Insiders Are Selling CGI Group: Should You?

Description

Successful investing requires analyzing financial reports, evaluating a company's growth prospects, and assessing whether a company has the right management team. A shortcut, used by some traders, is to rely on insider activity to guide investing decisions. Insiders, which includes senior officers and directors, need to disclose their purchases and sales of company stock.

According to INK Research, **CGI Group** (TSX: GIB.A)(NYSE: GIB) had the third-highest dollar volume of insider selling on the Toronto Stock Exchange over the past 60 days — nearly $60 million of stock. With a presence in the Americas, Europe, and Asia-Pacific, CGI provides end-to-end IT consulting, outsourcing, and systems integration services to customers within specific sectors, including government, healthcare, financial services, and telecommunications.

For bottom-up, long-term investors, insider activity is just one piece of information to consider. Like every investor, insiders have their own reasons for buying and selling, and their actions may not be a clear signal on where the stock price is headed.

Apart from insider activity, let's take a closer look at the case for, and against, an investment in CGI Group.

The case for CGI Group

CGI had a solid second quarter that saw profit more than double, driven by a 7% rise in revenue and strong European orders.

The company booked $2.9 billion in new business during the quarter, and reported a book-to-bill ratio of 105%. Book-to-bill is the ratio of orders added to the company's backlog versus completed work that's been billed to clients. A ratio over 100% means CGI is winning work faster than it's completing existing orders, and increasing backlog. CGI's acquisition of U.K.-based competitor Logica in 2012 for £1.7 billion appears to be paying off — the company recorded a book-to-bill ratio of 110% in Europe compared to just 98% in North America.

Despite the strong quarter, CGI has lost 6% of its value over the past six months compared to a 9%

gain in the **S&P/TSX Composite Index** (TSX: ^OSPTX). It's currently trading 9% below its 52-week high. Today, CGI offers investors an attractive valuation. Its trailing and forward price to earnings ratios trade at a slight discount to their five-year averages. Its forward PEG, which is the forward P/E ratio divided by the five-year forecasted growth rate, is just 0.6 — significantly lower than the five-year average of 1.1.

The case against CGI Group

Reduced U.S. government spending on IT-related services and the issues surrounding the troubled roll-out of President Obama's healthcare website are two reasons why CGI's book-to-bill ratio for North America slipped below 100% for the most recent quarter. CGI Group's contract to manage the online U.S. health exchange program was subsequently not renewed.

The business of IT outsourcing, systems integration, and consulting is very competitive, and pricing pressure is sure to increase as competitors try to capitalize on CGI's recent missteps in North America.

Then there is the issue of CGI's dual-share structure. Thanks to the company's Class B shares, the direction of the company is tightly controlled by the company's co-founders. Good corporate governance usually requires that equity ownership and voting rights go hand in hand — not so at CGI.

Finally, because CGI reports in Canadian dollars, its results are positively impacted by a lower Canadian dollar relative to a range of currencies it does business in. The Canadian dollar has lost nearly 10% of its value compared to the U.S. greenback over the past 18 months. Any appreciation in the value of the loonie from current levels will hurt CGI's financial performance.

So should you invest?

CGI is among the world's five largest computer services companies. And with a market capitalization of $11.3 billion, CGI is nearly three times larger than Canada's best known technology brand, **BlackBerry** (TSX: BB)(NASDAQ: BBRY).

CGI has grown to approximately 68,000 employees, and has proven adept at identifying and acquiring companies that can be successfully integrated into its business model. And it's delivered for investors, gaining nearly 300% over the past five years.

CGI is a Canadian success story, even if it's not as well-known as BlackBerry. I don't think CGI is going anywhere but up over the next five to 10 years; it offers an excellent opportunity for long-term investors to achieve market-beating returns.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:BB (BlackBerry)
2. NYSE:GIB (CGI Group Inc.)
3. TSX:BB (BlackBerry)
4. TSX:GIB.A (CGI)

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