Why Canfor Corporation May Be Immune to Macroeconomic Events

Description

Canada's largest forest products company **Canfor Corporation** (TSX:CFP) has been on a fantastic ride of late. The company's share price has appreciated nearly 25% year to date.

The business has largely weathered concerns about U.S. countervailing and anti-dumping duties and has seen share price appreciation of late, despite the Bank of Canada indicating it would raise interest rates — a move that should have severely impacted the share price of Canfor.

I'm going to discuss potential reasons why the share price of Canfor has not moved as expected to the recent news and shed some light on what investors may expect over the medium term, as economic conditions continue to change over time.

Anti-dumping and countervailing duties seemingly have no impact on Canfor

The fact that the U.S.-imposed anti-dumping and countervailing duties have not had a significant effect of Canfor's stock price should not surprise investors.

The Canadian government has made it clear that Canfor happens to fall into one of the protected Canadian industries which will receive government support via loan guarantees or potential bailout funds any time it is challenged by international scrutiny.

Other industries, such as the Canadian dairy industry and aerospace manufacturing industries, have received substantial government support, and the softwood lumber industry is no exception.

Interest rate hikes seemingly have no impact on Canfor

The latest concern that has seemingly not phased the company's stock price is interest rate hikes. The largest export market for Canfor remains the U.S. market.

With the Canadian dollar being so weak of late, Canfor's profitability has jumped in recent quarters, and investors have largely cheered this profitability by buying more shares.

With the Canadian dollar appreciating significantly against its U.S. counterpart ahead of expected rate hikes today, it stands to reason that should the Bank of Canada indeed follow through and raise interest rates, and the Canadian dollar appreciates more and maintains a higher level (many analysts believe an $0.80 dollar is not out of the question in the near term), Canfor’s profitability could be significantly impacted over the coming quarters.

The potential currency exchange impact on Canfor’s profitability has mysteriously had no impact on the company’s share price, with CFP shares trading at a 6% discount to their 52-week high.

Canfor stock is not as liquid as many investors think

Jim Pattison is Canfor’s largest shareholder, owning nearly 60 million shares out of 132 million outstanding shares. He has been vocal about purchasing additional shares over the most recent quarters.

When a few shareholders can continue to buy shares of a firm in such a way that the total float outside the top two or three shareholders is diminished to a level where any shares sold will be immediately snapped up by the company’s largest shareholders, share float pool liquidity can become an issue.

Bottom line

The only explanation for the lack of elasticity with respect to Canfor’s stock price and the clear, unambiguous negative macroeconomic changes of late is that Canfor’s largest shareholders and the Canadian government, by way of loan guarantees, are not interested in seeing Canfor’s stock price trade lower.

On a fundamental basis, factoring in these changes, Canfor remains overvalued, and I would expect (in a well-functioning market) that a softening of the stock price over the medium term would be in order.

Stay Foolish, my friends.

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Date
2025/06/30
Date Created
2017/07/12
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