January 2020: Steer Clear of This 1 Stock!

Description

MAV (TSX:MAV) is a global personal care company that sells hair care, body care, and beauty products in Canada, the U.S., and internationally. The company offers the products through retail partners and distributors.

The company reports a market capitalization of $129 million with a 52-week high of $10.74 and a 52-week low of $2.25.

Intrinsic price

Based on my calculations, using a discounted cash flow valuation model, I determined that MAV has an intrinsic value of $1.40 per share. Assuming less-than-average industry growth, the intrinsic value would be $0.87 per share, and higher-than-average industry growth would result in an intrinsic value of $2.06 per share.

At the current share price of $3.51, I believe MAV is overvalued. Investors looking to add a beauty and cosmetic manufacturer to their TFSA or RRSP should avoid buying shares of MAV.

MAV has an enterprise value of US$163 million, which represents the theoretical price a buyer would pay for all of MAV outstanding shares plus its debt. One of the concerning things about MAV is its leverage, with debt at 46.7% of total capital versus equity at 53.3% of total capital.

Financial highlights

For the nine months ended September 30, 2019, the company reported a mediocre balance sheet with negative retained earnings of US$7 million. This is not a good sign for investors as it signifies the company has more years of cumulative net loss than net income. That said, the company significantly improved its retained earnings from -US$12 million as at December 31, 2018 to -US$7 million nine months later.

The company reports US$5 million in cash on hand, in addition to an 82.5% unutilized revolving credit facility (US$16.5 million undrawn on a US$20 million facility). Further to this, the company has an accordion option for an additional US$50 million for working capital and general corporate purposes which effectively increases the credit facilities to US$70 million. This provides the company with ample liquidity to fuel future business growth.

Overall revenues are up year over year from US$65 million during the nine-month period in 2018 compared to US$78 million in 2019 (+19.5%). This is complemented by a reduction in operating expenses for after-tax income of US$5 million.

From a cash flow perspective, the company made a US$5 million drawdown of revolving facilities while repaying US$7 million in borrowings and revolving facilities which demonstrates fiscal responsiblity on the part of management.

From a financial perspective, MAV is doing well. That said, my analysis considers unleveraged free cash flows, which means the growing inventory and accounts receivables for MAV results in increasing cash outflows and reduces the intrinsic value of the company. Accounts receivables have grown 142% from FY17 to FY18 complemented by accounts receivable growth of 302% from FY17 to FY18. This represents significant cash outflows.

Foolish takeaway

Investors looking to buy shares of a beauty and cosmetic manufacturing company should avoid MAV. Using a discounted cash flow model, I calculated MAV's intrinsic value to be $1.40 per share. Even with a generous long-term growth rate, MAV's intrinsic value increases to only $2.06, which is significantly less than the $3.51 it is currently trading at. Fellow fool Ambrose O'Callaghan begs to differ.

2020 may present opportunities to buy shares at less than intrinsic value, but for now I would steer clear of MAV.

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