Trinity Industries, Inc. (TRN)

Updated July 30th, 2022, by Yiannis Zourmpanos

Key Metrics

Current Price:	$26	**5 Year CAGR Estimate:**	1.5%	**Market Cap:**	$2.2 B
Fair Value Price:	$15	**5 Year Growth Estimate:**	8.0%	**Ex-Dividend Date:**	07/14/2022
% Fair Value:	170%	**5 Year Valuation Multiple Estimate:**	-10.1%	**Dividend Payment Date:**	07/29/2022
Dividend Yield:	3.5%	**5 Year Price Target**	$22	**Years Of Dividend Growth:**	12
Dividend Risk Score:	D	**Retirement Suitability Score:**	C	**Rating:**	Sell

Overview & Current Events

Trinity Industries is a leading provider of rail transportation products and services in North America. The business of the company is classified primarily under two reporting segments: Railcar Leasing, which owns and operates a fleet of railcars and provides third-party fleet leasing, management, and administrative services; and the Rail Products Group, which manufactures and sells railcars and related parts and components and provides railcar maintenance and modification services.

On July 27th, 2022, the company announced results for the second quarter of 2022, ending June 30th, 2022. Trinity reported diluted EPS of $0.14, up 75% YoY, but missed analysts' expectations by $0.03. The company reported revenues of $416.8 million for the quarter, up 42.1% compared to $293.3 million in Q2 2021. The higher revenues during the quarter were driven by higher external deliveries in the Rail Products Group.

The segment reported net revenue of $221.7 million in the second quarter compared with $108.3 million in the same period last year. Specifically, the increase in revenue for the rail products business was driven by higher deliveries during the quarter. The Rail Products Group received orders for 4,335 railcars and delivered 2,510 railcars compared to deliveries of 1,765 and new railcar orders of 4,570 in Q2 2021. Despite the higher sales, the company reported lower operating margins of 17.5% for Q2 2022 compared with 19.7% for Q2 2021. The lower margins were driven by higher input costs and increased depreciation in the Leasing Group. The Leasing Group's lease fleet of 110,560 company-owned railcars was 97.2% utilized during Q2 2022, compared to a lease fleet of 94.3% on 108,635 company-owned railcars during Q2 2021.

The management also provided the full-year guidance for 2022. The industry deliveries of railcars are expected to be between 40,000 to 50,000. In addition, the company forecasts capital expenditures of $35 million to $45 million, while net investment in the lease fleet will be $425 million to $475 million during the year (revised downwards from $450 million to $550 million). As a result, the full-year EPS is expected to be in the range of $0.85 to $1.05.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	$1.58	$2.34	$4.19	$5.08	$2.25	$1.41	$0.70	$1.27	$0.34	$0.56	***$1.02***	***$1.49***
DPS	$0.19	$0.25	$0.38	$0.43	$0.44	$0.50	$0.52	$0.64	$0.76	$0.84	***$0.92***	***$1.24***
Shares	163.4	163.4	155.7	152.9	152.2	150.9	133.3	119.7	111.2	83.3	***83.0***	***60.2***

Trinity Industries has been adversely affected by the supply chain disruptions and higher costs after the pandemic outbreak over the past two years, along with implementing the Precision Scheduled Railroading model. As a result, the company's net income declined to $0.56 per share in 2021 as production inefficiencies and increased cost pressures weighed on the company's margins. However, the near-term outlook has improved with the re-opening after COVID lockdowns and increased demand reflected by the current book-to-bill ratio of 1.7 times. In addition, we expect cost pressures to reduce as steel prices are expected to normalize. As a result, we maintain our forecast of EPS growth at a CAGR of 8% over the next five years, leading to our estimated EPS of $1.49 by 2027. The company has a solid record of paying dividends despite operating in a cyclical sector as Trinity Industries has paid an increasing dividend for the past 12 years and we do expect the company to maintain its dividend growth and have forecasted dividend CAGR of 10% leading to a dividend to $1.24 in 2027.

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Avg. P/E	9.6	9.3	9.0	5.6	9.6	20.8	46.5	16.4	60.4	51.0	***25.6***	***15.0***
Avg. Yld.	1.7%	1.6%	1.4%	2.1%	2.8%	2.3%	2.2%	3.1%	3.7%	3.0%	***3.5%***	***5.5%***

The railcar manufacturer currently trades at a forward P/E of 25.6, slightly higher than its long-term nine-year average P/E of 23.8, but below its five-year average P/E of 39.0. Even though we believe that the declining steel prices and an uptick in demand will benefit the company in the near term, we assign a P/E of 15.0 to the stock, which we believe is a fair reflection of its value. Accordingly, with an EPS of $1.49 and P/E of 15.0 our 2027 target price for the stock stands at $22.

Safety, Quality, Competitive Advantage, & Recession Resiliency

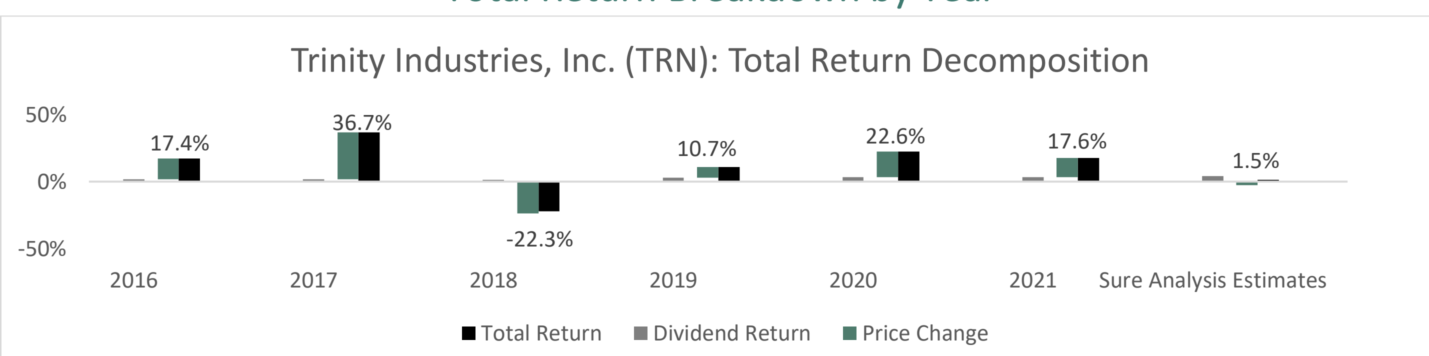
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	12%	11%	9%	8%	20%	35%	74%	50%	224%	150%	***91***%	***83***%

The company has paid a consistent dividend to its shareholders with a 10-year payout ratio averaging 59%, and we expect the company to maintain and increase its payout in the future. While commenting on the results, management noted that the repercussions of COVID-19 have negatively influenced the company as it incurred higher operating costs and reduced demand and employee availability. This is a good example of how macro-economic factors can easily affect the company's financials due to its highly cyclical nature. As a result, the company's operations are expected to remain under pressure in the near term. However, as demand lifts off and the price of steel normalizes in the future, the company would be in a much better position compared to where it is today. In addition, the leasing margins will improve in a rising rate environment, and the fleet's utilization ought to be high, driven by solid railcar demand. Nevertheless, an upcoming recession could adversely affect its performance. The share buybacks by the company have also played a pivotal role in sustaining the high EPS growth rate as well. Trinity returned $895 million to shareholders through $88 million in dividends and $807 million in share repurchases in 2021.

Final Thoughts & Recommendation

While Trinity Industry runs a capital-intensive cyclical business, we believe that increased bookings and reduced cost pressures will be a positive catalyst to EPS growth. Indeed, Trinity Industry’s dividend growth prospects could remain strong throughout the cycle. However, we believe that any return potential to be produced by the underlying EPS and DPS growth could be offset by a valuation headwind. Therefore, shares earn a sell rating based on this rationale.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	3,812	4,365	6,170	6,393	3,090	2,397	2,509	2,752	1,750	1,516
Gross Profit	760	1,043	1,550	1,737	778	622	570	574	422	355
Gross Margin	19.9%	23.9%	25.1%	27.2%	25.2%	26.0%	22.7%	20.9%	24.1%	23.4%
SG&A Exp.	224	291	404	476	314	339	297	217	341	179
D&A Exp.	194	212	245	266	217	230	252	277	259	266
Operating Profit	536	752	1,147	1,260	464	283	274	357	81	176
Op. Margin	14.1%	17.2%	18.6%	19.7%	15.0%	11.8%	10.9%	13.0%	4.6%	11.6%
Net Profit	255	376	678	797	344	703	159	138	(147)	182
Net Margin	6.7%	8.6%	11.0%	12.5%	11.1%	29.3%	6.3%	5.0%	-8.4%	12.0%
Free Cash Flow	58	(69)	355	(90)	242	131	(607)	(817)	(46)	41
Income Tax	134	204	355	426	107	(415)	43	59	(274)	16

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	6,670	7,313	8,695	8,886	9,125	9,543	7,989	8,701	8,702	8,236
Cash & Equivalents	573	429	888	786	563	779	179	166	132	167
Accounts Rec	390	365	405	370	379	204	277	260	164	228
Inventories	702	815	1,068	943	666	403	525	433	285	433
Goodwill & Int.	240	278	773	754	754	209	209	209	147	154
Total Liabilities	4,532	4,564	5,298	4,837	4,814	4,685	5,427	6,323	6,686	6,939
Accounts Payable	188	216	295	217	156	120	212	204	146	206
Long-Term Debt	3,009	2,948	3,476	3,160	3,025	3,214	4,029	4,882	5,017	5,171
Total Equity	2,053	2,402	2,996	3,654	3,919	4,501	2,211	2,030	1,739	1,030
LTD/E Ratio	1.47	1.23	1.16	0.86	0.77	0.71	1.82	2.40	2.89	5.02

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	4.0%	5.4%	8.5%	9.1%	3.8%	7.5%	1.8%	1.6%	-1.7%	2.1%
Return on Equity	13.0%	16.9%	25.1%	24.0%	9.1%	16.7%	4.7%	6.5%	-7.8%	13.1%
ROIC	5.1%	6.9%	10.8%	11.3%	4.7%	9.1%	2.2%	2.0%	-2.1%	2.7%
Shares Out.	163.4	163.4	155.7	152.9	152.2	150.9	133.3	119.7	111.2	83.3
Revenue/Share	24.58	28.55	39.37	42.00	20.79	15.77	17.14	21.62	15.10	14.61
FCF/Share	0.38	(0.45)	2.26	(0.59)	1.63	0.86	(4.14)	(6.41)	(0.40)	0.40

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.