These 3 Deep Value Stocks Are Poised to Soar in 2019

Description

When executed correctly, deep value investing can be one of the most profitable ways to put your money to work.

Like most strategies, it appears simple on the surface. Investors need to find the cheapest stocks, make sure they have fixable problems, and then take a position. It doesn't appear to be that hard.

The proof, as always, is in the pudding. Every deep value stock has noticeable warts. If you haven't found them, it means you're not looking hard enough. Figuring out which names are about to soar is no easy task, either. Deep value portfolios are filled with many so-called "value traps" — cheap names that just can't shake off their woes.

Still, the potential rewards more than make up for these issues. Some former deep value names are up 200%… 300%… even 500% from their lows. There's no guarantee that these three stocks will do that well, of course, but they all have similar potential. Let's take a closer look.

Air Transat

Transat A.T. Inc. (TSX:TRZ), the parent company of Air Transat, is often ignored by investors who are more focused on Canada's two largest airlines. The company only dabbles in domestic flights, choosing instead to focus on two segments — trips to the south in the winter and flights to Europe in the summer.

These routes are extremely competitive and don't leave much room for error. 2018's results were marred by increasing fuel prices, which hit Transat particularly hard despite the company hedging some of that exposure. Operating profit fell to just $16.5 million after exceeding $100 million in 2017.

Shares are cheap on a number of different metrics. They currently trade at just under $6 each, a 40%+ decline in the last year. The stock trades at just 0.4 times book value and 0.1 times sales, and trades at just over 2 times 2017's operating income. It also has a pristine balance sheet with little debt and is taking steps to expand into the hotel business, which should provide steadier profits.

Transat's upside potential could easily be $11 per share, a level it saw as recently as 2017.

CI Financial

CI Financial Corp (TSX:CIX) is a former dividend darling that fell out of favour when it slashed its distribution by approximately 50% in 2018. The company's exposure to the mutual fund industry, a sector that's currently out of favour, doesn't help either. Shares are down almost 40% over the last year.

Management also believes shares are massively undervalued, and this time actually put their money where their mouth is. CI is in the process of taking the cash it was formerly paying out as dividends and adding it to the share buyback program. It has pledged to repurchase $1 billion worth of its shares in the next 12-18 months, which works out to approximately 23% of its market cap.

CI's shares currently trade at 8.3 times trailing earnings. If the share buyback program is successful and earnings stay the same, the stock will trade at less than six times earnings a year from now. Investments don't get much cheaper than that.

Baytex

Baytex Energy Corp (TSX:BTE)(NYSE:BTE) is definitely the riskiest name on this list. But it also has the most upside. If oil recovers, the company's stock could easily surpass $10 per share, representing more than 300% upside from today's price.

The problem is oil must recover in a somewhat short period. Baytex' revolving credit facilities must be renewed in 2020 and it has an additional US$550 million worth of debt due in 2021. If the underlying crude market doesn't recover, there's a risk that creditors simply won't allow Baytex any additional leeway, which will inevitably lead to some sort of restructuring.

The good news is that Baytex has operations in low-cost areas like the Eagle Ford basin in Texas, which are generating cash flow despite the weakness plaguing the rest of the sector. Next up is further expansion in its East Duvernay leases, which has the potential to be a multi-billion find.

Baytex shares trade at just over $2 each at the time of writing. If crude oil recovers to the $80 range, the stock could easily soar to $8 or $10, which is outstanding return potential.

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