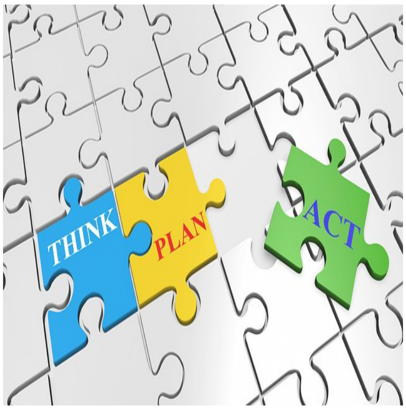

Fundamentals, Valuation Show Badger Daylighting Ltd. Remains Overvalued

Description

In determining whether or not a company is overvalued or oversold, an investor should take a look at a wide range of factors to come to a determination. When a company such as **Badger Daylighting Ltd.** (TSX:BAD) experiences a drop of nearly 35% in fewer than two months, investors should be asking if the selling is warranted, or if this is a case of the bears getting the better of the bulls.

I'm going to dive into a few key fundamentals and valuation-based drivers of the decline in Badger's stock price, irrespective of the current short attack on Badger from high-profile short-seller Marc Cohodes.

Fundamentals

On a fundamental basis, we can see that Badger's profitability has actually been declining for some time.

Since 2014, the company's EBITDA, net income, earnings per share (EPS), and a number of other key fundamental metrics have been deteriorating at a similar rate across the board.

Specifically concerning to me are the company's return on equity (ROE) and return on invested capital (ROIC) ratios, which measure the company's ability generate value for shareholders and the company's ability to generate returns on the existing capital within the business (a pretty good overall measure of relative operating performance), respectively. The numbers are below and speak for themselves.

	2011	2012	2013	2014	2015	2016
ROE	30.7%	24.5%	26.0%	26.9%	15.7%	10.6%
ROIC	21.0%	18.9%	19.6%	19.0%	12.2%	8.5%

Valuation

While Badger's profitability and other key fundamentals have been deteriorating for the past few years, we can see that the company's valuation metrics have simply picked up the slack during this period of depressed fundamentals with investors ascribing a higher premium to Badger than the S&P/TSX Index.

The company's current price-to-equity (P/E) ratio, price-to-book (P/BV) ratio, price-to-sales (P/S) ratio, and price-to-cash flow (P/CF) ratio are all substantially higher than the industry average. Most are higher than the company's own historical average and higher than the company's peers.

We can also see that these key ratios began to increase around the same time as profitability began to decline, suggesting that the company's stock price has remained relatively inelastic with respect to the company's performance (this is a big red flag for a long-term investor such as myself).

With a short attack currently underway, I remain flabbergasted as to how Badger's valuation metrics remain elevated at current levels.

Bottom line

If we ignore the noise on this stock and look purely at the numbers, it is clear from a valuation standpoint that Badger's current stock price is elevated at best and grossly inflated at worst. With a business model built on technology and processes that are hard to insulate from competition, resulting in a business with a rather small moat in an industry with deteriorating margins, I remain very cautious with this name and would encourage investors or potential investors to dig in to Badger's numbers further.

Stay Foolish, my friends.

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1. Investing

Date
2025/08/18
Date Created
2017/06/13
Author
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