



## TFSA Investors: AVOID This 1 Top TSX Stock...for Now

### Description

**Saputo** ([TSX:SAP](#)) produces, markets and distributes a wide array of dairy products from Canada, the United States, Australia, Argentina and the United Kingdom.

The company is one of the top three cheese producers in the US (48% of revenues) and one of the largest cheese manufactures in Canada (30% of revenue). Its brands include Stella, Armstrong, Frigo and Saputo.

Saputo reports a market capitalization of \$16.61 billion with a 52-week low of \$37.38 and a 52-week high of \$46.41.

### Intrinsic price

Based on my calculations using a discounted cash flow (DCF) valuation model, I determined that Saputo has an intrinsic value of \$23.70 per share.

Assuming less than average industry growth, the intrinsic value would be \$23.43 per share and higher than average industry growth would result in an intrinsic value of \$23.99 per share.

At the current share price of \$40.70 at writing, I believe Saputo is significantly overvalued. Investors looking to add a dairy manufacturer to their portfolio should avoid Saputo [for now](#).

I would suggest that investors follow the stock through 2020 and wait for an opportunity to buy shares at less than intrinsic value.

Saputo has an enterprise value of \$12.1 billion, representing the theoretical price a buyer would pay for all of Saputo's outstanding shares plus its debt.

One of the good things about Saputo is its leverage with debt at 12.8% of total capital versus equity at 87.2% of total capital.

## Financial highlights

For the six months ended September 30, 2019, the company reports a strong balance sheet with \$3.9 billion in retained earnings, up from \$3.7 billion as at March 31, 2019.

This is a good sign for investors, as it suggests the company has more years of cumulative net income than net loss, which is reinvested into the company to fuel growth.

Saputo reports cash and equivalents of \$173 million, with \$633 million in short-term debt obligations, indicating that the company does not have enough cash on hand to cover its current debt liabilities. Given its \$1.6 billion credit facilities (16% utilized), this is not a concern.

Revenues are up significantly to \$7.3 billion during this period, compared to \$6.7 billion in 2018 (+9.7%), largely driven by its acquisitions of Murray Goulburn in Australia, Shepherd Gourmet Dairy in Canada, F&A Dairy Products, Inc in the United States and [Dairy Crest](#) Group in the U.K.

Pre-tax income is strong at \$409 million, up from \$384 million in 2018 (+6.4%), with relatively flat net income at \$296 million in 2019.

Senior management is committed to managing its long-term debt, as indicated by a \$1.1 billion pay down in 2019 following a \$648 million pay down in 2018. This is offset by the issuance of long-term debt amounting to \$2.1 billion in 2019 and \$1.6 billion in 2018.

As mentioned, the company engages in an acquisition-centric growth strategy that resulted in cash outflows of \$1.7 billion in 2019, following \$1.4 billion in cash outflows in 2018.

The company is a dividend paying entity with a current dividend yield of 1.67%.

## Foolish takeaway

Investors looking to buy shares of a dairy manufacturing company should avoid Saputo for now. The company reports a solid balance sheet with positive retained earnings, offset by cash and equivalents of \$173 million with \$633 million of short-term liabilities.

The company's acquisition-centric growth strategy is paying off with a growth in revenues of 9.7% year over year, complemented by growth in pre-tax income.

That said, with an intrinsic price of \$23.70 compared to its current share price of \$40.75, I believe Saputo is significantly overvalued.

### CATEGORY

1. Investing

### TICKERS GLOBAL

1. TSX:SAP (Saputo Inc.)

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1. Investing

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