



SNC-Lavalin Group Inc.: How Undervalued Is This Dividend Stock?

Description

Dividend investors are always on the lookout for stocks that pay reliable and increasing distributions. Most of the time these companies command a premium, but once in a while you get a chance to pick one up on sale.

You might think **SNC-Lavalin Group Inc.** (TSX:SNC) is a risky pick given all the troubles the company has been facing over the past few years, but it could be one of the most undervalued stocks in Canada right now.

The company's dodgy dealings in Libya continue to be a big overhang on the shares. Investors thought the scandal was done and buried once all the staff members connected to the corruption issues were fired, but a new RCMP charge filed against the company in February has been an added thorn in management's side.

The reason for investor concern is that any company convicted of corrupting or bribing public officials is supposed to receive a 10-year ban on bidding for Government of Canada contracts.

SNC-Lavalin does a lot of business with the Canadian government, so a conviction would certainly not be good for the stock price.

The shares initially took a nosedive in February on news of the RCMP charges, but they have slowly regained most of those losses.

The market seems to think the company will avoid the ban. Some observers feel that SNC will either pay a fine, as SNC has publicly said it would prefer to do, or the government will modify the wording on the rules so that SNC can continue to win contracts in the country.

The latter possibility arose when the budget came out. Wording buried in the budget document said new bidding rules will be "consistent with best practices in Canada and abroad" and ensure that companies are provided with "due process and a whole-of-government perspective."

One interpretation could be that SNC is simply "too important to ban." Whether or not that is the

government's position is anyone's guess, but the company and its consortium partners recently won a large 35-year contract to build, operate, and maintain Montreal's new Champlain Bridge. For the time being, at least, it's business as usual.

Scandal aside, the company looks like a pretty good buy. SNC reported Q1 2015 earnings of \$0.68 per share, a 10% increase over the same period last year. The company finished the quarter with \$2 billion in cash and short-term investments and a revenue backlog of \$11.6 billion.

SNC is in the process of finding a buyer for its ownership stake in the Highway 407 toll road. Some analysts estimate the sale could bring in \$3 billion, which works out to be about \$20 per share on the 150 million shares outstanding. The cash and short-term investments are worth another \$13.3 per share, so that's about \$33.3 per share right there.

With the stock currently trading at \$44.30, you are really only paying \$11 per share for the rest of the company, which includes the nearly \$12 billion in revenue backlog.

Dividend growth and share buybacks

SNC pays a dividend of \$1 per share. The company has increased the payout by 47% in the past five years and recently announced plans to buy back 10% of the outstanding shares.

Risks

The RCMP charges should be taken seriously and any indication that the company could be convicted would be bad news for the stock, at least in the short term.

The company is also suffering from the slump in both the energy and mining sectors and that situation will probably persist through next year. At the moment, the Kentz Corp. operations, which SNC bought last year for \$2.1 billion, are carrying the team.

Should you buy?

SNC-Lavalin has been volatile in the past few years, but the upside potential is huge, especially if the RCMP charge gets sorted out in a positive way. The company is doing a good job of reducing costs and the cycle will eventually turn in both mining and energy.

With so much value tied up in the 407 highway and cash, it wouldn't be a surprise to see a takeover offer by a deep-pocketed suitor. At this point, the long-term opportunity probably outweighs the short-term risk.

CATEGORY

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1. TSX:ATRL (SNC-Lavalin Group)

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