Sea-Doo? More Like Sea Don't Invest in This 1 Stock!

Description

One of the biggest mistakes I see people making in their TFSA or RRSP is buying into a stock that provides a want instead of a need.

Companies I am referring to include **Air Canada**, **Canopy Growth** and **BRP** (TSX:DOO)(NASDAQ:DOOO), to name but a few.

Air Canada is the premier airline for Canada. Unfortunately for the company, its success is entirely dependent on the state of the economy. When times are good, business is booming, but when times are bad, flights are one of the first things that people sacrifice.

The same thing is true for Canopy Growth. As people have more disposable income, they can afford to spend it on weed. As the state of the economy deteriorates, however, this money will be put toward necessities such as food and utility bills.

For those of you who are unfamiliar with BRP, it designs, manufactures, develops, distributes and markets snowmobiles, all-terrain vehicles and personal watercraft.

Its brand portfolio consists of Ski-Doo, Sea-Doo, Can-Am and Lynx.

Similar to the aforementioned companies, BRP's recent success is tied to the success of the economy as a whole. With tumultuous times expected ahead, BRP is a stock you want to avoid based on the industry as a whole and its low asset to liability ratio.

Recreational products industry

According to a recent reports released by research firm Zacks, the Leisure and Recreation Products industry is ranked at #186 out of more than 250 Zacks industries, placing it in the bottom 27%.

The data indicates that the top 50% of the industries outperformed the bottom 50% by a factor of more than 2 to 1.

The poor performance of this industry is due to the bearish sentiment shared by analysts, as they're losing confidence in the group's earnings growth potential. The industry's earnings estimate for fiscal 2019 have decreased 11.5% since the beginning of the year.

BRP is directly affected by this, as it operates in the Leisure and Recreation Products industry. Despite its revenues increasing every year for the past five fiscal years, this report indicates looming volatility that will negatively impact BRP's bottom line.

Low asset to liability ratio

I was quite surprised when I looked at the balance sheet for BRP.

Given that revenues have increased each year for the past five fiscal years, I was shocked to see that BRP has more liabilities than assets.

This suggests that the company is highly leveraged, which is true given its $1.2 billion in debt and capital lease obligations.

As an investor, this should concern you, as a high debt adversely affects a company in one of two ways.

First, debt comes with interest, which means a company with a great deal of debt is paying significant amounts of interest. This is true for BRP, which paid $62 million in interest in fiscal 2018.

Second, debt puts pressure on the company to generate adequate cash. Cash is used for interest and principal debt payments, which means that a company that can't generate adequate cash may default on its payments.

Summary

With a declining Leisure and Recreation Products industry and liabilities that exceed assets, BRP is not in a good position to deliver decent returns to its investors.

Despite an income statement that indicates increasing revenues in each of the past five years, its balance sheet is another story. With the amount of debt that BRP currently has, investors are taking a big risk by investing in the company.

I would avoid this stock if I were you.

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