Could This Apparel Stock Rally Another 45% in 2015?

Description

Performance Sports Group (TSX: PSG)(NYSE: PSG), one of the world's leading designers, manufacturers, and distributors of sporting apparel, equipment, and accessories, has been one of the market's best performing stocks in 2014, rising more than 48% year-to-date compared to the TSX Composite Index's return of just over 6.6%. Strong earnings results have played a crucial role in the company's rising stock price and it could continue higher following the release of its second-quarter earnings on January 12.

Let's take a look at three of the most important factors Performance Sports Group will need to satisfy in its report if its stock is going to react positively and then determine if its stock represents a long-term investment opportunity today.

1. EPS and revenue results must meet or beat expectations

First and foremost, Performance Sports Group's earnings per share and revenue results must meet or exceed analysts' expectations. Here's a chart of the current consensus estimates and the company's actual results in the year-ago period.

Metric	Expected	Year-Ago
Earnings Per Share	$0.20	$0.20
Revenue	$162.8 million	$117.1 million

Source: Financial Times

The estimates above call for Performance Sports Group's earnings per share to remain unchanged and its revenue to increase 39% year-over-year, which would be an improvement from 19% earnings per share decline and 28% revenue growth reported in the first quarter.

2. The gross and operating margins must stabilize

Secondly, Performance Sports Group needs to get its expenses under control, so its margins can stabilize. In the first quarter, gross margin contracted 270 basis points to 37.2% and its operating margin contracted 800 basis points to 11.2%. These weak results can be attributed to costs of sales and selling, general, and administrative expenses increasing 41.3% and 38.8%, respectively, both of which far outpaced the company's 28% revenue growth. Performance Sports Group will need to better hedge itself from commodity cost inflation or implement a costs savings program to get its expenses under control going forward.

3. The company needs to begin paying down its debt

Lastly, Performance Sports Group needs to begin paying down both its short-term and long-term debt. In the first quarter, the company reported $420 million in total debt compared to just $206.6 million in the year ago period, and a large portion of this debt can be attributed to the financing of its acquisition of Easton in 2014. Even though the acquisition of Easton will be a driver of revenue growth going forward, Performance Sports Group can simply not afford to carry the increased debt load for an extended period of time without negatively impacting shareholders' returns.

Is now the time to buy Performance Sports Group?

Performance Sports Group is one of the world's leading providers of sporting apparel and equipment, and increased demand for its products led it to a solid financial performance in 2014. Its stock has responded by rising more than 48% year-to-date. The company is currently scheduled to release second-quarter earnings on January 12, and if it can meet or exceed analysts' earnings per share and revenue expectations, stabilize its margins, and begin paying down its debt, I think its stock could rally even higher in 2015.

I think Performance Sports Group represents an intriguing long-term investment opportunity, because its stock trades at inexpensive valuations today, including only 19.1 times fiscal 2015's estimated earnings per share of $1.10 and just 16.7 times fiscal 2016's estimated earnings per share of $1.26. With these valuations in mind, I think long-term investors should consider initiating positions in Performance Sports Group prior to its earnings report and adding to them on any weakness following the release.

CATEGORY

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