Get Rich Slowly With This Undervalued Canadian Gem

Description

As a value investor, a margin of safety is usually the most important trait to look for, then comes potential upside. If you like to take a preservation-of-capital approach to investing, then you probably like looking for beaten-up stocks that trade at a significant discount to their underlying assets. The TSX has been quite the laggard this year, but don't fret; instead, concentrate on capitalizing on long-term buying opportunities.

For most investors, losing money is way more painful than gaining the same amount of money on an investment. Even if a stock soars and surrenders a small chunk of the gains, it can still feel like you've lost money! That's just the way we're wired as humans. Fortunately, as we gain more experience, we'll start to become more disciplined and not think about short-term ups and downs, and instead focus on what matters: the long-term fundamentals of the business.

Here's a beaten-up stock that I believe may offer investors a considerable margin of safety at current levels:

Cara Operations Ltd. (TSX:CARA) is the company behind popular Canadian dine-in restaurants such as Swiss Chalet. Shares are down ~35% from all-time highs thanks to in part to the weakness in the Albertan economy, where Cara has a considerable chunk of its restaurants.

Most of Cara's locations are in Ontario, which has been a pretty strong province, but the Albertan exposure continues to be a drag on the stock. As the energy patch continues its recovery, I think it's likely that Cara's Albertan businesses will gradually become less of a drag on the company's overall results.

Minimum wage hikes are also expected to be a drag on Cara's performance; however, it appears that the downside from such a negative trend has already been baked in to the stock at current levels. The Ontario economy still looks good, and Cara may have the flexibility to increase prices to offset the headwind of higher minimum wage. Alberta, however, will probably experience a further drop in same-store sales if menu items were to increase, so it'll be interesting to see what Cara will do.

Cara is an incredibly cyclical stock due to the dine-in nature of its restaurants. Fast-food restaurants are more defensive, and Cara has a few fast-food businesses, such as St-Hubert Express, but the majority of its restaurants are dine-in and are thus highly sensitive to the economic environments where Cara operates.

Bottom line

Cara currently trades at a 14.98 price-to-earnings multiple, a 2.4 price-to-book multiple, and a 2.2 price-to-sales multiple. The stock is definitely cheap right now, so value investors could stand to benefit over the next few years as the sluggish Albertan economy starts to improve. In the meantime, you can collect a safe 1.71% dividend yield.

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