Getting In on the Resource Recovery, Dividends Included!

Description

As Canadian investors, we are aware of a number of fantastic companies trading on the Toronto Stock Exchange which are priced in Canadian dollars. Looking south of the border, however, stocks are priced in U.S. dollars, which presents another variable: foreign exchange.

Although one of my favourite U.S.-traded stocks is **Caterpillar Inc.** (NYSE:CAT), which is traded in U.S. dollars, not every investor is willing to follow me into a U.S.-denominated security. Enter the Canadian alternative: **Finning International Inc.** (TSX:FTT). Currently trading at a price of approximately $26.50 per share, the dividend yield is almost 2.75% and there is potential for capital appreciation.

The company, which operates Caterpillar equipment dealerships across Canada, is a major player in the industrial, mining, forestry, and construction industries. Uniquely positioned in a country with a significant amount of resources in the ground, Finning would trade at a price earnings (P/E) multiple of 62 times after we remove the one-time items. Although this may be viewed by some as a very high multiple, let's not forget two things.

The first thing to remember is Caterpillar has also experienced a significant write-down and loss in the past year. Further, the company also traded at a P/E in excess of 50 times in the past six months.

The second thing to remember is, cyclical companies such as these are typically bought at times when there is a significant decline in profit and the multiples are in nose-bleed territory. The stock market is clearly pricing in a return to profitability in the near future.

As is the case with most cyclical businesses, investors must try to answer this question: what did management do during the company's darkest hours?

In the case of Finning, management undertook a share buyback during fiscal 2015, retiring a small amount of stock and potentially paving the way for a dividend increase in the coming quarters. The company has been very good at consistently raising the dividend over time. The dividends paid were $0.55 in 2012, $0.60 in 2013, $0.69 in 2014, and $0.72 in 2015. Currently, the company is on pace to pay $0.72 in dividends in 2016, but when earnings for the fourth quarter are reported, management may surprise us.

From 2012 to 2015, the compounded annual growth rate of the dividend was 9.4%. While this is an excellent number, investors have also experienced an increase in the dividend-payout ratio in recent years. What was previously close to a 30% dividend-payout ratio has increased to over 100% in recent years. Although this could be a problem over the long term, the company has clearly shown the potential to be profitable and has enough cash on the balance sheet to cover at least one year’s dividends in addition to a significant amount of accounts receivable.

Looking at Finning as a long-term investment, it will be difficult for investors to be disappointed over the long term. With the hopes of seeing a growing dividend and a pickup in earnings, this name is at the top of my watch list for 2017.

CATEGORY

1. Dividend Stocks
2. Investing

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1. NYSE:CAT (Caterpillar)
2. TSX:FTT (Finning International Inc.)

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Date
2025/06/29
Date Created
2017/02/06
Author
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