

TriNet (NYSE: TNET), Our Newest Tri-Valley Addition

EXECUTIVE SUMMARY

Recommendation Snapshot

Rating	Outperform – Buy
Share Price (9/25/18)	\$54.66
52wk Hi/Low	\$33.24-60.15
NTM Target Price	\$78.00-90.00

TriNet (“the Company”) is a professional employer organization that employs over 300,000 employees in the US. In 2018 the Company relocated its corporate headquarters to Dublin, CA. and is the latest addition to the Mirador Tri-Valley Index.

TriNet Reports a Positive Q2, and the Company has Never Been More Profitable

On July 31, 2018, TriNet reported their Q2 2018 financial results. Here are our key takeaways from this quarter.

Q2 2018 Reported vs Estimates

Metric	Actual	Analyst est	Mgmt Guid
Total Revenue	\$850M	-	\$850-863M (Met)
Net Revenue	\$220M	\$208.40M (Beat)	\$201-216M (Beat)
EBITDA	\$99M	\$81.50M (Beat)	\$71-86M (Beat)
EPS	\$0.87	\$0.67 (Beat)	\$0.60-0.77 (Beat)
EPS (GAAP)	\$0.80	\$0.60 (Beat)	\$0.53-0.70 (Beat)

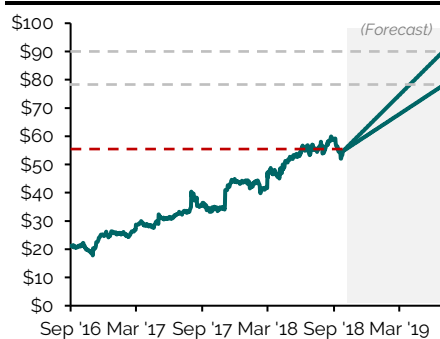
- Beat guidance and analyst estimates on all profitability numbers
- Net revenue grew +9.4% YoY
- Net revenue-per-client employee (CE) increased +12.9% YoY
- Adjusted EBITDA grew +33.1% YoY
- Adjusted EBITDA-per-CE increased +37.1% YoY
- Profitability is at an all-time high, but core growth is stagnant
- Finished transitioning the last client onto the new technology platform
- Management will be shifting back to growth mode

Expecting Strong Outperformance over NTM Despite the Recent Lag in Growth

We project that earnings growth will slow in Q3 as TriNet ramps the sales & marketing spend to kick the business into growth mode. We will be watching the client-employee number closely, and expecting the Company to deliver mid double-digit new sales growth, while curbing the attrition.

We see no barriers to future growth. There is a new CRO leading the sales team, the arduous product migration of 2017 is now complete, and the total addressable market is still untapped. Also, the Company is positioned as one of the top providers in the space. If management can execute as planned, then TriNet should generate sizable returns for its investors over the next 12 months.

TriNet Target Share Price



Financial Snapshot (in \$ millions except for CE)

	2016	2017	LTM	2018E	2019E	2020E
Net Revenue	646	810	850	919	1,105	1,330
Adj EBITDA	186	282	332	394	475	525
Total CE	337,885	325,370	318,921	343,239	388,175	426,993
Net Debt	260	72	177	(23)	(271)	(519)
OCF	145	299	111	205	378	412
EPS	\$0.85	\$2.49	\$3.16	\$3.23	\$4.14	\$4.47

OVERVIEW

Tri Who?

TriNet is a cloud-based professional employer organization (PEO), headquartered in Dublin, CA. The Company provides full-service HR solutions, via its SaaS platform, to small-to-medium enterprises (SMEs) in the US. The platform provides HR management, payroll processing, benefits administration, compliance and more. Different companies use TriNet in different ways. Some companies rely on TriNet as their effective end-to-end HR department, while others with existing HR teams use it to automate core payroll/admin processes. In all cases, TriNet becomes the employer of record for tax and insurance purposes, also called a 'co-employer'.

TriNet was originally founded in 1988 in San Leandro, CA. In 2000, the Company had planned for a \$138M IPO, but the offer was later withdrawn. In 2005, the Company was generating approximately \$50M in annual revenue and was bought out by the private equity group General Atlantic. The group eventually took TriNet public in 2014, raising a \$240M IPO on a \$1B valuation (\$16/share), TriNet had acquired 8 different HR solution providers during its time under General Atlantic, and annual revenue at IPO was approximately \$1.6B.

TriNet currently employs over 3,000 employees across the US. The Company was notably awarded 100 Fastest Growing Companies in 2017 by Fortune.

PEO Landscape

Nearly all the HR solutions on the market today are delivered through a software platform that aims to streamline the standard group of HR functions like talent management, recruiting and time & attendance. To a certain extent, these companies all compete with each other. Being able to identify where TriNet sits in this opaque market is extremely important when analyzing the security, because although from a marketing perspective these companies look identical, their underlying business models are completely different:

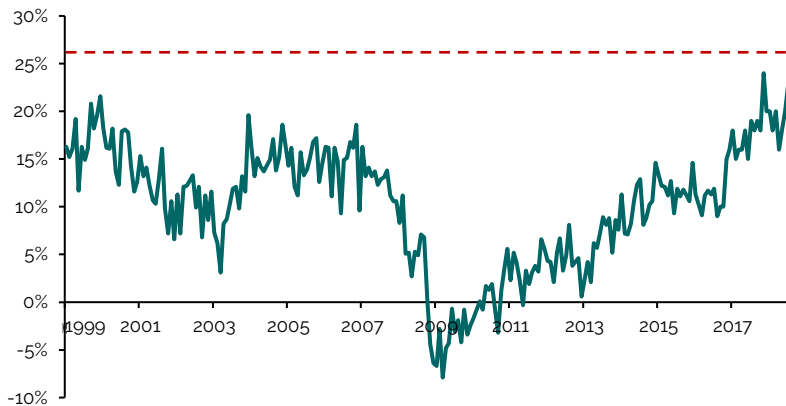
- Human Capital Management (HCM) – These are product-oriented companies that provide clients with software tools to more easily manage their HR administration. The client remains the employer of record, and is responsible for processing payroll and providing its own benefits, insurance, workers comp, etc. Example HCMs include Workday and Ultimate Software.
- HR outsourcing/Payroll processing – Companies in this category, sometimes called BPOs (business process outsourcers), help clients by managing the entire payroll and benefits administration process as an on-going service. The client still remains the employer of record. Example companies include ADP and Namely.

- Professional Employer Organization (PEO) – PEOs act as a co-employer and become the official employer of record for their clients' employees. The PEOs effectively take on all payroll and benefits-related liabilities. Most clients who use a PEO do so for the pooled-benefits advantage – since the PEO is technically the single employer of a large number of client employees, it can offer better benefits that aren't typically available to independent SMEs. Example PEOs include TriNet, Insperty and Justworks.

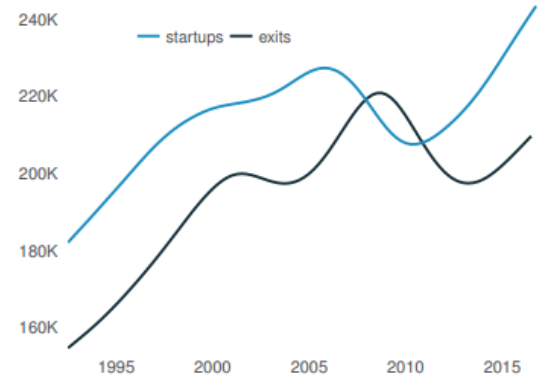
In 2017 there were an estimated 900 PEOs in the US responsible for paying out over \$175B in annual employee wages. We estimate that the top 5 PEOs hold approximately 40% of client market share, and 55% of the total client employees.

The total addressable market for PEOs is large and growing. The US Small Business Administration estimates there to be 58M+ SMEs (<500 employees) as of 2015, and startups, a large part of TriNet's business, are popping up faster than ever. The US unemployment rate is near its 20-year low, and SME sentiment is the highest it has ever been – 25% of SME's plan to increase employment over the next year, and 31% plan to raise wages in order to attract more talent. We see nothing but blue skies for the PEO market over the next 12-18 months, and our view is reinforced by TriNet's report that 75% of new sales quotes issued are to greenfield opportunities.

SME Plans to Increase Employment



US Quarterly Startups and Exits

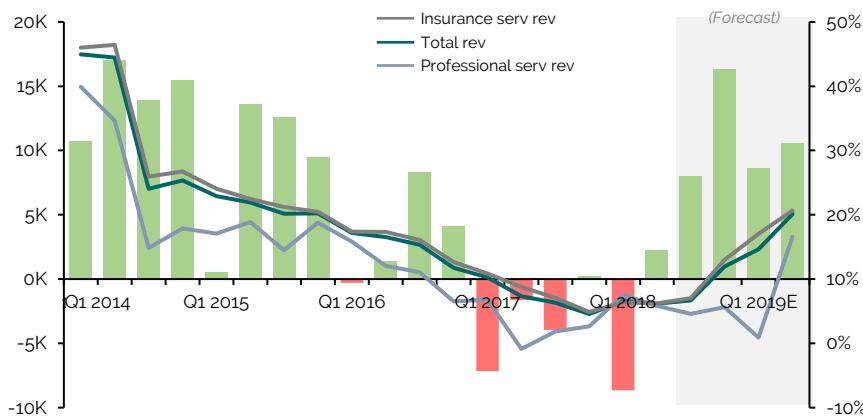


BUSINESS & FINANCIALS

Q3 Will Be a Critical Turning Point, Expect Growth to Bounce Back

TriNet's focus on rolling out its new platform damaged its client employee numbers over the past couple years. Prior to the roll out, management had foreseen the high level of attrition in 2017, and planned for growth to return in the second half of 2018. Q1 2018 was the Company's worst month of attrition when it lost net over 8,500 client employees. We had expected Q2 to also end net negative, the month of April being a big contract renewal quarter, but the Company finished the last of its customer migrations and actually ended the quarter net positive 2,200 client employees – a small yet promising signal.

Client Employee Gain/Loss | Revenue Growth Rates
(Quarterly | YoY)



Q2 2018 YoY growth rates:

- Insurance service revenue: +6.2%
- Professional service rev: +5.9%
- Total revenue: +6.2%
- New sales: +10-12% (est.)
- Net revenue: +9.4%

In Q3 2017, TriNet brought on Barrett Boston as the new Chief Revenue Officer. Prior, Barrett had held executive sales roles at TravelClick, a Thoma Bravo-backed hospitality software provider, and spent over 10 years at IBM. At

TriNet, his primary responsibilities will be increasing customer retention and growing the client employee base. Management has stated repeatedly that growing the client employee number will be its primary focus over the next 12-18 months. The early results have been promising – Q1 and Q2 2018 new sales volume growth were both in the double digits.

We see no barriers to TriNet delivering strong client employee growth numbers in Q3. The platform migration is behind them which will bring attrition back down to more normal levels, Barrett Boston has now had a year to understand how to sell the offerings and the total addressable market is still largely greenfield. Thus, it would come as a shock if Q3 client employee numbers did find a way to disappoint.

Prove Out the Platform, Then Return to M&A

Under General Atlantic's ownership TriNet made on average one acquisition every year, the majority of them being smaller PEOs. Since going public in 2014, TriNet has only made one small technology tuck-in. The Company's balance sheet is currently healthy enough to support a lower mid-market PEO acquisition, but they have not done so. Last quarter, management even seemed reluctant to address its M&A initiatives head on.

Acquisition History

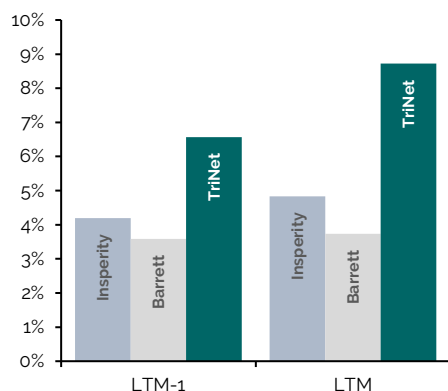
Date	Target
Apr 2016	Teleborder
Mar 2014	IPO
Jul 2013	Ambrose Employer Group
Oct 2012	Strategic Outsourcing
May 2012	ExpenseCloud
Apr 2012	Accord Human Resources
Jun 2009	Gevity HR
April 2008	LMC Resources
Jul 2007	John Parry & Alexander
Jul 2006	The Outsource Group
Jun 2005	Acquired by General Atlantic

M&A is too core of a growth strategy for TriNet to ignore, after all it is how the Company got to where it is today. We speculate that management is likely waiting for organic client employee numbers to stabilize under the new platform first, before considering M&A. If Q3 and Q4 metrics are able to reflect core growth, and more importantly sustainable client retention, then acquiring other PEOs will return as a top priority (making sure they can keep their existing clients before paying for new ones). This is exactly why the client employee number will be the most important metric over the next 6-12 months. If TriNet's Spruce Goose can indeed take off, then reimplementing their old roll-up strategy will make it soar.

Crazy Profitable

Despite losing 6.3% of their client employee base between Q4 2016 to Q1 2018, TriNet still managed to grow net revenue 27%. This points to a positive shift in pricing power and product mix, and we estimate that this directly attributed to \$56-58M of Q1 and Q2 net revenue. Cash flow from operations increased 75% to \$253M between 2016 and 2017, and free cash flow per share increased 150% to \$3.66/share. Over the next 12 months, we are projecting for net revenue to reach 20-25% YoY growth, but driven primarily by client employee growth rather than product mix.

EBITDA Margin vs Comps



Q2 adjusted EBITDA-per-CE increased 37% YoY. Operating expenses have remained flat since Q1 2017, with sales & marketing spend trending back down to 2015 levels. Management has been trying to deal with recent sales team churn, but with a new platform, and leadership, in place we do not see this problem being a lasting issue. We project the Company will increase sales & marketing spend in the short-term which will stabilize adjusted EBITDA-per-CE at slightly under \$300/CE.

Net Revenue | Growth (Quarterly | YoY)

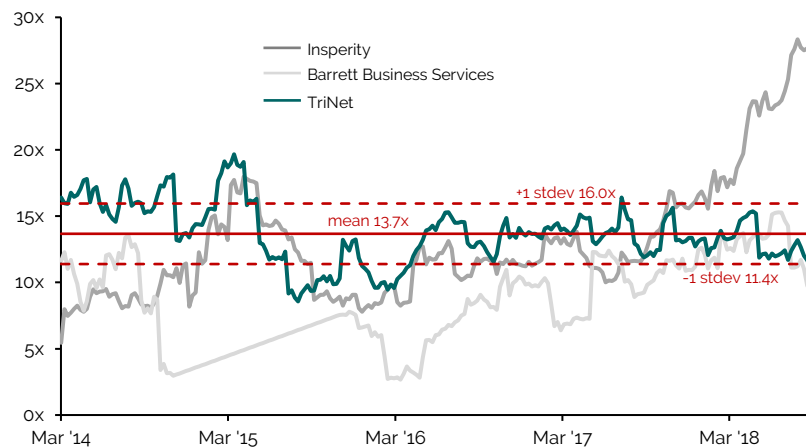


TriNet generates considerable returns for its equity investors. The Company does this, in part, by being highly leveraged. There is \$423M of debt on the balance sheet (54% debt-to-capital), which is extremely high considering Insperty only holds \$104M of debt and has an even larger market cap (\$4.9B). The Company pays a LIBOR floating rate for its debt which can be serious risk factor if the business starts turning south. Fortunately, the Company makes up for all of this by being hugely profitable. We do not expect to see any debt servicing problems to arise in the near term.

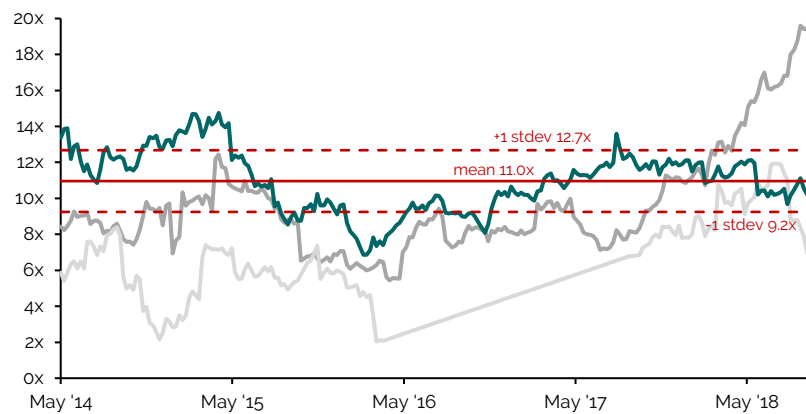
2017 return metrics:

- Free cash flow yield: 8.3%
- Return on equity: 148.0%
- Return on invested capital: 34.0%

EV/EBITDA LTM vs Comps



EV/EBITDA NTM vs Comps



P/E NTM vs Comps



Equity is Undervalued

Our discounted cash flow models show fair value market cap to be in the range of \$4.8-5.2B, implying a fair value share price of between \$66-72/share (assumes 11-13% WACC and a LTM EBITDA exit multiple of 10x). Realistically, the market is will to support a much higher EBITDA exit multiple, making our projections rather conservative. TriNet's share price closed 9/25/2018 trading at \$54.66

TriNet shares are currently trading cheap versus the broader market:

- EV/EBITDA LTM is 11.1x vs 13.6x for SP500
- P/E LTM is 17.1x vs 20.4x for SP500

Shares are also trading near low-end of the historical valuation ranges. The Company is currently being valued like its smaller competitor Barrett, which should not be the case given it is nearly 4x larger in revenue and generates 3x more EBITDA. Insperity, which is closer in size yet still only half as profitable as TriNet, is trading at twice TriNet's multiples.

We believe the Company's lack of recent client employee growth has placed a cap on valuations. For investors, this presents the perfect entry point, given the promising business outlook. We project EV/EBITDA LTM will reach, or surpass, 14-16x within the next 12 months.

PROJECTED FINANCIAL STATEMENTS

INCOME STATEMENT	FY 2017	Q1 2018	Q2 2018	Q3 2018E	Q4 2018E	FY 2018E	FY 2019E	FY 2020E	FY 2021E	FY 2022E	FY 2023E
Professional service revenues	458.17	129.00	115.00	117.68	123.57	485.25	545.98	644.59	723.23	811.46	910.46
Insurance service revenues	2,817.66	732.00	735.00	756.39	825.98	3,049.36	3,664.26	4,566.53	5,199.00	5,890.46	6,673.89
Total Revenue	3,275.83	861.00	850.00	874.07	949.54	3,534.61	4,210.24	5,211.12	5,922.22	6,701.93	7,584.36
Insurance costs	2,465.93	641.00	630.00	642.93	702.08	2,616.01	3,105.02	3,881.55	4,419.15	5,006.89	5,672.81
Cost of providing services excl D&A	213.81	57.00	51.00	52.37	55.60	215.97	245.69	290.06	325.45	365.16	409.71
COGS	2,679.75	698.00	681.00	695.30	757.68	2,831.98	3,350.71	4,171.62	4,744.60	5,372.05	6,082.52
Gross Profit	596.09	163.00	169.00	178.77	191.86	702.63	859.53	1,039.50	1,177.63	1,329.87	1,501.84
Sales and marketing	187.35	39.00	41.00	41.08	47.48	168.56	208.54	286.61	325.72	368.61	417.14
General and administrative	113.73	31.00	31.00	32.34	35.13	129.47	162.19	208.44	242.81	281.48	326.13
Research and development	44.60	13.00	11.00	12.24	13.29	49.53	61.15	83.38	100.68	113.93	128.93
Depreciation	28.21	8.00	8.00	8.13	8.45	32.58	37.56	46.00	55.23	65.41	76.82
Amortization of intangible assets	4.62	1.00	2.00	1.00	1.00	5.00	5.00	5.00	4.00	7.00	0.00
Operating expenses	378.49	92.00	93.00	94.79	105.35	385.15	474.44	629.44	728.44	836.43	949.02
EBIT	217.59	71.00	76.00	83.98	86.50	317.48	385.09	410.07	449.19	493.44	552.81
Interest expense, bank fees and other, net	18.24	4.00	4.00	4.05	4.00	16.05	15.73	14.80	15.71	16.40	15.35
EBT	199.35	67.00	72.00	79.93	82.51	301.44	369.36	395.27	433.48	477.04	537.46
Taxes	21.57	13.00	14.00	20.78	21.45	69.23	73.87	79.05	86.70	95.41	107.49
Net income / loss	177.79	54.00	58.00	59.15	61.06	232.20	295.49	316.21	346.78	381.64	429.97
Net sales	809.90	220.00	220.00	231.14	247.46	918.60	1,105.22	1,329.57	1,503.08	1,695.03	1,911.54
Adj EBITDA	282.42	89.00	96.00	102.54	106.50	394.04	475.16	524.70	582.03	649.90	725.58
Per share											
Basic		\$ 0.77	\$ 0.82	\$ 0.84	\$ 0.87	\$ 3.33	\$ 4.28	\$ 4.61	\$ 5.10	\$ 5.67	\$ 6.45
Diluted	\$ 2.49	\$ 0.75	\$ 0.80	\$ 0.82	\$ 0.84	\$ 3.23	\$ 4.14	\$ 4.47	\$ 4.94	\$ 5.49	\$ 6.25
Weighted average shares											
Basic		70.05	70.40	70.25	70.12	69.65	69.11	68.58	68.04	67.33	66.62
Diluted		72.27	72.60	72.45	72.32	71.85	71.31	70.78	70.24	69.53	68.82
Net revenue/WSE metrics	FY 2017	Q1 2018	Q2 2018	Q3 2018E	Q4 2018E	FY 2018E	FY 2019E	FY 2020E	FY 2021E	FY 2022E	FY 2023E
Net sales rev	809.90	220.00	220.00	231.14	247.46	918.60	1,105.22	1,329.57	1,503.08	1,695.03	1,911.54
Net sales rev/WSE (quarterly)	\$ 2,489	\$ 695	\$ 690	\$ 707	\$ 721	\$ 2,676	\$ 2,847	\$ 3,114	\$ 3,200	\$ 3,281	\$ 3,363
Net sales rev/WSE (monthly)	\$ 830	\$ 232	\$ 230	\$ 236	\$ 240	\$ 892	\$ 949	\$ 1,038	\$ 1,067	\$ 1,094	\$ 1,121
Net insurance serv rev	351.73	91.00	105.00	113.46	123.90	433.35	559.24	684.98	779.85	883.57	1,001.08
Net ins serv rev/WSE (quarterly)	\$ 1,081	\$ 287	\$ 329	\$ 347	\$ 361	\$ 1,263	\$ 1,441	\$ 1,604	\$ 1,660	\$ 1,710	\$ 1,761
Net ins serv rev/WSE (monthly)	\$ 360	\$ 96	\$ 110	\$ 116	\$ 120	\$ 421	\$ 480	\$ 535	\$ 553	\$ 570	\$ 587
BALANCE SHEET	FY 2017	Q1 2018	Q2 2018	Q3 2018E	Q4 2018E	FY 2018E	FY 2019E	FY 2020E	FY 2021E	FY 2022E	FY 2023E
Cash and cash equivalents	336.00	330.00	231.00	376.33	419.54	419.54	647.24	873.59	1,134.07	1,414.73	1,734.37
Restricted cash + investments, current	15.00	15.00	15.00	15.00	15.00	15.00	15.00	15.00	15.00	15.00	15.00
Worksite employee related assets	1,625.00	1,052.00	966.00	961.26	1,413.85	1,413.85	1,684.10	2,084.45	2,368.89	2,680.77	3,033.74
Prepaid expenses and other current assets	15.00	22.00	37.00	37.60	38.71	38.71	46.31	57.32	65.14	73.72	83.43
Total current assets	1,991.00	1,419.00	1,249.00	1,390.19	1,887.10	1,887.10	2,392.65	3,030.36	3,583.10	4,184.22	4,866.54
Restricted cash + investments, noncurrent	162.00	182.00	312.00	211.79	218.28	218.28	262.88	328.93	375.87	427.33	485.57
Workers compensation receivable	39.00	40.00	40.00	41.20	42.42	42.42	50.52	62.53	71.07	80.42	91.01
Property and equipment, net	70.00	74.00	79.00	82.24	85.44	85.44	101.41	124.19	149.10	176.59	207.40
Goodwill and other intangible assets, net	315.00	314.00	312.00	311.00	310.00	310.00	305.00	300.00	296.00	289.00	289.00
Other assets	16.00	18.00	23.00	24.03	24.74	24.74	29.47	36.48	41.46	46.91	53.09
Total assets	2,593.00	2,047.00	2,015.00	2,060.44	2,567.98	2,567.98	3,141.93	3,882.50	4,516.59	5,204.47	5,992.61
AP and other current liabilities	59.00	46.00	39.00	39.63	40.80	40.80	50.52	62.53	71.07	80.42	91.01
Accrued corporate wages	40.00	31.00	35.00	34.33	35.35	35.35	46.31	57.32	65.14	73.72	83.43
Notes payable, current	40.00	43.00	21.00	21.25	21.00	21.00	21.00	21.00	21.00	21.00	21.00
Worksite employee related liabilities	1,618.00	1,052.00	966.00	961.26	1,413.85	1,413.85	1,684.10	2,084.45	2,368.89	2,680.77	3,033.74
Total current liabilities	1,757.00	1,172.00	1,061.00	1,056.47	1,511.00	1,511.00	1,801.93	2,225.30	2,526.10	2,855.91	3,229.18
Notes payable, noncurrent	383.00	370.00	402.00	396.25	391.00	391.00	370.00	349.00	328.00	307.00	286.00
Workers compensation liabilities	165.00	162.00	157.00	161.15	164.81	164.81	201.83	256.18	296.08	340.47	391.42
Other liabilities	82.00	81.00	86.00	86.00	86.00	86.00	86.00	86.00	86.00	86.00	86.00
Total liabilities	2,387.00	1,785.00	1,706.00	1,699.87	2,152.80	2,152.80	2,459.76	2,916.49	3,236.18	3,589.38	3,992.61
Preferred stock	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Common stock	583.00	595.00	611.00	624.42	638.97	638.97	702.48	770.11	847.72	935.76	1,035.70
Accumulated deficit (Treasury)	(377.00)	(332.00)	(302.00)	(263.85)	(223.80)	(223.80)	(20.31)	195.90	432.69	679.32	964.30
Accumulated OCI	0.00	(1.00)	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Total equity	206.00	262.00	309.00	360.57	415.18	415.18	682.17	966.01	1,280.41	1,615.09	2,000.00