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| **Company: General Dynamics** | **Ticker: GD Current Price: $ 212.55** | **Industry: Industrial Goods – A&D**  |
| Target Price: $ 240Stop Loss: $191.3 (10%)52 Week High/ Low: $148.76 / $214.11 | TTM P/E: 21.86Forward P/E: 20.20EPS: $2.09 | Beta: 0.87Credit Rating: A+ (S&P)Rating Outlook: Stable | Market Cap: $63.85bAvg Vol (12 M): 1.1mDividend Yield: 1.83% |

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| **Company Background:**  |
| General Dynamics Corp. operates as an aerospace and defense company that offers a broad portfolio of products and services in business aviation; combat vehicles, weapons systems and munitions; shipbuilding; and communication and information technology systems and solutions. The company operates through the following business groups: Aerospace, Combat Systems, Marine Systems, and Information Systems and Technology. The Aerospace group designs, manufactures and outfits a comprehensive family of Gulfstream business. The Combat Systems group designs, develops, and produces tracked and wheeled military vehicles, weapons systems and munitions. The Marine Systems group designs, builds and supports submarines and surface ships. The Information Systems and Technology group provides critical technologies, products and services. |
| **Industry Outlook:**  |
| * Growth in the Defense sub-sector is expected to be primarily driven by the newly elected US Administration’s increased focus on strengthening the nation’s military.
* Rising global tensions has led to international demand for defense and military products is increasing in the Middle East, Eastern Europe, North Korea, and the East and South China Seas. This is in turn resulting in increased defense spending globally, especially, in the United Arab Emirates (UAE), Saudi Arabia, India, South Korea, Japan, India, China, Russia – many of these countries have already started to increase purchases of next generation military equipment.
* Following multiple years of positive, but a subdued rate of growth, the report forecasts the sector revenues will likely grow by about 2.0 percent in 2017.
* The top 100 aerospace & defense (A&D) companies accounted for $709 billion in revenue, resulting in $69 billion in profits for 2016 – an increase from $689 billion in revenue and $64 billion in profits compared with 2015.
* President Trump included an increase in defense spending of about $25 billion in 2017 and is also looking for a 10% increase in US defense spending for 2018
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| **Investment Thesis:**  |
| * The United States has been at war for 93% of its existence. This will likely continue for the next 10+ years with the constant threat from North Korea, Russia, Iran, and potential emerging threats in Africa and South America. Further non-nation states, such as ISIS and other fundamentalists continue their threat of global violence.
* With a Republican currently in the White House and a Republican controlled Congress, there will be continued growing investments into the military and defense funding.
* Large, long-term contracts, such as that of the next Ballistic Missile Submarine, and Next-Generation Combat Vehicle will provide stable revenue for years to come. GD is one of two companies authorized to construct submarines and typically shares these long-term contracts.
* Further stability is provided by the diversification of the General Dynamics portfolio, in both their Gulfstream business unit and their Information Technology Business Unit. Gulfstream has more than $11 B of a backlog entering 2017, and foresees a stable growth outlook. With the ever growing cyber security threat, GDIT should see strong growth from both governments as well as corporations looking to utilize their security services.
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| **Investment Risks:**  |
| * Peace in the U.S. and international markets could adversely affect its business and financial results.
* US Government Sequestration and/or significant budget cuts to defense spending.
* Significant design failure in its Aerospace division causing a large loss of life will result in decreased sales, thus harming companies diversified earnings
* Cyber Intrusion of a GD:IT managed client could result in negative publicity, similar to what we are currently seeing with Equifax.
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| **Most recent quarter financial highlights (Apr- Jun 2017):**  |
| * Company Wide – Operating earnings up 2.8% to $1.1B - Operating Costs and Expenses are down nearly 2%
* Combat Systems – Which comprises 44% of Revenue, has seen revenue increase 9%, and Operating Earnings up 9.8%
* Earnings from Continuous operations up 4.9% to $749 Million
* Diluted EPS up 6.5% to $2.45 – Company increased its full year EPS outlook from $9.50-9.55 to $9.70-9.75
* GD:EB Awarded $5B to design next Ballistic Missile Submarine
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| **Financial Performance:** | **Discounted Cash Flow**  |
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| In Millions of USD | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 Est | 2018 Est |
| Revenue  | 31,513.0 | 30,930.0 | 30,852.0 | 31,469.0 | 31,353.0 | 31,202.5 | 33,017.3 |
| Operating Profit | 3,518.0 | 3,727.0 | 3,918.0 | 4,155.0 | 4,309.0 | 4,200.9 | 4,409.4 |
| Net Income  | -332.0 | 2,357.0 | 2,533.0 | 2,965.0 | 2,955.0 | 2,977.8 | 3,151.4 |
| Revenue Growth % | -3.6 | -1.9 | -0.3 | 2.0 | -0.4 | -0.5 | 5.8 |
| EBITDA% | 13.1 | 13.7 | 14.3 | 14.7 | 15.2 | 15.0 | 14.8 |
| Operating Profit % | 11.16% | 12.05% | 12.70% | 13.20% | 13.74% | 13.46% | 13.35% |
| Net Income Margin | 7.1 | 8.1 | 8.7 | 9.4 | 9.8 | 7.1 | 8.1 |
| D/E | 2.01 | 1.45 | 1.99 | 1.98 | 2.22 | n/a | n/a |
| EPS | 6.36 | 7.10 | 7.89 | 9.03 | 9.87 | 9.81 | 10.53 |
| PE Ratio  | 10.89 | 13.46 | 17.45 | 15.20 | 17.49 | 21.67 | 20.20 |
| Current Ratio | 1.36 | 1.48 | 1.27 | 1.17 | 1.23 | n/a | n/a |
| ROE | -2.70 | 18.21 | 19.24 | 26.28 | 27.22 | n/a | n/a |
| ROA | -0.96 | 6.75 | 7.15 | 8.81 | 9.11 | n/a | n/a |
| Dividend Per share  | 2.04 | 2.24 | 2.48 | 2.76 | 3.04 | 3.31 | 3.61 |
| FCF | 2,235.0 | 2,675.0 | 3,207.0 | 2,038.0 | 1,806.0 | 3,004.4 | 3,178.0 |

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|  | 2012-16 | 2017-21 |
| Avg Revenue growth  | -0.81 | 4.04 |
| Avg EBITDA Margin  | 14.2 | 14.85 |
| Avg Net Income Margin  | 12.55 | 13.4 |
| Avg Debt/Equity  | 31.1 | 27.22 |
| Avg FCF / Margin  | 8.48 | 9.01 |
| Cost of Debt | 2.71 |
| Tax Rate | 27.765 |
| Cost of Equity  | 7.71 |
| WACC | 7.4 |
| Perpetuity growth rate  | 3 |

**Analyst Opinion**

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| --- | --- | --- |
| Buy:16 | Hold: 7 | Sell:1 |
| Target Price Range | 196-266 |  |
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| Source: Bloomberg |

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| **Relative Valuation** | **Total Return** |
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|  | GD | Lockheed  | Raytheon | UTC | Industry Avg.\* |
| P/E | 21.24 | 25.03 | 25.87 | 18.10 | 29.42 |
| P/B | 6.25 | 60.69 | 5.42 | 3.48 | 19.94 |
| Dividend Yield  | 1.57 | 2.52 | 1.7 | 2.36 | 1.33 |
| Revn Grth  | -1.27 | 9.6 | 4.2 | 2.7 | 3.41 |
| NI Grth  | 2.19 | 85.86 | 25.2 | 3.47 | 25.45 |
| Operating Margin  | 13.74 | 11.74 | 13.46 | 14.28 | 9.23 |
| Debt / Equity  | 37.74 | 945.2 | 52.53 | 86.66 | 269.63 |
| Market Cap | 63.77 B | 91.56 B | 54.39 B | 94.41 B | 44.33 B |
| Revenue TTM | 31.353 B | 47.248 B | 24.069 B | 57.244 B | 28.40 B |
| Net Income TTM | 3.062 B | 3.753 B | 2.173 B | 5.436 B | 1.73 B |
| FCF TTM | 979.25 M | 2.27 B | 1.04 B | 3.43 B | 2.35 B |

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|  | GD | A&D | S&P 500 |
| YTD | 22.38 | 29.34 | 11.90 |
| 2016 | 35.52 | 21.47 | 9.54 |
| Last 3 Years  | 86.65 | 70.01 | 24.61 |
| Last 5 Years  | 260.28 | 191.8 | 71.46 |

**CSR Characteristics**

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|  | GD | Industry  |
| Governance Disclosure Score | 55.36 | 54.82 |
| ESG Disclosure:  | 24.79 | 33.60 |
| Social Disclosure Score | 24.56 | 35.67 |
| Environmental Disclosure Score | 11.63 | 31.30 |

Data: Bloomberg |