

MARKET REPORT:

THE WILLBROS GROUP
It's Time To Sell the
Oil and Gas Segment



The TNL Strategies Group is a combined effort of LIUNA Corporate Affairs and IBT Capital Strategies. We provide information to pension funds with assets of over \$135 Billion. The group monitors performance and corporate governance and provides additional focus on industries that employ client fund participants and retirees.

RECOMMENDATION

The TNL Strategies Group recommends that the Willbros Group Inc. (WG) Board of Directors take immediate action to sell the company's Oil and Gas segment. WG's Professional Services, Utility T&D and Canadian business segments are the company's core businesses and appear to offer the best opportunity to begin changing WG's negative profit trend. Historic underperformance of the oil and gas segment illustrates the lack of management's ability to capitalize on opportunities. Current pressures impacting oil and gas contractors accelerate the need for WG to minimize its exposure, and safeguard shareholder value.

SUMMARY RECOMMENDATION OF THE TNL ADVISOR GROUP

- The Willbros Group Inc. is a publicly traded company (NYSE: WG) that operates in the field of energy infrastructure services. WG has traditionally focused on the oil and gas sector providing engineering services, mid-stream infrastructure construction, maintenance and electrical transmission.
- The U.S. oil & gas industry is in the midst of a renaissance due primarily to technological advances in energy exploration. Institutional investors have a wide variety of exposure to this sector and while many have profited by the rapid expansion of key sectors in the industry, investors are likewise affected by the volatility of oil and gas prices.
- The TNL Strategies Group conducts research and analysis on companies that provide construction services to the oil & gas industry. In a recent analysis, TNL identified WG as significantly underperforming when compared to its peers. The first nine months of 2014, WG's operating income was 23.8% lower than during the same 9-month period the year prior.¹ The company's five year share price fell by 66.0% from January 1, 2010 through December 31, 2014.²
- In 2015, oil and gas contractors such as Willbros Group are likely to experience increased price headwinds amidst cost pressures impacting the industry.³ As producers attempt to extract margins in the current environment, cost pressures are likely to soften earnings of service providers. Some companies within WG's peer group are better positioned to mitigate impacts. For example, Matrix Service Company recently reported flat revenues in its Oil, Gas & Chemical segment but increased revenue growth in its other segments.⁴ In addition, other WG competitors such as Dycom Industries and Granite Construction are less exposed to the oil and gas industry.⁵

WILLBROS GROUP: A HISTORY OF UNDERPERFORMANCE, A COMPANY IN CRISIS

- WG's challenges appear to be deeply rooted. Execution difficulties in its Oil & Gas segment have plagued the company in recent years. From the company's IPO in August of 1996 through December 31, 2014, the company's share price has declined by 34.9%.⁶
- WG lists 13 peers in its 2014 Proxy that are currently publicly-traded,⁷ and over a five year period, those companies have increased their share price by an average of 63.9%. During the same period, WG experienced a 69% decrease in share price, placing them at the bottom of the list.⁸

- Despite continual announcements of changes in management, analysts continue to downgrade their outlooks.⁹

TABLE 1: Willbros Stock Price Compared to Peers, Average Monthly Close: December 2009 – December 2014

Company	Dec-09	Dec-10	Dec-11	Dec-12	Dec-13	Dec-14	2009-2014 Growth
DY	\$8.25	\$14.33	\$20.33	\$19.16	\$27.63	\$32.60	295%
CBI	\$19.01	\$31.92	\$38.34	\$43.02	\$79.14	\$42.48	123%
MTRX	\$9.67	\$11.47	\$9.07	\$11.29	\$22.57	\$20.96	117%
TISI	\$18.51	\$22.16	\$28.37	\$37.63	\$40.21	\$39.28	112%
MTZ	\$12.83	\$14.40	\$16.05	\$23.84	\$31.43	\$21.93	71%
EXH	\$20.98	\$23.55	\$9.84	\$21.48	\$32.76	\$32.19	53%
MYRG	\$17.92	\$19.18	\$18.16	\$21.77	\$25.13	\$26.71	49%
PWR	\$20.10	\$19.53	\$20.94	\$26.85	\$29.99	\$28.14	40%
TPC	\$17.89	\$20.89	\$13.60	\$13.59	\$25.48	\$23.52	31%
GVA	\$32.43	\$28.05	\$24.03	\$32.54	\$32.39	\$37.00	14%
FWI	\$19.93	\$24.73	\$14.08	\$17.97	\$23.40	\$22.40	12%
TTEK	\$26.69	\$25.37	\$21.73	\$26.28	\$27.60	\$26.40	-1%
WG	\$16.57	\$8.50	\$3.55	\$5.30	\$8.57	\$5.11	-69%
MDR	\$23.16	\$19.88	\$11.11	\$10.71	\$8.24	\$2.84	-88%

Source: Capital IQ.

TABLE 2: Willbros Stock Price: August 1996 – December 2014



Source: Capital IQ. Chart represents daily closing price from August 15, 1996 through December 31, 2014

WILLBROS ANNOUNCES “RESTATEMENT” OF EARNINGS (OCTOBER, 2014)

On October 21, 2014, WG announced it would restate its 2014 second quarter earnings report, as the company failed to adequately record \$22 to \$24 million in losses associated with Lineal Industries' Allegheny Access pipeline project.¹⁰ Losses associated with this project resulted in pretax losses of \$11.9 million in the second quarter, wiping out 65% of WG's total operating income. In total, WG's net income loss for the second quarter was 325% greater due to the restatement.¹¹

Willbros executive management hosted a conference call with investors on October 22, 2014 to explain the restatement and problems on Lineal Industries' Ohio project. It revealed that the Oil and Gas segment management was, “spread too thin to support eight business units.” CEO John McNabb stated that Willbros experienced, “too much growth to manage effectively as needed.” Additionally, when reviewing the Allegheny Access project, WG management found lack of, “field quality control and assurance.” As a result, Willbros proposed to “reorganize” its Oil and Gas segment, cutting revenues by about 20%. Although Willbros stated it would reduce services offered in certain regions, Willbros management said that they remain committed to growing the mainline pipeline construction and pipeline integrity services business.¹²

- **Willbros Finds Additional Losses Associated With Another Pipeline Project (December, 2014)**

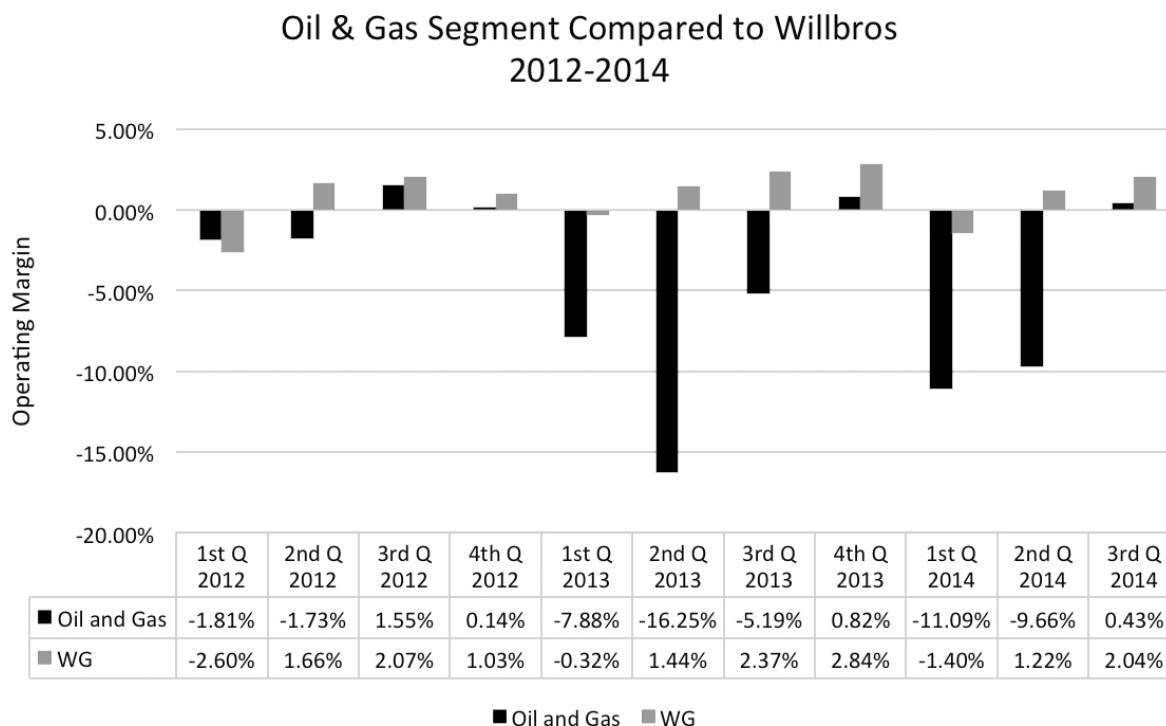
As part of WG's restated second quarter earnings, the company found project errors associated with another significant pipeline project in its Oil and Gas segment. In total, losses associated with both projects resulted in pretax charges of nearly \$30 million for the first six months of 2014. These losses wiped out virtually all of WG's previously reported operating income for the first half of 2014.¹³

- **Willbros Oil & Gas segment: Inadequate Oversight and Failed Execution**

In January of 2012, Willbros combined its Upstream Oil & Gas and Downstream Oil & Gas segments into a single segment. At that time, WG also started to report its Canada operations separately. For the quarter ending March 21, 2012, the Oil and Gas segment generated operating income greater than WG's consolidated operating margin. Unfortunately, after the first quarter of 2012, the Oil and Gas segment has consistently underperformed the company as a whole. In fact, the Oil and Gas segment's operating margins have been lower than WG's consolidated operating margins every quarter except for the first quarter of 2012.¹⁴ While the Canada segment capitalized on capital expenditures allocated to it, the Oil & Gas segment recorded losses in FY2011, FY2012 and FY2013, despite receiving the greatest share of WG's total capital investment in those years.¹⁵ Despite ongoing promises of change, and ongoing operational changes in executive management, the Oil & Gas Segment remains ineffective and unprofitable.

WG's restatement of earnings, brought on by ineffective execution within the company's Oil and Gas segment, illustrates that the company has failed to overcome the core challenges that have plagued this segment of the company's business. Thus, WG's potential for profitability remains a significant challenge.

TABLE 3: Oil & Gas segment Quarterly Operating Margins Compared to WG Consolidated Quarterly Operating Margins



Source: WG Form 10-Qs and YCharts.

2014: MANAGEMENT CHANGES & FINANCIAL PERFORMANCE – ARE WE MAKING PROGRESS?

- Year-to-date earnings remain lower than previous year, and significantly lower than management targets.¹⁶ On December 15, 2014, Willbros announced its third quarter earnings results. For the Oil & Gas segment, year-to-date operating results for the segment are a loss of \$42.5 million on revenue of \$665.3 million, compared to a loss of \$44.6 million on revenue of \$463.1 million in the first nine months of 2013. (For the Third Quarter, 2014, the Oil & Gas segment posted an operating income of \$1.1 million on revenues of \$253.7 million.)¹⁷
- Table 4 compares (WG and peers) year-over-year Revenue and Income growth for the first nine months of FY2013 and FY2014. WG’s underperformance is evident.
- In the past twelve months, Willbros’ stock performance has not improved. Its stock price dropped more than 32.2% in calendar year 2014, underperforming nearly all other companies in its peer group.

TABLE 4: Year-over-Year Revenue and Income Growth

Company	Year-over-Year REVENUE Growth: First 9 mos. of 2013 to First 9 mos. Of 2014	Year-over-Year NET INCOME Growth: First 9 mos. of 2013 to First 9 mos. of 2014
Willbros Group	13.72%	-53.50%
Exterran Holdings, Inc.	-13.02%	-21.39%
MYR Group	6.93%	-9.31%
MasTec	6.71%	-6.14%
Foster Wheeler	-0.42%	-4.62%
Quanta Services	23.23%	-2.17%
Dycom Industries	-1.13%	11.33%
Team, Inc.	6.89%	15.48%
Matrix Service Company	52.31%	21.46%
Tutor Perini	6.96%	48.52%
McDermott International	-30.22%	51.01%
CBI	18.64%	52.82%
Granite Construction	1.00%	Turned positive
Tetra Tech, Inc.	-9.85%	Turned positive

Source: Capital IQ.

TABLE 5: WG & Peer Stock Comparisons - 2014

Company	Stock Symbol	Stock Price Growth During Calendar 2014
McDermott International	MDR	-67.38%
MYR Group	MYRG	-49.28%
CBI	CBI	-48.54%
Willbros Group	WG	-32.22%
MasTec	MTZ	-30.30%
Quanta Services	PWR	-9.27%
Tutor Perini	TPC	-4.64%
Exterran Holdings, Inc.	EXH	-4.35%
Team, Inc.	TISI	-3.21%
Foster Wheeler	FWI	-3.01%
Tetra Tech, Inc.	TTEK	-2.94%
Matrix Service Company	MTRX	7.42%
Granite Construction	GVA	11.63%
Dycom Industries	DY	27.83%

Source: Capital IQ database; 12-month share price returns from 1/2/2014 - 12/31/2014

- Management changes have failed to generate growth for shareholders. On multiple occasions throughout FY2014, WG management announced leadership changes they believed would ultimately contribute to the company's profitability. However, the profitability has not occurred and the company's management has been in a constant state of transition.

- The new CEO and Executive Chairman, John T. McNabb, is a WG insider. McNabb has been on the Board of Directors since 2006, and served as the non-executive Chairman from September 2007 to August 2014 when he was appointed Executive Chairman.¹⁸ As non-executive Chairman for seven years, McNabb had a fiduciary responsibility to hold management accountable, and exercise his business judgment in the best interest of the company and shareholders. Unfortunately, during McNabb's tenure as non-executive Chairman, WG's stock price fell 61.5%.¹⁹
- Willbros recently appointed a former WG executive, Harry New, as President of the Oil & Gas segment. New rose through the ranks at the company during his employment from 2005 to 2011. According to WG, New left the company after reaching the position of President of Willbros U.S. Construction.²⁰ During New's last years of employment, the Oil and Gas segment failed to generate any operating income in FY2010 and FY2011. The Oil and Gas segment also experienced an operating loss in FY2012.²¹ Lastly, while New was President of Willbros U.S. Construction in FY2011, the U.S. Construction business reported an operating loss of \$9.7 million in 2011. The pipeline business also experienced a drop in operating income driven by lower margins on fixed price contracts.^{22, 23}

CONCLUSIONS – A NEW DIRECTION FOR WILLBROS:

- TNL Strategies Group members recommended changes and called for strengthening of the Oil & Gas segment in the spring of 2014. TNL members remained cautiously optimistic after changes in leadership were announced at the annual shareholder meeting. However, given the accelerated decline in performance, ineffective leadership changes, and recent announcements regarding the restatement of earnings, TNL is no longer optimistic on WG's outlook. TNL has concluded that current management is unable to capitalize on the profit potential of its Oil & Gas segment. Thus, the Board of Directors should take immediate steps to sell the Oil & Gas segment of the company. Shedding the Oil & Gas segment could help WG optimize its profit potential and increase value, allowing long-term investors to receive some return on their investment.
- TNL recommends that WG's Oil & Gas segment be sold to a buyer at a price that maximizes the value of investor shares. Even at current market value, the most prudent and financially responsible option is for the Oil and Gas segment of WG to be sold as soon as possible. An immediate sale could benefit long-term shareholders, as it would allow WG management to focus on maximizing profits and increasing shareholder value.

IS SALE OF THE OIL AND GAS SEGMENT A REALISTIC OPTION?

- Despite the current volatility upheavals in the oil & gas industry, WG's most inefficient business segment (oil & gas) could be an attractive entity for the right buyer. WG has operations in many shale basins in the U.S., and similar to peers who have been able to capitalize on opportunities to grow shareholder value, the right buyer with experienced managers could do the same for WG's weak segment.
- Several recent transactions demonstrate an interest of larger companies to acquire energy focused construction contractors. These acquisitions indicate that larger companies may be

better equipped at absorbing risks inherent in the industry, as well as aligning resources to support major construction projects.

- In 2013, MasTec acquired Big Country Energy Services, Inc. (BCES), an oil and gas pipeline construction company, for \$103 million in cash and \$24 million in BCES debt. In announcing the acquisition, MasTec noted BCES inventory of construction equipment, personnel, and the opportunity to expand MasTec's footprint in energy infrastructure work in North America.
- In October of 2014, Aecom Technology Corp. (AECOM) acquired URS Corporation, an engineering and construction-management company, for about \$4 billion, gaining new services in markets such as oil and gas. Aecom paid the equivalent of \$56.31 a share in the cash-and-stock deal, or about a 19% premium to URS' 30-day average closing price.²⁴
- In December of 2014, WG competitor Pike Energy (NYSE:PIKE), a large specialty construction and engineering firm, was acquired by Court Square Capital Partners. The acquisition price of \$12 per share represented a premium of approximately 50.8% over PIKE's closing price the day prior to the acquisition announcement, and a premium of approximately 39.6% percent over the 30-day average closing price.²⁵ This example is further illustration that WG's Oil & Gas segment could be attractive to large buyers in the industry. Moreover, it illustrates that under the right conditions and competent management, WG's Oil & Gas Segment could be turned profitable.

TIME FOR EVALUATION & CHANGE:

The TNL Strategies Group believes that it is time for WG's Board of Directors to conduct a forceful review of responsible options for the Oil & Gas segment, including exploring the option of selling the segment as soon as possible, so as to mitigate further shareholder losses.

FOR MORE INFORMATION REGARDING THIS REPORT, contact Carin Zelenko at 202-624-8100 or Erin Hutson at 202-639-4149.

ENDNOTES

- ¹ Willbros Group, Inc., September 30, 2014 Form 10-Q, www.willbros.com, accessed January 2015.
- ² Willbros Group, Inc. closing price on December 31, 2014 and January 1, 2010, Ycharts.com, accessed January 2015.
- ³ Peter Parry, "Steering through the oil storm," Bain Capital, January 9, 2015, <http://www.bain.com/publications/articles/steering-through-the-oil-storm.aspx>, accessed February 2015.
- ⁴ Matrix Service (MTRX) Q2 2015 Results - Earnings Call Transcript, Feb. 5, 2015, <http://seekingalpha.com/article/2890706-matrix-service-mtrx-q2-2015-results-earnings-call-transcript>, accessed February 2015.
- ⁵ See Dycom Industries, September 30, 2014 Form 10-Q and Granite Construction, September 30, 2014 Form 10-Q, www.pro.edgar-online.com, accessed February 2015.
- ⁶ Willbros Group, Inc. closing price on December 31, 2014 and August 15, 1996, Ycharts.com, accessed January 2015.
- ⁷ All publicly traded companies listed in Willbros Group, Inc. 2014 Proxy were included except Pike Corporation (PIKE). PIKE went private in December of 2014. See: "Pike Completes Go-Private Transaction," press release, December 22, 2014, <http://ir.pike.com/releasedetail.cfm?ReleaseID=888725>, accessed January 2015.
- ⁸ Willbros Group, Inc. and publicly-traded peer group average monthly closing price, December 2009 to December 2014, Capital IQ, Inc., a division of Standard & Poor's, accessed January 2015.
- ⁹ See Moody's Investor Service, "Rating Action: Moody's changes Willbros outlook to stable from positive," December 22, 2014 and Dwight Einhorn, "UPDATE: Stifel Downgrades Willbros Group As Numerous Risk Remain," *benzinga.com*, January 5, 2015.
- ¹⁰ "Willbros Group Refocuses Business Strategy With New Management Leadership," press release, October 21, 2014, <http://phx.corporate-ir.net/phoenix.zhtml?c=95816&p=irol-newsArticle&ID=1980085>, accessed January 2015.
- ¹¹ Willbros Group, Inc., June 30, 2014 Form 10-Q/A, www.willbros.com, accessed January 2015.
- ¹² Willbros Group, Inc., Special Conference Call, October 22, 2014, webcast, <http://www.videonewswire.com/event.asp>, accessed October 2014.
- ¹³ Willbros Group, Inc., June 30, 2014 Form 10-Q/A, www.willbros.com, accessed January 2015.
- ¹⁴ Compiled from Willbros Group, Inc., September 30, 2014 Form 10-Q; Willbros Group, Inc., June 30, 2014 Form 10-Q/A; Willbros Group, Inc., March 31, 2014 Form 10-Q/A; Willbros Group, Inc., September 30, 2013 Form 10-Q; Willbros Group, Inc., June 30, 2013 Form 10-Q; Willbros Group, Inc., March 31, 2013 Form 10-Q; "Willbros Reports Fourth Quarter And Full Year 2013 Results From Continuing Operations," press release, February 27, 2014; and Willbros Group, Inc. quarterly financial statement, Ycharts.com, accessed January 2015.
- ¹⁵ Willbros Group, Inc., December 31, 2013 Form 10-K, www.willbros.com, accessed January 2015.
- ¹⁶ Willbros Group, Inc., December 15, 2014 Form 8-K, www.pro.edgar-online.com, accessed January 2015.
- ¹⁷ Willbros Group, Inc., September 30, 2014 Form 10-Q, www.willbros.com, accessed January 2015.
- ¹⁸ Willbros Group, Inc., September 11, 2007 Form 8-K, www.pro.edgar-online.com, accessed January 2015.
- ¹⁹ Willbros Group, Inc. closing price on September 11, 2007 and August 29, 2014, Ycharts.com, accessed January 2015.
- ²⁰ "Willbros Names President Of Oil & Gas Segment," press release, January 12, 2015, <http://phx.corporate-ir.net/phoenix.zhtml?c=95816&p=irol-newsArticle&ID=2007044>, accessed January 2015.
- ²¹ Willbros Group, Inc., December 31, 2013 Form 10-K and Willbros Group, Inc., December 31, 2011 Form 10-K, www.willbros.com, accessed January 2015.
- ²² Willbros Group, Inc., December 31, 2011 Form 10-K, www.willbros.com, accessed January 2015.
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- ²⁴ Caelainn Barr, Beth Jinks, and Matthew Monks, "Aecom Technology Agrees to Buy URS for About \$4 Billion," *Bloomberg.com*, July 13, 2014, <http://www.bloomberg.com/news/2014-07-13/aecom-technology-agrees-to-buy-urs-for-about-4-billion.html>, accessed January 2015.
- ²⁵ "Pike Shareholders to Receive Cash of \$12.00 Per Share in Transaction Led by Court Square Capital Partners," press release, August 4, 2014, <http://ir.pike.com/releasedetail.cfm?ReleaseID=863860>, accessed January 2015.