Now’s the Time to Ride This Financial Services Outlier

Description

Over the past week, I’ve been covering TSX stocks that are down more than 20% over the past year or year to date.

AGF Management (TSX:AGF.B), an asset management stock I’ve recommended in the past, is one of those poor performers. Trading around $5.50 as I write this, I believe that AGF’s stock is always a buy whenever it gets into oversold territory below $6.

Here’s why it’s time to ride this financial services outlier.

Profits are good

A quick look at AGF’s third-quarter earnings shows a number of positive results. Assets under management grew 11% to $38.8 billion. The S&P/TSX Composite Index’s total return over the past year grew 9.6%, which suggests its active managers didn’t do a horrible job of growing the assets.

Year-to-date net mutual fund sales were $23 million, well ahead of the $266 million net redemptions in the first nine months of 2017. Excluding institutional sales and redemptions, net sales year to date were $73 million.

It doesn’t matter how good a money manager you are if you don’t have assets to manage, so net sales, as opposed to net redemptions, is a very good thing.

During the months of June, July, and August, AGF repurchased 385,400 of its shares at an average price of $6.74. That might seem like a losing proposition given its shares are now trading well below $6.

However, during that 90-day period, its shares traded above $6.50 for at least 50-60% of the time, suggesting that it didn’t overpay for those shares.

I can guarantee you that AGF will buy as many shares as it possibly can in the fourth quarter — a sign it’s confident about the company’s future.

On the bottom line, in Q3 2018 AGF's adjusted EBITDA increased by 12.6% to $32.2 million, an EBITDA margin of 27.6% — 170 basis points higher than a year earlier. Meanwhile, its adjusted earnings per share increased by 33% to $0.20.

Today, AGF is trading at 3.9 times EBITDA. A year ago, it was trading at 5.8 times EBITDA. Its margins are getting stronger and yet its valuation has seen tremendous erosion.

Two years ago, AGF had net mutual fund redemptions of $899 million through the first nine months of the year. Last year through the first nine months, it lost another $360 million. However, this year, as I mentioned earlier, they were positive to the tune of $73 million.

No one else in the industry comes close in terms of a turnaround.

I could say more about AGF's quarter, but I think you get the point. It was above average.

Ride the volatility

This time two years ago, I recommended AGF stock when it was trading at $5.10 a share.

"I don't know if AGF will still be independent in 10 years, but what I do know is that paying $5 and change to find out isn't much of a gamble for anyone who's got the money to lose," I wrote in October 2016. "To me, the upside at this point far outweighs the downside."

A year later it was trading around $8.30, or 63% higher. I recommended it a second time, suggesting there was little downside now that CEO Blake Goldring had cleaned up AGF's business.

As Murphy's Law would happen, AGF stock rode its way all the way back down around $5, where it trades today.

Nothing's changed about the business. In fact, Blake Goldring is so confident about the business that he's stepped aside as CEO, handing the reins to Kevin McCreadie, the company's current president and chief investment officer, effective December 1.

McCreadie was hired as CIO in 2014 to grow the company's institutional assets under management. In Q3 2018, they were $12.7 billion, 19% higher than a year earlier, suggesting the executive was successful continuing AGF's transformation from mutual fund company to a global asset manager.

Unless something changes of a material nature, AGF stock is and will continue to be a great deal under $6.

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