

Jacobs Eng.

Mixed results: cleaner story likely to prevail yet requires a ramp through FY24

Reiterate Rating: NEUTRAL | PO: 145.00 USD | Price: 139.91 USD

Kicks off 2024 with a mixed print, yet reaffirms FY guide

In our view, Q1 results were mixed: EBITDA of \$328mn was down 3.1% YoY (flat excl. inventory write down), P&PS margin fell 125bps YoY (partly on shift in corporate unallocated costs), PA Consulting margin fell 30bps YoY. Yet at end of day, backlog up 5% YoY (gross margin up 29bps YoY), shift in costs to P&PS positive l-term (cost recovery from public sector clients), plans to spin off & combine CMS remain on track, and Jacobs reaffirmed its FY24 guidance (i.e., midpoint EBITDA/EPS growth +9/10%).

FY24 is a bit 2H weighted...yet positive exit rate into '25

FY24 guidance remains more 2H weighted. While achievable, investors likely to monitor how momentum builds: i) P&PS margin of 13.7% in Q1 vs FY guide of >14.6% in FY24 (slightly above FY23). ii) PA Consulting margin 17.8% in Q1 vs FY guide of 20%, as utilization rates recover and costs optimization likely result in positive exit rates in '25.

RemainCo backlog continues to build, observe momentum

Backlog of \$29.6bn increased 5% YoY. Book-to-bill was 1.12x with gross profit in the backlog up over 6% YoY. J highlighted two key growth drivers – water (with bookings up 30% YoY - traditionally higher margin business) and cities & places (for e.g., built environment business bookings). While the UK has been facing some challenges with election uncertainty (transportation pipeline), J noted that the US feels more secure given legislation. J also highlighted life sciences as a strong growth area around GLP-1 facilities and semiconductors as it sees the chip manufacturing market on the upswing.

FCF a clear bright spot

FQ1 FCF of \$401mn was up 48% YoY. Net leverage of 1.2x – targeting to remain investment grade. In our view, a RemainCo Jacobs is likely to be cash generative and capital allocation to pivot away from years of M&A building to shareholder returns.

Reiterate Neutral

We update estimates post FQ1. We raise our PO to \$145 (\$137 prior) based on 12.5x 2024 EBITDA (12x prior), as we believe a higher multiple warranted given the strong backlog. Reit. Neutral – prefer J's strategy to streamline into cleaner story yet path likely a bit bumpy. Continue to prefer Buy-rated ACM as a cleaner way to invest in infrastructure for now.

Estimates (Sep) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	6.93	7.11	8.10	9.05	10.10
GAAP EPS	4.98	5.30	7.44	9.05	10.10
EPS Change (YoY)	10.2%	2.6%	13.9%	11.7%	11.6%
Consensus EPS (Bloomberg)			8.07	9.02	10.20
DPS	0.92	1.04	1.16	1.30	1.46
Valuation (Sep)					
P/E	20.2x	19.7x	17.3x	15.5x	13.9x
GAAP P/E	28.1x	26.4x	18.8x	15.5x	13.9x
Dividend Yield	0.7%	0.7%	0.8%	0.9%	1.0%
EV / EBITDA*	16.9x	16.2x	14.4x	13.5x	12.5x
Free Cash Flow Yield*	1.8%	4.2%	5.1%	5.7%	6.5%

* For full definitions of *IQmethod*SM measures, see page 4.

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Timestamp: 07 February 2024 05:00AM EST

07 February 2024

Equity

Key Changes

(US\$)	Previous	Current
Price Obj.	137.00	145.00
2024E Rev (m)	14,227.1	14,194.9
2025E Rev (m)	14,948.8	14,914.5
2026E Rev (m)	15,635.2	15,598.8
2025E EPS	9.25	9.05
2026E EPS	10.20	10.10
2024E DPS	1.11	1.16

Michael Feniger

Research Analyst

BofAS

+1 646 855 1923

michael.feniger@bofa.com

Sherif El-Sabbahy

Research Analyst

BofAS

sherif.el-sabbahy@bofa.com

Nandita Nayar

Research Analyst

BofAS

nandita.nayar@bofa.com

Stock Data

Price	139.91 USD
Price Objective	145.00 USD
Date Established	7-Feb-2024
Investment Opinion	B-2-7
52-Week Range	109.00 USD - 143.93 USD
Mkt Val (mn) / Shares Out (mn)	20,133 USD / 143.9
Free Float	98.8%
Average Daily Value (mn)	110.52 USD
BofA Ticker / Exchange	J / NYS
Bloomberg / Reuters	J US / J.N
ROE (2024E)	15.1%
Net Dbt to Eqty (Sep-2023A)	31.8%
ESGMeter™	High

ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BofA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to "BofA ESGMeter Methodology".

CMS = Critical Mission Solutions,
P&PS = People & Places Solutions,
GLP-1 = Glucagon-like peptide-1, l-term = long term

iQprofileSM Jacobs Eng.

iQmethodSM – Bus Performance*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Return on Capital Employed	8.9%	9.7%	10.5%	10.8%	11.0%
Return on Equity	15.0%	14.3%	15.1%	15.4%	15.4%
Operating Margin	10.5%	10.7%	11.1%	11.4%	11.7%
Free Cash Flow	356	839	1,032	1,146	1,306

iQmethodSM – Quality of Earnings*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash Realization Ratio	0.5x	1.1x	1.1x	1.1x	1.2x
Asset Replacement Ratio	1.2x	1.3x	1.3x	1.2x	1.2x
Tax Rate	21.1%	22.4%	22.0%	22.0%	22.0%
Net Debt-to-Equity Ratio	39.6%	31.8%	21.2%	10.6%	-0.1%
Interest Cover	13.7x	10.1x	11.2x	12.6x	14.1x

Income Statement Data (Sep)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Sales	12,496	13,356	14,195	14,914	15,599
% Change	6.7%	6.9%	6.3%	5.1%	4.6%
Gross Profit	3,327	3,473	4,147	4,384	4,626
% Change	9.3%	4.4%	19.4%	5.7%	5.5%
EBITDA	1,364	1,425	1,597	1,710	1,836
% Change	9.7%	4.5%	12.1%	7.1%	7.3%
Net Interest & Other Income	(46)	(159)	(143)	(135)	(130)
Net Income (Adjusted)	897	904	1,027	1,134	1,246
% Change	8.7%	0.8%	13.6%	10.4%	9.9%

Free Cash Flow Data (Sep)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Income from Cont Operations (GAAP)	1,001	988	1,112	1,219	1,326
Depreciation & Amortization	301	307	317	317	317
Change in Working Capital	(803)	(146)	(88)	(165)	(117)
Deferred Taxation Charge	NA	NA	NA	NA	NA
Other Adjustments, Net	(24)	(175)	(168)	(85)	(80)
Capital Expenditure	(118)	(136)	(140)	(140)	(140)
Free Cash Flow	356	839	1,032	1,146	1,306
% Change	-43.8%	135.3%	23.1%	11.0%	14.0%
Share / Issue Repurchase	(231)	(218)	(300)	(300)	(300)
Cost of Dividends Paid	0	0	0	0	0
Change in Debt	719	(634)	0	0	0

Balance Sheet Data (Sep)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash & Equivalents	1,140	927	1,525	2,207	3,033
Trade Receivables	3,405	3,559	3,391	3,435	3,525
Other Current Assets	176	205	205	205	205
Property, Plant & Equipment	347	357	390	413	435
Other Non-Current Assets	9,592	9,570	9,360	9,160	8,960
Total Assets	14,660	14,617	14,871	15,419	16,158
Short-Term Debt	201	214	214	214	214
Other Current Liabilities	3,050	3,209	2,953	2,831	2,805
Long-Term Debt	3,357	2,813	2,813	2,813	2,813
Other Non-Current Liabilities	1,948	1,781	1,781	1,781	1,781
Total Liabilities	8,556	8,017	7,761	7,639	7,613
Total Equity	6,104	6,600	7,096	7,766	8,532
Total Equity & Liabilities	14,660	14,617	14,857	15,406	16,145

* For full definitions of iQmethodSM measures, see page 4.

Company Sector

Engineering & Construction

Company Description

Jacobs Engineering is ranked as the largest architectural & engineering design firm in the world. The portfolio consists of two main segments - PPS (People & Places Solutions) and CMS (Critical Mission Solutions) - providing a wide range of services for government agencies, municipalities, and industrial customers.

Investment Rationale

The Jacobs of today is very different from the Jacobs of last cycle, having undergone strategic changes under the helm of new management: Operational improvements, acquisitions (CH2M, KeyW), and the divestment of ECR (Energy, Chemicals, and Resources). These changes have created a less cyclical, higher return portfolio along with a strong balance sheet. That said, we see risk of less valuation upside as the market rotates to more cyclical sectors.

Stock Data

Average Daily Volume 789,938

Quarterly Earnings Estimates

	2023	2024
Q1	1.58A	2.02A
Q2	1.81A	1.95E
Q3	1.82A	2.01E
Q4	1.90A	2.12E

Price objective basis & risk

AECOM (ACM, B-1-7, \$88.59)

Our \$100 PO is based on 13x our 2024E EBITDA. This multiple is moving more in line with professional services/design peers and defensive/infrastructure related peers given AECOM's improving balance sheet (net leverage of 1.1x, net debt free in 18 months) and portfolio transformation into a professional services firm. We believe the growth outlook is recovering given potential for infrastructure, transportation, and environmental spending initiatives.

Downside risks to our PO are 1) weaker-than-expected global construction growth, particularly public spending in the US, 2) higher-than-expected headwind from COVID-19, 3) shortfall in execution around CS divestiture or hitting FCF conversion target.

Upside risks to our PO are 1) stronger-than-expected infrastructure spending by local, state, and federal agencies, 2) higher-than-forecast cost savings from the restructuring program, 3) better-than-expected free cash flow generation.

Jacobs Eng. (J)

Our \$145 PO is based on 12.5x 2024E EV/EBITDA. This is near the mid to high end of JEC's historical range of 9-16x, although we believe this is justified given the company's improved cost structure, less cyclical portfolio, and reduced exposure to riskier contracts. Additionally, we see evidence of momentum in certain areas of its portfolio including infrastructure, transportation, environmental services, and re-shoring. The valuation is more in line with other Government Services/IT players. Over time, we believe Jacobs' valuation discussion will likely shift away from E&Cs and more to steady compounders within industrials ranging from government services providers, business services, consulting IT, and waste.

Downside risks to our PO are: 1) Weaker-than-expected public spending outlook due to DoTs, state, local budgets 2) Lack of organic FCF generation and integration risks following notable acquisitions 3) Overhang from ongoing dispute related to power project in Australia Upside risks to our PO are: 1) Bigger than expected infrastructure bill at the state and federal level 2) A more favorable outlook for Department of Defense and Energy 3) Higher than expected synergies following acquisitions and technology investments

Analyst Certification

I, Michael Feniger, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Machinery Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY	AECOM	ACM	ACM US	Michael Feniger
	Blue Bird Corp	BLBD	BLBD US	Sherif El-Sabbahy
	Caterpillar Inc	CAT	CAT US	Michael Feniger
	CNH Industrial NV	CNHI	CNHI US	Michael Feniger
	Construction Partners Inc.	ROAD	ROAD US	Michael Feniger
	ESAB Corp	ESAB	ESAB US	Sherif El-Sabbahy



US - Machinery Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	Finning International Inc.	YFTT	FTT CN	Sherif El-Sabbahy
	H&E Equipment Services Inc	HEES	HEES US	Sherif El-Sabbahy
	Knife River Corp	KNF	KNF US	Sherif El-Sabbahy
	Republic Services	RSG	RSG US	Michael Feniger
	Techtronic Industries Co Ltd	TTNDF	669 HK	Michael Feniger
	Techtronic Industries Co Ltd	TTNDY	TTNDY US	Michael Feniger
	United Rentals Inc	URI	URI US	Michael Feniger
	Vulcan Materials	VMC	VMC US	Michael Feniger
	Waste Connections Inc	WCN	WCN US	Michael Feniger
	WillScot Mobile Mini	WSC	WSC US	Sherif El-Sabbahy

NEUTRAL

	AGCO Corp	AGCO	AGCO US	Michael Feniger
	Deere & Co	DE	DE US	Michael Feniger
	Fluor	FLR	FLR US	Michael Feniger
	GFL Environmental Inc	GFL	GFL US	Michael Feniger
	GFL Environmental Inc	YGFL	GFL CN	Michael Feniger
	Jacobs Eng.	J	J US	Michael Feniger
	Kennametal Inc.	KMT	KMT US	Michael Feniger
	Martin Marietta Materials	MLM	MLM US	Michael Feniger
	NV5 Global Inc.	NVEE	NVEE US	Michael Feniger
	PACCAR Inc	PCAR	PCAR US	Michael Feniger
	RB Global, Inc	RBA	RBA US	Michael Feniger
	Waste Management	WM	WM US	Michael Feniger

UNDERPERFORM

	Allison Transmission Holdings Inc.	ALSN	ALSN US	Sherif El-Sabbahy
	Casella	CWST	CWST US	Michael Feniger
	Cummins Inc	CMI	CMI US	Michael Feniger
	Herc Holdings Inc	HRI	HRI US	Sherif El-Sabbahy
	IPG Photonics	IPGP	IPGP US	Michael Feniger
	Oshkosh Corp.	OSK	OSK US	Michael Feniger
	Terex Corp.	TEX	TEX US	Michael Feniger
	Timken Company	TKR	TKR US	Michael Feniger

IQmethodSM Measures Definitions**Business Performance**

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

EV / EBITDA

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Numerator

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

EV = Current Share Price × Current Shares + Minority Equity + Net Debt +

Other LT Liabilities

Enterprise Value

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization

Shareholders' Equity

Sales

N/A

N/A

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Denominator

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

Sales

Basic EBIT + Depreciation + Amortization

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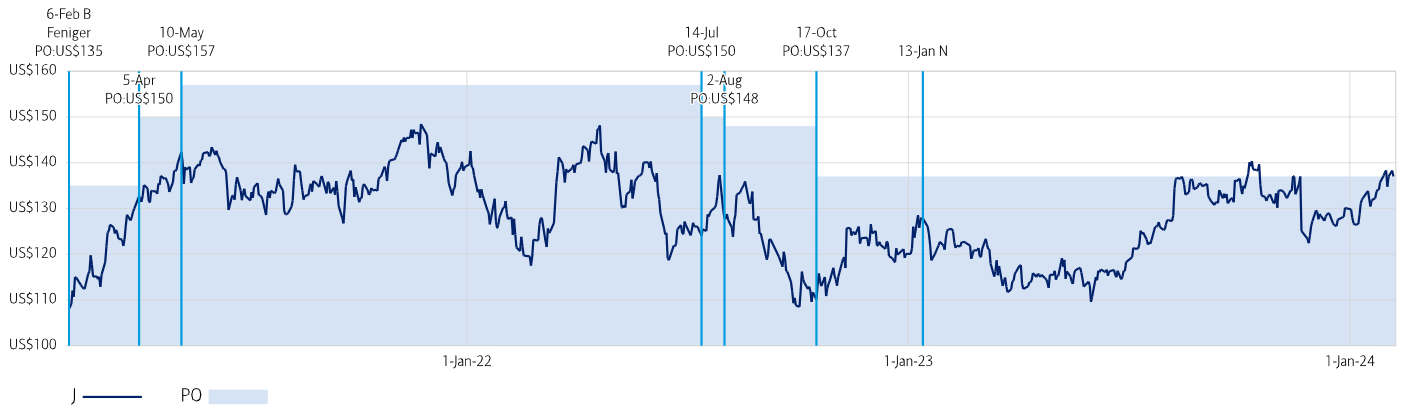
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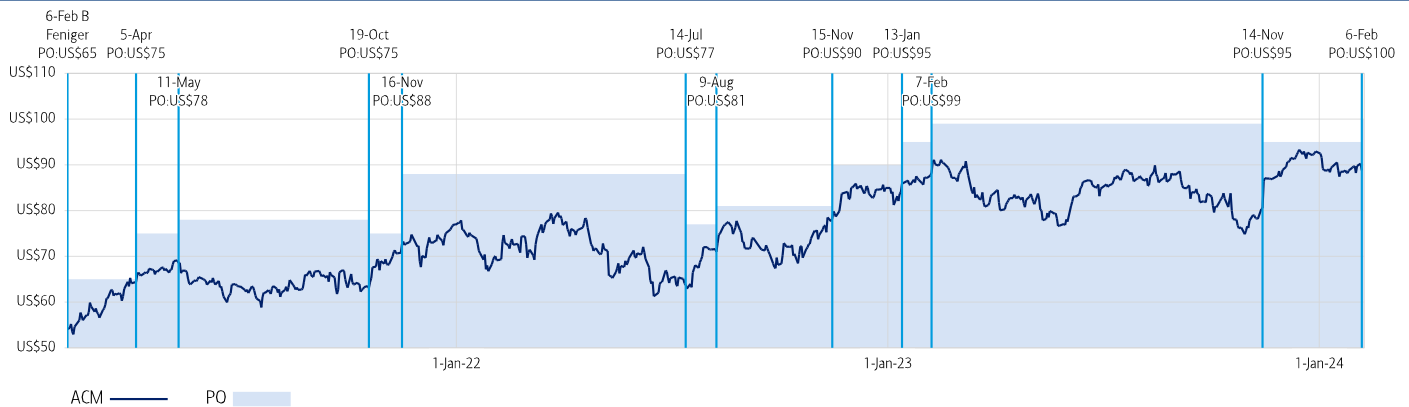
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Jacobs Eng. (J) Price Chart



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AECOM (ACM) Price Chart



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Equity Investment Rating Distribution: Engineering & Construction Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	9	42.86%	Buy	5	55.56%
Hold	7	33.33%	Hold	3	42.86%
Sell	5	23.81%	Sell	3	60.00%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2}Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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