This High-Quality Stock Is Down 20% Year to Date and Grossly Undervalued: Time to Buy

Description

In recent history, **Badger Daylighting Ltd**. (TSX:BAD) has been negatively affected by its exposure to the oil and gas sector, which represented 50% of total revenues.

So, now that oil prices are closing in on $60, why have Badger's shares declined 20% year to date?

While in the past the company's exposure to oil and gas sector represented 50% of total revenues, it's represented less in more recent quarters, as the oil and gas sector cut back its spending.

Also, the company was, at one point, trading at very rich valuations, and then margins came down a bit, and the stock got hit hard. But this is the opportunity today.

Here is why I think the stock is a very attractive buy at these levels.

Strong revenue growth

In the latest quarter, the third quarter of 2017, Badger reported revenue growth of 24.8% as a result of its U.S. operations, which saw a 36.2% increase in revenue. As a reminder, the U.S. represents 55% of total revenue.

The key here is that the company saw strong demand across geographies and end use markets.

Diversification

The fact that the company's hydrovac excavation services are in demand not only by the oil and gas industry, but also petro-chemical plants, power plants, and other large industrial facilities in North America gives the company good diversification and exposure to different industries.

So, we should not view it as a direct play on the energy sector, although it certainly benefits from the ups and gets hurt in the downs of the energy market. And with the strength in oil prices this year, the company is certainly benefiting.

Strong returns

Badger is a well-run company with a history of high margins and strong returns on equity, and at this point, it represents a good, diversified play in the industrial sector.

And while the company's EBITDA margin has been under pressure lately due to higher selling, general, and administrative expense, coming in at 27.5% this quarter compared to 29.6% last year, management is confident that they will come back up to the 28-29% level.

Attractive valuation

Valuations are much more attractive than recent history, trading at a P/E ratio of 21 times this year's expected earnings and 17.7 times next year's consensus EPS estimate.

Earnings per share increased 37.5% in the quarter to $0.44. And for the year, consensus expectations are calling for EPS of $1.26 compared to $0.78 in 2016 for an increase of 61%.

And since the stock was hit when the energy sector was collapsing, it follows that the shares should rise as the energy sector recovers.

Longer term, management still has a goal of doubling the U.S. business over the next three to five years, as they continue to see opportunities for more uses for the hydrovac as well as geographic expansion.

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