



Transcontinental Inc.: An Income Investor's Dream Stock

Description

The **iShares S&P/TSX 60 Index Fund** ([TSX:XIU](#)) currently yields 2.91%. That's based on the average yield of the 60 stocks that make up the index. It's not a bad return if you don't need the income. However, for those of you who need more from your dividend stocks, here are three reasons why **Transcontinental Inc.** ([TSX:TCL.A](#)) is an income investor's dream stock.

Dividend yield

There are 25 stocks in the S&P/TSX 60 Index whose current dividend yield is 3% or higher. As an income investor, you could buy all 25 in order to jump start your income generation. Even better, simply aim higher by purchasing only those paying 4% or more. That narrows your purchases to 15—a more manageable amount indeed. And since all are big companies with reasonable profits, your level of risk is relatively low.

One name that's not on this list is Transcontinental, Canada's largest printer as well as the third-largest in North America. And while most people view printing in a similar vane as the horse and buggy, Transcontinental investors have done pretty well over the past five years; its stock has delivered an annualized total return of 8.3%, 658 basis points higher than the S&P/TSX 60.

It pays a quarterly dividend of 18.5 cents and yields 4.2% as of the June 23rd close. That would put it in a special group if it was included in the S&P/TSX 60. However, it is one of the 248 components in the S&P/TSX Composite Index. With the exception of **Bank of Nova Scotia** and **BCE Inc.**, whose stocks are currently yielding 4.5% and 4.4%, respectively, Transcontinental's yield is better than the other eight companies in the composite index's top 10 holdings.

Free cash flow

While it's one thing to boast about Transcontinental's 4.2% yield, the skeptical investor is sure to criticize the company's business model; while its dividend might be 4.2% today, a nearly 15% Canadian market share in an obsolete business is sure to result in dividend cuts down the road as its business begins to choke on itself.

That's one way to look at it. Here's another.

Its free cash flow for the trailing 12 months ended April 30 was \$252 million—a free cash flow yield of 18.4%. Put another way, for every dollar it spends on capital expenditures, it generates \$2.96 in free cash, which it can reinvest in the business to pay down debt, to acquire other businesses, or to grow organically. It can also increase its dividend payout and repurchase its shares.

Good businesses know how to allocate capital. For my money, I'll invest in a good business that allocates capital well before I'll invest in a supposedly great business that doesn't. Since fiscal 2007 Transcontinental has generated \$1.1 billion in free cash flow, which has resulted in \$460 million in dividends, share repurchases of \$141 million, and \$675 million in acquisitions. Including capex, it's deployed \$2.1 billion of capital to create shareholder value, and a lot of the benefits have only been realized over the past five years.

Without that free cash, it either would have had to borrow the money to make this happen, issue more stock, or simply not reward shareholders; none of which would be popular with investors.

Family values

If you don't like companies that employ a dual-class structure, Transcontinental is definitely not for you. The Marcoux family control 73% of the votes backed by a 17% economic interest. Remi Marcoux, who still sits on the board, acquired a small printer 40 years ago along with two other partners, taking the company from less than \$3 million in annual revenue to in excess of \$2 billion.

His son-in-law, Francois Olivier, took over from the founder as CEO in 2008 after the senior Marcoux put a succession plan into place four years earlier that allowed for a smooth and successful transition. Since Olivier's been in the top job, Transcontinental's stock's achieved a cumulative total return of 52.5%, 23 percentage points greater than the XIU.

Results, as far as I'm concerned, are all that matters. As Al Davis, the former owner of the Oakland Raiders always said, "Just win, baby." Transcontinental does that in spades.

If you're an income investor, there are a lot worse places you can put your money. In many ways, it's an income investor's dream stock.

CATEGORY

1. Investing

TICKERS GLOBAL

1. TSX:TCL.A (Transcontinental Inc.)

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