

## Tetra Tech Inc. (TTEK)

**\$90.57** (As of 08/03/20)

Price Target (6-12 Months): **\$93.00**

Long Term: 6-12 Months

**Zacks Recommendation:**

**Neutral**

(Since: 04/02/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

**Zacks Rank:** (1-5)

**2-Buy**

Zacks Style Scores:

VGM:A

Value: B

Growth: A

Momentum: B

### Summary

Tetra Tech's third-quarter fiscal 2020 earnings surpassed the Zacks Consensus Estimate by 6.9% and revenues beat the same by 0.8%. Increased federal government spending and persistent solid demand for the company's services bode well for its businesses associated with each of its four client end markets. Acquisitions made by it over the past few quarters will likely prove beneficial in the upcoming quarters. In the past three months, its shares have outperformed the industry. However, reduction in oil and gas capital expenditure, commercial buildings work, and some industrial manufacturing programs will adversely impact its near-term results. Further increase in debt levels can raise the company's financial obligations. A stronger U.S. dollar might further depress its overseas business's results in the quarters ahead.

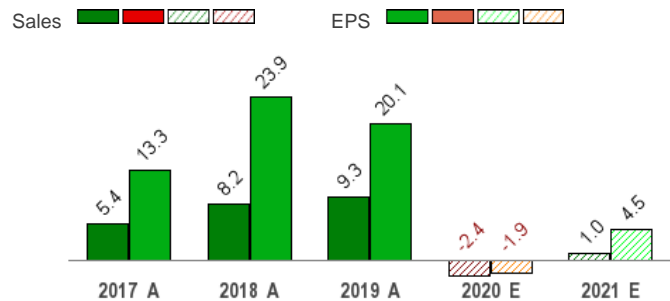
### Price, Consensus & Surprise



### Data Overview

52 Week High-Low	\$99.34 - \$63.61
20 Day Average Volume (sh)	235,364
Market Cap	\$4.8 B
YTD Price Change	2.9%
Beta	0.87
Dividend / Div Yld	\$0.68 / 0.8%
Industry	<a href="#">Pollution Control</a>
Zacks Industry Rank	Top 40% (100 out of 253)

### Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	6.9%
Last Sales Surprise	0.8%
EPS F1 Est- 4 week change	0.3%
Expected Report Date	NA
Earnings ESP	-1.7%

### Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	581 E	591 E	604 E	627 E	2,372 E
2020	614 A	584 A	560 A	602 E	2,349 E
2019	553 A	585 A	623 A	640 A	2,406 A

### EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.82 E	\$0.75 E	\$0.85 E	\$0.93 E	\$3.25 E
2020	\$0.84 A	\$0.73 A	\$0.78 A	\$0.83 E	\$3.11 E
2019	\$0.70 A	\$0.70 A	\$0.89 A	\$0.88 A	\$3.17 A

\*Quarterly figures may not add up to annual.

P/E TTM	27.5
P/E F1	29.1
PEG F1	1.9
P/S TTM	1.6

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 08/03/2020. The reports text is as of 08/04/2020.

## Overview

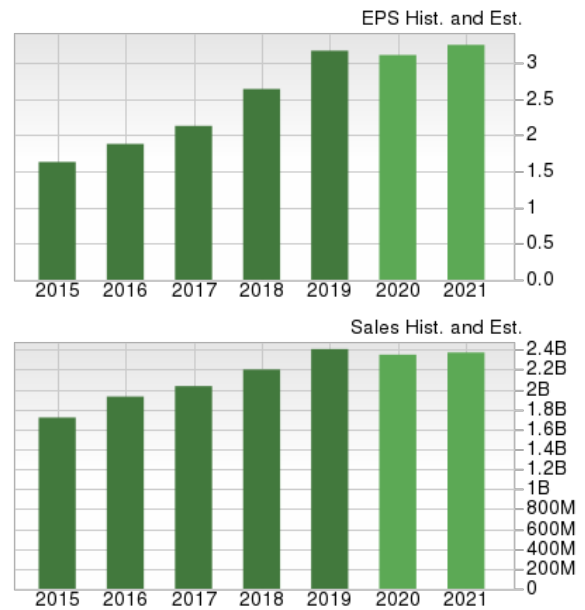
Headquartered in Pasadena, Tetra Tech is a leading provider of consulting, construction management, engineering, program management and technical services. It serves clients by providing cost-effective and innovative solutions on dealing with the fundamental needs for water, environmental and alternative energy services. Tetra Tech's has a diverse base of international and U.S. commercial clients, as well as U.S. federal and U.S. state and local government agencies.

Tetra Tech reports its businesses under the following two segments:

**Government Services Group** (57% revenues came from this segment in third-quarter fiscal 2020): This segment encompasses operations with U.S. government clients (federal, state and local) and all activities with development agencies.

Notably, the segment offers consulting and engineering services globally for a wide range of U.S. government clients. Some of the notable services offered are environmental monitoring, water and waste management, sustainable infrastructure design, international development and various civil infrastructure master planning and engineering design for transportation, facilities, as well as regional and local development.

**Commercial / International Services Group** (43%): This segment includes activities with U.S. commercial clients and all international activities excluding work performed for development agencies. The segment provides various services like environmental remediation, infrastructure and related environmental and geotechnical services as well as engineering and project management services.



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## Reasons To Buy:

▲ Tetra Tech has a diversified business structure, which allows it to mitigate the adverse impacts of weakness in one end-market, with strength across others. In a bid to maximize growth prospects, the company has been focusing on high-end consulting, design and engineering services, which are helping it promote high-value and high-margin business, thus differentiating it from peers in the marketplace. In the past three months, Tetra Tech's shares have gained 25.2% compared with the industry's growth of 16.4%. Also, in the past seven days, the consensus estimate for its earnings has risen 1.6% to \$3.11 per share for fiscal 2020 and 2.5% to 83 cents for fiscal fourth quarter.

Tetra Tech is enjoying strong backlog level. Also, the diversified business model, acquired assets and shareholder-friendly policies remain tailwinds for the company.

▲ Tetra Tech's backlog at the end of the fiscal third quarter increased to \$3.07 billion, up 8% and 3% on a year-over-year and sequential basis, respectively. For the fiscal fourth quarter, the company expects each of its four client end markets — the U.S. Federal, the U.S. state and local, the U.S. commercial, and the international — to grow on a sequential basis. This is due to the higher federal government spending, and persistent solid demand for the company's services related to water supply, wastewater treatment, flood control, and environmental restoration. Also, Tetra Tech's federal advanced analytics practice has been integrated with its business and carries more than \$1 billion in contract capacity for IT services and advanced analytics with the U.S. Federal Government. In fiscal 2020, the company expects to generate revenues of \$200 million from this practice, with the target of achieving revenues of \$500 million by fiscal 2023. In the quarters ahead, the company is also likely to benefit from strength across its renewable energy end market.

▲ Acquisitions made over the past few quarters will likely prove beneficial for Tetra Tech in the upcoming quarters. Notably, in July 2019, the company acquired shares of WYG plc, a provider of engineering and consulting services. Also, in April 2019, the company acquired eGlobalTech. Notably, eGlobalTech launched an AI solution named Auxilium in July 2019. In February 2020, Tetra Tech acquired Segue Technologies. The buyout is predicted to strengthen the company's business associated with government clients, especially the U.S. Department of Defense and commercial customers. The acquired assets are integrated with Tetra Tech's Government Services Group.

▲ Tetra Tech has consistently returned significant cash to shareholders through dividends and share repurchases. During the first three quarters of fiscal 2020, the company bought back shares worth \$102.2 million (\$21 million in the fiscal third quarter) and distributed dividends totaling \$25.6 million (\$9.2 million in the fiscal third quarter). Notably, the quarterly dividend rate was hiked 13% in April 2020. Also, in January 2020, the company received the approval for a new \$200-million share buyback program. Exiting the fiscal third quarter, it is left with \$223 million of share repurchase authorization. Such diligent capital deployment strategies boost shareholders' wealth.

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## Reasons To Sell:

- ▼ On a P/E (TTM) basis, Tetra Tech looks overvalued compared with the industry, with the respective tallies of 27.45X and 25.64X. Also, the company's current multiple is higher than the industry's three-month highest level of 25.64X. This makes us cautious about the stock. The duration of the coronavirus pandemic and the impacts of it on the company's business operations through some project delays will likely have a bearing on its results. For fiscal 2020, Tetra Tech projects adjusted earnings per share of \$3.13-\$3.18. The mid-point reflects a year-over-year decline of 0.5% from \$3.17 in fiscal 2019. Net revenues are anticipated to be \$2.32-\$2.36 billion, whereas it reported \$2.4 billion in fiscal 2019.
- ▼ International operations have exposed the company to the adverse impacts of macroeconomic cycles in the United States as well as unfavorable foreign currency movements. It is worth mentioning that approximately 30% of Tetra Tech's revenues were generated from international operations in the third quarter of fiscal 2020. A stronger U.S. dollar might further depress its overseas business's results in the quarters ahead.
- ▼ The company derives a significant portion of revenues from the U.S. federal, and the U.S. state and local customers. Such customers usually award multi-year contracts. We believe that any changes in the terms and clauses, and funding of the contracts will be detrimental. Also, the company's services offered in mining, and oil & gas markets are highly cyclical and vulnerable to economic downturns, which in turn are likely to impact its financials. For instance, fluctuations in market prices of metals — including uranium, precious metals, aluminum, copper, iron ore and potash — can cause its mining clients to cancel or curtail their projects, thus adding to the woes. In the quarters ahead, reduction in oil and gas capital expenditure, commercial buildings work, and some industrial manufacturing programs amid the coronavirus outbreak might adversely impact its performance.
- ▼ High debt levels can be concerning for Tetra Tech. In the last five fiscal years (2015-2019), the company's long-term debts recorded an increase of 7.8% (CAGR). Notably, at the end of the third quarter of fiscal 2020, the metric was \$264.7 million. Also, the company's cash and cash equivalents of \$141.7 million (exiting the fiscal third quarter) seems not to be impressive, considering its high debt profile. In addition, the company's ability to meet its debt obligations based on its current income has declined over the past quarter. Notably, its times interest earned ratio is 12.2, lower than 12.3 recorded at the end of the previous quarter. Further, increase in debt levels can raise the company's financial obligations.

High debt level, project delays and headwinds related to international exposure might be concerning for Tetra Tech.

## Last Earnings Report

### Tetra Tech Beats on Q3 Earnings and Sales, Ups View

Tetra Tech reported better-than-expected results for the third quarter of fiscal 2020 (ended Jun 28, 2020), with earnings surpassing estimates by 6.9%. This was the 12th consecutive quarter of impressive results.

The company's adjusted earnings per share in the reported quarter were 78 cents, surpassing the Zacks Consensus Estimate of 73 cents. Also, its earnings declined 12.4% from the year-ago quarter's 89 cents on weak sales generation, partially offset by lower costs and expenses.

Also, the bottom-line results fared well compared with the company's guidance of 72-75 cents per share.

Quarter Ending **06/2020**

Report Date	Jul 29, 2020
Sales Surprise	<b>0.76%</b>
EPS Surprise	<b>6.85%</b>
Quarterly EPS	<b>0.78</b>
Annual EPS (TTM)	<b>3.23</b>

### Revenues & Segmental Performance

In the reported quarter, Tetra Tech generated adjusted revenues of \$709.7 million, reflecting a year-over-year decline of 14%. Alternatively, adjusted net revenues (adjusted revenues minus subcontractor costs) were \$560.3 million, reflecting a decline of 10.1% from the year-ago quarter and in line with the higher-end of the company's guidance of \$540-\$560 million.

Further, its revenues surpassed the Zacks Consensus Estimate of \$556.1 million by 0.8%.

Backlog at the end of the quarter was \$3,066.6 million, reflecting growth of 2.6% from the previous quarter.

Revenues from the U.S. Federal customers (accounting for 31% of the quarter's revenues) were flat year over year. Growth in federal IT businesses was more than offset by a delay in international development projects.

However, U.S. Commercial sales (25% of the quarter's revenues) declined 7% year over year due to lower industrial programs. Stability was witnessed in regulatory-driven programs.

The U.S. State and Local sales (14% of the quarter's revenues) increased 5% on strength in water infrastructure business and higher revenues from operational technology. International sales (30% of the quarter's revenues) improved 3% year over year.

The company reports revenues under the segments discussed below:

Net sales of Government Services Group were \$319.2 million, down 9.5% year over year.

Revenues from Commercial / International Services Group totaled \$241 million, reflecting a year-over-year decline of 11%.

### Margin Profile

In the reported quarter, Tetra Tech's subcontractor costs totaled \$149.5 million, reflecting a decline of 26.2% from the year-ago quarter. Other costs of revenues were \$445.9 million, down 11.7% year over year. Selling, general and administrative expenses were \$50.8 million, down 4.4% year over year.

Adjusted operating income in the reported quarter decreased 8.8% year over year to \$59.6 million, while adjusted margin increased 10 basis points year over year to 10.6%.

### Balance Sheet and Cash Flow

Exiting the fiscal third quarter, Tetra Tech had cash and cash equivalents of \$141.7 million, up 4.9% from \$135 million recorded at the end of the last reported quarter. Long-term debt was down 20.5% sequentially to \$264.7 million.

During the first three quarters of fiscal 2020, the company's proceeds from borrowings amounted to \$298.4 million, while repayments totaled \$297.9 million.

In the first nine months of fiscal 2020, it generated net cash of \$194.6 million from operating activities, reflecting an increase of 71.6% from the prior-year comparable period. Capital expenditure was \$9.4 million, down 6.4% year over year.

### Shareholder-Friendly Policy

During the first three quarters of fiscal 2020, the company bought back shares worth \$102.2 million and distributed dividends totaling \$25.6 million.

Exiting the fiscal third quarter, the company has \$223 million worth authorization left under its approved buyback programs.

### Outlook

For fiscal 2020 (ending September 2020), Tetra Tech anticipates net revenues of \$2.32-\$2.36 billion, while adjusted earnings are predicted to be \$3.13-\$3.18. The earnings projection is higher than the previously mentioned \$3.05-\$3.13.

For the fiscal fourth quarter (ending September 2020), the company anticipates net revenues of \$560-\$600 million and adjusted earnings per share of 78-83 cents. Tax rate is expected to be 24%.

## Recent News

On **Jul 27, 2020**, Tetra Tech's board of directors approved the payout of a quarterly cash dividend of 17 cents per share to shareholders of record as of Aug 21, 2020. The dividend will be paid out on Sep 4, 2020.

On **Apr 22, 2020**, Tetra Tech announced that it clinched a \$90-million contract from the U.S. Air Force. The multiple-award deal will involve the company to offer environmental engineering support services to installations throughout Africa and Europe.

On **Apr 20, 2020**, Tetra Tech announced that it secured a contract from the U.S. Department of Defense. Per the \$300-million, multi-year contract, the company will be responsible for providing advanced analytics and high-end consulting services.

## Valuation

Tetra Tech shares are up 2.9% in the year-to-date period and increased 17.9% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Industrial Products sector are down 9.3% and 7.3% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry is up 3.2%, while the sector increased 7.5%.

The S&P 500 Index has moved up 1.7% year to date and increased 15.5% in the past year.

The stock is currently trading at 27.4x forward 12-month earnings per share, which compares to 24.4x for the Zacks sub-industry, 21.43x for the Zacks sector and 22.64x for the S&P 500 index.

Over the past five years, the stock has traded as high as 27.99x and as low as 12.46x, with a 5-year median of 19.22x. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$93 price target reflects 28.74x forward 12-month earnings per share.

The table below shows summary valuation data for TTEK.

Valuation Multiples - TTEK					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	27.4	24.4	21.43	22.64
	5-Year High	27.99	26.96	21.53	22.64
	5-Year Low	12.46	14.23	12.55	15.25
	5-Year Median	19.22	18.43	17.15	17.55
P/Sales F12M	Current	2.02	1.62	2.8	3.59
	5-Year High	2.1	1.67	2.8	3.59
	5-Year Low	0.75	0.8	1.52	2.53
	5-Year Median	1.27	1.29	2.03	3.04

As of 07/31/2020

## Industry Analysis Zacks Industry Rank: Top 40% (100 out of 253)



## Top Peers

Company (Ticker)	Rec	Rank
AECOM (ACM)	Neutral	3
Booz Allen Hamilton Holding Corporation (BAH)	Neutral	3
CECO Environmental Corp. (CECE)	Neutral	2
Casella Waste Systems, Inc. (CWST)	Neutral	2
Donaldson Company, Inc. (DCI)	Neutral	3
Exponent, Inc. (EXPO)	Neutral	3
ICF International, Inc. (ICFI)	Neutral	3
Leidos Holdings, Inc. (LDOS)	Neutral	3

Industry Comparison Industry: Pollution Control				Industry Peers		
	TTEK	X Industry	S&P 500	ACM	EXPO	ICFI
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	2	-	-	3	3	3
VGM Score	A	-	-	A	F	D
Market Cap	4.79 B	81.12 M	22.59 B	5.79 B	4.33 B	1.27 B
# of Analysts	3	2	14	3	2	3
Dividend Yield	0.77%	0.00%	1.83%	0.00%	0.90%	0.83%
Value Score	B	-	-	A	F	C
Cash/Price	0.03	0.15	0.07	0.19	0.04	0.05
EV/EBITDA	20.90	10.54	12.94	22.23	37.99	14.28
PEG Ratio	1.94	2.27	3.04	1.42	NA	1.88
Price/Book (P/B)	4.82	1.21	3.17	1.57	13.39	1.84
Price/Cash Flow (P/CF)	20.94	14.80	12.51	8.15	49.09	11.73
P/E (F1)	29.12	35.34	21.87	17.51	63.20	18.85
Price/Sales (P/S)	1.55	0.98	2.44	0.35	10.58	0.85
Earnings Yield	3.51%	1.35%	4.31%	5.72%	1.58%	5.31%
Debt/Equity	0.46	0.22	0.75	0.57	0.05	0.92
Cash Flow (\$/share)	4.23	0.09	6.94	4.44	1.71	5.76
Growth Score	A	-	-	C	F	D
Hist. EPS Growth (3-5 yrs)	18.50%	25.59%	10.85%	-3.33%	18.95%	12.65%
Proj. EPS Growth (F1/F0)	-1.89%	-23.77%	-7.75%	-24.85%	-13.07%	-13.57%
Curr. Cash Flow Growth	11.46%	8.18%	5.39%	-0.31%	19.56%	8.66%
Hist. Cash Flow Growth (3-5 yrs)	7.28%	14.42%	8.55%	15.22%	13.57%	9.89%
Current Ratio	1.31	1.76	1.31	1.23	3.81	1.65
Debt/Capital	31.63%	24.46%	44.32%	36.19%	4.78%	47.94%
Net Margin	4.56%	0.87%	10.44%	-2.63%	19.87%	4.30%
Return on Equity	18.03%	5.08%	14.73%	10.15%	23.68%	11.43%
Sales/Assets	1.35	0.96	0.52	1.15	0.77	1.01
Proj. Sales Growth (F1/F0)	-2.19%	0.00%	-1.95%	-36.26%	-4.34%	-0.32%
Momentum Score	B	-	-	B	C	D
Daily Price Chg	1.92%	0.00%	-0.92%	-1.21%	1.37%	1.15%
1 Week Price Chg	2.68%	0.00%	0.37%	-3.12%	-0.73%	-1.13%
4 Week Price Chg	10.77%	0.00%	3.81%	-0.82%	2.15%	3.89%
12 Week Price Chg	25.87%	7.53%	11.93%	2.96%	28.36%	4.05%
52 Week Price Chg	15.40%	-16.94%	-1.92%	3.64%	23.49%	-17.85%
20 Day Average Volume	235,364	32,890	1,887,986	731,516	186,028	119,523
(F1) EPS Est 1 week change	1.28%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	0.32%	0.00%	0.38%	0.00%	0.00%	0.00%
(F1) EPS Est 12 week change	2.60%	0.00%	-0.07%	8.58%	-6.34%	-8.50%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.16%	0.00%	0.00%	0.00%

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## 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.

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### 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>B</b>
Growth Score	<b>A</b>
Momentum Score	<b>B</b>
VGM Score	<b>A</b>

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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### Disclosures

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