Lockheed Martin (LMT)

Sector: Aerospace and defense

Price: 337.04$

Market Cap: 94.41B$

P/E ratio: 13.7

Dividend: 10.40$ yearly – 3.09%

KEY INFORMATIONS

Founded in 1912, one of the biggest and most famous companies in the sector.

They are the biggest defence contractor in US, they work with most federal agencies and they have very close relationships with government due to their business, they can't sell their products to whoever they want, the sales must be approved by US government agencies.

110k employees, one of the few companies that don't have unions or pension plans problems. 1 in 5 employees is a veteran, giving them both expertise and political influence.

They had a wonderful management in last years, Maryllin Hewson took the company to the next level and her guidance took the company on the top. She was replaced in June 2020 by James Taiclet, but we shouldn't worry about this, he's a top manager and Maryllin is the executive chairman of the board so she can still influence and help leading the company.

They are working hard on raising margins and they are slowly succeeding, cost reduction and price raising gives them the chance to create a lot of value for shareholders, a point on which they are very focused

Working with very niche and specialised products, they have an interesting business system. They can't produce enough products to fulfill all the orders they receive, they always have orders backlog, so they already have orders for like 150B$, which means they already have enough work for the next 2.5

Working so close with government agencies, they have both political influence, unique privileges and no matter what problem they could have, they will always have government's help.

STRENGHT POINTS

The company is very old and very experienced, they have huge experience in all the fields, their products are everywhere in the world and everyone wants to stay at top in warfare. The company shines when there's a war ongoing, and they keep selling during calmer times because countries pile up weapons and technologies to be always ready. United States is one of the most active countries in this field, facing competition from both Russia and China, and US Department of Defence is their main customer.

While their business need a good amount of research and development, once they create a new aircraft or missile or other technologies, they can sell it for a good amount of time, there are aircrafts and helicopters which have been around for decades, some more than 50 years. Once they have a top level product, they can keep selling it for years, giving them enough time to create new ones. Their technology doesn't go obsolete in few months or in a couple years.

Military expenses are the second higher US expense, after social security. This means the market is huge, and if we look at the spending trend, it's going up more and more, over 930B$ in 2020. Biggest program for department and defence is F35 aircraft program, worth 11.4B$ and Lockheed Martin is the manufacturer.

71% of their revenue comes from US government, but I don't see this as a huge problem, because US have always been leaders in military and space programs, so even if they have a single huge customer, it's the best customer they could want.

US has around 615 operating F35 aircrafts, and they plan to have more than 2400 by 2044, which means roughly 100 a year. Lockheed Martin has capability of building around 150 a year, so 66% of their F35 is already sold for the next 24 years, allowing them to plan very good both the manufacturing and the expansion of the company.

The company has a huge importance for US government, so they will receive any help they need, no matter what the problem is. Lockheed Martin represents the back spine of US armed forces and they must keep building the weaponry no matter what happens, including supply chain disruption or pandemic related problems. Their factories have never been shut down, because they are vital for national security, global communications, and infrastructure.

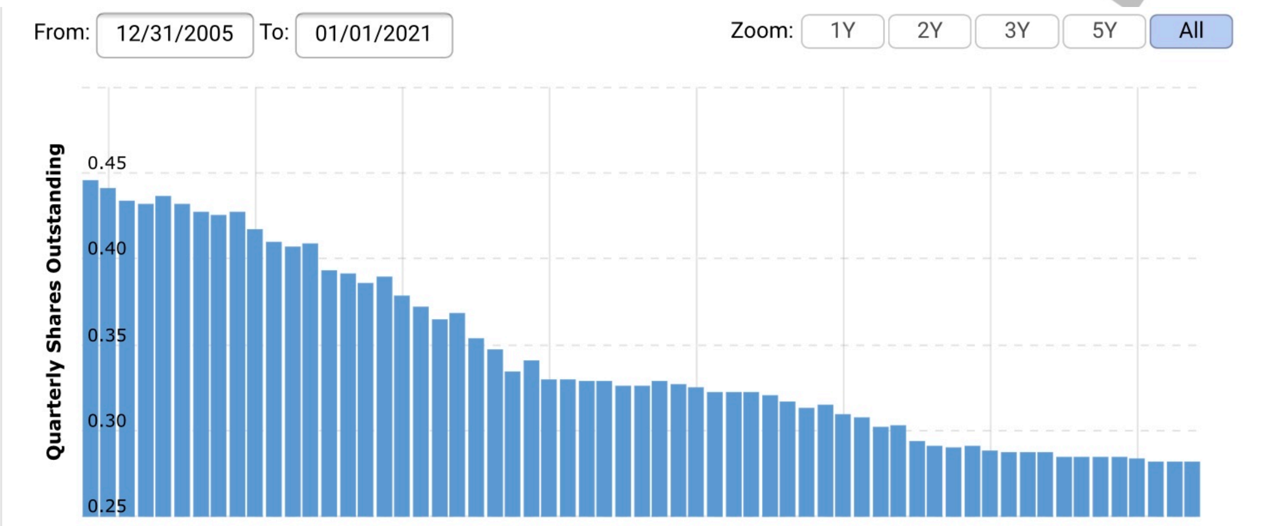
Dividend is interesting, 3.09% with a payout ratio around 40% so there's enough room to keep it growing. They raised it for 18 years and the compound annual growth rate of the last 5 years is 9.77%, a very nice number for a good dividend company with a very interesting future. They slowed down the buyback program because in last 15 years they bought a lot and that drove up the prices so the company slowed down the shares repurchase. This is not a problem because the company will use the money to raise the dividend more and more.

FINANCIALS

3.16B$ cash - 11.33$ per share, totally free, it's not a huge amount considering a share is 330$ but it's still a plus.

A very nice looking 21.6B$ retained earnings cover almost twice the long term debt which is 11.6B$, without even considering the buyback program that we don't see on the books because they burn the shares. During the last 15 years the buyback program was a good one, for 60 quarters in a row they lowered the shares outstanding number. Last twelve months buyback yield was only 1.7%, but we already told it's not something that should worry us. In last 15 years they reduced shares outstanding by a nice 37%.

Price/earnings ratio is looking good, right now it's 13.7 with a 5 year average of 23.6 and a 10 year average of 18.6 it's one of the best P/E we could ask for, the lowest in last 7 years.


From: 12/31/2005 To: 01/01/2021
Zoom: 1Y 2Y 3Y 5Y All
Quarterly Shares Outstanding
0.45
0.40
0.35
0.30
0.25


PE Ratio
40
30
20
10
2014
2015
2016
2017
2018
2019
2020
2021
2008
2010
2012
2014
2016
2018
2020


From: 12/31/2005 To: 01/01/2021
Zoom: 1Y 2Y 3Y 5Y All
TTM Gross Margin
14
12
10
8
6
TTM Operating Margin
14
12
10
8
6
TTM Net Margin
12
10
8
6
4
2
2008
2010
2012
2014
2016
2018
2020

The management was very good in last 10 years, they are working both on company's growth and on their margins, to maximise profits and lower costs. All this with a constant focus on the shareholders which is exactly what we're looking for.

The inventory is kinda small if we consider the costs of their products, so they don't have a lot of items sitting there, most of the inventory is there because they're waiting to fulfil an order and send everything to the customer. Properties plants and equipment is fine because they need investments to keep the factories operating and efficient. Interesting fact is that they don't own most of the properties but just lease them from the government itself.

POTENTIAL THREATS

They are very exposed to US government regulations, they don't operate on a free market they can only sell to certain countries after US Department of Defence authorises them. It's not a huge problem because their production is kinda low and can't satisfy the request at all, they have orders for years incoming.

Changes in management are not great usually, especially if it's a great CEO that's being replaced, but I don't worry in this case for 2 reasons: the new CEO is a very good one that did a great job in his career, and the former CEO will just become the executive chairman of the board so she'll still be involved in the company and will keep helping it grow.

A potential threat could be the election of president Joe Biden, as democrats tend to lower the military expenses. I don't worry about this, the company has seen times with both democrats and republicans and they always succeeded. Even if it slightly decreases, they have enough international customers that want their products.

In 2017 they had a worse year in net income because they paid a lot of taxes due to the tax cuts and jobs act law, so their net income was affected. Looking at the data below we can easily see there was no problem in the business, it was just a tax expense that happened once and doesn't affect the business.

	2016-12-31 FY-4	2017-12-31 FY-3	2018-12-31 FY-2	2019-12-31 FY-1	2020-12-31 FY
Operating Income	5,417.0	5,897.0	6,506.0	7,894.0	8,826.0
Net Interest Expenses	-663.0	-651.0	-668.0	-653.0	-591.0
EBT, Incl. Unusual Items	4,754.0	5,246.0	5,838.0	7,241.0	8,235.0
Earnings of Discontinued Ops.	1,512.0	73.0	-	-	-55.0
Income Tax Expense	-1,093.0	-3,356.0	-792.0	-1,011.0	-1,347.0
Net Income to Company	5,173.0	1,963.0	5,046.0	6,230.0	6,833.0

FINAL THOUGHTS

The company looks great and the price is very fine, we're talking about a huge sector leader whose only problem is that they can't produce more aircrafts. Their importance in military panorama allows them to not worry much about lawsuits or small problems because their products importance is too high and the worse that can happen to this company is they have to pay some small fees, absolutely ridiculous compared to the numbers the company makes.

Price of 337$ could scare some investors but we're looking at one of the most interesting companies right now, and it's trading below the 200 days moving average which is 372$, or 10% lower. I don't see any reasons in the company for such low price for a company that has no problems and with such a big political influence.

The price is very very interesting, hardly we can expect to buy at a lower, if we want to be more conservative we can make a 2 steps buy strategy, 50% of capital now and 50% if it drops 5% so at 320. A more conservative can buy at 3 steps, 337$, 320$ and 300$ but I doubt it'll hit 300$. Maximum risk should be 10%, maybe 15% if we see a bearish market ahead but I don't think the price will go below 300. Potential profit is around 30-40% in first year dividend included, which means a price of 440-470$. If it's not in a year, it could be slightly longer because of the lower volatility of the company, but that's the target we can expect.

Timeline goes from medium to long/very long term, since we're buying it so low we can be happy with a good medium term gain, or we can wait and let it grow both for the price appreciation and for the potential dividend growth. It's not a company that should worry us in the long term, we just have to keep an eye on the management and the numbers to be 100% sure our money is still safe. I don't see any short or medium term problems that could affect a lot the company.

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