Does Saputo Inc.'s Strong Balance Sheet Make it a Buy?

Description

Shares of **Saputo Inc.** (TSX:SAP) have been on an interesting ride of late, decreasing approximately 18% from their all-time high set earlier this year. On this dip, investors have come to assess what the growth prospects of the Canadian dairy company are moving forward. Any time a company loses close to one-fifth of its value, the company's shares deserve another look.

I'm going to discuss how Saputo has performed over the long run and what the company's prospects look like moving forward.

Fundamentals

From a fundamentals standpoint, Saputo stands out among the crowd, with a very strong balance sheet compared to its peers. While the company maintains very small margins (representative of the dairy industry), Saputo's return on equity and return on invested capital remain substantial at 17.5% and 13%, respectively.

The dairy producer has a modest dividend-payout ratio of 32% supporting a dividend yield of 1.5% and has grown free cash flow on a compounded annual growth rate of 14.8%. Saputo's modest debt levels are supported by an interest coverage ratio of 29 with the company's debt level staying relatively stable and manageable over time.

Long-term prospects

Saputo is one of the largest dairy companies in Canada and remains profitable due in part to the company's membership in an elite oligopoly of companies which control the vast majority of the dairy products consumed by Canadians and Americans. Along with Agropur Cooperative and Kraft Canada, Saputo rounds out three companies which control more than 70% of Canada's milk production.

In the U.S. market, Saputo is the second-largest dairy producer in the country, and the U.S. market currently accounts for about one-third of Saputo's revenues. With the Canadian dairy industry increasingly under scrutiny by the Trump administration and other governments around the world, Saputo remains uniquely tied to the political ability of Canada to maintain its protectionist supplymanagement system.

Saputo's long-term prospects thus now have some additional level of uncertainty moving forward — something it appears investors have begun to price into SAP stock of late.

Bottom line

From a balance sheet perspective, Saputo remains strong. I would encourage investors who'd managed to load up on Saputo shares years ago to hold on to these equities and avoid paying taxes, as it remains difficult to find any sort of undervalued securities in today's stock market.

For investors considering initiating a long-term position in Saputo, I would suggest doing an analysis of what the catalysts would be for Saputo to outperform in the long run, factoring in macroeconomic risks and uncertainties accordingly.

Stay Foolish, my friends.

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