



Why SNC-Lavalin (TSX:SNC) Stock Fell 21% in August

Description

SNC-Lavalin Group (TSX:SNC) was crushed last month, with shares falling roughly 21%. The **S&P/TSX Composite Index**, for comparison, rose by 2%. If you've been paying attention, the steep decline isn't anything new. Since 2019 began, shares have shed more than 50%.

In August, the company faced another slew of difficult news, but a buying opportunity might be just around the corner. If you want to take advantage, you'll need to understand the pressures hitting the stock. Only then will the big upside potential be clear.

Here's what happened

If you're looking for [recession-proof stocks](#), SNC-Lavalin isn't a candidate. The company's business model is highly impacted by economic swings and changes in sentiment. In addition, the company has been embroiled by multiple scandals that have nearly brought this 100-year-old firm to its knees.

Back in January, the stock lost one-fourth of its value in a single trading session after management released its worst earnings report in a decade. The company posted an enormous \$9.11-per-share loss. SNC-Lavalin booked a \$346 million charge in its mining segment and a \$47 million hit due to separate legal matters. But even without those extraordinary items, the underlying businesses *still* generated a net loss.

Then things got worse. **Standard & Poor's** cut its credit rating to BBB-, while news reports surfaced claiming the company was involved in a political scandal involving Justin Trudeau. According to the *Toronto Sun*, Trudeau "led a government-wide campaign — involving his highest-ranking officials and advisors — to politically interfere in SNC-Lavalin's criminal prosecution on corruption charges." His goal was allegedly to reduce political blowback, but it seems as if the actions made things even worse.

Entering August, investors were struggling to make sense of the political crisis and a deteriorating business, all in the face of a weakening economy. On August 1, the company reported second-quarter earnings. Adjusted EPS came in at *negative* \$1.34, but official GAAP EPS was a truly terrifying *negative* \$12.07. Revenue for the quarter was \$2.3 billion — a 10% reduction from the year before.

The stock fell roughly 10% over the coming days.

Then, a new report from the Office of the Conflict of Interest and Ethics Commissioner opined that Trudeau “violated the country’s Conflict of Interest Act by trying to influence the former justice minister to overrule a decision to not grant a deferred prosecution agreement to SNC-Lavalin.” The final conclusion is far from determined, but this news added speculation that SNC-Lavalin may eventually face penalties or government blowback.

What to expect

As you can tell, this is a troubled stock. In May, I called it the “most controversial stock on the TSX.” The events in August made it even *more* controversial. Eventually, if the business stabilizes, shares could be worth \$40 or more. That represents at least 100% in potential upside. But critically, the risk factors here are impossible to quantify. Additionally, the company’s debt load now exceeds its equity value, adding financing risk to an already complex situation.

Many investors are tempted to catch this falling knife, but I’m sticking to the sidelines. SNC-Lavalin stock will eventually be due for another look, but not before some clarity is achieved.

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