

Leonardo DRS, Inc.

**4Q23 adj. EPS above Street and BofAe;
2024 EPS outlook below expectations**

Maintain Rating: BUY | PO: 22.00 USD | Price: 21.09 USD

Topline growth of 13% Y/Y on strong ASC

Leonardo DRS (NASDAQ: DRS) reported 4Q23 adj. EPS of \$0.31 vs. STe \$0.30 and BofAe \$0.29 as softer margins were offset by lower-than-expected share count. Revenue grew 13% Y/Y driven by strength at Advanced Sensing and Computing (multi-mission advanced sensing, naval and ground network computing). 4Q23 adj. EBITDA margins were higher at ASC on higher volumes and strong mix (15.5% vs. 4Q22 15.3%), while the opposite led to weaker margins at IMS (11.2% vs. 4Q22 13.2%). 4Q23 FCF came in strong at \$494mn (consistent with seasonality), above STe \$466mn and BofAe \$480mn. Demand remains robust, with book-to-bill was 1.1x for 4Q23 and 1.2x for 2023.

2024 EPS outlook softer than expected, revenue in line

DRS initiated 2024 outlook of \$2.925-3.025bn in revenue and \$365-390mn in adj. EBITDA, both in line with consensus. However, adj. EPS range of \$0.74-0.82 is below STe of \$0.83 and BofAe of \$0.85. this could be partially attributed to higher-than-expected share count. We look favorably upon these results, but the market might not react well to the softer than expected EPS outlook. We maintain our Buy rating and may revisit our estimates after the call with management.

Exhibit 1: DRS 4Q23 Results

Revenue grew 13% Y/Y driven by strength at Advanced Sensing and Computing

Quick-take of results vs. Expectations:	
Adj. EPS	3Q23: \$0.20 vs. BofAe: \$0.15 vs. BBG: \$0.15 vs. 3Q22: \$0.17 (3Q23 up 17.3% Y/Y)
Revenue	3Q23: \$703mn vs. BofAe: \$663mn vs. BBG: \$682mn vs. 3Q22: \$634mn (3Q23 up 10.9% Y/Y)
Operating margin	3Q23: 8.4% vs. BofAe: 8.1% vs. 3Q22: 59.3%
FCF	3Q23 Actual: \$21mn vs. BofAe: \$66mn vs. BBG: \$30mn vs. 3Q22: \$-17mn (increased 223.5% Y/Y)
Segment Revenue	Advanced Sensing and Computing (ASC): 3Q23: \$431mn vs. BofAe: \$426mn vs. 3Q22: \$408mn
	Integrated Mission Systems (IMS): 3Q23: \$277mn vs. BofAe: \$247mn vs. 3Q22: \$229mn
	Corporate & eliminations: 3Q23: \$-5mn vs. BofAe: \$-11mn vs. 3Q22: \$-3mn
Backlog	3Q23: \$4.7bn vs. \$3.1bn in 3Q22
Book-to-bill	3Q23: 1.5x vs. 1.4x in 3Q22
EPS outlook	\$0.70-0.72 (vs. prior \$0.66-0.69)

Source: BofA Global Research, company filings

BofA GLOBAL RESEARCH

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Stock Data

Price	21.09 USD
Price Objective	22.00 USD
Date Established	20-Nov-2023
Investment Opinion	B-1-9
52-Week Range	10.80 USD - 21.35 USD
Mrkt Val (mn) / Shares Out (mn)	5,533 USD / 262.4
Free Float	19.7%
Average Daily Value (mn)	10.35 USD
BofA Ticker / Exchange	DRS / NAS
Bloomberg / Reuters	DRS US / DRS.OQ
ROE (2023E)	8.6%
Net Dbt to Eqty (Dec-2022A)	4.1%

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Refer to important disclosures on page 3 to 5. Analyst Certification on page 2. Price Objective Basis/Risk on page 2.

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Timestamp: 27 February 2024 09:10AM EST

Price objective basis & risk

Leonardo DRS, Inc. (DRS)

We derive our \$22 PO based on a sum-of-the-parts EV/EBITDA multiple of 13x on the Advanced Sensing and Computing (ASC) 2024e earnings and 17x on the Integrated Mission Systems (IMS) segment. We view an EV/EBITDA multiple as the best way to value the equity as it accounts for the margin expansion expected from newly priced Columbia-class shipsets.

The SOTP valuation implies a 15x multiple, or 1.2x relative multiple to the S&P 500 on 2024 estimates and a 1.0x multiple to the defense primes. A multiple above the broader market and in line with SMID cap defense peers alludes to the company's high growth profile and exposure to long term programs with strongly predictable schedules and funding.

Downside risks to our PO are continued supply chain challenges pertaining to microelectronics, lumpiness of Columbia-class revenues, poor execution on fixed-price programs, continued fixed-price contract awards, poor award activity in the international market, potentially diminished funding for land systems in which DRS supports, and volatility from potential parent company secondary offering.

Upside risks to our PO are even higher-than-expected growth in defense spending, accelerated margin ramp on the Columbia-class program, more cost-plus contract awards, continued strength in the international market, continued funding for land systems, and the gradual reduction in Leonardo SpA's ownership stake.

Analyst Certification

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Leonardo DRS (DRS) Price Chart



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Equity Investment Rating Distribution: Aerospace/Defense Electronics Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	31	62.00%	Buy	23	74.19%
Hold	11	22.00%	Hold	9	81.82%
Sell	8	16.00%	Sell	6	75.00%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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