Are These 3 Cheap Value Stocks too Good to Be True?

Description

As a value investor, I spend a lot of time cruising the 52-week low lists to find companies that are trading at low levels. But just because a stock is trading at a depressed price doesn't mean it's a buy. On the contrary, most beaten-down stocks are that way for a very good reason. The value investor must differentiate between stocks that can recover and stocks that might be headed for bankruptcy.

How can someone do that? It's complicated, obviously, but one way is to look at the balance sheet. A stock that's sitting on lots of cash with no debt is a much better turnaround candidate than one that needs to pay back millions in interest and debt repayment.

There are other factors in play too, including the viability of the company's business over the long term, the quality of management, and the magnitude of the problems. Investors must look past the numbers to see whether a company is capable of turning around, or whether there are deeper problems.

Let's take a closer look at three cheap turnaround candidates and see if they're on the verge of shooting higher or doomed to suffer a slow and painful death.

Reitmans

Reitmans (Canada) Limited (TSX:RET.A) is one of Canada's largest retailers of women's fashion under the Reitmans, Addition Elle, Thyme Maternity, RW & CO, and Penningtons's banners. Shares have been hurt from increased competition, the weakness in the Canadian dollar, and from some less than stellar operating results posted lately. Since 2010, shares are down more than 65%, excluding dividends.

But Reitmans is primed for a turnaround. The company has outlasted many of its competitors, including one of the biggest, **Target** Canada. Present management has been in charge since the 1970s, and the company is focusing on beefing up its online shopping selection. And it has been closing underperforming stores for years, finally improving on worsening same-store sales that have plagued the company for years.

Financially, Reitmans is in fine shape. It's sitting on more than $120 million in cash, and has barely any debt to the balance sheet. It also trades at just 11.5 times it's most recent free cash flow, and would only trade at just over 15 times earnings if we stripped out the massive cash pile.

I think Reitmans has great potential to recover, and that's why I hold it in my portfolio.

Bombardier

Shares of beleaguered **Bombardier Inc.** (TSX:BBD.B) are currently sitting at 10-year lows as investors are punishing the company for its terrible execution on the CSeries line of regional jets. Deliveries have been pushed back twice now, with expectations that they'll start sometime in 2016.

But the rest of the company isn't in such bad shape. The transportation division continues to be profitable, so management plans to spin off a portion of it to raise cash. If you combine that with the $5.3 billion in cash already on the balance sheet, that should be enough to take it through this rough patch.

The issue with Bombardier continues to be the debt. The company currently owes creditors some $9.5 billion, including the preferred shares. That's a lot, especially considering the projected cash burn coming up over the next couple of years.

Although Bombardier is cheap by many metrics, I just can't add a company with that much debt to my portfolio.

IGM Financial

Even though it's the parent company of Investors Group, one of Canada's largest and most respected wealth managers, **IGM Financial Inc.** (TSX:IGM) still trades at a bargain price. Shares currently have a price-to-earnings ratio of just 13.3, and shares yield an eye-popping 5.6%.

The issue is upcoming changes to Canada's mutual funds. New disclosure rules going into place in 2016 mean that investment advisors must disclose a dollar amount in annual fees rather than just a percentage. Skittish investors are scared that this will send droves of people out of mutual funds and into cheaper ETFs.

Although the sell-off in shares is probably overdone, I think investors should take a wait and see attitude with IGM. Cheap shares can always get cheaper, especially when much of the company's assets are intangible in nature. If earnings take a hit, shares will fall even further.

CATEGORY

1. Investing

TICKERS GLOBAL

1. TSX:BBD.B (Bombardier)
2. TSX:IGM (IGM Financial Inc.)

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