



Chow Down on Maple Leaf Foods Inc.

Description

Maple Leaf Foods Inc. ([TSX:MFI](#)) recently announced a 70.4% increase in third-quarter profit—a large increase warranting further analysis. We will assess the business fundamentals and take a look at the quality of earnings and the long-term outlook for a value investor.

Sources of profitability

Maple Leaf has engaged in an aggressive earnings-growth campaign, focusing on plant modernization and targeted divestitures. The company began its cost-cutting and modernization efforts in 2010 and has just completed its mandate.

We view the corresponding reduction in capital expenditures (from \$39.4 million to \$29.5 million) and the significant positive earnings growth associated with such endeavours as encouraging for the long-term investor.

Business fundamentals

The company has a diverse portfolio of businesses; however, both top- and bottom-line earnings are driven by the company's meat products business unit. Maple Leaf's meat business has driven the majority of earnings growth with its net income increasing to \$66 million—more than double its 2015 total.

Strong earnings growth is also very encouraging. Company earnings increased from \$0.13 per share last year to \$0.23 per share this year.

The company's net cash position also increased substantially due primarily to increased cash from operations in excess of dividends, capital expenditures, and share repurchases as compared with the previous year.

Maple Leaf's cash position of \$434.4 million provides the long-term investor with a greater margin of safety (as opposed to last year's cash position of \$295.9 million). All ratios measuring the company's liquidity, such as the quick ratio, current ratio, etc., have been further enhanced, and this positive

change in the company's cash position appears to be a long-term "new normal."

Performance incentives a driver of growth?

Another interesting line item on the company's Q3 financial statements is SG&A. The company has reported an increase in SG&A of 14.1% year over year, resulting primarily from short-term incentives programs.

The company's long-term investment/divestment plan coupled with a strong short-term incentivization program could potentially result in an elevated long-term level of profit. We will continue to monitor Maple Leaf stock over the coming quarters to attempt to quantify if a new long-term growth level should be applied to our discounted cash flow analysis of MFI stock.

Overall outlook

Moving forward, we see Maple Leaf as a great pick for a long-term investor looking for exposure to Canadian manufacturing and Canadian exchange rates. We expect strong earnings growth and continued profitability in the medium term.

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