Forget $60: This Quebec Stock Is Worth More

Description

BRP Inc. (TSX:DOO) stock is on a roll at the moment, up 21% over the past three months and closing in on $60, an all-time high.

I've been talking up the Quebec manufacturer of recreational products including Ski-Doos, Sea-Doos, Can-Am ATVs and SSVs (side-by-sides) for some time.

Although the products it sells aren't cheap, BRP operates in an industry that's surprisingly resistant to the economy. People just want to blow off steam, which is especially true when the economy isn't doing well. I'm sure there are some who would give up their homes before parting with their off-roaders.

When I first started recommending BRP stock in June 2016, I wasn't nearly as enthusiastic about its potential as I am now. However, I've followed its U.S. competitor, **Polaris Industries Inc.** (NYSE:PII), since before the 2008 market collapse; its stock is up 1,393% since the March 2009 bottom.

There is money to be made in recreational vehicles, and given that young people are drawn to experiences rather than buying a lot of stuff, that's never been truer than it is today.

Think about it.

A lot of millennials believe that they're never going to own a home in the big city. So what will they do? Buy cabins in the middle of nowhere and furnish them with SSVs and Ski-Doos. I'll bet dollars to donuts that that will happen.

How is it worth $75?

Well, it isn't at the moment, but here's how it could reach the triple digits within the next two to three years.

The first and most obvious way is by selling a lot more of its product. To do that, it moved its North American headquarters to Plano, Texas to be closer to its U.S. customers, who can't seem to get enough of the company's SSVs.

“Over little more than a decade, sales momentum in the off-road industry has swung dramatically toward vehicles offering a more collective experience. Lone or double-rider ATV sales are in decline,” wrote *The Globe and Mail's* Nicolas Van Praet on May 23. “Side-by-sides, which can seat as many as six people, are on the rise. The new thrill-craft models are increasingly carlike and cost much more than the older versions, juicing up companies' profits.”

As an aside, if you want to get a little background information about BRP's past, I suggest you read Von Praet's article. It's very informative.

The second thing it needs to do in addition to selling more vehicles is to make more money off each one that it does sell.

Canaccord Genuity Group Inc. analyst Derek Dley is a big believer in BRP. He recently upped its 12-month target to $60 from $57 ahead of first-quarter earnings on May 31.

“We are increasing our target multiple, as we believe BRP deserves to trade at a premium to its peers, which currently trade at 10.5 times,” Dley wrote in a recent note to clients. “We believe the company's fiscal 2021 EPS target of $3.50 is readily achievable, and that the current valuation represents an attractive entry point for what we believe is a healthy medium-term growth profile.”

Earnings projections fall short

Okay, like all analysts, he's not ready to jump into the deep end of the pool just yet, but let's assume that BRP is right and that its $3.50 estimate is bang on the money. At $75 a share, BRP would be trading at 21 times earnings, higher than any premium that Dley might consider reasonable.

However, if you look at the consensus estimate for the 13 analysts covering its stock, they see $2.78 EPS in 2018, $3.18 in 2019, and $3.51 in 2020, thereby hitting the $3.50 target a year ahead of the company's projections.

Let's assume the analysts are correct. That would mean EPS growth of 14.4% and 10.0% over the next two years. Another 10% growth in 2021 would bring the number to $3.86 a share, a multiple of 19 times earnings. That's still too large a premium.

The bottom line on getting to $75

So, to get to $75 or higher, I'm suggesting that BRP grow its earnings per share to $5 by 2021, an annual growth rate of 22%, which is considerably higher than its current growth rate.

By growing its earnings faster than expected along with a multiple of 15 times earnings, it can get to $75.

It won't be easy, but it's definitely doable. And May 31 will tell us just how doable.

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Date
2025/08/30
Date Created
2018/05/28
Author
washworth