This Beaten-Down Canadian Equipment Dealer Could Go Up by 30%

Description

It's a good idea to pick up fundamentally strong stocks when they are going through a rough patch.

Cervus Equipment (TSX:CERV) has been taking a beating since May this year. The stock has fallen almost 47% in 2019 and is currently trading at $7.89. A micro-cap stock with a market cap of $117.2 million, Cervus is an equipment dealer (agricultural, transportation, and industrial), powered by six iconic brands: John Deere, Peterbilt, JLG, Clark, Doosan, and Sellick.

The company runs and manages 63 dealerships across Canada, Australia, and New Zealand. The company has reported three consecutive years of profits and looked to be on track for the fourth year but the latest results haven't been great.

Not so great Q3 numbers

Third-quarter results for Cervus reported less than desirable numbers. Total revenue for Cervus came in at $317 in the third quarter of 2019, down 19% from the same period last year. This was attributed to a weak Western Canadian agriculture market. There was a 26% decline in equipment sales, partly offset by an 8% increase in product support revenue.

The company reported a loss of $1.7 million compared to income of $12 million for the same period of 2018. Gross profit declined 28% in the quarter on reduced new equipment revenue, margins, and OEM incentives, along with margin concessions on used equipment across the industry.

Cervus has been quick to take action, reducing its used agriculture equipment inventory by $33 million or 18% compared to the second quarter of 2019, which is also below the inventory levels reported on September 30, 2018.

Inventory write-downs associated with these aggressive reductions increased $6.5 million in the quarter, and $4.9 million year to date compared to 2018. These actions have resulted in a comparatively strong inventory turn ratio of 3.87 for new agriculture equipment and 1.65 for used agriculture equipment.

What next for Cervus stock?

Cervus still remains a good stock to keep an eye on. While the company may not match its 2018 revenues, there are all indications that the stock will bounce back in 2020.

As Fool contributor Christopher Liew said, analysts are expecting a potential upside of over 68.67% beyond 2020. Analysts expect the company sales to fall by 14.9% in 2019 to $1.15 billion and then rise by 1.9% to $1.17 billion in 2020. Its earnings are estimated to fall from $1.62 in 2018 to -$0.32 in 2019. However, it is expected to rise to $0.39 in 2020 and at an annual rate of 80% between 2020 and 2023.

A forward dividend yield of 5.58% makes Cervus a very attractive passive income stock as well, especially after considering its low forward price-to-earnings multiple of 14.35. This indicates that the stock is undervalued if it manages to stabilize the revenue and increase margins post-2019.

All indicators point to the fact that Cervus is in oversold territory right now. It looks like the perfect time to start picking up shares to make sure one capitalises on higher share prices when business turns around. Until then, there is always the dividend to put some extra cash in your accounts.

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