Can You Become Rich as a Deep-Value Investor?

Description

There's value investing, and then there's deep-value investing.

Although the two strategies may seem similar on the surface, the latter approach requires a greater degree of patience, discipline, and conviction. Frequently, deep-value investing involves taking a bet in a severely beaten-up stock that may not have seen a sustained rally in many years.

Although such names may seem like they possess attractive margins of safety, significant due diligence is required since there are a lot of value traps out there that are disguised as deep-value plays, and some investors are insistent on bottom-fishing with the lack of a sound long-term thesis.

Even if you don't have a value trap on your hands, you need to be comfortable with waiting for many years for a rebound to come to fruition.

Deep-value plays are typically ridiculously cheap, but they're cheap for a reason, and a lot of the time that reason is due to immense headwinds that have gotten the better of them. In some cases, a secular decline may be to blame for a stock's implosion, and if this is the case, investors ought to exercise extreme caution, because secular downturns are a tough ship to turn around.

You probably don't want to place a bet on a reversion of a secular downtrend, unless you've got an extremely sound thesis that you're willing to bet on. And if it turns out you were wrong, you'll probably end up going down with the ship. Case in point: **Corus Entertainment Inc.** (TSX:CJR.B).

Thus, deep-value investors who desire incredibly cheap stocks ought to avoid "cigar-butt" stocks by avoiding ships that are too large to turn around. Some ships are more natural to turn around than others, especially if there's a sound turnaround plan. Deep-value investors need to do exert all of their efforts in the homework before initiating a sizable position. After that comes the hardest part: waiting for the turnaround plan to come to fruition.

A lot of the time, a management's turnaround plan may take an exorbitant amount of time to affect the stock, so you not only need conviction and discipline to ride the rough waters, but you'll also need the time for your ship to get back to shore.

Think **Empire Companies Ltd.** (TSX:EMP.A), a grocer that was troubled by a complicated mess of operational inefficiencies that ultimately led the stock to lose over half of its value over the course of two years. After Michael Medline was hired as CEO, things started looking brighter, and the stock had rallied 72% from its bottom in about a year and a half. Medline's "Project Sunrise" allowed the company to see the light of day again, and if you were patient enough to average down during tough times, you would have profited profoundly once the Empire finally struck back!

What are some potential deep-value plays that exist today?

Cameco Corp. (TSX:CCO)(NYSE:CCJ), a uranium producer, is a dirt-cheap play that's been in the doghouse for many years. Over the next few years, several nations have shown interest in turning nuclear power plants back on, and that could finally bring uranium prices and Cameco stock out of their nuclear winters. It's an untimely play, and you'll probably be waiting a while before you'll reap significant rewards.

Foolish takeaway

If you've got what it takes to be a deep-value investor, you can make a great deal, but it's essential that you get the long-term story right. While timing your entry isn't critical, any flaws in your thesis could end up with you wasting your principal and years of waiting for a bounce that will never end up happening.

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2. TSX:CCO (Cameco Corporation)
3. TSX:CJR.B (Corus Entertainment Inc.)
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