

Equities

18 April 2012 | 13 pages

Textron Inc. (TXT)

A Saved by the Bell Rerun, but Cessna's Still Clipped

- Company Update
- Target Price Change
- Estimate Change

■ **Stock Call** – We're still Neutral on TXT following a strong 1Q12 print (beat Street EPS ests. by 17%) driven by commercial Bell helicopter demand & seasonally strong auto demand in N. America. Meanwhile, Cessna lost money this Q & still sees pricing pressure, although customer sentiment improved (albeit off record lows). Overall, we're still waiting for sustained bizjet volume recovery to allow for better capacity utilization & pricing power. In our view, shares underperformed by ~300 bps today due to profit-taking (TXT up 49%+ YTD) & Cessna falling short of relatively high expectations.

■ **Key Q Positives** – **1)** Bell commercial deliveries doubled y/y as sales beat our est. by 9%, driving better margins (244 bps better y/y and 184 bps better than our est.); while these high margins are likely unsustainable over 2012 as dilutive commercial sales increase, the segment's performing well; **2)** Cessna jet deliveries up 23% y/y & margins improved 600 bps y/y after 1Q11's charge, but it still lost money despite aftermarket growth (we calculate negative 8% margins ex-accretive aftermarket) due to negative pricing environment & low volumes (vs. capacity); **3)** Industrial had its strongest margin quarter in years (9.7% beat our est. by 317 bps) on higher volumes (strong North America auto) & improved business practices; implies potential upside to 2012 margin guidance (6.5-7.5%), although still some Europe risks this year; **4)** TFC profitable earlier than expected (& first time since 3Q08); we expect volatility over the next few quarters TFC but could be source of upside vs. guidance. Our PT increases to \$27.

■ **Key Negatives** – **1)** Beat Street EPS est. by 6c but maintained guidance of \$1.80-2.00 vs. Street's \$1.91 due to lack of visibility in turns-based Cessna market & Europe auto production risks; **2)** Cessna is spot market & lacks visibility as 2013 delivery slots appear unfilled, backlog down ~9% q/q (36% y/y) & pricing pressured by supply/demand imbalance; **3)** Systems sales down 15% y/y w/ 9.3% margin (down 260 bps y/y) due to a pressured budget environment that is seeing contracts move through the system slowly; implies risk to guidance (flat sales & 9.5-10.5% margins), although long-term prospects supported by recent UAV wins.

Neutral	2
Price (18 Apr 12)	US\$26.65
Target price	US\$27.00
from US\$25.00	
Expected share price return	1.3%
Expected dividend yield	0.3%
Expected total return	1.6%
Market Cap	US\$7,457M

Price Performance (RIC: TXT.N, BB: TXT US)



EPS	Q1	Q2	Q3	Q4	FY	FC Cons
2011A	0.10A	0.29A	0.45A	-0.06A	0.79A	1.31A
2012E	0.41A	0.46E	0.50E	0.61E	1.98E	1.91E
Previous	0.30E	0.44E	0.48E	0.65E	1.88E	na
2013E	0.45E	0.53E	0.55E	0.71E	2.24E	2.30E
Previous	0.42E	0.50E	0.53E	0.69E	2.15E	na
2014E	0.51E	0.59E	0.61E	0.78E	2.50E	2.70E
Previous	0.47E	0.56E	0.60E	0.76E	2.40E	na

Source: Company Reports and dataCentral, CIR. FC Cons: First Call Consensus.

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See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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TXT.N: Fiscal year end 31-Dec						Price: US\$26.65; TP: US\$27.00; Market Cap: US\$7,457m; Recomm: Neutral					
Profit & Loss (US\$m)	2010	2011	2012E	2013E	2014E	Valuation ratios	2010	2011	2012E	2013E	2014E
Sales revenue	10,525	11,275	12,601	13,171	13,674	PE (x)	32.9	33.8	13.5	11.9	10.7
Cost of sales	-8,605	-9,308	-10,403	-10,874	-11,288	PB (x)	2.5	2.7	2.2	1.9	1.6
Gross profit	1,920	1,967	2,198	2,298	2,386	EV/EBITDA (x)	13.2	9.4	6.0	5.2	4.6
Gross Margin (%)	18.2	17.4	17.4	17.4	17.4	FCF yield (%)	9.0	7.9	3.9	6.5	8.3
EBITDA	619	880	1,367	1,517	1,611	Dividend yield (%)	0	0	0	0	0
EBITDA Margin (%)	5.9	7.8	10.8	11.5	11.8	Payout ratio (%)	0	0	0	0	0
Depreciation	-393	-403	-364	-430	-430	ROE (%)	3.0	8.5	19.0	17.9	16.9
Amortisation	0	0	0	0	0	Cashflow (US\$m)	2010	2011	2012E	2013E	2014E
EBIT	226	477	1,003	1,087	1,181	EBITDA	619	880	1,367	1,517	1,611
EBIT Margin (%)	2.1	4.2	8.0	8.3	8.6	Working capital	48	-147	-182	-139	-82
Net interest	-140	-140	-145	-117	-100	Other	326	335	-428	-406	-422
Associates	0	0	0	0	0	Operating cashflow	993	1,068	757	972	1,107
Non-op/Except	0	0	0	0	0	Capex	-270	-423	-451	-460	-460
Pre-tax profit	86	337	857	970	1,081	Net acq/disposals	1,785	1,153	948	1,000	250
Tax	6	-95	-275	-310	-346	Other	34	113	-2	0	0
Extraord./Min.Int./Pref.div.	-6	0	-2	0	0	Investing cashflow	1,549	843	495	540	-210
Reported net profit	86	242	581	660	735	Dividends paid	-22	-22	-23	-24	-24
Net Margin (%)	0.8	2.1	4.6	5.0	5.4	Financing cashflow	-3,493	-1,951	-430	-688	-224
Core NPAT	245	242	583	660	735	Net change in cash	-961	-46	825	824	674
Per share data	2010	2011	2012E	2013E	2014E	Free cashflow to s/holders	723	645	306	512	647
Reported EPS (\$)	0.28	0.79	1.97	2.24	2.50						
Core EPS (\$)	0.81	0.79	1.98	2.24	2.50						
DPS (\$)	0	0	0	0	0						
CFPS (\$)	3.28	3.48	2.57	3.30	3.76						
FCFPS (\$)	2.39	2.10	1.04	1.74	2.20						
BVPS (\$)	10.81	9.86	12.07	14.36	16.92						
Wtd avg ord shares (m)	274	278	276	278	278						
Wtd avg diluted shares (m)	303	307	294	294	294						
Growth rates	2010	2011	2012E	2013E	2014E						
Sales revenue (%)	0.2	7.1	11.8	4.5	3.8						
EBIT (%)	nm	111.1	110.2	8.4	8.6						
Core NPAT (%)	57.4	-1.4	140.7	13.2	11.5						
Core EPS (%)	36.8	-2.9	151.3	13.3	11.5						
Balance Sheet (US\$m)	2010	2011	2012E	2013E	2014E						
Cash & cash equiv.	931	885	1,710	2,534	3,208						
Accounts receivables	892	856	1,044	1,100	1,139						
Inventory	2,277	2,402	2,612	2,753	2,852						
Net fixed & other tangibles	4,286	3,964	4,166	4,204	4,266						
Goodwill & intangibles	1,632	1,635	1,635	1,635	1,635						
Financial & other assets	5,264	3,873	2,849	1,874	1,645						
Total assets	15,282	13,615	14,016	14,101	14,745						
Accounts payable	622	833	1,085	1,122	1,162						
Short-term debt	19	146	464	0	0						
Long-term debt	5,943	4,287	3,687	3,487	3,287						
Provisions & other liab	5,726	5,604	5,420	5,496	5,588						
Total liabilities	12,310	10,870	10,656	10,105	10,037						
Shareholders' equity	2,972	2,745	3,360	3,996	4,708						
Minority interests	0	0	0	0	0						
Total equity	2,972	2,745	3,360	3,996	4,708						
Net debt	5,031	3,548	2,441	953	79						
Net debt to equity (%)	169.3	129.3	72.6	23.8	1.7						

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Reviewing Our Neutral Rating

In our view, Cessna plays in a particularly pressured portion of the bizjet market and likely relies on spot sales over the next year.

Bell's recovery appears to be in full swing as commercial demand picks up and military demand persists.

We believe UAV and military helo demand mostly offsets pressures from falling op tempo abroad.

We expect margins to rebound off historic lows driven by Cessna and Bell. This is offset by potential weakness in Systems and Industrial. Also contributing is the Finance segment's ability to turn a profit thanks to the reclassification of some non-captive assets in 4Q11.

- **Uncertain Cessna** – Although Cessna is working to reduce its cost base, robust demand still isn't materializing for smaller-cabin jets while the segment is only becoming busier with new entrants (ie Embraer), forcing TXT to maintain elevated R&D through 2014 as it brings new models on line. On the plus side, we see positive incremental margins over the long-term as Cessna reduces headcount and moves facilities to Mexico.
- **Better Bell** – Bell ceded commercial market share over the past several years (from 55% to 15%) while it focused on developing the military V-22. While this likely requires further investment over the next few years, volume and margin performance to-date are indicative of a recovering segment seeing a pick up in commercial (better demand & new products) and persistent military demand (at least through 2014 while marquee platforms are producing at max rate).
- **Pressured defense has windows of opportunity** – While decreasing operational tempo pressures armored vehicle and precision weapon sales, we expect Bell military (including international sales) and international UAVs to provide some support to an otherwise pressured defense business. Textron systems is also looking to ship-to-shore connector, Humvee recap, Canadian TAPV, and large SFW sales to provide some resiliency, although risks abound amidst a pressured budget environment.
- **Potential weakness from auto exposure** – European automotive production could decelerate over the coming years, impacting the Industrial segment which saw its historic lows in 2009. We note that ~60% of the segment is comprised of automotive supplier Kautex which has 81% international sales (mostly Europe).
- **Finance segment (TFC) still a wild card** – While TFC is a non-core asset, 4Q11 changed strategy to further pare down the non-captive portfolio leaving TFC primarily with assets that help support TXT sales (mostly aviation). As such, we now expect TFC to breakeven in 2012 and potentially turn a profit in 2013E, although the driver here is an accounting change that moved \$266m of distressed golf mortgage assets to "held for sale."

Figure 1. Updated Earnings Snapshot

\$ in Millions	2011	1Q12	2Q12E	3Q12E	4Q12E	2012E	2013E	2014E
Revenue	\$11,275	\$2,856	\$3,082	\$3,136	\$3,527	\$12,601	\$13,171	\$13,674
Y/Y Growth	7%	15%	13%	11%	8%	12%	5%	4%
Operating Income (EBIT)	\$477	\$212	\$237	\$253	\$301	\$1,003	\$1,087	\$1,181
Total Operating Margin	4.2%	7.4%	7.7%	8.1%	8.5%	8.0%	8.3%	8.6%
Pre-Tax Income	\$337	\$177	\$199	\$217	\$265	\$857	\$970	\$1,081
Income Taxes	(95)	(57)	(64)	(69)	(85)	(275)	(310)	(346)
Effective Tax Rate	28.2%	32.2%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%
Net Income (Cont. Ops)	\$242	\$120	\$135	\$147	\$180	\$583	\$660	\$735
EPS (Cont.Ops) ex Charges	\$0.79	\$0.41	\$0.46	\$0.50	\$0.61	\$1.98	\$2.24	\$2.50
Average Diluted Shares	307.3	294.6	294.3	294.3	294.3	294.4	294.3	294.3

Source: Citi Investment Research and Analysis, Company Reports

Model and Target Price Changes

1Q12's EPS beat of 11c flows through our model as we improve our outlook for Bell and Industrial margins.

Our PT increases to \$27 as we boost our Bell and Industrial sales estimates after a strong 1Q12. This is offset by our weaker Systems outlook which appears to be impacted by a slower defense environment, especially for TXT's ground-exposed military goods. We've also boosted our margin expectations for Bell and Industrial, again due to strong 1Q12's performance. Specifically, the Industrial segment appears set to realize strong margins based on extensive efforts to restructure the business. TFC also appears to be positioned to earn in 2012.

Figure 2. Model Changes

\$ millions, except EPS	2Q12E		2012E		2013E		2014E		Comments
	Old	New	Old	New	Old	New	Old	New	
Net Sales	\$3,010	\$3,082	\$12,421	\$12,601	\$13,019	\$13,171	\$13,515	\$13,674	Better Bell commercial vs. weaker Systems
Cessna	\$758	\$769	\$3,422	\$3,437	\$3,657	\$3,675	\$3,883	\$3,902	No material change
Bell	\$1,027	\$1,064	\$4,211	\$4,314	\$4,545	\$4,637	\$4,776	\$4,873	Expect better commercial deliveries
Systems	\$450	\$422	\$1,808	\$1,726	\$1,771	\$1,731	\$1,749	\$1,701	Expect weaker defense sales
Industrial	\$744	\$766	\$2,803	\$2,880	\$2,855	\$2,936	\$2,912	\$3,004	Auto production stronger than expected
Finance	\$31	\$61	\$178	\$244	\$192	\$192	\$195	\$195	Better 2012 as non-captive is sold off
Manuf. Op. Margin	8.7%	9.0%	9.0%	9.3%	9.3%	9.5%	9.6%	9.8%	
Cessna	3.0%	3.0%	4.4%	4.2%	5.6%	5.6%	6.7%	6.7%	Worse 2012 on 1Q12 miss
Bell	13.8%	14.0%	13.7%	14.0%	13.5%	13.6%	13.5%	13.6%	Better performance in 2012
Systems	10.3%	10.3%	10.3%	10.0%	10.3%	10.3%	10.3%	10.3%	Low volumes in 2012
Industrial	6.8%	7.5%	6.7%	7.7%	6.7%	7.3%	6.8%	7.3%	Improved management processes & restructured biz
Finance	0.0%	0.0%	0.0%	4.9%	2.0%	2.3%	4.0%	4.3%	Profitable in 2012
Segment Op. Margin	8.6%	8.8%	8.9%	9.2%	9.2%	9.4%	9.6%	9.7%	
Special Charges	-	0	-	0	-	-	-	-	
Corporate	(36)	(36)	(145)	(155)	(145)	(145)	(145)	(145)	Higher 1Q12 (due to share px) flows through 2012
Total Op. Margin	7.4%	7.7%	7.7%	8.0%	8.1%	8.3%	8.5%	8.6%	
Interest Expense	(36)	(38)	(139)	(145)	(121)	(117)	(109)	(100)	Lower 1Q12 flows through & expect 2013 retirement
Tax Rate	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	
EPS	\$0.44	\$0.46	\$1.88	\$1.98	\$2.15	\$2.24	\$2.40	\$2.50	Slightly better sales & better Bell & Industrial margin
Diluted Shares O/S	294.3	294.3	295.8	294.4	294.3	294.3	294.3	294.3	No material change

Sales % y/y	2Q12E		2012E		2013E		2014E	
	Old	New	Old	New	Old	New	Old	New
Net Sales	10.3%	13.0%	10.2%	11.8%	4.8%	4.5%	(20.8%)	(15.7%)
Cessna	16.3%	18.0%	14.4%	15.0%	6.9%	6.9%	6.2%	6.2%
Bell	17.8%	22.0%	19.5%	22.4%	7.9%	7.5%	5.1%	5.1%
Systems	(0.4%)	(6.6%)	(3.4%)	(7.8%)	(2.1%)	0.3%	(1.2%)	(1.8%)
Industrial	3.4%	6.6%	0.6%	3.4%	1.9%	2.0%	2.0%	2.3%
Finance	(6.9%)	84.8%	72.5%	136.9%	7.8%	(21.3%)	2.0%	1.8%

Source: Citi Investment Research and Analysis, Company Reports

Guidance

TXT maintained overall guidance, but Industrial & TFC appear poised to outperform based on a strong 1Q12, while Systems appears set to miss after a weak Q.

Figure 3. 2012 Guidance

	2010 Actual	2011 Actual	2012 Guidance		2012	
			4Q11 Low	High	1Q12 Low	High
Sales (\$M)	\$10,525	\$11,275	~\$12,500		unchanged	
Diluted EPS ex-Special Charges	\$0.81	\$0.79	\$1.80	\$2.00	unchanged	
Manufacturing CF (pre-pension)	\$759	\$1,000	\$700	\$750	unchanged	
By Segment						
Cessna Sales	\$2,563	\$2,990	~\$3,400		unchanged	\$3,437
Cessna Margins	(1.1%)	2.0%	3.5%	4.5%	unchanged	4.2%
Bell Sales	\$3,241	\$3,525	~\$4,200		unchanged	\$4,314
Bell Margins	13.2%	14.8%	13%	14%	unchanged	14.0%
Systems Sales	\$1,979	\$1,872	~\$1,900		unchanged	\$1,726
Systems Margins	11.6%	7.5%	9.5%	10.5%	unchanged	10.0%
Industrial Sales	\$2,524	\$2,785	~\$2,800		unchanged	\$2,880
Industrial Margins	6.4%	7.3%	6.5%	7.5%	unchanged	7.7%
Finance Sales	\$218	\$103	~\$200		unchanged	\$244
Finance Profit	(\$237)	(\$333)	breakeven		profitable	12

Source: Citi Investment Research and Analysis

Reviewing 1Q12

1Q12 EPS of \$0.41 beat estimates due to performance at Bell and a record quarter (margin-wise) from Industrial. Cessna visibility remains limited and defense sales were weak.

EPS of \$0.41 beat the Street (\$0.35) and Citi (\$0.30) due to stronger earnings at Bell Helicopter (7c) and Industrial (6c). Bell sales were up 33% y/y and commercial deliveries doubled y/y, and margins contracted q/q on the negative mix but still beat our estimates by 184 bps. Industrial volumes were up 7% y/y and turned in its best quarterly margins ever (9.7% beat our est. by 317 bps) driven by strong North American auto demand. After 4Q11's asset reclassification, TFC made money in 1Q12 for the first time since 3Q08, contributing 3c of the EPS beat. On the downside, Cessna lost money in 1Q12, missing our estimate of breakeven margins by 90 bps despite 23% y/y growth in deliveries. Plus, Cessna visibility remains limited as backlog was down to \$1.7b (down ~35% y/y), representing the segment's smallest backlog ever. Systems sales missed our est. by 13% and our earnings estimate by 21% (2c EPS headwind) due to a slower defense environment.

Figure 4. Estimate vs. Actual

\$ in Millions except EPS	1Q12			Comments on the Quarter	1Q11	
	Reported	Estimate	Var.		Reported	Y/Y
Segment Sales						
Cessna	\$669	\$632	6%	Higher deliveries & higher aftermarket	\$556	20%
Bell	994	909	9%	Commercial deliveries up 100% y/y	\$749	33%
Textron Systems	377	431	(13%)	Weak defense environment	\$445	(15%)
Industrial	755	719	5%	Better volumes across all businesses	703	7%
Finance	61	19	218%		26	135%
Total sales	\$2,856	\$2,710	5%		\$2,479	15%
Operating Margin						
Cessna	(0.9%)	0.0%	(90 bps)	Up y/y on higher volume	(6.8%)	594 bps
Bell	14.6%	12.8%	184 bps		12.1%	244 bps
Textron Systems	9.3%	10.3%	(97 bps)	Lower volumes	11.9%	(263 bps)
Industrial	9.7%	6.5%	317 bps	Higher volumes (best Q ever)	8.7%	99 bps
Finance	20%	0%	nm		(169.2%)	nm
Segment margin	9.1%	7.6%	144 bps		5.0%	411 bps
Special Charges	0.0%	0.0%	-		0.0%	-
Corporate	-1.6%	-1.3%	(31 bps)		-1.6%	(7 bps)
Total Operating Margin	7.4%	6.3%	113 bps		3.4%	403 bps
Operating Income						
Cessna	(6)	-	NA	(1c) vs. Citi	(38)	(84%)
Bell	145	116	25%	+7c vs. Citi	91	59%
Textron Systems	35	44	(21%)	(2c) vs. Citi	53	(34%)
Industrial	73	47	56%	+6c vs. Citi	61	20%
Finance	12	-	NA	+3c vs. Citi	(44)	(127%)
Segment Operating Income	\$259	\$207	25%	+12c vs. Citi	\$123	111%
Corporate & Other	(47)	(36)	30%	(2c) vs. Citi	(39)	21%
EBIT	\$212	\$171	24%		\$84	
Net Interest	(35)	(36)	(3%)	+1c vs. Citi	(38)	(8%)
Pre-tax income	177	134	32%		46	285%
Taxes	(57)	(43)	32%		(15)	
Effective tax rate	32.2%	32.0%	20 bps		32.6%	(41 bps)
Income from Cont Ops	120	\$91	31%		31	
Non-GAAP EPS (ex-Charges)	\$0.41	\$0.30	34%	Beat est. on Bell, Industrial, Finance	\$0.10	319%
Diluted shares outstanding	294.6	300.3	(2%)	+1c vs. Citi	319.1	(8%)

Source: Citi Investment Research and Analysis, Company Reports

Summary Models

Figure 5. Income Statement

\$ in Millions	2010	1Q11	2Q11	3Q11	4Q11	2011	1Q12	2Q12E	3Q12E	4Q12E	2012E	2013E	2014E
Revenue													
Cessna	\$2,563	\$556	\$652	\$771	\$1,011	\$2,990	\$669	\$769	\$892	\$1,107	\$3,437	\$3,675	\$3,902
Bell	3,241	749	872	894	1,010	3,525	994	1,064	1,085	1,172	4,314	4,637	4,873
Textron Systems	1,979	445	452	462	513	1,872	377	422	435	491	1,726	1,731	1,701
Industrial	2,524	703	719	655	708	2,785	755	766	663	696	2,880	2,936	3,004
Manufacturing Subtotal	10,307	\$2,453	\$2,695	\$2,782	\$3,242	11,172	\$2,795	\$3,021	\$3,075	\$3,466	12,357	12,979	13,478
Finance	218	26	33	32	12	103	61	61	61	61	244	192	195
Total Revenue	\$10,525	\$2,479	\$2,728	\$2,814	\$3,254	\$11,275	\$2,856	\$3,082	\$3,136	\$3,527	\$12,601	\$13,171	\$13,674
Q/Q Growth		(20.7%)	10.0%	3.2%	15.6%		(12.2%)	7.9%	1.7%	12.5%			
Y/Y Growth	0.2%	12.2%	0.7%	13.5%	4.1%	7.1%	15.2%	13.0%	11.4%	8.4%	11.8%	4.5%	3.8%
Operating Margins													
Cessna	-1.1%	-6.8%	0.8%	4.3%	5.9%	2.0%	-0.9%	3.0%	5.7%	7.0%	4.2%	5.6%	6.7%
Bell	13.2%	12.1%	13.8%	16.0%	16.5%	14.8%	14.6%	14.0%	13.8%	13.8%	14.0%	13.6%	13.6%
Textron Systems	11.6%	11.9%	10.8%	10.2%	-1.6%	7.5%	9.3%	10.3%	10.3%	10.3%	10.0%	10.3%	10.3%
Industrial	6.4%	8.7%	7.6%	5.6%	6.9%	7.3%	9.7%	7.5%	6.8%	6.8%	7.7%	7.3%	7.3%
Manufacturing Subtotal	7.7%	6.8%	8.5%	9.3%	8.3%	8.3%	8.8%	9.0%	9.4%	9.7%	9.3%	9.5%	9.8%
Finance	-108.7%	-169.2%	-100.0%	-75.0%	-193.3%	-323.3%	19.7%	0.0%	0.0%	0.0%	4.9%	2.3%	4.3%
Segment Operating Margin	5.3%	5.0%	7.2%	8.4%	1.1%	5.2%	9.1%	8.8%	9.2%	9.5%	9.2%	9.4%	9.7%
Special Charges	-1.8%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Corporate	-1.3%	-1.6%	-0.8%	-0.5%	-1.2%	-1.0%	-1.6%	-1.2%	-1.1%	-1.0%	-1.2%	-1.1%	-1.1%
Total Operating Margin	2.1%	3.4%	6.3%	7.9%	-0.1%	4.2%	7.4%	7.7%	8.1%	8.5%	8.0%	8.3%	8.6%
Operating Profit													
Cessna	(29)	(38)	5	33	60	60	(6)	23	50	77	145	207	260
Bell	427	91	120	143	167	521	145	149	150	162	605	630	665
Textron Systems	230	53	49	47	(8)	141	35	43	45	50	173	178	175
Industrial	162	61	55	37	49	202	73	57	45	47	222	213	218
Manufacturing Subtotal	790	167	229	260	268	924	247	273	289	337	1,146	1,228	1,318
Finance	(237)	(44)	(33)	(24)	(232)	(333)	12	-	-	-	12	4	8
Segment Operating Profit	\$553	\$123	\$196	\$236	\$36	\$591	\$259	\$273	\$289	\$337	\$1,158	\$1,232	\$1,326
Segment Operating Margin	5.3%	5.0%	7.2%	8.4%	1.1%	5.2%	9.1%	8.8%	9.2%	9.5%	9.2%	9.4%	9.7%
Special Charges/One-timers	(190)	-	-	-	-	-	-	-	-	-	-	-	-
Corporate & Other	(137)	(39)	(23)	(13)	(39)	(114)	(47)	(36)	(36)	(36)	(155)	(145)	(145)
Total Operating Profit	\$226	\$84	\$173	\$223	(3)	\$477	\$212	\$237	\$253	\$301	\$1,003	\$1,087	\$1,181
Net Interest Expense	(140)	(38)	(38)	(37)	(27)	(140)	(35)	(38)	(37)	(36)	(145)	(117)	(100)
Pre-Tax Income	\$86	\$46	\$135	\$186	(30)	\$337	\$177	\$199	\$217	\$265	\$857	\$970	\$1,081
Income Taxes	6	(15)	(43)	(50)	13	(95)	(57)	(64)	(69)	(85)	(275)	(310)	(346)
Effective Tax Rate	-7.0%	32.6%	31.9%	26.9%	43.3%	28.2%	32.2%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%
Net Income (Cont. Ops)	\$92	\$31	\$92	\$136	(17)	\$242	\$120	\$135	\$147	\$180	\$583	\$660	\$735
Net margin	0.9%	1.3%	3.4%	4.8%	(0.5%)	2.1%	4.2%	4.4%	4.7%	5.1%	4.6%	5.0%	5.4%
EPS (Cont.Ops) ex Charges (Non-GAAP)	\$0.81	\$0.10	\$0.29	\$0.45	\$(0.06)	\$0.79	\$0.41	\$0.46	\$0.50	\$0.61	\$1.98	\$2.24	\$2.50
Average Diluted Shares	302.6	319.1	315.2	300.9	292.5	307.3	294.6	294.3	294.3	294.3	294.4	294.3	294.3

Source: Citi Investment Research and Analysis, Company Reports

Figure 6. Balance Sheet

\$ in Millions	2010	1Q11	2Q11	3Q11	4Q11	2011	1Q12	2Q12E	3Q12E	4Q12E	2012E	2013E	2014E
Manufacturing Cash	898	986	610	1,517	871	871	628	712	1,021	1,568	1,568	2,011	3,031
Accounts receivable, net	892	910	874	927	856	856	937	1,013	962	1,044	1,044	1,100	1,139
Inventory	2,277	2,453	2,562	2,607	2,402	2,402	2,593	2,802	2,788	2,612	2,612	2,753	2,852
Other Current Assets	980	1,050	1,395	1,094	1,134	1,134	1,032	1,059	1,065	1,110	1,110	1,135	1,156
Property, Plant and Equipment	1,932	1,950	1,964	1,957	1,996	1,996	2,003	2,038	2,073	2,108	2,108	2,138	2,168
Other Assets	3,354	3,302	3,343	3,329	3,143	3,143	3,141	3,181	3,190	3,254	3,254	3,292	3,322
Total Manufacturing Assets	\$10,333	\$10,651	\$10,748	\$11,431	\$10,402	\$10,402	\$10,334	\$10,806	\$11,099	\$11,696	\$11,696	\$12,429	\$13,668
Total Finance Assets	\$4,949	\$4,408	\$4,091	\$3,850	\$3,213	\$3,213	\$2,946	\$2,737	\$2,528	\$2,320	\$2,320	\$1,671	\$1,078
Total Assets	\$15,282	\$15,059	\$14,839	\$15,281	\$13,615	\$13,615	\$13,280	\$13,543	\$13,628	\$14,016	\$14,016	\$14,101	\$14,745
Current portion of debt	19	216	351	589	146	146	464	464	464	464	464	-	-
Other Current Liabilities	2,638	2,577	2,657	2,762	2,785	2,785	2,707	2,870	2,898	3,098	3,098	3,182	3,260
Other Liabilities	2,993	2,986	2,865	2,808	2,826	2,826	2,657	2,727	2,743	2,857	2,857	2,923	2,976
Long-term debt, net	2,283	2,333	2,192	2,473	2,313	2,313	2,013	2,013	2,013	2,013	2,013	2,013	2,013
Total Manufacturing Liabilities	\$7,933	\$8,112	\$8,065	\$8,632	\$8,070	\$8,070	\$7,841	\$8,075	\$8,118	\$8,432	\$8,432	\$8,119	\$8,248
Total Finance Liabilities	\$4,377	\$3,895	\$3,600	\$3,337	\$2,800	\$2,800	\$2,524	\$2,424	\$2,324	\$2,224	\$2,224	\$1,986	\$1,789
Total Liabilities	\$12,310	\$12,007	\$11,665	\$11,969	\$10,870	\$10,870	\$10,365	\$10,499	\$10,442	\$10,656	\$10,656	\$10,105	\$10,037
Shareholder's equity	\$2,972	\$3,052	\$3,174	\$3,312	\$2,745	\$2,745	\$2,915	\$3,044	\$3,186	\$3,360	\$3,360	\$3,996	\$4,708
Total Liabilities & Shareholder Equity	\$15,282	\$15,059	\$14,839	\$15,281	\$13,615	\$13,615	\$13,280	\$13,543	\$13,628	\$14,016	\$14,016	\$14,101	\$14,745

Source: Citi Investment Research and Analysis, Company Reports

Figure 7. Manufacturing Cash Flow Statement

\$ in Millions	2010	1Q11	2Q11	3Q11	4Q11	2011	1Q12	2Q12E	3Q12E	4Q12E	2012E	2013E	2014E
Income (loss) from Cont Ops	\$320	\$62	\$113	\$155	\$134	\$464	\$110	\$185	\$197	\$229	\$721	\$835	\$896
Dividends received from TFC	505	130	49	-	-	179	240	20	-	-	260	-	-
Capital contributions paid to TFC	(383)	(63)	(49)	(40)	(30)	(182)	(240)	(20)	-	-	(260)	-	-
Depreciation & Amortization	362	87	93	87	104	371	84	91	91	91	357	430	430
Changes in WC	(44)	(243)	5	140	152	54	(275)	(150)	87	250	(87)	(139)	(82)
Changes in Other Assets/Liabs/non-cas	(30)	100	(138)	31	(118)	(125)	(96)	30	7	49	(9)	29	23
Manufacturing Operating CF	730	73	73	373	242	761	(177)	157	382	619	982	1,155	1,267
CapEx	(270)	(78)	(91)	(102)	(152)	(423)	(73)	(126)	(126)	(126)	(451)	(460)	(460)
Acquisitions	(57)	-	(3)	-	(11)	(14)	-	-	-	-	-	-	-
Other Investing, net	(26)	(43)	4	12	41	14	-	-	-	-	-	-	-
Manufacturing Investing CF	(353)	(121)	(90)	(90)	(122)	(423)	(73)	(126)	(126)	(126)	(451)	(460)	(460)
L-T debt & Line of Credit	(1,297)	(7)	-	496	(16)	473	-	-	-	-	-	-	-
Net intergroup borrowings	98	(60)	(335)	120	100	(175)	-	50	50	50	150	200	200
S-T Debt	-	203	(14)	38	(227)	-	-	-	-	-	-	(464)	-
Stock & warrant issuance	-	3	-	-	-	3	-	-	-	-	-	-	-
Option Exercises	6	-	-	-	-	-	-	-	-	-	-	-	-
Cash Dividends	(22)	(5)	(6)	(6)	(5)	(22)	(5)	(6)	(6)	(6)	(23)	(24)	(24)
Other	-	(5)	(5)	(17)	(612)	(639)	9	9	9	9	36	36	36
Manufacturing Financing CF	(1,215)	129	(360)	631	(760)	(360)	4	53	53	53	163	(252)	212
Manufacturing Total CF from Cont Ops	(838)	81	(377)	914	(640)	(22)	(246)	84	309	546	694	443	1,020
Total CF from Disco Ops	(9)	(1)	(1)	(1)	(2)	(5)	(1)	-	-	-	(1)	-	-
Exchange Rate Effects	(3)	8	2	(6)	(4)	-	4	-	-	-	4	-	-
Manufacturing Net Change in Cash	(850)	88	(376)	907	(646)	(27)	(243)	84	309	546	697	443	1,020
Manufacturing Beg Cash Balance	1,748	898	986	610	1,517	898	871	628	712	1,021	871	1,568	2,011
Manufacturing Ending Cash Balance	\$898	\$986	\$610	\$1,517	\$871	\$871	\$628	\$712	\$1,021	\$1,568	\$1,568	\$2,011	\$3,031

Source: Citi Investment Research and Analysis, Company Reports

Textron Inc.

Company description

Headquartered in Providence, Rhode Island, Textron (TXT) is a diversified manufacturer of a variety of industrial goods. Once a far-flung conglomerate, the company has streamlined into five operating segments: Cessna (business jets), Bell (helicopters), Textron Systems (UAVs, armored security vehicles, precision weapons), Industrial (automotive parts, golf carts, turf-care, tools), and Finance. The Finance segment has been in wind-down mode since December 2008, when the company decided to exit all lines of financing business not associated with sales of Textron-made products (bizjets & golf carts). The company generated \$11.3b in sales in 2011 with 4.2% operating margins.

Investment strategy

We rate shares of TXT as Neutral given our concerns about the pace of recovery at Cessna and the potential that consensus estimates will head lower for 2012 and 2013 over the next several months. In our view, current valuation level is appropriate in light of the uncertainty facing the company, including a rebound in the small-cabin business jet market and broader macroeconomic weakness impacting the company's industrial businesses.

Valuation

In our view, a sum-of-the-parts methodology is appropriate at this time given the varying stages of recovery at each of the company's businesses, and it should give investors a better sense of break-up value. We apply a target multiple of 12.8x FTM PE to Cessna, representing a discount to our target commercial multiple of 15x given the low margins and pressured outlook in the SMID cabin bizjet business. Our Bell target multiple of 11.4x is a blend of military (70%) and commercial (30%). Our Systems multiple is 9.1x multiple, representing a 30% discount to the market (13x), in line with where we believe a ground-exposed defense business should trade. For the company's finance business, we use a 7.5x multiple given the valuation levels of a broad selection of financial companies. The resulting blended multiple of 11.6x yields our \$27 PT when applied to our FTM EPS estimate twelve months from now.

Risks

Strong brand recognition and relatively broad end-market exposure are offset by limited end-market visibility (i.e. bizjets) and risks associated with other elements of the portfolio (i.e. finance and end-market industrial demand). Aviation and helicopter sales could experience further weakness based on economic pressure and increased competition. And in our view, Cessna's small-cabin bizjets are still relatively out-of-favor given macro uncertainty. The finance segment may also be volatile due to broader market gyrations impacting valuation and liquidation pace, despite the segment being in wind-down mode. Meanwhile, US Government spending (31% of revenues) is under increasing fiscal pressure which could result in program cancellations or delays, including the V-22 Osprey. As war op tempo slows, war budgets may also move away from TXT. Meanwhile, there is headline risk associated with Systems' Sensor Fuzed Weapon, which some consider a banned cluster munition.

We would become more negative if op tempo decreased faster than anticipated, the bizjet recovery was delayed beyond 2012, or commercial demand for new aircraft

was slower to materialize than expected. We would become more positive if the small-cabin market improved faster than expected and if evidence emerged of Bell's ability to recapture commercial market share. If the impact on the company from any of these factors proves to be greater than we anticipate in either direction, the stock will likely have difficulty achieving our target price.

Appendix A-1

Analyst Certification

The research analyst(s) primarily responsible for the preparation and content of this research report are named in bold text in the author block at the front of the product except for those sections where an analyst's name appears in bold alongside content which is attributable to that analyst. Each of these analyst(s) certify, with respect to the section(s) of the report for which they are responsible, that the views expressed therein accurately reflect their personal views about each issuer and security referenced and were prepared in an independent manner, including with respect to Citigroup Global Markets Inc and its affiliates. No part of the research analyst's compensation was, is, or will be, directly or indirectly, related to the specific recommendation(s) or view(s) expressed by that research analyst in this report.

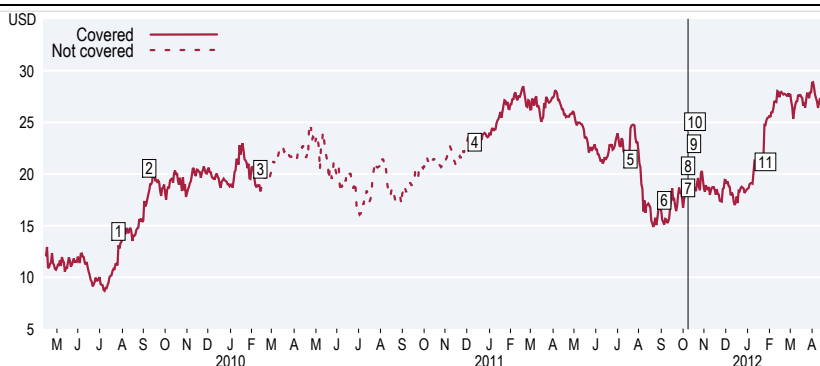
IMPORTANT DISCLOSURES

Textron Inc. (TXT)

Ratings and Target Price History Fundamental Research

Analyst: Jason Gursky

Covered since December 13 2010



	Date	Rating	Target Price	Closing Price
1	28-Jul-09	2H	*15.00	13.11
2	9-Sep-09	2H	*20.00	18.41
3	12-Feb-10	Coverage terminated		
4	13-Dec-10	2H	*26.00	23.66

* Indicates change

	Date	Rating	Target Price	Closing Price
5	20-Jul-11	2H	*28.00	24.43
6	6-Sep-11	2H	*18.50	15.11
7	8-Oct-11	Stock rating system changed		
8	8-Oct-11	*2	18.50	18.34

	Date	Rating	Target Price	Closing Price
9	18-Oct-11	2	*18.70	18.66
10	19-Oct-11	2	*21.00	18.59
11	26-Jan-12	2	*25.00	24.74

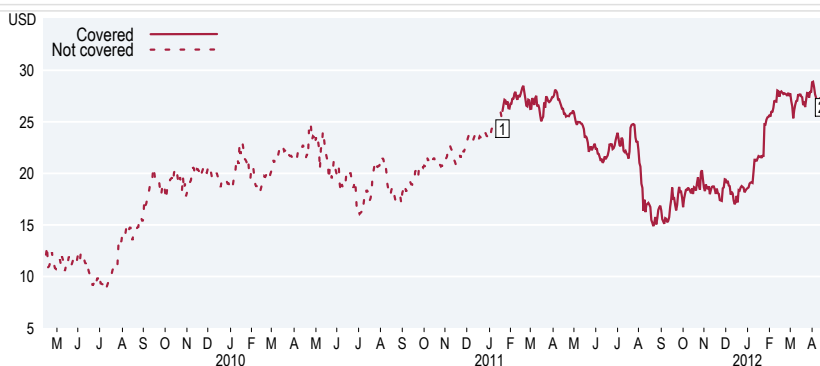
Rating/target price changes above reflect Eastern Standard Time

Textron Inc. (TXT)

Ratings and Target Price History Best Ideas Research Relative Call (3 Month)

Analyst: Jason Gursky

Covered since December 13 2010



	Date	Rating	Target Price	Closing Price
1	20-Jan-11	*ADD LP	-	26.05

* Indicates change

	Date	Rating	Target Price	Closing Price
2	16-Apr-12	*REM LP	-	26.85

Rating/target price changes above reflect Eastern Standard Time

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Data current as of 31 Mar 2012	12 Month Rating			Relative Rating		
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% of companies in each rating category that are investment banking clients	44%	42%	40%	47%	42%	43%

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Jason Gursky; Jonathan Raviv

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