



## Aecon Group Inc.: The Right Ingredients

### Description

I am always on the lookout for an attractively valued, overlooked company that has all the right characteristics that tend to lead to stock price outperformance. And I am always excited when I find one, and equally excited to share my findings.

**Aecon Group Inc.** ([TSX: ARE](#)) is one of Canada's largest publicly traded construction and infrastructure development companies and has been active since 1877. Aecon is involved in the following business segments:

- Mining, which offers mine-site installation services and contract mining services
- Infrastructure, which groups all of Aecon's transportation, heavy civil, utilities, and social infrastructure capabilities and services
- Energy, which offers a full suite of construction and fabrication services to the oil and gas, nuclear, co-generation, and renewable sectors.

### The Right Stuff

Aecon has been steadily growing its business over the last 6 years, and has increased revenue from just over \$1 billion in 2006 to \$2.9 billion in 2012. This represents a compound annual growth rate (CAGR) of 17%. EBITDA has grown at a CAGR of 28% over the same period, and dividends have grown at a 13% CAGR.

Another check on the checklist is Aecon's free cash flow generation, calculated as operating income less capital expenditures. Free cash flow was positive in 2011 and 2012, at \$99 million and \$17 million respectively. Free cash flow is a measure of whether a company can sustain its business without the use of external funds.

Aecon's backlog as at the end of the first quarter of 2013 stands at \$2.073 billion. This speaks to the ability to forecast the health of the business on a go forward basis. Not only does Aecon have a strong backlog, the portion of the company's revenues that are recurring is also increasing. As at the end of

the first quarter of 2013, recurring revenue was \$700 million, up from less \$200 million in 2006. The recurring revenues are related to a variety of construction services, in particular much of the work performed in Contract mining and utilities, and they give more predictability to revenue and earnings going forward.

Finally, Aecon is very attractively valued in the market at this time. In my view, Aecon's P/E multiple of 10.4x is low considering the growth in earnings that we can expect in the next few years, the company's 2012 ROE of 14.7%, the good visibility going forward, and the fact that this is a well-managed company that has provided investors with good financial results over time.

## Review of first quarter results

### Results for the quarter ended March 31

	2013	2012	% change
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Revenue	\$567	\$486	17%
Operating loss	-\$31.1	-\$17.3	
EPS	-\$0.53	-\$0.33	

In the first quarter, revenue increased 17%, driven by increases in the utilities segment, the energy segment, and strong growth in volume in the mining segment. Aecon recorded a loss in EPS of \$0.53, higher than the loss of \$0.33 in the first quarter of 2012.

At this juncture, let's remind ourselves that Aecon's business is seasonal, and that the first half of the year, particularly the first quarter, typically generates lower revenue and profits than the second half of the year. But this quarter was also impacted by a one-time \$19 million provision. This provision was due to client-related delays, unseasonably wet weather, and the bankruptcy of a key contractor. Aecon is pursuing claims with respect to this project, which was 89% complete as at the end of the first quarter, and the full anticipated loss on the project has been recognized in the first quarter. Without this provision, operating income would have improved this quarter versus the first quarter of 2012. Also, progress was made from a revenue and margin perspective.

## Bottom Line

Management has stated that they will focus on returning capital to shareholders over time and that they see unprecedented opportunities in their key sectors. And in my view, they are in the position to do both going forward. Revenue is growing nicely and profitability is strong. Canada's infrastructure requires big investment over the next few years, and the energy sector also requires investment in its infrastructure. Aecon is very well positioned to take advantage of these opportunities.

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*Fool contributor Karen Thomas does not own shares in any companies mentioned at this time. The Motley Fool doesn't own shares of any of the companies mentioned at this time.*

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1. Investing

## TICKERS GLOBAL

1. TSX:ARE (Aecon Group Inc.)

## Category

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