Should You Invest in Canada’s Most Hated Companies?

Description

In 2015 it seems like success in business almost goes hand in hand with being successful at public relations.

Think about Canada’s top companies. Banks sponsor everything from charity events to the naming rights for stadiums and arenas, while padding their bottom lines by increasing account fees and charging hefty fees for things like overdraft or bouncing a cheque. The largest media companies are happy to profit off of the goodwill Canadians feel towards their favorite media personalities and channels, all while a different division of the same company will charge as much as possible for cable, Internet, or wireless service.

So, as a consumer I can see how these companies can be unpopular. I hate the inevitable yearly increase of my cable bill just as much as anyone. But over the years, I’ve come to a conclusion—the kinds of companies who are well enough established to be hated are usually pretty good investments. They tend to provide a service people need where there aren’t many alternatives. Those are the kinds of companies we should have in our portfolios.

Let’s take a look at two different names that are constantly mentioned as the most hated in the country and see whether they look to be attractive investments.

Royal Bank

Royal Bank of Canada (TSX:RY)(NYSE:RY) sent the world of main street finance into a fluster when it recently announced increases in the fees charged for bank accounts.

The reaction by consumers would be interesting if it wasn’t so predictable. Just like every other time this happens, a very small minority got very vocally upset, vowing to take their business to another bank—usually to an online one with no branches.

From Royal Bank's perspective, seeing these customers go isn't so bad. They've proven themselves to be extremely price conscious. I don't care what business you're in; those types of customers are the worst. By raising fees, it gives these customers a good reason to leave and be another bank's problem.

Besides, it's other areas of retail banking that are the most profitable. It takes 30 years of charging someone $10 per month to make the same amount of revenue as the annual interest on a $100,000 mortgage.

If anything, shareholders should applaud moves like this one. The extra fees charged to customers will more than make up for the people who leave. This is nothing more than a vocal minority making noise.

Just Energy

Just Energy Group Inc. (TSX:JE)(NYSE:JE) is the middleman in the world of electricity and natural gas. In exchange for a certain fee every month, it takes care of monitoring, recording, and then billing customers for usage.

On the surface, this seems like a pretty risk-free business. What can go wrong if it charges a fixed fee for these services each month?

It comes down to the marketing. Company sales reps will often go door to door, which is not popular in 2015. Additionally, reps are paid heavily on commission, which increases their motivation to fudge the numbers to get a sale. One Google search confirms this problem is very real.

But perhaps the most compelling reason to stay away from Just Energy is its unsustainable dividend. Through the first nine months of its fiscal 2014, the company generated just $19 million in free cash flow, while paying out more than $64 million in dividends. That's not sustainable in the long term.

There's a history of the company being unable to pay its dividend, too. After converting from an income trust to regular corporation in 2010, the company paid $0.10 per share monthly. Two years ago, the dividend was cut to $0.07 per share per month, eventually getting cut again last year to just $0.50 per year.

The difference between these two unpopular companies is the quality of the underlying business. Royal Bank is consistently profitable, while Just Energy isn't. Just Energy has a weak balance sheet, and is constantly accused of lying to customers. Say what you want about Royal Bank, but it doesn't often get accused of that.

Hated companies can be great investments, provided the underlying business is sound. In this case, Royal Bank is as solid as they come, while Just Energy has some issues.

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