3 Reasons to Avoid Westport Innovations

Description

Here at The Motley Fool, you will find plenty of arguments for why you should buy **Westport Innovations** (TSX: WPT)(Nasdaq: WPRT) shares. And there's a pretty compelling case to make for the natural gas engine technology provider. Growth potential is sky-high – revenue was up 39% year-over-year last quarter. Profitability metrics are improving. And the shares have gotten bludgeoned, perhaps creating a nice buying opportunity.

But there are also plenty of reasons to avoid the company's shares. Below are the top three.

1. Problems with competitiveness

The main appeal with Westport's technology centres around cheap natural gas in North America. But over the past couple of years, natural gas prices have increased, reducing the cost advantage that natural gas enjoys over diesel. Longer term, there is the prospect of electric vehicles playing a more significant role in transportation, pushing aside natural gas vehicles.

This is a problem that investors face whenever a company must constantly innovate just to compete with other technologies. To illustrate, Westport spent over half its revenue on Research & Development last year; it's hard to make money when you're doing such a thing.

2. A lack of profitability

Besides high natural gas prices, Westport's stock has also fallen because of a lack of profitability. In 2013, the company lost a staggering $185 million on just $164 million of sales. The good news is that this number is improving. Management expects positive adjusted EBITDA from operations by the end of 2014, and the company to be profitable overall by 2015.

But Westport has been burning cash for years now, and it looks like the company will need to grow revenue significantly to improve the bottom line. In situations like this, an investment in the shares becomes especially risky.

3. Still an expensive stock

Despite the recent share drop, Westport still has a market capitalization of about $1 billion – about six times revenue. This puts Westport on par with other high-technology companies, including plenty of companies that are more profitable.

A simple comparison draws a clearer picture. Consider auto parts manufacturer **Magna International** (TSX: MG)(NYSE: MGA), whose product line is not as sexy as Westport's. Magna trades at only 0.6 times revenue, and unlike Westport, Magna actually makes money.

So despite the share price drop, Westport shares still are a very speculative investment opportunity. Higher natural gas prices have hurt competitiveness in the short run, and other technologies may hurt Westport in the long run.

The company is not profitable, partly due to a need to spend so much on research and development. And its shares are still very expensive. Eventually the company may grow enough to justify its share price, but so far it may be best just to wait and see.

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