Value Investors: This Dirt-Cheap 7.3% Yielder Has Massive Potential

Description

One of the frustrating things for value investors is how limiting returns can be.

For instance, there are virtually zero value stocks with massive potential. A successful value investing strategy is somewhat formulaic. You buy when the stock is cheap and sell when it approaches fair value. It has traditionally been a good way to earn a nice return on your money – except for the last decade or so. Returns from value stocks have lagged while growth stocks did quite well.

Every now and again, however, a stock shows up that should be appreciated by value investors and growth investors alike, a company that's trading at a dirt-cheap valuation today with massive upside potential in the future.

I've found such a stock, a company that many investors completely misunderstand. Here's why it appeals to both value investors and growth aficionados.

For value investors…

Capital Power (TSX:CPX) is one of the cheapest stocks on the entire **Toronto Stock Exchange**. Value investors were amazed at its rock bottom valuation even before the market crashed, and shares have only gotten cheaper since.

The company has pretty much transformed itself since 2015. Its primary assets were coal-fired power plants in Alberta, but management was forced to embark on a diversification plan when the province passed legislation that banned coal as a fuel starting in 2030. It used government funds to help pay for the conversion of its Alberta plants to natural gas, as well as acquiring and developing greener assets around North America.

These days, Capital Power has a portfolio of 28 different power facilities generating some 6,400 MW of energy. It also has an additional 650 MW in various stages of development. Essentially, it took thecash flow from its Alberta assets and put it to work in other locations. It's a simple long-term strategy,but an effective one.

Here's the part that gets value investors really excited. Capital Power projects it'll earn around $5 per share in adjusted funds from operations in 2020, a number that shouldn't be affected too much by COVID-19. Shares trade at $26.32 each as I type this. That translates into just over 5 times earnings.

Capital Power is also an exciting dividend stock. The current dividend yield is 7.3% and the company has already promised an increase in the payout in both 2020 and 2021. Capital Power's payout ratio is quite low, meaning it should be able to deliver on this promise.

For growth investors…

Capital Power isn't just for value investors. It has an interesting growth avenue nobody ever talks about. Heck, I'd be willing to bet most shareholders don't even know this part of the company exists.

Back in 2018, Capital Power made a small investment in a company called C2CNT, a startup ran by Dr. Stuart Licht, who is a Professor of Chemistry at George Washington University. C2CNT removes carbon dioxide from emitting power plants to make carbon nanotubes, tiny structures that are used to make materials like cement, steel, or aluminum much stronger.

It's easy to see the value of carbon nanotubes. Using fewer expensive materials would be a very big deal to the construction industry. There's just one problem: carbon nanotubes are incredibly expensive to produce. It's cheaper to just use the extra material today.

But C2CNT may be on the verge of something big. Capital Power's CEO Brian Vassjo told investors back in December that the technology the company uses was feasible, and the big stumbling block right now is cost. Small scale tests designed to test cheaper production techniques have been promising, and Capital Power seems cautiously optimistic.

This technology could be massive for the construction business. It would allow these industries to significantly reduce their carbon footprints, since they wouldn't have to produce nearly as much material. C2CNT could license the technology to these companies, something that could deliver massive upside to Capital Power's share price. We're talking 50%–100% as a conservative estimate.

The bottom line

Capital Power isn't just for value investors. The carbon nanotube technology might be a long-shot, but it's a very interesting one. And while you wait for the potential upside from this exciting part of the company, investors can collect one of the best high yields on the TSX.

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