Growth Stocks: Less Promise, More Delivery

Description

Let's face it: sometimes financial markets can be about as irrational as a toddler after taking their toy away.

Park Lawn (TSX:PLC) released Q3 earnings on November 13. It posted 92% year-over-year revenue growth, and yet its share price got smacked with a 4.7% drop on the same day. One-day reactions are no way to make conclusions.

What's behind the numbers for this $540 million market cap company?

In Park Lawn's words, the business provides "goods and services associated with the disposition and memorialization of human remains." It's not your usual investment industry, but with a gross margin north of 70%, the business caught the eyes of bullish investors, pushing the stock price up and leading to a trailing price-to-earnings ratio that is on par with growth names like **Netflix**.

Is Park Lawn actually as disruptive as Netflix? I wouldn't go that far. There are similarities, though. Park Lawn is a cash-generating machine, and despite being in an industry that is fairly fragmented, it has perfected the art of the deal in the form of serial acquisitions (akin to Netflix hoarding content).

The recent pullback warrants some discussion on the negative sentiment. Growing at all costs has meant long-term debt is building — a strategy that, although sustainable in this case, is still somewhat going against the grain.

Another irksome tendency is for the company to overestimate earnings. In the last eight quarters, Park Lawn has met or beat earnings four times and missed the other four. I'd prefer to see more under promising and more over delivering, especially given the small size and the clear aggressive acquisition strategy.

Another option with high margin and return on equity

Next is **goeasy** (TSX:GSY), which is of comparable size and operates as a financial lending for personal loans (called easyfinancial) or repayment plans for furniture, appliances, or electronics (called easyhome). In recent years, the easyfinancial part of the business has outpaced the home division — a trend that will likely persist. goeasy fills the gap between Money Mart shops that loan smaller amounts to large sums like a home equity line of credit from banks. goeasy customers can still access a maximum of $25,000 and the steep annual interest rate ranges from 19% to 29%.

Revenue growth over the last three years has climbed 57%, which is impressive until you consider that Park Lawn revenue is up 320%. In reading goeasy's Q3 financial statements, it is good to see transparency on business expenses. The numbers are a bit sobering, however, as goeasy has to eat bad debts on the proportion of loans not paid back. In the nine months of 2018, bad debt increased 70% from the same period in 2017, pushing this expense line item above the cost of paying >1,800 employee salaries and benefits.

With a track record that dates back to 1990, the investor has to trust that goeasy will continue to walk this fine lending line. In the last eight quarters, goeasy met or beat earnings in all but one quarter.

Wrapping up

Investors apprehensive about adding equities to their portfolios at a time when recession clouds may be forming on the horizon would do better by selecting Park Lawn over goeasy. A contrarian view is that even during tough times, people will still seek fast cash from among the 228 goeasy kiosk/store locations.

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Date
2025/07/19
Date Created
2018/11/18
Author

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