



Is Western Forest Products a Buy at These Levels?

Description

Western Forest Products (TSX:[WEF](#)) is a lumber company that offers a diverse mix of specialty wood products, such as cedar, hemlock, balsam, and Douglas fir products. These products are used in outdoor living, interior and exterior appearance, and structural and industrial applications. After delivering impressive returns of more than 68% last year, the shares are under pressure amid a decline in lumber prices this year — trading about 3% lower year to date.

Does this change offer investors a smart buying opportunity for Western Forest Products?

First, let's look at its recently reported first-quarter performance and growth prospects.

First-quarter earnings

Last week, Western Forest Products reported its [first-quarter performance](#), with its top line growing 13%, to \$359.6 million. The favorable sales mix and higher price realizations more than offset a decline in its sales volume. Year-over-year, sales volume declined 9%. The company's management cited logistical constraints for the decline.

The company produced 175 million board feet of lumber during the quarter, 12% lower than its previous year's quarter. The issues related to log supplies and temporary shutdowns at certain sawmills lowered its production. Meanwhile, the company's net income declined from \$53.8 million to \$38 million, primarily due to the non-core asset sales and significant tax loss carryforwards in the previous year's quarter. If you ignore these restructuring and other items, the company's operating income increased by 7%.

Supported by its strong cash flows, Western Forest Products purchased around 3.34 million shares for approximately \$7.3 million during the quarter. Its financial position also looks healthy, with liquidity of \$316.3 million at the end of the quarter. Now, let's consider its growth prospects.

Western Forest Products's outlook

After touching a low in March, lumber prices are rising as the home building season heats up. During the summer months, home building activities will increase. Meanwhile, analysts expect lumber prices to trade around US\$1,000 – US\$1,400 over the next few months. The higher prices could benefit Western Forest Products.

The company has a well-diversified market, with 36% and 27% of its revenue coming from the Canadian and U.S. markets, respectively. The remaining 37% of its revenue comes from international markets. Because of constrained rail capacity and improving container availability, the company is looking at expanding the use of low-cost container shipping in the coming months. Western Forest Products is also focusing on increasing the shipment of its higher-margin specialty products, which could boost its margins. So, I'd say its business outlook looks healthy.

Dividends and valuation

Despite returning more than 68% last year, Western Forest Products stock still trades at an attractive valuation today. Its NTM (next 12-months) price-to-sales and NTM price-to-earnings multiples stand at 0.5 and 4.9, respectively. Meanwhile, the company recently raised its quarterly dividend by 25%, to \$0.0125, with its forward yield at 2.45%.

Bottom line

If you're considering investing in Western Forest Products, know that rising interest rates and logistical constraints are a cause of concern. And rising home prices could create an affordability crisis, hurting the lumber market — including Western Forest Products.

Despite these risks, I am bullish on the company thanks to rising lumber demand during the beginning of the home building season, along with its diversified market, favorable sales mix, and attractive valuation today.

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