



Canadians: Do NOT Invest In This 1 Brewery Stock!

Description

Waterloo (TSX:WBR) is engaged in the production and distribution of alcohol-based products. The company operates an Ontario-based facility with the majority of its customers being in Ontario.

Its brands include Waterloo Brewing, Landshark, Margaritaville, Laker and Seagram. The company reports a market capitalization of \$122 million with a 52-week low of \$2.60 and a 52-week high of \$4.10.

Intrinsic price

Based on my calculations using a discounted cash flow (DCF) valuation model, I determined that Waterloo has an intrinsic value of \$1.53 per share.

Assuming less than average industry growth, the intrinsic value would be \$1.49 per share and higher than average industry growth would result in an intrinsic value of \$1.56 per share.

At the current share price of \$3.46 at writing, I believe Waterloo is significantly overvalued. Investors looking to add a brewery company to their RRSP or TFSA should avoid Waterloo [for now](#).

Waterloo has an enterprise value of \$69 million, representing the theoretical price a buyer would pay for all of Waterloo's outstanding shares plus its debt.

One of the good things about Waterloo is its leverage with debt at 10.7% of total capital versus equity at 89.3% of total capital.

Financial highlights

For the fiscal year ended October 27, 2019, the company reports a mediocre balance sheet with \$5.5 million in negative retained earnings. This is not ideal for investors, however, as it suggests that the company has had more years of cumulative net loss than net income.

Waterloo reports cash of \$560,000 on \$3.9 million in current portion of long-term liabilities. I'm not

content with this, however, as a company with this history should have enough cash on hand to cover its short-term obligations.

That said, the company reports an operating line of \$8 million (24% utilized) as at January 31, 2019, which means it has more than enough room on its facility to cover the shortfall.

Overall revenues are up materially to \$45.7 million, compared to \$37.7 million in 2018 (+21%) resulting in gross profits of \$13.6 million for 2019 (gross profit margin of 30%). Pre-tax income of \$2.1 million, up from \$837,000 in 2018 (+153%).

From a cash flow perspective, management has done a very good job of managing its debt as indicated by long-term debt repayments of \$1.4 million in 2019 and \$1.1 million in 2018.

This is complemented by a decrease in bank indebtedness of \$1.9 million in 2019 and \$788,000 in 2018, offset by issuance of long-term debt of \$2.6 million in 2018.

I commend management for taking such as proactive approach to its debt management as interest payments can be a significant drain on a company's cash.

The company is a [dividend paying entity](#) with a current yield of 3.03%, which is achieved through quarterly payments of \$0.02625 per share.

Foolish takeaway

Investors looking to buy shares of a brewery company should avoid Waterloo. With an intrinsic value of \$1.53 compared to its current share price of \$3.46, I believe that Waterloo is significantly overvalued.

The company reports negative retained earnings and insufficient cash to cover short-term portion of long-term debt. This is offset by growing revenues, an adept management team and a decent dividend yield of 3.03%.

If Waterloo stretches its accounts payable and tightens the collection period for accounts receivables, its intrinsic value will appreciate significantly. I would like to see management implement this strategy to deliver greater value to shareholders.

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