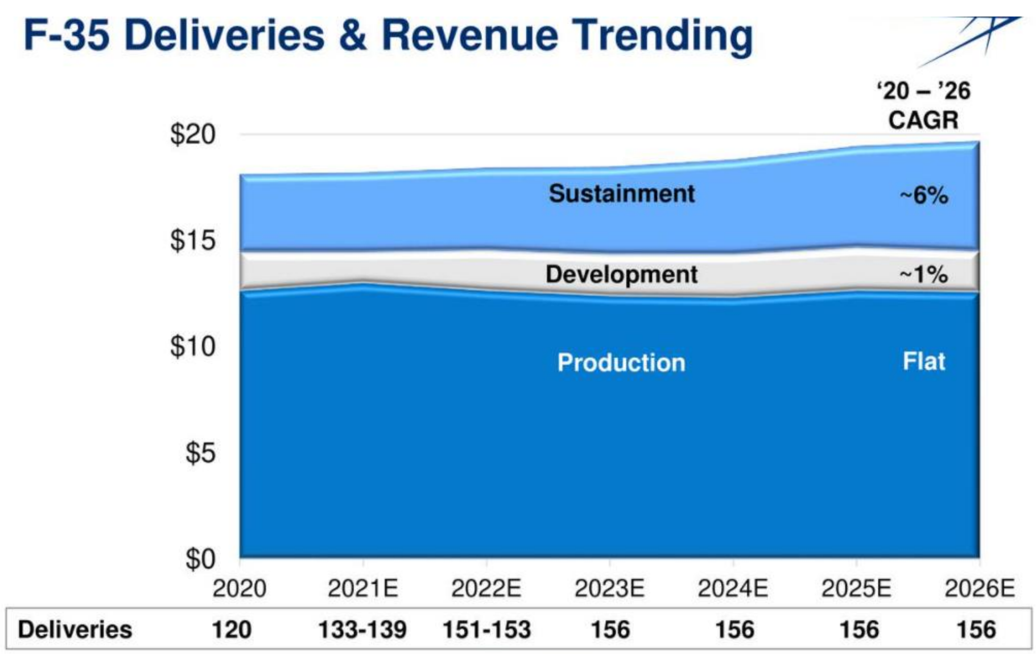
Inside Lockheed Martin: Last Quarter's Progress.

Oct. 29, 2021

Usually, Lockheed's quarterly earnings calls are rather repetitive: sales up 5-10% with one business area or the other having a moment, but all positively trending upwards. Not this time around. Lockheed surprised analysts and investors by issuing a new 5-year plan, which includes decelerating sales over the next year and a half (by 1-2%) before returning to growth in 2023. There are several factors leading to its paused growth and several business areas that are expected to fuel future growth. In the "pause" period, Lockheed's plan is to increase its cash benefits to shareholders to keep us happy.

Revenue this quarter fell by 3%. This was mostly caused by larger-than-expected supply chain issues, especially in the F-35 program. Lockheed expects these supply chain issues to persist for at least a year, which is part of the reason for Lockheed's decelerating sales expectations for 2022. Another large component to the revised plan comes from Great Britain's renationalization of its Atomic Weapons Establishment in an attempt to become an independent nuclear force. Lockheed provided products and services to that program including the Trident missile containing thermonuclear warheads. The loss of that program is an almost $1 billion dollar hit to Lockheed's top line. Lockheed and the US government came to a new agreement on F-35 production timelines, which decreased the number of jets per year from about 170 to 156. The total number of jets planned remains unchanged, but the pace of production has changed.



Those 2 "hits" to Lockheed's sales come down to the risk of changing political environments, which is a constant fact of life for Lockheed, where "government" is always Customer Number One. This change has been a negative, though relatively minor. But long-term investors should always remember that political environments and attitudes toward defense spending change in the other direction, too—sometimes suddenly, when things happen in the world which remind everyone about danger, and the role of defense spending in reaction to danger.

Management's focus, right now, will turn to 4 growth areas expected to contribute to revenues in the 2023 to 2026 timeframe. Those areas are hypersonics, classified programs, current programs which are ramping up like the CH-53 heavy lift helicopter, and a few new programs that Lockheed is currently competing for. In total, these 4 focus areas should add close to 10% growth annually.

To curb investors' disappointment in 2022's expectations, Lockheed plans on pouring on the shareholder returns. It announced an 8% dividend increase and increased its share repurchase amount and rate. In the past 9 months, Lockheed has repurchased $2 billion worth of shares. In the next 18 months, Lockheed plans on repurchasing $6 billion worth of shares, or about 7% of the company. The goal is that by the time 2023 rolls around and the company is back to its normal growth rates, investors will be rewarded even more because the share count will be significantly lower. As Lockheed's stock performance the day after earnings showed (falling 11%), Wall Street reacted strongly and negatively to management's news. But it's important to keep the big picture in mind: as long-term investors, having patience over the next year or so will pay off greatly in the future—especially now that the stock has gone from "reasonably valued" to "cheaply and doubtfully valued." Lockheed has gone through years of declining revenue before (even worse than 1-2%) and still has rewarded investors greatly over time.