

Mercury Systems

Restructuring: Two divisions into one,
Roger Wells named new COO

Maintain Rating: UNDERPERFORM | PO: 30.00 USD | Price: 30.97 USD

Mission Systems & Microelectronics divisions unifying

On January 17, Mercury Systems (NASDAQ: MRCY) announced that it would be unifying its Mission Systems and Microelectronics divisions into one structure. The company expects the consolidation to streamline operations and establish clearer accountability. In an effort to further simplify the business and rightsize the cost structure, MRCY also initiated a workforce reduction on January 12. The company intends to eliminate 100 positions and take restructuring charges of \$10-12mn, which will be recognized in 3QFY24 (ending March 29).

Wells as COO, CGO Harbison and EVP Couture step down

MRCY also announced the appointment of Roger Wells as Chief Operating Officer, who will be tasked with leading the resulting unified business effective January 22. Wells brings to the COO role over 25 years of experience in operations, engineering, and program management. Most recently, Wells served as President of the MRCY's Microelectronics division. Between 2008 and 2021, he served in various VP positions at FLIR Systems, including VP of Operations and VP/GM of Unmanned Systems and Integrated Solutions. Between 1998 and 2006, he served as a Director in various roles at Northrop Grumman. The organizational restructuring also extends to MRCY leadership, with Chief Growth Officer Christine Harbison and EVP of Execution Excellence Allen Couture scheduled to step down after a brief transition period.

Steps in the right direction, but awaiting results

We note that these measures are in line with Mercury's four focus areas outlined during 4QFY23 earnings ([see our report](#)). We expect MRCY to be in a better position to enhance execution and rationalize costs with a more streamlined operational structure. However, the road to margin and free cash flow expansion is long and winding. While these measures are a step in the right direction, they are the first of many that must be taken to correct course. Additionally, we fear that the consolidation could limit transparency into MRCY's different business lines. We maintain our Underperform rating.

18 January 2024

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Stock Data

Price	30.97 USD
Price Objective	30.00 USD
Date Established	29-Nov-2023
Investment Opinion	B-3-9
52-Week Range	28.90 USD - 59.13 USD
Mrkt Val (mn) / Shares Out (mn)	1,722 USD / 55.6
Free Float	87.8%
Average Daily Value (mn)	13.79 USD
BofA Ticker / Exchange	MRCY / NAS
Bloomberg / Reuters	MRCY US / MRCY.OQ
ROE (2023E)	3.7%
Net Dbt to Eqty (Jun-2022A)	25.1%
ESGMeter™	Medium

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EVP – Executive Vice President

VP – Vice President

GM – General Manager

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Timestamp: 18 January 2024 03:00AM EST

Price objective basis & risk

Mercury Systems (MRCY)

Our \$30 PO is based on a 0.9x relative EV/EBITDA multiple on CY24 estimates, below the historical average of 1.4x. We believe this fairly accounts for the operational challenges across a higher mix of development programs and long semiconductor lead times.

Risks to the upside: Faster than expected improvement to the high-end processing supply chain could positively impact our estimates. Accretive acquisitions could provide upside to our estimates.

Risks to the downside: If there were a reversal in the defense primes' secular shift towards subsystems outsourcing, Mercury Systems' revenue would be negatively affected. Despite the complex and costly defense business process and high-capital requirements, the large commercial enterprises (such as blade server providers) or Silicon Valley technology companies could enter the military secure processing and storage subsystems business. Should MRCY run into any further problems with integrating M&A, containing its costs, or transitioning development programs to production, there could be downside risk to our estimates.

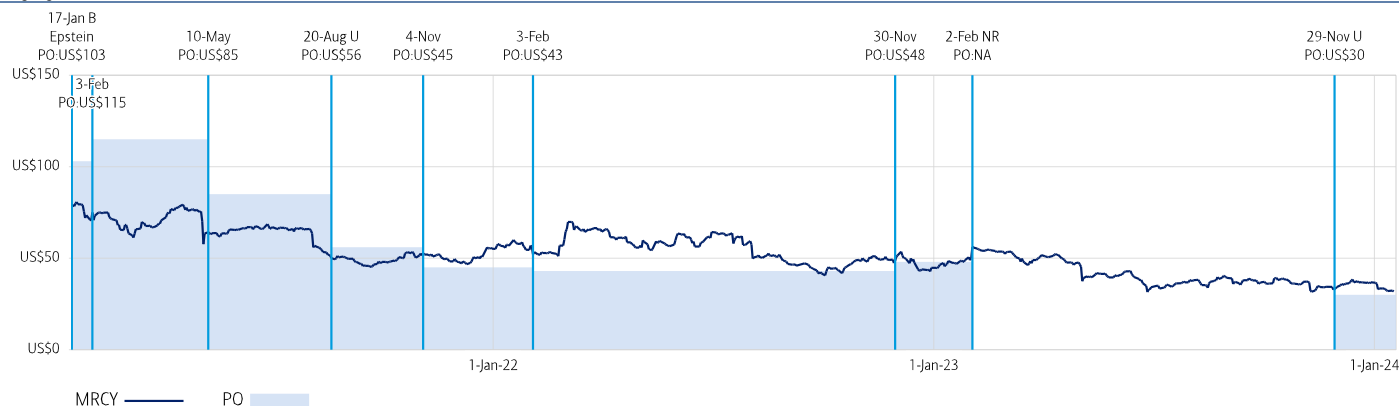
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Disclosures

Important Disclosures

Mercury Systems (MRCY) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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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%
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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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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

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