

Lockheed Martin Corp (NYSE: LMT)

Fundamental Investments

Current price (10/21/23): \$444.13 | Target Price: \$526 | Implied Upside: 18%



October 2023

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Company Overview

Largest US defense contractor focused on aeronautics, rotary and mission systems, missiles and fire control, and space

Business Description & Strategy

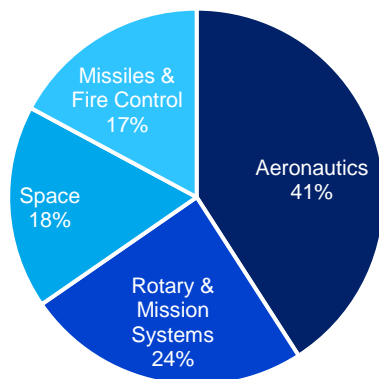
Overview: Lockheed Martin Corp is one of the worlds largest defense contractors. The company mainly operates in aerospace and defense markets with a focus on four business avenues: Aeronautic, Missiles and Fire Control, Rotary and Mission Systems, and Space. As of 2023, they are the largest federal defense contractor, having received over 11% of all spending by the Department of Defense in 2022.

Strategy: Lockheed is focused on Accelerating the adoption of advanced networking and leading-edge defense technologies. Lockheed aims to integrate and execute these strategies by moving from the developmental phase of many projects (F-35 sustainment activity, increased PAC-3 production, CH-53K heavy lift helicopter, and enhancements to the Trident II D5 Fleet Ballistic Missile) and entering early development phase between 2023-2026 though the 21st Century Security Program.

Valuation: DCF and comparable company analysis show Lockheed is currently trading at a discounted valuation with continued innovation and contracting opportunities driving a target share price of \$526.

Revenue Breakdown

2022 Revenue by Business Area

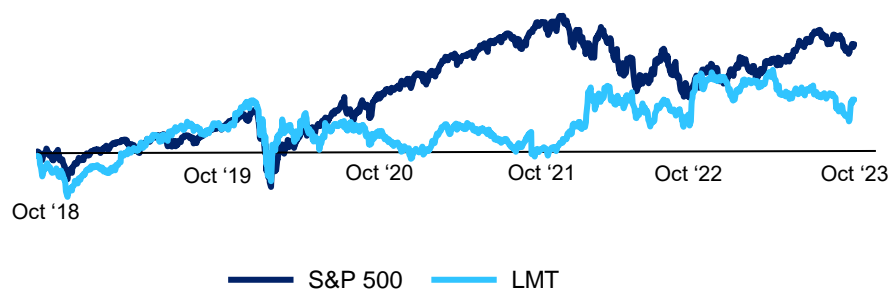


Current Market Data (10/21/23)

Market Cap	\$111.09B	Enterprise Value	\$124.96B
Price	\$ 441.13	Q3 2023 Debt	\$17.22B
52 Week High	\$508.10	FY22 Revenue	\$65.98B
52 Week Low	\$393.77	FY22 EBITDA Margin	13.20%
Div. Yield % (LTM)	2.86%	EV/EBITDA (LTM)	11.96x
Float %	83.56%	P/E (LTM)	16.18x


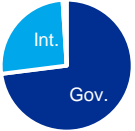
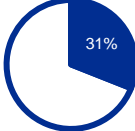
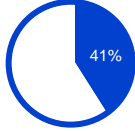
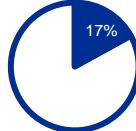
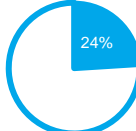
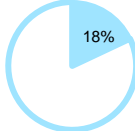



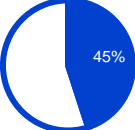
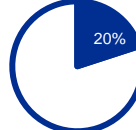
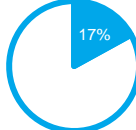
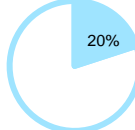

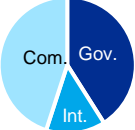

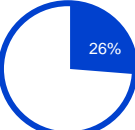
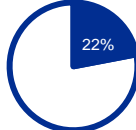
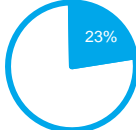
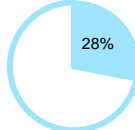

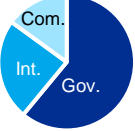
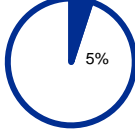
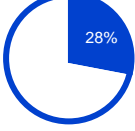

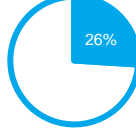
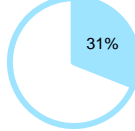

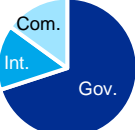

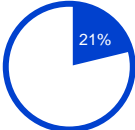
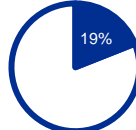
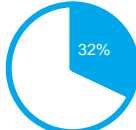
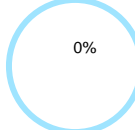
Historic Share Price vs. Benchmark

LMT CAGR: 9.4%
S&P 500 CAGR: 11.22%



Competitive Landscape

LMT is the prime contractor for the US. Government's aerospace fleet, including cutting-edge F-35s, F-16s, and more

Company	Key Products	Revenue by Customer Source	2022 Defense Revenue as % of Total Market Share	Aerospace	Missiles & Fire Control	Rotary & Mission Systems	Space
	<ul style="list-style-type: none"> F-35 Lightning C-130 Hercules F-22 Raptor PAC-3 Missile 						
	<ul style="list-style-type: none"> Boeing 737 F/A-18 KC-46A Tanker Red Hawk 						
	<ul style="list-style-type: none"> AIM 9x AMRAAM Missile Joint Strike Missiles 						
	<ul style="list-style-type: none"> Integrated Air & Missile Global Hawk Satellites 						
	<ul style="list-style-type: none"> Gulfstream Jet Abrams Tank Stryker Attack Submarine 						

Comparable Companies Analysis

LMT is one of the top defense contractors in scale and profitability while maintaining an attractive market valuation

Top Operational and Stock Performance Among Peers

Operational Overview: LMT is well within or above the industry profit margin averages. The average difference between the GPM and the NPM is 8.64%. The LMT's operational costs are also significantly lower than its competitors with 2.3%. When looking at the operational costs of LMT's main competitor, NOC, has a 7.9% operational cost difference. Overall, LMT's lower operational costs compared to the average and competition position the company to keep more returns in the future.

Performance Overview: The industry average EV/EBITDA multiplier is 14.73x and their P/E ratio is 9.50x. This benchmark implies that LMT is undervalued with a 12.50x EV/EBITDA and its biggest competitor NOC is valued at 17.38x in comparison.

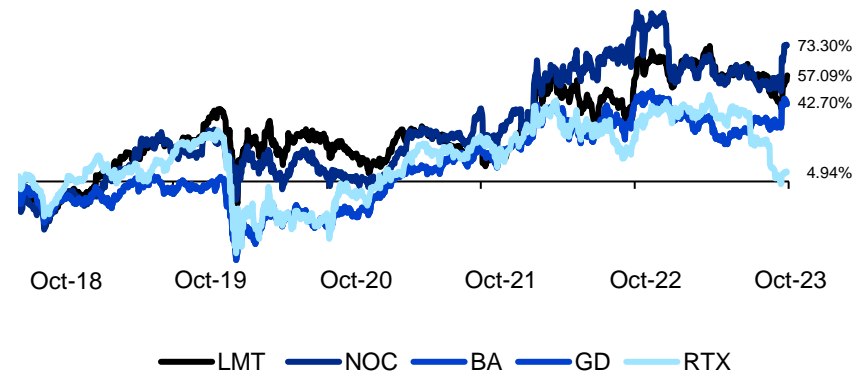
Stock Growth Comparison: LMT's CAGR is at the higher end in the industry and the company's stock has grown 57.09% over the last 5 years putting it 2nd in overall growth to its competitors.

Operating Margins Comparison

Company	Gross Margin	EBITDA Margin	EBIT Margin	Pretax Margin	Net Margin
Lockheed Martin	12.8%	14.9%	12.8%	12.3%	10.5%
Northrop Grumman	20.2%	13.2%	9.7%	14.6%	12.3%
Boeing	6.6%	(2.1%)	(4.6%)	(6.4%)	(6.1%)
General Dynamics	16.1%	12.5%	10.3%	9.9%	8.2%
RTX	20.4%	14.3%	8.4%	9.4%	7.9%
Average	15.22%	10.56%	7.32%	7.96%	6.58%
Median	16.1%	13.2%	9.7%	9.9%	8.2%

Comparable Stock Price Growth over Past 5 years

LMT CAGR: 9.4% **NOC CAGR: 10.37%** **BA CAGR: (31.15)%**
GD CAGR: 0.26% **RTX CAGR: 5.19%**



Market Valuation Comparison

Company	EV (M)	P/E	EV/Sales	EV/EBITDA
Lockheed Martin	125,404	16.13x	1.86x	12.50x
Northrop Grumman	86,793	16.20x	2.29x	17.38x
Boeing	157,055	(24.4x)	2.13x	(98.56x)
General Dynamics	77,467	19.80x	1.90x	15.14x
RTX	139,989	19.59x	1.98x	13.89x
Average		9.50x	2.03x	14.73x
Median		16.20x	1.98x	14.52x

Investment Thesis

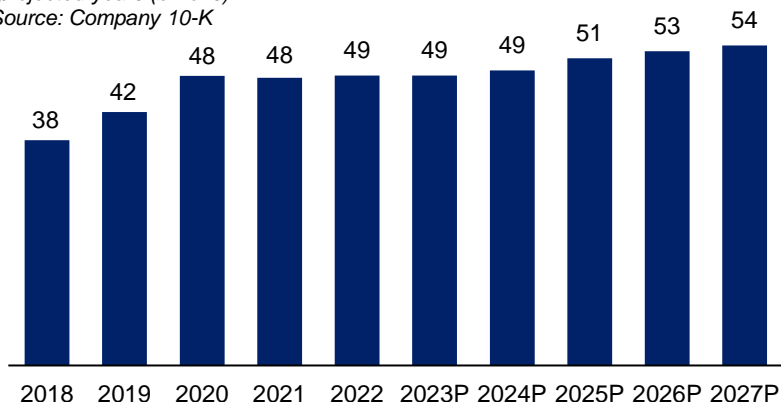
LMT presents a strong opportunity stemming from a dominant competitive position and strong geopolitical tailwinds

Consistent DoD Awards At Large Volumes

Lockheed Martin Total Contract Award Amounts

*projected years (billions)

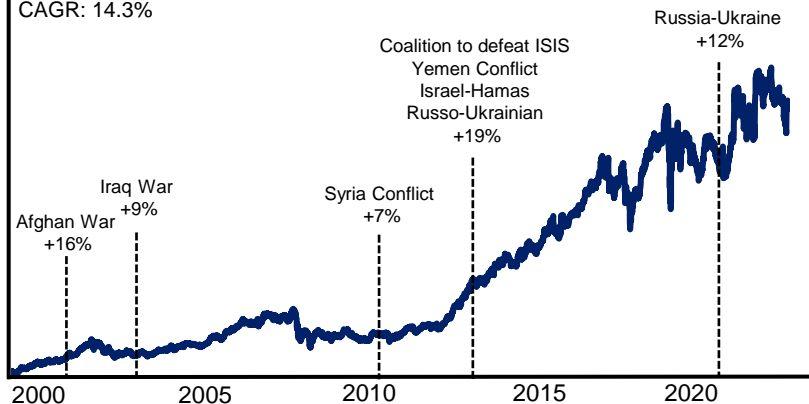
Source: Company 10-K



Positive Performance Driven by Geopolitical Tensions

2000-2023 LMT Stock Price

CAGR: 14.3%



Leading Aeronautics	Diversified Portfolio	Dominant Market Position
<p>Aeronautic revenues is currently the driver of more than 40% of Lockheed's revenue.</p> <p>Proven by F-22 and F-35's capabilities, Lockheed serves as a primary provider within the aeronautics industry.</p> <p>Lockheed is currently on track to become the primary developer of 6th generation fighter jets.</p>	<p>Lockheed specialized in cybersecurity systems like the integrated combat systems or the DoD cyber crime center.</p> <p>Development of training tools like the Advanced Gunnery Training System (AGTS).</p> <p>Maritime technologies like the Aegis Combat System for Australian fleets.</p>	<p>Lockheed currently holds 1.8x more contract obligations compared to its biggest competitor.</p> <p>When looking at industry wide factors, Lockheed holds a 65% market share by revenue.</p> <p>Lockheed remains one of the primary pioneers and innovators within the industry, top 3 spender in R&D in the industry.</p>

Recession Resilience	Geopolitical Factors	Global Military Modernization
<p>The defense industry overall has faced minor volatility during economic recessions and uncertainties.</p> <p>Government spending packages and budgets serves as a key driver for revenue.</p> <p>Back-order list, share buybacks, and high dividend proves high confidence within LMT.</p>	<p>Geopolitical tension often are the primary factor for increase in demand for defense.</p> <p>During periods of high uncertainty, emergency spending packages and aids are distributed more often.</p> <p>Crucial industry with key players who provide solutions to identify and end various conflicts</p>	<p>Continued increase in global military spending between the top super-powers.</p> <p>Competition amongst countries drives global defense budget expansions higher than analyst projections.</p> <p>Urgency for increase in R&D and innovation fighting for technological superiority</p>

Catalyst I: War & Geopolitical Tension

LMT presents a strong opportunity stemming from a dominant competitive position and strong geopolitical tailwinds

Current and Potential Conflicts

Russia-Ukraine: With Russia announcing its military and defense spending increase of 4% to 6% of GDP in 2024, we can expect the conflict to remain a recurring source of business for Javelins, Patriots, HIMARS, and now recently ATACMS.

Greater Asia: An increase in Chinese assertiveness have increased territorial disputes between China and neighboring countries in the East and South China Sea. Japan, Vietnam, and the Philippines in particular have complained officially about Chinese fishing and coast guard insurgences.

Greater Middle East: While conflict is now isolated to skirmishes between Israel and surrounding militias, Israel has expressed willingness to inflict retribution to Iran for militia funding and its nuclear program. American carrier patrols aim to reduce the risk of conflict expansion, but it may backfire by adding tension to the situation. Whether or not contagion happens, the risks of such will likely lead to an arms race of F-35s and Patriots by US allies like Israel, the UAE, and the Saudis.

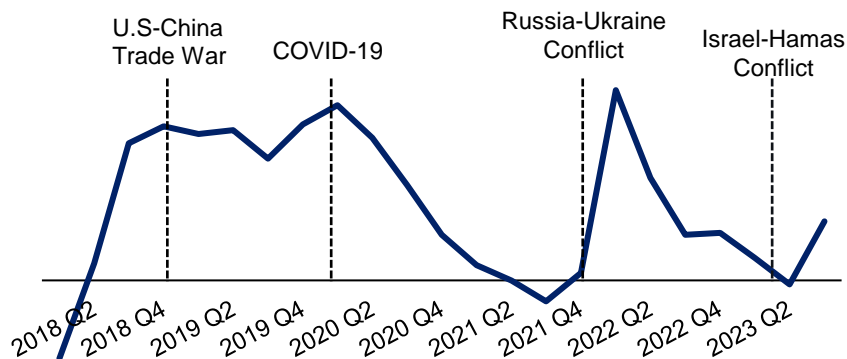
Increasing Foreign Defense Drives Geopolitical Risk

Increase in International Spending: Russia and China have both significantly increased military spending over the past 5 years and many of our most important allies like Ukraine, Israel, and Saudi Arabia has done the same. Such increase in spending is often the result of rising tensions or the country's active involvement with ongoing conflicts.

Impact on Lockheed: The increase in demand seen in allied countries for highly advanced defense technologies is often left for the US defense contractors to full-fill. In this case, Lockheed Martin has often played a major role like supplying the Javelin missiles to Ukraine, as well as the PAC-3 Patriot (missile system).

Demonstration of Effectiveness: Lockheed Martin's system against modern militaries provides soundness to US technologies. Russia's assault on US Patriot batteries in Ukraine shows that the system is practicality flawless. Bolstering LMT's attractiveness in the global weapons market.

Blackrock Geopolitical Risk Indicator



International Defense Spending Growth Over 5 Years

Country	2022 Spending	Past 5Y Total Growth
China	\$291 Billion	25.6%
Russia	\$86 Billion	40.2%
Saudi Arabia	\$75 Billion	0.5%
Israel	\$23 Billion	17.6%
Iran	\$6 Billion	48.9%
Average	\$96 Billion	26.6%
Median	\$75 Billion	25.6%

Catalyst II: Rising US Military Budget

Growth in defense budgets and current spending fuels substantial sales growth

Optimistic Company Outlook Due to Increasing Budgets

Impact of Increasing Spending: A continued increase in defense spending within both the domestic and international markets will further increase both the volume and value of incoming defense contracts. Competition will arise between countries, and demand for exports to important allies will surge.

Need for Innovation: Technological progress is now a key component of advantages in the real world. Additional research and development of various programs throughout aeronautics, missile & fire control, and rotary & mission systems will continue to surge in the coming decades. The urgency to remain dominant in all areas will remain as a key driver for increasing budgets and spending.

Key Revenue and Profit Drivers: Consistent growth in budgets is projected to heavily increase Lockheed's performance and market share in aeronautics, missiles & fire control, products that account for more than 50% of its revenue.

Top Primary CTA Contractor In the Biggest Contracts

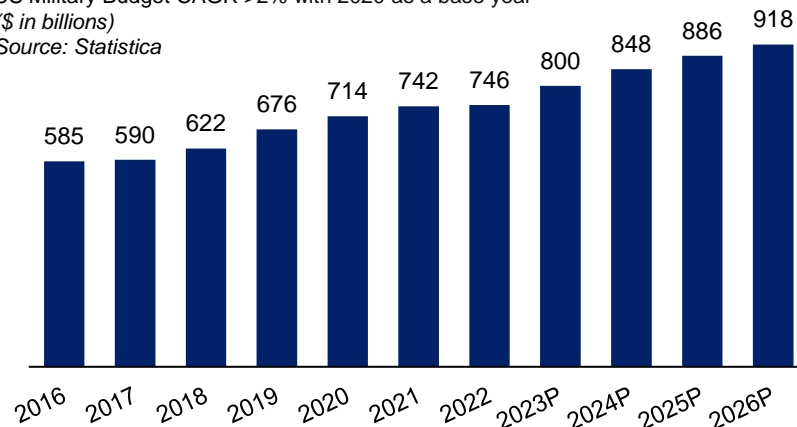
Primary Contractor versus Sub-Contractor: As a primary contractor, Lockheed is not only responsible for the overall design and completion of each project but also assigning and appointing its sub-contractors during the development period. In addition to being one of the top primary contractors, Lockheed is also involved in various other projects as a sub-contractor.

Top Contracts and Projects Served: Lockheed Martin was awarded some of the biggest contracts by The Pentagon throughout 2000-2023, these include: The Joint Strike Fighter Program (\$250B+), The Special Operations Forces Global Logistics Support Services (\$8B+), Global F-35 fleet operation support and sustainment (\$6.6B+), and Army Black Hawk Deal (\$2.3B+).

Increase In Contract Assets: Lockheed's latest quarterly filings revealed continuous 10% increase in contract assets on an annual basis, beating analyst estimates. This is mainly due to the recognition of revenue for fulfilling performance obligations in recent months, indicating high reliability, stable completion rates of its awarded projects, and collections of the revenues within.

Projected Department of Defense Budget

US Military Budget CAGR >2% with 2020 as a base year
(\$ in billions)
Source: Statista



LMT Leads The Defense Sector As The #1 Contract Holder

Company	Ranking	Contract Obligations (Billions)	Percent of Total Contract Obligations
Lockheed Martin Corp.	1	\$45.61	28%
Raytheon Technologies Corp.	2	\$25.70	16%
General Dynamics Corp.	3	\$21.93	13%
Pfizer Inc.	4	\$16.67	10%
The Boeing Co.	5	\$14.48	9%
Northrop Grumman Corp.	6	\$13.81	8%
Humana Inc.	7	\$7.74	5%
HII Corp.	8	\$6.49	4%
L3Harris Technologies Inc.	9	\$6.45	4%
BAE System PLC	10	\$5.17	3%

Catalyst III: Next Generation Air Dominance & Advancement in Production

LMT is best positioned to take advantage of increased demand in defense spending

Outlook for Aeronautics

Procurement and Maintenance: The Joint Strike Fighter program is the Department of Defense's most expensive weapons system program. The DOD estimates that this program will require nearly \$1.7 trillion in funding. This estimate includes the creating, purchasing, operating, and sustaining of all F-35 Lightning II aircraft weaponry. In 2022, there was a significantly higher demand for the F-35. In 2022, Finland, Switzerland, and Germany signed the Letter of Offer and Acceptance to be the seventh, eighth, and ninth FMS customer to join the program to procure more of the F-35.

Next Generation Air Dominance: The Next Generation Air Dominance is a United States Air Force sixth-generation air superiority initiative with a goal of fielding a "family of systems," specifically a fighter built to battle alongside drones that is to succeed the Lockheed Martin F-22 Raptor. Currently, The USAF awarded LMT \$975 million for the prototyping phase of the Next Generation Adaptive Propulsion program. Currently, the 6th Gen fighter \$2.3 billion contract is only being fought for by Boeing and Lockheed Martin as Northrop Grumman has decided to pull out of the race for the contract worth.

Other Growing Business Segments

Missile and Fire Control: There was a \$108M (4%) increase in net sales for 3rd quarter 2023 compared to the same period in 2022, with a \$15M (4%) increase in operating profits. In 2022 Lockheed Martin opened an 85,000 square-foot building expansion in Arkansas to support increased production of its PAC-3 MSE system. They are increasing production from 500 MSE's a year to 550 a year.

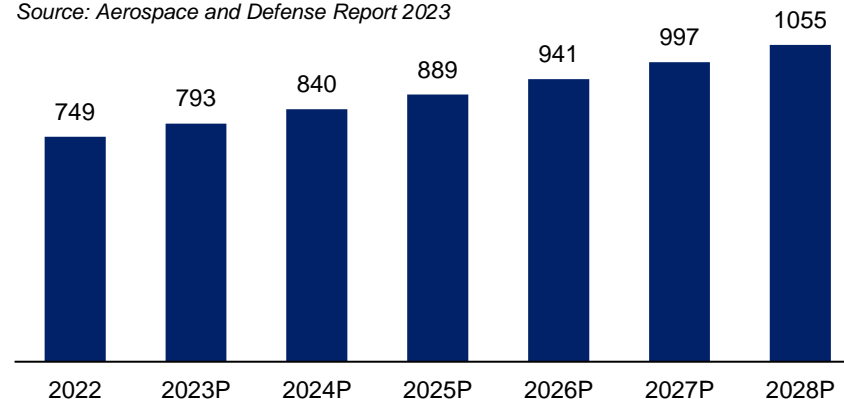
Rotary and Mission Systems: There was a \$340M (9%) growth in the net sales for this segment in 3rd quarter of 2023 compared to the 3rd quarter of 2022 which can be primarily attributed to a \$235M increase in net sales for integrated warfare systems and sensors (IWSS).

Space: Although there was \$219M (8%) growth in net sales in the 2023 3rd quarter compared to the 2022 3rd quarter, there was a 15% (\$45m) drop in operating profit primarily attributed to a drop in ULA launch volume.

Aeronautics Revenue Projection

Aeronautics CAGR with 2022 as base year: 5.88%
(\$ in billions)

Source: Aerospace and Defense Report 2023



Production Priorities

Investment in Production: While F-35 production remains constrained, focus has better more geared towards its F-16s, compromising of its backlog. It is expected it will hit production goals by 2025. PAC-3 interceptor production will be expected to increase by 66% with its new factory in Arkansas and winning \$142 million in investments. Meanwhile, a new factory is also being opened in Colorado to build new small space force satellites. Overall, the emphasis on more cost efficient weapons highlights the US's expectation to expect smaller conflicts as opposed to ones between major powers.

"One Lockheed Martin": This program intends to join all of Lockheed Martin's business's supply needs by using a company wide perspective. This means managing demand across all units of LMT which will result in large scale bulk purchasing of raw materials and mid-stage components. This adds to LMT's previous use of accelerated payments for smaller at-risk suppliers by not only providing them with cash in advance for orders, but also certainty in order volume and number of potential orders.

Valuation

Driven by the three expected catalysts, LMT presents significant value both on a relative and intrinsic basis

Discounted Cash Flow Analysis	2023E	2024E	2025E	2026E	2027E
Unlevered Free Cash Flow	8,033	7,198	7,587	8,107	8,696
Terminal Value @ 2% TGR					153,539
Present Value of UFCF	7,454	6,197	6,060	6,008	5,980
Present Value of TV					105,581

Enterprise Value		WACC		Assumptions
Enterprise Value	137,280			Operating Assumptions: Revenue CAGR of 6.47% during projections driven by rising geopolitical tensions and increasing US military budget. COGS of 84% and SG&A of 3% based on average. DCF: 2% Perpetuity growth rate based on analyst consensus and expected US growth. WACC based on stock price and current yield. Comps: Comps chosen based on similar industries and size.
Cash	2547	Rf (5-Year Treasury)	4.95%	
Total Debt	12,882	Equity Risk Premium	5.05%	
Equity Value	126,944	Beta	0.66	
Total Shares Outstanding	253	Cost of Equity	8.28%	
Implied Share Price	502	Percentage of Equity	86.10%	
Current Price	446	Cost of Debt	4.64%	
Implied DCF Return	13%	Percentage of Debt	13.90%	
Implied Comps Return	22%	WACC	7.78%	
Avg. Expected Return	18%			

Comparable Companies Analysis				EV/EBITDA Multiple			P/E Multiple		
Company Name	Ticker	Equity Value	Enterprise Value	2022A EV/EBITDA	2023E EV/EBITDA	2024E EV/EBITDA	2022A P/E	2023E P/E	2024E P/E
Northrop Grumman	NOC-US	74,358	86,793	19.7x	16.4x	15.2x	21.4x	21.4x	19.5x
Boeing	BA-US	114,226	157,055	(64.8x)	62.5x	17.6x	(16.3x)	(46.2x)	36.9x
General Dynamics	GD-US	66,796	77,467	15.7x	14.2x	12.5x	20.4x	18.7x	15.8x
RTX	RTX-US	108,428	139,989	15.4x	12.2x	10.8x	21.1x	14.5x	12.9x
Lockheed Martin	LMT-US	111,566	125,404	14.6x	12.8x	12.9x	22.5x	16.3x	16.5x
Upper Quartile					27.9x	15.8x		20.0x	23.9x
Median					15.3x	13.9x		18.7x	17.7x
Mean					26.3x	14.0x		2.1x	21.3x
High						62.5x		21.4x	36.9x
Low						12.2x		(46.2x)	12.9x

Risks and Mitigations

Easing geopolitical tensions, government regulations and supply chain are major risk factors for Lockheed Martin

Risk 1: Easing Global Tensions

- LMT's stock price rose 10% in the last week due to announcement of the war outbreak.
- If Ukraine-Russia and Israel-Hamas war end earlier than expected, then demand will subside resulting in a decline in stock price.
- Defense stocks typically rise after conflicts but soon lose their gains. Even if Israel-Hamas war continues, if it doesn't expand to other parts of the Middle East, the market may forget about it.

Risk 2: Government Regulation & Potential Shutdown

- Defense contractors like LMT can't raise prices and take more margin due to prices being fixed under past agreements with the U.S. Government and the defense industry struggling with supply chain issues.
- If a government shutdown happens, LMT may find their payments delayed and new contracts with LMT will most likely be postponed or not rewarded.
- The Stop Price Gouging the Military Act introduced by Sen. Elizabeth Warren would close loopholes in the law, preventing defense contractors from price-gouging the Pentagon.

Risk 3: Supply Chain & Faulty Product

- Geopolitical tensions and war can disrupt global supply chain and logistics, impacting the production of defense systems.
- Additionally, stricter government regulations may be implemented during times of war, slowing down LMT's supply chain and export processes.
- Increase risk of theft and loss of parts due to terrorist group targeting exports.
- Another issue is an increase in incorrect or incomplete parts being delivered costing the U.S. Defense Department \$183 million in labor costs.
- With faulty parts the data projected from EELs becomes skewed. Failing to meet the F-35s contract requirements damages LMT's finances & relationships.

High Impact

Low Impact

2

Increase in defense spending means the US will most likely be bidding out new contracts to defense contractors. Government shutdown should only last for a couple weeks, so LMT's stock price should only be volatile for a short amount of time. If the bill is passed, LMT will experience reduced profit margins, however, it will still be a strong competitor in the defense industry

3

LMT is certified by US CBP as CTPAT Tier III, the highest security status for import companies, meaning their suppliers have security controls specifically designed to mitigate risk of theft and loss of supplies. In response to delivering faulty parts, LMT has taken accountability and repaid those parts through compensating the government with \$70.6 Million in Lockheed Martin investments.

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War declining leading to a dip in the stock price. However, impact will be moderate as the US still spends a large portion of their budget to defense. Ever since 2016, the US defense budget has been rising steadily every year. An overall increase of 25% since 2016.

Low Probability

High Probability