TFSA Investors: Say Cheese to This Dairy Manufacturer

Description

The Tax-Free Savings Account (TFSA) is a flexible investment account for Canadians. The TFSA contribution limit for 2020 stands at $6,000. As withdrawals from this account are tax-free, it makes sense to allocate equity investments to your TFSA. For this, you need to identify companies that can outperform the broader markets in the upcoming decade.

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Dairy producer and distributor **Saputo** (TSX:SAP) is one such company that has the potential to create long-term wealth.

A good pick for your TFSA

Saputo's revenue for the fiscal fourth quarter was at $3.72 billion, up 14.9% from the same period last year. EBITDA rose 8.5% to $298.4 million, while net earnings fell 28.6% to $88.7 million. In fiscal 2020, company sales rose 10.7% to $14.95 billion. Comparatively, EBITDA rose 20.2% to $1.47 billion, and net income was up 4.8% at $653.7 million.

Saputo operates in the Americas (Canada, U.S., and Argentina), Australia, and Europe. The company expects a below-average June quarter, but it says demand in Australia is surging back to pre-COVID levels. The U.K. is an outlier and has hit historic highs during this pandemic, while demand in Argentina has been stable as well.

There is a fall in demand and revenue in the U.S. and Canada. The company has written down $44.8 million in inventory in Q4 and expects a write-down in the first quarter of fiscal 2021 as well. However, this hasn't stopped Saputo from issuing a quarterly dividend of $0.17.

Saputo has a robust balance sheet and has enough resources to come out of this pandemic almost unscathed. It definitely has enough to pay its employees. The company very proudly said on its analyst call that it will pay all its employees in full, whether they are working full hours or no. It has a no-layoff policy in place throughout this crisis.

Focus on acquisitions

While this spells good news for Saputo employees, the company is not averse to taking advantage of the misfortunes of some of its competitors. Saputo stated that competitors have fallen short of fulfilling deliveries and other commitments. They have high leverage and are burdened with debt. According to Saputo, a lot of these assets may be up for acquisitions at discounted prices.

Lino Saputo, CEO, Saputo said, "We are in a fantastic position to wait on the sidelines and wait for the right opportunity to come along at the right price for the right strategic orientation for our business. So I tell you I'm truly optimistic about what's to come after COVID-19 is behind us."

Saputo says that there are three to four acquisition files on his desk at any given point in time and that its phones have been ringing, dialed in by companies that want to be acquired. In fact, the only reason why Saputo says it hasn't closed an acquisition in this period is that the management hasn't been able to travel to complete its due diligence process.

Saputo has completed phase I (a preliminary evaluation) and phase II (a due diligence that gets a letter of intent). However, the third phase that involves meeting the management and visiting the facilities is put on hold because of travel restrictions. Saputo is confident that when the governments lift these restrictions, its acquisition process will resume.

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What's next for investors?

Saputo stock is trading at a forward price-to-earnings multiple of 19. Its price-to-sales ratio is 0.9. These multiples indicate that the stock is trading at a reasonable valuation, especially considering its five-year estimated earnings growth of 15% and a dividend yield of 2%.

Analysts tracking Saputo have a 12-month average target price of $41, which is 22% above the current trading price.

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Date
2025/08/25
Date Created
2020/06/08
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