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April 13, 2018

# Tutor Perini: (TPC)

**Emilien MARY**

**Sector: Materials**
**Industry: Construction**
**Current Price: $21.60**
**Target Price: $31.80**

**Company Description: Tutor Perini Corporation and its subsidiaries provide general contracting, construction management and design-build services to private clients and public agencies throughout the United States and selected overseas areas.**

## BUY

| | |
|---|---|
| Current Price: | $21.60 |
| Target Price: | $31.80 |
| Market Cap: | 1,070.5M |
| Beta: | 1.61 |

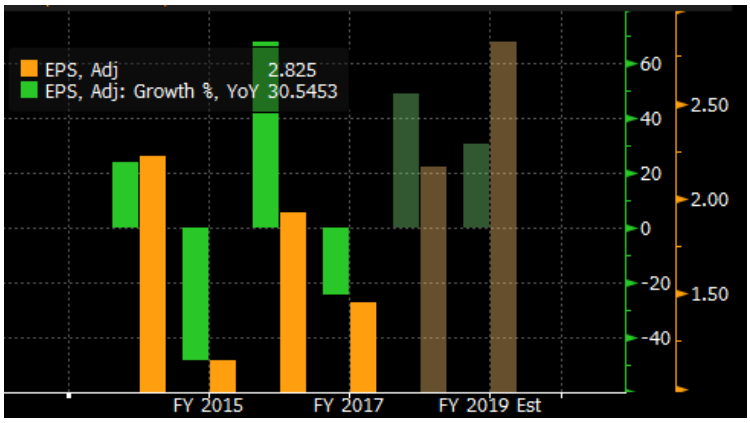
ROIC: 5.89%
Gross Profit margin: 9.6%
EBITDA margin: 4.9%
NI margin: 3.1%
Backlog yoy: 16.96%
Debt/Com Eq: 43%

**Catalysts:** Forward looking projections that call for positive/negative outlook that will strengthen your thesis. Example:

- Short Term(within the year): Ability to take profitable investment
- Mid Term(1-2 years): Demand for Civil projects
- Long Term(3+): US market is stimulate by the Trump's government fiscal policy and the requirement of maintenance of infrastructures

**Thesis:** Tutor Perini Corporation is concentrating its revenue on a new segment with 6.5 to 7.5 higher margin compared to previous years. This segment, civil construction, is a secured way to improve significantly the financial health of the company. It is strengthen by the recent earning performance and by the long-term revenue upside which at it records.

## Earnings Performance:




The company earnings has lowered by 24.5% in 2017 compared to the previous year. However, EPS is expected to increase by 45% in 2018 and by 30% in 2019. This significant increase in earnings are due to the significance increase of 54% yoy in civil segment backlog growth, a significant indicator of performance in this industry.

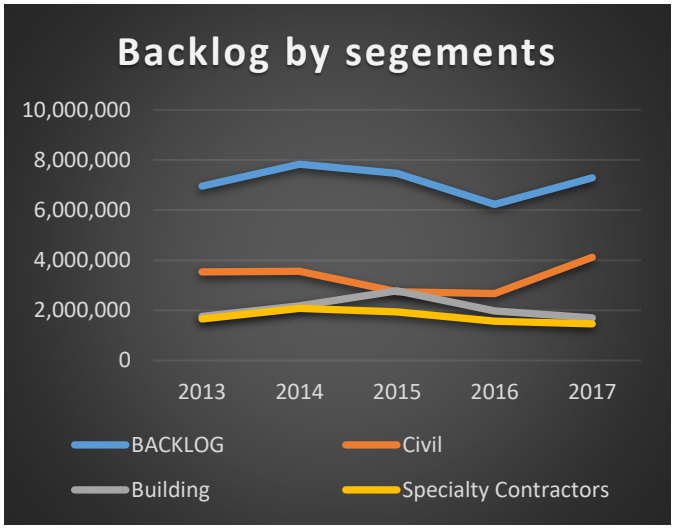
This backlog impact on the company performance is even more significant due to the TPC's highest margin segment with a 12.0% operating margin while Building segment and Specialty Contractors segments stand at 1.8% and 1.6% of operating margin, respectively.

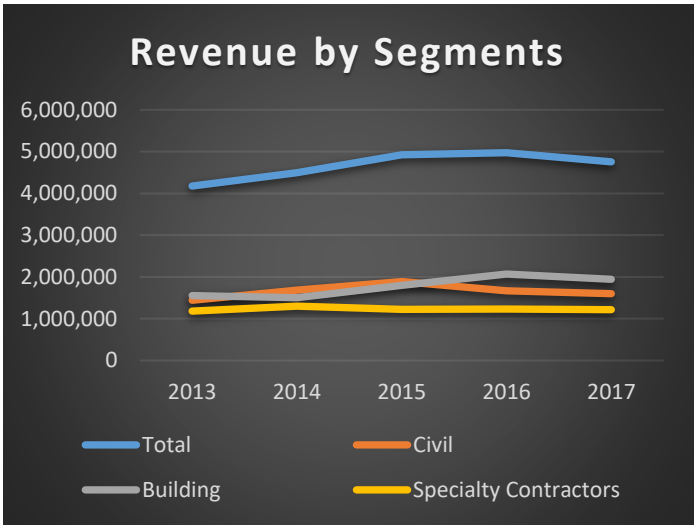
Earnings performance went down mainly due to the decrease of 4.3% in revenue, adj. to $4,757.2M compared to a revenue of $4,973.1M in 2016. As a result, Net Income decrease from $96.1M to $74.0M during the same period and income margin decrease by 30bps to 1.6%.

However, the Cash flow from operations has significantly increased by 44.4% between 2016 and 2017 from $113.3M to $163.6M mainly due to the tax benefit of the Trump's tax cut.

## Long-term Revenue Upside:

While revenue has decreased for the first year since 2010, long-term revenue upside is strengthen by the recent backlog records of $4.1 billion the company has recently provide for the Civil segment, the highest margin division for Tutor Perini company. As a result, backlog increased for the first time since 2014 at $7.3 billion. The impact of this backlog is generally seen on the total revenue after one or two years.




The government transportation spending has been decreasing under Obama's administration to $82.7 billion in 2016 from $86.0 billion in 2013 (source: federal-budget.insidegov.com). As a result, the gap between the requirement fund needed for surface transportations and the fund allocated has significantly increased to 1.1 trillion dollars needed for the period 2016-2025 (source: ASCE). This underinvestment leads to additional cost of maintenance such as more frequent inspection on aging infrastructure.

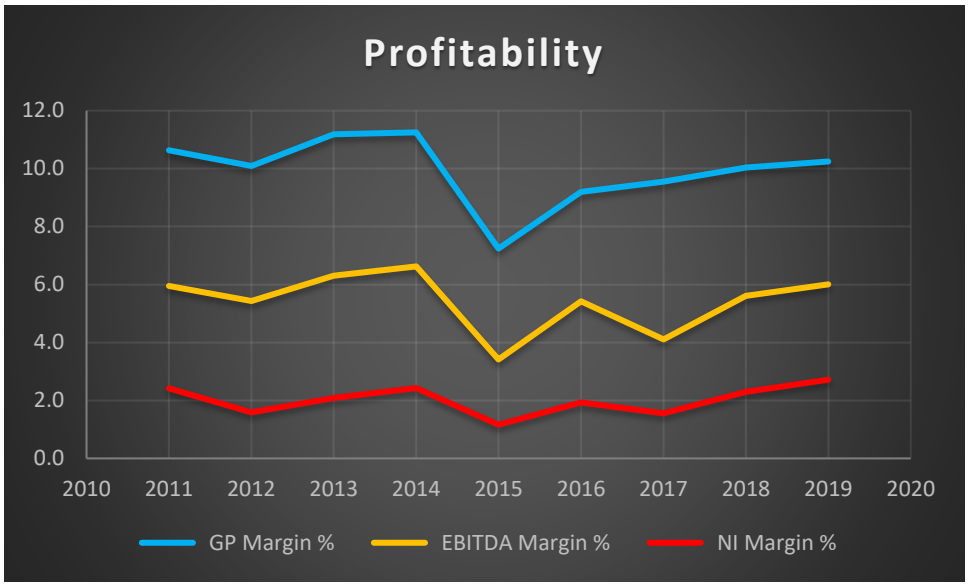
However, the first year of the Trump's government has marked a turning point in the industry. This emphasis the logic of the trump's government policy to increase the transportation spending with an increase of 6.65% in 2017 to $88.2 billion and to prepare an infrastructure bill around $1.1/1.7 trillion, a cash cow for this industry if the bill is approved. The materials industry is now able to see a bright future, one of the first time since the crisis, a decade ago.

And this industry growth has already started. The Fast Act, Fixing Americas Surface Transportation Act, is the first long-term transportation funding bill signed by the government for a decades. It will provide long-term contract with funding of $305 billion between 2016 and 2020. Public and private bridge spending is forecast to increase from $149.7 billion to $167.2 billion.

In addition, States have taken measure to increase future spending in transportation and infrastructure and this result are planned to impact the market in the coming years. In 2017, Texas approved two laws that increased transportation from $4.0 to $4.5 billion annually. In 2016, Utah approved a gas tax increase of five cents/gallon that should result in an increase of over $75 to $85 million in additional spending. In addition, the state of Utah also approved in 2017 a $1 billion bond package for infrastructure improvements. In California, the states approved in 2016 a $3 billion bill a year for local road, bridge and transit projects.

All these law approvals are long-term opportunities for the infrastructure market and Tutor Perini Corporation and they will drive the long-term growth to the business over time.

## Margin Upside:




The recent increase of the backlog should climb NI margin by a significant way. Because the civil segment contribute to the highest margin of the firm, the backlog record in this segment should contribute to increase the margin by a significant way as the margin is 6.5 to 7.5 time higher compare to the other segment of the firm. In addition, the company has a better controlling cost especially due to a better bidding activity and bid pipeline over the last years. Gross profit margin is forecasted to increase by 40 bps in 2018 and 30 bps in 2019 to 10.3%. EBITDA margin is forecasted to increase by 190 bps over the next 2 years leading to an increase of the NI margin by 120bps, a record since 2011.

Moreover, the vertical integration of the company through civil, building and specialty service capabilities provide a competitive advantage for Tutor Perini Corporation. The greater control over the schedule and the greater visibility into price bring to the company a better collaborative bidding approach, making project more profitable and leading the margin up.

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## Financial Improvement:

The finance health of the company is forecasted to increase. The unprecedented civil project bidding activity and pipeline of prospective projects reflect an increase in the demand of the most profitable division of the company. As a result, the revenue and income provided by civil project should increase at faster rate than its other division, leading to a better profitability of Tutor Perini Corporation.

In addition, the performance of the company's cash flow could lead the company to take advantage on other more profitable projects. In 2017, free cash flow stand at $133.3M, the highest since 2007 since 2007. Tutor Perini Corporation plan to increase its capital expenditure to $50M in 2018, to strengthen its leading position in the industry and catch the new opportunities provided by the increase in demand of civil projects.

Since 2015, ROIC has increased by a stunning 2.43 times from 2.41 to 5.89. This significant increase show the company efficiency to use their capital under more profitable investment.

## Competitors Comparison:

| Name (BICS Best Fit) | Mkt Cap (USD) | Last Px | Rev - 1 Yr Gr:Y | WACC Ratio | P/E | ROIC LF | Grs Mrgn Adj:Y | OPM:Y | EBITDA Mrgn Adj:Y | NI Mrgn Adj:Y | ROIC LF |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Median | 2.40B | 30.94 | 14.76% | 0.61 | 17.96 | 9.74% | 9.55% | 4.06% | 6.84% | 3.01% | 9.74% |
| TUTOR PERINI COR | 1.08B | 21.60 | -4.34% | 0.56 | 14.89 | 5.95% | 9.55% | 3.02% | 4.11% | 1.56% | 5.95% |
| FLUOR CORP | 8.10B | 57.92 | 2.54% | 0.48 | 19.90 | 5.35% | 3.17% | 3.52% | 4.67% | 2.04% | 5.35% |
| PRIMORIS SERVICE | 1.36B | 26.34 | 19.18% | 0.99 | 17.96 | 9.74% | 11.70% | 4.06% | 6.84% | 3.01% | 9.74% |
| MASTEC INC | 3.72B | 45.20 | 28.67% | 1.27 | 16.67 | 14.76% | 13.04% | 5.95% | 8.80% | 3.38% | 14.76% |
| KBR INC | 2.40B | 17.05 | -2.27% | 0.57 | 12.09 | 31.51% | 8.20% | 7.07% | 8.22% | 5.07% | 31.51% |
| MYR GROUP INC/D | 509.50M | 30.94 | 22.83% | 0.61 | 27.49 | 7.14% | 8.91% | 1.87% | 4.62% | 0.80% | 7.14% |
| DYCOM INDUSTRIE | 3.29B | 105.41 | 14.76% | 1.26 | 31.43 | 11.60% | 21.59% | 8.97% | 13.79% | 4.81% | 11.60% |

While almost all Tutor Perini's Competitors have a positive revenue growth, the company has faced the worst growth in 2017 with a negative 4.34%, far from the median of 14.76%. This emphasis the significant upside for the company thought better management. As mentioned early, even if their ROIC has significantly increased since 2015, it is far from the company's competitor of 9.74% and the upside will be achieve by completing more profitable project with a stronger cash flow. The recent improvement should easily lead the company to reach the median industry in the next years. Gross Profit margin is already at the median of the industry and the SG&A expenses are expected to decrease proportionally to revenue, which is going to increase EBITDA margin and NI margin in the futures.

## Cost of Capital:

Cost of Capital - Current Market Value

| | Weight | Cost | W x C |
|---|---|---|---|
| 3) Equity | 63.2% | 14.4% | 9.1% |
| 4) Debt Cost (A-T) | 36.8% | 4.6% | 1.7% |
| 5) Preferred Equity | 0.0% | 0.0% | 0.0% |
| WACC | | | 10.8% |

Capital Structure (Millions of USD)

| | | |
|---|---|---|
| Market Cap | 1,261.9 | 63.2% |
| ST Debt | 30.7 | 1.5% |
| LT Debt | 705.5 | 35.3% |
| Pref. Eqty | 0.0 | 0.0% |
| Total | 1,998.2 | 100.0% |

The capital structure of the company is principally based on equity with a weight of 63.2% for a relative high cost of 14.4%. On the other hand, the company use only 36.8% debt to finance its operation for a cost of 4.6%, rated ba3 by Moody's. The WACC of the company is at a high 10.8%. Since January 2016, the economic value added spread has been significantly better, even if it stay negative, from -9.50 % to -4.80%. The future of this ratio is reinforce by the strong balance sheet of the company.

## Conclusion:

Tutor Perini Corporation has faced difficult period in the last 5 years but the company has shifted its strategy during the last two years and bring strong financial health to the company. The increase in demand in higher margin segment provides a bright forecast for the company.

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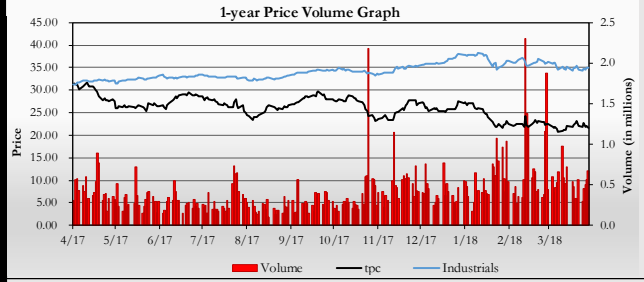
# CENTER FOR GLOBAL FINANCIAL STUDIES

**BULLISH**

| | | | | |
|---|---|---|---|---|
| Analysis by Al Capone | Current Price: | $21.60 | Intrinsic Value | $39.64 |
| 4/15/2018 | Divident Yield: | 0.0% | Target Price | $31.80 |

Target 1 year Return: 47.22%
Probability of Price Increase: 100%

**1-year Price Volume Graph**




**Description**

Tutor Perini Corporation, a construction company, provides diversified general contracting, construction management, and design-build services to private customers and public agencies worldwide.

**General Information**

| | |
|---|---|
| Sector | Industrials |
| Industry | Construction and Engineering |
| Last Guidance | February 12, 2018 |
| Next earnings date | May 3, 2018 |

**Market Assumptions**

| | |
|---|---|
| Estimated Equity Risk Premium | 5.00% |
| Effective Tax rate | 29% |

**Market Data**

| | |
|---|---|
| Market Capitalization | $1,075.49 |
| Daily volume (mil) | 0.67 |
| Shares outstanding (mil) | 49.79 |
| Diluted shares outstanding (mil) | 50.76 |
| % shares held by institutions | 109% |
| % shares held by investments Managers | 81% |
| % shares held by hedge funds | 2% |
| % shares held by insiders | 20.79% |
| Short interest | 12.41% |
| Days to cover short interest | 10.12 |
| 52 week high | $32.30 |
| 52-week low | $20.20 |
| Volatility | 43.76% |

**Past Earning Surprises**

| Quarter ending | Revenue | EBITDA |
|---|---|---|
| 12/31/2016 | -8.71% | -9.49% |
| 3/31/2017 | -1.43% | 14.00% |
| 6/30/2017 | -13.09% | -37.23% |
| 9/30/2017 | -21.89% | -36.15% |
| 12/31/2017 | -14.56% | 5.09% |
| Mean | **-11.94%** | **-12.76%** |
| Standard error | 0.9% | 4.6% |

**Market and Credit Scores**

| |
|---|
| Recommendation (STARS) Value--0 |
| Recommendation (STARS) Description--0 |
| Quality Ranking Value--B- |
| Quality Ranking Description--Lower |
| Short Score--4 |
| Market Signal Probability of Default % (Non-Ratings)--7.192% |
| CreditModel Score (Non-Ratings)--bb+ |

**Industry and Segment Information**

| LTN Revenues by Geographic Segments | LTM Revenues by Business Segments |
|---|---|
| United States--97% | Civil (Including Management Services)--39% |
| Foreign and U.S. Territories--3% | Building (Including Management Services)--42% |
| -- | Specialty Contractors--26% |
| -- | Elimination of Intersegment Revenue---6% |
| -- | -- |

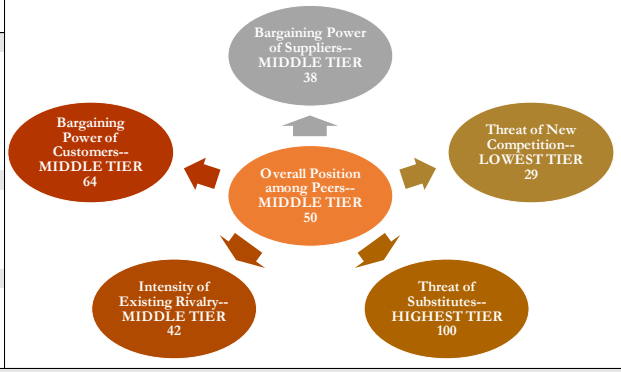
**Peers**

| | |
|---|---|
| Granite Construction Incorporated | AECOM |
| KBR, Inc. | Quanta Services, Inc. |
| Aegion Corporation | MasTec, Inc. |
| Fluor Corporation | EMCOR Group, Inc. |
| Jacobs Engineering Group Inc. | Primoris Services Corporation |

| Management | Position | Total Compensations Growth | Stock Price Growth During Tenure |
|---|---|---|---|
| Tutor, Ronald | Chairman & CEO | 4.35% per annum over 5y | 5.47% per annum over 5y |
| Frost, James | President, COO & Director | 15.82% per annum over 5y | 5.47% per annum over 5y |
| Smalley, Gary | Executive VP, CFO & Principal Accounting Office | 54.24% per annum over 1y | 67.26% per annum over 1y |
| Shaw, Craig | Executive Vice President | -5.13% per annum over 5y | 5.47% per annum over 5y |
| Casado, Jorge | Vice President of Investor Relations & Corporat | | |
| Barrett, John | Executive VP, Treasurer & Corporate Secretary | | |

| Profitability | tpc (LTM) | tpc Historical | Peers' Median (LTM) |
|---|---|---|---|
| Return on Capital (GAAP) | 6.4% | 5.66% | 9.37% |
| Operating Margin | 4% | 3.12% | 5.82% |
| Revenue/Capital (GAAP) | 1.66 | 1.82 | 1.61 |
| ROE (GAAP) | 9.6% | 8.0% | 18.7% |
| Net margin | 3.1% | 2.2% | 3.9% |
| Revenue/Book Value (GAAP) | 3.06 | 3.67 | 4.82 |
| **Invested Funds** | **tpc (LTM)** | **tpc Historical** | **Peers' Median (LTM)** |
| Cash/Capital | 7.6% | 6.6% | 17.5% |
| NWC/Capital | 52.1% | 40.1% | 10.0% |
| Operating Assets/Capital | 17.2% | 23.9% | 37.3% |
| Goodwill/Capital | 23.1% | 29.4% | 35.2% |
| **Capital Structure** | **tpc (LTM)** | **tpc Historical** | **Peers' Median (LTM)** |
| Total Debt/Market Capitalization | 0.33 | 0.39 | 0.42 |
| Cost of Debt | 9.3% | 6.3% | 3.9% |
| CGFS Rating (F-score, Z-score, and default Probability) | BB | | |
| WACC | 11.4% | 8.5% | 7.9% |

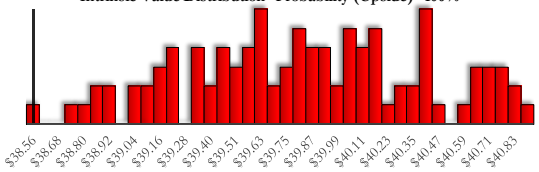
**Porter's 5 forces (Scores are percentiles)**




**Valuation**

| Forecast Assumptions | Explicit Period (10 years) | Continuing Period |
|---|---|---|
| Revenue Growth CAGR | 11% | 2% |
| Average Operating Margin | 4% | 4% |
| Average Net Margin | 2% | 2% |
| Growth in Capital CAGR | 7% | 2% |
| Growth in Claims CAGR | 2% | 2% |
| Average Return on Capital | 8% | 9% |
| Average Return on Equity | 8% | 10% |
| Average Cost of Capital | 9% | 10% |
| Average Cost of EquityKe | 11% | 11% |

**Intrinsic Value Distribution--Probability (Upside)=100%**




**Sensitivity Attribution Analysis**