



A Systematic Approach to Reviewing a New Stock – Part II

Description

[Jumping right in from where we left off](#), let's take a break from the numbers and find out what **Mediagrif Interactive (TSX:MDF)** is all about. What we're looking for is an indication of barriers to entry and a competitive advantage.

Background

Mediagrif has been around since 1996 and is a provider of e-commerce solutions for business. Not an overly focused pitch. The company provides solutions in the fields of electronic components, computer equipment and telecomm, medical equipment, automotive aftermarket, wine and spirits, diamonds and jewellery, classified ads, supply chain, and government opportunities. Why not taxidermy?

Luckily, the model is not as scattered as it may appear. A great resource for business descriptions is the annual information form (AIF), typically found at www.sedar.com. From the AIF we learn that Mediagrif provides e-commerce platforms that enable clients to find, purchase and sell products, exchange info, gain access to business opportunities and manage supply chain collaboration. These platforms are largely industry agnostic, hence the diverse range that the company serves.

This business model explains the cyclical nature that we uncovered [in Part I](#). As the economy slowed, less transactions were flowing through the Mediagrif platforms. It also explains the operating leverage. The platform is there. The more transactions, the more profitable it is.

Unfortunately, this business model does not fit very well with our desire for barriers to entry or a competitive advantage. This is a significant obstacle to our review. The company's business is not about the platforms that it owns. Others do the same thing and barriers to entry are non-existent. It's about who uses the platforms. The only possible competitive advantage would be if the company could somehow lock-up its clientele to prevent them from moving their business to another platform. The reality is, the users will go to the e-commerce platform that is best for them. Today it might be Mediagrif. Tomorrow, nobody knows.

Valuation

Given the nature of this business model, valuation doesn't matter. You can't accurately assess the value of a company that carries such a high risk of having customers today and not tomorrow. This company has potential value trap written all over it should it slide again as past numbers do not reflect future results. The recovery may not be as kind next time. Time to move on.

The Foolish Bottom Line

A systematic approach to evaluating potential investments is one of the best things that you can do to help ensure success. Eliminate the noise, like stock performance. Focus on simple metrics and concepts. If these metrics check out, go deeper. If you keep poking and find nothing that pokes back, chances are good you've found a great candidate for your hard-earned savings. At the very least, you will build an inventory of go-to stocks for when prices co-operate.

We could have started with the business model for Mediagrif and tossed this name aside right away. Numbers however help paint a picture, and they are relatively quick and easy to access. If Mediagrif would have had a heavy debt load, or no history of generating free cash, we would have moved on. It just so happened it didn't, so we kept poking.

Investing takes time and effort and you're going to (or at least should be taking a) pass on many more ideas than you end up transacting on. However, if you focus on key variables like financial risk, free cash flow, barriers to entry and competitive advantage, the long-term will reward your time and effort.

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Fool contributor Iain Butler does not own shares in any of the companies mentioned in this report at this time. The Motley Fool has no positions in the stocks mentioned above.

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