GRANITE CONSTRUCTION INC
Form 10-K
February 26, 2008

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2007
OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _____ to _____
Commission file number 1-12911
Granite Construction Incorporated
(Exact name of registrant as specified in its charter)

Delaware	77-0239383
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
585 West Beach Street Watsonville, California	95076
(Address of principal executive offices)	(Zip Code)

Registrant’s telephone number, including area code: (831) 724-1011

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, $0.01 par value	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes x No o

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant’s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company (as defined by Rule 12b-2 of the Exchange Act). Large accelerated filer x Accelerated filer o Non-accelerated filer o Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No x

The aggregate market value of voting and non-voting common equity held by non-affiliates of the registrant was approximately $2.3 billion as of June 30, 2007, based upon the average of the bid and asked prices per share of the registrant's Common Stock as reported on the New York Stock Exchange on such date. Shares of Common Stock held by each executive officer and director and by each person who owns 5% or more of the outstanding Common Stock have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

At February 13, 2008, 38,952,477 shares of Common Stock, par value $0.01, of the registrant were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Certain information called for by Part III is incorporated by reference to the definitive Proxy Statement for the Annual Meeting of Shareholders of Granite Construction Incorporated to be held on May 19, 2008, which will be filed with the Securities and Exchange Commission not later than 120 days after December 31, 2007.

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FORWARD-LOOKING DISCLOSURE

This Annual Report on Form 10-K contains statements that are not based on historical facts and which may be forward-looking in nature. Under the Private Securities Litigation Reform Act of 1995, a "safe harbor" may be provided to us for certain of these forward-looking statements. Words such as "outlook," "believes," "expects," "appears," "may," "w "should," "anticipates" or the negative thereof or comparable terminology, are intended to identify these forward-looking statements. These forward-looking statements are estimates reflecting the best judgment of our senior management and are based on our current expectations and projections concerning future events, many of which are outside of our control, and involve a number of risks and uncertainties that could cause actual results to differ materially from those suggested by the forward-looking statements. Factors that might cause or contribute to such differences include, but are not limited to, those more specifically described in this Report under "Item 1A. Risk Factors." Granite undertakes no obligation to publicly revise or update any forward-looking statements for any reason. As a result, the reader is cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this Report.

PART I

Item 1. BUSINESS

Introduction

We were originally incorporated in 1922 as Granite Construction Company. In 1990, Granite Construction Incorporated was incorporated in Delaware as the holding company for Granite Construction Company and its wholly owned subsidiaries. Unless otherwise indicated, the terms "we," "us," "our," "Company" and "Granite" refer to Granite Construction Incorporated and its consolidated subsidiaries.

We are one of the largest heavy civil construction contractors in the United States. We operate nationwide, serving both public and private sector clients. Within the public sector, we primarily concentrate on infrastructure projects, including the construction of roads, highways, bridges, dams, canals, mass transit facilities and airport infrastructure. Within the private sector, we perform site preparation and infrastructure services for residential development, commercial and industrial buildings, plants and other facilities. Our diversification in both the public and private sectors and our mix of project types and sizes have contributed to our profitability in various economic environments.

We own and lease substantial aggregate reserves and own a number of construction materials processing plants. We also have one of the largest contractor-owned heavy construction equipment fleets in the United States. We believe that the ownership of these assets enables us to compete more effectively by ensuring availability of these resources at a favorable cost.

Operating Structure

Historically, we were organized into two operating segments, the Branch Division and the Heavy Construction Division ("HCD"). The Branch Division was comprised of branch offices that served local markets, while HCD was composed of regional offices and pursued major infrastructure projects throughout the nation.

In February 2007, we announced an organizational realignment of our business operations which is designed to accommodate growth of our vertically integrated Branch business in the West and improve profitability of our large, complex HCD projects. This realignment involved the reorganization of our operating divisions geographically into "Granite West" and "Granite East." Granite West includes the operations of our former Branch Division as well as the western portion of our large project business that was formerly included in HCD. Granite West retains our successful

decentralized operating structure, with each of its branch locations aligning under one of three operating groups: Northwest, Northern California and Southwest. Granite East includes the eastern portion of our large project business that had been included in HCD and is aligned to focus on enhancing project management oversight and discipline from estimating through execution. With the Division office in Lewisville, Texas, Granite East also operates out of three regional offices: the Central Region, based in Lewisville, Texas; the Southeast Region, based in Tampa, Florida; and the Northeast Region, based in Tarrytown, New York.

During 2007, we completed the reassignment of our large projects in the West from our former Heavy Construction Division to our Granite West Division (with the exception of certain projects nearing completion which remain with our Granite East Division) and made substantial progress on other aspects of the realignment. As a result, we are reporting Granite West and Granite East as new reportable segments. Prior period results have been reclassified to conform to the new organizational structure (see Note 1 of the "Notes to the Consolidated Financial Statements").
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The following table shows the impact on revenue and gross profit of the three projects reassigned from our former Heavy Construction Division to the newly created Granite West:

Granite West	Years ended December 31,		
(in thousands)	2007	2006	2005
Branch Division revenue	$ 1,828,024	$ 1,848,725	$ 1,591,545
Reassigned projects revenue	100,727	79,271	7,913
Granite West Division revenue	1,928,751	1,927,996	1,599,458
Branch Division gross profit	357,871	364,878	253,890
Reassigned projects gross profit (loss)	12,558	(14,291)	-
Granite West Division gross profit	370,429	350,587	253,890

Granite East	Years ended December 31,		
(in thousands)	2007	2006	2005
Heavy Construction Division revenue	$ 869,178	$ 1,085,888	$ 1,030,109
Reassigned projects revenue	(100,727)	(79,271)	(7,913)
Granite East Division revenue	768,451	1,006,617	1,022,196
Heavy Construction Division gross profit (loss)	38,382	(86,856)	50,470
Reassigned projects gross profit	(12,558)	14,291	-
Granite East Division gross profit (loss)	25,824	(72,565)	50,470

The backlog related to the three reassigned projects was $208.0 million and $122.1 million at December 31, 2006 and 2005, respectively.

Granite West: In 2007 and 2006, Granite West contract revenue and sales of construction materials was $1.9 billion (70.4% and 64.9% of our total revenue, respectively). Granite West has both public and private sector clients. Typical public sector projects include both new construction and improvement of streets, roads, highways and bridges. Typical major private sector contracts include site preparation for housing and commercial development, including excavation, grading and street paving and installation of curbs, gutters, sidewalks and underground utilities.

Granite West currently has 15 branch offices in the western United States with additional satellite operations. Each branch reports under one of three operating groups: Northwest, Northern California and Southwest. Although most Granite West projects are started and completed within a year, the division also has the capability of constructing larger projects and currently has five active projects, each with total contract revenue greater than $50.0 million, including two projects from our legacy Heavy Construction Division. In 2007, individual branch revenues ranged from $72.7 million to $236.4 million.

As part of our strategy, our branches mine aggregates and/or operate plants that process aggregates into construction materials for internal use and for sale to others. These activities are vertically integrated into Granite West, providing both a source of profits and a competitive advantage to our construction business through the readily available supply of materials. We have significant aggregate reserves that we have acquired by ownership in fee or through long-term leases. The amount of aggregate products produced that were used in our construction projects was approximately 43.0% during 2007 and has ranged from 37.0% to 44.0% over the last five years. The remainder is sold to unaffiliated parties and accounted for the following:

Years Ended December 31, (in thousands)	2007	2006	2005
Material sales to unaffiliated parties	$ 375,700	$ 410,159	$ 334,290

Percent of total revenue	13.7%	13.8%	12.7%
Percent of Granite West revenue	19.5%	21.3%	20.9%

Granite East: In 2007, revenue from Granite East was $768.5 million (28.1% of our total revenue), compared with $1.0 billion (33.9% of our total revenue) in 2006. Granite East operates in the eastern portion of the United States with a focus on large, complex infrastructure projects including major highways, large dams, mass transit facilities, bridges, pipelines, canals, waterway locks and dams, and airport infrastructure. It also performs activities such as demolition, clearing, large-scale earthwork and grading, dewatering, drainage improvements, structural concrete, rail signalization, and concrete and asphalt paving. Granite East also has the ability, if needed, to process locally sourced aggregates into construction materials using owned or rented portable crushing, concrete and asphalt processing plants.

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With Division offices in Lewisville, Texas, Granite East also operates out of three regional offices: the Central Region, based in Lewisville, Texas; the Southeast Region, based in Tampa, Florida; and the Northeast Region, based in Tarrytown, New York. These regional offices provide management and administrative support and are the primary hubs for estimating efforts. Granite East construction contracts are typically greater than two years in duration with an average contract size of greater than $100.0 million.

Both Granite East and Granite West participate in joint ventures with other large construction companies. Joint ventures are used for large, technically complex projects, including design/build projects, where it is desirable to share risk and resources. Joint venture partners typically provide independently prepared estimates, shared financing and equipment and often also bring local knowledge and expertise (see “Joint Ventures; Off-Balance-Sheet Arrangements” under “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operation”).

Design/build is increasingly being used as a method of project delivery. Unlike traditional projects where owners first hire a design firm or design a project themselves and then put the project out to bid for construction, design/build projects provide the owner with a single point of responsibility and a single contact for both design and construction. Revenue from design/build projects represented 62.2% and 65.3% of Granite East revenue in 2007 and 2006, respectively. Revenue from design/build projects represented 8.1% and 6.0% of Granite West revenue in 2007 and 2006, respectively. Although these projects carry additional risk as compared to traditional bid/build projects, the profit potential can also be higher. We frequently bid design/build projects as a part of a joint venture team.

Granite Land Company: We purchase, develop, operate, sell and otherwise invest in real estate through our Granite Land Company subsidiary (“GLC”), which also provides real estate services for other Granite operations. GLC’s portfolio of projects includes both commercial and residential development and is geographically diversified throughout the West and Texas. In 2007, revenue from GLC was $40.7 million (1.5% of our total revenue), compared with $35.0 million (1.2% of our total revenue) in 2006.

Additional information about our business segments is contained in Note 16 of the “Notes to the Consolidated Financial Statements.”

Business Strategy

Our fundamental objective is to increase long-term shareholder value by focusing on consistent profitability from controlled revenue growth. Shareholder value is measured by the appreciation of the value of our common stock over a period of years as well as a return from dividends. Further, it is a specific measure of our financial success to achieve a return on net assets greater than the cost of capital, creating “Granite Value Added.” We believe that the following are key factors in our ability to achieve this objective:

Employee Development - We believe that our employees are key to the successful implementation of our business strategies. Significant resources are employed to attract, nurture and retain extraordinary talent and fully develop each employee’s capabilities.

Infrastructure Construction Focus - We concentrate our core competencies on this segment of the construction industry, which includes the building of roads, highways, bridges, dams and tunnels, mass transit facilities, railroad infrastructure and underground utilities as well as site preparation. This focus allows us to most effectively utilize our specialized strengths, which include grading, paving and concrete structures.

Ownership of Aggregate Materials and Construction Equipment - We own and lease aggregate reserves and own processing plants that are vertically integrated into our construction operations and we own a large fleet of carefully

maintained heavy construction equipment. By ensuring availability of these resources and providing quality products, we believe we have bidding advantages in many of our markets, as well as a reliable source of revenue and income from the sale of construction materials to unaffiliated parties.

Selective Bidding - We focus our resources to bid on jobs that meet our selective bidding criteria, which include analyzing the risk of a potential job in relation to available personnel to estimate and prepare the proposal, as well as personnel to effectively manage and build the project, degree of competition, experience with the type of work, relationship with the owner, local resources and partnerships, equipment resources, size and complexity of the job and profitability.

Diversification - To mitigate the risks inherent in construction and general economic factors, we pursue projects: (i) in both the public and private sectors; (ii) for a wide range of customers within each sector (from the federal government to small municipalities and from large corporations to individual homeowners); (iii) in diverse geographic markets; (iv) that are design/build, lump sum and fixed unit price; and (v) of various sizes, durations and complexity.

Decentralized Profit Centers - We approach each selected market with a local focus through our decentralized structure. Each of our Granite West branch offices and Granite East regional offices are individual profit centers.

Profit-based Incentives - We incentivize our profit center managers with a substantial variable cash and restricted stock incentive element based primarily on the annual profit performance of their respective profit centers.

Controlled Expansion - We intend to continue our expansion by selectively adding branches or branch satellite locations in the western United States, exploring opportunities to establish branch-like businesses in other areas of the country through acquisitions, and selectively pursuing major infrastructure projects throughout the nation where we have an established presence. Additionally, we intend to leverage our financial capacity by investing in a limited number of real estate development projects that we believe will provide an acceptable return on our investment.

Accident Prevention - We believe that preventing accidents is both a moral obligation and good business. By identifying and concentrating resources to address jobsite hazards, we continually strive to reduce our incident rates and the costs associated with accidents.

Environmental Responsibility - We believe it benefits everyone to maintain environmentally responsible operations. We are committed to effective measures to protect the environment and maintain good community relations. We continually monitor our performance in this area and take our responsibilities to the communities where we work and compliance with government agency requirements seriously.

Quality and High Ethical Standards - We emphasize the importance of performing high quality work and maintaining high ethical standards through an established code of conduct and an effective corporate compliance program.

Customers

We have customers in both the public and private sectors. The largest volume customer of Granite West is the California Department of Transportation (“Caltrans”). In 2007, contracts with Caltrans represented 10.0% of our total revenue, and total public sector revenue generated in California represented 23.5% of our total revenue. Other Granite West customers include departments of transportation of other states, county and city public works departments, school districts and developers and owners of industrial, commercial and residential sites. Granite East’s customers are predominantly in the public sector and currently include the numerous state departments of transportation as well as local transit authorities and federal agencies (see “Concentrations” in Note 1 of the “Notes to the Consolidated Financial Statements”).

Backlog

Our backlog includes the total value of awarded contracts that have not been completed, including our proportionate share of unconsolidated joint venture contracts. Our backlog was approximately $2.1 billion and $2.3 billion at December 31, 2007 and 2006, respectively. Approximately $1.2 billion of the December 31, 2007 backlog is expected to be completed during 2008. With the exception of certain federal government contracts, we include a construction project in our backlog at such time as a contract is awarded and funding is in place. Substantially all of the contracts in our backlog may be canceled or modified at the election of the customer; however, we have not been materially adversely affected by contract cancellations or modifications in the past (see “Contract Provisions and Subcontracting”). Certain Granite West projects are added and completed within each year and therefore not reflected in our year-end backlog. Backlog by segment is presented in “Backlog” under “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operation.”

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Equipment and Plants

We own many pieces of equipment, including cranes, bulldozers, barges, backhoes, excavators, scrapers, motor graders, loaders, trucks, pavers and rollers as well as construction materials processing plants. In 2007 and 2006, we spent approximately $88.4 million and $91.0 million, respectively, for construction equipment, plants and vehicles. Additionally, our equipment fleet increased in 2007 as a result of our acquisitions (see Note 17 of the “Notes to the Consolidated Financial Statements”). At December 31, 2007 and 2006, we owned the following construction equipment, plants and vehicles:

December 31,	2007	2006
Heavy construction equipment (units)	3,366	2,641
Trucks, truck-tractors and trailers and vehicles (units)	5,579	5,338
Aggregate crushing plants	55	55
Asphalt concrete plants	69	53
Portland cement concrete batch plants	25	25
Asphalt rubber plants	5	4
Lime slurry plants	9	9

We believe that ownership of equipment is generally preferable to leasing because ownership ensures the equipment is available as needed and normally results in lower equipment costs. We keep our equipment as fully utilized as possible by pooling certain equipment for use by both Granite West and Granite East. We regularly lease or rent equipment on a short-term basis to supplement existing equipment and respond to construction activity peaks.

Employees

On December 31, 2007, we employed approximately 2,100 salaried employees, who work in management, estimating and clerical capacities, plus 2,100 hourly employees. The total number of hourly personnel employed by us is subject to the volume of construction in progress. During 2007, the number of hourly employees ranged from 2,100 to 5,400 and averaged approximately 4,600. Three of our wholly owned subsidiaries - Granite Construction Company, Granite Construction Northeast, Inc. and Wilder Construction Company (“Wilder”) are parties to craft collective bargaining agreements in many areas in which they work.

We believe our employees are our most valuable resource and that our workforce possesses a strong dedication to and pride in our company. Among salaried and non-union hourly employees, this dedication is reinforced by 16.8% equity ownership through our Employee Stock Ownership Plan, our Profit Sharing and 401k Plan and performance-based incentive compensation arrangements at December 31, 2007. Our managerial and supervisory personnel have an average of approximately 10 years of service with us.

Competition

Factors influencing our competitiveness include price, reputation for quality, the availability of aggregate materials, machinery and equipment, financial strength, knowledge of local markets and conditions, and project management and estimating abilities. Although some of our competitors are larger than us and may possess greater resources, we believe that we compete favorably on the basis of the foregoing factors. Historically, the construction business has not usually required large amounts of capital, particularly for the smaller size construction work pursued by Granite West, which can result in relative ease of market entry for companies possessing acceptable qualifications. Granite West competitors range from small local construction companies to large regional and national construction companies. While the market areas of these competitors overlap with several of the markets served by our branches, few compete in all of our market areas. Many of our Granite West competitors have the ability to perform work in either the private

or public sectors. When the market for projects in one sector contracts, these competitors will move to the other. This greater competition can reduce revenue growth and/or increase pressure on gross profit margins. In addition, we own and/or have long-term leases on aggregate resources that provide an extra measure of competitive advantage in certain markets. Granite East normally competes with large regional and national construction companies, which may or may not be larger than Granite. Although the construction business is highly competitive, we believe we are well positioned to compete effectively in the markets in which we operate.

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Contract Provisions and Subcontracting

Our contracts with our customers are primarily either "fixed unit price" or "fixed price." Under fixed unit price contracts, we are committed to provide materials or services required by a project at fixed unit prices (for example, dollars per cubic yard of concrete poured or cubic yard of earth excavated). While the fixed unit price contract shifts the risk of estimating the quantity of units required for a particular project to the customer, any increase in our unit cost over the expected unit cost in the bid, whether due to inflation, inefficiency, faulty estimates or other factors, is borne by us unless otherwise provided in the contract. Fixed price contracts are priced on a lump-sum basis under which we bear the risk of performing all the work for the specified amount. The percentage of fixed price contracts in our backlog increased to approximately 72.0% at December 31, 2007 compared with approximately 68.0% at December 31, 2006. Our contracts are generally obtained through competitive bidding in response to advertisements by federal, state and local government agencies and private parties. Less frequently, contracts may be obtained through direct negotiations with private owners. Our contract risk mitigation process includes identifying risks and opportunities during the bidding process, review of bids fitting certain criteria by various levels of management and, in some cases, by the executive committee of our Board of Directors.

There are a number of factors that can create variability in contract performance and results as compared to a project's original bid. The most significant of these include the completeness and accuracy of the original bid, costs associated with added scope changes, extended overhead due to owner and weather delays, subcontractor performance issues, changes in productivity expectations, site conditions that differ from those assumed in the original bid (to the extent contract remedies are unavailable), the availability and skill level of workers in the geographic location of the project and a change in the availability and proximity of equipment or materials. All of these factors can impose inefficiencies on contract performance, which can drive up costs and lower profits. Conversely, if any of these or other factors are more positive than the assumptions in our bid, project profitability can improve. However, the ability to realize improvements on project profitability is more limited than the risk of lower profitability. Design/build projects carry additional risks such as the risk inherent in estimating quantities and prices before the project design is completed and design error risk, including higher construction costs due to any design errors, liability to the contract owner for the design of the project and right-of-way and permit acquisition costs. Although we manage this additional risk by adding contingencies to our bid amounts, obtaining errors and omissions insurance and obtaining indemnifications from our design consultants where possible, there is no guarantee that these risk management strategies will always be successful.

All of our state and federal government contracts and most of our other contracts provide for termination of the contract for the convenience of the contract owner, with provisions to pay us for work performed through the date of termination. We have not been materially adversely affected by these provisions in the past. Many of our contracts contain provisions that require us to pay liquidated damages if specified completion schedule requirements are not met and these amounts can be significant.

We act as prime contractor on most of the construction projects we undertake. We accomplish the majority of our projects with our own resources and subcontract specialized activities such as electrical and mechanical work. As prime contractor, we are responsible for the performance of the entire contract, including subcontract work. Thus, we may be subject to increased costs associated with the failure of one or more subcontractors to perform as anticipated. We manage this risk by reviewing the size of the subcontract, the financial stability of the subcontractor and other factors and, based on this review, determine whether to require that the subcontractor furnish a bond or other type of security that guarantees their performance. Disadvantaged business enterprise regulations require us to use our best efforts to subcontract a specified portion of contract work done for governmental agencies to certain types of disadvantaged subcontractors. As with all of our subcontractors, some may not be able to obtain surety bonds or other types of performance security.

Insurance and Bonding

We maintain general and excess liability, construction equipment and workers' compensation insurance; all in amounts consistent with industry practices.

In connection with our business, we generally are required to provide various types of surety bonds that provide an additional measure of security for our performance under certain public and private sector contracts. Our ability to obtain surety bonds depends upon our capitalization, working capital, past performance, management expertise and external factors, including the capacity of the overall surety market. Surety companies consider such factors in light of the amount of our backlog that we have currently bonded and their current underwriting standards, which may change from time to time. The capacity of the surety market is subject to market-based fluctuations driven primarily by the level of surety industry losses and the degree of surety market consolidation. When the surety market capacity shrinks it results in higher premiums and increased difficulty obtaining bonding, in particular for larger, more complex projects throughout the market. In order to help mitigate this risk, we employ a co-surety structure involving three sureties. Although we do not believe that fluctuations in surety market capacity has significantly impacted our ability to grow our business, there is no assurance that it will not significantly impact our ability to obtain new contracts in the future (see "Item 1A. Risk Factors").

Government and Environmental Regulations

Our operations are subject to compliance with regulatory requirements of federal, state and local government agencies and authorities, including regulations concerning workplace safety, labor relations and disadvantaged businesses. Additionally, all of our operations are subject to various federal, state and local laws and regulations relating to the environment, including those relating to discharges to air, water and land, the handling and disposal of solid and hazardous waste, the handling of underground storage tanks and the cleanup of properties affected by hazardous substances. Certain environmental laws impose substantial penalties for non-compliance and others, such as the federal Comprehensive Environmental Response, Compensation and Liability Act, impose strict, retroactive, joint and several liability upon persons responsible for releases of hazardous substances. We continually evaluate whether we must take additional steps at our locations to ensure compliance with environmental laws. While compliance with applicable regulatory requirements has not materially adversely affected our operations in the past, there can be no assurance that these requirements will not change and that compliance will not adversely affect our operations in the future. In addition, our aggregate materials operations require operating permits granted by governmental agencies. We believe that tighter regulations for the protection of the environment and other factors will make it increasingly difficult to obtain new permits and renewal of existing permits may be subject to more restrictive conditions than currently exist.

In July 2007, the California Air Resources Board (“CARB”) approved a regulation that will require California equipment owners/operators to reduce diesel particulate emissions from in-use off-road diesel equipment to meet emission targets proposed for each year from 2010 to 2020. The emission targets will require California off-road diesel equipment owners to retrofit equipment with diesel particulate filters or replace equipment with new engine technology as it becomes available. Between now and the year 2020, Granite will be required to implement an equipment management strategy that includes accelerated turnover of off-road diesel equipment and retrofitting equipment with CARB approved diesel particulate filters. This will increase equipment related expenses in an amount which has not yet been determined.

As is the case with other companies in our industry, some of our aggregate products contain varying amounts of crystalline silica, a common mineral. Also, some of our construction and material processing operations release as dust crystalline silica that is in the materials being handled. Excessive, prolonged inhalation of very small-sized particles of crystalline silica has allegedly been associated with respiratory disease (including silicosis). The Mine Safety and Health Administration and the Occupational Safety and Health Administration have established occupational thresholds for crystalline silica exposure as respirable dust. We monitor to verify that our dust control procedures are keeping occupational exposures at or below the requisite thresholds and to verify that respiratory protective equipment is made available when required. We also communicate, through safety information sheets and other means, what we believe to be appropriate warnings and cautions to employees and customers about the risks associated with excessive, prolonged inhalation of mineral dust in general and crystalline silica in particular.

Website Access

Our website address is www.graniteconstruction.com. On our website we make available, free of charge, our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to those reports as soon as reasonably practicable after such material is electronically filed with or furnished to the Securities and Exchange Commission (“SEC”). The information on our website is not incorporated into, and is not part of, this report. These reports, and any amendments to them, are also available at the website of the SEC, www.sec.gov.

Item 1A. RISK FACTORS

Set forth below and elsewhere in this Report and in other documents we file with the SEC are various risks and uncertainties that could cause our actual results to differ materially from the results contemplated by the forward-looking statements contained in the Report or otherwise adversely affect our business.

- Our success depends on attracting and retaining qualified personnel in a competitive environment. The single largest factor in our ability to profitably execute our work is our ability to attract, develop and retain qualified personnel particularly as we grow. Our success in attracting qualified people is dependent on the resources available in individual geographic areas and the impact on the labor supply due to general economic conditions as well as our ability to provide a competitive compensation package and work environment.

- Reductions in government funding could have a negative impact on our business. A substantial majority of our revenues are derived from contracts that are funded by federal, state and local government agencies. Our ability to obtain future public sector work at reasonable margins is highly dependent on the amount of work that is available to bid, which is largely a function of the level of government funding available.

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- Our commercial and residential site development work may be affected by economic downturns. The availability of private sector work can be adversely affected by economic downturns in the residential housing market, demand for commercial property or the availability of credit. To the extent these events occur, our operating results will be adversely affected.

- Our fixed price and fixed unit price contracts subject us to the risk of increased project cost. As more fully described under “Contract Provisions and Subcontracting” above, the profitability of our fixed price and fixed unit price contracts can be adversely affected by a number of factors that can cause our actual costs to materially exceed the costs estimated at the time of our original bid.

- Accounting for our revenues and costs involves significant estimates. As further described in “Critical Accounting Estimates” under “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operation,” accounting for our contract related revenues and costs, as well as other cost items, requires management to make a variety of significant estimates and assumptions. Although we believe we have sufficient experience and processes to enable us to formulate appropriate assumptions and produce reasonably dependable estimates, these assumptions and estimates may change significantly in the future, and these changes could result in the reversal of previously recognized revenue and profit and have a material adverse effect on our financial position and the results of our operations.

- Many of our contracts have penalties for late completion. In some instances, including many of our fixed price contracts, we guarantee that we will complete a project by a scheduled date. If we subsequently fail to complete the project as scheduled we may be held responsible for cost impacts resulting from any delay, generally in the form of contractually agreed-upon liquidated damages. To the extent that these events occur, the total costs of the project could exceed our original estimates and we could experience reduced profits or, in some cases, a loss for that project.

- Weather can significantly impact our quarterly revenues and profitability. Our ability to perform work is significantly impacted by weather conditions such as precipitation and temperature. Changes in weather conditions can create significant variability in our quarterly revenues and profitability, particularly in the first and fourth quarters of the year. Additionally, delays and other weather impacts may increase a project’s cost and decrease its profitability.

- Our Granite Land Company is greatly affected by the performance of the real estate industry. Our real estate development activities are subject to numerous factors beyond our control, including local real estate market conditions, substantial existing and potential competition, general national, regional and local economic conditions, fluctuations in interest rates and mortgage availability and changes in demographic conditions. If our outlook for a project’s forecasted profitability deteriorates, we may find it necessary to curtail our development activities and evaluate our real estate assets for possible impairment. If our real estate assets are determined to be impaired, the impairment would result in a charge to income from operations in the year of the impairment with a resulting decrease in our recorded net worth.

- We work in a highly competitive marketplace. As more fully described under “Competition” above, we have multiple competitors in all of the areas in which we work. During economic down cycles or times of lower government funding for

public works projects, competition for the fewer available projects intensifies and this increased competition may result in a decrease in our ability to be competitive at acceptable margins.

- An inability to secure and permit aggregate reserves could negatively impact our future operations and results. Tighter regulations for the protection of the environment and the finite nature of property containing suitable aggregate reserves are making it increasingly challenging and costly to secure and permit aggregate reserves. Although we have thus far been able to secure and permit reserves to support our business, it is likely to become increasingly difficult to do so and there is no assurance that we will be able to secure and permit reserves in the future.

- We are subject to environmental and other regulation. As more fully described under “Government and Environmental Regulations” above, we are subject to a number of federal, state and local laws and regulations relating to the environment, workplace safety and a variety of socioeconomic requirements, the noncompliance of which can result in substantial penalties, termination or suspension of government contracts as well as civil and criminal liability. While compliance with these laws and regulations has not materially adversely affected our operations in the past, there can be no assurance that these requirements will not change and that compliance will not adversely affect our operations in the future.

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- Strikes or work stoppages could have a negative impact on our operations and results. We are party to collective bargaining agreements covering a portion of our craft workforce. Although our results and operations have not been significantly impacted by strikes or work stoppages in the past, such labor actions could have a significant impact on our operations if they occur in the future.

- Unavailability of insurance coverage could have a negative impact on our operations and results. We maintain insurance coverage as part of our overall risk management strategy and pursuant to requirements to maintain specific coverage that are contained in our financing agreements and in most of our construction contracts. Although we have been able to obtain insurance coverage to meet our requirements in the past, there is no assurance that such insurance coverage will be available in the future.

- An inability to obtain bonding would have a negative impact on our operations and results. As more fully described in “Insurance and Bonding” above, we generally are required to provide surety bonds securing our performance under the majority of our public and private sector contracts. Our inability to obtain surety bonds in the future would significantly impact our ability to obtain new contracts, which would have a material adverse effect on our business.

- Our joint venture contracts with project owners subject us to joint and several liability. If a joint venture partner fails to perform we could be liable for completion of the entire contract and, if the contract were unprofitable, this could result in a material adverse effect on our financial position, results of operations and cash flows.

- We use certain commodity products that are subject to significant price fluctuations. Diesel fuel, liquid asphalt and other petroleum-based products are used to fuel and lubricate our equipment and fire our asphalt concrete processing plants and also constitute a significant part of the asphalt paving materials that are used in many of our construction projects and sold to outside parties. Although we are partially protected by asphalt or fuel price escalation clauses in some of our contracts, many contracts provide no such protection. We also use cement, steel and other commodities in our construction projects that can be subject to significant price fluctuations. We have not been significantly adversely affected by price fluctuations in the past; however, there is no guarantee that we will not be in the future.

- As a part of our growth strategy we expect to make future acquisitions and acquisitions involve many risks. These risks include difficulties integrating the operations and personnel of the acquired companies, diversion of management’s attention from our ongoing operations, potential difficulties and increased costs associated with completion of any assumed construction projects, insufficient revenues to offset increased expenses associated with acquisitions and the potential loss of key employees or customers of the acquired companies. Acquisitions may also cause us to increase our liabilities, record goodwill or other non-amortizable intangible assets that will be subject to subsequent impairment testing and potential impairment charges and incur amortization expenses related to certain other intangible assets. Failure to manage and successfully integrate acquisitions could harm our business and operating results significantly.

- Failure of our subcontractors to perform as anticipated could have a negative impact on our results. As further described under “Contract Provisions and Subcontracting” above, we subcontract a portion of many of our contracts to specialty subcontractors and we are ultimately responsible for the successful completion of their work. Although we seek to require bonding or other forms of guarantees, we are not always successful in obtaining those bonds or guarantees from our higher risk subcontractors, and there is no guarantee that we will not incur a material loss due to subcontractor performance issues.

- We may be unable to identify qualified Disadvantaged Business Enterprise (“DBE”) contractors to perform as subcontractors. Certain of our government agency projects contain minimum DBE participation clauses. If we subsequently fail to complete these projects with the minimum DBE participation we may be held responsible for damages due to breach of contract including restrictions on our ability to bid on future projects and monetary damages. To the extent that these events occur, the total costs of the project could exceed our original estimates and we could experience reduced profits or, in some cases, a loss for that project.

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- A significant portion of our revenue is from government funded contracts. Approximately 70% of our consolidated revenue in 2007 was derived from contracts funded by federal, state and local government agencies and authorities. These government contracts are subject to specific procurement regulations, contract provisions and a variety of socioeconomic requirements relating to their formation, administration, performance and accounting. Many of these contracts include express or implied certifications of compliance with applicable laws and contract provisions. As a result of our government contracting, claims for civil or criminal fraud may be brought by the government for violations of these regulations, requirements or statutes. We may also be subject to qui tam ("Whistle Blower") litigation brought by private individuals on behalf of the government under the Federal Civil False Claims Act, which could include claims for up to treble damages. Further, if we fail to comply with any of these regulations, requirements or statutes, our existing government contracts could be terminated, we could be suspended from government contracting or subcontracting, including federally funded projects at the state level. If our government contracts are terminated for any reason, or if we are suspended from government work, we could suffer a significant reduction in expected revenue.

- Our long-term debt and credit arrangements contain restrictive covenants and failure to meet these covenants could significantly harm our financial condition. Our long-term debt and credit arrangements and related restrictive covenants are more fully described in Note 10 of the "Notes to the Consolidated Financial Statements" included in this report. In most cases, failure to meet the restrictive covenants would result in an immediate repayment of all amounts due and cancellation of open lines of credit. Additionally, failure to meet restrictive covenants related to our debt and credit agreements would trigger cross-default provisions that would cause us to also be in default of our surety agreements. Although we have not had difficulty meeting these covenants in the past, failure to do so in the future could have material adverse effects on our business and financial condition.

- Our backlog is subject to unexpected adjustments and cancellations and could be an uncertain indicator of our future earnings. We cannot guarantee that the revenues projected in our backlog will be realized or, if realized, will result in profits. Projects may remain in our backlog for an extended period of time. In addition, project cancellations or scope adjustments may occur, from time to time, with respect to contracts reflected in our backlog. Backlog reductions can adversely affect the revenue and profit we actually receive from contracts reflected in our backlog. Future project cancellations and scope adjustments could further reduce the dollar amount of our backlog and the revenues and profits that we actually receive.

The foregoing list is not exhaustive. There can be no assurance that we have correctly identified and appropriately assessed all factors affecting our business or that the publicly available and other information with respect to these matters is complete and correct. Additional risks and uncertainties not presently known to us or that we currently believe to be immaterial also may adversely impact us. These developments could have material adverse effects on our business, financial condition and results of operations. For these reasons, the reader is cautioned not to place undue reliance on our forward-looking statements.

Item 1B. UNRESOLVED STAFF COMMENTS

None.

Item 2. PROPERTIES

The following table provides our estimate of certain information about our properties as of December 31, 2007:

	Land Area (acres)	Building Square Feet	Permitted Aggregate Reserves (tons)	Unpermitted Aggregate Reserves (tons)
Office and shop space (owned and leased)	1,300	1,300,000	N/A	N/A
Owned quarry property	N/A	N/A	424.0 million	435.0 million
Leased quarry property	N/A	N/A	359.0 million	565.0 million
Real estate held for development and sale	2,500	57,000	N/A	N/A

Approximately 83% of the office and shop space is used by Granite West at their various locations throughout the western United States and the remainder is primarily used by Granite East. The quarry property is located at Granite West locations throughout the western United States. We consider our available and future aggregate reserves adequate to meet our expected operating needs. We pursue a plan of acquiring new sources of aggregate reserves to replenish those depleted and to support future growth.

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Item 3. LEGAL PROCEEDINGS

Silica Litigation

Our wholly owned subsidiary Granite Construction Company (“GCCO”) is one of approximately 100 to 300 defendants in nine active California Superior Court lawsuits. Of the nine lawsuits, five were filed against GCCO in 2005 and four were filed against GCCO in 2006, in Alameda County (Riley vs. A-1 Aggregates, et al.; Molina vs. A-1 Aggregates, et al.; Dominguez vs. A-1 Aggregates, et al.; Cleveland vs. A. Teichert & Son.; Guido vs. A. Teichert & Son, Inc.; Williams vs. A. Teichert & Son, Inc.; Horne vs. Teichert & Son, Inc.; Kammer vs.A-1 Aggregates, et al.; and Solis vs. The 3M Company et al.). Each lawsuit was brought by a single plaintiff who is seeking money damages by way of various causes of action, including strict product and market share liability, and alleges personal injuries caused by exposure to silica products and related materials during the plaintiffs’ use or association with sand blasting or grinding concrete. The plaintiff in each lawsuit has categorized the defendants as equipment defendants, respirator defendants, premises defendants and sand defendants. We have been identified as a sand defendant, meaning a party that manufactured, supplied or distributed silica-containing products. Our preliminary investigation revealed that we have not knowingly sold or distributed abrasive silica sand for sandblasting, and therefore, we believe the probability of these lawsuits resulting in an incurrence of a material liability is remote. We have been dismissed from fifteen other similar lawsuits.

Hiawatha Project DBE Issues

The Hiawatha Light Rail Transit (“HLRT”) project was performed by Minnesota Transit Constructors (“MnTC”), a joint venture that consisted of GCCO and other unrelated companies. GCCO was the managing partner of the joint venture, with a 56.5% interest. The Minnesota Department of Transportation (“MnDOT”) is the contracting agency for this federally funded project. MnDOT and the U.S. Department of Transportation Office of Inspector General (“OIG”) each conducted a review of the Disadvantaged Business Enterprise (“DBE”) program maintained by MnTC for the HLRT project. In addition, the U.S. Department of Justice (“USDOJ”) is conducting an investigation into compliance issues with respect to MnTC’s DBE Program for the HLRT project. MnDOT and the OIG (collectively, the “Agencies”) have initially identified certain compliance issues in connection with MnTC’s DBE Program and, as a result, have determined that MnTC failed to meet the DBE utilization criteria as represented by MnTC. Although there has been no formal administrative subpoena issued, nor has a civil complaint been filed in connection with the administrative reviews or the investigation, MnDOT has proposed a monetary sanction of $4.3 million against MnTC and specified DBE training for personnel from the members of the MnTC joint venture as a condition of future bidding on MnDOT work by joint venture members of MnTC. MnTC is fully cooperating with the Agencies and the USDOJ and, on July 2, 2007, presented its response to the initial determinations of the Agencies as well as the investigation by the USDOJ. We have yet to receive a formal reply from the Agencies or the USDOJ, although informal discussions have been continuing and we cannot rule out the possibility of a criminal action being brought against MnTC or one of its members.

I-494 Project DBE Issues

The I-494 project was performed by a joint venture (“JV”) that consisted of GCCO and another unrelated party. GCCO was the managing partner of the JV, with a 60% interest. MnDOT is the contracting agency for this federally funded project. MnDOT conducted a review of the DBE program maintained by the JV for the I-494 project. MnDOT has initially identified certain compliance issues in connection with the JV’s DBE program, and as a result, has determined that the JV failed to meet the DBE utilization criteria as represented by the JV. Although there has been no formal administrative subpoena, nor has a civil complaint been filed in connection with the administrative reviews, MnDOT has proposed a monetary sanction of $200,000 against the JV and specified DBE training for personnel from the members of the JV as a condition of future bidding on MnDOT work by joint venture members of the JV. The JV is

fully cooperating with MnDOT and has the opportunity to present its response to MnDOT’s initial determinations. The JV is investigating MnDOT’s initial determinations and preparing its response thereto. Therefore, we cannot reasonably estimate the amount of any monetary sanction or what, if any, other sanction conditions might ultimately be imposed.

US Highway 20 Project

GCCO and its subsidiary, Wilder are the members of a joint venture known as Yaquina River Constructors (“YRC”) which is currently constructing a new road alignment of US Highway 20 near Eddyville, Oregon under contract with the Oregon Department of Transportation (ODOT). The project involves constructing seven miles of new road through steep and forested terrain in the Coast Range Mountains. During the fall and winter of 2006, extraordinary rain events produced runoff that overwhelmed erosion control measures installed at the project and resulted in discharges to surface water in alleged violations of the stormwater permit. The Oregon Department of Environmental Quality (“DEQ”) has issued notices of violation and fine of $90,000 to ODOT and $240,000 to YRC for these alleged violations. YRC has filed an answer to the notice of violation and is attempting to negotiate resolution with the DEQ. The Oregon Department of Justice is conducting a criminal investigation in connection with stormwater runoff from the project. YRC and its members are fully cooperating in the investigation, but YRC does not know whether criminal or civil charges, if any, will be brought or against whom. Therefore, we cannot estimate what, if any, criminal or civil penalty or conditional assessment will result from this investigation.

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Other Legal Proceedings

We are a party to a number of other legal proceedings arising in the normal course of business which, from time to time, include inquiries from public agencies seeking information concerning our compliance with government construction contracting requirements and related laws and regulations. We believe that the nature and number of these proceedings and compliance inquiries are typical for a construction firm of our size and scope. Our litigation typically involves claims regarding public liability or contract related issues. While management currently believes, after consultation with counsel, that the ultimate outcome of such proceedings and compliance inquiries which are currently pending, individually and in the aggregate, will not have a material adverse effect on our financial position or overall trends in results of operations or cash flows, litigation is subject to inherent uncertainties. Were an unfavorable ruling to occur, there exists the possibility of a material adverse impact on the results of operations, cash flows and/or financial position. While any one of our pending legal proceedings is subject to early resolution as a result of our ongoing efforts to settle, whether or when any legal proceeding will resolve through settlement is neither predictable nor guaranteed.

Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

During the fourth quarter of 2007, no matter was submitted to a vote of security holders through the solicitation of proxies or otherwise.

Executive Officers of the Registrant

Our executive officers are as follows:

Name	Age	Position
William G. Dorey	63	President, Chief Executive Officer and Director
Mark E. Boitano	59	Executive Vice President and Chief Operating Officer
William E. Barton	63	Senior Vice President and Chief Financial Officer
Michael F. Donnino	53	Senior Vice President and Granite East Division Manager
James H. Roberts	51	Senior Vice President and Granite West Division Manager

Granite Construction Incorporated was incorporated in Delaware in January 1990 as the holding company for Granite Construction Company, which was incorporated in California in 1922. All dates of service for our executive officers include the periods in which they served for Granite Construction Company.

Mr. Dorey has been an employee of Granite since 1968 and has served in various capacities, including President and Chief Executive Officer since January 2004, President and Chief Operating Officer from February 2003 to December 2003, Executive Vice President and Chief Operating Officer from 1998 to February 2003, Senior Vice President and Manager, Branch Division from 1987 to 1998, and Vice President and Assistant Manager, Branch Division from 1983 to 1987. Mr. Dorey has also served as a member of our Board of Directors since January 2004 and as a director of TIC Holdings, Inc. from 1997 to 2002. He received a B.S. degree in Construction Engineering from Arizona State University in 1967.

Mr. Boitano has been an employee of the Company since 1977 and has served in various capacities, including Chief Operating Officer since January 2004 and Executive Vice President since February 2003. He also served as Branch Division Manager from 1998 to January 2004, and Senior Vice President from 1998 to February 2003. Mr. Boitano received a B.S. degree in Civil Engineering from Santa Clara University in 1971 and an M.B.A. degree from California State University, Fresno in 1977.

Mr. Barton has been an employee of the Company since 1980 and has served as Senior Vice President and Chief Financial Officer since 1999, and as Vice President and Chief Financial Officer from 1990 to 1999. In 1997, he became a director of TIC Holdings, Inc. Mr. Barton received a B.S. degree in Accounting and Finance from San Jose State University in 1967 and an M.B.A. degree from Santa Clara University in 1973.

Mr. Donnino joined Granite in 1977 and has served as Senior Vice President since January 2005, Manager of Granite East since February 2007, and Heavy Construction Division Manager from January 2005 to February 2007. He served as Vice President and Heavy Construction Division Assistant Manager during 2004, Texas Regional Manager from 2000 to 2003 and Dallas Estimating Office Area Manager from 1991 to 2000. Mr. Donnino received a B.S.C.E. in Structural, Water and Soils Engineering from the University of Minnesota in 1976.

Mr. Roberts joined Granite in 1981 and has served in various capacities, including Senior Vice President since May 2004, Granite West Manager since February 2007, Branch Division Manager from May 2004 to February 2007, Vice President and Assistant Branch Division Manager from 1999 to 2004, and Regional Manager of Nevada and Utah Operations from 1995 to 1999. He received a B.S.C.E. in 1979 and an M.S.C.E. in 1980 from the University of California, Berkeley, and an M.B.A. from the University of Southern California in 1981.

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PART II

Item 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common stock trades on the New York Stock Exchange under the ticker symbol GVA. See "Quarterly Results" under "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operation" for a two-year summary of quarterly dividends and high and low sales prices of our stock.

We have paid quarterly cash dividends since the second quarter of 1990, and we expect to continue to pay quarterly cash dividends. However, declaration and payment of dividends is within the sole discretion of our Board of Directors, subject to limitations imposed by Delaware law and compliance with our credit agreements, and will depend on our earnings, capital requirements, financial condition and other such factors as the Board of Directors deems relevant.

As of February 13, 2008, there were 38,952,477 shares of our common stock outstanding held by 1,259 shareholders of record.

During the three months ended December 31, 2007, we did not sell any of our equity securities that were not registered under the Securities Act of 1933, as amended. The following table sets forth information regarding the repurchase of shares of our common stock during the three months ended December 31, 2007:

Period	Total number of shares purchased	Average price paid per share	Total number of shares purchased as part of publicly announced plans or programs[2]	Approximate dollar value of shares that may yet be purchased under the plans or programs[2]
October 1, 2007 through October 31, 2007	-	-	-	$ 200,000,000
November 1, 2007 through November 30, 2007	1,672,930	$ 36.13	1,672,930	$ 139,552,782
December 1, 2007 through December 31, 2007[1]	798,836	$ 40.50	797,500	$ 107,253,170
	2,471,766	$ 37.54	2,470,430	

[1]The number of shares purchased includes 1,336 shares purchased in connection with employee tax withholding for shares granted under our Amended and Restated 1999 Equity Incentive Plan and shares purchased under our share repurchase program.

[2]In October 2007, our Board of Directors authorized us to repurchase, at management's discretion, up to $200.0 million of our common stock. Under the new repurchase program, the Company may repurchase shares from time to time on the open market or in private transactions. The specific timing and amount of repurchases will vary based on market conditions, securities law limitations and other factors. The share repurchase program may be suspended or discontinued at any time without prior notice. This new program replaced a $25.0 million share repurchase program announced in 2002.

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Performance Graph

The following graph compares the 5-year cumulative total return to shareholders on Granite Construction Incorporated's common stock relative to the cumulative total returns of the S&P 500 index and the Dow Jones US Heavy Construction index. The Dow Jones US Heavy Construction index includes the following companies: EMCOR Group Inc., Fluor Corp., Granite Construction Inc., Insituform Technologies Inc., Jacobs Engineering Group Inc., McDermott International Inc., Quanta Services Inc. and Shaw Group Inc. An investment of $100 (with reinvestment of all dividends) is assumed to have been made in our common stock and in each of the indexes on December 31, 2002 and its relative performance is tracked through December 31, 2007.

The comparisons in the graph below are based on historical data and are not intended to forecast the possible future performance of our common stock.

	2002	2003	2004	2005	2006	2007
Granite Construction Incorporated	$ 100	$ 154.79	$ 178.40	$ 243.98	$ 344.72	$ 250.01
S & P 500	100	128.68	142.69	149.70	173.34	182.87
Dow Jones US Heavy Construction	100	136.41	165.42	239.03	298.17	566.39

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Item 6. SELECTED FINANCIAL DATA

The selected consolidated operations data for 2007, 2006 and 2005 and consolidated balance sheet data as of December 31, 2007 and 2006 set forth below have been derived from our audited consolidated financial statements included herein, and are qualified by reference to those consolidated financial statements. The selected consolidated operations data for 2003 and 2004 and the consolidated balance sheet data as of December 31, 2003, 2004 and 2005 have been derived from our audited consolidated financial statements not included herein. These historical results are not necessarily indicative of the results of operations to be expected for any future period.

Selected Consolidated Financial Data

Years Ended December 31,	2007	2006	2005	2004*	2003
Operating Summary		(In Thousands, Except Per Share Data)			
Revenue	$ 2,737,914	$ 2,969,604	$ 2,641,352	$ 2,136,212	$ 1,844,491
Gross profit	410,744	295,720	319,372	222,021	226,450
As a percent of revenue	15.0	10.0	12.1	10.4	12.3
General and administrative expenses	246,202	204,281	183,392	157,035	151,879
As a percent of revenue	9.0	6.9	6.9	7.4	8.2
Provision for (reversal of) legal judgment	-	(4,800)	9,300	-	-
Goodwill impairment charge**	-	18,011	-	-	-
Acquisition expense***	7,752	-	-	-	-
Net income	112,065	80,509	83,150	57,007	60,504
As a percent of revenue	4.1	2.7	3.1	2.7	3.3
Net income per share:					
Basic	$ 2.74	$ 1.97	$ 2.05	$ 1.41	$ 1.51
Diluted	2.71	1.94	2.02	1.39	1.48
Weighted average shares of common stock:					
Basic	40,866	40,874	40,614	40,390	40,175
Diluted	41,389	41,471	41,249	41,031	40,808
Balance Sheet					
Total assets	$ 1,786,418	$ 1,632,838	$ 1,472,230	$ 1,277,954	$ 1,060,410
Cash, cash equivalents and marketable securities	485,348	394,878	301,381	277,692	201,985
Working capital	397,568	319,762	367,801	355,927	274,947
Current maturities of long-term debt	28,696	28,660	26,888	15,861	8,182
Long-term debt	268,417	78,576	124,415	148,503	126,708
Other long-term liabilities	46,441	58,419	46,556	40,641	29,938
Shareholders’ equity	700,199	694,544	621,560	550,474	504,891
Book value per share	17.75	16.60	14.91	13.23	12.16
Dividends per share	0.43	0.40	0.40	0.40	0.40
Common shares outstanding	39,451	41,834	41,682	41,612	41,528
Backlog	$ 2,084,545	$ 2,256,587	$ 2,331,540	$ 2,437,994	$ 1,985,788

* Effective January 1, 2004, we adopted Financial Accounting Standards Board Interpretation No. 46 (revised December 2003) “Consolidation of Variable Interest Entities”.

**During the year ended December 31, 2006, we recorded a goodwill impairment charge of approximately $18.0 million related to our Granite Northeast operation in New York .

***During the fourth quarter ended December 31, 2007, we incurred a charge of $7.8 million associated with the acquisition of the remaining shares of Wilder Construction Company (see Note 15 of the “Notes to the Consolidated Financial Statements”).

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Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION

General

We are one of the largest heavy civil contractors in the United States as well as one of the largest construction materials production companies in the Western United States. We are engaged in the construction of highways, dams, airport infrastructure, mass transit facilities and other infrastructure-related projects as well as residential and commercial site development. We have offices in Alaska, Arizona, California, Florida, Minnesota, Nevada, New York, Texas, Utah and Washington. Our business involves three operating segments: Granite West, Granite East and Granite Land Company ("GLC") .

Our contracts are obtained primarily through competitive bidding in response to advertisements by federal, state and local agencies and private parties and to a lesser extent through negotiation with private parties. Our bidding activity is affected by such factors as backlog, current utilization of equipment and other resources, ability to obtain necessary surety bonds and competitive considerations. Bidding activity, backlog and revenue resulting from the award of new contracts may vary significantly from period to period.

The two primary economic drivers of our business are (1) federal, state and local public funding levels and (2) the overall health of the economy, both nationally and locally. The level of demand for our services will have a direct correlation to these drivers. For example, a weak economy will generally result in a reduced demand for construction in the private sector. This reduced demand increases competition for fewer private sector projects and will ultimately also increase competition in the public sector as companies migrate from bidding on scarce private sector work to projects in the public sector. Greater competition can reduce revenue growth and/or increase pressure on gross profit margins. A weak economy also tends to produce less tax revenue, thereby decreasing the funds available for spending on public infrastructure improvements. There are funding sources that have been specifically earmarked for infrastructure spending, such as gasoline taxes, which are not necessarily directly impacted by a weak economy. However, even these funds can be temporarily at risk as state and local governments struggle to balance their budgets. Conversely, higher public funding and/or a robust economy will increase demand for our services and provide opportunities for revenue growth and margin improvement.

Our general and administrative costs include salaries and related expenses, incentive compensation, discretionary profit sharing and other variable compensation, as well as other overhead costs to support our overall business. In general, these costs will increase in response to the growth and the related increased complexity of our business. These costs may also vary depending on the number of projects in process in a particular area and the corresponding level of estimating activity. For example, as large projects are completed or if the level of work slows down in a particular area, we will often re-assign project employees to estimating and bidding activities until another project gets underway, temporarily moving their salaries and related costs from cost of revenue to general and administrative expense. Additionally, our compensation strategy for selected management personnel is to rely heavily on a variable cash and restricted stock performance-based incentive element. The cash portion of these incentives is expensed when earned while the restricted stock portion is expensed over the vesting period of the stock (generally five years). Depending on the mix of cash and restricted stock, these incentives can have the effect of increasing general and administrative expenses in very profitable years and decreasing expenses in less profitable years.

In February 2007, we announced an organizational realignment of our business operations which is designed to accommodate growth of our vertically integrated Branch business in the West and improve profitability of our large, complex Heavy Construction Division ("HCD") projects. This realignment involved the reorganization of our operating divisions geographically into "Granite West" and "Granite East." Granite West includes the operations of our former Branch Division as well as the western portion of our large project business that was formerly included in HCD.

Granite West retains our successful decentralized operating structure, with each of its branch locations aligning under one of three operating groups: Northwest, Northern California and Southwest. Granite East includes the eastern portion of our large project business that had been included in HCD and is aligned to focus on enhancing project management oversight and discipline from estimating through execution. With the Division office in Lewisville, Texas, Granite East also operates out of three regional offices: the Central Region, based in Lewisville, Texas; the Southeast Region, based in Tampa, Florida; and the Northeast Region, based in Tarrytown, New York.

During 2007, we completed the reassignment of our large projects in the West from our former Heavy Construction Division to our Granite West Division (with the exception of certain projects nearing completion which remain with our Granite East Division) and made substantial progress on other aspects of the realignment. As a result, we are reporting Granite West and Granite East as new reportable segments. Prior period results have been reclassified to conform to the new organizational structure (see Note 1 of the "Notes to the Consolidated Financial Statements").

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Current Year Overview

Comparative Financial Summary

Years ended December 31, (in thousands)	2007	2006	2005
Total revenue	$ 2,737,914	$ 2,969,604	$ 2,641,352
Gross profit	410,744	295,720	319,372
General and administrative expenses	246,202	204,281	183,392
Provision for (reversal of) legal judgment	-	(4,800)	9,300
Goodwill impairment charge	-	18,011	-
Gain on sales of property and equipment	10,343	10,408	8,235
Operating income	174,885	88,636	134,915
Acquisition expense	7,752	-	-
Net income	112,065	80,509	83,150

Our results of operations for the year ended December 31, 2007 reflect improved results from Granite East which realized positive gross margins during the year compared with negative gross margins for the year ended December 31, 2006 and higher gross profit from Granite West. Our operating results for the year ended December 31, 2007 included increases in general and administrative expenses due primarily to costs incurred to support our acquisitions, growth strategy and higher variable compensation resulting from improved profitability. Additionally, our net income for the year ended December 31, 2007 reflects a one-time expense related to our acquisition of the remaining shares of Wilder Construction Company which was partially offset by an increase in non-operating income due primarily to the gain on a sale of a building by a partnership in which we hold an equity method investment which was recorded as equity in income of affiliates in our statements of income.

Critical Accounting Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Our estimates, judgments and assumptions are continually evaluated based on available information and experience; however, actual amounts could differ from those estimates.

Certain of our accounting policies and estimates require higher degrees of judgment than others in their application. These include the recognition of revenue and earnings from construction contracts, the valuation of certain assets and insurance estimates. We evaluate all of our estimates and judgments on an on-going basis.

Revenue Recognition for Construction Contracts: Our contracts with our customers are primarily either “fixed unit price” or “fixed price.” Under fixed unit price contracts, we are committed to provide materials or services required by a project at fixed unit prices (for example, dollars per cubic yard of concrete poured or cubic yards of earth excavated). While the fixed unit price contract shifts the risk of estimating the quantity of units required for a particular project to the customer, any increase in our unit cost over the expected unit cost in the bid, whether due to inflation, inefficiency, faulty estimates or other factors, is borne by us unless otherwise provided in the contract. Fixed price contracts are priced on a lump-sum basis under which we bear the risk that we may not be able to perform all the work profitably for the specified contract amount. The percentage of fixed price contracts in our backlog increased from approximately 68.0% at December 31, 2006 to approximately 72.0% at December 31, 2007. All state and federal government contracts and many of our other contracts provide for termination of the contract for the convenience of the party contracting with us, with provisions to pay us for work performed through the date of termination.

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We use the percentage of completion accounting method for construction contracts in accordance with the American Institute of Certified Public Accountants Statement of Position 81-1, “Accounting for Performance of Construction-Type and Certain Production-Type Contracts.” Revenue and earnings on construction contracts, including construction joint ventures, are recognized using the percentage of completion method in the ratio of costs incurred to estimated final costs. Revenue in an amount equal to cost incurred is recognized prior to contracts reaching 25% completion. The related profit is deferred until the period in which such percentage completion is attained. It is our judgment that until a project reaches 25% completion, there is insufficient information to determine what the estimated profit on the project will be with a reasonable level of assurance. In the case of large complex design/build projects we may continue to defer profit recognition beyond the point of 25% completion based on an evaluation of specific project risks. The factors considered in this evaluation of risk associated with each design/build project include the stage of design completion, the stage of construction completion, status of outstanding purchase orders and subcontracts, certainty of quantities, certainty of schedule and the relationship with the owner.

Revenue from contract claims is recognized when we have a signed settlement agreement and payment is assured. Revenue from contract change orders, which occur in most large projects, is recognized when the owner has agreed to the change order in writing. Provisions are recognized in the statements of income for the full amount of estimated losses on uncompleted contracts whenever evidence indicates that the estimated total cost of a contract exceeds its estimated total revenue. Contract cost consists of direct costs on contracts, including labor and materials, amounts payable to subcontractors, direct overhead costs and equipment expense (primarily depreciation, fuel, maintenance and repairs). Depreciation is provided using accelerated methods for construction equipment. Contract cost is recorded as incurred and revisions in contract revenue and cost estimates are reflected when known. The completion threshold for the start of contract profit recognition is applied to all percentage of completion projects unless and until we project a loss on the project, in which case the estimated loss is immediately recognized.

The accuracy of our revenue and profit recognition in a given period is almost solely dependent on the accuracy of our estimates of the cost to complete each project. Our cost estimates for all of our significant projects use a highly detailed “bottom up” approach and we believe our experience allows us to provide materially reliable estimates. There are a number of factors that can contribute to changes in estimates of contract cost and profitability. The most significant of these include the completeness and accuracy of the original bid, costs associated with added scope changes, extended overhead due primarily to owner and weather delays, subcontractor performance issues, changes in productivity expectations, site conditions that differ from those assumed in the original bid (to the extent contract remedies are unavailable), the availability and skill level of workers in the geographic location of the project and a change in the availability and proximity of equipment and materials. The foregoing factors as well as the stage of completion of contracts in process and the mix of contracts at different margins may cause fluctuations in gross profit between periods and these fluctuations may be significant. Substantial changes in cost estimates, particularly in our larger, more complex projects have had and can in future periods have a significant effect on our profitability.

Valuation of Real Estate Held for Development and Sale and other Long Lived Assets: Real Estate held for development and sale and other long-lived assets, which include property, equipment and intangible assets, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. We assess impairment of long-lived assets in accordance with FAS No. 144, “Impairment of Long-Lived Assets” (“FAS 144”). Circumstances which could trigger an impairment review include, but are not limited to: significant decreases in the market price of the asset; significant adverse changes in the business climate or legal factors; accumulation of costs significantly in excess of the amount originally expected for the acquisition or construction of the asset; current period cash flow or operating losses combined with a history of losses or a forecast of continuing losses associated with the use of the asset; or current expectation that the asset will more likely than not be sold or disposed of significantly before the end of its estimated useful life.

Recoverability is assessed based on the carrying amount of the asset and its fair value, which is generally determined based on the sum of the cash flows expected to result from the use and eventual disposal of the asset. An impairment loss is recognized in the Statement of Income when the carrying amount is not recoverable and exceeds fair value. In 2007, our analysis determined that a $3.0 million portion of our real estate held for development and sale was impaired. As a result, we recorded this amount as an impairment charge in the quarter ended December 31, 2007.

The process of estimating future cash flows related to an asset involves significant judgment, including future cash inflows related to the use or eventual sale of the asset and future cash outflows related to the development or use of the asset. Although we believe the estimates and assumptions we used in testing for impairment are reasonable and supportable, significant changes in any one of our assumptions could produce a significantly different result.

Insurance estimates: We carry insurance policies to cover various risks, primarily general liability and workers compensation, under which we are liable to reimburse the insurance company for a portion of each claim paid. The amounts that we are liable for generally range from the first $250,000 to $1.0 million per occurrence. We accrue for the estimated ultimate liability for incurred losses, both reported and unreported, using actuarial methods based on historic trends modified, if necessary, by recent events. Changes in our loss assumptions caused by changes in actual experience would result in a change in our assessment of the ultimate liability that could have a material effect on our operating results and financial position.

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Current Year

Revenue

Total Revenue

Years ended December 31,	2007		2006		2005	
(in thousands)	Amount	Percent	Amount	Percent	Amount	Percent
Revenue by Division:						
Granite West	$ 1,928,751	70.4	$ 1,927,996	64.9	$ 1,599,458	60.6
Granite East	768,451	28.1	1,006,617	33.9	1,022,196	38.7
GLC	40,712	1.5	34,991	1.2	19,698	0.7
Total	$ 2,737,914	100.0	$ 2,969,604	100.0	$ 2,641,352	100.0

Granite West Revenue

Years ended December 31,	2007		2006		2005	
(in thousands)	Amount	Percent	Amount	Percent	Amount	Percent
California:						
Public sector	$ 595,733	56.7	$ 537,967	48.5	$ 374,642	43.0
Private sector	215,770	20.5	300,245	27.0	282,752	32.4
Material sales	239,660	22.8	272,039	24.5	214,520	24.6
Total	$ 1,051,163	100.0	$ 1,110,251	100.0	$ 871,914	100.0
West (excluding California):						
Public sector	$ 563,392	64.2	$ 508,559	62.2	$ 445,590	61.2
Private sector	178,156	20.3	171,166	20.9	164,821	22.7
Material sales	136,040	15.5	138,020	16.9	117,133	16.1
Total	$ 877,588	100.0	$ 817,745	100.0	$ 727,544	100.0
Total Granite West Revenue:						
Public sector	$ 1,159,125	60.1	$ 1,046,526	54.3	$ 820,232	51.3
Private sector	393,926	20.4	471,411	24.4	447,573	28.0
Material sales	375,700	19.5	410,059	21.3	331,653	20.7
Total	$ 1,928,751	100.0	$ 1,927,996	100.0	$ 1,599,458	100.0

Granite West Revenue: Revenue from Granite West for the year ended December 31, 2007 increased by $0.8 million, or 0.1%, compared with the year ended December 31, 2006. Our California revenue in 2007 was most impacted by the continued slowing of residential construction which led to decreases in both private sector construction revenue and revenue from the sale of construction materials. These decreases were partially offset by increased California public sector revenue, primarily driven by a higher volume of projects available to bid. We continue to see additional competition for the available public sector work, as competitors migrate from the increasingly scarce private sector work. Our revenue from the West (excluding California) in 2007 included approximately $89.0 million generated as a result of our acquisition of certain assets of the Superior Group of Companies on April 3, 2007. Other than Northern Nevada, our locations outside of California have generally been less impacted by the slowing of residential construction.

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Granite East Revenue Years ended December 31,	2007		2006		2005	
(in thousands)	Amount	Percent	Amount	Percent	Amount	Percent
Revenue by Geographic Area:						
Midwest	$ 93,896	12.2	$ 43,480	4.3	$ 77,104	7.5
Northeast	196,653	25.6	259,462	25.8	299,950	29.4
South	125,164	16.3	217,647	21.6	199,579	19.5
Southeast	299,084	38.9	281,568	28.0	216,442	21.2
West	53,654	7.0	204,460	20.3	229,121	22.4
Total	$ 768,451	100.0	$ 1,006,617	100.0	$ 1,022,196	100.0
Revenue by Market Sector:						
Public sector	$ 747,580	97.3	$ 979,475	97.3	$ 987,794	96.6
Private sector	20,871	2.7	27,042	2.7	31,765	3.1
Material sales	-	-	100	-	2,637	0.3
Total	$ 768,451	100.0	$ 1,006,617	100.0	$ 1,022,196	100.0
Revenue by Contract Type:						
Fixed unit price	$ 128,501	16.7	$ 243,103	24.2	$ 323,048	31.6
Fixed price, including design/build	639,950	83.3	763,395	75.8	696,511	68.1
Other	-	-	119	-	2,637	0.3
Total	$ 768,451	100.0	$ 1,006,617	100.0	$ 1,022,196	100.0

Granite East Revenue: Revenue from Granite East for the year ended December 31, 2007 decreased by $238.2 million, or 23.7%, compared with the year ended December 31, 2006. Geographically, the largest decreases were experienced in the West, South and Northeast. Under the realignment, Granite East retained a project in the West that was nearing completion and the decrease in revenue in the West reflects progress on the retained project over time. In the South and Northeast the decreases were due primarily to certain large projects in Texas and New York nearing completion. Increases in the Southeast resulted from revenue contributions from a large design/build project in Mississippi that was awarded in February 2006. Increases in the Midwest resulted from revenue contributions from a large design/build project in Missouri that was awarded in the fourth quarter of 2006. The percent of our revenue from fixed price contracts increased in 2007 due primarily to a higher percentage of design/build projects in our backlog.

The following table provides additional information about our revenue from large projects for the years ended December 31, 2007, 2006 and 2005:

Large Project Revenue Years ended December 31,	2007	2006	2005
(in thousands)			
Granite West	$ 160,232	$ 185,474	$ 72,476
Number of projects *	6	6	3
Granite East	$ 732,086	$ 889,201	$ 899,475
Number of projects *	31	28	34
Total	$ 892,318	$ 1,074,675	$ 971,951

Number of projects *	37	34	37

* Includes only projects with a total contract value greater than $50.0 million and over $1.0 million of revenue in the respective periods.

Granite Land Company Revenue: Revenue from GLC for the year ended December 31, 2007 increased by $5.7 million, or 16.4%, compared with the year ended December 31, 2006. GLC's revenue is dependent on the timing of real estate sales transactions, which are relatively few in number and can cause variability in the timing of revenue and profit recognition.

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Backlog

Total Backlog December 31, (in thousands)	2007 Amount	2007 Percent	2006 Amount	2006 Percent
Backlog by Division:				
Granite West	$ 854,142	41.0	$ 1,015,674	45.0
Granite East	1,230,403	59.0	1,240,913	55.0
Total	$ 2,084,545	100.0	$ 2,256,587	100.0

Granite West Backlog December 31, (in thousands)	2007 Amount	2007 Percent	2006 Amount	2006 Percent
California:				
Public sector	$ 352,398	83.9	$ 423,542	84.2
Private sector	67,479	16.1	79,718	15.8
Total	$ 419,877	100.0	$ 503,260	100.0
West (excluding California):				
Public sector	$ 398,380	91.7	$ 438,256	85.5
Private sector	35,885	8.3	74,158	14.5
Total	$ 434,265	100.0	$ 512,414	100.0
Total Granite West backlog:				
Public sector	$ 750,778	87.9	$ 861,798	84.8
Private sector	103,364	12.1	153,876	15.2
Total Granite West backlog	$ 854,142	100.0	$ 1,015,674	100.0

Granite West Backlog: Granite West backlog of $854.1 million at December 31, 2007 was $161.5 million, or 15.9%, lower than at December 31, 2006. The lower private sector backlog at December 31, 2007 compared with December 31, 2006 is primarily a result of the slowing demand for residential construction, particularly in certain California and Nevada markets. The lower 2007 public sector backlog in California was largely due to increased competition for the available work as contractors migrate from the increasingly scarce private sector work. Additionally, the lower public sector backlog reflects progress on a $234.2 million joint venture highway reconstruction project in Utah that was awarded at the end of 2005. Granite West project awards in the fourth quarter 2007 included a $24.4 million highway reconstruction project near the California-Nevada border.

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Granite East Backlog

December 31,	2007		2006	
(in thousands)	Amount	Percent	Amount	Percent
Backlog by Geographic Area:				
Midwest	$ 328,971	26.8	$ 422,942	34.1
Northeast	133,052	10.8	219,835	17.7