



Lockheed Martin Q2 FY2022

Logan, Ethan, Luis, and Brandon

General Company Info

- **Stock Price:** \$398 per share
- **Market Cap:** \$105.53B
- **Headquarters:** Bethesda, Maryland
- **CEO:** James Taiclet 2020
- **Shares:** 300
- **Cost Basis:** \$339
- **Percentage of Portfolio:** 10%
- **Dividend Yield:** 2.84%



	2022 Q2	2021 Q2	Q2 2020	1-YR CAGR	2-YR CAGR
Net sales	\$ 15,446	\$ 17,029	\$ 16,220	-9.3%	-2.4%
Cost of sales	\$ (13,490)	\$ (14,878)	\$ (14,007)	-9.3%	-1.9%
Gross profit	\$ 1,956	\$ 2,451	\$ 2,213		
Other income, net	\$ 7	\$ 41	\$ (127)	-82.9%	
Operating profit	\$ 1,963	\$ 2,192	\$ 2,086	-10.4%	-3.0%
Interest expense	\$ (141)	\$ (142)	\$ (149)	-0.7%	-2.7%
Non-service FAS pension (expesne)	\$ (1,331)	\$ 94	\$ -		
Other non-operating (expense) income, net	\$ (161)	\$ 120	\$ 25		
Earnings before income taxes	\$ 330	\$ 2,170	\$ 1,962	-84.8%	-59.0%
Income tax epsense	\$ (21)	\$ (355)	\$ (336)	-94.1%	-75.0%
Net earnings	\$ 309	\$ 1,815	\$ 1,626	-83.0%	-56.4%
Diluted EPS	\$ 1.16	\$ 6.52	\$ 5.79	-82.2%	-55.2%
FCF	\$ 1,027	\$ 950	\$ 1,839	8.1%	-25.3%
				<i>Difference</i>	<i>Difference</i>
Operating Margin	12.7%	-2.1%	-2.1%	14.8%	14.8%
Net Profit Margin	2.0%	10.7%	10.0%	-8.7%	-8.0%
FCF Margin	6.6%	5.6%	11.3%	1.1%	-4.7%

(in millions, except per share data)

	Quarter Ended June 26, 2022			Quarter Ended June 27, 2021		
	Earnings Before Income Taxes	Net Earnings	Diluted EPS	Earnings Before Income Taxes	Net Earnings	Diluted EPS
As Reported (GAAP)	\$ 330	\$ 309	\$ 1.16	\$ 2,170	\$ 1,815	\$ 6.52
Pension settlement charge	1,470	1,156	4.33	—	—	—
Lockheed Martin Ventures investment losses (gains)	143	107	0.40	(14)	(11)	(0.04)
Losses (gains) on assets in trust for deferred compensation obligations	61	46	0.17	(24)	(18)	(0.06)
Debt refinancing transaction	34	26	0.10	—	—	—
Change in effective tax rate ¹	N/A	41	0.16	N/A	—	—
Total Adjustments	1,708	1,376	5.16	(38)	(29)	(0.10)
As Adjusted (Non-GAAP)²	\$ 2,038	\$ 1,685	\$ 6.32	\$ 2,132	\$ 1,786	\$ 6.42

¹ Represents the impact of the change in the estimated annual effective tax rate primarily due to lower earnings before income taxes associated with the pension settlement charge, which will be realized in the third and fourth quarters of 2022.

² See the "Use of Non-GAAP Financial Measures" section of this news release for more information.

Q2 2022 Highlights

Lockheed Martin posted a revenue and earnings decline, but improved segment operating margins. The company missed Q2 earnings and revenue estimates and lowered its full-year EPS and revenue guidance. A decrease in volumes, throughout the divisions, and a decline in volumes from the F-35 have led to revenue and operating profit falling. Management stated that problems stemming from winter and early spring COVID-19 outbreaks had hit the company and its suppliers, slowing production.

F-35 sales were down related to supply chain and inflationary pressures. Lockheed is waiting for additional funding on the F-35 Lots 15-17. Costs were negotiated in late 2019 and did not account for the supply chain headwinds and the inflationary environment. Since costs increased above available funding, it prevented the recognition of 5.5% of segment sales, and total aeronautics sales decreased by 12.1%.

The company generated \$15.45B in revenue which was 3.7% below analyst estimates. GAAP EPS of \$1.16 missed estimates by 6%. Earnings dropped significantly to \$309M, dropping from \$1.8B last year. Quarterly earnings were highly impacted by a non-cash pension risk transfer. Excluding the pension settlement of \$4.33 per share, LMT venture investment losses of \$0.40, losses on assets in trust for deferred compensation of \$0.17, debt refinancing of \$0.10, and the change in the change in the effective tax rate of \$0.16 the EPS would have been \$6.32, down by 1.6% from \$6.42 last year.

FY 2022 Guidance

Lockheed lowered its FY 2022 EPS guidance by 19.3% to \$21.55 from \$26.70 and sales by 1.13% to \$65.25B from \$66B. The company's expectations for three of its segments have been reduced due to supply chain impacts, award timing, and program schedule shifts. Management lowered its EPS guidance by \$5.15 due to the impact of one-time items, such as pension transfer, debt refinancing, and YTD mark-to-market adjustments. The pension settlement charge is now included in the company's outlook.



Revenue by Segment

For the Aeronautics segment sales were down by 12% due to lower F-35 sales related to supply chain impacts and the firm waiting for additional funding. For the Missile and Fire Control group sales were lower by 6.7% due to the withdrawal of US troops from Afghanistan. For Rotary and Mission Systems sales declined by 5.4% due to lower volumes for the Black Hawk and the Presidential helicopter. The Space segment sales decreased by 11.1% reduction from the renationalization of the atomic weapons establishment. The renationalization of the AWE program has been completed as it occurred in July 2021.



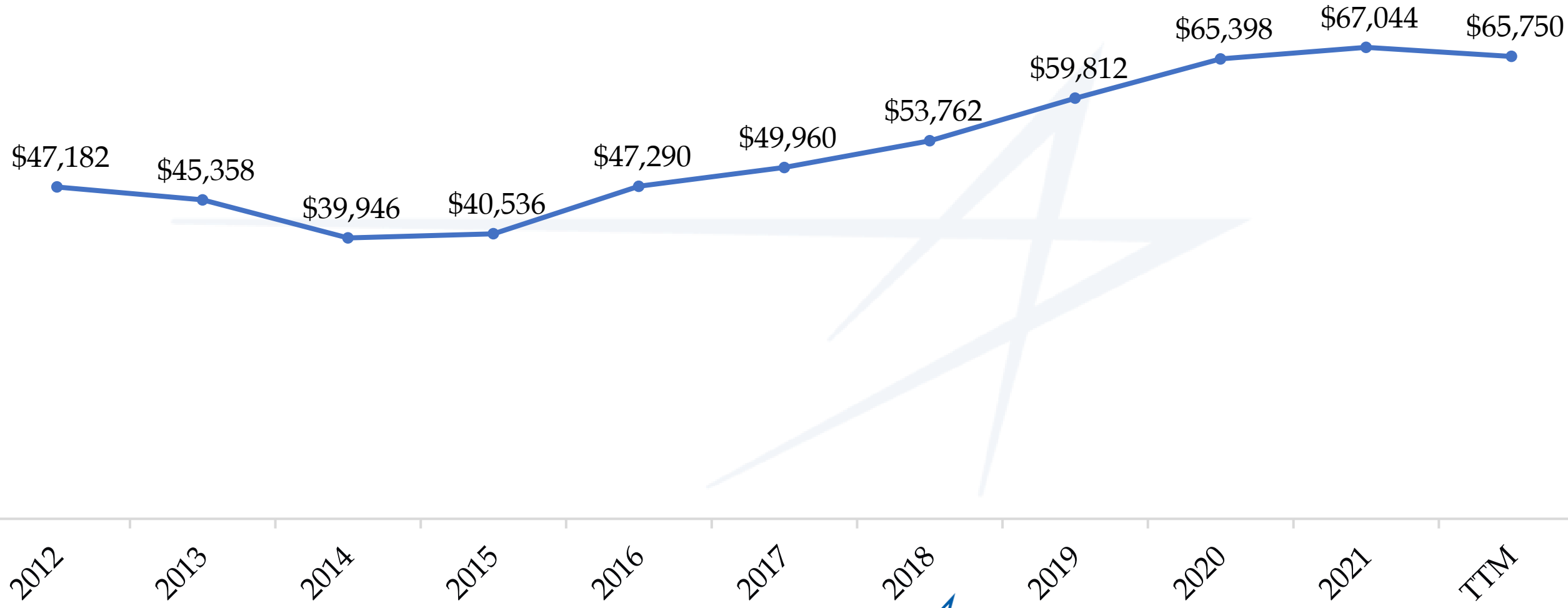
Segment Results	2022 Q2	2021 Q2	Q2 2020	1-YR CAGR	2-YR CAGR
Net sales					
Aeronautics	\$ 5,862	\$ 6,666	\$ 6,503	-12.1%	-5.1%
Missiles and Fire Control	\$ 2,747	\$ 2,944	\$ 2,801	-6.7%	-1.0%
Rotary and Mission Systems	\$ 4,012	\$ 4,242	\$ 4,039	-5.4%	-0.3%
Space	\$ 2,825	\$ 3,177	\$ 2,877	-11.1%	-0.9%
Total net sales	\$ 15,446	\$ 17,029	\$ 16,220	-9.3%	-2.4%
Operating profit					
Aeronautics	\$ 612	\$ 572	\$ 739	7.0%	-9.0%
Missiles and Fire Control	\$ 418	\$ 401	\$ 370	4.2%	6.3%
Rotary and Mission Systems	\$ 403	\$ 458	\$ 429	-12.0%	-3.1%
Space	\$ 268	\$ 335	\$ 252	-20.0%	3.1%
Total business segment profits	\$ 1,701	\$ 1,766	\$ 1,790	-3.7%	-2.5%
Unallocated items					
FAS/CAS operating adjustment	\$ 425	\$ 489	\$ 469	-13.1%	-4.8%
Severance and restructuring charges	\$ -	\$ -	\$ -	0.0%	0.0%
Other, net	\$ (163)	\$ (63)	\$ (173)	158.7%	-2.9%
Total unallocated items	\$ 262	\$ 426	\$ 296	-38.5%	-5.9%
Total consolidated operating profit	\$ 1,963	\$ 2,192	\$ 2,086	-10.4%	-3.0%
Operating margin				Difference	Difference
Aeronautics	10.4%	8.6%	11.4%	1.9%	-0.9%
Missiles and Fire Control	15.2%	13.6%	13.2%	1.6%	2.0%
Rotary and Mission Systems	10.0%	10.8%	10.6%	-0.8%	-0.6%
Space	9.5%	10.5%	8.8%	-1.1%	0.7%
Total business segment profits	11.0%	10.4%	11.0%	0.6%	0.0%
Total consolidated operating profit	12.7%	12.9%	12.9%	-0.2%	-0.2%



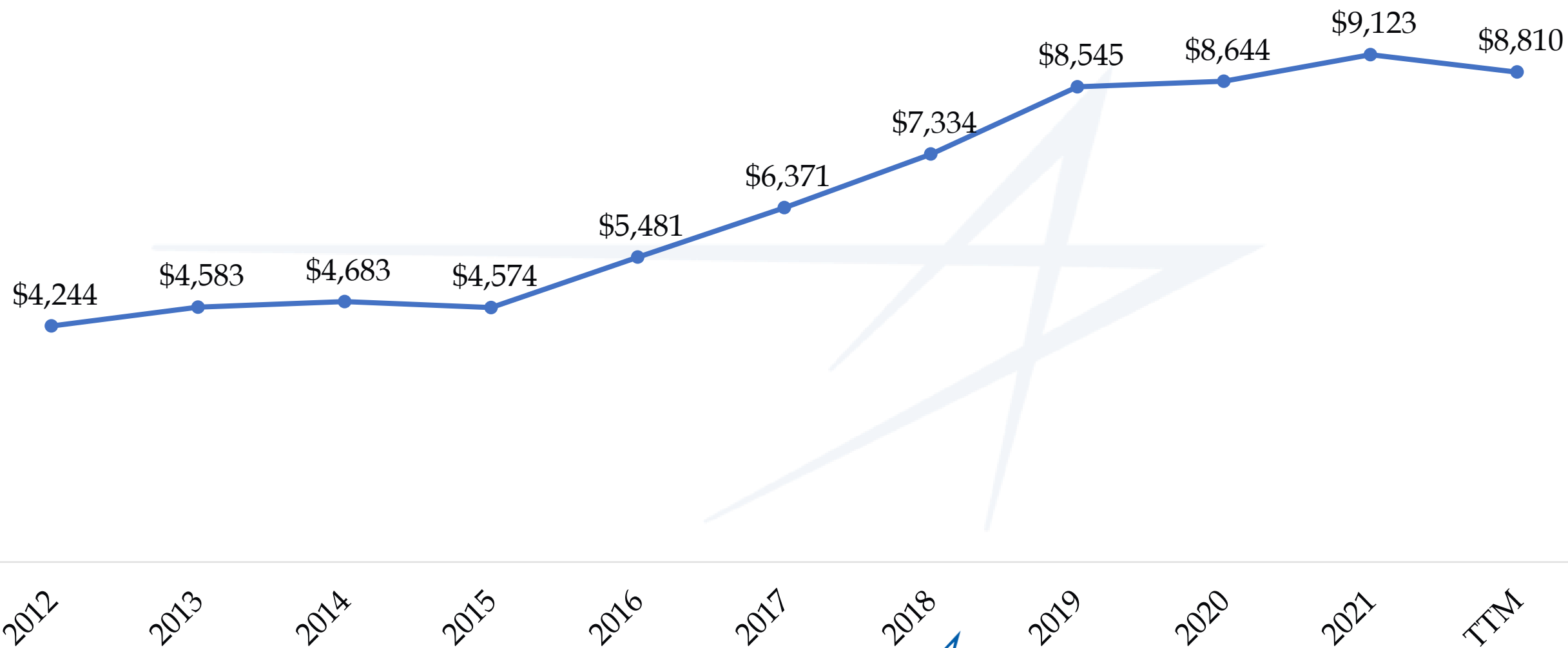
Interpretations of Financial Statements



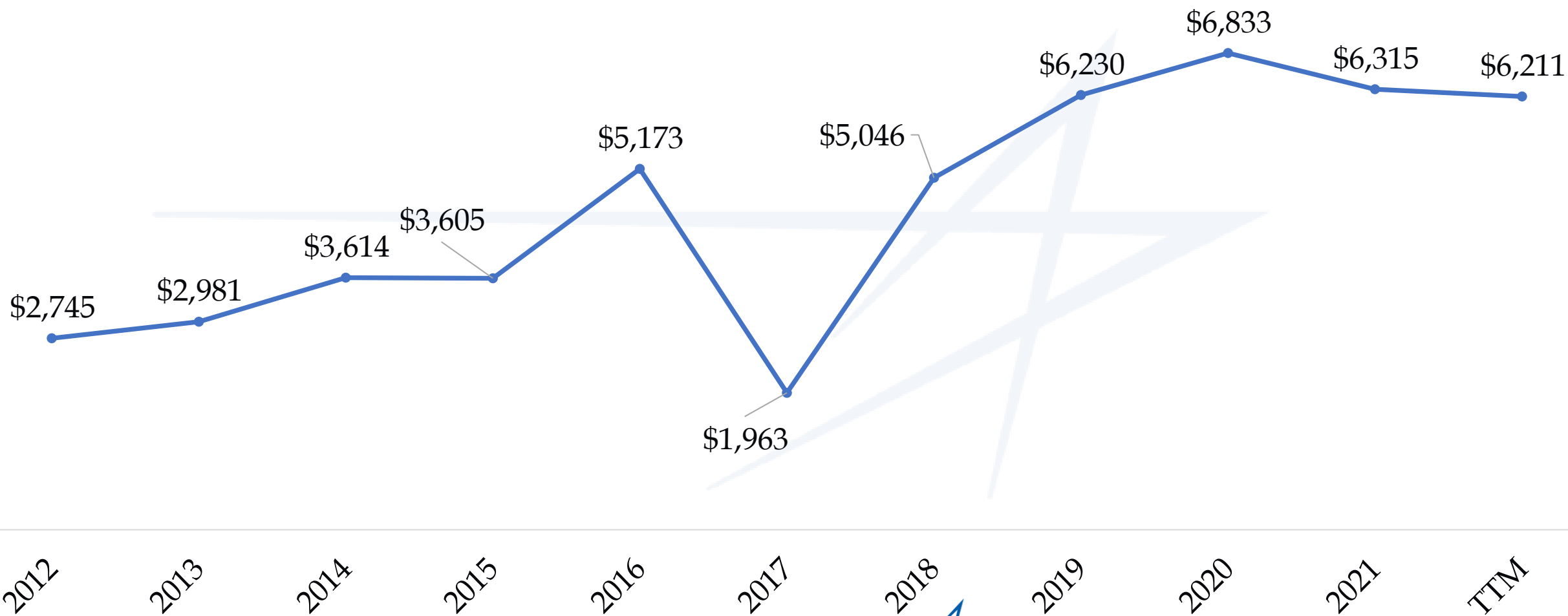
Revenue (in millions)



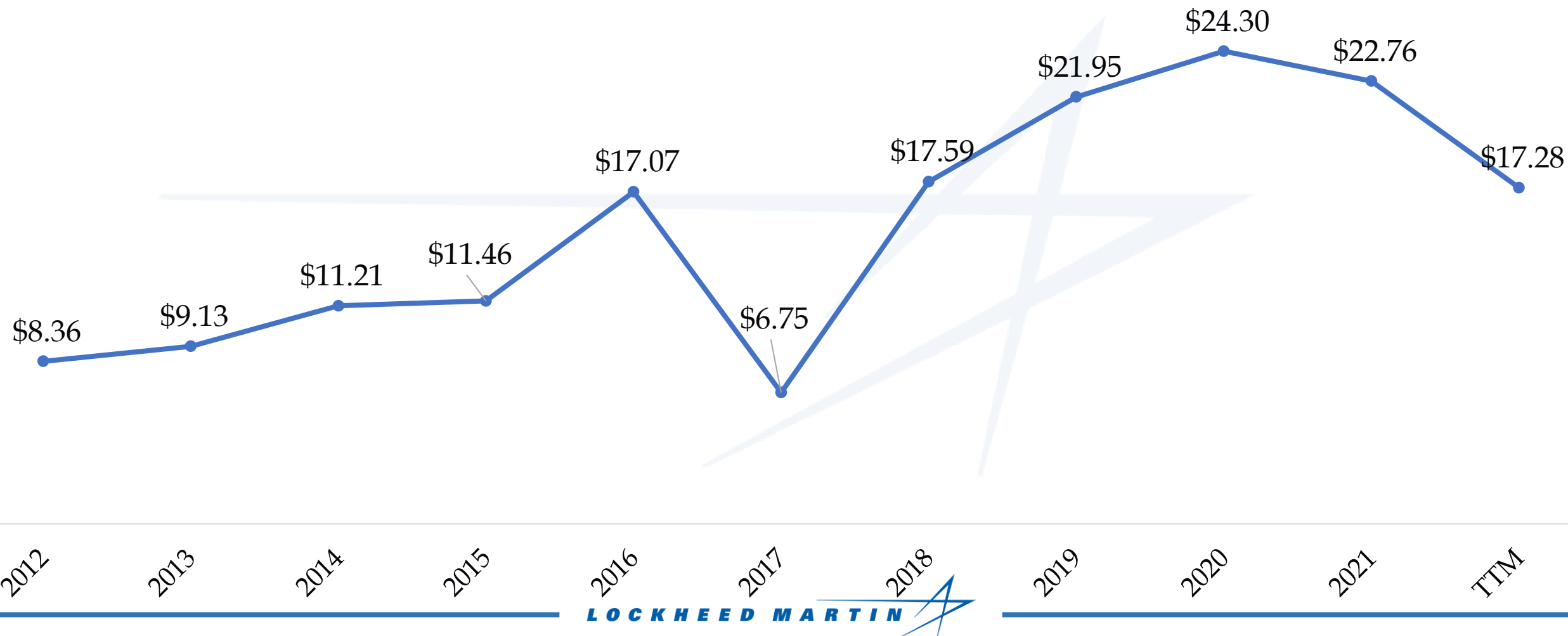
Operating Income (in millions)



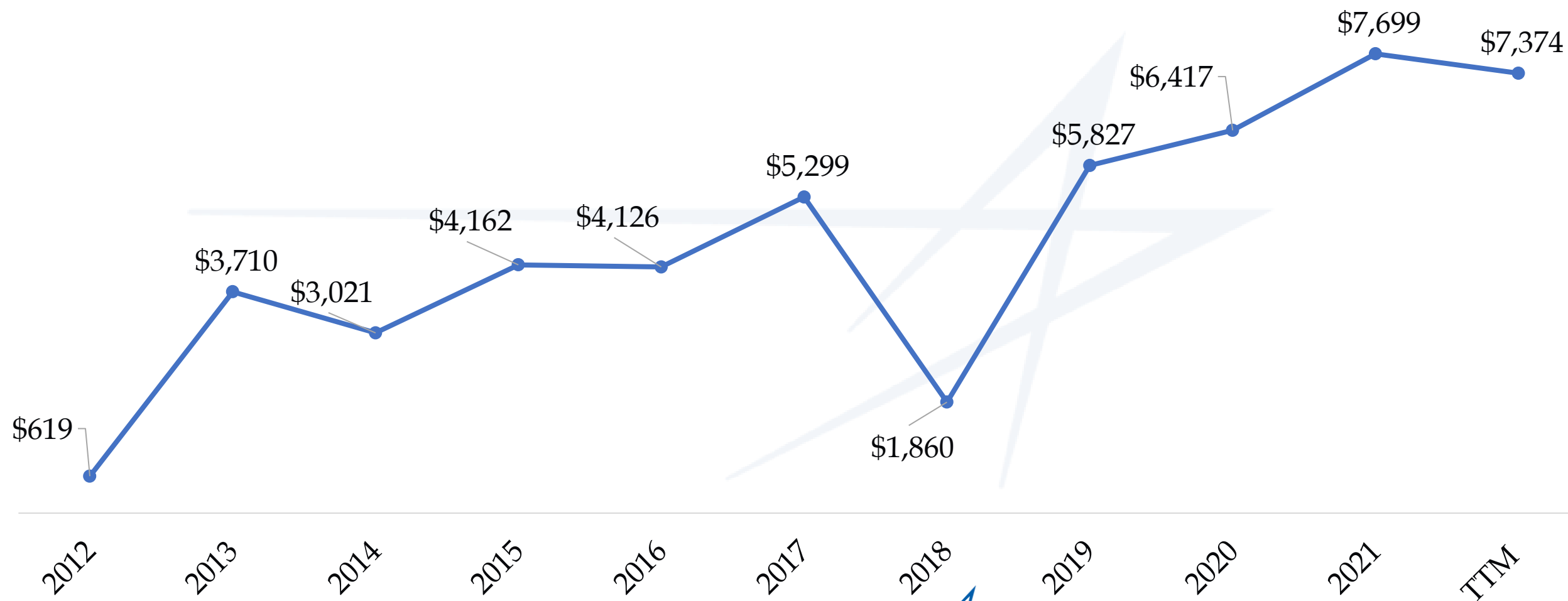
Net Income *(in millions)*



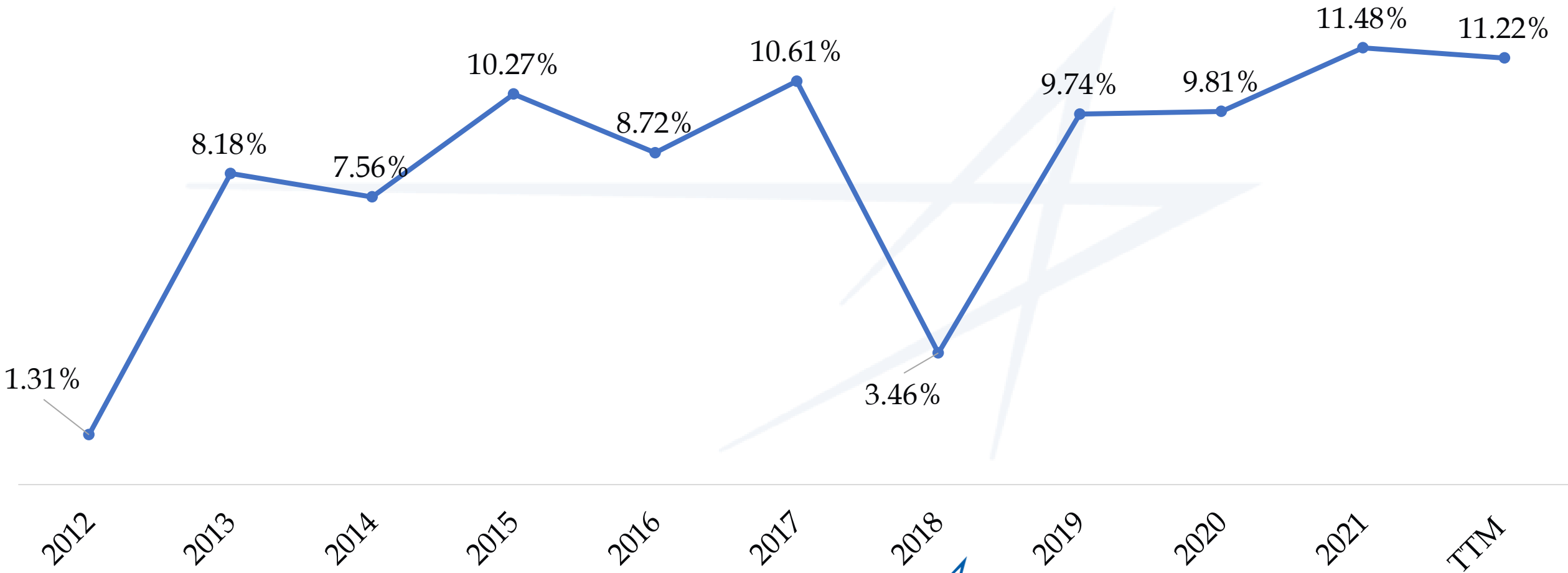
Earnings per Share (EPS)



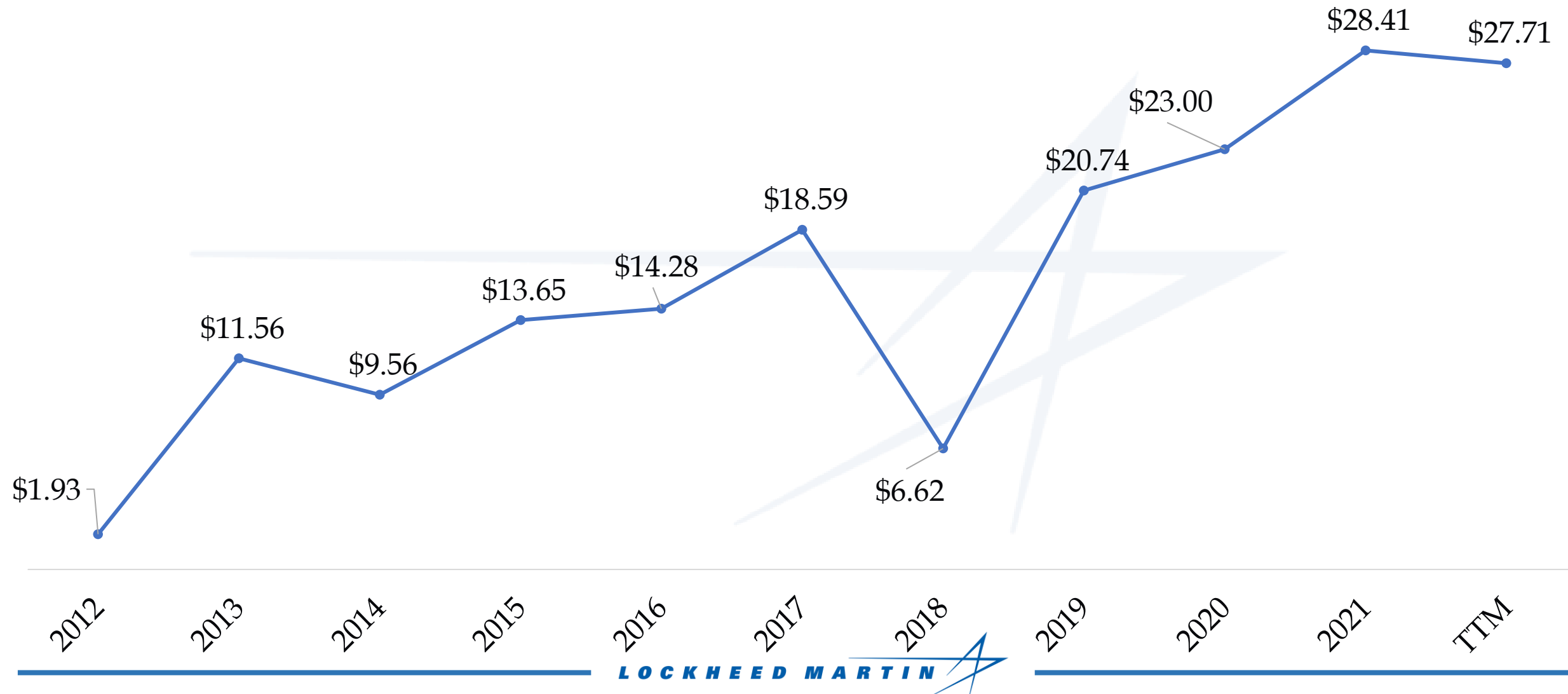
Free Cash Flow (in millions)



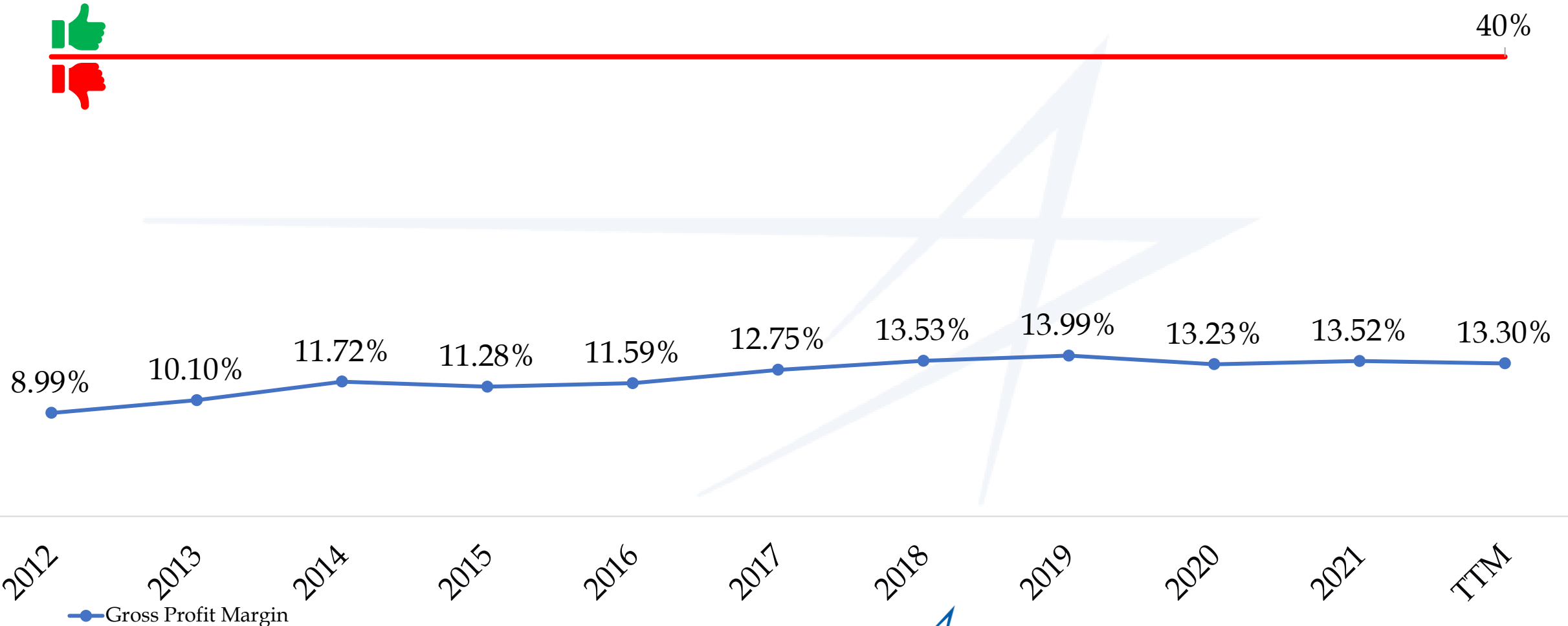
FCF Margin



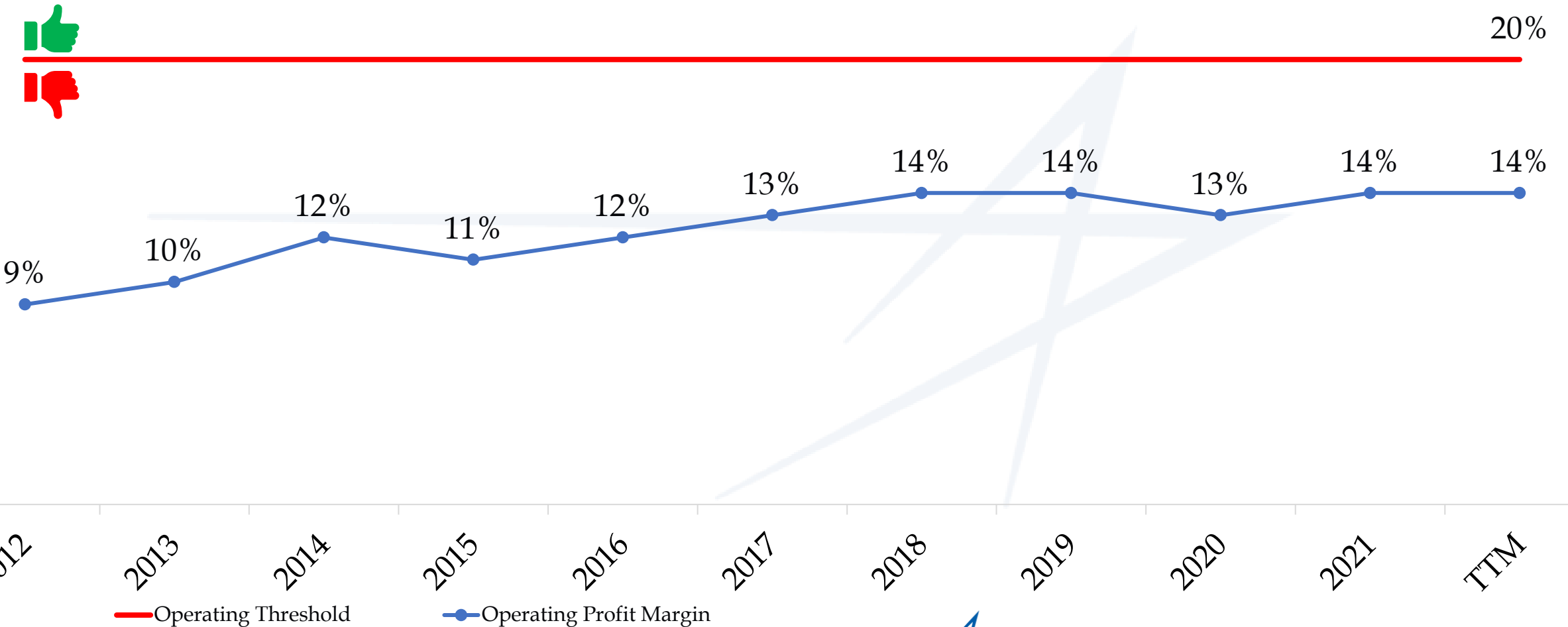
FCF Per Share



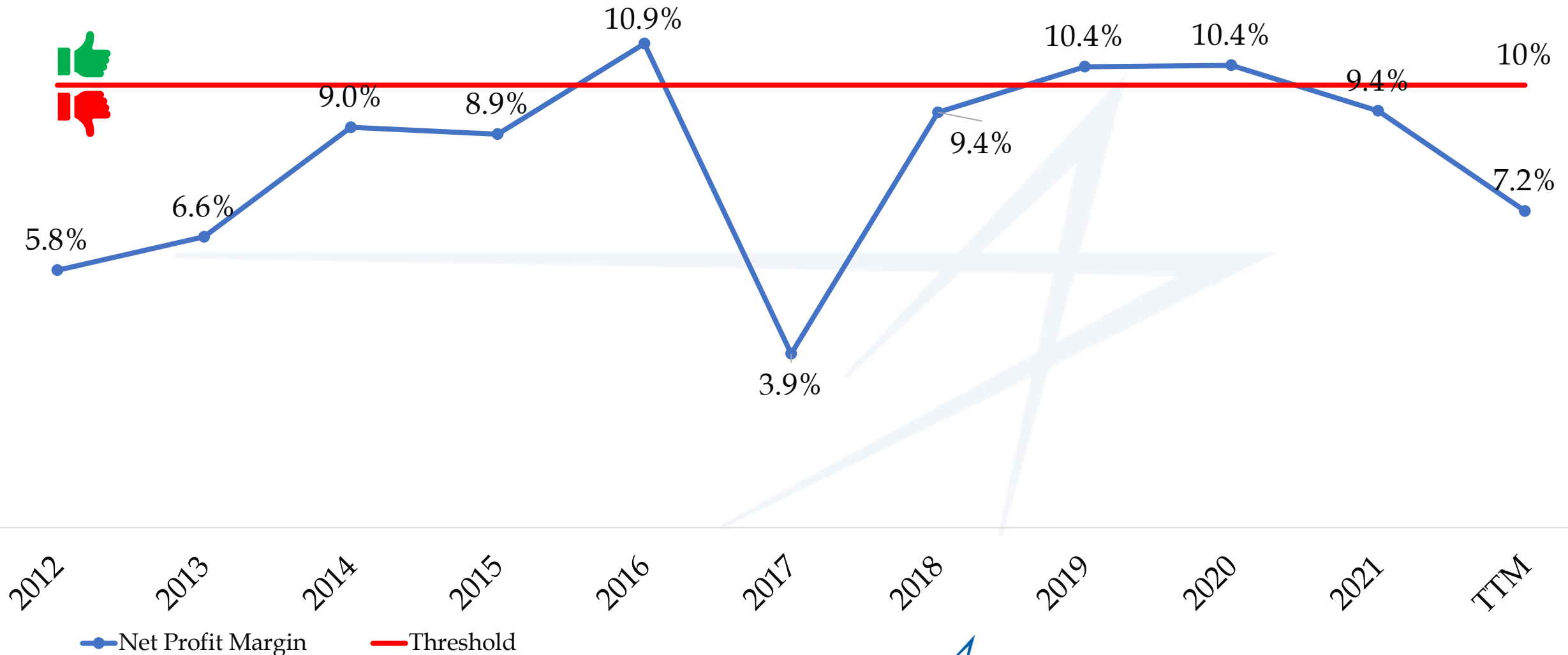
Gross Profit Margin



Operating Profit Margin



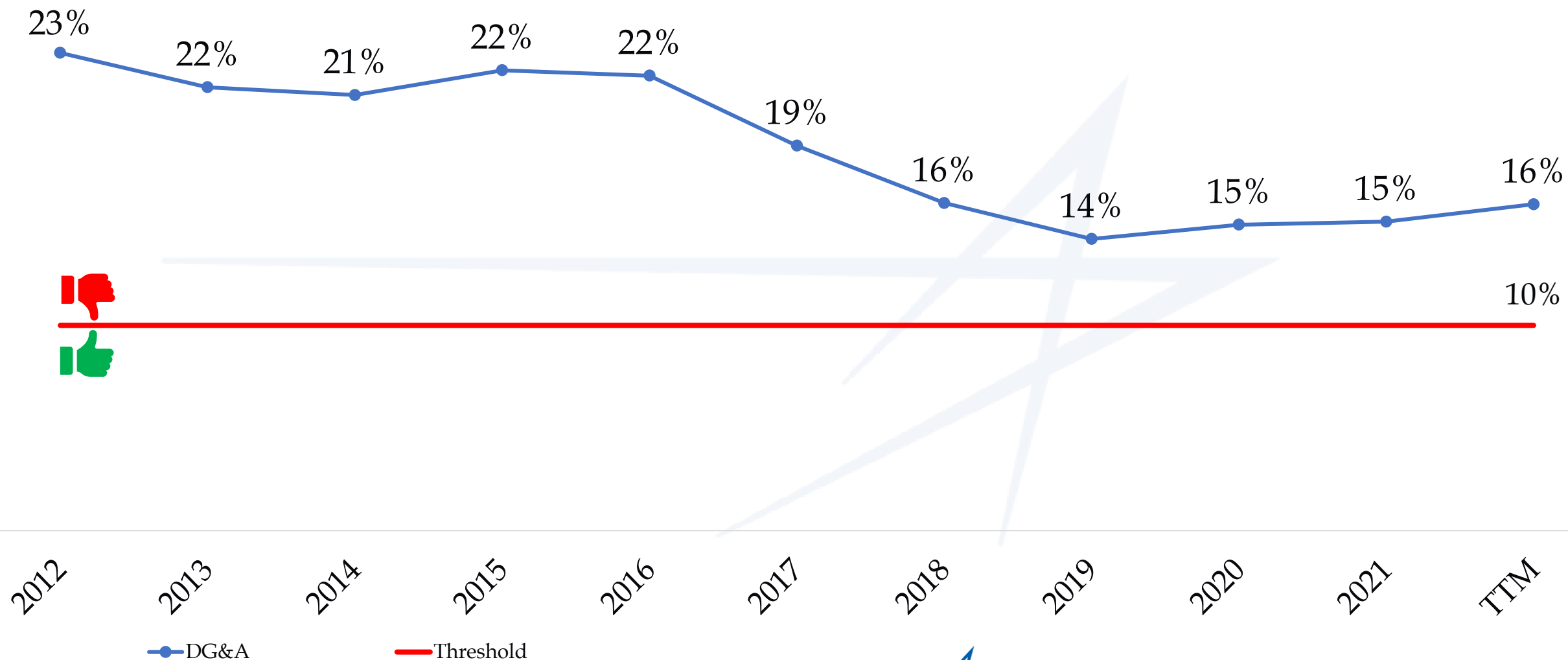
Net Profit Margin



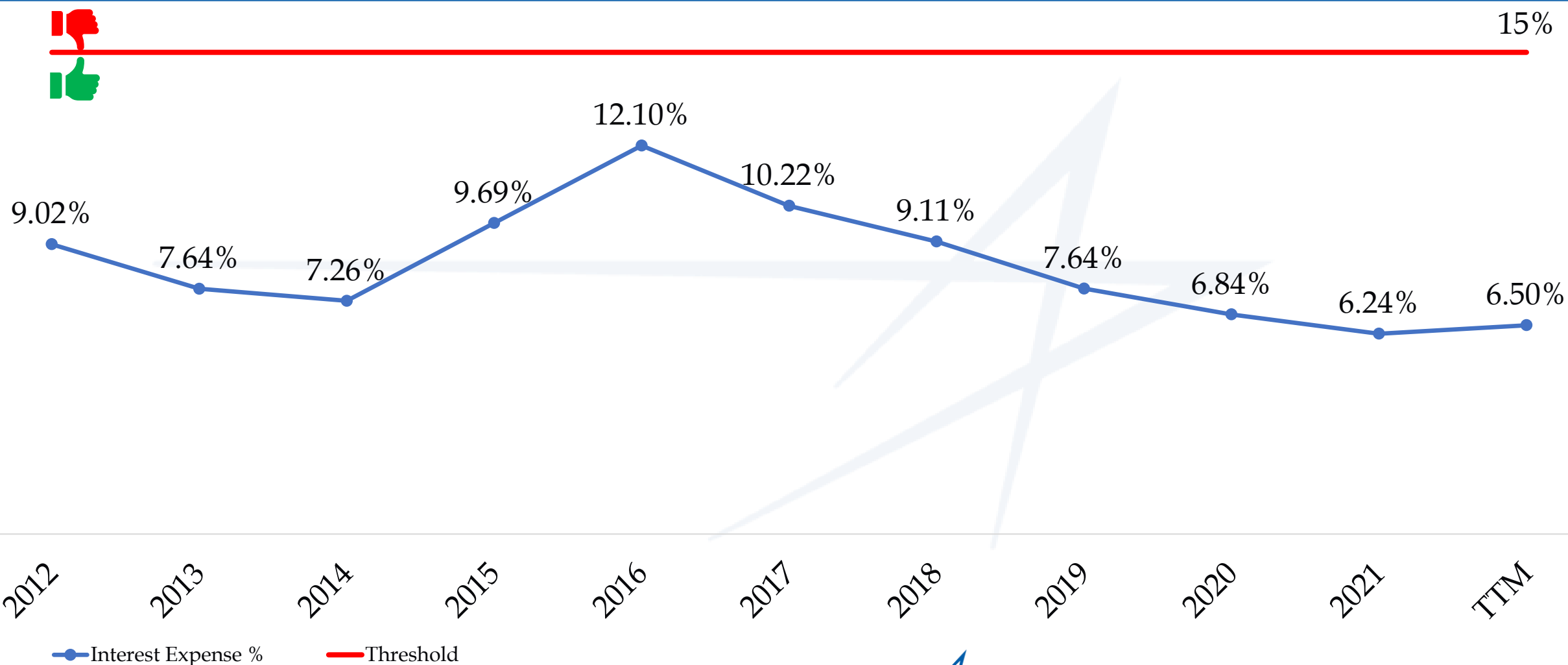
● Net Profit Margin — Threshold



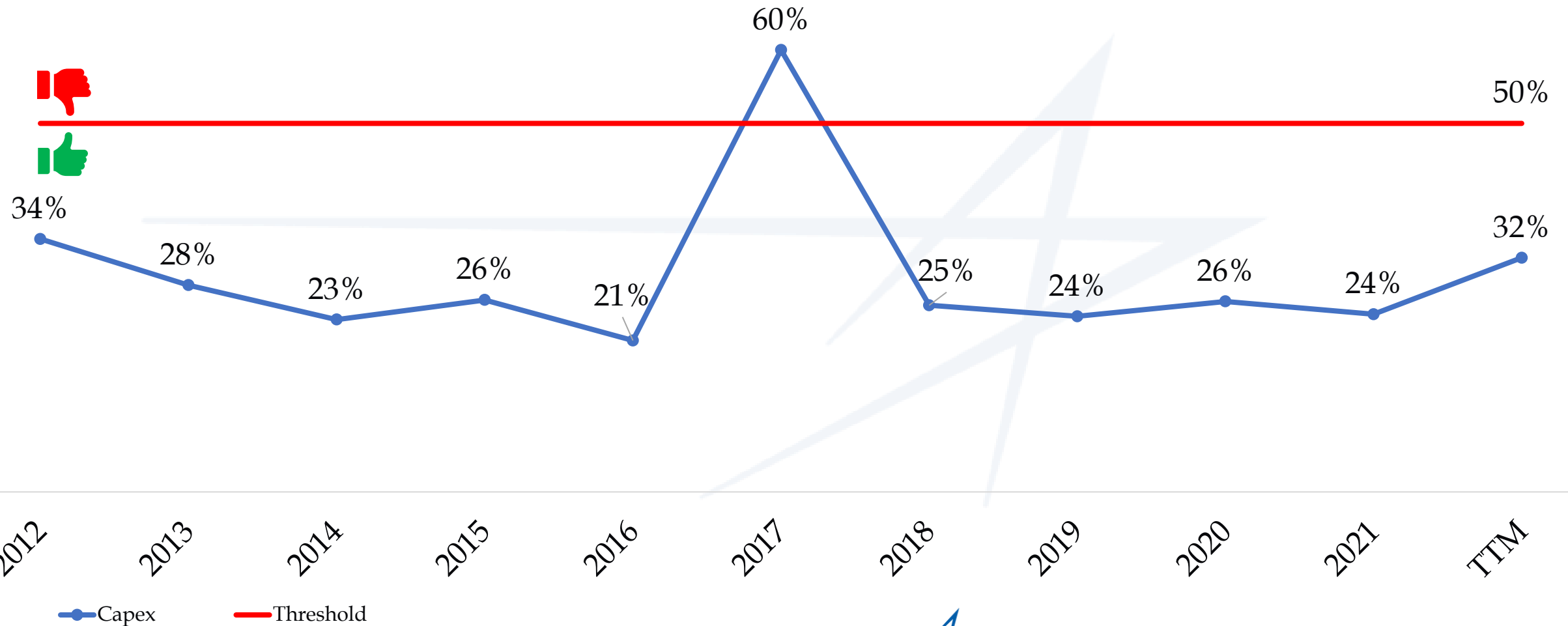
Depreciation as a % of Gross Profit



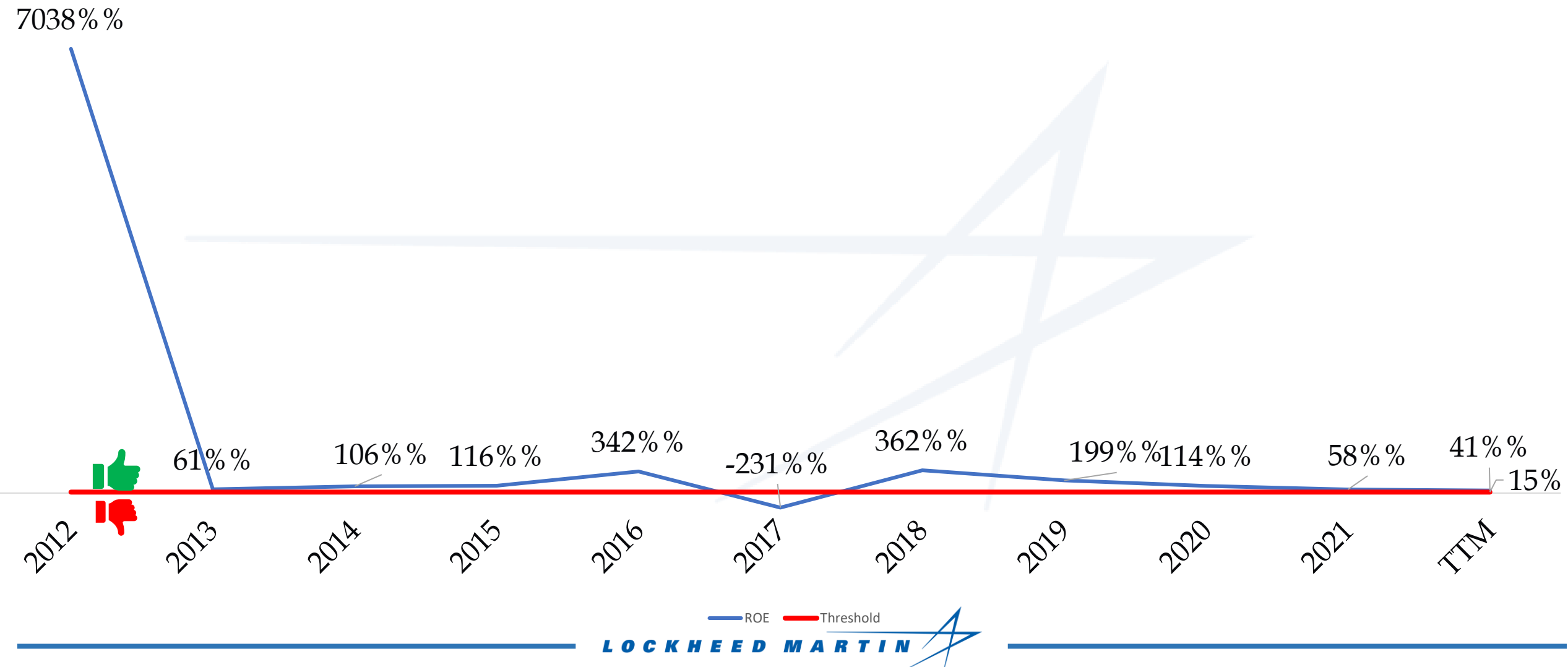
Interest Expense as a % of Operating Income



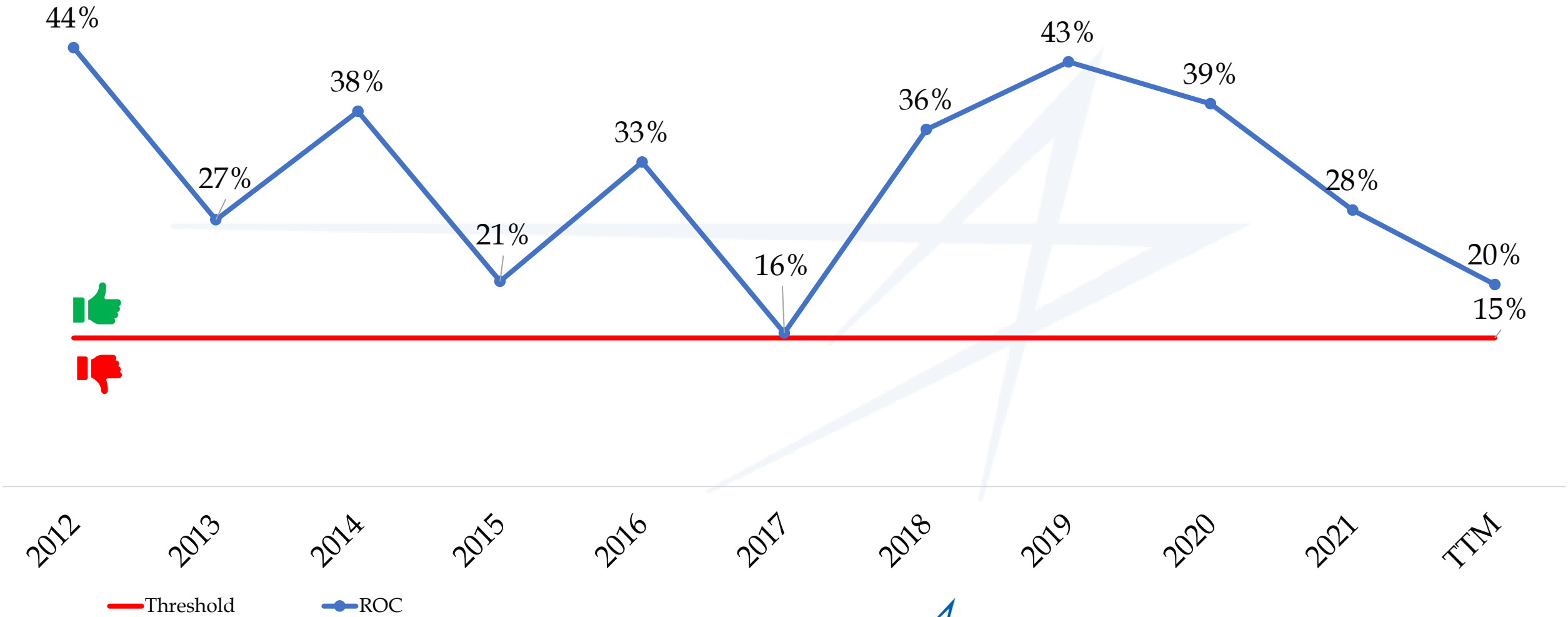
Capital Expenditures to Net Income



Return on Equity (ROE)



Return On Capital



Historical Growth Rates

CAGR	10-Year	5-Year	3-Year
Revenue	3.4%	1.2%	-4.9%
Net Income	8.5%	-6.5%	9.5%
FCF	28.1%	53.6%	88.7%



Obligation Ratio

(+) ST Debt	\$0	
(+) LT Debt	\$11,644	
(+) Leases *7	\$2,275	
(+) Pension Shortfall	\$5,808	
(+) Preferred Stock	\$0	
(-) Cash	\$1,775	
(/) Net Income	\$4,705	3.82 years
(/) 2022E Free cash flow	>\$6,000	2.99 years





Other News



Capital Allocation

Capital Allocation

Lockheed Martin returned \$1.1B of cash to shareholders in a form of dividends and buybacks. The company paid \$744M in cash dividends and repurchased \$356M worth of stock (0.35% of the market cap) or 0.9M shares. Over the first half of 2022, LMT has returned 178% of free cash flow through dividends and share repurchases. In the quarter, LMT returned 107% of FCF to shareholders in form of dividends and repurchases.

On May 5, 2022, the company received proceeds of \$2.3B from debt issuance, consisting of \$800M of 3.9% notes due 2032, \$850M notes of 4.15% due 2053, and \$650M notes of 4.30% due 2062. The company used the proceeds from this debt offering to redeem \$500M in principal amount of its 3.10% notes due 2023, \$750M 2.9% notes due in 2025, and \$1B 3.55% notes due in 2026.

The company incurred a charge of \$34M or \$0.10 per share on these transactions.

News

- Lockheed is trying to close the German F-35 Contract.
- Out of the US Missile Defense Agency's Glider Interceptor Program. This cuts out \$41.5 million that could've been received, as well as future investments.
- Successful hypersonic weapon test moves the Lockheed Martin's weapon to the next phase.
- Lockheed reach a deal with the F-35 Joint Program Office. This deal, if followed through, could be worth up to \$30 billion, for Lots 15 through 17.
 - 375 fighter jets would be delivered over the next three years.

Defense Budget

The Senate Armed Services Committees (SASC) approved their versions of the FY 2023 National Defense Authorization Act. SASC recommended a \$45B increase to the President's request and the full House chamber passed the completed authorization bill with a \$37B increase. This is a 6% increase from President Biden's \$773B request making the total \$818B and up 5% from his total national defense request of \$813B bringing the total to \$858B. Half of the \$45B in the Senate's bill will go to offset inflation. While the budget process remains in the early stages, management is encouraged with the support of LMT programs with the Senate recommending additional F-35 and Black Hawk helicopters, increases over the lower-than-expected volumes that were in the initial presence request. Both the Senate markup and the House bill received a strong bipartisan supporting committee with recognition of the need for greater investment to respond to increasing global security threats and the imperative of improving the readiness of armed forces.

Source: Earnings Transcript

The national defense budget for FY 2022 is \$782B, a 3.9% increase over the administration's request for 2022, and a 5.6% increase over 2021. China's military budget is estimated to be \$252B, India \$72.9B, Russia \$61.7B, The UK, \$59.2b, Saudi Arabia \$57.5B, Germany \$52.8B.

Demand and Backlog

CH-53K King Stallion Helicopter

The U.S. Marine Corps approved the Sikorsky CH-53K heavy lift helicopter. The Marine Corps Infantry Officer Course validates the operational readiness of the King Stallion to forward deploy Marines across the globe and positions the Marine Corps for a full-rate production decision in 2023. The 53K has a plan of record to deliver 200 domestic aircraft and a total program life cycle value to be \$50B.

Black Hawk Helicopter

Sikorsky received \$2.3B to provide 120 H60 helicopters. This contract includes the potential to deliver an additional 135 rotorcraft with a value of up to another \$4.4B.

Missile and Fire Control THAAD

The Missile and Fire Control Received a \$1.6B contract to produce THAAD interceptors for both domestic and international customers. The THAAD team will provide both the US government and the Kingdom of Saudi Arabia with additional interceptors in support of integrated air and missile defense.

Javelin Missiles

The US alone has committed more than 5,500 Javelin Missiles to Ukraine in defense of their country.



Valuation



Fiscal Year 2022 Guidance

The company expects supply chain challenges to continue for the remainder of the year. Given the challenges, LMT reduced its FY 2022 guidance.

Exhibit 3 – FY 2022 Guidance

	Previous Outlook	New Outlook	Percent Change	FY 2021	YoY Change
Net sales	\$66,000	\$65,250	-1.1%	\$67,044	-2.7%
Diluted EPS	\$27	\$22	-19.3%	\$23	-5.3%
Cash from Operations	\$7,900	\$7,900	0.0%	\$9,221	-14.3%
Capex	\$1,900	\$1,900	0.0%	\$1,522	24.8%
Free cash flow	\$6,000	\$6,000	0.0%	\$7,699	-22.1%

Diluted EPS

April 2022 Outlook

~\$26.70

One-Time Pension Settlement

(4.33)

FAS/CAS Income (Remeasurement)

(0.15)

} Pension Risk Transaction

YTD LM Ventures/Deferred Comp., Mark-to-Market

(0.57)

Debt Refinancing

(0.10)

July 2022 Outlook

~\$21.55



Ticker: LMT		Price: \$393.69										
5 Year EPS Forecast												
								P/E	Total Return Price	PV	5 YR Return	Annual Return
Bear	EPS	<u>2021</u>	<u>2022</u>	<u>2023</u>	<u>2024</u>	<u>2025</u>	<u>2026</u>	8	\$294.54	\$182.89	(25.2)%	(5.6)%
		\$22.76	\$21.39	\$26.51	\$27.57	\$28.67	\$29.82	12	\$413.81	\$256.94	5.1%	1.0%
		-6%	24%	4%	4%	4%	16	\$533.08	\$331.00	35.4%	6.2%	
Base	EPS	<u>2021</u>	<u>2022</u>	<u>2023</u>	<u>2024</u>	<u>2025</u>	<u>2026</u>	10.0x	\$399.26	\$247.91	1.4%	0.3%
		\$22.76	\$21.55	\$28.02	\$29.98	\$32.08	\$34.33	15.0x	\$570.88	\$354.47	45.0%	7.7%
		-5%	30%	7%	7%	7%	20.0x	\$742.51	\$461.04	88.6%	13.5%	
Bull	EPS	<u>2021</u>	<u>2022</u>	<u>2023</u>	<u>2024</u>	<u>2025</u>	<u>2026</u>	12.0x	\$504.21	\$313.07	28.1%	5.1%
		\$22.76	\$21.85	\$28.84	\$31.44	\$34.27	\$37.35	18.0x	\$728.31	\$452.22	85.0%	13.1%
		-4%	32%	9%	9%	9%	24.0x	\$952.41	\$591.37	141.9%	19.3%	

Discount
rate:
10%

Total RoR Sensitivity				
Est. EPS growth rate				
Average		6%	9%	11%
P/E	10.0x	(5.6)%	0.3%	5.1%
	15.0x	1.0%	7.7%	13.1%
	20.0x	6.2%	13.5%	19.3%

Value projects EPS to be \$28.25 in FY 2023
 Refinitiv projects EPS to be \$28.39 in FY 2023
 S&P Global projects EPS to be \$28.09 IN FY 2023

Two Stage DCF Using Non-GAAP EPS

Fair Value?	\$ 414.41
Margin Of Safety	👍 3.84%
Stock Price	\$ 398.50

Based on ☒ EPS w/o NRI ☐ FCF \$ 26.7

Discount Rate %? : - 9 +

Tangible Book Value \$ -7.34
(☐ Add to Fair Value)

Growth Stage?		Terminal Stage?	
Years	- 10 +	Years	- 10 +
Growth Rate	- 7 +	Growth Rate	- 4 +
Growth Value	\$ 241.49	Terminal Value	\$ 172.93

Fair Value?	\$ 338.23
Margin Of Safety	👎 -17.82%
Stock Price	\$ 398.50

Based on ☒ EPS w/o NRI ☐ FCF \$ 26.7

Discount Rate %? : - 9 +

Tangible Book Value \$ -7.34
(☐ Add to Fair Value)

Growth Stage?		Terminal Stage?	
Years	- 10 +	Years	- 10 +
Growth Rate	- 4 +	Growth Rate	- 4 +
Growth Value	\$ 208.11	Terminal Value	\$ 130.12

Fair Value?	\$ 508.86
Margin Of Safety	👍 21.69%
Stock Price	\$ 398.50

Based on ☒ EPS w/o NRI ☐ FCF \$ 26.7

Discount Rate %? : - 9 +

Tangible Book Value \$ -7.34
(☐ Add to Fair Value)

Growth Stage?		Terminal Stage?	
Years	- 10 +	Years	- 10 +
Growth Rate	- 10 +	Growth Rate	- 4 +
Growth Value	\$ 280.85	Terminal Value	\$ 228.01





Appendix



F-35 Lots 15-17

F-35 Lots 15-17 Contract Update

Lot 15 includes 169 jets, Lot 16 includes 157 jets, and Lot 17 includes 159 jets. The company reached an agreement with the U.S. Government on the F-35 Lots 15-17 production contract. The company has been performing work on the Lots 15-17 production and initial funding to begin work under an advance acquisition contract received in December 2019. The company's costs began to exceed the contract value and funding on the Lots 15-17 contract in Q2 2022. As a result, this prevented the recognition of \$325M of sales (2.3% of total sales) in Q2. Additionally, it prevented the company from invoicing and receiving cash of \$465M for costs incurred in Q2. The company expects to recover the unrecognized sales and resume invoicing costs incurred upon receiving contractual authorization, which expects to occur in Q3 2022. However, until a final agreement is reached, or the US Government provides additional contractual authorization and funding, the company's results of operation will continue to be impacted. As part of the Lots 15-17 production contract, the US Government reduced the acquisition quantities based on budget availability. While the company expects the Lots 15-17 contract to support its long-term objective to produce 156 aircraft a year, COVID-19 and other impacts experienced by the F-35 enterprise have required it to modify its near-term production plan. Deliveries are expected to remain in the range of 147-153 aircraft per year in 2023 and 2024 before the company achieves its 156 aircraft delivery target in 2025. The company continues to anticipate annual deliveries of 156 aircraft beyond 2025 for the foreseeable future. July 18, 2022 – [Reuters](#)

Lockheed Martin reached an agreement with the Department of Defense to deliver 375 jets valued at around \$30B over three years. For the foreseeable future, the production rates will only be able to be increased to 156 and stabilize, as opposed to the previously expected 175 deliveries. Amid expectations, the price of the F-35 would increase in price due to inflation and slower production. The first version of the F-35 cost \$221M when it came off the production line in 2007. Since then, production quantities and know-how have increased, helping the price fall to \$79M. The price of the jet will increase given the supply chain and inflationary pressures. The previous three-year block buy, signed in 2019, was for 478 F-35 jets, allowing LMT to buy larger quantities of components to reduce costs by 8% to \$34B.



Purchase Group Annuity

Purchase Group Annuity Contracts and Pension Remeasurement

On June 24, 2022, the company purchased group annuity contracts to transfer \$4.3B of gross defined benefit pension obligations and related plan assets to an insurance company for 13,600 US retirees and beneficiaries. The group annuity contracts were purchased using assets from Lockheed's master retirement trust and no additional funding was required. In connection with the transaction, the company recognized a non-cash, non-operating settlement charge of \$1.5B or \$4.33 per share after-tax for Q1 2022, which represents the accelerated recognition of actuarial losses that were included in the accumulated other comprehensive loss account within stockholders' equity. As a result of this transaction, the company was required to remeasure the benefit obligations and plan assets for the affected defined benefit pension plans in the quarter ended June 26, 2022. Management now expects final average salary FAS pension expense of approximately \$1.1 billion in 2022, inclusive of the non-cash, non-operating pension settlement charge of \$1.5 billion (pre-tax) described above. Excluding the non-cash, non-operating pension settlement charge, the expected FAS pension income will be approximately \$410 million in 2022, which is \$50 million lower than the prior 2022 FAS pension income estimate of \$460 million.