3rd-Time Lucky for Transcontinental Inc.

Description

It's been a while since I've written about **Transcontinental Inc.** (TSX:TCL.A).

It's not my favourite stock by any means, but it is one I've recommended twice since June 2016. A recent stock screen in the *Globe and Mail*, as I was looking for quality North American companies, listed the printing and packaging company among 14 other large-cap stocks, and reminded me about those previous recommendations.

In June 2016, I called Transcontinental an income investors' dream stock. Ten months later, despite being up 38% since my first recommendation, I recommended it again in April 2017. Since then, it's up another 13.3% over five months, considerably better than the TSX.

So, is Transcontinental still worth owning, despite the fact its stock is up 44.5% in the last 12 months, 10 times the TSX?

Dividend yield lower than in the past

When I first recommended Transcontinental, it was yielding 4.2%. Today, 14 months later, that's down to 3.3%. However, if it can deliver anywhere near 44.5% over the next 12 months, I'll gladly take 90 basis points less in yield for all that upside.

As for its third-quarter earnings announced September 7, they were unspectacular but solid, given it is still transforming from media company to a printing and packaging enterprise.

Adjusted operating earnings and revenues increased 11.5% and 2.1% year over year to $68.2 million and $477.7 million, respectively.

"I am proud of what we achieved in the third quarter as we continued to deploy our transformation plan while improving the Corporation's performance," said François Olivier, president and CEO of Transcontinental. "Our enviable financial position and our significant cash flows provide the solid foundations that will allow us to maintain our momentum and invest in our development."

A successful transformation

In April, Transcontinental found a buyer for its Atlantic Canada newspapers — one that already ran Halifax's *Chronicle Herald* newspaper — delivering a win for all shareholders.

A few days after the Atlantic papers were sold, Transcontinental announced that it was looking to divest its 93 local and regional papers and related websites in both Ontario and Quebec. Over the summer, various assets were sold, including papers in Mt. Tremblant, Sainte-Agathe, and Drummondville.

"The process to sell our local newspapers in Quebec and Ontario is thriving," said Olivier in its Q3 2017 press release. "Discussions are continuing with potential acquirers in several regions."

Included in the sale is the Montreal version of *Metro,* a free daily paper well known to commuters in various cities across Canada. It's yet to be sold.

All of the proceeds from this methodical sale of its media assets will go to investing in its flexible packaging business, which, along with Transcontinental's printing business, accounts for 87% of its overall revenue and 96% of its adjusted operating earnings.

With its level of net debt lower than it's been over the past five quarters at $195.4 million and margins higher than they've been for some time, its finances have never been better.

It all comes down to valuation

The fact that it's up almost 50% in the past year means it's bound to be expensive, right? Wrong.

Although some of the usual valuation metrics, such as price to sales and price to cash flow, are higher than they've been in recent years, it still has a free cash flow yield of 11%.

Considering Transcontinental's free cash flow is growing, a significant factor in determining which dividend-paying stocks to own, I like its chances of continuing to balance dividend payouts with capital appreciation.

Let me recommend Transcontinental for the third time in 14 months.

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