

TopBuild Corp. (BLD)

\$103.38 (As of 01/03/20)

Price Target (6-12 Months): **\$119.00**

Long Term: 6-12 Months

Zacks Recommendation: **Outperform**

(Since: 11/04/19)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

2-Buy

Zacks Style Scores:

VGM:A

Value: B

Growth: A

Momentum: A

Summary

Shares of TopBuild have broadly outperformed its industry in the past year. Earnings estimates have improved over the past seven days, depicting analysts' optimism surrounding the company's bottom-line growth potential. Its efforts toward strategic acquisitions are encouraging. Notably, the USI acquisition and strong selling prices partly offset reduced sales volume in the Distribution business. Also, the company's strength in the Insulation Installation business raises hope. However, higher raw material and closure costs have been putting pressure on its profitability. Also, seasonal fluctuations and federal government's actions are pressing concerns.

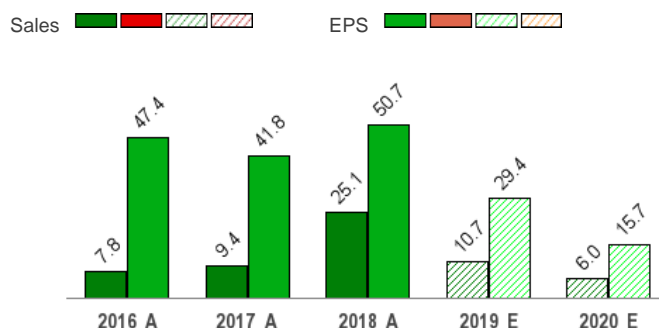
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$113.74 - \$46.06
20 Day Average Volume (sh)	286,810
Market Cap	\$3.5 B
YTD Price Change	0.3%
Beta	0.79
Dividend / Div Yld	\$0.00 / 0.0%
Industry	<u>Building Products - Miscellaneous</u>
Zacks Industry Rank	Bottom 33% (168 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	9.3%
Last Sales Surprise	1.7%
EPS F1 Est- 4 week change	1.2%
Expected Report Date	02/25/2020
Earnings ESP	0.0%
P/E TTM	19.8
P/E F1	16.5
PEG F1	0.6
P/S TTM	1.4

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2020	651 E	706 E	731 E	717 E	2,799 E
2019	619 A	660 A	682 A	673 E	2,640 E
2018	491 A	606 A	647 A	640 A	2,384 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2020	\$1.22 E	\$1.70 E	\$1.79 E	\$1.65 E	\$6.27 E
2019	\$1.06 A	\$1.43 A	\$1.53 A	\$1.40 E	\$5.42 E
2018	\$0.73 A	\$1.03 A	\$1.23 A	\$1.20 A	\$4.19 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 01/03/2020. The reports text is as of 01/06/2020.

Overview

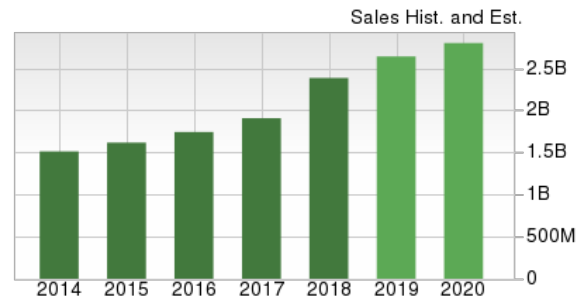
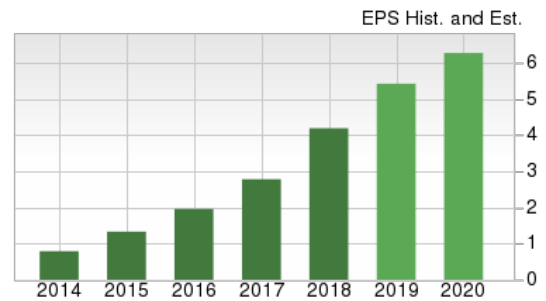
Headquartered in Daytona Beach, FL, **TopBuild Corp.** is an installer and distributor of insulation and other building products to the U.S. construction industry. TopBuild, which earlier operated as a subsidiary of Masco Corporation, provides insulation and building material services across the nation through TruTeam and Service Partners. The company started trading on the NYSE under the symbol "BLD" from Jul 1, 2015.

The company has two reportable segments — Installation (TruTeam) and Distribution (Service Partners).

Installation segment (accounting for 73% of total third-quarter 2019 net sales) installs insulation and other building products through the TruTeam contractor services business, which had nearly 200 branches located in 40 states, as of Sep 30, 2019. The company installs various insulation applications including fiberglass batts and rolls, blown-in loose fill fiberglass, blown-in loose fill cellulose and polyurethane spray foam. Also, it installs other building products like rain gutters, glass and windows, fire proofing, garage doors, shower enclosures, as well as closet shelving. The installation process includes procurement supplied by leading manufacturers, project scheduling and logistics, multi-phase professional installation, as well as installation quality assurance.

Distribution segment (32.4%) sells and distributes insulation and other building products including rain gutters, fireplaces, closet shelving and roofing materials through the Service Partners business, which had approximately 75 branches located in 32 states, as of Sep 30, 2019. Its Service Partners customer base consists of thousands of insulation contractors of all sizes, gutter contractors, weatherization contractors, other contractors, dealers, metal building erectors and modular home builders.

[Intercompany eliminations accounted for 5.4% of total third-quarter 2019 net sales.]



Reasons To Buy:

▲ **Strong Performance & Prospects:** Shares of TopBuild have outperformed its industry over a year. The company has been recording solid earnings and revenue growth over the last few quarters. During the first nine months of 2019, the company's sales increased 12.4%, adjusted earnings per share grew 34.4%, adjusted EBITDA was up 32.7% and adjusted EBITDA margin expanded 210 basis points (bps) from the corresponding period of 2018. The strong performance was mainly driven by the USI acquisition and increased selling prices. Also, higher sales growth in the Installation segment and operational efficiencies added to the bliss.

Strategic acquisitions and favorable construction market bode well for the company.

Overall, the business has been gaining momentum and growing significantly faster than the underlying market. Based on the last two months' starts data and solid prospects, the company raised its view for full-year 2019 housing starts to the range of 1.245-1.275 million. Earlier, it projected starts within 1.23-1.27 million.

Moreover, it expects 2019 net sales between \$2.625 billion and \$2.645 billion, indicating 10.1-10.9% growth from 2018. The company expects adjusted EBITDA between \$354 million and \$360 million during the year, suggesting an improvement from \$283.4 million registered a year ago.

In a nutshell, considering the company's performance so far this year and upbeat view, shares of TopBuild have gained more than 112.1% year to date, broadly outperforming its industry's 39.5% growth. Earnings estimates for 2020 have moved 0.5% upward over the past seven days. This reflects analysts' optimism surrounding the company's earnings growth potential.

Meanwhile, TopBuild's superior return on equity (ROE) is indicative of growth potential. The company's ROE is currently 16.2%. This compares favorably with ROE of 12.4% for the industry it belongs to. This indicates efficiency in using its shareholders' funds.

▲ **Inorganic Moves:** Acquisitions are an important part of TopBuild's growth strategy. In 2017, the company had acquired six insulation businesses that generated \$70.7 million of net sales during the year.

Again in 2018, it had completed the acquisition of three companies: ADO, a distributor of insulation accessories, Santa Rosa, a residential and commercial insulation company, and USI, a leading distributor and installer of insulation in both residential and commercial construction markets. These three businesses together had generated \$297.1 million of net sales in 2018. Notably, the said buyouts added \$311.7 million to net sales in the last three quarters.

On Jul 15, 2019, it acquired Burbank, CA-based Viking Insulation — an insulation installation company — for a purchase price of approximately \$7.7 million. The company expects solid improvement in net sales and earnings, and plans to invest more in such companies going forward.

In addition to acquisitions, the company plans to close some low-margin businesses to focus on its core areas in a bid to accelerate growth and improve shareholder value.

▲ **Solid Economy & Improved Homebuilding Market:** The U.S. housing market has gained considerable strength on the back of declining mortgage rates, solid job market and a moderate rise in home prices. All these positives point toward continually strong demand through the balance of 2019 and in 2020, which is anticipated to benefit its business. Moreover, the recently announced starts data, strong household formations and optimistic builder sentiment show TopBuild's strength.

Additionally, strong industry fundamentals in both light and heavy commercial markets provide attractive growth opportunities for TopBuild.

▲ **Driving Shareholder Value:** The company plans to drive shareholder value through investing in new areas of production, selectively pursuing acquisitions with the right fit and return, as well as returning cash to its shareholders through share repurchases.

TopBuild had returned 1,063,528 shares for approximately \$65 million to its shareholders through stock repurchases in 2018. In the first three quarters of 2019, it bought back 810,077 shares (including 176,327 shares received as final settlement of 2018 ASR Agreement) for \$52.2 million through the repurchase program. On Feb 22, 2019, the board authorized the repurchase of an additional \$200 million shares under the 2019 repurchase program.

Risks

- **Raw Material Inflation:** Higher raw material costs remain a concern for TopBuild. Although inflation was moderate during the third quarter, it may hurt the company in future. In 2018, gross margin was under significant pressure due to record material cost increases driven by tighter supply and higher freight costs.

Although the company has been working to recover higher commodity costs through price increases, we expect ongoing volatility in material costs to continue in the near term.

- **Lower Distribution Business Volumes:** TopBuild is witnessing lower sales volumes, primarily in the Distribution segment. In the past nine months, the segment registered 1.8% decline in volumes. The downfall was mainly due to its deliberate decisions with respect to prices and volume, as well as decision to exit some low-margin businesses.
 - **Seasonal Influence on Business:** TopBuild's business has been historically subjected to seasonal influences. The company typically realizes higher sales in the third and fourth calendar quarters, corresponding with the peak season for residential new construction and residential repair/remodel activity. Sales during winters are seasonally slower due to lower construction activity. Hurricanes, severe storms, earthquakes, droughts, floods, fires and other natural disasters also hamper its performance.
 - **Federal Government Actions:** As TopBuild's business prospects are highly correlated with U.S. housing market condition and repair and remodeling activity, any untoward situation influencing the construction and housing sectors will impact the company's financials. The housing industry is cyclical and is affected by consumer confidence levels, prevailing economic conditions and interest rates. The federal government's actions related to economic stimulus, taxation and borrowing limits could affect consumer confidence and spending levels, which in turn may hurt both the economy and the housing market.
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Last Earnings Report

TopBuild Beats on Q3 Earnings & Revenues, Raises Guidance

TopBuild Corp. reported third-quarter 2019 results, wherein earnings and revenues surpassed the Zacks Consensus Estimate. Also, both the top and bottom lines grew on a year-over-year basis, backed by national scale, strong customer and supplier relationships, as well as operational efficiency initiatives.

The company reported adjusted earnings of \$1.53 per share, beating the consensus estimate of \$1.40 by 9.3%. Also, the said metric increased 24.4% from the prior-year figure of \$1.23. The uptrend was primarily backed by improvement in residential and commercial markets.

Total revenues of \$682.3 million topped the consensus mark of \$671 million by 1.7%. Also, the reported figure rose 5.4% on a year-over-year basis, driven by increased volume, and pricing.

Quarter Ending 09/2019

Report Date	Oct 31, 2019
Sales Surprise	1.66%
EPS Surprise	9.29%
Quarterly EPS	1.53
Annual EPS (TTM)	5.22

Operating Highlights

Gross margin improved 130 basis points (bps) year over year to 26.3%. Adjusted operating profit also increased 16% year over year to \$80.6 million. Adjusted operating margin in the quarter came in at 11.8%, improving 110 bps from the year-ago period. Both gross and operating margin improvements were driven by higher selling prices, strong commercial sales growth, operational efficiencies and synergies from USI, partially offset by increased material costs.

Adjusted EBITDA margin improved 140 bps to 14.4% during the quarter.

Segmental Performance

TruTeam's revenues increased 7.3% year over year to \$498.4 million. Volume accounted for 3.8% of this growth and selling price contributed 3%. Adjusted operating margin in the quarter expanded 80 bps to 14%.

Revenues of the **Service Partners** segment grew 3.8% year over year to \$220.9 million, driven by a 4.4% price increase, partially offset by a slight decline in volume. Adjusted operating margin also improved 150 bps from the year-ago level to 10.6%.

Financial Update

Cash and cash equivalents as of Sep 30, 2019 were \$171.6 million, up from \$100.9 million at 2018-end. Net cash provided by operations was \$182.8 million in the first nine months of 2019 compared with \$96 million recorded in the comparable period last year.

The company completed the acquisition of Viking Insulation during the reported quarter. Based in Southern California, Viking focuses on fiberglass installation in a wide variety of light commercial and residential projects.

Also, the company repurchased 364,074 shares at an average price of \$89.76 per share in the quarter under review. As of Sep 30, 2019, \$147.8 million of the \$200-million authorization remained.

2019 Guidance

Based on the last two months' starts data and conversations in the field with customers, TopBuild raised its view for housing starts in 2019 to 1.245-1.275 million from 1.23-1.27 million projected earlier.

Also, it raised its revenue and adjusted EBITDA guidance for 2019. Revenues are now expected within \$2,625-\$2,645 million compared with \$2,610-2,640 million projected earlier. Adjusted EBITDA is projected between \$354 million and \$360 million versus \$345-\$355 million anticipated earlier.

Valuation

TopBuild shares are up 112.1% in the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Construction sector are up 39.5% and 32.9%, respectively, in the past year.

The S&P 500 index is up 25.7% in the past year.

The stock is currently trading at 16.44X forward 12-month price to earnings, which compares to 14.1X for the Zacks sub-industry, 15.72X for the Zacks sector and 18.71X for the S&P 500 index.

Over the past four years, the stock has traded as high as 27.64X and as low as 8.87X, with a 4-year median of 16.47X. Our Outperform recommendation indicates that the stock will perform better than the market. Our \$119 price target reflects 18.92X forward 12-month earnings.

The table below shows summary valuation data for BLD

Valuation Multiples - BLD					
		Stock	Sub-Industry	Sector	S&P 500
P/E F 12M	Current	16.44	14.1	15.72	18.71
	4-Year High	27.64	16.14	17.52	19.34
	4-Year Low	8.87	7.19	10.63	15.17
	4-Year Median	16.47	12.99	15.69	17.58
P/S F12M	Current	1.25	1.22	1.91	3.47
	4-Year High	1.43	3.63	2.23	3.47
	4-Year Low	0.49	0.69	1.25	2.63
	4-Year Median	0.97	0.91	1.72	3.05
EV/EBITDA TTM	Current	12.68	22.11	19	11.99
	4-Year High	32.01	30.09	22.53	12.86
	4-Year Low	8.89	17.59	14.4	8.48
	4-Year Median	14.99	22.94	19.23	10.95

As of 01/03/2019

Industry Analysis Zacks Industry Rank: Bottom 33% (168 out of 252)



Top Peers

Foundation Building Materials, Inc. (FBM)	Outperform
Installed Building Products, Inc. (IBP)	Outperform
Arcosa, Inc. (ACA)	Neutral
Aegion Corporation (AEGN)	Neutral
Frontdoor, Inc. (FTDR)	Neutral
James Hardie Industries PLC. (JHX)	Neutral
Patrick Industries, Inc. (PATK)	Neutral
Advanced Drainage Systems, Inc. (WMS)	Neutral

Industry Comparison Industry: Building Products - Miscellaneous				Industry Peers		
	BLD Outperform	X Industry	S&P 500	FBM Outperform	JHX Neutral	PATK Neutral
VGM Score	A	-	-	B	B	A
Market Cap	3.51 B	1.05 B	23.66 B	845.61 M	8.65 B	1.24 B
# of Analysts	4	3	13	6	1	3
Dividend Yield	0.00%	0.00%	1.79%	0.00%	1.02%	1.91%
Value Score	B	-	-	C	D	A
Cash/Price	0.05	0.09	0.04	0.03	0.02	0.09
EV/EBITDA	16.37	9.40	13.88	15.49	20.81	7.74
PEG Ratio	0.59	1.39	1.99	0.30	NA	1.77
Price/Book (P/B)	3.01	2.01	3.36	2.14	8.32	2.59
Price/Cash Flow (P/CF)	19.26	10.06	13.62	8.43	24.80	7.21
P/E (F1)	16.49	17.16	18.74	15.97	22.74	12.16
Price/Sales (P/S)	1.35	1.33	2.67	0.39	3.42	0.54
Earnings Yield	6.07%	5.66%	5.32%	6.25%	4.40%	8.22%
Debt/Equity	0.65	0.68	0.72	1.68	1.38	1.51
Cash Flow (\$/share)	5.37	2.50	6.94	2.33	0.79	7.25
Growth Score	A	-	-	A	B	B
Hist. EPS Growth (3-5 yrs)	44.81%	22.67%	10.56%	NA	-5.29%	32.29%
Proj. EPS Growth (F1/F0)	15.67%	14.47%	7.41%	20.37%	65.38%	14.77%
Curr. Cash Flow Growth	60.10%	13.50%	14.83%	7.16%	46.24%	55.61%
Hist. Cash Flow Growth (3-5 yrs)	64.16%	13.23%	9.00%	NA	6.13%	40.89%
Current Ratio	1.64	1.75	1.23	2.09	1.66	2.61
Debt/Capital	39.39%	41.82%	42.92%	62.68%	57.92%	60.22%
Net Margin	7.06%	5.51%	11.08%	2.28%	10.22%	4.16%
Return on Equity	16.15%	12.44%	17.10%	10.31%	26.00%	20.73%
Sales/Assets	1.02	1.06	0.55	1.53	0.62	1.73
Proj. Sales Growth (F1/F0)	6.04%	3.80%	4.20%	3.72%	4.68%	4.35%
Momentum Score	A	-	-	F	B	C
Daily Price Chg	0.26%	0.00%	-0.61%	0.51%	-1.26%	-1.10%
1 Week Price Chg	-0.21%	0.00%	0.13%	7.90%	0.71%	0.92%
4 Week Price Chg	-6.34%	-0.25%	2.60%	-2.38%	-0.76%	2.35%
12 Week Price Chg	6.82%	7.77%	8.87%	17.93%	17.90%	24.38%
52 Week Price Chg	127.11%	41.43%	29.34%	119.53%	82.80%	74.77%
20 Day Average Volume	286,810	198,121	1,603,615	628,002	13,244	153,350
(F1) EPS Est 1 week change	0.59%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	1.16%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 12 week change	8.79%	-3.58%	-0.57%	4.25%	NA	-7.19%
(Q1) EPS Est Mthly Chg	1.04%	0.00%	0.00%	0.00%	NA	0.00%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	B
Growth Score	A
Momentum Score	A
VGM Score	A

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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