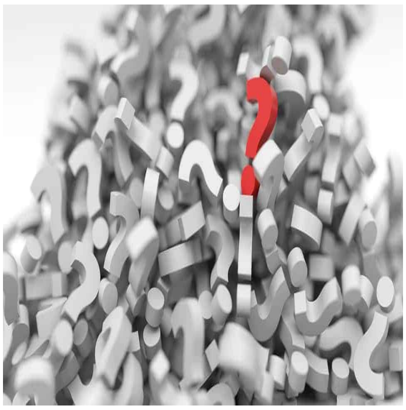

Power Corporation of Canada: Opportunity or Value Trap?

Description

Power Corporation of Canada (TSX:POW) is a diversified international management and holding company with interests in financial services, communications, and other businesses.

The company has a very enticing 4.71% yield and shares are now down about 6% from the 52-week high. Many income-hungry investors may be considering adding shares of this conglomerate to their portfolios on weakness, but without any real long-term catalysts, Power Corporation could continue to be a laggard when it comes to stock price appreciation.

The company has a healthy balance sheet and a sustainable dividend with a 48.4% payout ratio. The dividend has remained intact even during the Financial Crisis, which the company has yet to recover from.

Power Corporation is a huge web of subsidiary businesses, and it can be easy to lose track of what you're actually investing in. So, let's take a look at what you get with an investment in Power Corporation.

An indirect bet on the sale of high-fee mutual funds

The company has a 65.6% stake in **Power Financial Corp.** (TSX:PWF), which owns **IGM Financial Inc.** (TSX:IGM). Power Financial is a financial services company which profits from selling high-fee mutual funds through its subsidiaries.

As you may be aware, high-fee mutual funds are going out of favour, and for good reason. Although an advisor may tell you 2.5% MERs are "not much," over the long term, these fees quickly add up. The next thing you know, your retirement could be in jeopardy thanks to the ridiculously high management fees that IGM's subsidiaries charge its clients.

With the rise in popularity of ETFs and low-fee index funds, I believe there is no more room to make easy profits from the sale of high-fee mutual funds. Such funds claim to outperform the market by a substantial amount of a consistent basis, yet many fail to live up to expectations, and many actuallyend up doing worse than the market.

A venture investment in robo-advisors?

Power Corporation’s venture capital fund, Portag3 has been investing in FinTech start-ups as a hedge against the downfall of mutual fund sales. Protag3 invested about $100 million in the robo-advisor Wealthsimple, which uses algorithms to give financial advice.

While such investments sound promising, I believe the initiative is just a drop in the ocean. IGM Financial is going to continue to suffer major headwinds from the downfall of mutual funds, and I don’t think the “if you can’t beat them, join them” strategy is going to work out in the end.

What else is under the Power Corporation umbrella?

In addition to Power Financial, the company also owns a stake in communications businesses and many international firms across various different industries. Although such businesses may be attractive, I don’t believe they offset the headwinds caused by Power Corporation’s stake in IGM Financial.

Bottom line

IGM Financial is just a chunk of what you get with an investment in Power Corporation, but I think it’s enough to avoid the company, no matter how cheap it is. While the company’s investment in Wealthsimple is an intriguing play on FinTech, I believe the deal will do absolutely nothing to offset IGM Financial’s incoming headwinds. There are much better options out there if a high yield is what you’re after.

Stay smart. Stay hungry. Stay Foolish.

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