

Tetra Tech Inc. (TTEK)

\$71.68 (As of 05/05/20)

Price Target (6-12 Months): **\$77.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 04/02/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:A

Value: B

Growth: A

Momentum: C

Summary

Tetra Tech's second-quarter fiscal 2020 earnings beat the Zacks consensus estimate by 1.4%, while sales missed the same by 1.6%. The company is currently focusing on high-end consulting and engineering services. Also, increased federal government spending and persistent solid demand for the company's services bode well for its businesses associated with the U.S. Federal, and the U.S. state and local clients. However, over the past three months, its shares have underperformed the industry. The company believes that the coronavirus outbreak-led market downturn and the volatile oil market will adversely impact its near-term results. Also, rising costs and expenses might be detrimental to its financials in the upcoming quarters. A stronger U.S. dollar might further depress the company's overseas business results in the quarters ahead.

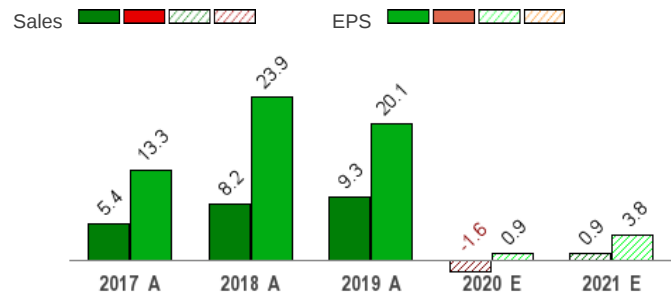
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$99.34 - \$63.61
20 Day Average Volume (sh)	318,323
Market Cap	\$3.9 B
YTD Price Change	-16.8%
Beta	0.88
Dividend / Div Yld	\$0.68 / 0.8%
Industry	Pollution Control
Zacks Industry Rank	Bottom 43% (145 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	1.4%
Last Sales Surprise	-1.6%
EPS F1 Est- 4 week change	-4.8%
Expected Report Date	07/29/2020
Earnings ESP	1.3%
P/E TTM	21.5
P/E F1	22.4
PEG F1	1.5
P/S TTM	1.2

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	581 E	593 E	610 E	621 E	2,390 E
2020	614 A	584 A	569 E	595 E	2,368 E
2019	553 A	585 A	623 A	640 A	2,406 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.78 E	\$0.72 E	\$0.86 E	\$0.92 E	\$3.32 E
2020	\$0.84 A	\$0.73 A	\$0.69 E	\$0.79 E	\$3.20 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.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 05/05/2020. The reports text is as of 05/06/2020.

Overview

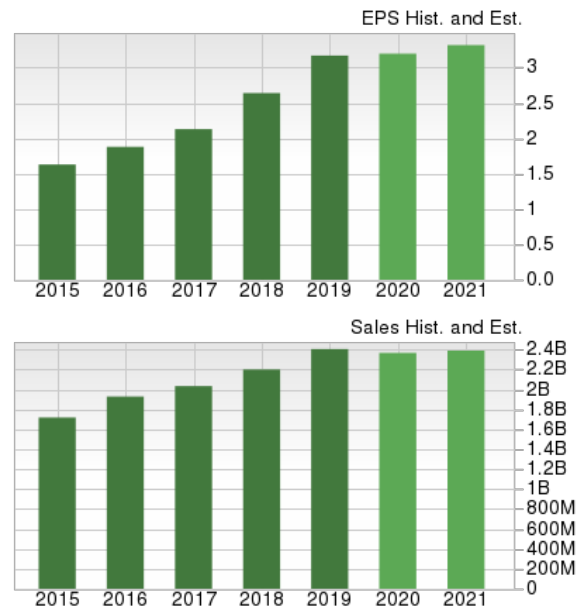
Headquartered in Pasadena, Tetra Tech is a leading provider of consulting, construction management, engineering, program management and technical services. It serves clients by providing cost-effective and innovative solutions on dealing with the fundamental needs for water, environmental and alternative 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 (54.9% revenues came from this segment in second-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 (45.1%): 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.



Reasons To Buy:

- ▲ In second-quarter fiscal 2020, Tetra Tech's earnings surpassed estimates by 1.4% and grew 4.3% from the year-ago quarter. The bottom-line results benefited from sales growth. The company 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.
- ▲ Tetra Tech's top-line performance in second-quarter fiscal 2020 was impressive, with adjusted revenues rising 2% year over year. Notably, net revenues were roughly flat year over year. Backlog at the end of the quarter grew 9% year over year to \$3.06 billion. Going forward, the company expects some of its businesses, associated with the U.S. Federal, and the U.S. state and local clients, to show resilience during the coronavirus-led global market downturn. This is due to the higher federal government spending, and persistent solid demand for the company's services related to water supply, wastewater treatment, watershed management and flood protection. Also, moving ahead, Tetra Tech expects to benefit from the strength across its renewable energy end market. Moreover, the company has been coordinating with its clients for adding new COVID-19-related services, and expand its scope of services and work, which will ultimately boost its top-line performance.
- ▲ 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 from the government, especially the U.S. Department of Defense, and commercial customers. The acquired assets will be integrated with Tetra Tech's Government Services Group.
- ▲ Tetra Tech has consistently returned significant cash to shareholders through dividends and share repurchases. During the second quarter of fiscal 2020, the company bought back shares worth \$60 million and distributed dividends totaling \$8.2 million. Notably, quarterly dividend rate was hiked by 13% in April 2020. Also, in January 2020, the company received the approval for a new \$200-million share buyback program. Exiting the fiscal second quarter, it is left with \$243 million of share repurchase authorization. Such diligent capital deployment strategies boost shareholders' wealth.

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

Reasons To Sell:

- ▼ Over the past three months, Tetra Tech's shares have lost 22.7% compared with the industry's decline of 21.4%. Also, on an EV/EBITDA (TTM) basis, the stock looks overvalued compared with the industry, with the respective tallies of 15.19x and 10.5x. Also, the company's current multiple is higher than the industry's three-month highest level of 13.36x. In addition to stock's overvaluation compared with the industry, lowered earnings estimates for the company make us cautious. Notably, on uncertainties, regarding the impacts of the coronavirus outbreak on financial and operating results, Tetra Tech withdrew its revenue and earnings guidance for fiscal 2020. In the past seven days, the consensus estimate for its earnings has declined 11.5% to 69 cents per share for the fiscal third quarter.
- ▼ Escalating costs have been concerning Tetra Tech over the past few quarters. For instance, the company's subcontractor costs and other cost of revenues (combined) rose 1.8% in the second quarter of fiscal 2020 from the year-ago comparable quarter. Also, selling, general and administrative expenses expanded 4.3%. We believe that unwarranted rise in costs and expenses might be detrimental to Tetra Tech's financials in the upcoming quarters. Moreover, 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 33% of Tetra Tech's revenues were generated from international operations in the second quarter of fiscal 2020. Notably, in the fiscal second quarter, adverse foreign currency translation impact hurt its revenues by \$6 million and earnings by about 1 cent per share. 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 is 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 addition, Tetra Tech expects an adverse impact on its businesses, associated with the U.S. commercial and international clients in the quarters ahead due to a weaker outlook for oil and gas capital expenditure, and the weakened demand environment, owing to the coronavirus-led market downturn.
- ▼ 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 second quarter of fiscal 2020, the metric was \$333 million, marking an increase of 3.3% on a sequential basis. Further, increase in debt levels can raise the company's financial obligations. In addition, the company's ability to meet its debt obligations based on its current income has declined over the past quarter. Notably, the company's times interest earned ratio is 12.3, lower than 12.5 recorded at the end of the previous quarter.

Concerns related to the U.S. commercial and international businesses, high costs, and headwinds related to international exposure might be concerning for Tetra Tech.

Last Earnings Report

Tetra Tech Q2 Earnings Surpass Estimates, Rise Y/Y

Tetra Tech reported mixed second-quarter fiscal 2020 (ended Mar 29, 2020) results, wherein earnings surpassed the Zacks Consensus Estimate but revenues lagged the same.

The company's adjusted earnings per share in the reported quarter were 73 cents, surpassing the Zacks Consensus Estimate of 72 cents. Also, its earnings grew 4.3% from the year-ago quarter's 70 cents on sales growth.

Quarter Ending **03/2020**

Report Date	Apr 29, 2020
Sales Surprise	-1.63%
EPS Surprise	1.39%
Quarterly EPS	0.73
Annual EPS (TTM)	3.34

Revenues & Segmental Performance

In the reported quarter, Tetra Tech generated adjusted revenues of \$734.1 million, reflecting year-over-year growth of 2%. Alternatively, net revenues (adjusted revenues minus subcontractor costs) were \$584.5 million, roughly flat year over year. Notably, the company's revenues missed the Zacks Consensus Estimate of \$594 million by 1.6%.

Backlog at the end of the quarter was \$3.06 billion, reflecting growth of 9% from the year-ago figure.

Revenues from the U.S. Federal customers accounted for 30% of the quarter's revenues. Conversely, the U.S. Commercial, and the U.S. State and Local sales accounted for 24% and 13% of the quarter's revenues, respectively. International sales accounted for 33% of the quarter's revenues.

The company reports revenues under the segments discussed below:

Net sales of Government Services Group were \$321 million, up 1.6% year over year.

Revenues from Commercial / International Services Group totaled \$263.5 million, reflecting a year-over-year decline of 3.8%.

Operating Margin

In the reported quarter, Tetra Tech's subcontractor costs totaled \$149.7 million, reflecting growth of 9.1% from the year-ago quarter. Other costs of revenues were \$487.5 million, down 0.3% year over year. Selling, general and administrative expenses were \$51 million, up 4.3% year over year.

Adjusted operating income in the reported quarter declined 3.5% year over year to \$52.6 million and adjusted margin decreased 20 basis points to 9%.

Balance Sheet and Cash Flow

Exiting the fiscal second quarter, Tetra Tech had cash and cash equivalents of \$135 million, down 11.8% from \$120.7 million recorded at the end of fiscal 2019. Long-term debt was up 3.3% sequentially to \$333 million.

In the first six months of fiscal 2020, the company generated net cash of \$83.2 million from operating activities, down 16.1% from the year-ago comparable period. Capital expenditure was \$5.9 million, down 18.1% year over year.

Shareholder-Friendly Policy

In the first six months of fiscal 2020, the company bought back shares worth \$81.7 million and distributed dividends totaling \$16.4 million.

Outlook

On uncertainties, regarding the impacts of the coronavirus outbreak on financial and operating results, Tetra Tech has withdrawn its revenue and earnings guidance for fiscal 2020.

Recent News

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.

On **Mar 5, 2020**, Tetra Tech announced that it secured a contract from the United States Postal Services. Per the \$125-million, multi-year contract, the company will be responsible for providing emergency and response services.

On **Feb 28, 2020**, Tetra Tech's paid out a quarterly dividend of 15 cents per share to shareholders of record as of Feb 12. Also, On Jan 27, 2020, the company received approval for a new \$200-million share buyback program.

On **Feb 25, 2020**, Tetra Tech announced that it acquired Arlington, VA-based Segue Technologies, Inc. Financial terms of the transaction were kept under wraps.

Segue specializes in providing management consultancy, IT solutions and cybersecurity to customers, including commercial, non-profit and government. The firm's government clients include the U.S. Air Force, the U.S. Navy and the U.S. Marine Corps. It employs more than 200 people.

Details of Buyout: Per Tetra Tech, the buyout of Segue will strengthen its ability to better serve customers with innovative techniques — including enterprise-wide software applications, advanced data analytics and cloud services. In addition, the buyout is predicted to solidify Tetra Tech's business from the government, especially the U.S. Department of Defense and commercial customers.

The company will integrate Segue with its Government Services Group.

Valuation

Tetra Tech shares are down 16.8% in the year-to-date period but increased 6.4% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Industrial Products sector are down 21.8% and 23.2% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and the sector are down 11.7% and 19.5%, respectively.

The S&P 500 Index has moved down 11.8% in the year-to-date period and 1.7% in the past year.

The stock is currently trading at 21.81x forward 12-month earnings per share, which compares to 20.94x for the Zacks sub-industry, 17.72x for the Zacks sector and 20.36x for the S&P 500 index.

Over the past five years, the stock has traded as high as 27.2x and as low as 12.46x, with a 5-year median of 18.9x. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$77 price target reflects 23.43x 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	21.81	20.94	17.72	20.36
	5-Year High	27.2	22.47	19.93	20.36
	5-Year Low	12.46	14.23	12.55	15.19
	5-Year Median	18.9	18.29	16.56	17.44
EV/EBITDA F12M	Current	15.22	10.72	16.39	12.29
	5-Year High	18.41	10.72	18.05	12.64
	5-Year Low	6.88	5.16	10.56	9.09
	5-Year Median	10.91	7.82	14.08	10.82
EV/Sales F12M	Current	1.86	1.37	2.31	2.59
	5-Year High	2.27	1.94	3.12	3.52
	5-Year Low	0.8	0.86	1.76	2.3
	5-Year Median	1.32	1.37	2.29	2.81

As of 05/05/2020

Industry Analysis Zacks Industry Rank: Bottom 43% (145 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
Booz Allen Hamilton Holding Corporation (BAH)	Outperform	3
AECOM (ACM)	Neutral	4
Advanced Emissions Solutions, Inc. (ADES)	Neutral	4
CECO Environmental Corp. (CECE)	Neutral	2
Casella Waste Systems, Inc. (CWST)	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)	3	-	-	4	3	3
VGM Score	A	-	-	F	C	A
Market Cap	3.87 B	29.05 M	19.65 B	5.60 B	3.40 B	1.32 B
# of Analysts	4	3	14	3	2	3
Dividend Yield	0.84%	0.00%	2.18%	0.00%	1.15%	0.80%
Value Score	B	-	-	F	F	B
Cash/Price	0.03	0.14	0.06	0.13	0.04	0.00
EV/EBITDA	17.50	10.50	11.77	27.16	29.54	12.31
PEG Ratio	1.49	2.99	2.49	1.50	NA	1.78
Price/Book (P/B)	4.08	1.00	2.64	1.45	10.51	1.84
Price/Cash Flow (P/CF)	16.93	14.58	10.48	7.95	38.52	12.14
P/E (F1)	22.38	43.61	19.10	18.55	49.59	17.84
Price/Sales (P/S)	1.21	0.93	2.00	0.34	8.02	0.88
Earnings Yield	4.46%	2.22%	4.99%	5.38%	2.02%	5.60%
Debt/Equity	0.57	0.22	0.74	0.87	0.05	0.40
Cash Flow (\$/share)	4.23	0.09	7.01	4.44	1.71	5.76
Growth Score	A	-	-	F	A	B
Hist. EPS Growth (3-5 yrs)	18.50%	29.67%	10.87%	-2.37%	18.95%	13.01%
Proj. EPS Growth (F1/F0)	0.87%	2.16%	-9.07%	-30.79%	-13.07%	-5.54%
Curr. Cash Flow Growth	11.46%	18.75%	5.88%	-0.31%	19.56%	8.66%
Hist. Cash Flow Growth (3-5 yrs)	7.28%	13.48%	8.55%	15.22%	13.57%	9.89%
Current Ratio	1.36	1.45	1.24	1.16	3.81	1.29
Debt/Capital	36.46%	23.43%	44.07%	46.53%	4.78%	28.49%
Net Margin	4.52%	1.16%	11.00%	-2.63%	20.28%	4.30%
Return on Equity	18.64%	4.20%	16.39%	9.89%	25.03%	11.43%
Sales/Assets	1.43	1.00	0.55	1.12	0.80	1.06
Proj. Sales Growth (F1/F0)	-1.44%	0.00%	-2.17%	-37.47%	-4.34%	3.85%
Momentum Score	C	-	-	D	D	B
Daily Price Chg	1.26%	0.00%	0.74%	2.62%	0.23%	-1.07%
1 Week Price Chg	-3.78%	0.19%	0.53%	3.09%	-4.86%	4.41%
4 Week Price Chg	-4.67%	6.70%	6.47%	20.48%	-6.81%	-0.10%
12 Week Price Chg	-25.45%	-19.69%	-20.68%	-25.47%	-15.08%	-19.89%
52 Week Price Chg	6.35%	-28.57%	-10.95%	6.61%	17.58%	-8.43%
20 Day Average Volume	318,323	18,603	2,492,530	1,800,203	263,617	92,788
(F1) EPS Est 1 week change	-0.31%	0.00%	0.00%	0.00%	-9.52%	0.00%
(F1) EPS Est 4 week change	-4.84%	0.00%	-7.39%	-26.80%	-17.22%	-5.01%
(F1) EPS Est 12 week change	-8.84%	-47.53%	-14.21%	-21.92%	-16.70%	-14.54%
(Q1) EPS Est Mthly Chg	-17.50%	0.00%	-13.52%	-24.59%	-45.00%	-7.93%

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	C
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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