Siena Market Line
3rd week of February 2016

Dril-Quip, Inc.

NYSE: DRQ

Analyst: Senan Lonergan
Sector: Energy

SELL

Price Target: $46.37

Key Statistics as of 2/17/2016

Market Price:	$53.38
Industry:	Oil/Gas Drilling and Exploration
Market Cap:	$2.05B
52-Week Range:	$48.88 - $81.78
Beta:	0.21

Thesis Points:

- Recent oil supply freezes will significantly impact revenue growth
- Market is optimistic about oil futures and is overvaluing DRQ
- Recent jump in stock price presents an ideal entry point

Company Description:

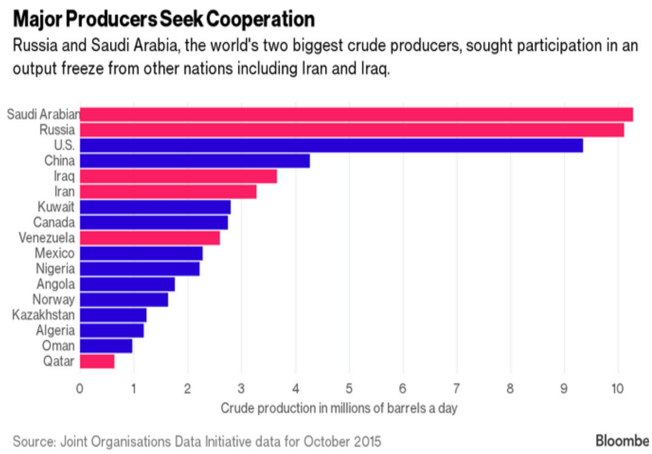
Dril-Quip, Inc., together with its subsidiaries, designs, manufactures, sells, and services engineered offshore drilling and production equipment for use in deep-water, harsh environment, and severe service applications worldwide. The company operates through three segments: Western Hemisphere, Eastern Hemisphere, and Asia-Pacific. Its principal products comprise subsea and surface wellheads, subsea and surface production trees, subsea control systems and manifolds, mudline hanger systems, specialty connectors and associated pipe, drilling and production riser systems, liner hangers, wellhead connectors, and diverters. The company also provides technical advisory services, and rework and reconditioning services, as well as rental of running tools for use in the installation and retrieval of its products. Its products are used for drilling and production of oil and gas wells on offshore platforms; tension leg platforms, which are floating production platforms connected to the ocean floor via vertical mooring tethers; Spars, a floating cylindrical structure; and floating production, storage, and offloading monohull moored vessels, as well as to explore for oil and gas from offshore drilling rigs, such as floating rigs and jack-up rigs. The company sells its products directly through its sales personnel, independent sales agents, and representatives to integrated, independent, and foreign national oil and gas companies, as well as offshore drilling contractors, and engineering and construction companies. Dril-Quip, Inc. was founded in 1981 and is headquartered in Houston, Texas.

Thesis

The macro environment and the overvaluation by the market provide investors with an opportunity to profit from a short sell of DRQ. With oil prices seemingly to have bottomed, the upcoming years do not present an optimal environment for DRQ. The company relies on the demand of its offshore drilling equipment, as well as its service and maintenance. The combination of oil prices hovering $30 a barrel and the significant decline in drilling for 2016, will decline revenue growth by 25%. Furthermore, the recent jump in oil prices have carried DRQ's stock price by nearly 6%. While DRQ is prone to moving with sudden changes in oil prices, a stable low price will expose the company and allow its stock price to fall. Ultimately, the current $53.38 a share provides an optimal entry point for a short sell.

Industry Outlook

On 2/16/2016, Iran agreed to join Saudi Arabia, Russia, Qatar, Venezuela, and other OPEC members in capping their supply to stabilize global oil markets. The collaboration of OPEC, the organization that controls more than 80% of the world's oil, and Russia, the world's second biggest crude producer, will ultimately halt the decline of crude prices. However, capping the supply does not mean an increase in oil prices. With global production reaching the greatest barrels per day since 2008, the markets will have a surplus for years to come. Although oil has increased to over $30 this week, analysts do not expect a significant incline for some time. U.S. companies have been decreasing production since April 2015, and still there is an incredible surplus. The energy sector, particularly companies with high D/E ratios, will continue to lag, and equipment and services providers, such as Dril-Quip, will have declining revenue growth.



Business Model

The company has a very strong global presence, as well as a wide range of customers and competitors. While the Company is not dependent on any one customer or group of customers, the loss of one or more of its significant customers could, at least on a short-term basis, have an adverse effect on the company's results of operations. Approximately 54% of Dril-Quip's business comes from the U.S., Mexico, and Canada, while the remainder comes from OPEC and other Eastern hemisphere companies. The company's principal customers are major integrated, large independent and foreign national oil and gas companies. Offshore drilling contractors and engineering and construction companies also represent a minor customer base. DRQ's customers are generally oil and gas companies that are well-known participants in offshore exploration and production such as Exxon Mobile, Chevron, Shell, BP, Hess and many others. Furthermore, Dril-Quip faces significant competition from other manufacturers and suppliers of exploration and production equipment. Several of its primary competitors are diversified multinational companies such as AkerSolutions, FMC Technologies, OneSubsea, and GE Oil and Gas. While DRQ does hold a significant market share for subsea drilling equipment sales, the overall microenvironment continues to hurt their customers, and consequently, hinder the company's growth.

People

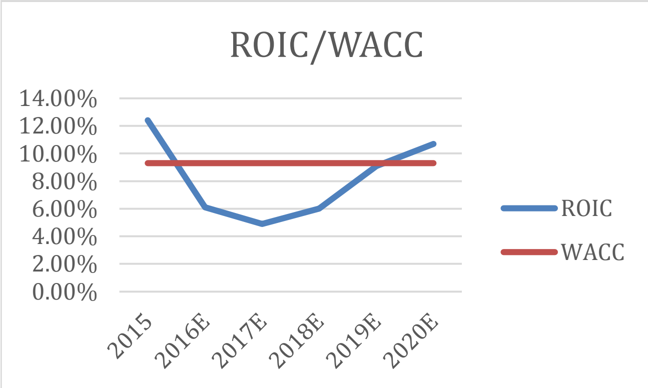
While DRQ has been given a short sell recommendation, it is not at the fault of management. The company is managed by a professional team of individuals, all of whom have considerable experience in their field. Blake T. DeBerry was appointed President and Chief Executive Officer in October 2011, prior to which he was Senior Vice President – Sales and Engineering. James A. Gariepy was appointed Senior Vice President and Chief Operating Officer in October 2011 as well. Jerry M. Brooks, Vice President of Finance and Chief Financial Officer, has been Chief Financial Officer since March 1999. Lastly, James C. Webster, Vice President of General Counsel and Secretary, joined the Company in February 2011.

Product Differentiation

FY 2014 demonstrates that over 83% of DRQ's sales come from drilling equipment, while the remainder is attributed to service. Their product line includes 17 internally developed products in which they are all vertically integrated into manufacturing operations. The company has very reliable subsea control systems, as well as 19 floating production platforms worldwide. Moreover, DRQ has been recognized on several cases for innovation in their industry. They were the first company to perform a full-scale system level validation test on a Subsea Wellhead System, and also the first to fully implement Advanced Product Quality Planning (APQP). However, while DRQ is diversified in location, their focus on drilling equipment and services specifically makes them very susceptible to oil prices.

Financials

From 2010 until 2014, Dril-Quip grew substantially. With U.S. and global customers drilling at an exceptionally high rate, DRQ's revenue grew by nearly 65%. In addition, as a result of sufficient management, operating costs were able to remain relatively stable. As a result, the company's EBITDA grew by just under 82%. However, the slowdown in drilling has severely impacted DRQ; revenue fell by 1% and EBITDA by 5%. Estimates for 2016-2019 are pessimistic and WAAC is expected to far exceed ROIC in the following years. The company will survive the market conditions, as it has nearly a 0 D/E, but the next 2-3 years are expected to be turbulent and each year will eat away at its value. Further research demonstrates that the main driver for a decline in the stock price is accredited to revenue and operating cost changes. Operating costs/revenue are expected to remain relatively stable, around 72%, but revenue will decline. A sensitivity analysis shows that 74.9% of stock price changes is attributed to revenue by operations. For FY2016, revenue is expected to decrease by 25%, followed by another 16% decrease in 2017.



Conclusion

In conclusion, DRQ is recommended as a short-sell for reasons largely attributed to macro-environment factors. With oil prices to seemingly have bottomed, the company's revenue is expected to decrease by 25% in 2016. With WAAC far exceeding ROIC, DRQ's stock price will decrease, presenting short selling investors with an opportunity to profit. The very recent rise in oil prices has brought up DRQ by nearly 6% this week- an ideal entry point for a short. An intrinsic value target price, based off of invested capital, is set at $46.37.

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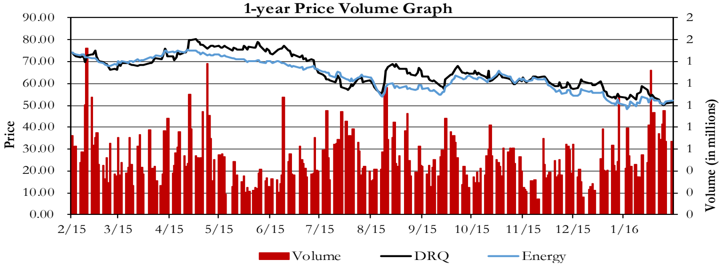
3rd week of February 2016

Dril-Quip, Inc. (DRQ) — CENTER FOR GLOBAL FINANCIAL STUDIES — BEARISH

Analysis by P.C. Principal	**Current Price:**	$53.38	**Intrinsic Value**	$8.27	**Target 1 year Return: -80.82%**
2/21/2016	**Divident Yield:**	0.0%	**Target Price**	$10.24	**Probability of Price Increase: 0%**

1-year Price Volume Graph



Description

Dril-Quip, Inc., together with its subsidiaries, designs, manufactures, sells, and services engineered offshore drilling and production equipment for use in deepwater, harsh environment, and severe service applications worldwide.

General Information

Sector	Energy
Industry	Energy Equipment and Services
Last Guidance	November 3, 2015
Next earnings date	February 27, 2016
Estimated Country Risk Premium	7.28%
Effective Tax rate	34%
Effective Operating Tax rate	35%

Market Data

Market Capitalization	$2,047.43
Daily volume (mil)	0.61
Shares outstanding (mil)	38.36
Diluted shares outstanding (mil)	38.95
% shares held by institutions	64%
% shares held by investments Managers	100%
% shares held by hedge funds	3%
% shares held by insiders	0.49%
Short interest	4.53%
Days to cover short interest	3.47
52 week high	$81.78
52-week low	$48.88
Levered Beta	0.88
Volatility	33.85%

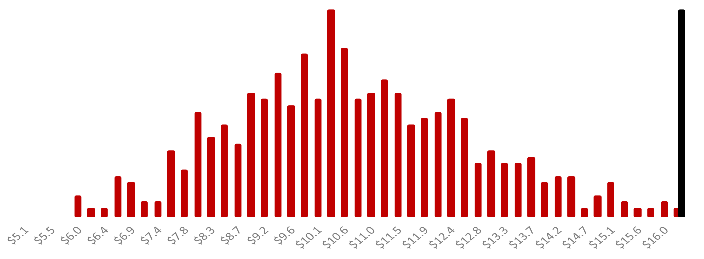
Past Earning Surprises

Quarter ending	Revenue	EBITDA
9/30/2014	0.76%	4.35%
12/31/2014	3.00%	10.47%
3/31/2015	1.61%	17.63%
6/30/2015	-3.67%	-14.36%
9/30/2015	-4.48%	7.02%
Mean	-0.56%	5.02%
Standard error	1.5%	5.3%

Peers

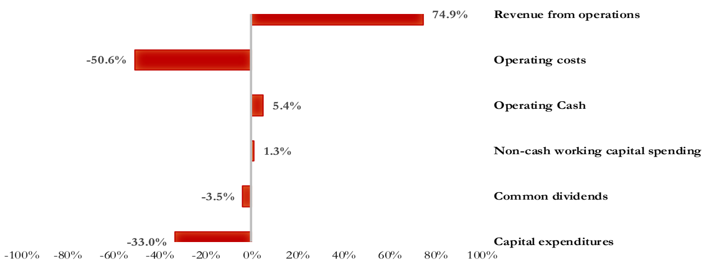
- Forum Energy Technologies, Inc.
- Oil States International Inc.
- FMC Technologies, Inc.
- Newpark Resources Inc.
- Superior Energy Services, Inc.
- RPC Inc.
- Helix Energy Solutions Group, Inc.
- TETRA Technologies, Inc.

Target Price Distribution--Prob(Price Increase)= 0%



Management	Position	Total compensations growth	Total return to shareholders
DeBerry, Blake	Chief Executive Officer, Pre	18.01% per annum over 3y	4.39% per annum over 3y
Brooks, Jerry	Chief Financial Officer, Pri	23.49% per annum over 5y	5.94% per annum over 5y
Gariepy, James	Chief Operating Officer and	16.5% per annum over 3y	4.39% per annum over 3y
Webster, James	Vice President, General Coun	13.29% per annum over 3y	4.39% per annum over 3y
	0 0	N/M	N/M
	0 0	N/M	N/M

Sensitivity Analysis



Profitability	DRQ (LTM)	DRQ (5 years historical average)	Industry (LTM)
ROIC	12.4%	14.64%	6.17%
NOPAT Margin	21%	22.76%	11.3%
Revenue/Invested Capital	0.59	0.64	0.55
ROE	12.5%	14.77%	9.14%
Adjusted net margin	21%	22.73%	9.9%
Revenue/Adjusted Book Value	0.59	0.65	0.92
Invested Funds	**DRQ (LTM)**	**DRQ (5 years historical average)**	**Industry (LTM)**
Total Cash/Total Capital	24.6%	23.3%	17%
Estimated Operating Cash/Total Capital	22.2%	21.5%	N/A
Non-cash working capital/Total Capital	38.4%	37.9%	13%
Invested Capital/Total Capital	97.6%	98.1%	82%
Capital Structure	**DRQ (LTM)**	**DRQ (5 years historical average)**	**Industry (LTM)**
Total Debt/Common Equity (LTM)	0.02	0.01	0.86
Cost of Existing Debt	1.25%	1.29%	4.12%
Estimated Cost of new Borrowing	1.16%	1.16%	4.12%
CGFS Risk Rating	AAA	AAA	B
Unlevered Beta (LTM)	0.87	1.58	1.02
WACC	9.32%	14.66%	9.42%

Valuation

Period	Revenue growth	ROIC/WACC	Invested Capital	Net Claims	Price per share
Base Year			$931.39	$9.32	$44.63
9/30/2016	-25.0%	0.66	$1,040.59	-$433.39	$49.15
9/30/2017	-16.0%	0.53	$1,286.52	-$684.20	$52.70
9/30/2018	1.0%	0.64	$1,453.39	-$770.66	$56.03
9/30/2019	10.0%	0.98	$1,525.26	-$805.51	$59.55
9/30/2020	12.5%	1.15	$1,575.60	-$832.21	$63.55
9/30/2021	10.9%	1.25	$1,243.40	-$882.31	$68.08
9/30/2022	9.3%	1.28	$1,054.87	-$954.56	$72.97
9/30/2023	7.7%	1.27	$1,033.68	-$1,048.42	$78.10
9/30/2024	6.2%	1.25	$1,098.46	-$1,164.57	$83.38
9/30/2025	4.6%	1.22	$1,205.07	-$1,303.83	$88.74
Continuing Period	3.0%	1.20			