Will This Company Be Privatized in 2018?

Description

The past year was a terrific one for shareholders of **Lassonde Industries Inc.** (TSX:LAS.A), as company shares increased by close to 15%, and the dividend was increased by almost 20%.

In spite of operating in a very defensive business with historically low returns on equity, the company has managed to become a dominant player in the juice market and has remained an attractive investment for quite some time. Over the past five years, the company has seen the share price increase by more than 225%, which translates to a compounded annual growth rate (CAGR) of almost 27% in addition to the dividend yield.

With such a low dividend yield, however, investors need to start asking if and when they will see a substantial increase, as the excess cash flow the company is generating is not being sent to the shareholders. Currently, the yield is no more than a token 1%.

The reason this question must be asked is due to past decisions the company has made in regards to the allocation of capital. In spite of a dividend yield of only 1%, the cost of capital by most analysts is estimated at 10%, as long-term stock market returns have proved this is the right number to use time and again.

With a market capitalization of $810 million and approximately $192 million in debt, the company has paid only $2.1 million to service this debt over the first three quarters of the year (which works out to $2.87 million on an annual basis). With a cost of debt expected to be close to 1.5% on a pre-tax basis for the year, we have to wonder why the company would focus on paying down debt instead of conducting a share buyback or increasing the dividend.

Throughout the first three quarters of 2017, a total of $44 million in debt was retired. For fiscal 2016, the company retired a total of $83 million in debt. Clearly, the priority is to repay debt rather than retire shares that have a cost of 10%.

What makes this company a potential buyout (or privatization) candidate is because more than 90% of the voting shares are controlled by family ownership. Although there are A and B class shares, only the A shares trade on the stock exchange, while the B shares (which do not trade) carry 10 votes for every share (in comparison to one vote for each A share).

Although many may be frowning at the chance that a family-run company with multiple voting shares could be taken private, the truth is that shareholders have had very little to complain about over the past five years, as this investment has delivered exceptionally well for investors. In addition, should any offer be made, shareholders can expect to be treated fairly by management and the potential buyers, which is in line with management's track record.

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Date
2025/07/05
Date Created
2018/01/09
Author
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