
THE SPIN-OFF REPORT

May 18, 2015

Masco Corp. (Pre-Spin)

Current Share Price (5/15/15): \$26.80
Fair Value Estimate: \$33 per share
Shares Outstanding: 348.6 million
Market Capitalization: \$9.2 billion

Ticker: MAS
Dividend: \$0.36
Yield: 1.4%

Masco Corp. (Post-Spin)

Fair Value Estimate: \$31 per share
Shares Outstanding*: 348.6 million
Market Capitalization: \$10.9 billion

Ticker: MAS
Dividend: TBD
Yield: N/A

TopBuild Corp.

Fair Value Estimate: \$1.93 per share
Shares Outstanding*: 348.6 million
Market Capitalization: \$673 million

Ticker: BLD
Dividend: TBD
Yield: N/A

*Assumes a distribution ratio of 1:1.

TBD ó To be determined. N/A ó Not applicable.

Note: Market capitalization is based on fair value estimate for post-spin entities and current market cap for pre-spin Masco Corp.



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Investment Thesis

On September 30, 2014, Masco Corp. (NYSE: MAS) announced a plan to spin off the company's Installation and Other Services businesses ("Services Business") into a separately traded public company. Shares in the new company, which will be named TopBuild Corp., will be distributed to MAS shareholders via a tax-free spin-off. The transaction is expected to be completed by mid-2015 and is subject to any required regulatory approvals, receipt of an opinion from counsel as to the tax-free status of the spin-off, an effectiveness declaration of the company's Form 10 filing with the SEC, and final approval by Masco's Board of Directors. Concurrent with the announcement of the spin-off, MAS announced a series of strategic initiatives, including a share repurchase program of 50 million shares and an expense reduction program estimated to achieve between \$35 million and \$40 million in annual cost savings (excluding \$30 million in one-time charges), primarily through headcount reductions. Jerry Volas, currently Masco Group President, will become Chief Executive Officer of the spin-off company, which will be headquartered in central Florida. Keith Allman, current Chief Executive Officer of Masco, will remain with the parent company, which will continue to be headquartered in Taylor, Michigan.

Masco is a manufacturer of building products as well as a provider of services that include the installation of insulation and other building products. The company, which reported total revenue of \$8.5 billion in 2014, currently operates under five business segments: Plumbing Products, Decorative Architectural Products, Installation and Other Services, Cabinets & Related Products, and Other Specialty Products. The Cabinets and Related segment sells semi-custom assembled cabinetry for kitchen, bath, storage, home office, and entertainment. The plumbing segment sells faucets, bathing, and showering devices sold in North America and Europe under the brand names DELTA, PEERLESS, HANSGROHE, AXOR, and BRIZO, among others. The Decorative Architectural segment sells architectural coatings, including paints, primers, specialty paint products, stains, and waterproofing products, in the U.S., Canada, China, Mexico, and South America under the brand names BEHR and KILZ to "do-it-yourself" and professional customers through home centers, paint stores, and other retailers.

Masco's Installation and Other Services segment, which includes Masco Contractor Services, the leading installer of insulation in the U.S., and Service Partners, a distributor of residential insulation products and related accessories in the U.S., reported revenue of \$1.5 billion in 2014. The business, which comprises over 190 branch locations and over 70 distribution centers, sells installed building products and distributes building products, primarily for new home construction, to contractors and dealers, and, to a lesser extent, retrofit and commercial construction, throughout the U.S. In addition to insulation, this segment sells installed gutters, after-paint products, garage doors, and fireplaces. This segment primarily competes with regional and local contractors and lumber yards.

The spin-off of TopBuild makes sense for Masco for a couple of reasons. First, separating the lower-margin business should immediately improve the financial profile of the parent company. The separation makes the parent company look like a better investment as the lower-margin installation and other services business is jettisoned; EBITDA margins at the parent are expected to improve by over 100 basis points. The parent company appears positioned to benefit from

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both macro tailwinds and the recent restructuring of the struggling cabinets business. New home construction is forecast to remain above 1 million annual starts over the next several years, providing ample opportunities for TopBuild, while contractor confidence in the remodeling market appears bullish for Masco's prospects. Lastly, TopBuild and post-spin Masco serve differing end markets. TopBuild's products are primarily sold for use in new residential construction, whereas the remainder of Masco is focused on repair and remodeling of existing homes. Spinning off the services and installation business creates a less cyclical business at the parent entity with more exposure to the repair and remodeling market versus new home construction. For its part, TopBuild has increased its exposure to commercial construction in an attempt to diversify its revenue away from residential construction. The decision to spin off the Installation and Other Services business follows activist investor Third Point taking a 1.3% stake in mid-2014 and having discussions with MAS management. Third Point subsequently increased its ownership in MAS to 2.9% (10 million shares).

Masco currently trades at a discount to most peers across its diversified portfolio. Separating the installation services business should help alleviate some of the discount, as, optically speaking, the company's margins improve if the lowest-margin business is jettisoned. The discount may also be related to the struggling performance of the company's Cabinets business. While the business has struggled to achieve profitability in recent years, management has right-sized costs for profitable operations in the current housing environment. Any improvement in sales could provide additional upside to projected earnings and fair value.

Based on comparable multiples and cash flow generation potential, a fair value of \$1.93 per share is derived for TopBuild. Post-spin Masco is fairly valued at \$31 per share based on comparable multiples and incorporating cost reduction and a reduced share count. Shares of Masco Corp. are valued at \$33 per share on a sum-of-the-parts basis and are recommended for purchase prior to the spin-off of TopBuild. Following the separation it may be expected that shares of TopBuild would be sold by existing holders, as the larger, higher-margin, more stable business is preferred to TopBuild.

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Company Description

Masco Corp. (NYSE: MAS) is a leading manufacturer of faucets, paint, and cabinets based in Taylor, Michigan. The company's history began in 1929 when founder Alex Manoogian started the Masco Screw Products Company, which was originally focused on machining parts for the automotive industry. The company eventually focused on manufacturing supplies to support America's World War II efforts, allowing it to benefit from technology experimentation and resulting in Masco's becoming a leader in the metalworking industry. Manoogian used Masco's new skills to enter the plumbing products category, inventing the Delta single-handle faucet, which gained almost immediate market acceptance and moved MAS into the building products industry. Masco Screw Products changed its corporate moniker to Masco Corp. in 1961.

Over the next several decades, under the stewardship of Richard Manoogian, the founder's son, the company acquired numerous industrial and building products manufacturers, including its 1985 entrance into the cabinet manufacturing business, and eventually entered the service, architectural coatings (paint), and windows businesses. Since 2000, the company has streamlined its operations by selling non-core businesses. MAS generated \$8.5 billion in revenue and \$984 million in adjusted EBITDA in 2014, representing an 11.5% margin. Since 2009, revenue has increased 9.4% (1.8% CAGR), while adjusted operating margins increased to 9.6% from 5.5% in 2009. Today Masco reports operations under five segments: Plumbing Products, Decorative Architectural Products, Installation and Other Services, Cabinets and Related Products, and Other Specialty Products (see Exhibit 1 on following page).

The **Plumbing Products** segment sells bathroom and kitchen products focused on faucets, bathing, and showering systems that are manufactured by MAS, and a variety of brass and copper components, including fittings used in the installation of faucets, baths, showers, and toilets. Plumbing Products accounted for 39% of Masco's revenue and 52% of adjusted EBITDA (17.5% margin) in 2014. Products are sold directly to major retailers, wholesalers, and distributors. Major brands include DELTA, PEERLESS, HANSGROHE, and AXOR, among others. The company's exposure to the HANSGROHE brand is through 68% ownership of Hansgrohe SE. The plumbing segment also sells spas branded HOT SPRING and CALDERA, among others. Its products are sold in North America and Europe. The company is widening the product offerings within the plumbing segment, recently introducing toilets and other products in an attempt to capture market share through brand awareness.

Decorative Architectural Products (23% of revenue, 34% of adjusted EBITDA, 18.8% adjusted EBITDA margin) comprises MAS's paint, primer, specialty paint products, stains, and waterproofing products. Brand names include BEHR, BEHRPRO, and KILZ. The segment also sells hardware for cabinets, doors, and windows, sold to retailers, original equipment manufacturers, and wholesalers. The segment's largest customer is The Home Depot Inc. (NYSE: HD), the exclusive supplier of BEHR branded paint products. The U.S. consumer paint market (do-it-yourself) totals \$4.9 billion, of which BEHR controls 28%.

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Exhibit 1 Masco Corp: Historical Segment Results

(\$ in millions)

Revenue	2009	2010	2011	2012	2013	2014
Plumbing Products	\$ 2,564	\$ 2,692	\$ 2,913	\$ 2,955	\$ 3,183	\$ 3,308
Decorative Architectural Products	1,714	1,693	1,670	1,818	1,927	1,998
Installation and Other Services	1,256	1,041	1,077	1,209	1,412	1,515
Cabinets and Related Products	1,674	1,464	1,231	939	1,014	999
<u>Other Specialty Products</u>	<u>584</u>	<u>596</u>	<u>576</u>	<u>574</u>	<u>637</u>	<u>701</u>
	\$ 7,792	\$ 7,486	\$ 7,467	\$ 7,495	\$ 8,173	\$ 8,521

Adjusted Operating Income	2009	2010	2011	2012	2013	2014
Plumbing Products	\$ 295	\$ 347	\$ 338	\$ 332	\$ 418	\$ 517
Decorative Architectural Products	376	350	283	329	353	360
Installation and Other Services	(107)	(106)	(71)	(18)	38	60
Cabinets and Related Products	(21)	(71)	(115)	(83)	2	(31)
Other Specialty Products	27	19	4	24	41	48
<u>Corporate</u>	<u>(144)</u>	<u>(109)</u>	<u>(119)</u>	<u>(112)</u>	<u>(134)</u>	<u>(136)</u>
	\$ 426	\$ 430	\$ 320	\$ 472	\$ 718	\$ 818

Adjusted Operating Margin	2009	2010	2011	2012	2013	2014
Plumbing Products	11.5%	12.9%	11.6%	11.2%	13.1%	15.6%
Decorative Architectural Products	21.9%	20.7%	16.9%	18.1%	18.3%	18.0%
Installation and Other Services	-8.5%	-10.2%	-6.6%	-1.5%	2.7%	4.0%
Cabinets and Related Products	-1.3%	-4.8%	-9.3%	-8.8%	0.2%	-3.1%
<u>Other Specialty Products</u>	<u>4.6%</u>	<u>3.2%</u>	<u>0.7%</u>	<u>4.2%</u>	<u>6.4%</u>	<u>6.8%</u>
	5.5%	5.7%	4.3%	6.3%	8.8%	9.6%

Adjusted EBITDA	2009	2010	2011	2012	2013	2014
Plumbing Products	\$ 365	\$ 410	\$ 406	\$ 389	\$ 479	\$ 580
Decorative Architectural Products	394	368	298	344	369	376
Installation and Other Services	(72)	(73)	(39)	12	66	86
Cabinets and Related Products	63	41	(37)	(31)	37	1
Other Specialty Products	55	45	52	45	60	66
<u>Corporate</u>	<u>(127)</u>	<u>(89)</u>	<u>(103)</u>	<u>(112)</u>	<u>(123)</u>	<u>(125)</u>
	\$ 678	\$ 702	\$ 577	\$ 647	\$ 888	\$ 984

Adjusted EBITDA Margin	2009	2010	2011	2012	2013	2014
Plumbing Products	14.2%	15.2%	13.9%	13.2%	15.0%	17.5%
Decorative Architectural Products	23.0%	21.7%	17.8%	18.9%	19.1%	18.8%
Installation and Other Services	-5.7%	-7.0%	-3.6%	1.0%	4.7%	5.7%
Cabinets and Related Products	3.8%	2.8%	-3.0%	-3.3%	3.6%	0.1%
<u>Other Specialty Products</u>	<u>9.4%</u>	<u>7.6%</u>	<u>9.0%</u>	<u>7.8%</u>	<u>9.4%</u>	<u>9.4%</u>
	8.7%	9.4%	7.7%	8.6%	10.9%	11.5%

Capital Expenditures	2009	2010	2011	2012	2013	2014
Plumbing Products	\$ (47)	\$ (65)	\$ (85)	\$ (67)	\$ (71)	\$ (65)
Decorative Architectural Products	(7)	(9)	(8)	(11)	(16)	(12)
Installation and Other Services	(30)	(6)	(9)	(11)	(14)	(13)
Cabinets and Related Products	(30)	(34)	(26)	(15)	(9)	(9)
Other Specialty Products	(7)	(18)	(17)	(11)	(10)	(28)
<u>Corporate</u>	<u>(1)</u>	<u>(4)</u>	<u>(6)</u>	<u>(2)</u>	<u>(4)</u>	<u>(1)</u>
	\$ (122)	\$ (136)	\$ (151)	\$ (117)	\$ (124)	\$ (128)

Source: Company reports and Bloomberg.

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Installation and Other Services sells and distributes building products for use in new home construction, home remodels, and commercial construction in the U.S. The segment operated with a 5.7% margin in 2014, generating \$1.5 billion of revenue (18% of the total) and \$86 million of adjusted EBITDA (8%). While sales are primarily related to insulation, the product portfolio also includes gutters, garage doors, and fireplaces. Insulation installation and distribution sales comprised 13% of overall sales in 2014. The segment's profitability is heavily tied to new home construction, which has picked up in recent years, improving segment profitability. Installation services are provided through 190 locally branded branches across 43 states, while distribution is accomplished from 72 distribution centers across 35 states.

Masco also sells stock and semi-custom cabinets through its **Cabinets and Related Products** segment. The segment generated revenue of \$999 million (12% of the total) and negligible adjusted EBITDA of \$1 million in 2014. Cabinetry is available for kitchen, bath, storage, home office, and home entertainment under the brand names KRAFTMAID, sold primarily to dealers, home centers, and mass merchants, and MERILLAT, MOORES, and QUALITY CABINETS, sold to dealers and homebuilders for home improvement and new home construction. The cabinets segment is also highly tied to new home construction and home remodels. As such, the segment was significantly affected by the most recent housing industry collapse. As a point of reference, in 2006 the segment had sales of \$3.3 billion while generating operating income of \$122 million, and prior to 2006 the segment achieved operating margins in the mid-teens. Since the housing crash, however, profitability on a consistent basis has been elusive. In an attempt to improve segment earnings, the company has consolidated North American manufacturing plants, increased brand building efforts, and introduced new products.

Other Specialty Products manufactures and sells windows (vinyl, fiberglass, and aluminum), patio doors, and windows and doors that combine wood interiors with fiberglass exteriors. Products are sold primarily through dealers, with some direct sales to homebuilders, lumber yards, and home centers. Brands include PELLA and ANDERSON, along with regional brands in the U.S., while in the U.K. products are branded GRIFFIN, PREMIER, and DURAFLEX. The segment generated \$701 million in sales and \$66 million in adjusted EBITDA, representing 8% and 6% of Masco's 2014 results, respectively.

On September 30, 2014, Masco announced its intention to spin off the company's Installation and Other Services business into a separately traded public company. Shares in the new company, which will be named TopBuild Corp., will be distributed to MAS shareholders via a tax-free spin-off. The transaction is expected to be completed by mid-2015 and is subject to any required regulatory approvals, receipt of an opinion from counsel as to the tax-free status of the spin-off, an effectiveness declaration of the company's Form 10 filing with the SEC, and final approval by Masco's Board of Directors. Concurrent with the announcement of the spin-off, MAS disclosed a series of strategic initiatives, including a share repurchase program of 50 million shares and an expense reduction program estimated to achieve between \$35 million and \$40 million in annual cost savings (excluding \$30 million in one-time charges), primarily through headcount reductions.

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TopBuild Corp.

TopBuild will consist of the current Installation and Other Services businesses, which provides installation and distribution services, primarily related to the sale of insulation. Insulation products include fiberglass batts and rolls, blown-in loose-fill fiberglass, blown-in loose-fill cellulose, and polyurethane spray foam. TopBuild also supplies insulation accessories, including caulks, sealants, fasteners, and installation safety equipment, among others. Additionally, the company sells other building products (both distribution and installation) including rain gutters, garage doors, and shower enclosures, among others.

End-market sales are highly concentrated to residential new construction, 66% of sales in 2014, with a residential repair/remodel contribution of 18%, and commercial construction at 16%. The company will operate two distinct segments: Installation and Distribution. Installation services are facilitated through over 190 branches spread across 43 states, while Distribution services has 72 distribution centers in 35 states (see Exhibit 2). Installation services that historically operated under the Masco Contractor Services banner have been renamed TruTeam Contractor Services. Distribution services will continue to operate under the Service Partners brand name. Installation comprises 64% of sales, with Distribution making up the remainder.

Exhibit 2 TopBuild Corp.: Distribution and Installation Locations and Product Sales



	<u>2012</u>	<u>2013</u>	<u>2014</u>
Insulation	68%	70%	71%
Rain gutters	7%	7%	7%
Garage doors	2%	3%	3%
Roofing material	4%	3%	2%
<u>Other building products</u>	<u>19%</u>	<u>17%</u>	<u>17%</u>
	100%	100%	100%

○ TruTeam Locations
★ Service Partners Locations

Source: Company reports.

TopBuild had sales of \$1.5 billion in 2014, and generated \$66.8 million in EBITDA (4.4% margin). Revenue has increased from \$1.0 billion in 2010 based on a strengthening housing market (discussed in the Outlook section of this report). The Distribution segment carries a higher operating margin than Installation at 8.3% margin (before corporate expenses) versus 2.5% for Installation (see Exhibit 3). Given the higher level of depreciation associated with the Installation business, that segment's EBITDA margin would increase to 4.8% versus 8.9% at the Distribution business.

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Exhibit 3 TopBuild Corp.: Historical Segment Results

(\$ in thousands)

	<u>2012</u>	<u>2013</u>	<u>2014</u>		<u>2012</u>	<u>2013</u>	<u>2014</u>
Net Sales				Depreciation and Amortization			
Installation	744,910	904,570	963,350	Installation	25,740	23,930	22,560
Distribution	528,330	578,140	628,810	<u>Distribution</u>	<u>3,900</u>	<u>3,560</u>	<u>3,520</u>
<u>Intercompany eliminations</u>	<u>(65,350)</u>	<u>(71,180)</u>	<u>(80,080)</u>	Total*	29,640	27,490	26,080
Total	1,207,890	1,411,530	1,512,080				
				Segment EBITDA			
Segment Operating Profit (Loss)				Installation	(10,820)	30,090	46,530
Installation	(36,560)	6,160	23,970	<u>Distribution</u>	<u>41,020</u>	<u>49,970</u>	<u>55,850</u>
Distribution	37,120	46,410	52,330	Total*	10,620	73,670	88,750
<u>Intercompany eliminations</u>	<u>(19,580)</u>	<u>(6,390)</u>	<u>(13,630)</u>				
Total	(19,020)	46,180	62,670	Segment Operating Margin			
				Installation	-4.9%	0.7%	2.5%
General corporate expense, net	(20,910)	(22,070)	(21,950)	<u>Distribution</u>	<u>7.0%</u>	<u>8.0%</u>	<u>8.3%</u>
<u>Charge for litigation settlements</u>	<u>(76,000)</u>	<u>-</u>	<u>-</u>	Total*	-1.6%	3.3%	4.1%
Total operating profit (loss)	\$ (115,930)	\$ 24,110	\$ 40,720				
<u>Other income (expense), net</u>	<u>(13,810)</u>	<u>(13,330)</u>	<u>(12,380)</u>	Segment EBITDA Margin			
Pre Tax Income	(129,740)	10,780	28,340	Installation	-1.5%	3.3%	4.8%
				<u>Distribution</u>	<u>7.8%</u>	<u>8.6%</u>	<u>8.9%</u>
Corporate EBITDA	\$ (10,290)	\$ 51,600	\$ 66,800	Total*	0.9%	5.2%	5.9%
Margin	N/A	3.7%	4.4%				

* excludes corporate expenses

Source: Company reports.

The company expects to incur \$200 million in debt, with proceeds being used to fund a \$200 million cash distribution to MAS. The company also plans to have in place a \$100-\$150 million credit facility.

Masco Corp.: Post Spin

Following the spin-off of TopBuild, Masco's financial profile will be improved due to the removal of the lower-margin Installation and Other Services segment. On a pro forma basis, Masco (ex TopBuild) generated \$7 billion in revenue and \$899 million in adjusted EBITDA in 2014 (see Exhibit 4).

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Exhibit 4 Masco Corp.: Historical Segment Results, ex TopBuild

(\$ in millions)

Revenue	2009	2010	2011	2012	2013	2014
Plumbing Products	\$ 2,564	\$ 2,692	\$ 2,913	\$ 2,955	\$ 3,183	\$ 3,308
Decorative Architectural Products	1,714	1,693	1,670	1,818	1,927	1,998
Cabinets and Related Products	1,674	1,464	1,231	939	1,014	999
<u>Other Specialty Products</u>	<u>584</u>	<u>596</u>	<u>576</u>	<u>574</u>	<u>637</u>	<u>701</u>
	\$ 6,536	\$ 6,445	\$ 6,390	\$ 6,286	\$ 6,761	\$ 7,006
Adjusted Operating Income	2009	2010	2011	2012	2013	2014
Plumbing Products	\$ 295	\$ 347	\$ 338	\$ 332	\$ 418	\$ 517
Decorative Architectural Products	376	350	283	329	353	360
Cabinets and Related Products	(21)	(71)	(115)	(83)	2	(31)
Other Specialty Products	27	19	4	24	41	48
<u>Corporate</u>	<u>(144)</u>	<u>(109)</u>	<u>(119)</u>	<u>(112)</u>	<u>(134)</u>	<u>(136)</u>
	\$ 533	\$ 536	\$ 391	\$ 490	\$ 680	\$ 758
Depreciation and Amortization	2009	2010	2011	2012	2013	2014
Plumbing Products	\$ 70	\$ 63	\$ 68	\$ 57	\$ 65	\$ 63
Decorative Architectural Products	18	18	15	15	17	16
Cabinets and Related Products	84	112	78	41	42	33
Other Specialty Products	28	26	48	21	22	18
<u>Corporate</u>	<u>17</u>	<u>20</u>	<u>16</u>	<u>-</u>	<u>11</u>	<u>11</u>
	\$ 217	\$ 239	\$ 225	\$ 134	\$ 157	\$ 141
Adjusted EBITDA	2009	2010	2011	2012	2013	2014
Plumbing Products	\$ 365	\$ 410	\$ 406	\$ 389	\$ 479	\$ 580
Decorative Architectural Products	394	368	298	344	369	376
Cabinets and Related Products	63	41	(37)	(31)	37	1
Other Specialty Products	55	45	52	45	60	66
<u>Corporate</u>	<u>(127)</u>	<u>(89)</u>	<u>(103)</u>	<u>(112)</u>	<u>(123)</u>	<u>(125)</u>
	\$ 750	\$ 775	\$ 616	\$ 635	\$ 822	\$ 898
Adjusted EBITDA Margin	2009	2010	2011	2012	2013	2014
Plumbing Products	14.2%	15.2%	13.9%	13.2%	15.0%	17.5%
Decorative Architectural Products	23.0%	21.7%	17.8%	18.9%	19.1%	18.8%
Cabinets and Related Products	3.8%	2.8%	-3.0%	-3.3%	3.6%	0.1%
<u>Other Specialty Products</u>	<u>9.4%</u>	<u>7.6%</u>	<u>9.0%</u>	<u>7.8%</u>	<u>9.4%</u>	<u>9.4%</u>
Total (inc. Corporate Expense)	11.5%	12.0%	9.6%	10.1%	12.2%	12.8%

Source: Company reports, Bloomberg.

Outlook

Masco's product and service sales, in the current corporate structure, are predominantly focused in North America (81%), with a heavy bias toward the repair and remodel end market (71%) versus new construction (see Exhibit 5). The obvious outlier is the Installation and Other Services segment (to become TopBuild), which is predominantly focused on new construction (82%). Following the separation of TopBuild, North American exposure will decline to 77% owing to the larger contribution of Plumbing Products, while repair and remodel exposure will increase to over 82% of sales.

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Exhibit 5 Masco Corp.: End-Market and Geographical Concentration of Sales

(\$ in billions)

	PRESPIN				POST SPIN MAS			
	Revenue	% of	R&R %	NA %	Revenue	% of	R&R %	NA %
	<u>2014</u>	<u>Total</u>	<u>vs. NC</u>	<u>vs. Int'l</u>	<u>2014</u>	<u>Total</u>	<u>vs. NC</u>	<u>vs. Int'l</u>
Plumbing Products	\$3.3	39%	82%	59%	\$3.3	47%	82%	59%
Decorative Architectural Products	\$2.0	23%	99%	100%	\$2.0	29%	99%	100%
Installation and Other Services	\$1.5	18%	18%	100%				
Cabinets and Related Products	\$1.0	12%	55%	91%	\$1.0	14%	55%	91%
<u>Other Specialty Products</u>	<u>\$0.7</u>	<u>8%</u>	<u>74%</u>	<u>74%</u>	<u>\$0.7</u>	<u>10%</u>	<u>74%</u>	<u>74%</u>
Total Company	\$8.5	100%	71%	81%	\$7.0	100%	82%	77%

R&R = % of sales to repair and remodel channels.

NC = % of sales to new construction channels.

NA = % of sales within North America.

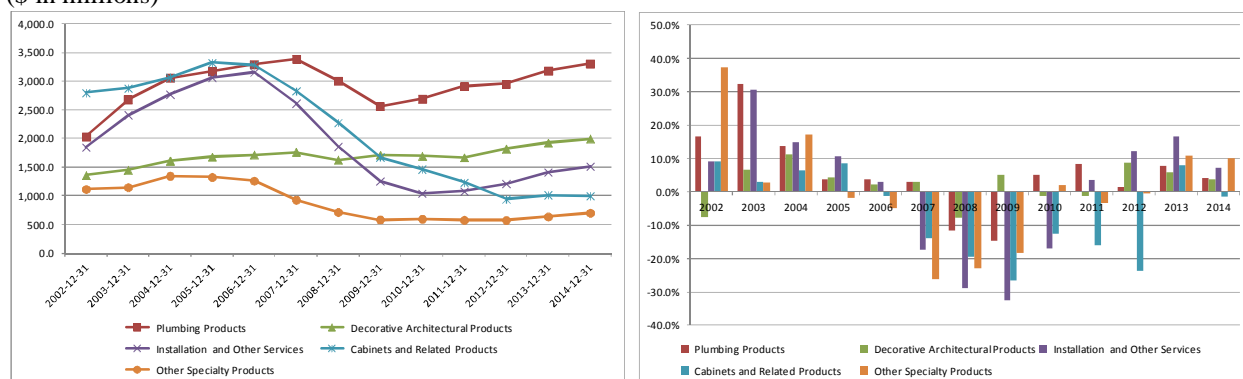
Int'l = % of sales outside of North America.

Source: Company reports, *The Spin-Off Report* estimates.

Given that Masco's product and service portfolios are heavily tied to residential construction, it is not surprising that across each segment the company experienced significant revenue declines associated with the housing market crash and the resultant recession of 2007 through 2009 (see Exhibit 6). The notable exception to the sustained decline in sales was the Decorative Architectural Products segment (paint), where demand experienced only a modest decline initially, before returning to growth (see Exhibit 6).

Exhibit 6 Masco Corp.: Historical Revenue Trends

(\$ in millions)

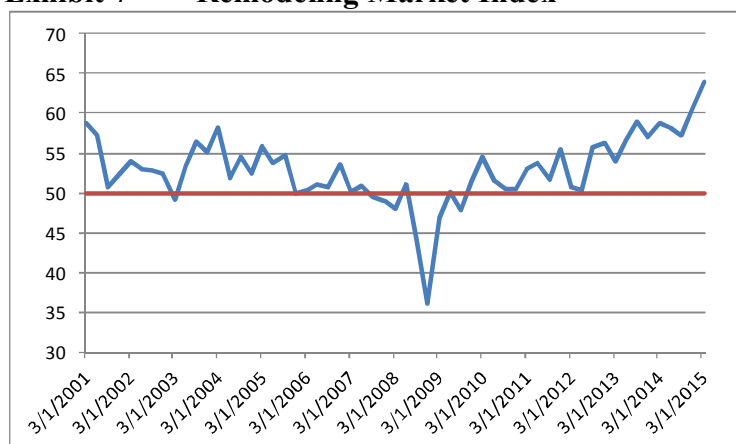


Source: Company reports.

MAS's paint sales are almost exclusively tied to home remodels by do-it-yourselfers, with painting being a relatively low-cost component that held fairly steady through the economic downturn. BEHR paint products are exclusively sold at Home Depot. Decorative Architectural Products would have contributed 37% of adjusted EBITDA in 2014 on a pro forma basis. For insight into the strength of the North American remodeling market, investors can look to the National Association of Home Builders' remodeling market index (RMI). The index, which is a quarterly survey of 2,000 residential remodelers in the U.S., has been above 50 (the level indicating increased activity versus the prior quarter) since late 2009 (see Exhibit 7). Sustained increases in North American remodeling activity should support future growth for post-spin Masco.

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Exhibit 7 Remodeling Market Index



Source: National Association of Home Builders.

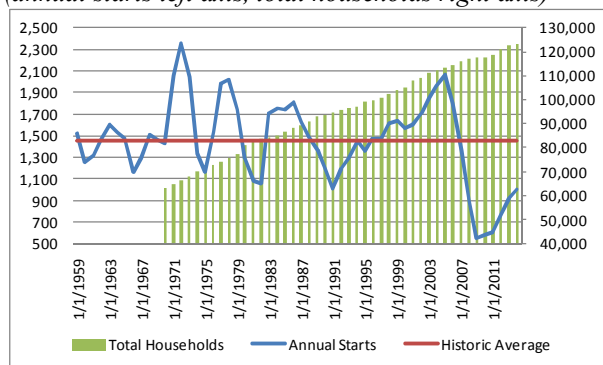
New housing starts can also be used to help anticipate product demand for the remainder of Masco's sales, and for demand for the installation and other services that will become TopBuild. TopBuild's sales are 82% related to new construction. Cabinet sales are roughly 55% remodels and 45% new home construction. As of the latest reading, annual housing starts of 926,000 (March 2015) remain well below the historical average of 1.4 million since 1959 (see Exhibit 8). However, increased activity since the bottoming in 2009 (below 500,000) should also support growth. It can be noted that month-to-month starts data can be lumpy due to several factors, including weather, and management states that insulation installation typically lags housing starts by a couple of months. Recent increases signal that demand for TopBuild's products and services should continue to climb over the next year. Longer term it is expected that housing starts should return to the historical average of approximately 1.5 million by 2020. It should be noted that while projections call for housing starts to revert to the historical mean, this may actually underestimate the potential demand for new housing. As a point of reference, there were 52.8 million total households in 1970, and at year end 2014 the number increased to 123.2 million.

Exhibit 8 U.S. Housing Starts

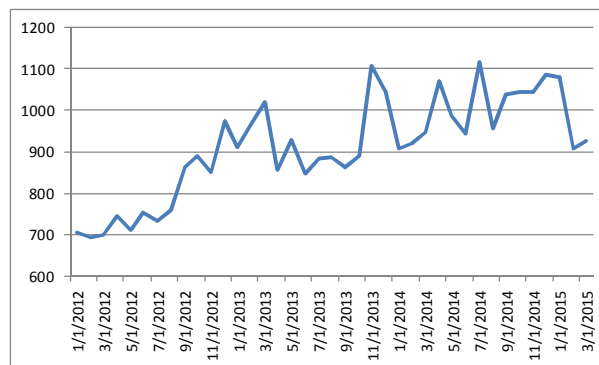
(starts in thousands)

Annual since 1959

(annual starts left axis, total households right axis)



Monthly since January 2012



Source: National Association of Home Builders

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A return to the historical starts average is not necessarily required to benefit the Cabinets division. Since the downturn, capacity has been reduced at the Cabinet segment. While tied to new home construction, Cabinet sales and profit have yet to experience a rebound. On a pro forma basis, Cabinets will contribute about 15% of revenue and 0.1% of adjusted EBITDA (before corporate expenses). If MAS has right-sized the Cabinet segment's cost structure, at current sales levels the company can operate generating a marginal level of profit. If the company is able to accelerate sales, margins could increase dramatically. Prior to the housing downturn, the Cabinets business was generating mid-teens operating margins. As a point of reference, competitors American Woodmark Corp. (NASDAQ: AMWD), Fortune Brands Home & Security Inc. (NYSE: FBHS), and Norcraft Companies (NYSE: NCFT) each have cabinet manufacturing operations similar to that of MAS. The peers operate within a wide range of margins (~5%-11%); however, each company's cabinet operating margins significantly exceed that of MAS.

At year-end 2007, MAS had 32 manufacturing properties (19 in North America) and 38 warehouse and distribution facilities (23 in North America) related to the Cabinet segment. At year-end 2014, the company had 9 cabinet manufacturing facilities (8 in North America) and 8 warehouse and distribution sites (7 in North America). This reduction does include the exit of less profitable product lines. With slimmed-down manufacturing overhead, modest increases in sales should provide a high degree of fixed cost leverage and could become a significant earnings growth factor in future years. Anecdotally, in March 2015, Fortune Brands announced that it would acquire Norcraft to expand its cabinet operations.

In conjunction with the initial spin announcement, Masco also disclosed a 50 million share repurchase authorization and a plan to reduce corporate costs by \$35-\$40 million over the next three years. Masco currently has \$4.1 billion in long-term debt (including minority interest) and \$1.8 billion in cash. In MAS's 1Q 2015 earnings conference call, management noted that it had repurchased 1.4% of shares outstanding during the quarter for \$106 million, that it expects to retire \$400-\$500 million in shares in 2015, and that it is positioned to retire \$300-\$500 million in debt in 2016.

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Valuation

TopBuild Corp.

TopBuild is a somewhat unusual business in that it primarily competes with contractors (national and local); however, given its business model of both installing the building products and distributing the products, it also sells to its competitors through the distribution segment. Given that most contractors are not public, and instead are smaller in nature, a peer group is limited to select building products manufacturers and installers. The comp group includes Installed Building Products Inc. (NYSE: IBP), Builders FirstSource Inc. (NASDAQ: BLDR), and Stock Building Supply Holdings Inc. (NASDAQ: STCK) (see Exhibit 10 on next page), most of which are focused more on wood-based products (floor and roof trusses, among others) than on insulation as is the case for TopBuild. Some of these peers also compete against segments that will remain with Masco. HD Supply Holdings Inc. (NASDAQ: HDS) can also be included as a comparable; however, the company distributes a wider array of products that extend beyond building products (janitorial supplies). On average the peer group trades at 23.7x 2015E consensus earnings (excluding outliers) and 15.7x 2016E consensus EPS. (See Exhibit 10)

In projecting an earnings scenario for TopBuild, a forecast for housing starts can be used to estimate revenue. The National Association of Home Builders forecasts 2015 starts of 1.099 million and 2016 starts of 1.398 million. NAHB's 2016 forecast appears aggressive, as it implies a nearly 27% year-over-year increase following a 10% forecast increase in 2015. A more conservative and likely more realistic estimate would imply 1.25 million starts in 2016. Management has stated that at the level of 750,000 housing starts, the company would operate at break-even under its current cost structure. Incremental margin above the break-even level approximates 20%. Assuming 8% and 10% revenue growth in 2015E and 2016E, respectively, TopBuild could generate revenue of \$1.8 billion in 2016E. Assuming EBITDA margins of 5.5%, \$26 million in depreciation and amortization, and a 36% tax rate, TopBuild would earn \$0.12 per share in 2016E, assuming a one-for-one share distribution. The 5.5% EBITDA margin appears reasonable, given that the company operated at a 4.4% margin in 2014 and considering incremental 20% margins. The 2016 forecast revenue implies a \$284 million increase over 2014, or an additional \$56.9 million in EBITDA at a 20% margin, versus \$66.8 million in 2014. Applying a 15.7x multiple to our 2016 EPS estimate results in a fair value estimate of \$1.93 per share (see Exhibit 9).

Exhibit 9 TopBuild Corp.: Fair Value Estimate Based on 2016E EBITDA

(\$ in millions, except per share data; shares in millions)

2014 Revenue	1,512.1	2016E EBIT	72.8
<u>2015E Revenue Growth</u>	<u>8.0%</u>	<u>Interest Expense</u>	<u>6.0</u>
2015E Revenue	1,633.0	Pre Tax Income	66.8
<u>2016E Revenue Growth</u>	<u>10%</u>	Tax Rate	36.0%
2016E Revenue	1,796.4	<u>Tax Expense</u>	<u>24.0</u>
<u>2016E EBITDA Margin</u>	<u>5.5%</u>	Net Income	42.8
2016E EBITDA	98.8	<u>Shares Outstanding</u>	<u>348.6</u>
<u>D&A</u>	<u>26.0</u>	EPS	\$ 0.12
2016E EBIT	72.8	<u>Multiple</u>	<u>15.7x</u>
		FVE	\$ 1.93

Source: Company reports, Bloomberg, *The Spin-Off Report* estimates.

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Exhibit 10 Masco Corp. Peer Comparisons

(\$ in millions, except per share data; shares in millions)

Ticker	INSTALLATION SERVICES					DECORATIVE ARCHITECTURAL PRODUCTS						PLUMBING PRODUCTS			CABINETS			OTHER			
	Installed	Stock	HD			Sherwin-		PPG	Axalta			Spectrum	Fortune		Fortune	American		Fortune			
	Masco Corp	Products	Builders	Building	Supply	Williams	Valspar	Industries	Coating	RPM	Akzo	Brands	Brands	Whirlpool	Brands	Woodmark	Norcraft	Ply Gem	Brands	Masonite	
MAS	Inc	FirstSource	Supply	Holdings	Co/The	Corp/The	Inc	Ltd	Inc	Nobel NV	Holdings	Home &	Corp	Home &	Corp	Cos Inc	Holdings	Home &	Security		
	IBP	BLDR	STCK	HDS	SHW	VAL	PPG	AXTA	RPM	AKZA NA	SPB	Security	FBHS	FBHS	AMWD	NCFT	PGEM	PGTI	FBHS	DOOR	
Price	\$ 27.05	\$ 20.82	\$ 12.58	\$ 19.04	\$ 32.40	\$ 291.71	\$ 85.84	\$ 230.13	\$ 34.30	\$ 50.32	\$ 67.03	\$ 93.61	\$ 45.30	\$ 186.71	\$ 45.30	\$ 51.39	\$ 25.50	\$ 12.73	\$ 12.20	\$ 45.30	\$ 68.76
Shares Out	342.6	31.5	98.5	26.2	196.0	93.2	81.5	135.9	229.8	133.2	246.9	53.3	159.4	78.0	159.4	15.9	17.3	67.9	47.6	159.4	30.1
Market Capitalization	9,429.5	652.6	1,248.7	498.4	6,391.1	27,183.4	6,974.3	31,280.6	7,884.2	6,703.7	16,547.6	5,495.2	7,221.8	14,683.7	7,221.8	817.3	483.2	864.8	582.5	7,221.8	2,075.6
Net Debt (Cash)	2,339.0	43.0	372.0	79.4	5,172.0	2,467.2	1,514.5	3,554.0	3,454.7	1,649.9	2,808.0	3,332.0	584.5	4,842.0	584.5	(140.3)	99.1	1,032.4	144.7	584.5	411.5
EV	11,768.5	695.6	1,620.7	577.8	11,563.1	29,650.6	8,488.8	34,834.6	11,338.9	8,353.6	19,355.6	8,827.2	7,806.3	19,525.7	7,806.3	677.0	582.3	1,897.1	727.2	7,806.3	2,487.1
Revenue 2014E	8,521.0	518.0	1,604.1	1,295.7	8,228.0	11,129.5	4,522.4	15,360.0	4,391.5	4,376.4	14,296.0	4,429.1	4,013.6	19,872.0	4,013.6	726.5	376.0	1,566.6	306.4	4,013.6	1,837.7
Revenue 2015E	8,753.9	639.0	1,938.2	1,421.0	8,897.7	11,852.8	4,530.2	15,782.4	4,296.6	4,589.9	14,908.3	4,583.1	4,472.9	22,171.8	4,472.9	828.3	410.0	1,956.8	389.2	4,472.9	1,926.3
Revenue 2016E	9,106.1	748.7	3,705.8	1,634.0	9,481.9	12,589.8	4,754.9	16,501.1	4,516.2	4,968.4	15,422.4	4,809.3	4,926.4	23,110.4	4,926.4	913.3	447.0	2,135.4	428.8	4,926.4	2,110.0
EBITDA																					
2014	955.0	40.6	59.5	31.7	718.0	1,503.0	660.8	2,307.0	699.2	575.7	1,605.0	639.6	502.3	1,748.0	502.3	48.6	45.7	110.0	42.4	502.3	94.3
2015E	1,097.0	69.0	93.0	47.8	852.8	1,806.0	726.6	2,673.3	877.2	605.5	2,081.8	764.7	613.8	2,219.6	613.8	67.0	62.3	173.8	70.3	613.8	191.8
2016E	1,233.2	96.4	193.7	72.8	961.1	2,028.6	786.5	2,900.9	960.1	702.7	2,219.6	830.9	735.2	2,633.5	735.2	81.7	72.1	230.8	84.1	735.2	240.7
EV/Sales ttm	1.3x	1.2x	0.6x	0.4x	1.2x	2.6x	1.8x	2.2x	N/A	1.9x	1.4x	1.8x	1.9x	1.0x	1.9x	0.6x	1.1x	1.2x	2.0x	1.9x	1.3x
EV/Sales 2015E	1.3x	1.1x	0.8x	0.4x	1.3x	2.5x	1.9x	2.2x	2.6x	1.8x	1.3x	1.9x	1.7x	0.9x	1.7x	0.8x	1.4x	1.0x	1.9x	1.7x	1.3x
EV/Sales 2016E	1.3x	0.9x	0.4x	0.4x	1.2x	2.4x	1.8x	2.1x	2.5x	1.7x	1.3x	1.8x	1.6x	0.8x	1.6x	0.7x	1.3x	0.9x	1.7x	1.6x	1.2x
EV / EBITDA																					
2014	12.3x	17.1x	27.2x	18.2x	16.1x	19.7x	12.8x	15.1x	16.2x	14.5x	12.1x	13.8x	15.5x	11.2x	15.5x	13.9x	12.7x	17.3x	17.2x	15.5x	26.4x
2015E	10.7x	10.1x	17.4x	12.1x	13.6x	16.4x	11.7x	13.0x	12.9x	13.8x	9.3x	11.5x	12.7x	8.8x	12.7x	10.1x	9.3x	10.9x	10.3x	12.7x	13.0x
average		13.3x				12.9x						11.0x			10.7x			11.7x			
2016E	9.5x	7.2x	8.4x	7.9x	12.0x	14.6x	10.8x	12.0x	11.8x	11.9x	8.7x	10.6x	10.6x	7.4x	10.6x	8.3x	8.1x	8.2x	8.6x	10.6x	10.3x
average		8.9x				11.6x						9.6x			9.0x			9.5x			
P/E 2014	27.6x	39.1x	73.1x	38.1x	61.4x	33.1x	20.8x	23.9x	41.6x	23.3x	21.8x	22.0x	24.5x	16.9x	24.5x	38.0x	31.4x	909.3x	27.5x	24.5x	N/A
P/E 2015	22.0x	21.0x	33.4x	23.9x	26.1x	25.9x	18.6x	20.1x	30.8x	21.7x	17.5x	21.4x	22.1x	15.0x	22.1x	25.5x	21.3x	26.2x	20.1x	22.1x	53.7x
average		26.1x				22.4x						19.5x			22.9x			30.5x			
P/E 2016	17.4x	14.0x	12.6x	14.4x	17.1x	22.3x	16.4x	17.7x	24.9x	18.5x	16.1x	19.1x	18.0x	12.1x	18.0x	20.2x	16.9x	10.6x	15.6x	18.0x	27.0x
average		14.5x				19.3x						16.4x			18.4x			17.8x			
P/B	12.1x	7.1x	36.5x	3.5x	N/A	57.9x	7.3x	6.2x	8.1x	5.4x	2.7x	4.8x	3.1x	3.0x	3.1x	3.6x	11.3x	N/A	7.1x	3.1x	3.2x
average		15.7x				14.6x						3.7x			6.0x			4.5x			
ROA 2014	12.1%	6.6%	3.3%	3.0%	-3.2%	14.3%	8.6%	12.6%	0.4%	6.9%	3.4%	3.8%	3.8%	3.7%	3.8%	6.6%	1.1%	-2.7%	7.0%	3.8%	-2.3%
ROE 2014	113.1%	N/A	65.3%	7.8%	N/A	63.1%	32.4%	41.6%	2.5%	22.1%	9.6%	22.1%	6.4%	13.3%	6.4%	12.2%	7.8%	N/A	26.7%	6.4%	-5.0%
Operating Margin ttm	9.4%	4.9%	2.8%	1.6%	7.0%	11.8%	13.6%	12.1%	N/A	10.8%	7.5%	10.5%	9.9%	5.9%	9.9%	5.7%	9.5%	4.0%	12.8%	9.9%	1.6%
EBITDA Margin 2014	11.2%	7.8%	3.7%	2.4%	8.7%	13.5%	14.6%	15.0%	15.9%	13.2%	11.2%	14.4%	12.5%	8.8%	12.5%	6.7%	12.2%	7.0%	13.8%	12.5%	5.1%
EV / Total Assets	1.6x	2.9x	2.6x	1.5x	1.9x	5.1x	2.1x	2.0x	1.9x	1.8x	1.1x	1.5x	1.9x	1.0x	1.9x	1.9x	2.0x	1.5x	2.2x	1.9x	1.6x
average		2.3x				2.3x						1.5x			1.9x			1.8x			
FCF Yield	5.9%	2.2%	-0.5%	-5.6%	2.8%	3.2%	2.8%	1.0%	N/A	2.9%	0.8%	6.9%	2.9%	3.6%	2.9%	4.8%	N/A	-1.3%	0.5%	2.9%	0.8%

Source: Bloomberg.

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Alternatively, the company's ability to generate free cash flow can be used to estimate a fair value. Using 2016 estimated net income and the average capital expenditures and change in working capital over the past three years, it can be forecast that TopBuild should generate \$58.8 million in free cash flow. If investors were to require a free cash flow yield of 10%, a fair value of \$1.69 per share would be derived (see Exhibit 11). It can be noted that among the peer group, the two positive cash flow generators have free cash flow yields of 2.1% and 2.7%. At the \$1.93 fair value estimate, the shares would yield 8.8%.

Exhibit 11 TopBuild Corp.: Fair Value Estimate Based on Free Cash Flow

(\$ in millions, except per share data; shares in millions)

2016E Net Income	42.8	
D&A	26.0	
<u>Working Capital</u>	<u>3.0</u>	
Operating Cash Flow	71.8	
<u>Capital Expense</u>	<u>13.0</u>	
FCF	58.8	
<u>FCF Yield</u>	<u>10.0%</u>	<u>8.7%</u>
Market Capitalization	587.52	672.79
<u>Shares Outstanding</u>	<u>348.6</u>	
FVE \$ / Share	\$ 1.69	\$ 1.93

Source: Company reports, Bloomberg, *The Spin-Off Report* estimates.

Lastly, the ability to generate return on equity should be considered. Based on the above exercises estimating net income (\$31.8 million in 2015 and \$42.8 million in 2016), and the current book value (\$952 million as of December 31, 2014), TopBuild should generate ROE of just 3.3% and 4.3% in 2015E and 2016E, respectively. While this is initially lower than peers, which may result in a discounted multiple being applied to shares of the standalone company, management has opportunities to improve the returns. First, an improving housing market will increase the rate of earnings growth. If 2017 net income were to increase by \$15 million to \$57.8 million, ROE would increase to 5.6% (see Exhibit 12), still below that of the current peers. However, an ROE increase of 69% over three years may provide sufficient return to longer-term investors.

Exhibit 12 TopBuild Corp.: Return on Equity, Potential Growth

(\$ in millions)

	<u>2015E</u>	<u>2016E</u>	<u>2017E</u>
Book Value	\$952.3	\$984.1	\$1,026.8
Net Income	\$31.8	\$42.8	\$57.8
ROE	3.3%	4.3%	5.6%

Source: Company reports, *The Spin-Off Report* estimates.

Masco Corp.: Post Spin

Post separation, Masco will remain a diversified building products company. Comparables differ by segment, and some overlap across segments. Given the disparate businesses, a sum-of-the-parts methodology is used to derive a fair value estimate for post-spin Masco based on estimated 2015E segment EBITDA.

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Decorative Architectural Products' most comparable peers include The Sherwin-Williams Co. (NYSE: SHW) and The Valspar Corp. (NYSE: VAL); other peers include PPG Industries Inc. (NYSE: PPG) and Axalta Coating Systems Inc. (NYSE: AXTA), among others, as shown in Exhibit 10. The peer group as a whole trades at 12.5x 2015E consensus EBITDA, and direct peers SHW and VAL trade at 15.8x and 11.4x 2015E consensus EBITDA, respectively (see Exhibit 10). Considering BEHR's market leadership position with do-it-yourselfers, and a growing presence in the professional market, it can be argued that the paint segment should garner a premium multiple to the peer group. The paint segment could be expected to increase revenue at 4.0%, slightly above management's estimate for industry gallons shipped, to account for growth in professional use. Segment margins of 19.0% (slightly above 2014 margins of 18.8%) imply EBITDA of \$394.8 million; valued at 13.6x 2015E EBITDA (average of SHW and VAL), the Decorative Architectural segment has an enterprise value of \$5.4 billion (see Exhibit 13).

Exhibit 13 Masco Corp.: Decorative Architectural Segment, Post-Spin Valuation

(\$ in millions)

	<u>Paint</u>
2014 Revenue	\$ 1,998.0
<u>2015E Revenue Growth</u>	<u>4.0%</u>
2015E Revenue	2,077.9
<u>EBITDA Margin</u>	<u>19.0%</u>
2015E EBITDA	394.8
<u>Multiple</u>	<u>13.6x</u>
Enterprise Value	5,369.3

Source: Company reports, *The Spin-Off Report* estimates.

Plumbing peers include more diversified companies such as Spectrum Brands Holdings Inc. (SPB) and Fortune Brands Home & Security (FBHS) (see Exhibit 10). Given MAS's growing spa business (the company made a small bolt-on acquisition in 1Q 2015), Whirlpool Corp. (NYSE: WHR) can also be included, while noting that it is a small portion of MAS's business. FBHS and SPB trade at 11.7x average 2015E consensus EBITDA. Plumbing products sales are estimated to grow 5% in 2015, while segment margins are forecast at 16.5%, both at the midpoint of management's three-year CAGR projection. Applying the FBHS/SPB multiple to estimated EBITDA of \$582 million implies an enterprise value of \$6.7 billion (see Exhibit 14).

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Exhibit 14 Masco Corp.: Plumbing Products Segment, Post-Spin Valuation

(\$ in millions)

	<u>Plumbing</u>
2014 Revenue	\$ 3,308.0
<u>2015E Revenue Growth</u>	<u>5.0%</u>
2015E Revenue	3,473.4
<u>EBITDA Margin</u>	<u>16.5%</u>
2015E EBITDA	573.1
<u>Multiple</u>	<u>11.7x</u>
Enterprise Value	\$ 6,705.4

Source: Company reports, *The Spin-Off Report* estimates.

Cabinet manufacturers are somewhat limited in number, with the major competitors being American Woodmark Corp. (AMWD), Fortune Brands Home & Security Inc. (NYSE: FBHS), and Norcraft Companies Inc. (NYSE: NCFT), which on average trade at 10.4x 2015E consensus EBITDA. Norcraft is in the process of being acquired by FBHS at 12.5x trailing EBITDA. Masco's Cabinet operations have seen the most difficulty in rebounding from the downturn in housing, and as such have the most potential for accelerating earnings growth in future years. However, sustained earnings have been elusive thus far in the housing recovery. In 1Q 2015 revenue increased 5% based on improved home center and builder channel sales, and adjusted EBITDA margins were 2.0%. Management is targeting roughly \$43 million in 2015 segment EBITDA (\$10 million EBIT assuming stable depreciation expenses). If revenue were to maintain the 5% growth rate and margins expanded to 4.0% through 2015, the segment would earn \$42 million in EBITDA. With the segment valued at 10.4x 2015E EBITDA, a fair enterprise value of \$436 million is derived (see Exhibit 15).

Exhibit 15 Masco Corp.: Cabinets Segment, Post-Spin Valuation

(\$ in millions)

	<u>Cabinets</u>
2014 Revenue	\$ 999.0
<u>2015E Revenue Growth</u>	<u>5.0%</u>
2015E Revenue	1,049.0
<u>EBITDA Margin</u>	<u>4.0%</u>
2015E EBITDA	42.0
<u>Multiple</u>	<u>10.4x</u>
Enterprise Value	\$ 436.4

Source: Company reports, *The Spin-Off Report* estimates.

Lastly, the Other Specialty segment must be valued. Revenue growth at the segment has outpaced the other segments (11% in 2013 and 10% in 2014) due to more favorable product mix and increased selling prices. Assuming growth roughly in line with the 1Q 2015 rate of 7%, 2015 revenue can be anticipated to increase 8% (below management's forecast 9%-11% CAGR through 2017), and margins could approximate the 2014 level of 9.5%, implying that segment EBITDA would total \$71.9 million. A fair enterprise value of \$842 million is derived when applying an 11.8x multiple (see Exhibit 16). The 11.8x multiple is based on a basket of peers that sell building products, including windows and doors, comprising FBHS, Masonite International

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Corp. (NYSE: DOOR), Ply Gem Holdings Inc. (NYSE: PGEM), and PGT Inc. (NASDAQ: PGTI) (see Exhibit 10).

Exhibit 16 Masco Corp.: Other Specialty Products Segment, Post-Spin Valuation

(\$ in millions)

	<u>Other Specialty</u>
2014 Revenue	\$ 701.0
<u>2015E Revenue Growth</u>	<u>8.0%</u>
2015E Revenue	757.1
<u>EBITDA Margin</u>	<u>9.5%</u>
2015E EBITDA	71.9
<u>Multiple</u>	<u>11.7x</u>
Enterprise Value	\$ 841.5

Source: Company reports, *The Spin-Off Report* estimates.

On a sum-of-the-parts basis a fair value estimate for post-spin Masco of \$29 per share is derived when accounting for \$125 million in corporate costs (capitalized at 12.3x, the weighted average multiple used in the segment valuations), and estimated net debt of \$1.7 billion, including \$190 million in minority interest related to the 68% ownership of Hansgrohe SE (see Exhibit 17).

Exhibit 17 Masco Corp.: Post Spin Sum-of-the-Parts Valuation

(\$ in millions, except per share data; shares in millions)

	<u>Paint</u>	<u>Plumbing</u>	<u>Cabinets</u>	<u>Other Specialty</u>	<u>Corporate</u>	<u>Total</u>
2014 Revenue	\$ 1,998.0	\$ 3,308.0	\$ 999.0	\$ 701.0		\$ 7,006.0
<u>2015E Revenue Growth</u>	<u>4.0%</u>	<u>5.0%</u>	<u>5.0%</u>	<u>8.0%</u>		<u>5.0%</u>
2015E Revenue	2,077.9	3,473.4	1,049.0	757.1		7,357.4
<u>EBITDA Margin</u>	<u>19.0%</u>	<u>16.5%</u>	<u>4.0%</u>	<u>9.5%</u>		<u>13.0%</u>
2015E EBITDA	394.8	573.1	42.0	71.9	(125.0)	956.8
<u>Multiple</u>	<u>13.6x</u>	<u>11.7x</u>	<u>10.4x</u>	<u>11.7x</u>	<u>12.3x</u>	<u>12.3x</u>
Enterprise Value	\$ 5,369.3	\$ 6,705.4	\$ 436.4	\$ 841.5	\$ (1,542.9)	\$ 11,809.7
<u>Net Debt</u>						<u>1,739.0</u>
Market Capitalization						10,070.7
<u>Shares Outstanding</u>						<u>348.6</u>
FVE \$ / Share						\$ 28.89

Source: Company reports, Bloomberg, *The Spin-Off Report* estimates.

The above valuation does not give the company any credit for either share repurchases or cost-cutting initiatives. MAS has 40.9 million shares remaining in its current repurchase authorization, and management has stated that it intends to spend \$400-\$500 million on share repurchases in 2015. MAS repurchased 4.1 million shares in 1Q 2015 for a total amount of \$106 million. MAS could retire 3.6% of shares at the midpoint of the expected spending, based on current market price, raising the fair value estimate to \$30 per share. Management has also targeted cost cuts of \$35-\$40 million annually, which at the midpoint would also raise the fair value to \$30 per share. Combined, repurchases and cost cuts increase the fair value estimate to \$31 per share (see Exhibit 18).

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Exhibit 18 Masco Post-Spin Fair Value Estimate Including Repurchases and Cost Cuts

(\$ in millions, except per share data; shares in millions)

	Share	\$35 million	Repurchase and
	Repurchases	Cost Cuts	Cost Cuts
Enterprise Value	\$ 11,809.7	\$ 12,273.2	\$ 12,273.2
<u>Net Debt</u>	<u>1,739.0</u>	<u>1,739.0</u>	<u>1,739.0</u>
Market Capitalization	10,070.7	10,534.2	10,534.2
<u>Shares Outstanding</u>	<u>335.9</u>	<u>348.6</u>	<u>335.9</u>
FVE \$ / Share	\$ 29.98	\$ 30.22	\$ 31.36

Source: Company reports, Bloomberg, *The Spin-Off Report* estimates.

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Conclusion

The spin-off of TopBuild makes sense for Masco for a couple of reasons. First, separating the lower-margin business would immediately improve the financial profile of the parent company. The separation makes the parent company look like a better investment, as the lower-margin Installation and Other Services business is jettisoned; EBITDA margins at the parent are expected to improve by over 100 basis points. The parent company appears positioned to benefit from both macro tailwinds and the recent restructuring of the struggling Cabinets business. New home construction is forecast to remain above 1 million annual starts over the next several years, providing ample opportunities for TopBuild, while contractor confidence in the remodeling market appears bullish for Masco's prospects. Lastly, TopBuild and post-spin Masco serve differing end markets. TopBuild's products are primarily sold for use in new residential construction, whereas the remainder of Masco is focused on the repair and remodeling of existing homes. Spinning off the services and installation business creates a less cyclical business at the parent entity, with more exposure to the repair and remodel market versus new home construction. For its part, TopBuild has increased its exposure to commercial construction in an attempt to diversify its revenue away from residential construction. The decision to spin off the Installation and Other Services business follows activist investor Third Point taking a 1.3% stake in mid-2014 and engaging in discussions with MAS management. Third Point subsequently increased its ownership in MAS to 2.9% (10 million shares).

Masco currently trades at a discount to most peers across its diversified portfolio. Separating the installation services business should help alleviate some of the discount, as, optically speaking, the company's margins improve if the lowest-margin business is jettisoned. The discount may also be related to the struggling performance of the company's Cabinets business. While the business has struggled to achieve profitability in recent years, management has right-sized costs, including a reduction in manufacturing and distribution facilities from 70 to 17 including the sale of less profitable product lines, for profitable operations in the current housing environment. Any improvement in sales could provide additional upside to projected earnings and fair value.

Based on comparable multiples and cash flow generation potential, a fair value of \$1.93 per share is derived for TopBuild. Post-spin Masco is fairly valued at \$31 per share based on comparable multiples and incorporating cost reduction and a reduced share count. Shares of Masco Corp. are valued at \$33 per share on a sum-of-the-parts basis and are recommended for purchase prior to the spin-off of TopBuild. Following the separation it may be expected that shares of TopBuild would be sold by existing holders as the larger, higher-margin, more stable business is preferred to TopBuild.

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Exhibit 19 TopBuild Corp.: Pro Forma Income Statement

(\$ in thousands)

		Year ended December 31, 2014	
	<u>Historical</u>	<u>Pro Forma Adjustments</u>	<u>Pro Forma</u>
Net sales	1,512,080		
<u>Cost of sales</u>	<u>1,180,410</u>		
Gross profit	331,670		
<u>Selling, general and administrative expenses</u>	<u>290,950</u>		
Operating profit	40,720		
Other income (expense), net:			
Interest expense related party	(12,400)		
Other, net	<u>20</u>		
	(12,380)		
Income from continuing operations before income taxes	28,340		
<u>Income tax expense</u>	<u>17,840</u>		
Income from continuing operations	10,500		
Unaudited Pro Forma Earnings Per Share			
Basic			
Diluted			
Average Number of Shares Used in Calculating			
Unaudited Pro Forma Earnings Per Share			
Basic			
Diluted			

Source: Company reports.

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Exhibit 20 TopBuild Corp.: Pro Forma Balance Sheet

(\$ in thousands)

	<u>Historical</u>	<u>Pro Forma Adjustments</u>	<u>Pro Forma</u>
ASSETS			
Current Assets:			
Cash and cash equivalents	\$ 2,970		
Receivables, net	220,180		
Inventories	106,970		
Prepaid expenses and other	5,120		
Total current assets	\$ 335,240		
Property and equipment, net	93,160		
Goodwill	1,044,040		
Other intangible assets, net	2,960		
Other assets	1,030		
Total Assets	\$ 1,476,430		
LIABILITIES and EQUITY			
Current Liabilities:			
Accounts payable	\$ 228,720		
Accrued liabilities	72,750		
Total current liabilities	\$ 301,470		
Long-term debt	-		
Deferred income taxes	182,280		
Other liabilities	40,390		
Total Liabilities	\$ 524,140		
Commitments and contingencies			
Equity:			
Common stock, \$1.00 par value	\$ -		
Paid-in capital	-		
Parent Company investment	952,290		
Total Equity	952,290		
Total Liabilities and Equity	\$ 1,476,430		

Source: Company reports.