SNC-Lavalin Group Inc.: a Value Play With Dividend Growth

Description

Sometimes, value investors get a chance to buy an oversold stock that is also a dividend-growth play.

That's the situation with **SNC-Lavalin Group Inc.** (TSX:SNC) right now, and a number of contrarians are looking at the numbers and wondering how the stock could be trading at such a discount.

Dark days

The answer lies in the ongoing fraud and corruption troubles connected to a series of dodgy deals; the most damaging being those connected to the former regime in Libya. All of the company's employees connected to the issue have left the company and SNC thought it had finally put the problems behind it.

Then, the story took another turn.

Earlier this year, the RCMP filed charges against the company that could lead to a 10-year ban on bidding for contracts with the Government of Canada. SNC-Lavalin is an important player in the Canadian infrastructure space and a ban would certainly hurt the company and its shareholders.

When the news first broke back in February, SNC's shares took a nosedive, but most of those losses have been erased and the market is starting to realize that a ban might not be in the cards.

New contracts

SNC and its partners just won a long-term contract to build, operate, and maintain Montreal's new Champlain Bridge. According to various reports, the contract is worth anywhere from $2.5 billion to $5 billion and runs 35 years. SNC is a 50% partner in the project.

This week, SNC won another bid to manage Atomic Energy of Canada Limited's Canadian nuclear laboratories. The Government of Canada will finalize the contract over the next few months.

These deals don't guarantee the company won't be found guilty of the charges, but the fact that SNC got the green light on two important projects at such a precarious time suggests a ban might not be the end result of the process.

Earnings strength, dividend growth, and share buybacks

The company is doing a good job of staying focused on reducing expenses and delivering earnings growth in a difficult market.

SNC reported higher year-over-year Q1 earnings of $0.68 per share, a 10% increase compared with Q1 2014.

The company pays a dividend of $1 per share that yields about 2.3%. Despite all the scandals, SNC has managed to increase the payout by 47% over the past five years and management recently announced plans to repurchase up to 10% of the outstanding shares.

Value play

The company currently trades at just 1.8 times book value compared with its five-year average of 3.9 times.

SNC plans to sell its holdings in Toronto’s 407 Highway. Estimates put the value of SNC’s stake in the toll-road at $3 billion, which translates into about $20 per share of the company’s value.

SNC finished Q1 with $2 billion in cash and short-term investments. Long-term debt at the end of the quarter was just $865 million. The difference of $1.135 billion translates into another $7.50 per share.

The company reported a revenue backlog of $11.6 billion at the end of Q1. This doesn’t include SNC’s share of the new deals announced in the second quarter, which probably puts the total close to $13 billion.

At the current share price of $42.50, investors are only paying about $15 per share for the project portfolio and the rest of the company’s operations.

Another way to look at it would be a price of 10 times a very conservative estimate for adjusted earnings of $1.50 per share in 2015.

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aswalker