Is Terex the right Industrial sector stock to own to ride the economic recovery?





Valuation Master Class



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Is Terex the right Industrial sector stock to own to ride the economic recovery?





Sector: Industrials



Among the world's largest manufacturers of aerial work platforms and materials processing machineries

Sources: A. Stotz Investment Research, Refinitiv

My value estimate:

US\$48

(Upside 14%)

BUY



3 things to know about this company

- Heavy gov't spending on infrastructure drives top-line growth
- Costs cuts to drive sustainably higher margins
- Strong ROE and ROIC might be overlooked by the market

Key statistics

Analyst consensus (16)

PE ratio

Dividend yield

US\$59

(**Upside 39%**)

12x

0.6%

BUY

Revenue breakdown 2020



Sales

Story

FVMR

Value

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Risks

Elevation platforms 40%



Specialty equipment 16%



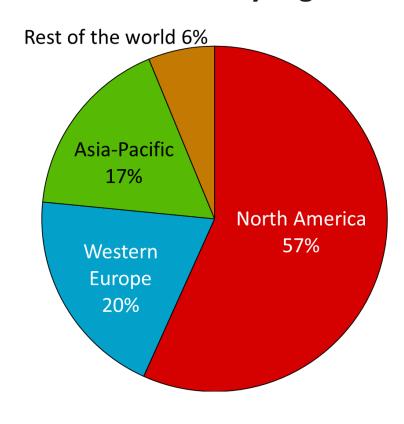
Material processing 25%



Others 19%

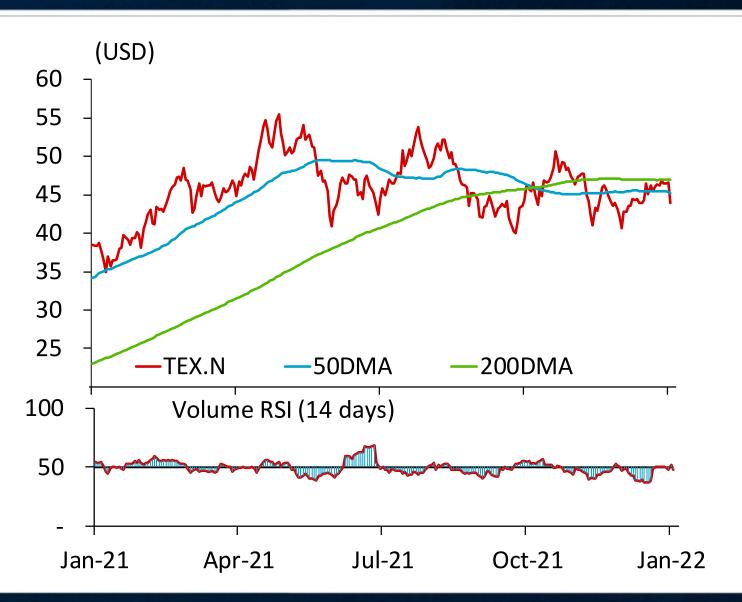


Breakdown by region



Sideward movement could last much longer



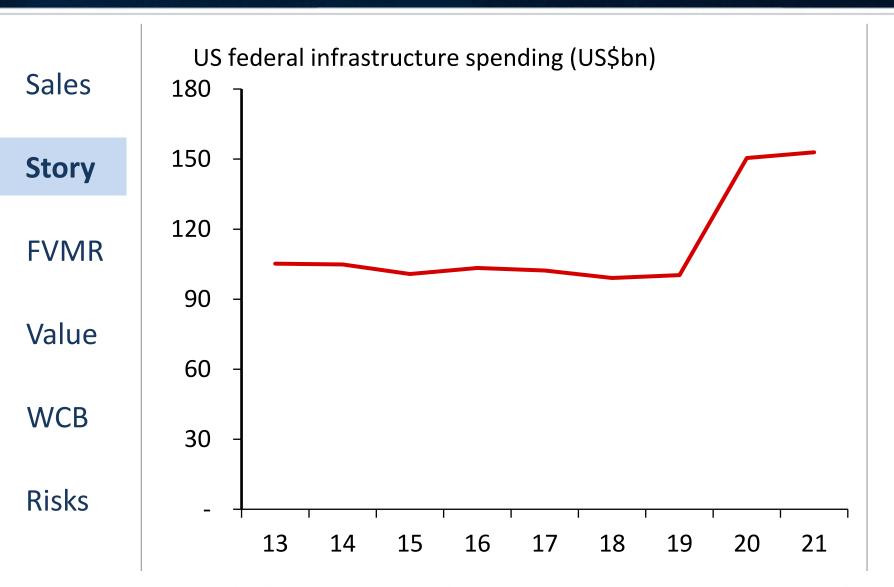


- Throughout the past year, the stock price mainly moved sideward
 - Since 3Q21, the 50DMA moved in line with 200DMA, providing no clear signal yet
- Volume RSI has been weak recently
 - Currently, it is at the 50%-line, which also does not help to derive a meaningful conclusion



Heavy gov't spending on infrastructure drives top-line growth



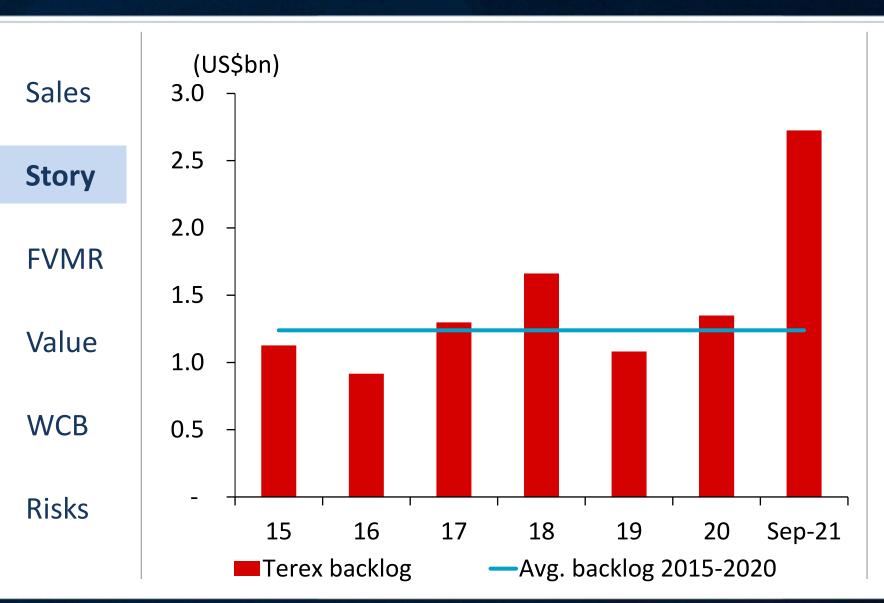


- Most of Terex customers are dependent on gov't funding for infrastructure projects, e.g., highway construction
- The US gov't has increased its spending by over 50% in 2020 and 2021 compared to previous years
 - The heightened level of spending is likely to stay over the next few years, providing good growth opportunities for the industrials sector

Near-term strength already reflected in backlog

Sources: A. Stotz Investment Research, company data



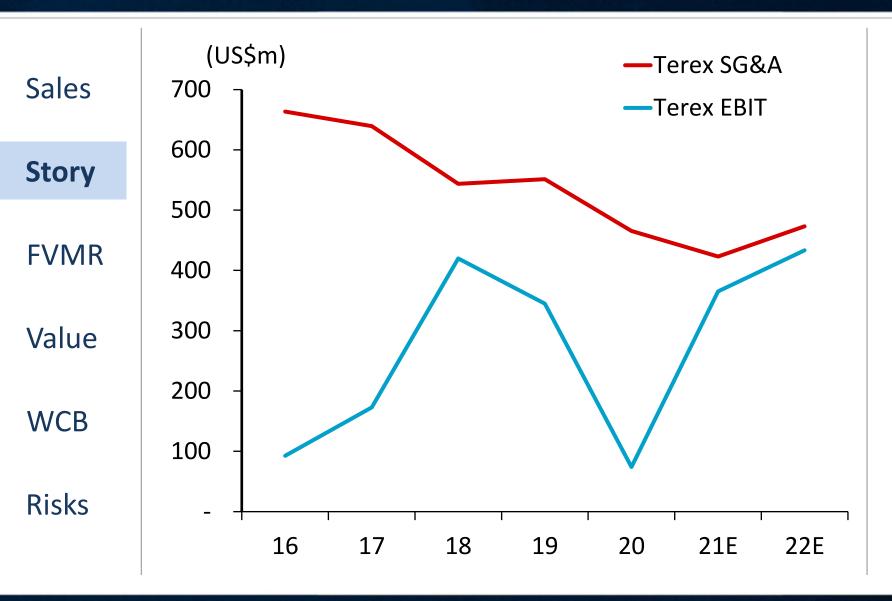


- In 3Q21, Terex's backlog stood at US\$2.7bn, which is double than the average backlog of previous years
 - Therefore, I expect strong revenue growth in the upcoming 3 years



Costs cuts to drive sustainably higher margins

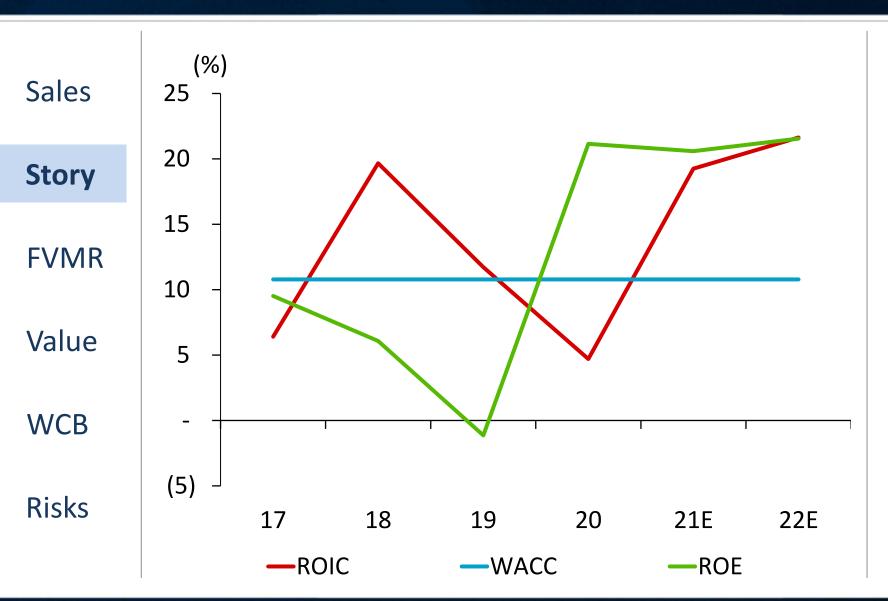




- Terex continued its efforts to reduce its costs and drive its margin closer to the level of its competitors
 - Therefore, the management considered divestments of inefficient business
 - In 2019, Terex sold its crane business
- The efforts start to pay off as the operating profit achieves a higher level
 - I see some more room for the operating profit to expand

Strong ROE and ROIC might be overlooked by the market





- Both ROIC and ROE could climb up to 20% in 21E
- The company needs to prove itself to maintain such a heightened level of profitability
 - If the company is able to do so, it could be a key catalyst for a re-rating
 - Given the strong demand outlook, I believe that the market should be more optimistic about the profit growth



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FVMR Scorecard

- Measures a stock's
 attractiveness relative to all
 other companies
- * Attractiveness is based on four elements
 - Fundamentals, Valuation,
 Momentum, and Risk
- *Scale from 1 (Best) to 10 (Worst)



Strong fundamentals in a cyclical industry



Sales

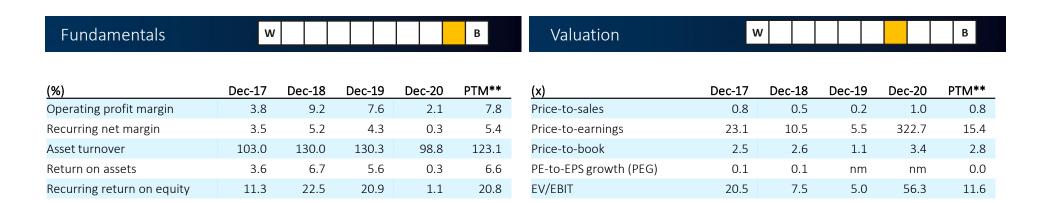
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W				В	Risk	W				В
Dec-17	Dec-18	Dec-19	Dec-20	PTM**	<u>(x)</u>	Dec-17	Dec-18	Dec-19	Dec-20	PTM**
(1.8)	3.5	(3.6)	(29.3)	16.0	Current ratio	2.3	2.0	2.3	2.6	2.1
276.0	88.4	(14.4)	(94.5)	1,438.0	Net debt-to-equity (%)	29.4	101.8	68.7	55.2	32.4
179	543	(160)	(546)	599	Times-interest-earned	2.4	5.7	3.8	1.0	5.1
6mth	3mth	1mth	3wk	1wk		5yr	3yr	1yr	6mth	3mth
(18.6)	(12.4)	(9.2)	(12.7)	(4.4)	Beta	1.5	1.5	2.0	2.9	2.0
	Dec-17 (1.8) 276.0 179 6mth	Dec-17 Dec-18 (1.8) 3.5 276.0 88.4 179 543 6mth 3mth	Dec-17 Dec-18 Dec-19 (1.8) 3.5 (3.6) 276.0 88.4 (14.4) 179 543 (160) 6mth 3mth 1mth	Dec-17 Dec-18 Dec-19 Dec-20 (1.8) 3.5 (3.6) (29.3) 276.0 88.4 (14.4) (94.5) 179 543 (160) (546) 6mth 3mth 1mth 3wk	Dec-17 Dec-18 Dec-19 Dec-20 PTM** (1.8) 3.5 (3.6) (29.3) 16.0 276.0 88.4 (14.4) (94.5) 1,438.0 179 543 (160) (546) 599 6mth 3mth 1mth 3wk 1wk	Dec-17 Dec-18 Dec-19 Dec-20 PTM** (x) (1.8) 3.5 (3.6) (29.3) 16.0 Current ratio 276.0 88.4 (14.4) (94.5) 1,438.0 Net debt-to-equity (%) 179 543 (160) (546) 599 Times-interest-earned 6mth 3mth 1mth 3wk 1wk	Dec-17 Dec-18 Dec-19 Dec-20 PTM** (x) Dec-17 (1.8) 3.5 (3.6) (29.3) 16.0 Current ratio 2.3 276.0 88.4 (14.4) (94.5) 1,438.0 Net debt-to-equity (%) 29.4 179 543 (160) (546) 599 Times-interest-earned 2.4 6mth 3mth 1mth 3wk 1wk 5yr	Dec-17 Dec-18 Dec-19 Dec-20 PTM** (x) Dec-17 Dec-18 (1.8) 3.5 (3.6) (29.3) 16.0 Current ratio 2.3 2.0 276.0 88.4 (14.4) (94.5) 1,438.0 Net debt-to-equity (%) 29.4 101.8 179 543 (160) (546) 599 Times-interest-earned 2.4 5.7 6mth 3mth 1mth 3wk 1wk 5yr 3yr	Dec-17 Dec-18 Dec-19 Dec-20 PTM** (x) Dec-17 Dec-18 Dec-18 Dec-19 (1.8) 3.5 (3.6) (29.3) 16.0 Current ratio 2.3 2.0 2.3 276.0 88.4 (14.4) (94.5) 1,438.0 Net debt-to-equity(%) 29.4 101.8 68.7 179 543 (160) (546) 599 Times-interest-earned 2.4 5.7 3.8 6mth 3mth 1mth 3wk 1wk - 5yr 3yr 1yr	Dec-17 Dec-18 Dec-19 Dec-20 PTM** (x) Dec-17 Dec-18 Dec-19 Dec-19 Dec-20 (1.8) 3.5 (3.6) (29.3) 16.0 Current ratio 2.3 2.0 2.3 2.6 276.0 88.4 (14.4) (94.5) 1,438.0 Net debt-to-equity(%) 29.4 101.8 68.7 55.2 179 543 (160) (546) 599 Times-interest-earned 2.4 5.7 3.8 1.0 6mth 3mth 1mth 3wk 1wk 5yr 3yr 1yr 6mth

Note: Benchmarking against 2,160 non-financial companies in USA.

Recently, I created a short online course explaining my FVMR investing approach

I usually sell it for \$97 but for a limited time I am offering it for FREE





Consensus sees strong upside



Sales

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Analyst consensus valuation				
Recommendation	Oct-21	Nov-21	Dec-21	Current
Strong buy	4	4	4	4
Buy	5	5	5	5
Hold	6	6	6	6
Sell	-	1	1	1
Strong sell	-	-	-	-
Average score	2.3	2.3	2.3	2.2

Price target	Oct-21	Nov-21	Dec-21	Current
Median	55	59	59	59
Mean	56	57	57	57

2.5

16 analysts



Upside: 39%

Analyst consensus 3-year forecast (%) 20 18 19 **21E 22E 23E** Revenue growth 2.5 (3.6)(29.3)25.3 14.8 8.9 Gross margin 21.3 20.6 17.5 19.9 20.5 21.6 **EBIT** margin 2.4 8.3 9.4 9.3 7.9 10.4

(0.3)

5.2

1.2

- The majority of analysts issued a BUY recommendation, while 6 analysts recommend a HOLD
- Consensus expects strong revenue prospects, and a rising margin
 - Considering growing infrastructure spending, the company could realize the targets

6.6

7.5

Net margin

Profit & loss statement



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(YE Dec, US\$ m)	2019A	2020A	2021E	2022E
Revenue	4,353	3,076	3,846	4,422
Cost of goods & services	(3,457)	(2,537)	(3,057)	(3,516)
Gross profit	896	539	788	907
SG&A	(551)	(465)	(423)	(473)
Other operating (exp)/inc	(0)	(0)	-	-
EBIT	345	74	365	433
Interest expense (net)	(81)	(62)	(52)	(45)
Other non-operating inc/(exp)	(12)	5	-	-
Earnings before taxes (EBT)	251	17	313	389
Income tax	(38)	(2)	(60)	(76)
Earnings after taxes (EAT)	213	15	253	313
Equity income/Minority interest	-	-	_	-
Earnings from cont. operations	213	15	253	313
Forex/Exceptionals before tax	(159)	(25)	(26)	(27)
Net profit	54	(11)	227	286

The company is likely to turnaround its loss in 2020 and recognize strong profits in 21E and 22E

Balance sheet - assets



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(YE Dec, US\$ m)	2019A	2020A	2021E	2022E
Cash & short-term investments	535	665	491	589
Accounts receivable	402	381	502	565
Inventories	848	610	713	820
Other current assets	235	222	192	221
Total current assets	2,020	1,879	1,899	2,196
Long-term investments	-	-	-	-
Net fixed assets	512	510	528	548
Intangible assets	10	8	13	12
Goodwill	270	275	281	287
Other long-term assets	384	360	364	367
Total assets	3,196	3,032	3,084	3,410

★ Significant increases in inventories and receivables as sales volume likely to ramp up as shown by the strong backlog

Balance sheet - liabilities



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(YE Dec, US\$ m)	2019A	2020A	2021E	2022E
Overdrafts & short-term loans	7	8	9	9
Accounts payable	608	504	637	703
Other current liabilities	257	212	250	287
Total current liabilities	872	723	896	999
Long-term debt	1,169	1,166	872	845
Other long-term liabilities	222	221	201	203
Total liabilities	2,263	2,110	1,968	2,047
Minority interest	-	-	-	-
Paid-up capital - Common shares	825	839	839	839
Paid-up capital - Preferred shares	-	-	-	-
Retained earnings	771	750	945	1,191
Revaluation/Forex/Others	(664)	(668)	(668)	(668)
Total equity	932	922	1,116	1,362
Total liab & shareholders' equity	3,196	3,032	3,084	3,410

- ★ The company started to reduce its long-term debt
 - In 3Q21, its net debt-toequity ratio stood at 0.3x, compared to 0.6x in 2020



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(YE Dec)	2019A	2020A	2021E	2022E
General growth (YoY, %)				
Revenue	(3.6)	(29.3)	25.0	15.0
Assets	(8.3)	(5.1)	1.7	10.6
Gross profit	(7.0)	(39.8)	46.2	15.0
Operating profit	(17.9)	(78.6)	394.3	18.6
Attributable profit	(52.2)	(119.5)	nm	26.2
EPS	(48.7)	(119.6)	nm	26.2
Recurring EPS	(26.3)	(90.0)	nm	24.2
Du Pont analysis (%)				
Net profit margin	1.2	(0.3)	5.9	6.5
Revenue per US\$100 of assets	130.3	98.8	125.8	136.2
Assets/equity (x)	3.7	3.4	3.0	2.6
Return on equity	6.1	(1.1)	22.3	23.1

★ The company is characterized by a strong efficiency, which also boosts future return on equity

Ratios (cont.)



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(YE Dec)	2019A	2020A	2021E	2022E
Internal liquidity (x)				
Current ratio	2.3	2.6	2.1	2.2
Quick, or acid test ratio	1.3	1.8	1.3	1.4
Working cap. mgmt (Days)				
Inventory conversion period	92	103	78	79
Receivables collection period	39	46	41	43
Days from raw mat to coll	131	149	119	122
Payables deferral period	74	79	67	69
Cash conversion cycle	57	70	52	53
Profitability ratios (%)				
Gross profit margin	20.6	17.5	20.5	20.5
EBIT margin	7.9	2.4	9.5	9.8
EBIT return on avg assets	10.3	2.4	11.9	13.3
Return on average assets	1.6	(0.3)	7.4	8.8
Financial risk (x)				
Liabilities-to-assets (%)	70.8	69.6	63.8	60.0
Debt-to-equity	1.3	1.3	0.8	0.6
Net debt-to-equity	0.7	0.6	0.3	0.2
Times-interest-earned	4.5	1.9	7.6	10.5
Effective interest rate (%)	7.4	5.6	5.5	5.5

★ With the increased focus on its most profitable products, Terex could return to a gross margin above 20%, with further room to improve over time

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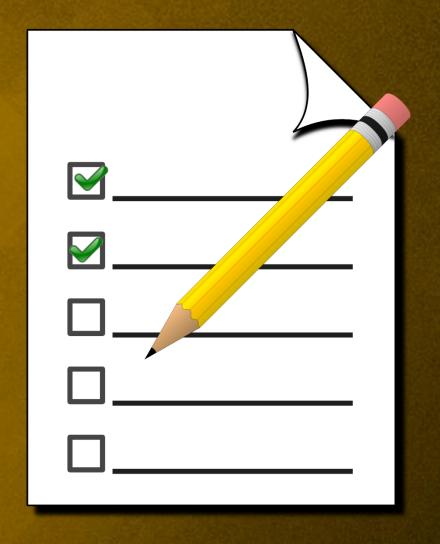
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A. Stotz Investment Research
Stock Picking Checklist

*Inspired by Peter Lynch's ten baggers (A stock that has gone up 10x)

- * Based on our extensive research
- * 9 factors that drive long-term share price performance



Long-term share price performance potential



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A. Stotz Investment Research			Good
Stock Picking Checklist	Potential	Comment	
1. Management – Management has a proven commitment to growth	Weak	Revenue steadily declined between 2015 and 2 management focus is on profitability	2020;
2. Growth – Product and industry can support a decade of 10%+ annual growth	Moderate	Industry is cyclical and is likely to grow roughly with global GDP	in line
3. Sustainable – Competitive strategy creates sustainably high gross margin	Weak	Competition is intense and existing players are challenged by low-cost manufacturers from Chi	
4. Quality – Good earnings quality, non-core items are small or non-existent	Weak	High fluctuations; net profit has been negative 2016 and 2020	in
5. Efficiency – In the long run sales grow faster than assets	Good	The company is characterized by a high efficien asset turnover is above 120%	ncy;
6. Tight – Relatively low cash conversion cycle, negative is best	Moderate	Cash conversion is relatively high and stood at a days in 2020	70
7. Cash flow – Operating cash flow is consistently positive	Moderate	Operating cash flows fluctuated a lot but were to cover investing outflows	able
8. Capacity – Company has access to capital to fund growth	Good	The company continued to reduce its debt (net to-equity ratio stood at 0.3x in 3Q21	t debt-
9. Inexpensive – Valuation is reasonable, avoid very expensive stocks	Good	Trades cheap on both 21E PE and PB compared Industrials companies, and in line with ROE	to US

Free cash flow



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(YE Dec, US\$ m)	2018A	2019A	2020A	2021E	2022E
EBIT	420	345	74	365	433
Est tax rate (%)	26	41	-	21	21
NOPAT	311	203	74	289	342
Add: Depre & amort	60	50	50	62	67
Less: CAPEX	(102)	(105)	(62)	(77)	(84)
Chg in A/R	45	133	21	(121)	(63)
Chg in inventory	51	71	237	(103)	(107)
Chg in oth curr assets	(423)	395	13	30	(29)
Chg in A/P	14	(202)	(104)	133	66
Chg in oth curr liabs	167	(143)	(45)	38	37
Less: Chg in working cap	(147)	254	121	(23)	(95)
Less: Chg in invest cap					
Free cash flow to firm	122	402	183	251	231

★ FCFF has been consistently positive, and there is no reason to assume differently in the future

Value estimate



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Forecast assumptions		
3-year average	Consensus I	My assumptions
Revenue growth (CAGR)	16.1	15.8
Gross margin	20.7	20.8
EBIT margin	9.3	10.0
Net margin	6.4	6.6

My valuation method		
Market: United States of America		
Market risk-free rate	2.5	
Market equity risk premium	9.0	
Market return	11.5	
Company beta (x)	1.3	Valuation Method:
COE	13.8	FCFF
WACC	11.1	
Terminal growth rate	3.0	

- Similar to consensus, I expect strong revenue and a margin improvement
 - Terex is likely to ride the demand wave induced by gov't infrastructure support
- ★ The company is highly cyclical reflected in the above-average beta of 1.25x

Value estimate



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Bear **US\$44** (Upside 3%)



Base **US\$48** (Upside 14%)



Bull **US\$54**

(Upside 27%)



World Class Benchmarking Scorecard

- We identify a company's competitive position relative to global peers
- * We use a composite rank of profitability and growth, called "Profitable Growth"
- Scale from 1 (Best) to 10 (Worst)



Strong profitability and growth rebound



Sales

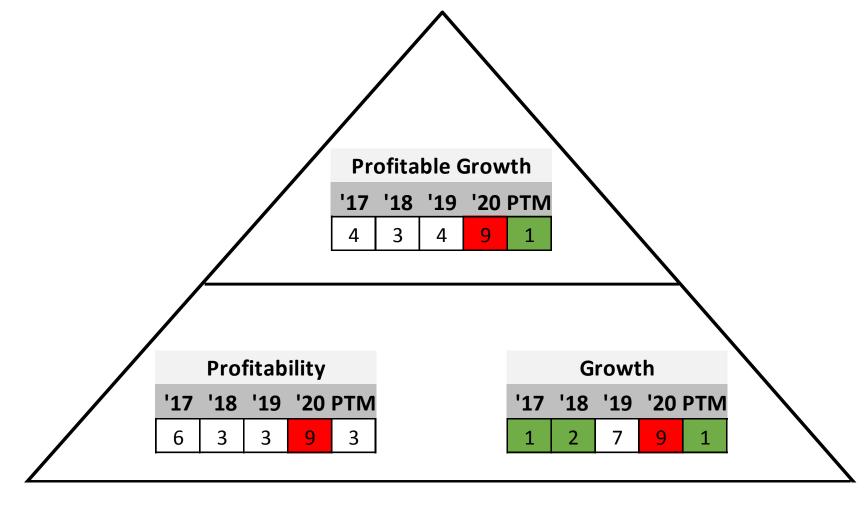
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Benchmarked against 1,480 large Industrials companies worldwide.

Key risk is intensified price competition



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- ★ Low-cost competitors from China could result in loss of customers
- ★ Its customers are dependent on gov't spending
- ★ Dependency on suppliers can lead to volatile margin

CONCLUSION

- Ramp up of gov't infrastructure spending makes it worth to look at industrial companies
- Terex has room to expand its margin, making it a profitable growth play
- Valuation is relatively cheap, trading at a 50% discount

