On Sale! Buy General Motors Company for Substantial Capital Gains

Description

From a high of US$39, **General Motors Company** (TSX:GMM.U)(NYSE:GM) has dropped to US$33, a decline of 15%. It now yields an attractive 4.4% that's supported by earnings. The company is reporting its third-quarter earnings results on October 21. Should you buy the automaker today? First, let's take a look at its business.

The business

Under its umbrella, General Motors has 11 brands: Chevrolet, Buick, GMC, Cadillac, Opel, Vauxhall, Holden, Autobaojun, Wuling, and Faw Jiefang. In 2014 it was a market leader in the United States with roughly 18% of market share.

Sales growth and earnings growth

September marked the automaker's sixth consecutive month of increased retail market share year over year. Its earnings could also grow at a double-digit rate for the next two years partly due to low oil prices and the growing number of aging cars. For example, at the end of 2014 the average age of a car in the United States was over 11 years old.

Valuation

Currently, at US$33 per share, General Motors is priced at a price-to-earnings ratio (P/E) under eight. That's very cheap for a company of its size; it has a market cap of US$52.4 billion.

Since General Motors was reborn after its bankruptcy in 2009, it has normally traded at a P/E of 10.8. So, its shares have the potential to hit at least US$49 per share, indicating it has a margin of safety of over 32%. If General Motors's price gets back to US$49, that would imply a return of 48% in addition to the 4.4% dividend.

Dividend safety

General Motors's 2014 annual payout was US$1.20 per share. The payout ratio based on earnings was 58.2%. Another way to check dividend safety is to use free cash flow (FCF). After subtracting capital spending from its operating cash flow, is GM's FCF enough to cover its dividends?

In 2014 General Motors generated close to US$3 billion of FCF. The payout ratio was 68.2% based on its generated FCF. Assuming its quarterly dividend remains at 36 cents per share in December, its annual payout for this year would be US$1.38 per share.

Based on its trailing 12-month FCF, there is an increase from 2014; its 2015 payout ratio is 70.7%. Based on the more strict metric of the payout ratio based on FCF, the automaker is still able to cover its dividends.

In conclusion

General Motors is a cheap stock priced at P/E under eight. It has the potential to deliver substantial capital gains of 48-75% in the next few years, with a safe 4.4% dividend to wait. That said, because it's in the consumer discretionary sector, investors shouldn't bet the farm on it, but instead should view it as a potential for substantial capital appreciation.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. NYSE:GM (General Motors Company)

Category

1. Dividend Stocks
2. Investing

Date
2025/08/27
Date Created
2015/10/14
Author
kayng