McGrath RentCorp (MGRC)

Updated October 28th, 2022 by Nathan Parsh

Key Metrics

Current Price:	$95	**5 Year CAGR Estimate:**	0.7%	**Market Cap:**	$2.3 B
Fair Value Price:	$76	**5 Year Growth Estimate:**	3.0%	**Ex-Dividend Date:**	01/13/23[1]
% Fair Value:	124%	**5 Year Valuation Multiple Estimate:**	-4.3%	**Dividend Payment Date:**	01/27/23[2]
Dividend Yield:	1.9%	**5 Year Price Target**	$89	**Years Of Dividend Growth:**	31
Dividend Risk Score:	A	**Retirement Suitability Score:**	C	**Rating:**	Sell

McGrath RentCorp is a leading business-to-business rental and sales company that provides portable buildings for use as classrooms, office space and places to test electronic equipment. The company's products can also be used as secure storage for both hazardous and non-hazardous materials, restrooms, health care and child care facilities. Many of McGrath's portable buildings are used to meet a variety of demands and can be moved easily from location to location.

On October 27th, 2022, McGrath RentCorp announced third quarter earnings results for the period ending September 30th, 2022. Revenue grew 16% to $200.5 million, which was $13 million more than expected. Earnings-per-share of $1.25 compared favorably to $0.95 in the previous year and was $0.08 above estimates.

Rental revenues increased 15% to $118.4 million. Revenues for Mobile Modular, the company's largest division, were up 17%, primarily because of higher average rental equipment in use and an increase in average monthly rental rates. TRS-RenTelco rental revenues grew 9%, also due to higher average higher average rental equipment in use and an increase in average monthly rental rates. Adler Tanks rental revenues were up 18%, due to strong demand across regions and vertical markets.

McGrath RentCorp now expects revenue in a range of $720 million to $735 million for the year, up from the prior range of $675 to $705 million. We continue to expect that the company will generate $4.34 of earnings-per-share in 2022, which would be an 18.6% improvement from 2021.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	$1.78	$1.67	$1.73	$1.59	$1.60	$2.12	$3.24	$3.93	$4.16	$3.66	***$4.34***	***$5.03***
DPS	$0.94	$0.96	$0.98	$1.00	$1.02	$1.04	$1.28	$1.50	$1.64	$1.73	***$1.82***	***$2.11***
Shares[3]	25	26	26	24	24	24	24	25	24	24	***24***	***24***

McGrath RentCorp has experienced volatility in its earnings-per-share over the past decade. Earnings-per-share dropped almost 19% in 2009 and it wasn't until 2011 that earnings recovered above 2008's total. We continue to expect earnings-per-share to grow at a rate of 3% per year through 2027.

McGrath RentCorp raised its dividend by 4.6% for the April 29th, 2022 payment. This marks 31 consecutive years of dividend growth. Shares offer an annualized yield 1.9% presently, slightly higher than the average yield of the S&P 500. Despite McGrath RentCorp's variance in earnings-per-share over the last decade, the company has been able to raise its dividend each year for more than three decades. This is an impressive feat for a company that can be very cyclical.

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	15.7	20.1	20.5	18.6	18.4	6.1	17.0	16.0	20.1	21.9	***21.9***	***17.6***
Avg. Yld.	3.4%	2.9%	2.8%	3.4%	3.5%	1.9%	2.5%	2.0%	2.5%	2.2%	***1.9%***	***2.4%***

[1] Estimated ex-dividend date
[2] Estimated dividend date
[3] Share count in millions

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Shares of McGrath RentCorp have increased $11, or 13.1%, since our July 30th, 2022 update. Based off of earnings expectations for 2022, McGrath RentCorp's stock currently has a price-to-earnings ratio of 21.9. We maintain our target valuation of 17.6 times earnings as this is nearly in-line with given the quality of results over the past few years. If shares were to revert to this multiple by 2027, then valuation be a 4.3% headwind to annual results over this time period.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	53%	58%	57%	63%	64%	49%	40%	38%	39%	47%	***42%***	***42%***

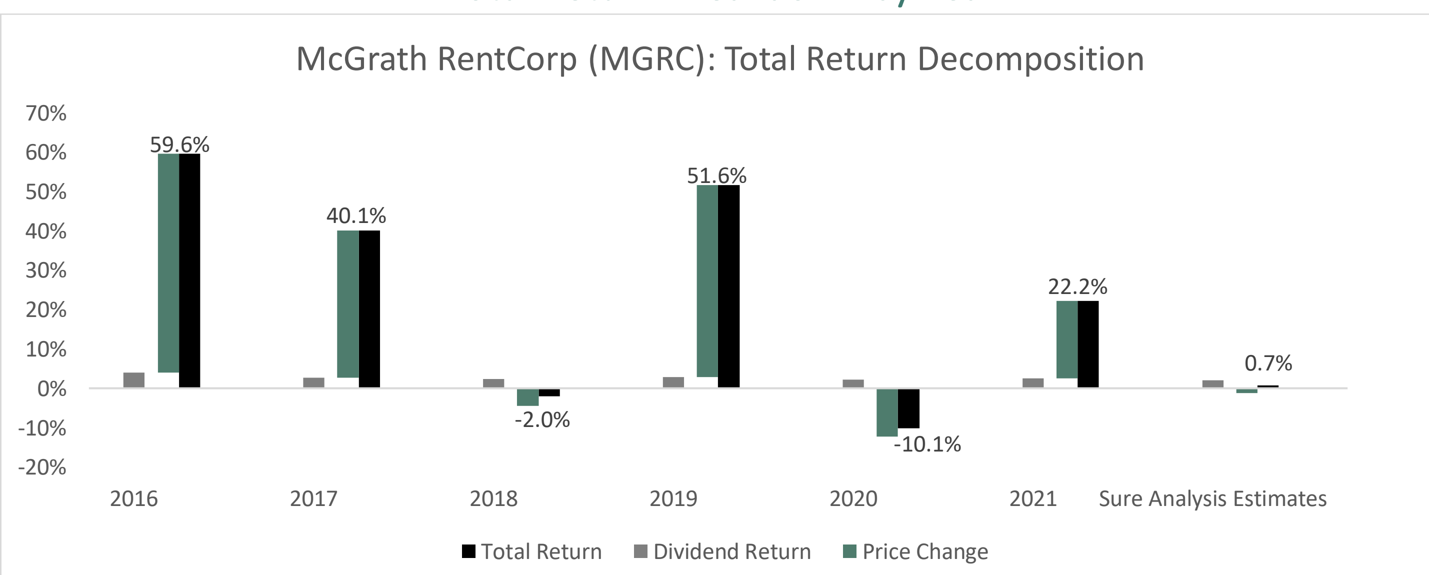
McGrath RentCorp showed in the last recession that its earnings are at risk during a downturn. The company's rental business would most likely see earnings decline in the next recession as customers might not be willing to add additional classroom or office space, and would make do with current facilities. Even when the economy strengthened, McGrath RentCorp had difficulty growing earnings until very recently. One area McGrath RentCorp has succeeded in is lowering its debt over the past decade. The amount of debt as a percentage of assets has gone down almost every year since 2008. McGrath RentCorp's payout ratio is in a healthy range and the company has increased its dividend by at least 9% for the three years prior to 2020, though the last two raises have been below this range. Higher-than-average increases could mean that management believes earnings will grow at a higher than usual rate.

McGrath RentCorp's key competitive advantage is that company's rental portfolio is fairly diverse. The company's products are used for office space, school classrooms, telecommunications and energy purposes. While still sensitive to the state of the economy, this product diversity does give McGrath RentCorp some cushion against weakness in any one area of its business.

Final Thoughts & Recommendation

After third quarter results, McGrath RentCorp is projected to return 0.7% per year through 2027, down from our previous estimate of 3.2%. Our projected return stems from a 3% earnings growth rate and 1.9% starting yield that are nearly offset by a low single-digit headwind from multiple compression. McGrath RentCorp's segments continue to show strong growth rates. The valuation, however, leaves much to be desired. We maintain our five-year price target of $89 as well as our sell rating on shares of McGrath RentCorp due to projected returns.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	364	380	408	405	424	462	498	570	573	617
Gross Profit	168	169	182	177	184	206	233	266	264	281
Gross Margin	46.2%	44.5%	44.6%	43.7%	43.4%	44.7%	46.8%	46.7%	46.1%	45.6%
SG&A Exp.	86	89	97	100	105	112	116	125	123	149
D&A Exp.	72	77	81	84	81	78	82	89	95	107
Operating Profit	82	80	85	77	79	95	117	141	141	132
Operating Margin	22.5%	21.1%	20.9%	19.0%	18.7%	20.5%	23.6%	24.8%	24.6%	21.5%
Net Profit	45	43	46	40	38	154	79	97	102	90
Net Margin	12.3%	11.4%	11.2%	10.0%	9.0%	33.3%	15.9%	17.0%	17.8%	14.5%
Free Cash Flow	(20)	(11)	(42)	4	51	13	4	8	80	79
Income Tax	28	28	31	26	29	(70)	25	32	30	32

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	972	1,028	1,116	1,153	1,128	1,148	1,217	1,310	1,276	1,596
Cash & Equivalents	2	2	1	1	1	3	2	2	1	1
Accounts Receivable	92	88	101	95	97	106	121	128	123	159
Goodwill & Int. Ass.	39	38	38	37	36	36	35	36	35	179
Total Liabilities	608	627	692	773	734	624	646	676	593	864
Long-Term Debt	302	290	322	381	326	303	299	293	223	426
Shareholder's Equity	365	401	425	380	394	524	572	634	683	732
LTD/E Ratio	0.83	0.72	0.76	1.00	0.83	0.58	0.52	0.46	0.33	0.58

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	4.7%	4.3%	4.3%	3.6%	3.4%	13.5%	6.7%	7.7%	7.9%	6.2%
Return on Equity	12.8%	11.3%	11.1%	10.1%	9.9%	33.5%	14.5%	16.1%	15.5%	12.7%
ROIC	6.9%	6.4%	6.4%	5.4%	5.2%	19.9%	9.4%	10.8%	11.1%	8.7%
Shares Out.	25	26	26	24	24	24	24	25	24	24
Revenue/Share	14.47	14.64	15.59	15.89	17.69	19.04	20.31	23.16	23.34	25.16
FCF/Share	(0.78)	(0.42)	(1.60)	0.15	2.13	0.54	0.16	0.33	3.28	3.22

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