

Quanta Services Inc. (PWR)

\$34.97 (As of 05/01/20)

Price Target (6-12 Months): **\$36.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 01/02/20)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:A

Value: A

Growth: A

Momentum: B

Summary

Quanta Services' shares have outperformed its industry year to date. The trend is likely to continue in the near term, given its fourth-quarter results, wherein earnings and revenues surpassed the respective Zacks Consensus Estimate by 10.7% and 2.6%. Moreover, 2019 marked the fourth consecutive year of growth with record revenues, operating income, adjusted EBITDA and adjusted EPS. The performance was backed by continued growth across base business (infrastructure hardening and grid modernization), along with the communications segment in the Electric Power division. Its communications infrastructure services business is anticipated to benefit from the present industry trends. However, inadequate resource utilization, regulatory challenges and risks like project delays, stiff competition, and oil & gas volatility remain concerns.

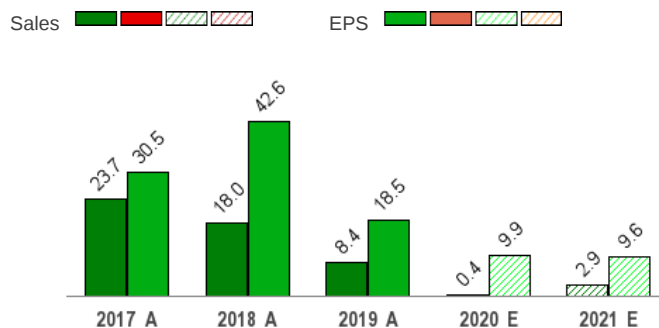
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$44.09 - \$23.77
20 Day Average Volume (sh)	1,480,848
Market Cap	\$4.8 B
YTD Price Change	-14.1%
Beta	1.15
Dividend / Div Yld	\$0.20 / 0.6%
Industry	Engineering - R and D Services
Zacks Industry Rank	Bottom 26% (187 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	10.7%
Last Sales Surprise	2.7%
EPS F1 Est- 4 week change	-3.7%
Expected Report Date	05/07/2020
Earnings ESP	-7.5%

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	2,649 E	2,838 E	3,136 E	2,886 E	12,522 E
2020	2,765 E	3,015 E	3,416 E	3,073 E	12,166 E
2019	2,807 A	2,839 A	3,353 A	3,113 A	12,112 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.50 E	\$0.93 E	\$1.08 E	\$0.91 E	\$4.01 E
2020	\$0.47 E	\$0.96 E	\$1.22 E	\$0.97 E	\$3.66 E
2019	\$0.96 A	\$0.31 A	\$1.14 A	\$0.93 A	\$3.33 A

*Quarterly figures may not add up to annual.

P/E TTM	10.5
P/E F1	9.6
PEG F1	0.7
P/S TTM	0.4

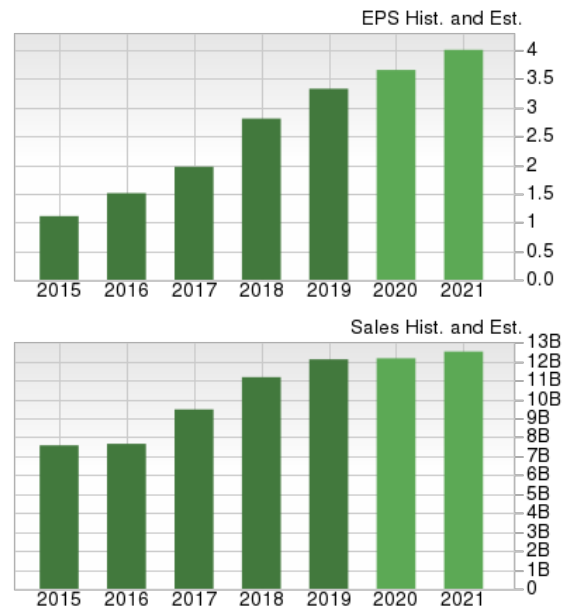
The data in the charts and tables, except sales and EPS estimates, is as of 05/01/2020. The reports text and the analyst-provided sales and EPS estimates are as of 05/04/2020.

Overview

Quanta Services is a leading national provider of specialty contracting services, and one of the largest contractors serving the transmission and distribution sector of the North American electric utility industry. Quanta Services has operations in United States, Canada, Australia and other selected international markets. The company has two reportable segments that are as follows:

The Electric Power Infrastructure Services segment (which contributed 59% to 2019 revenues) provides comprehensive network solutions to customers in the electric power industry. Services performed include the design, installation, upgrade, repair and maintenance of electric power transmission and distribution networks, and sub-station facilities and the installation of "smart grid" technology on electric power networks.

The Pipeline and Industrial Infrastructure Services segment (41%) provides comprehensive network solutions to customers involved in the transportation of natural gas, oil and other pipeline products. Services include the design, installation, repair and maintenance of oil and gas transmission and distribution systems and related trenching and directional boring services. Also, this segment provides pipeline protection services and performs pipeline integrity and rehabilitation services.



Reasons To Buy:

- ▲ **Strong Performance & Robust Growth Strategy:** Quanta Services has been delivering robust performance over the last few quarters. Notably, the company's earnings grew 18.5% year over year in 2019, backed by strong segmental performance. Moreover, 2019 marked the fourth consecutive year of growth with record revenues, operating income, adjusted EBITDA and adjusted earnings per share. The company's revenues witnessed a double-digit CAGR over the last four years. Quanta Services believes that the delivery of energized services differentiates it from its competitors and helps win new businesses. Currently, the company is pursuing a three-pronged growth strategy focusing on timely delivery of projects to exceed customer expectation; leverage on core business to expand in complementary adjacent service lines and continuation of exploring new service lines.

Solid end-market prospects of both of its segments, namely Electric Power and Pipeline and Industrial Infrastructure, are likely to boost profit.

Overall, the company's engineering and project management capabilities allow it to capitalize on market trends that are currently skewed toward an engineering, procurement and construction or EPC model. The company ended 2019 with a record total backlog that exceeded \$15 billion for the first time in its history, with 12-month backlog \$7.95 billion. This compares favorably with \$12.34 billion of total backlog and \$6.98 billion of 12-month backlog at 2018-end. This demonstrates the strength of its core operations.

Going forward, it expects base business activity to remain robust, which currently accounts for approximately 90% of revenue guidance in 2020. Quanta Services' optimism stems from healthy backlog levels which are expected to grow further. Quanta Services remains confident about end-market prospects of both of its segments, namely Electric Power and Pipeline and Industrial Infrastructure Services.

- ▲ **Solid Performance of Electric Power Operations:** Electric Power operations continued to execute well from a top line perspective. Segment revenues, with revenues from base business activities including communications operations, grew 20% from 2018 level. The increase in California fire hardening activities, which significantly expanded in 2019 and more than offset almost \$400 million of reduced revenues from larger projects, led to the upside. Solid performance in 2019 was also backed by base business activities, courtesy of robust spending by electric utilities on grid modernization and infrastructure hardening, particularly in the western United States, as well as by gas utilities on distribution system modernization and safety programs. It is important to note that approximately 65% of Quanta's revenues is directly tied to regulated electric and gas utility customers, which is core to its business. Acquisitions also added to the positives. As of Dec 31, 2019, the segment's 12-month backlog was \$5.36 billion and total backlog was \$9.82 billion, up 17.4% and 14.9% year over year, respectively. Prospects of the Electric Power segment remain robust, given customers' investment in grid modernization programs to accommodate a changing fuel generation mix toward natural gas and renewables, intended to address the aging infrastructure, strengthen systems for resiliency against extreme weather conditions, and support long-term economic growth.

The company has been witnessing solid Telecom revenues, which are included within the Electric Power segment, mainly from U.S. operations. U.S. telecom revenues have recorded sequential growth in each quarter since first-quarter 2017, when the company officially reentered into the U.S. telecommunications market. With the larger diameter pipeline market expanding, and a multi-year cycle ahead of it, the company remains optimistic about its communications infrastructure services operations. Quanta Services continues to make inroads with customers as they deploy capital for fiber-to-the-home and business, long-haul fiber, 4G wireless backhaul and the early stages of 5G. Meanwhile, the North America electric transmission and distribution markets are expected to act as one of the key growth drivers for the company, as the region continues to deploy more capital for transmission and distribution upgrades to improve system reliability, and deliver renewable electricity from new generation sources to the demand centers. Its Communication Services revenues increased more than 40% in 2019 and ended the year with a total backlog of approximately \$770 million.

In a nutshell, growth of the electric power segment is expected to be fueled by the need to maintain and replace aging infrastructure, generation mix shifting to more renewable and natural gas, grid modernization and regulation aimed at improving grid reliability.

- ▲ **Robust Prospect for Pipeline and Industrial Infrastructure Services Operations:** Quanta Services' Pipeline and Industrial Infrastructure segment outlook looks equally promising, primarily due to the improving mainline and natural gas distribution, and integrity markets. The release of customer budgets, improved weather, and commencement of scheduled projects should boost the segment's results in the coming quarters. Going forward, the company continues to expect healthy levels of base load work including supporting midstream infrastructure, downstream support services and natural gas distribution. The company expects strong performance from pipeline projects going forward, driven by a considerable increase in large pipeline revenue contributions amid an active bidding and negotiating environment.

In 2019, the company's Pipeline and Industrial Infrastructure segment grew 4.9% despite meaningful less contribution from larger pipeline projects. The upside was mainly supported by base business activity in natural gas distribution, pipeline integrity and industrial services operations, as well as significantly larger pipeline project activity. Moreover, a gradual shift from coal to gas for power generation from commercial and residential customers is expected to boost natural gas pipeline projects in the long run. In addition, the company's infrastructure services business continues to thrive, supported by robust demand from communications industry. Quanta Services plans to grow its infrastructure solutions capabilities with strategic partnerships with customers and capital partners. As of Dec 31, 2019, the segment's 12-month backlog was \$2.59 billion and total backlog amounted to \$5.18 billion, up 7.3% and 36.5% respectively, from 2018-end.

- ▲ **Acquisitions/Partnerships to Boost Market Share & Backlog:** Quanta Services sees acquisitions as a fundamental component of its strategy to boost market share and develop incremental backlog. Quanta Services invested \$400 million in the strategic acquisition of seven companies in 2019 (compared to four buyouts in 2018). 2019 and 2018 buyouts strategically expanded its domestic electric power and communications service offerings.

Reasons To Sell:

- ▼ **Absence of Larger Pipeline Projects:** Volatility in Pipeline and Industrial operations, and consumer spending have been affecting the company's projects, as well as orders. The segment's 2019 revenues were somewhat offset by a decline in revenues from larger pipeline projects. Also, in 2019, its Electric Power Infrastructure Services operating margin declined 150 bps due to the absence of large projects compared with 2018.

Although Quanta Services' shares have outperformed its industry in the past year, estimates for 2020 have moved 1.8% downward over the past seven days, depicting analysts' concern over the company's earnings growth potential.

Quanta Services remains vulnerable to inadequate resource utilization, regulatory challenges and risks like project delays, stiff competition, and oil & gas volatility.

- ▼ **Regulatory Hurdles/Intense Competition:** Quanta Services operates in a highly uncertain environment. Both the company and its customers face stringent regulatory and permit hurdles for projects, especially regarding product quality, safety measures and environmental protection. For instance, on Jul 28, American Electric Power announced that due to regulatory challenges, it was terminating its effort to build Wind Catcher Generation Tie Line, for which Quanta had been awarded the EPC contract. Moreover, the company operates in a highly competitive industry, which already contains numerous small owner-operated private companies, few public companies and several large regional companies. Low barriers-to-entry in the industry and adequate financial resources as well as access to technical expertise may further intensify the competition.

Additionally, as a large chunk of Quanta Services' business involves outdoor activities, it is vulnerable to unfavorable weather conditions. Traditionally, it experiences lower gas distribution business activity in the first quarter due to seasonal weather, which impacts revenues and pressurizes margins. Although the company expects margins to improve in third-quarter 2019, decline in revenues and normal seasonality will likely cause a sequential decline in margins in the fourth quarter.

- ▼ **Project Delays:** At present, one of the biggest challenges for Quanta Services is obtaining the sighting and permission of energy infrastructure projects, including major electric transmission programs, and this is seriously weighing on its profitability. Also, Quanta Services deals with many large projects that are inherently prone to weaknesses such as irregular start-ups, delays and sudden stoppage during work. Intensive regional competition and delay in the bidding activity of transmission projects are headwinds that might hurt the performance of this segment going forward.

For instance, the Atlantic Coast Pipeline Project or ACP has been halted for the past several months due to permitting issues.

Last Earnings Report

Quanta Services' (PWR) Q4 Earnings Beat Estimates

Quanta Services Inc. reported impressive results in fourth-quarter 2019. Both the top and bottom lines surpassed the Zacks Consensus Estimate. However, adjusted earnings fell marginally on a year-over-year basis. Also, the company believes that strategic growth initiatives will help it post impressive results going forward.

Into the Numbers

In the quarter under review, the company reported adjusted earnings of 93 cents per share, beating the consensus estimate of 84 cents by 10.7%. However, the reported figure fell 3.1% from 96 cents per share reported a year ago.

Total revenues of \$3.11 billion surpassed the consensus mark of \$3.03 billion by 2.6%. In addition, the said metric grew marginally from the prior-year period. Revenue growth in the Electric Power Infrastructure Services segment was offset by softness in the Pipeline and Industrial Infrastructure Services business.

Segment Details

The company reports results under two reportable segments: Electric Power Infrastructure Services segment (accounting for 59.3%), and Pipeline and Industrial Infrastructure Services (40.7%).

Revenues from Electric Power Infrastructure Services totaled \$1,847.4 million, increasing 11.3% year over year. However, operating margins contracted 110 basis points (bps) to 8.7%.

Within the Pipeline and Industrial Infrastructure Services segment, revenues declined 12.9% from the prior-year quarter to \$1,265.4 million. However, operating margins of 7% improved 330 bps year over year.

Operating Highlights

Operating margin during the quarter contracted 10 bps from a year ago to 4.7%. Adjusted EBITDA of \$262.3 million declined 4% from \$273.3 million a year ago.

As of Dec 31, 2019, the company reported total backlog of \$15 billion and 12-month backlog of \$7.9 billion. This compares favorably with \$12.3 billion of total backlog and \$7 billion of 12-month backlog at 2018-end. Also, the reported metrics were up from third-quarter end respective figures of \$13.3 billion and \$7.6 billion.

Liquidity

As of Dec 31, 2019, Quanta Services had cash and cash equivalents of \$164.8 million compared with \$78.7 million at 2018-end. The company's long-term debt and notes payable (net of current maturities) amounted to \$1,292.2 million, up from \$1,040.5 million as of Dec 31, 2018.

Net cash used in operating activities was \$526.6 million in 2019 versus \$358.8 million cash provided by operating activities in the prior year. Free cash flow was \$297.9 million in the quarter versus \$97.7 million a year ago.

2019 Highlights

In 2019, the company's adjusted earnings came in at \$3.31 per share, increasing 18.5% from the year-ago figure of \$2.81 and surpassing analysts' expectation of \$3.25 by 1%. Revenues in the year totaled \$12.11 billion, reflecting an increase of 8.4% year over year. Also, the metric surpassed the consensus mark of \$12.03 billion by 0.7%.

Notably, the company completed seven acquisitions in 2019.

2020 Guidance

The company expects revenues in the range of \$12.2-\$12.6 billion. It expects adjusted earnings between \$3.62 and \$4.02 per share. Adjusted EBITDA is projected within \$1.03-\$1.12 billion, indicating a significant increase from \$941.8 million reported in 2019.

Notably, the company completed a strategic review of its Latin American (LATAM) operations owing to the conditions experienced in Peru during 2019 and political volatility in other countries. In 2020, LATAM operations are expected to generate revenues within \$20-\$40 million, operating loss in the \$15-\$20 million range and loss per share in the band of 10-13 cents.

Quarter Ending **12/2019**

Report Date	Feb 27, 2020
Sales Surprise	2.72%
EPS Surprise	10.71%
Quarterly EPS	0.93
Annual EPS (TTM)	3.34

Valuation

Quanta Services' shares are down 14.1% in the year-to-date period and 9.7% in trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Construction sector are down 33.6% and 23.3% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are down 27.2% and 13.1%, respectively.

The S&P 500 index is down 12.1% in the year-to-date period and 3.7% in the past year.

The stock is currently trading at 10.05X forward 12-month earnings, which compares to 12.22X for the Zacks sub-industry, 15.73X for the Zacks sector and 20.18X for the S&P 500 index.

Over the past five years, the stock has traded as high as 25.43X and as low as 6.64X, with a 5-year median of 13.48X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$36 price target reflects 10.59X forward 12-month earnings.

The table below shows summary valuation data for PWR

Valuation Multiples - PWR					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	10.05	12.22	15.73	20.18
	5-Year High	25.43	17.56	17.94	20.18
	5-Year Low	6.64	10.33	10.76	15.19
	5-Year Median	13.48	13.71	15.85	17.44
P/B TTM	Current	1.23	1.43	2.34	3.75
	5-Year High	1.67	2.83	6.73	4.55
	5-Year Low	0.84	0.82	1.7	2.84
	5-Year Median	1.4	1.9	3.28	3.64
EV/EBITDA TTM	Current	7.35	7.31	15.92	10.37
	5-Year High	12.02	10.42	21.48	12.86
	5-Year Low	5.54	5.05	12.48	8.28
	5-Year Median	8.57	7.62	17.88	10.77

As of 05/01/2020

Industry Analysis Zacks Industry Rank: Bottom 26% (187 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
AECOM (ACM)	Neutral	4
Fluor Corporation (FLR)	Neutral	4
Gates Industrial Corporation PLC (GTES)	Neutral	3
Jacobs Engineering Group Inc. (J)	Neutral	4
KBR, Inc. (KBR)	Neutral	4
MasTec, Inc. (MTZ)	Neutral	3
Dycom Industries, Inc. (DY)	Underperform	3
Willdan Group, Inc. (WLDN)	Underperform	4

Industry Comparison Industry: Engineering - R And D Services				Industry Peers		
	PWR	X Industry	S&P 500	ACM	FLR	KBR
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	4	4	4
VGM Score	A	-	-	F	C	B
Market Cap	4.81 B	2.39 B	20.61 B	5.55 B	1.43 B	2.79 B
# of Analysts	6	2	14	3	4	5
Dividend Yield	0.57%	0.00%	2.11%	0.00%	3.92%	2.04%
Value Score	A	-	-	F	B	B
Cash/Price	0.04	0.14	0.06	0.13	1.46	0.25
EV/EBITDA	6.87	7.54	11.87	27.67	1.74	7.54
PEG Ratio	0.64	1.48	2.47	1.49	NA	1.18
Price/Book (P/B)	1.23	1.55	2.67	1.44	0.85	1.50
Price/Cash Flow (P/CF)	7.06	7.78	10.66	8.16	2.92	8.30
P/E (F1)	9.32	15.50	19.01	18.39	8.24	11.41
Price/Sales (P/S)	0.40	0.49	2.10	0.30	0.08	0.48
Earnings Yield	10.47%	6.37%	5.05%	5.43%	12.16%	8.77%
Debt/Equity	0.37	0.65	0.72	0.87	0.97	0.74
Cash Flow (\$/share)	5.15	1.90	7.01	4.44	4.01	2.44
Growth Score	A	-	-	F	D	B
Hist. EPS Growth (3-5 yrs)	24.31%	15.11%	10.88%	-2.37%	NA	17.48%
Proj. EPS Growth (F1/F0)	9.81%	-23.36%	-7.32%	-30.79%	112.01%	1.66%
Curr. Cash Flow Growth	14.87%	6.22%	5.92%	-0.31%	14.03%	23.99%
Hist. Cash Flow Growth (3-5 yrs)	4.47%	9.65%	8.55%	15.22%	-9.29%	7.96%
Current Ratio	1.69	1.35	1.23	1.16	1.38	1.34
Debt/Capital	26.86%	39.25%	43.84%	46.53%	49.29%	42.67%
Net Margin	3.32%	1.04%	11.08%	-1.48%	-7.66%	0.99%
Return on Equity	11.66%	9.60%	16.44%	10.22%	8.94%	13.43%
Sales/Assets	1.47	1.08	0.54	1.24	1.96	1.09
Proj. Sales Growth (F1/F0)	0.45%	-2.18%	-1.42%	-37.47%	-1.87%	0.81%
Momentum Score	B	-	-	F	F	C
Daily Price Chg	-0.47%	-0.25%	-2.39%	-1.68%	0.78%	-5.37%
1 Week Price Chg	-2.66%	0.00%	-1.74%	3.38%	10.22%	-0.51%
4 Week Price Chg	17.98%	8.08%	17.07%	31.71%	88.71%	2.01%
12 Week Price Chg	-7.03%	-24.71%	-18.53%	-23.98%	-37.93%	-31.79%
52 Week Price Chg	-8.53%	-23.38%	-9.82%	9.51%	-60.63%	-9.55%
20 Day Average Volume	1,480,848	39,096	2,641,413	1,910,884	3,151,325	1,519,843
(F1) EPS Est 1 week change	-3.45%	0.00%	0.00%	-26.80%	-15.67%	-5.22%
(F1) EPS Est 4 week change	-3.68%	-9.24%	-6.62%	-26.80%	-19.64%	-10.31%
(F1) EPS Est 12 week change	-7.30%	-32.92%	-13.28%	-42.56%	-17.17%	-15.01%
(Q1) EPS Est Mthly Chg	-1.58%	-7.31%	-11.97%	-24.59%	-32.43%	-32.56%

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	A
Growth Score	A
Momentum Score	B
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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