



Why Investors Should Take a Closer Look at Ballard Power

Description

Last week, **Ballard Power** (TSX: BLD)([NASDAQ: BLDP](#)) signed an assembly licensing agreement with Azure Hydrogen for telecom backup systems in China. The stock was up 25% in the last five days amid continuing signs that Ballard's strategy will start to bear fruit. Here is why I believe that this stock has the real potential to go much higher.

The deal fits with Ballard's diversification strategy

The licensing deal is valued at \$6 million over the 2014/2015 period. Putting this into context, its 2013 revenue was \$17.3 million, so it is a significant deal. Furthermore, Ballard will be the exclusive supplier of subsystems and will receive a royalty payment for each telecom backup system sold in China if Azure meets its volume commitments.

This latest deal contributes to further diversifying the company's results, so it's not a one-trick pony anymore as it was in the days when Ballard was only involved in automotive fuel cells. Licensing is an important part of the company's reinvention, and this deal is an important step in that direction.

Ballard has already lowered its risk profile by diversifying its revenue base. Ballard's sources of revenue now span from telecom backup power to power generation, buses, and engineering services. In the first quarter of 2014, the company's revenue was segmented into four divisions: telecom backup power, at 20.7% of revenue; material handling, at 14.3% of revenue; engineering services, at 52.9% of revenue; and development stage markets, at 12.1% of revenue.

Latest results show continued momentum

In the first quarter of 2014, revenue increased 13%. Of note was the material handling segment, which saw a 125% increase in revenue as a result of its partnership with **Plug Power** ([NASDAQ: PLUG](#)). Plug Power's fuel cell product, GenDrive, is an alternative to lead-acid batteries for electric lift trucks that is gaining market acceptance and usage. Ballard supplies the company with the fuel cell stacks for its GenDrive power units. It was recently announced that **Walmart** ([NYSE: WMT](#)) has ordered 38 new GenDrive systems to be delivered over the next two years. On the fourth-quarter conference call, Ballard's management indicated that based on Plug Power's reported new orders, Ballard expects a

50% increase in shipments in 2014. This does not include the Walmart deal, which is very significant in itself.

On the negative side, the telecom backup power segment saw a 55% decrease in revenue. Management attributed this to uneven demand in early-stage markets, and given the strong pipeline in this segment, management's expectation for robust growth for this segment remains intact.

In the engineering services segment, revenue increased 185% as work with Volkswagen and other automotive OEMs remained on track.

The gross margin of 25% was up from 24% in the first quarter of 2013, EBITDA saw a 61% improvement, and earnings per share saw a 57% improvement to a loss of \$0.03 per share.

A strong balance sheet

At the end of the end of the first quarter on March 31, 2014, Ballard had \$40 million in cash on its balance sheet, compared to \$30 million at the end of 2013, which is an increase of 33%. The increase in the cash balance is primarily due to the 7.6 million share purchase warrants that were exercised for common shares and generated proceeds of \$11.7 million. Its debt remains negligible.

Management expects 30% revenue growth in 2014 and a break-even adjusted EBITDA.

Of course, when a stock has risen as much as Ballard has recently — 147% for the year to date — investors are wise to be cautious, especially when the stock has no earnings and trades at over nine times sales. There is an elevated level of risk due to its valuation, but there is also a lot of potential for growth and some very promising signs. Given the strategic changes that have occurred over the years like its greater diversification of revenues, its solid balance sheet, and the strong growth profile exhibited as of late, along with the expectation of finally becoming profitable, I view the risk/reward relationship favourably.

CATEGORY

1. Investing

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1. NASDAQ:BLDP (Ballard Power Systems Inc.)
2. NASDAQ:PLUG (Plug Power Inc.)
3. NYSE:WMT (Wal-Mart Stores Inc.)

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