How Has Maple Leaf Foods Inc. Beat the Market Every Year Since 2011?

Description

Maple Leaf Foods Inc. (TSX:MFI) is the largest protein supplier in Canada, producing processed foods made of pork, poultry, beef and more. Headquartered in Toronto, it has operations in Canada, the U.S., Mexico, the U.K. and Asia. Despite have a market cap of over $3 billion, few have noticed the company's outperformance over the past five years; shares have risen 90.1% versus the TSX's decline of 8.9%.

What's led the Maple Leaf's impressive returns, and can it continue?

A turnaround worth envying

In 2010 Maple Leaf engaged in a transformational turnaround, something that was very necessary given that its shares massively underperformed the market from 2005 to 2010. The transformation included the sale of non-core businesses and the upgrade of its entire manufacturing line; it invested $820 million in modern, high-efficiency plants. It also spent over $100 million in new information technology systems that would lower costs in nearly every segment of the business.

As late as 2013, the company was earning negative EBITDA margins. Investing nearly $1 billion into reviving a money-losing business is always a risk. For Maple Leaf, it was a risk worth taking. This year EBITDA margins turned starkly positive, reaching 7.1% last quarter. While the company has benefited from overall industry dynamics (such as higher-selling margins), the turnaround has largely been fueled by lower costs and more efficient plants.

Aren't shares expensive now?

After executing a solid turnaround, is all the easy money already made? Possibly, but that doesn't mean that the shares don't have further potential. Management is targeting 10% EBITDA margins over the next couple of years and this represents a sizable opportunity still to come.

If the company's historical performance is any indication, it seems more likely that Maple Leaf can pull it off.

"They have definitely turned the corner," says Bob Gibson, an analyst at Octagon Capital. "Everything is in place: They have shut down the old plants, they have got the new plant and they have to get it running smoothly and efficiently. There is significantly less cost, the machines are faster, there is less labour, and it's a lot cheaper to manufacture the various products."

Maple Leaf's CEO is also the largest shareholder, so he is highly incentivized to make this become a reality.

This year, the company is expected to earn $1.10 a share, implying a current valuation of 20.4 times earnings. While this certainly isn't cheap, keep in mind that profits should double this year from only $0.55 a share in 2015. For a company that is growing earnings at a rapid pace, its valuation isn't all that crazy. As long as Maple Leaf keeps executing, there's money to be made.

CATEGORY

1. Investing

TICKERS GLOBAL

1. TSX:MFI (Maple Leaf Foods Inc.)

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