



Why Now Is the Right Time to Buy Western Forest Products Inc.

Description

Looking at **Western Forest Products Inc.'s** ([TSX: WEF](#)) financials over the last five years, we can see a picture of a company that has grown its revenue, improved margins, and generated strong cash flows, even though all the while the lumber market has been tough, to say the least.

And now the company is faced with an improving outlook, a cheap stock, and a business that has been effectively managed and is very well set up to benefit from this. And, as icing on the cake, the 4.4% dividend yield will also appeal to investors.

Here is my bullish take on the company and stock:

Highly profitable business

Management's goal is to "maximize product margins while increasing sales volumes." Gross margins have increased over the years and now stand at 21% and EBIT margin currently sits at 9%. Furthermore, the company's ROE is roughly 30%.

The company has been free-cash-flow positive for many years now and its balance sheet is quite strong, with a debt-to-equity ratio of 20%. These numbers are well above **Interfor Corp.'s** profitability metrics, and Interfor has not been consistently free-cash-flow positive as Western Forest Products has been.

Western Forest Products is able to achieve higher and more stable margins because 74% of its lumber revenue is generated from non-commodity products, and this specialty lumber sells at a significant premium to commodity lumber.

Supply/demand balance improving

The company's latest presentation went over the four factors that they expect will favourably impact the demand/supply fundamentals of the industry.

First, they are seeing improving demand from the U.S., as the housing market and remodeling activity

are both recovering. Second, in China there is a shortage of domestic fibre, so the country will have to rely more on imports. Rising wealth in China makes it a good market that is expected to see strong demand over the long term. Third, Western Forest Products could see strong demand from Japan, as U.S. exporters are increasingly selling their products to U.S. customers. And lastly, we can thank the mountain pine beetle here in Canada for reducing the supply of North American lumber.

Benefits from weaker Canadian dollar

The Canadian dollar has fallen roughly 14% since last year, and Western Forest Products will benefit from this as U.S. dollar-denominated revenue accounts for 48% of total revenue. We are still seeing downward pressure on the Canadian dollar and can expect that it will continue to contribute to improved lumber pricing and volumes in North America.

Outlook

We can reasonably expect the previously mentioned factors to continue to benefit Western Forest Products, as the company continues to work on its \$125 million worth of projects that are aimed at reducing costs and improving productivity.

Based on consensus analyst estimates, Western Forest Products is expected to grow its EPS by 41% in 2015 and 50% in 2016. The stock trades at a P/E ratio of 7.6 times 2015 estimated EPS.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. TSX:WEF (Western Forest Products Inc.)

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