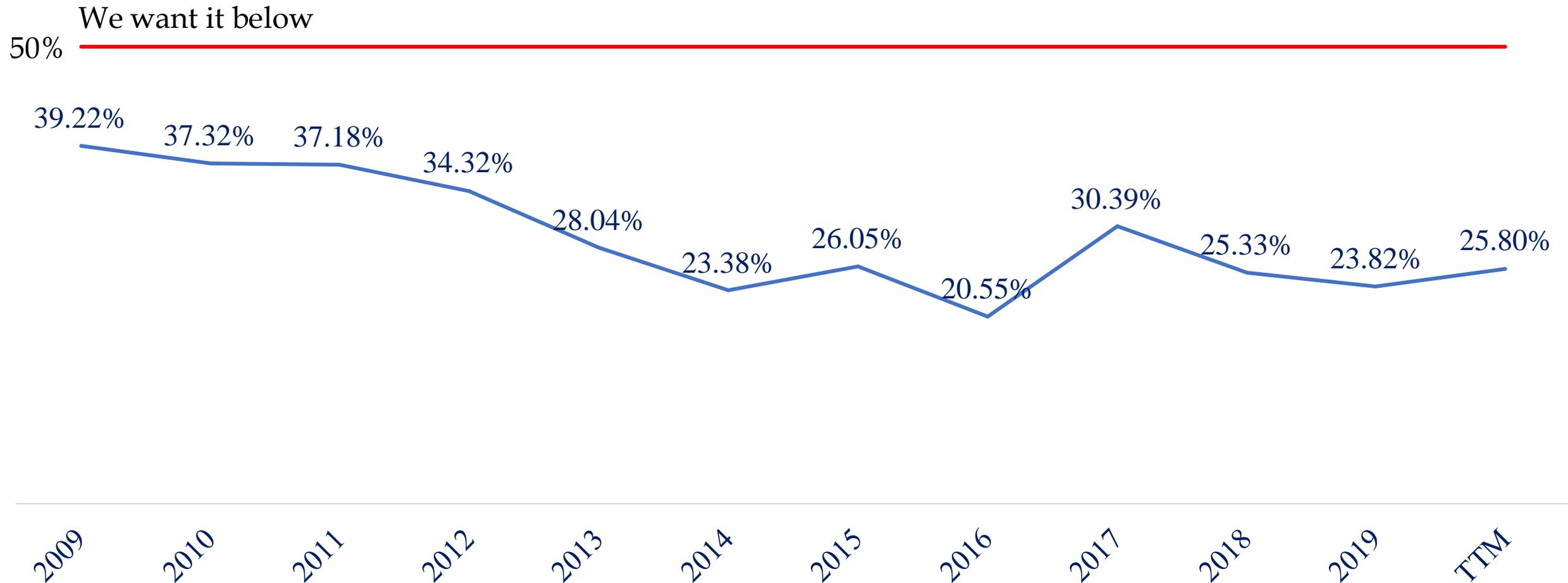


# Interest Expense to Operating Income



<b>Obligation Ratio</b>			
	<b>LT Debt</b>	\$ 11,675	
	<b>ST Debt</b>	\$ 1,000	
	<b>Leases * 7</b>	\$ 1,673	
	<b>Pen Shortfall</b>	\$ 13,300	
	<b>Cash Assets</b>	\$ 3,585	We want it below 5
2020	<b>GAAP Earnings</b>	\$ 6,539	3.68-years
2019	<b>GAAP Earnings</b>	\$ 6,230	3.86-years
2021	<b>VL Net Income</b>	\$ 7,300	3.30-years

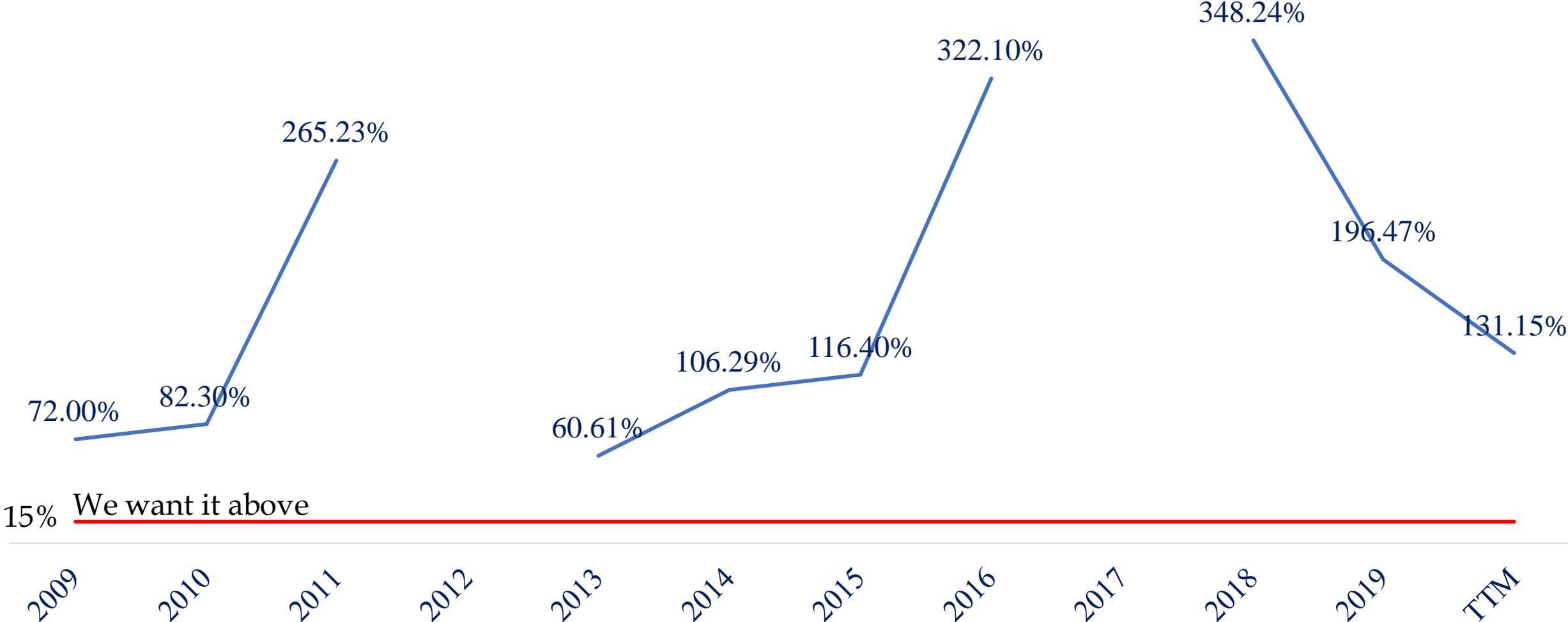
# Capital Expenditures to Net Income



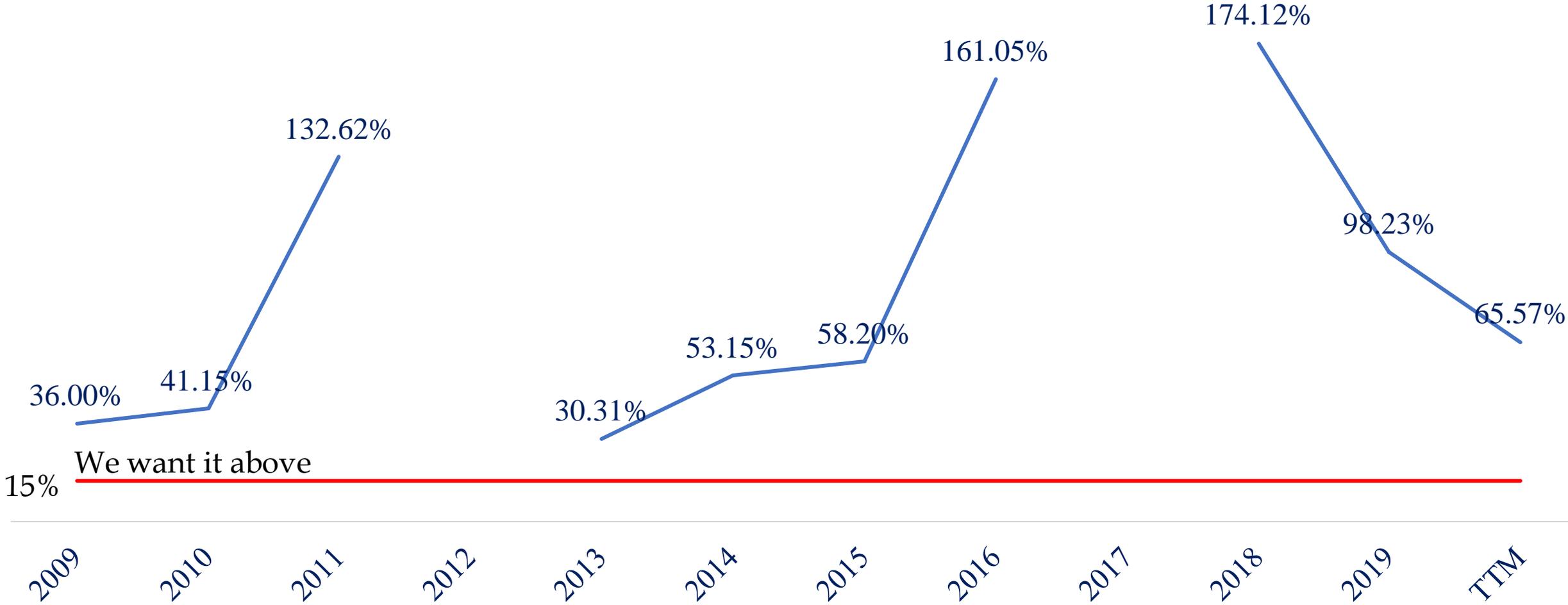
# Retained Earnings



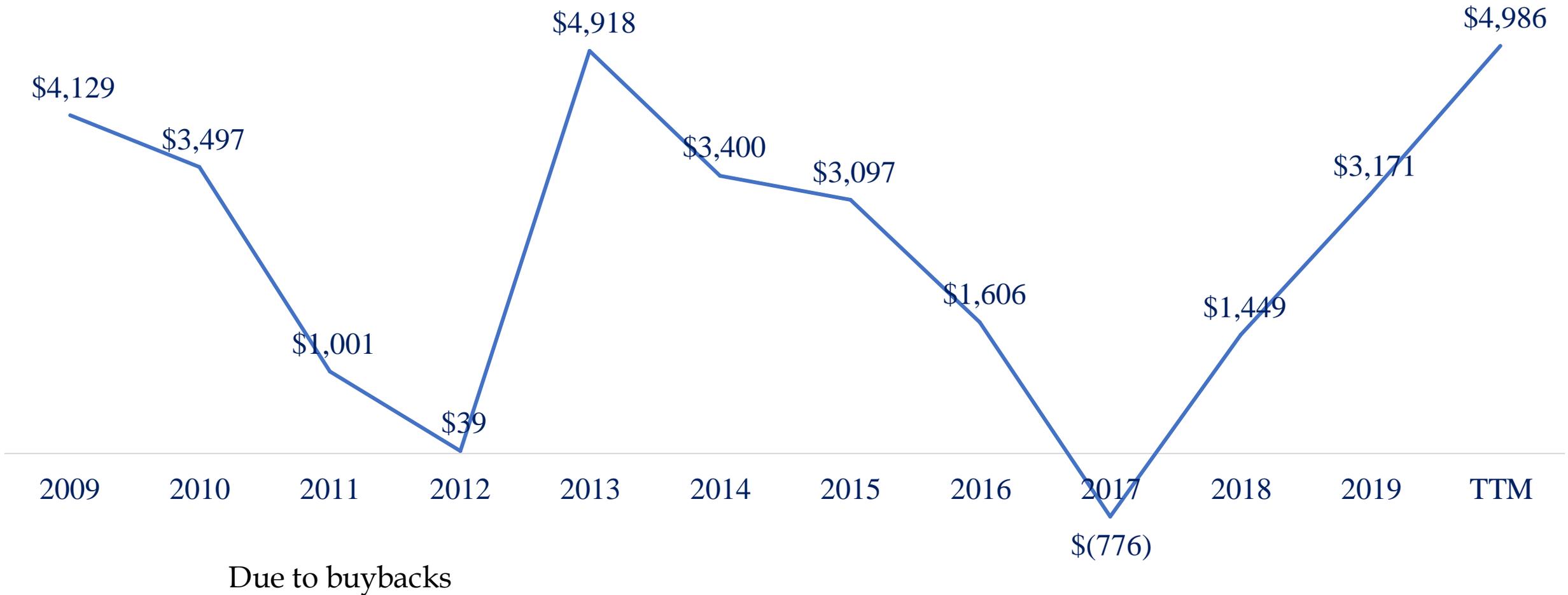
# Return on Equity



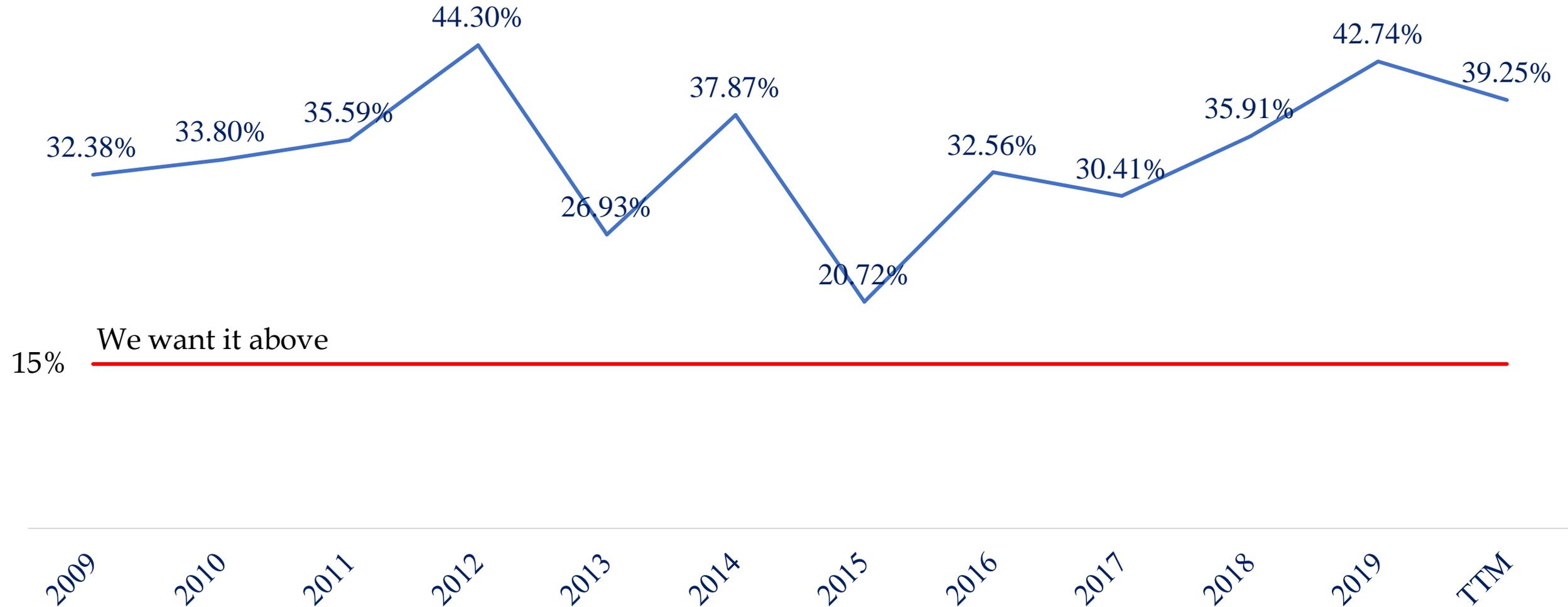
# Return on Equity with Treasury Stock



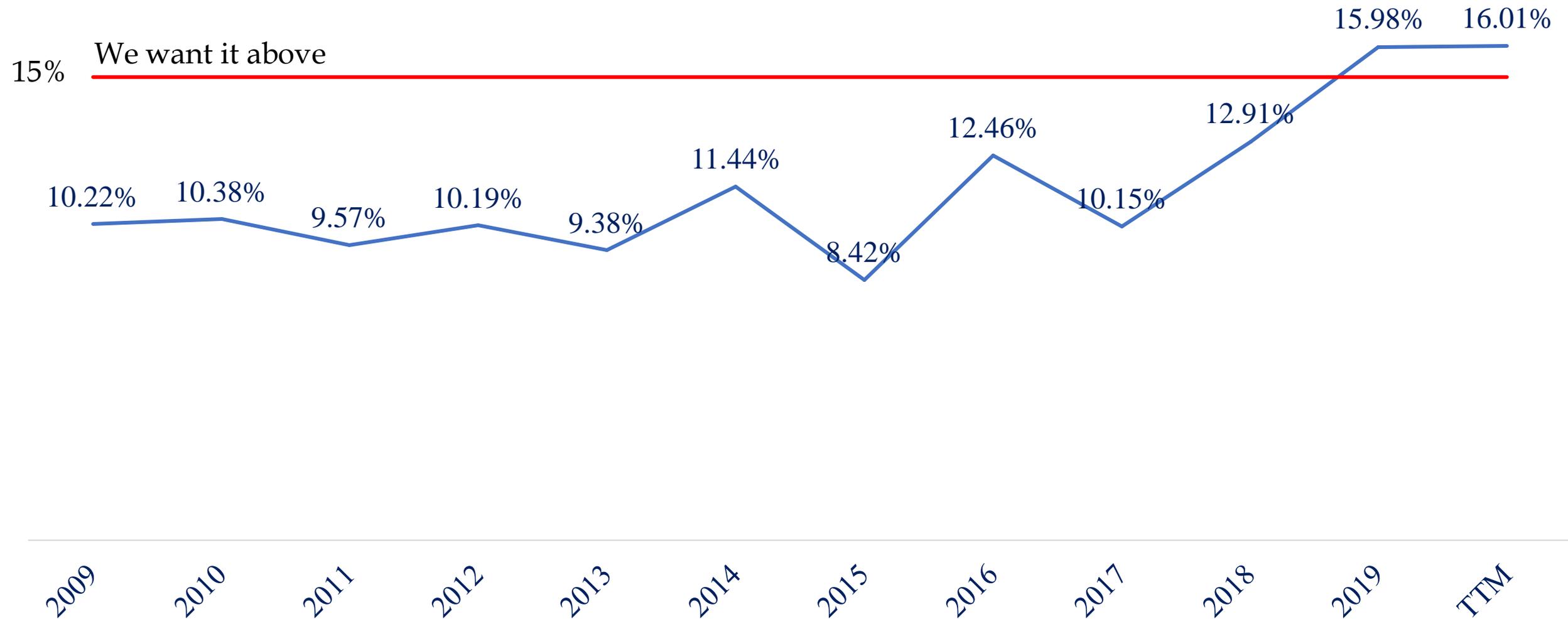
# Total Shareholder's Equity



# Return on Capital



# ROC with Intangible Assets & Goodwill



# Economic Moat



# Intangible Assets

- Product complexity, trade secrets guaranteed by the government because it is in their best interest
- Huge barriers to entry
- Product cycles last decades + lack of alternative suppliers
- Contract structure leads to excess returns



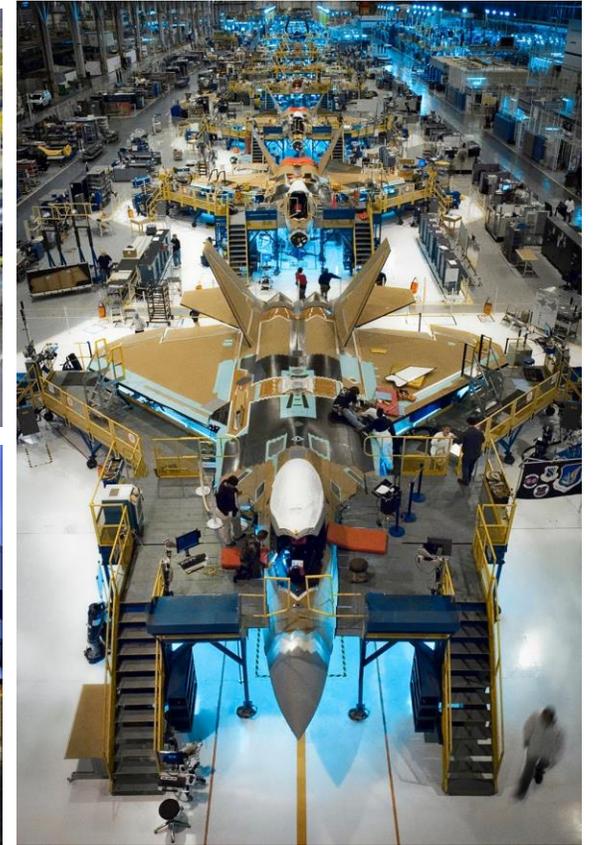
# Intangible Assets

- Classified Projects
  - Legal competitive advantage
  - Cannot disclose to competition
- Highly-skilled labor force
- Fixed-price contracts
  - Recurring revenue from older projects



# Switching Costs

- Sunk costs from the time spent developing a new product (New entrants)
- Contract awarding essentially grants a monopoly
- Historical lack of switching in DoD
- Costs to switch



# Switching Costs

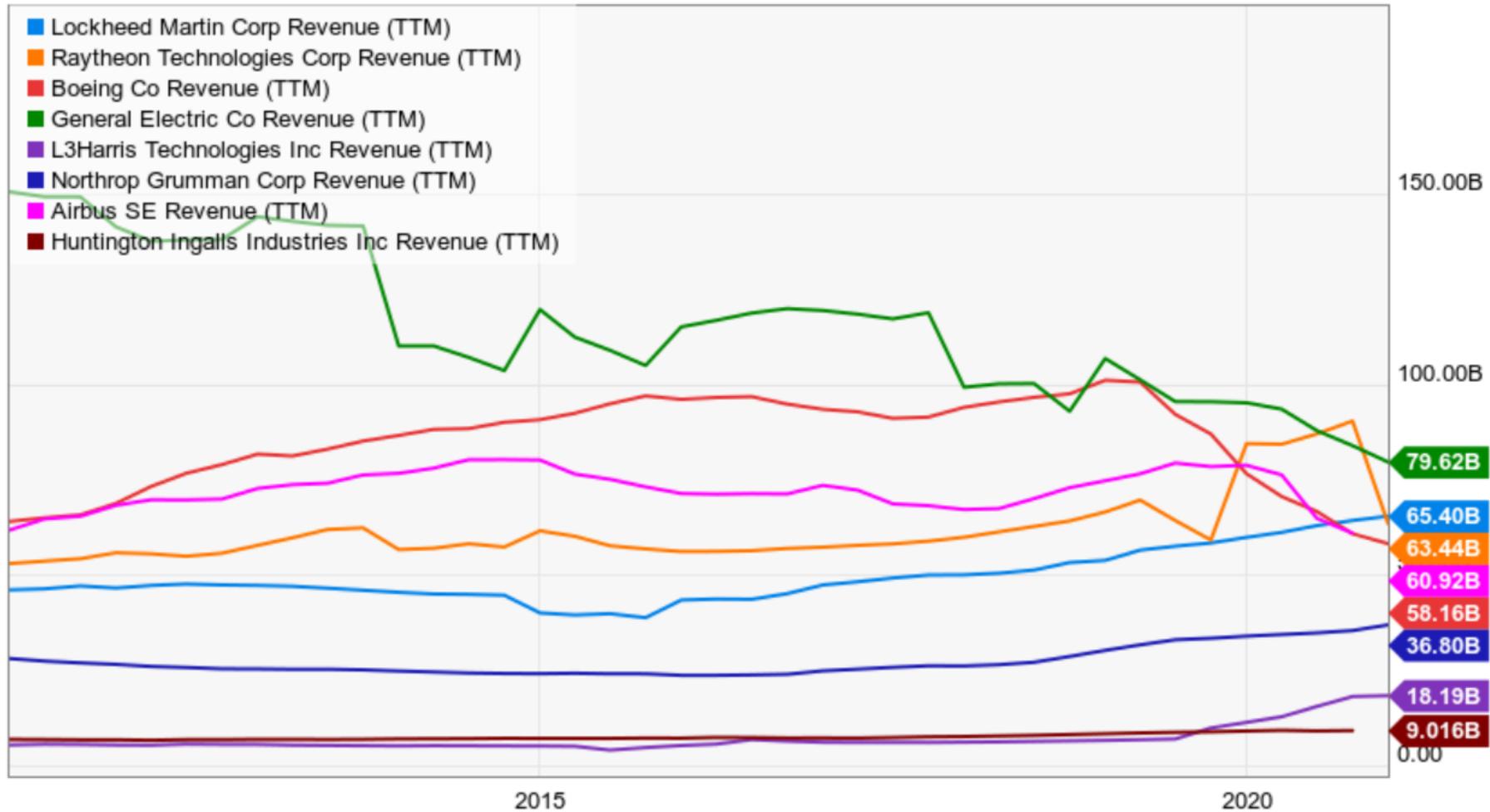
- Cost overruns
- Products are often mission-critical (Space, F-35)
- Lack of alternatives
- Mission criticality



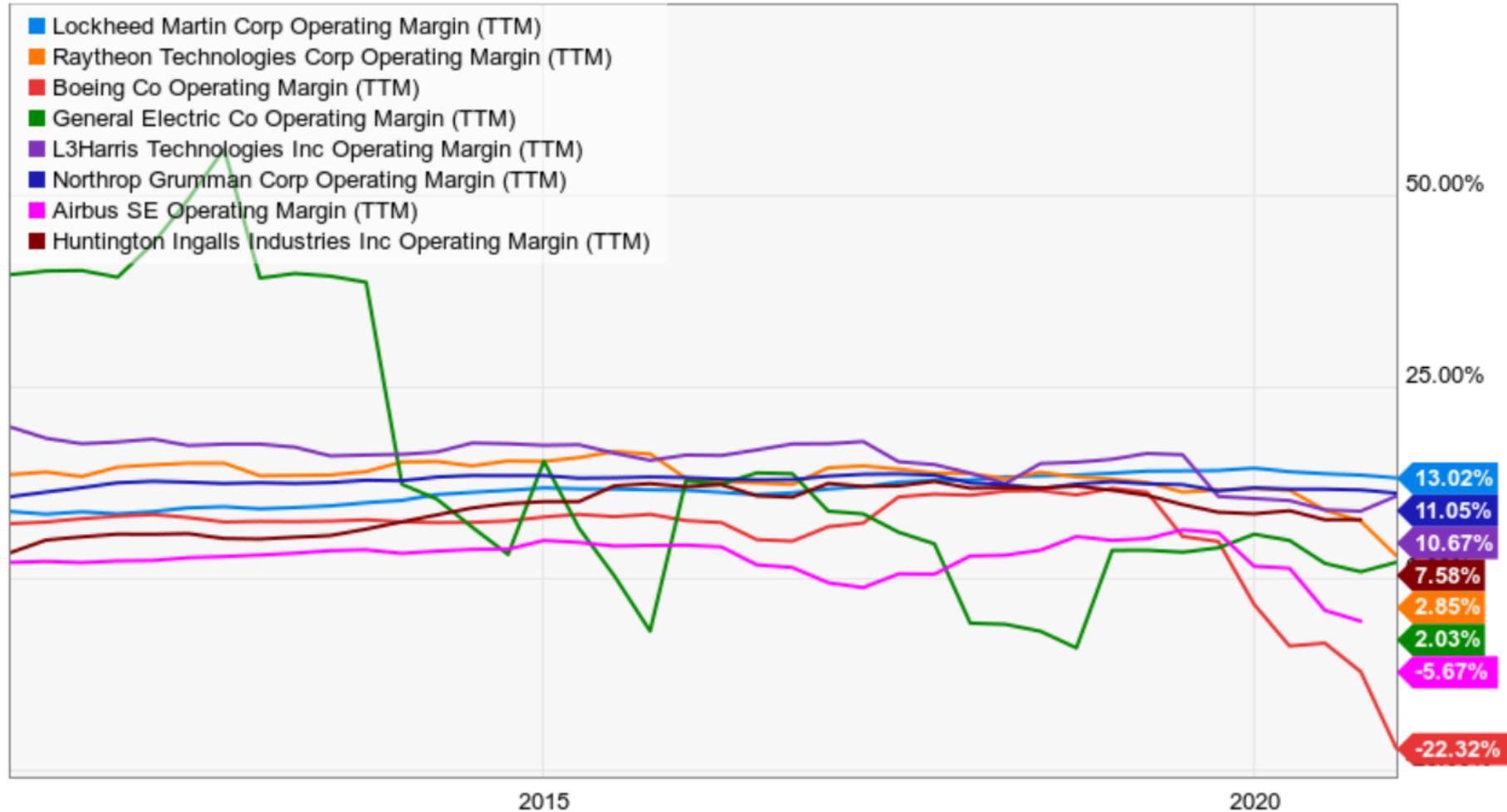
# Competitor Analysis



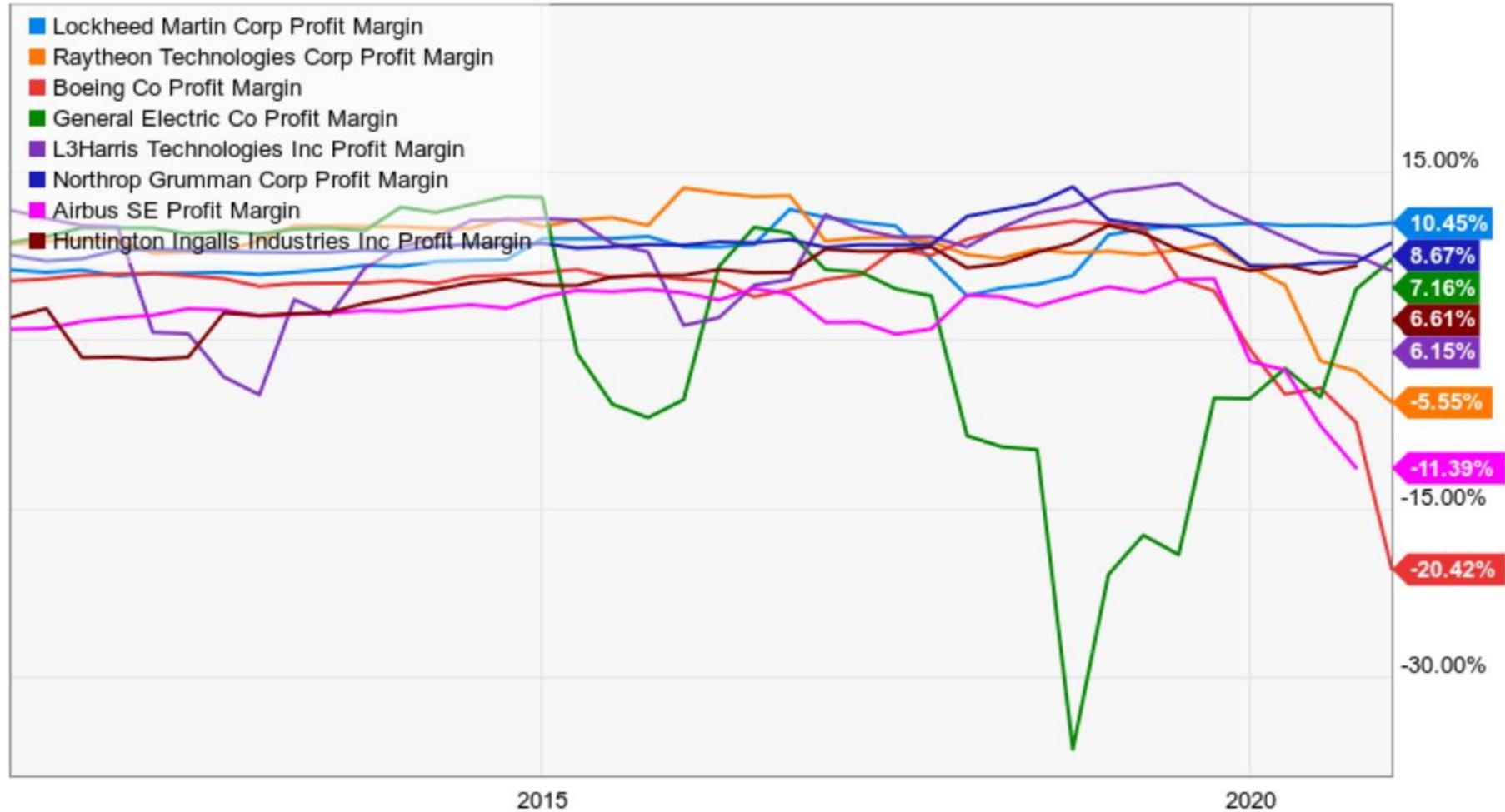
# Revenue



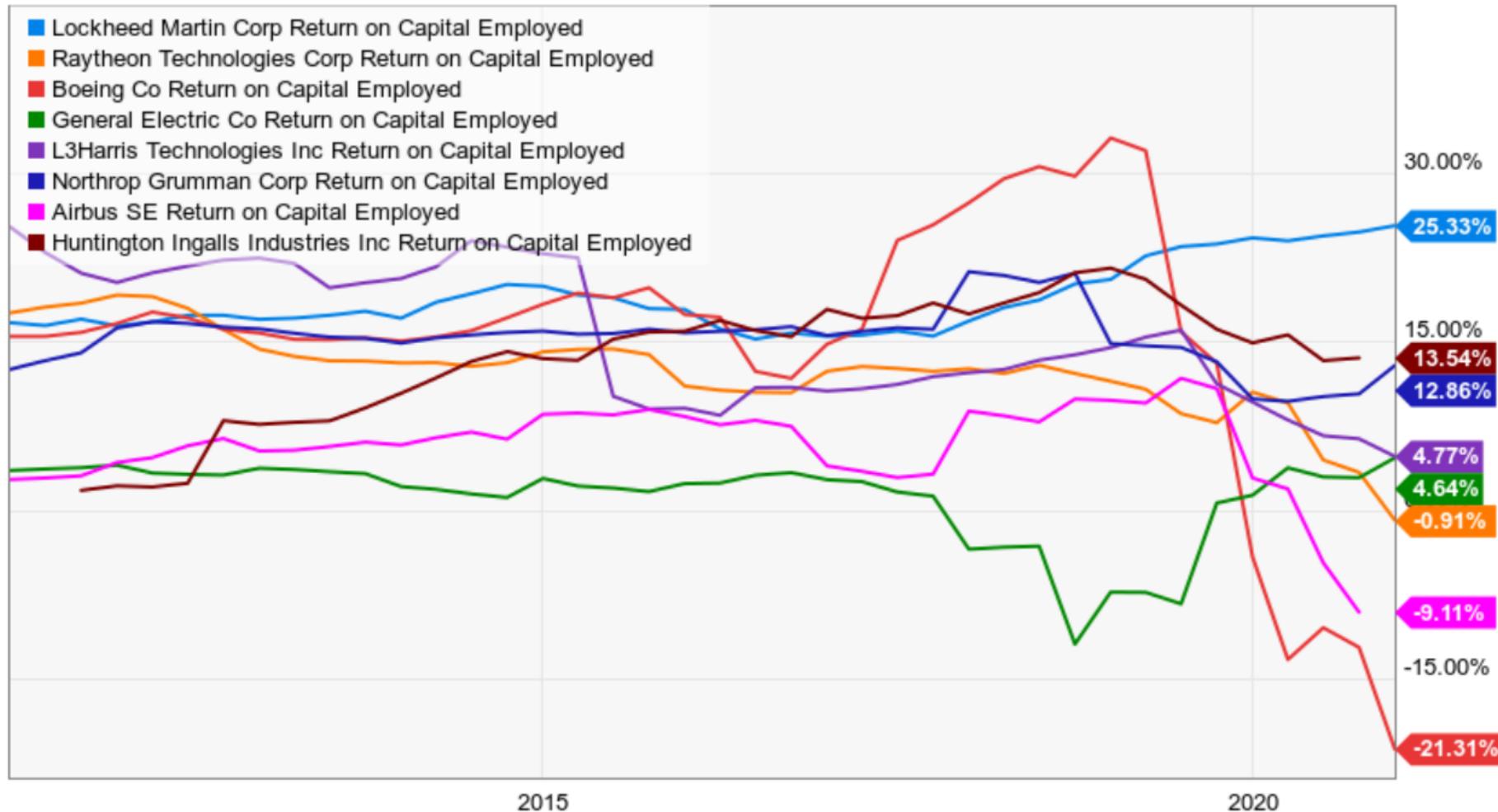
# Operating Margin



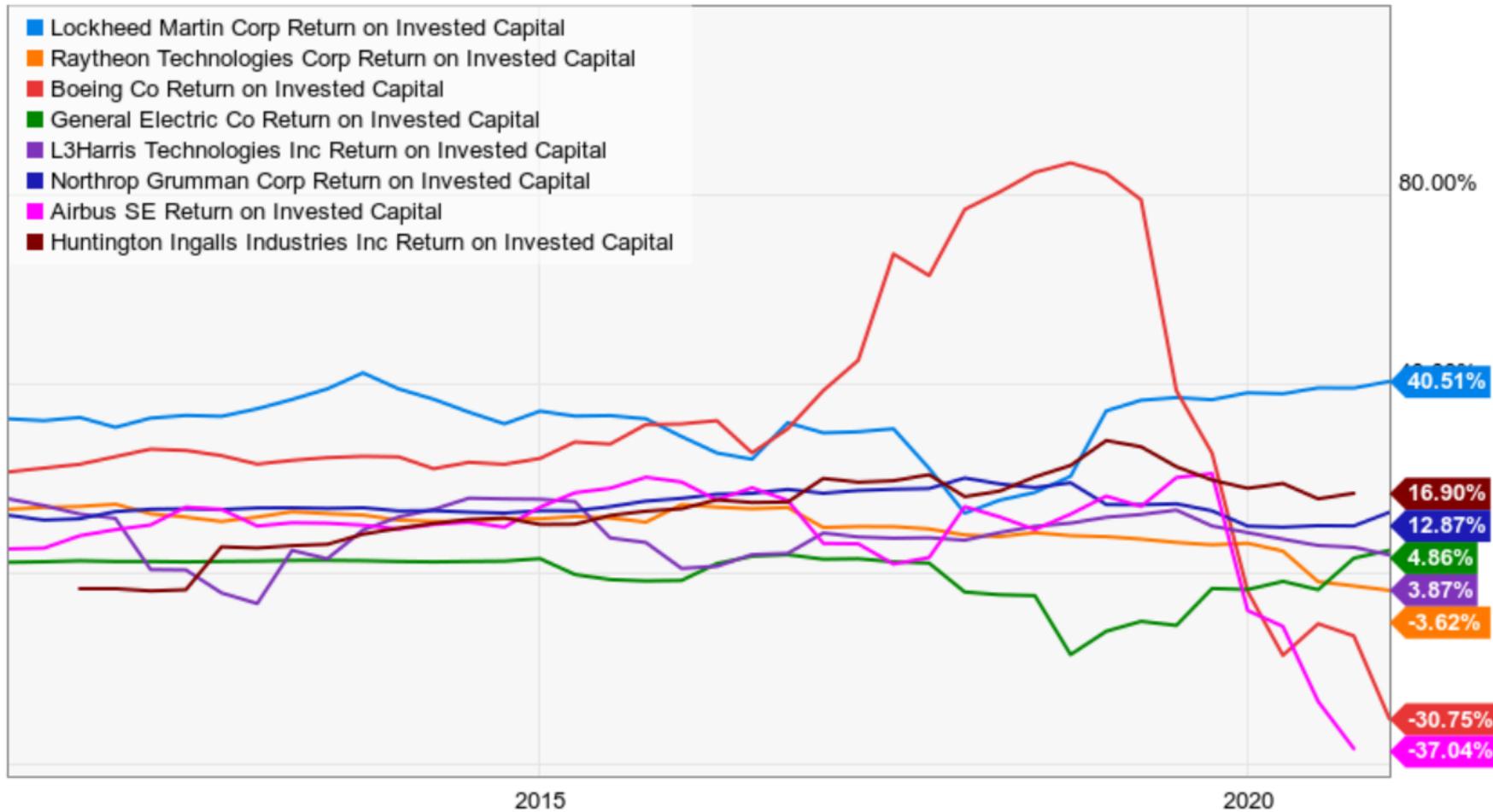
# Profit Margin



# Return On Capital Employed



# Return On Invested Capital



# Emerging Competitors

- Space X
- Blue Origin
- Virgin Galactic
- With their low-cost rockets that are reusable
- Able to take astronauts to US space base at a lower cost
- Have been winning contracts



# Risk Factors



# Risk Factors

- Customer Concentration
  - US Government: 71% of Sales
- Potential U.S. Defense Budget Cuts
  - 2020 Budget: \$721.5B
  - 2021 Budget: \$740B (proposed)
- Government's Right to Terminate Contracts
- Employee Unions and Pensions
  - 20% of Employees belong to unions



# Risk Factors

- Product Concentration
  - 27% of Sales from F-35
- Subcontractors and Suppliers failing to meet obligations
- Political Risk
- Fixed contracts – For newer programs potential cost overruns



**Donald J. Trump** @realDonaldTrump · 53m

Based on the tremendous cost and cost overruns of the Lockheed Martin F-35, I have asked Boeing to price-out a comparable F-18 Super Hornet!

← 3.1K ↻ 3.8K ❤️ 13K ⋮

# Management Overview



# Executive Changes

- James Taiclet joined June 2020
- Has been at the Board since 2018
- Replaced 35-year veteran Marilyn Hewson
- Michele Evans 32-year veteran passed
- Greg Ulmer who leads the F-35 program has filled in as LMT's Aeronautics unit in the interim



# Capital Allocation

## *Value to Shareholders*

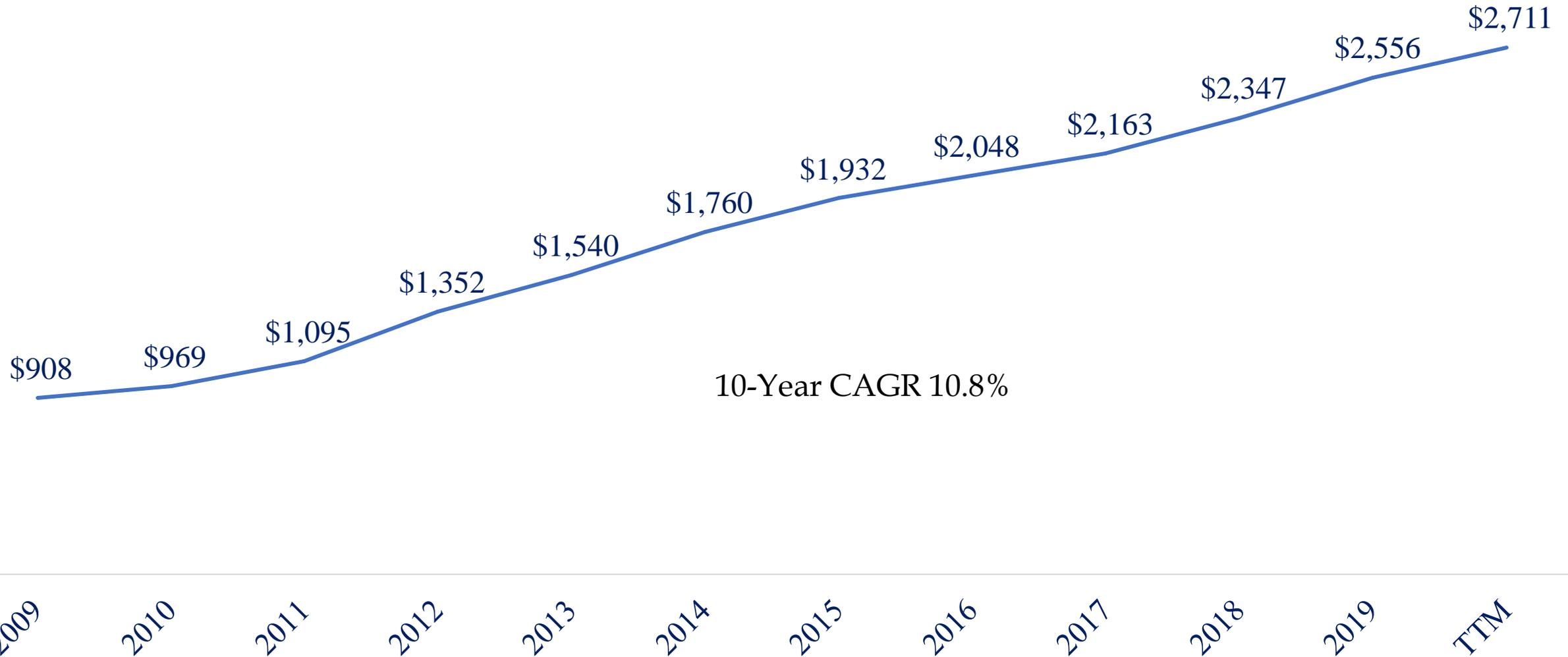
- Dividend yield 3%
- Dividend per share 13% 10-year CAGR
- Share buybacks 2.6% 10-year CAGR

## *Acquisitions*

- 1993 – General Dynamics aircraft division
- 1995 – Merger between Lockheed and Martin Marietta
- 2009 – Universal Systems & Technology
- 2015 – Sikorsky Manufacturing Corp.
- 2020 – Aerojet Rocketdyne

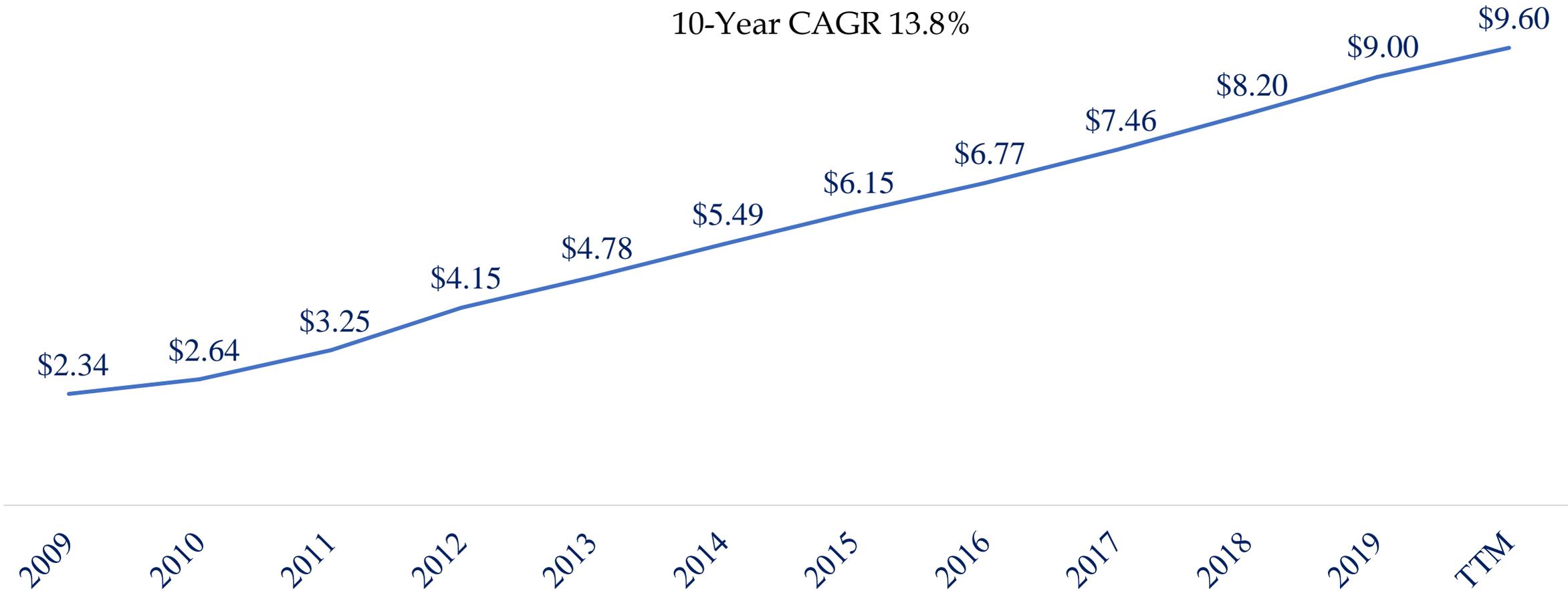


# Cash Flow Used For Dividends

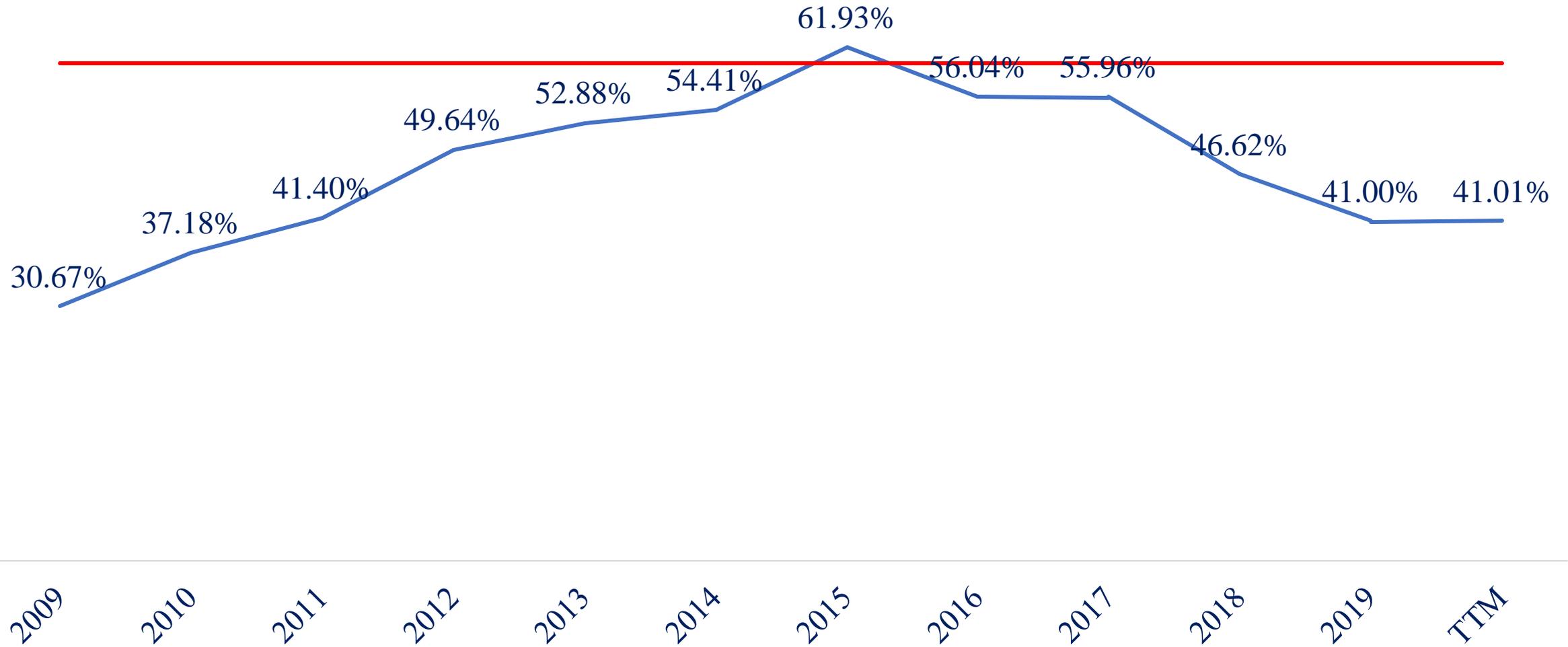


# Dividend Per Share

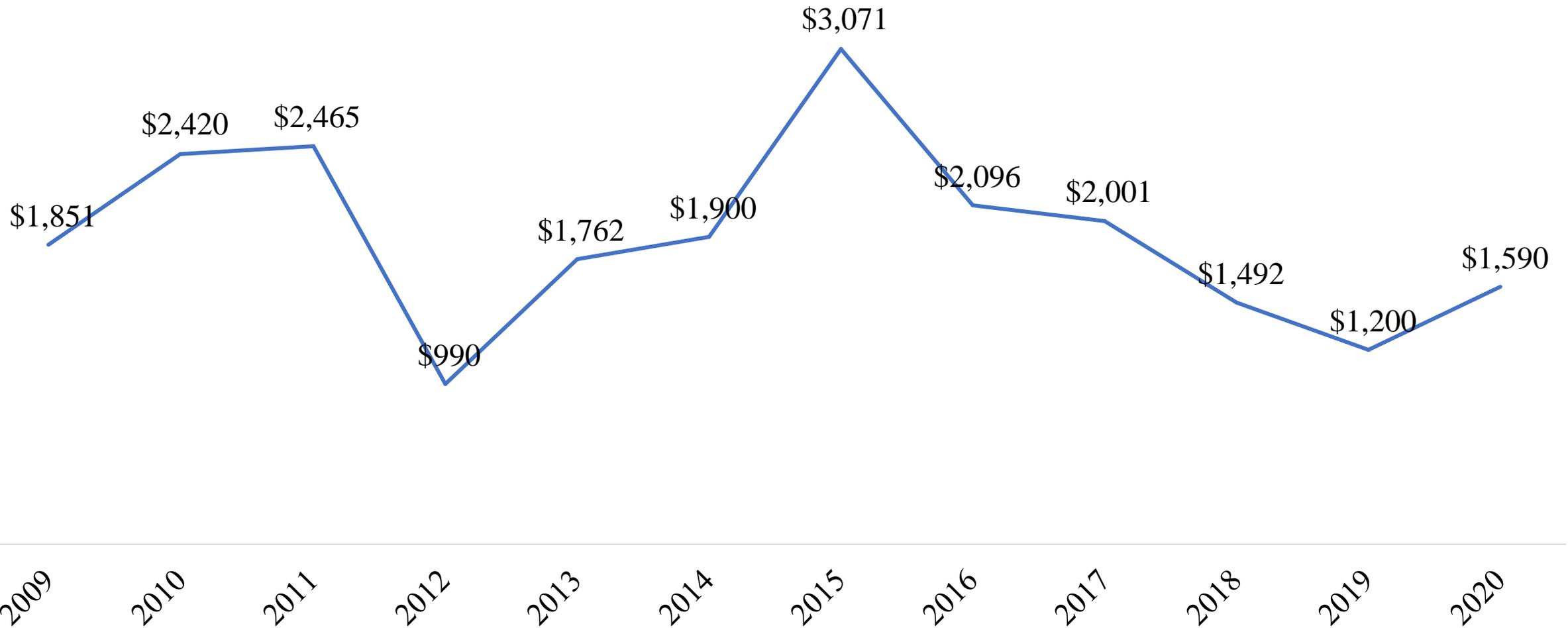
10-Year CAGR 13.8%



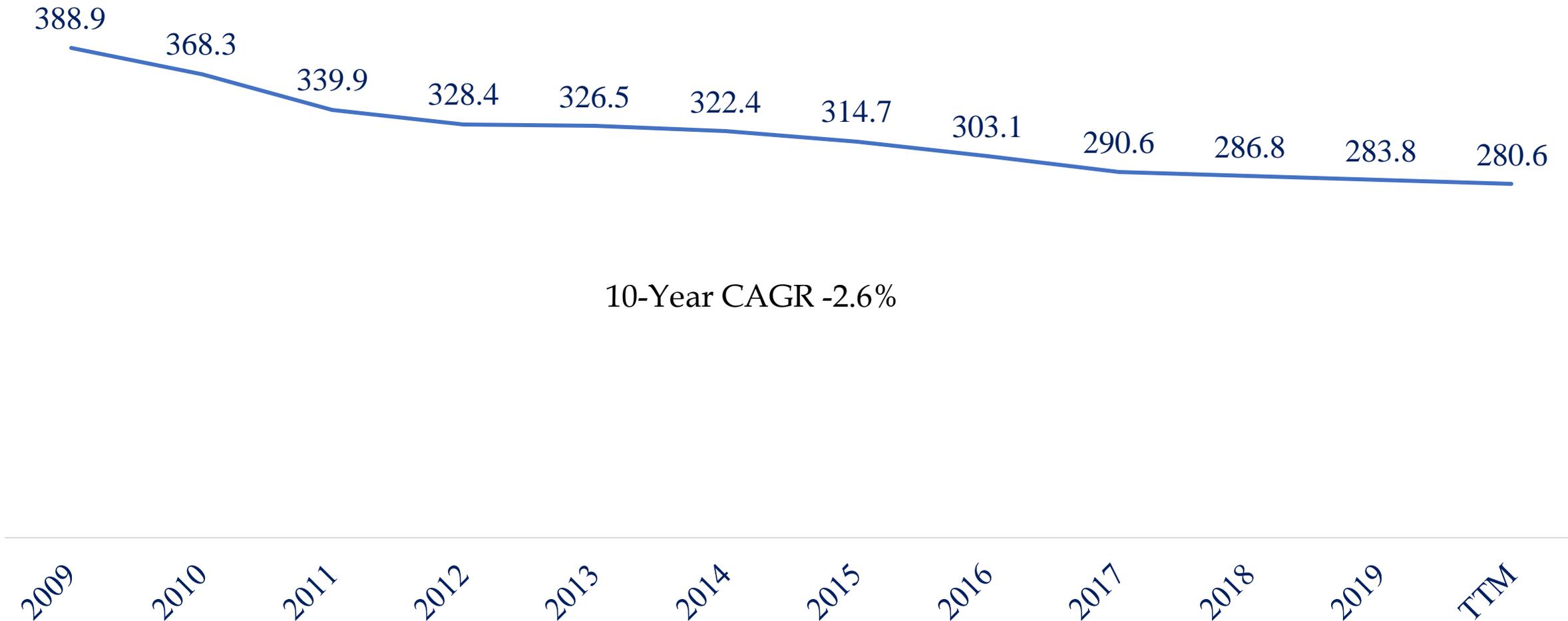
# Payout Ratio



# Cash Used To Repurchase Stock



# Shares Outstanding



# Growth Opportunities



# F-35 Lightning Fighter Jet

- \$80M fighter jet.
- Contracts span until 2070.
- \$34B with the U.S. Government produce 478 F-35s.
- Singapore is seeking to acquire 4 F-35s, with the option to buy 8 more.
- A proposed sale to Poland was approved for \$6.5B.



# Missile & Fire Control

- \$11.8B contract to upgrade missile-defense capabilities to the U.S and Allied forces.
- 7-year contract for more than 300,000 Training Aid missiles for \$3.53B.
- \$1.1B contract for 9,800 rockets for the GMLRS.
- \$988M contract with the U.S Air Force to take the ARRW program through review.



# Rotary & Mission Systems

- Build up to 22 next-generation GPS III satellite for the Air Force for \$7.2B.
- Contract for the THAAD program for \$4.8B.
- \$1.3B contract with the Navy to build 12 CH-35K King Stallion. Begin 2022.
- Secured a \$478.61M Navy contract to modify their Sikorsky aircraft. Expected by 2023.



# Aeronautics and Space Segments

## *Aeronautics*

- 40% Increase in delivered Aircraft.
- Bahrain ordered 16 and Slovakia 14 new F-16s.

## *Space*

- \$2.7B awarded to deliver the first 3 Orion spacecraft, and a second order in 2022



# Aerojet Rocketdyne

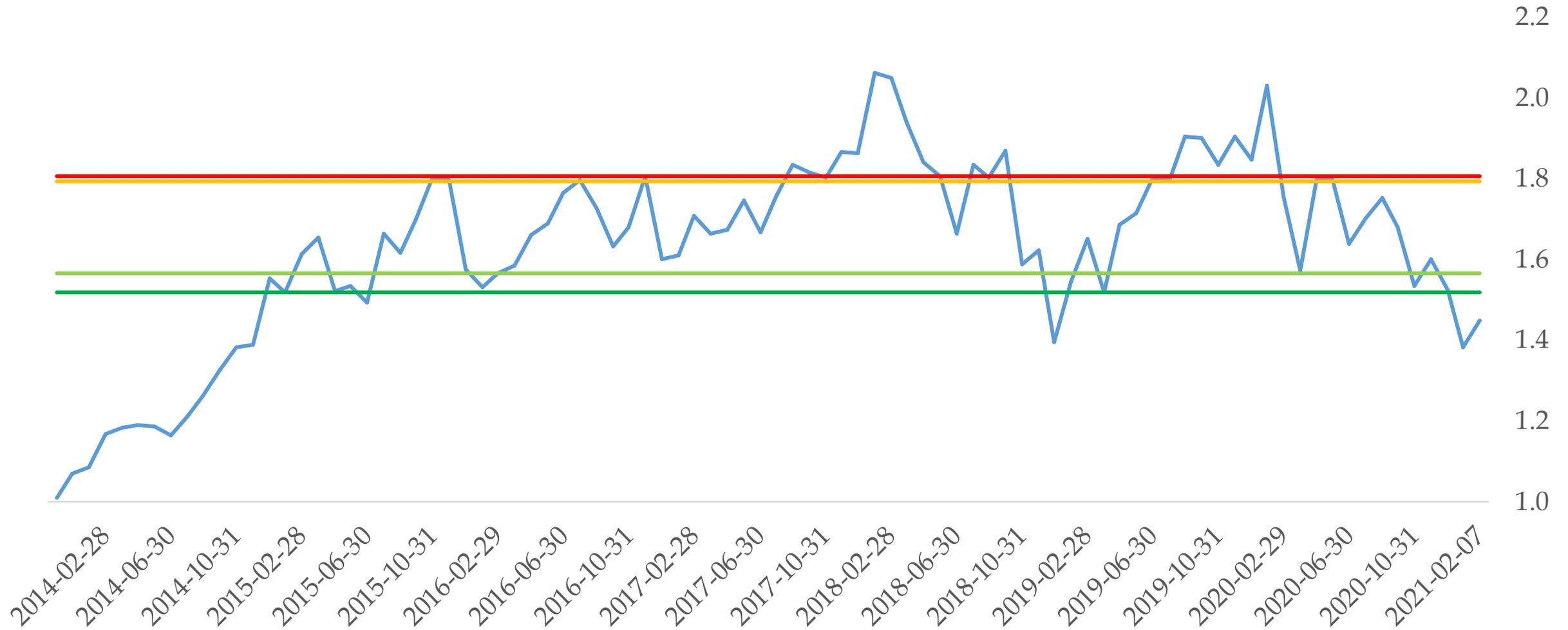
- To acquire AJRD for \$56 per share for \$4.4B cash
- Pre closing dividend of \$5 per share bringing deal down to \$51 per share or \$4.1B
- Deal closing 2<sup>nd</sup> half of 2021
- Friendly merger
- High regulatory hurdle
- LMT 33%, Raytheon 17% or revenues
- Annual revenue of \$2.2B, LMT makes that in two weeks
- Acquisition critical to missile defense, hyper sonics, and space segments



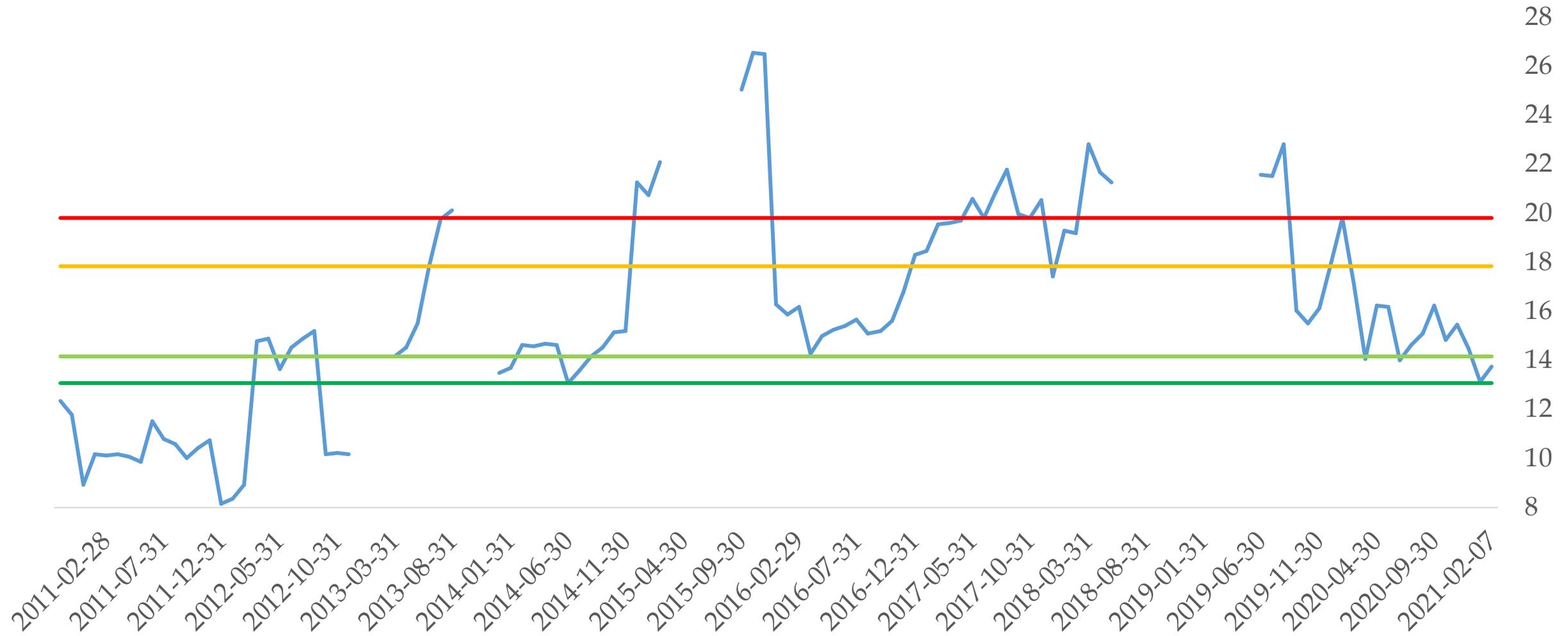
# Valuation



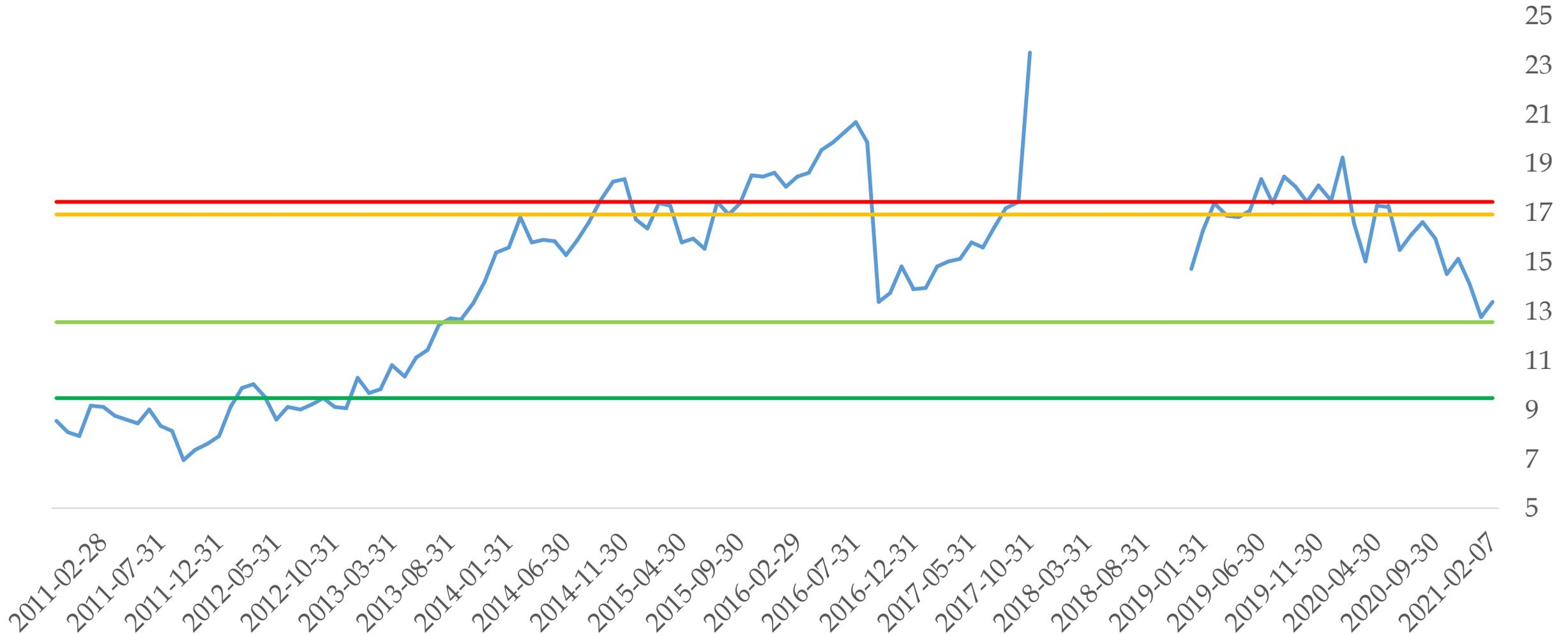
# Price to Sales



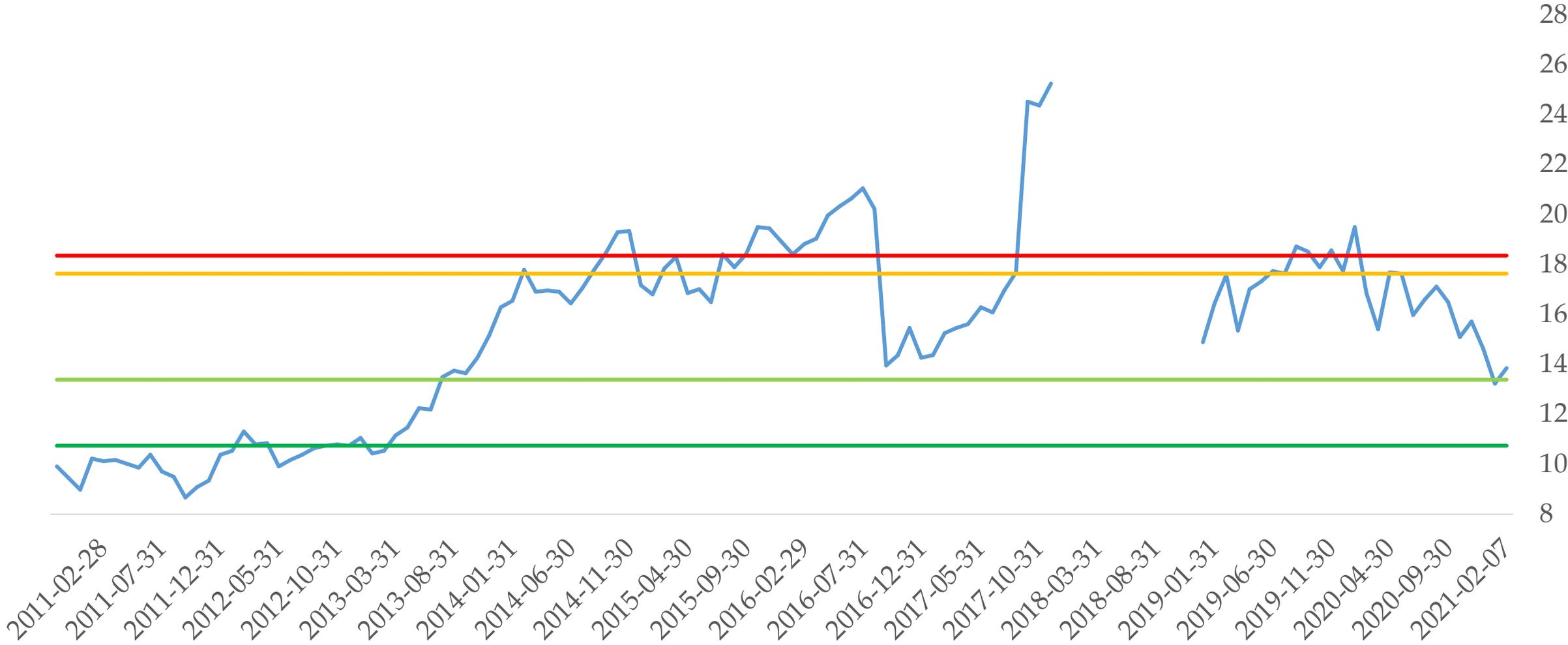
# Price to Owner's Earnings



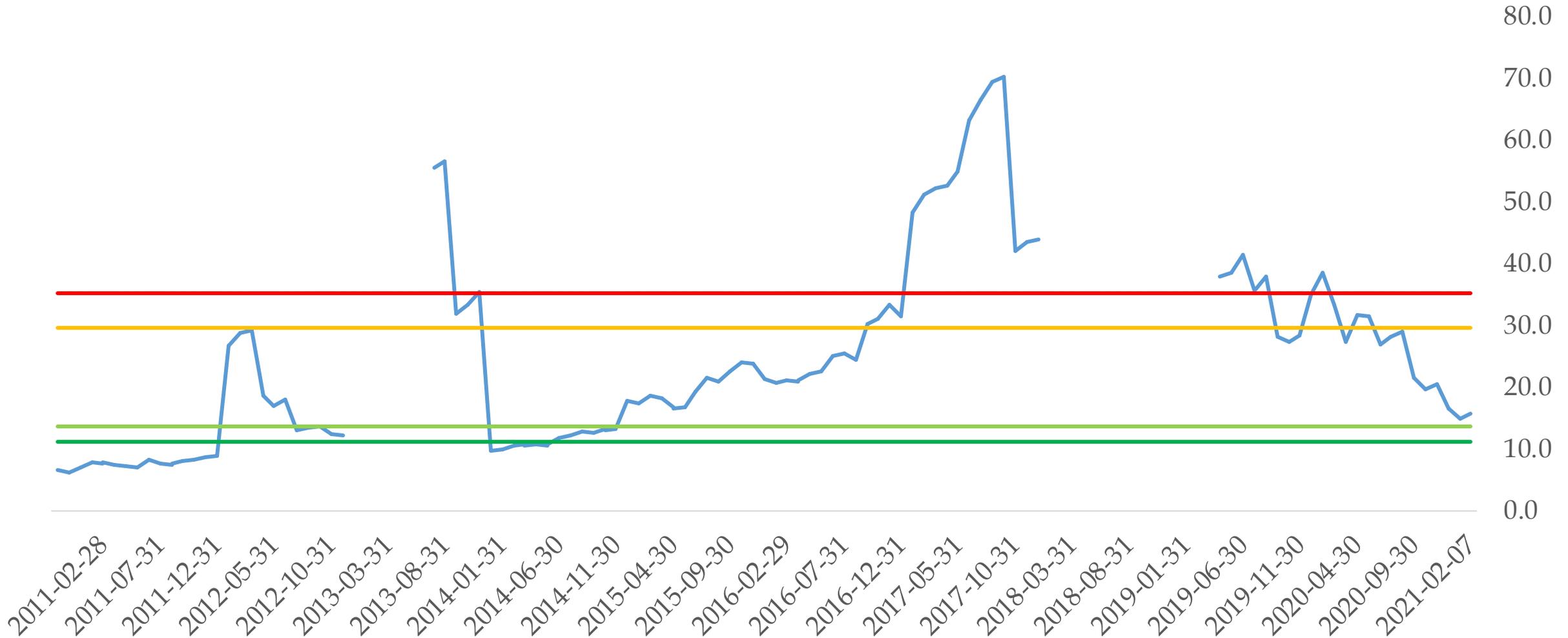
# Price to Earnings Less Cash



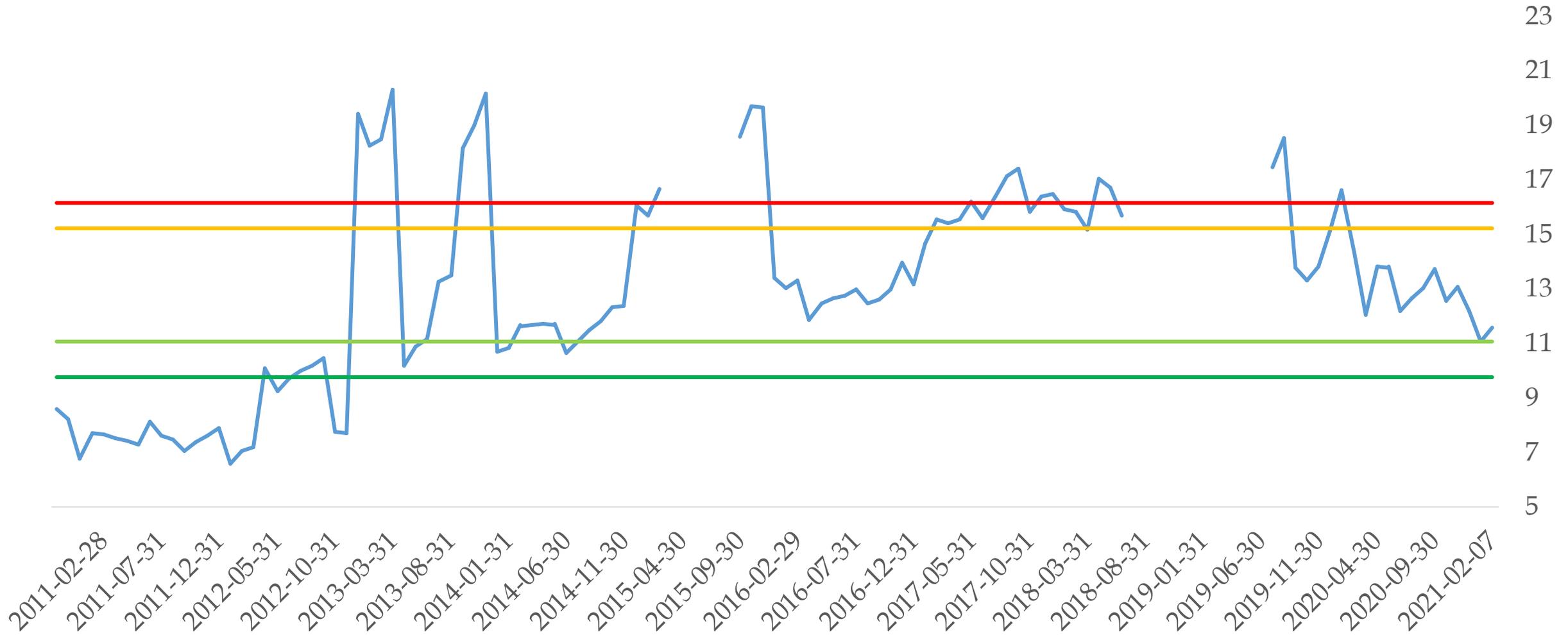
# Price to Earnings



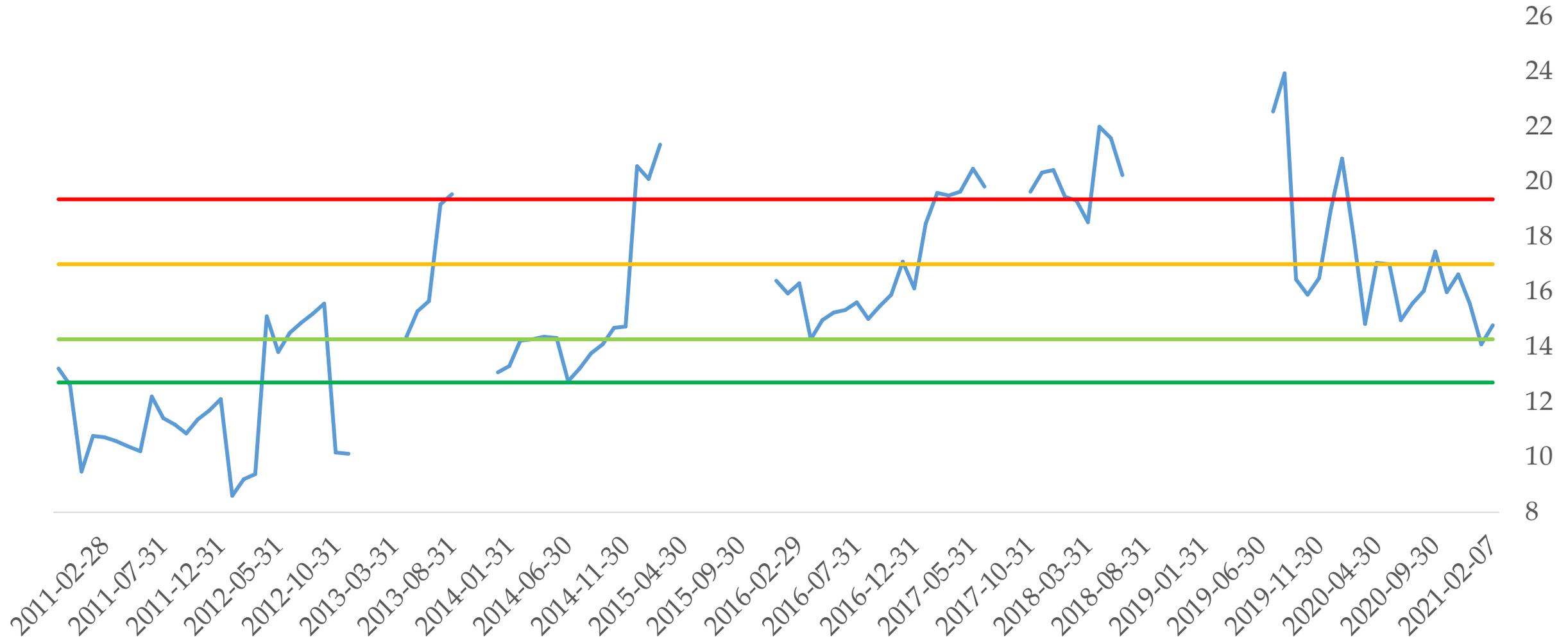
# Price to Book Value



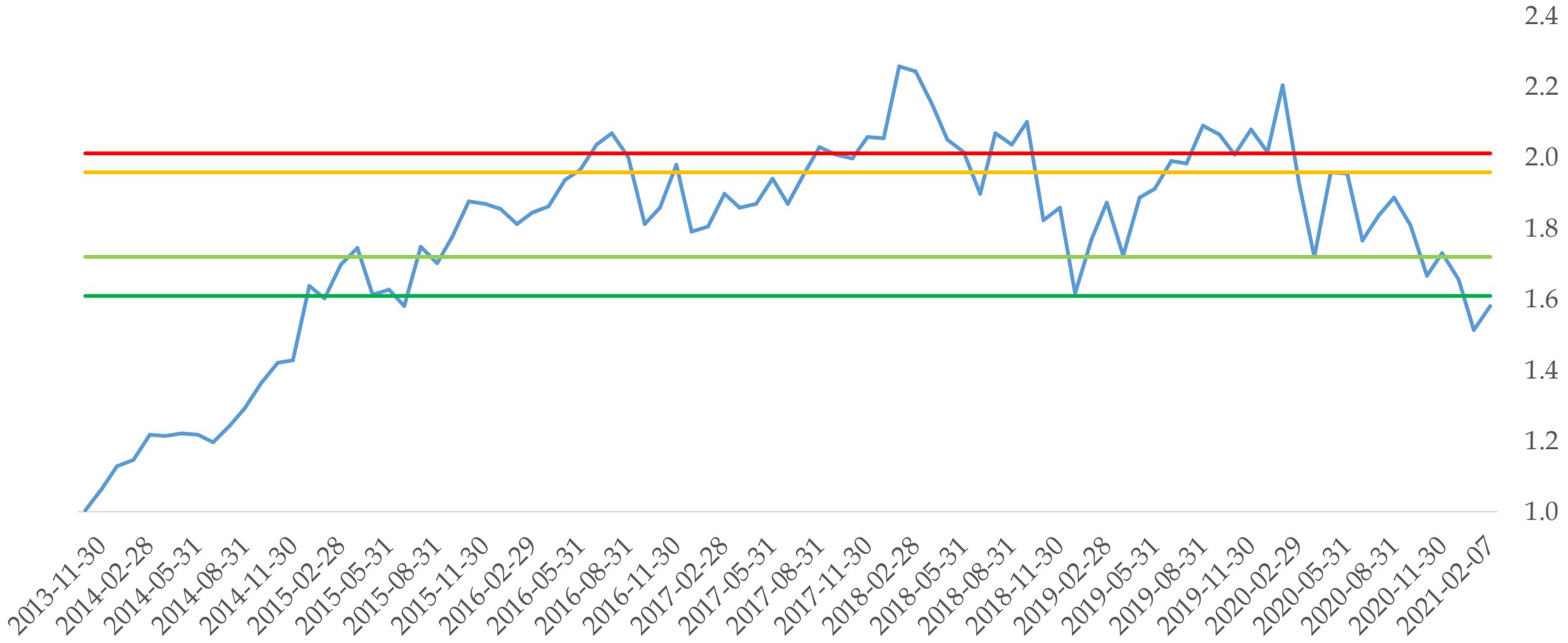
# Price to Cashflow



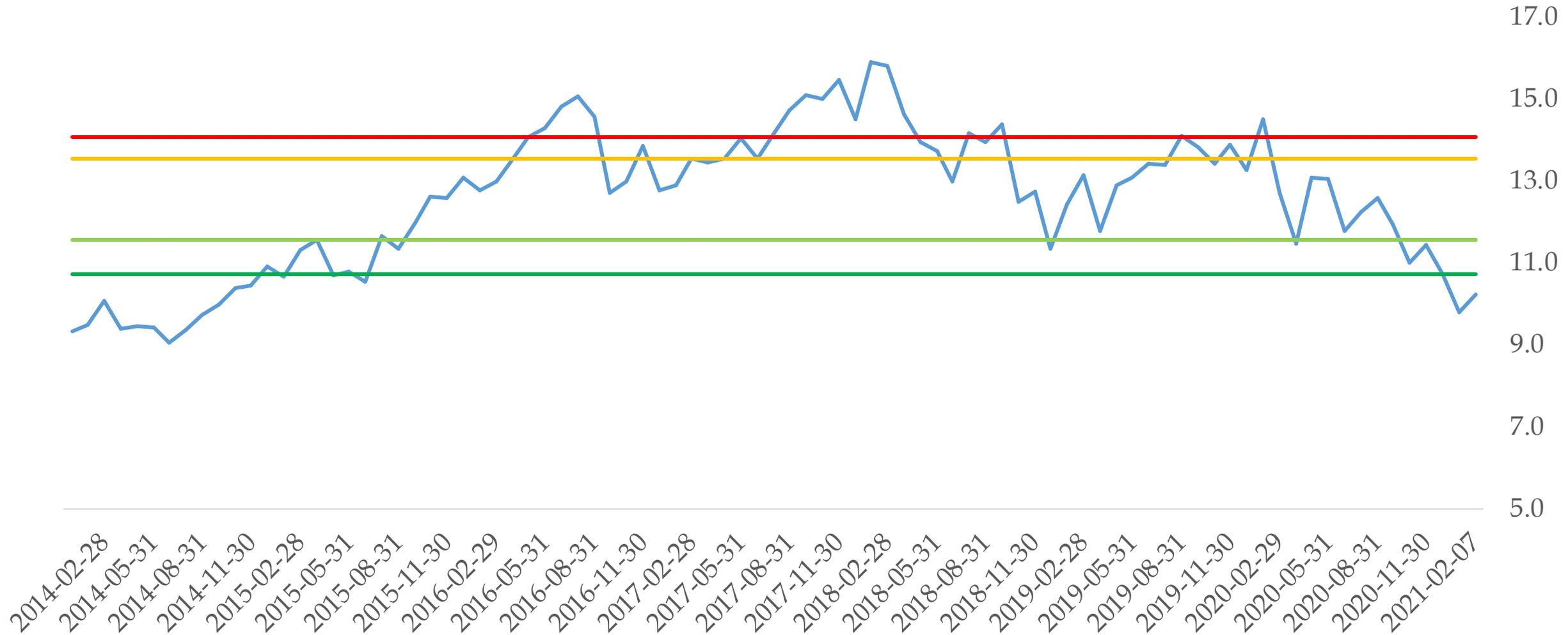
# Price to Free Cash Flow



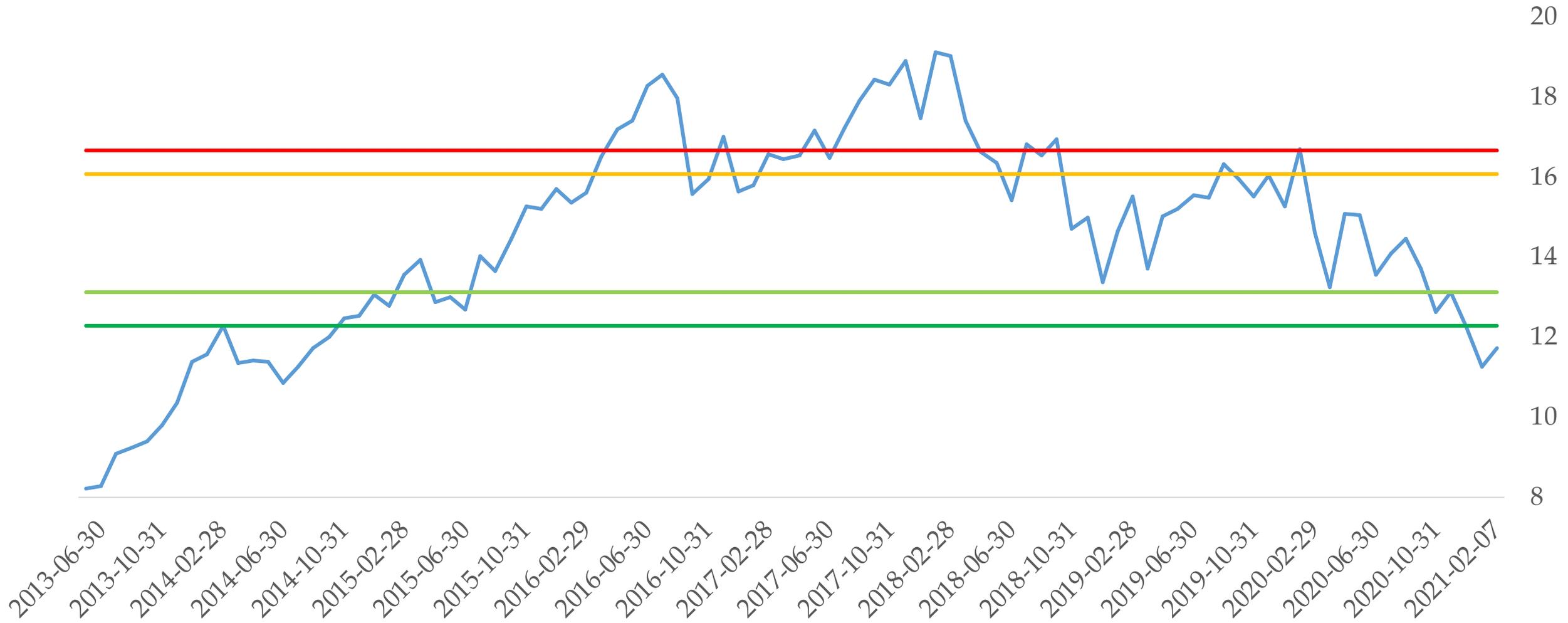
# EV to Revenue



# EV to EBITDA



# EV to EBIT



# Bear Case DCF

EPS \$24.30

Growth Rate 5%

Discount Rate 10%

Years 10

Terminal Rate 4%

Fair Value **\$303.38**

Current Price \$337.04

Margin of Safety **-11.09%**

# Base Case DCF

<u>EPS</u>	\$24.30
<u>Growth Rate</u>	7%
<u>Discount Rate</u>	10%
<u>Years</u>	10
<u>Terminal Rate</u>	4%

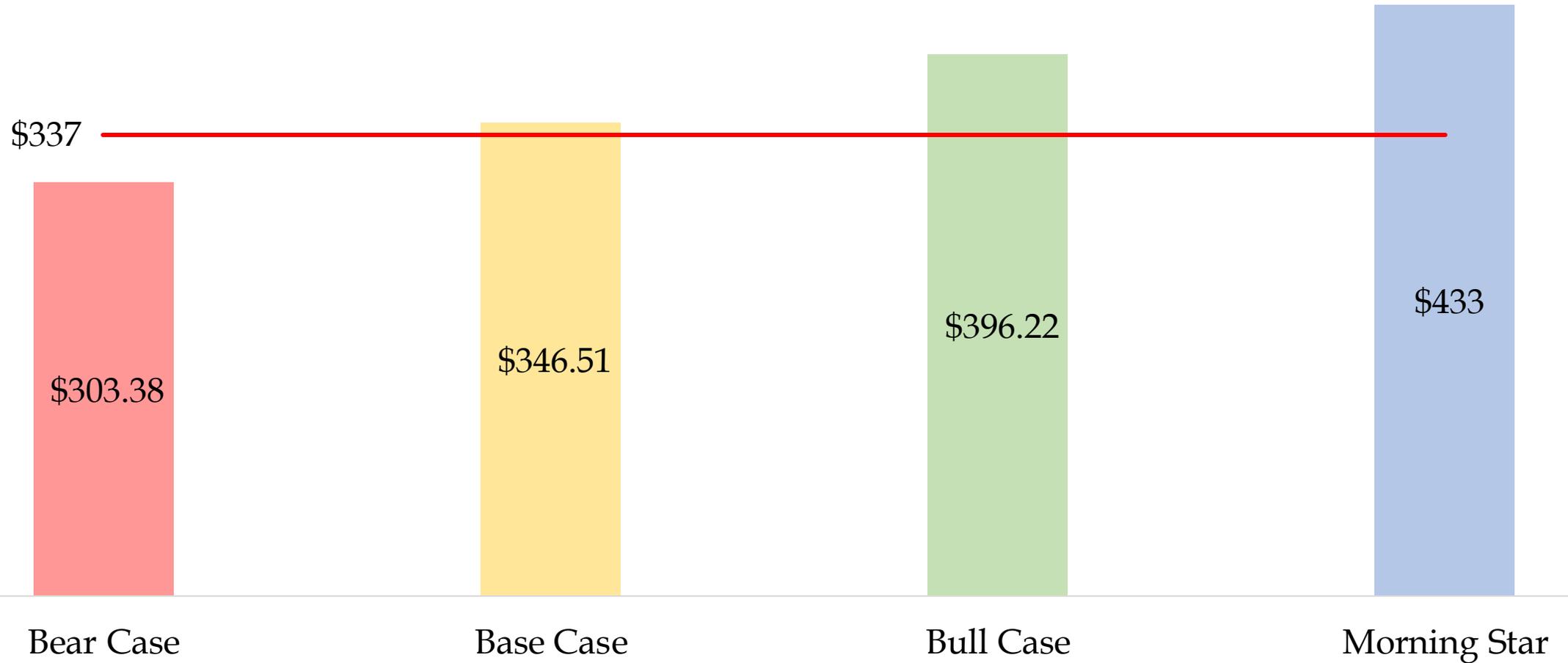
Fair Value	<b>\$346.51</b>
Current Price	<u>\$337.04</u>
Margin of Safety	<b>2.73%</b>

# Bull Case DCF

<u>EPS</u>	\$24.30
<u>Growth Rate</u>	5%
<u>Discount Rate</u>	10%
<u>Years</u>	10
<u>Terminal Rate</u>	4%

Fair Value	<b>\$396.22</b>
Current Price	<u>\$337.04</u>
Margin of Safety	<b>14.94%</b>

# Fair Value Scenarios



# Bear Case 5-year Magical DCF

P/E      Projected Price      Discount Rate 10%

Annual Return

10.0x

\$310.14

\$192.57

0.2%

15.0x

\$465.20

\$288.86

8.7%

20.0x

\$620.27

\$385.14

15.1%

Current

2021

2022

2023

2024

2025

EPS

\$24.30

\$25.52

\$26.79

\$28.13

\$29.54

\$31.01

5yr growth estimate

5%

5%

5%

5%

5%

# Base 5-year Magical DCF

P/E      Projected Price      Discount Rate 10%

	Current	2021	2022	2023	2024	2025	P/E	Projected Price	Discount Rate 10%	Annul Return
<b>EPS</b>	\$24.30	\$26.00	\$27.82	\$29.77	\$31.85	\$34.08	10.0x	\$340.82		<u>-1.7%</u>
							15.0x	\$511.23		<u>6.7%</u>
<b>5yr growth estimate</b>		7%	7%	7%	7%	7%	20.0x	\$681.64		<u>13%</u>
									\$211.62	
									\$317.43	
									\$423.24	

# Bull Case 5-year Magical DCF

							P/E	Projected Price	Discount Rate 10%	
	Current	2021	2022	2023	2024	2025	10.0x	\$373.89		Annual Return
EPS	\$24.30	\$26.49	\$28.87	\$31.47	\$34.30	\$37.39	15.0x	\$560.83	\$232.15	<u>2.1%</u>
5yr growth estimate		9%	9%	9%	9%	9%	20.0x	\$747.77	\$348.23	<u>10.7%</u>
									\$464.31	<u>17.3%</u>

# Conclusion



# Conclusion

- Highest quality prime contractor
- Wide moat company
- TINA – There Is no Alternative
- Trading at a significant discount to Fair Value
- Due to uncertainty not risk
- 3% of our portfolio \$337 per share limit order

The ICE Man



# The Frugalicious Team



Esam Hijazi



Luis Green



Brandon Chaney



Rafael Bracho



Diego Garcia



Ethan Sanchez



# Sensitivity Analysis

		Est. EPS growth rate		
		5%	7%	9%
Price/Earnings	10.0x	-1.7%	0.2%	2.1%
	15.0x	6.7%	8.7%	10.7%
	20.0x	13.0%	15.1%	17.3%