The Smart Money Is Buying Just Energy Group Inc.: Should You Buy, Too?

Description

It can be tough for many investors to choose stocks to invest in.

There are seemingly a million choices out there. For those of us without the analytical skills of a hedge fund manager, sifting through the potential investment opportunities can be daunting. Should an investor focus on value stocks, growth stocks, or a combination of the two? Should valuation matter, or is it the quality of the company? And are dividends really as important as the experts say?

As a response to this overload, many investors choose not to bother analyzing their own investments. Instead, they find a super investor who has great results and simply copy the guru's picks.

While there are certain downfalls to this strategy–an investor should always know what they own–I see no reason why borrowing ideas from billionaires is something that should be discouraged. At the very minimum, it can be a good idea generator. If one (or more) billionaires have invested in something, they might be on to something.

Just Energy Group Inc. (TSX:JE)(NYSE:JE) has not only one billionaire as a major investor, but two. Is that enough reason to buy this controversial company?

The smart money

Jim Pattison is ranked among Canada's richest men with a fortune that's estimated at US$6.6 billion. His privately held company is stuffed with business that are easy to understand like grocery stores, car dealerships, and advertising.

Among Pattison's holdings are more than 25 million Just Energy shares, a stake worth nearly $200 million.

Billionaire Ron Joyce might not be as well known as Pattison, but he's an investing behemoth in his own right. Joyce, who made his fortune growing Tim Hortons into the fast-food monster of today, owns 18.7 million Just Energy shares. Joyce's stake is worth just shy of $150 million at today's price.

The two billionaires own a combined 29% of the company, and both have representatives on the board.

Should you buy?

Like I mentioned earlier, investors shouldn't blindly follow billionaires into a stock unless they do their own research first.

There's just one big issue with Just Energy.

The company buys electricity (and in some jurisdictions, natural gas) from suppliers to resell to consumers. It does so in a variety of ways, including setting up booths at various locales and using door-to-door sales. The latter method already alienates some potential customers.

Because its door-to-door sales reps are compensated using commission, some of them use unsavoury tactics in order to try to get a sale. Some outright lie, while others simply stretch the truth a little. Thousands of consumers have complained about these mistruths. Websites dedicated to consumer issues are filled with complaints about the company.

But perhaps those arguments are overdone. Firstly, certain customers might have expectations that are simply too high. Many complaints are just sour grapes from customers who locked into fixed electricity rates at the wrong time. And finally, people love to complain about the cost of their utilities–myself included.

More than half of Just Energy's customers are businesses for one very important reason: a business that uses a lot of electricity has one objective–cost certainty. Just Energy allows businesses to accomplish just that.

Valuation and dividend

Just Energy doesn't have a great dividend history.

In the last five years alone, the company has cut its dividend twice. It started out paying $0.1033 per share each month in 2011, shortly after it converted from an income trust. It cut the payout to $0.07 per month in 2013, and then slashed it again a year later to $0.125 per quarter. In all, that's a cut of more than 60%.

The good news is the new dividend appears to be safe. The company generated approximately $112 million in free cash flow over the last nine months, while paying out just $56 million in dividends. That's a nice payout ratio for a company that has a 6.4% yield.

It's also cheap on an earnings basis. Over the last 12 months, the company has generated $148 million in free cash flow, giving it a price-to-free cash flow ratio of just 7.8, one of the lowest on the TSX.

Just Energy has ample free cash flow, a healthy dividend, and trades at a cheap valuation. Perhaps it's time investors follow Pattison and Joyce into this misunderstood name.

CATEGORY

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