

Can Shoppers Drugmart Win in a Tough Market?

Description

Shoppers Drugmart (TSX:SC) reported lackluster results last week, citing consumers who remain “value conscious and price competitive” according to CEO Dominic Pilla. As the closing date for the \$12.4 billion acquisition of Shoppers by **Loblaw** ([TSX:L](#)) approaches, let’s look at some of the key takeaways that investors should keep in mind and digest.

Review of Q4 results

Sales increased 0.9% in the fourth quarter. Pharmacy sales accounted for 44.8% of total sales. Same-store sales growth in pharmacy declined 0.5%. Similar to **Jean Coutu’s** (TSX:PJC.A) experience, the company saw a decline in the value of pharmacy sales due to an increase in generic prescriptions. On a positive note, prescriptions filled increased 4.7%, and front-end same-store sales growth was a respectable 1.7%.

Operating margins declined 5.1% in the quarter due partly to promotional activity, as price points decreased and marketing expense increased. The company also experienced an increase in store costs in general, as wages and other expenses also increased.

Marketplace still very competitive

Promotional activity during the quarter remained high, as an increasingly competitive environment and increasingly price-sensitive consumers continue to take a toll on the company and retailers in general.

We have seen **Target** ([NYSE:TGT](#)) enter the Canadian market last year, and although it has been struggling, it represents another competitor that Shoppers has to deal with. This has intensified the competitive landscape, and Shoppers is not alone in feeling the effects. Jean Coutu is also feeling pressure, as the company’s most recent quarter saw overall same store sales growth declining 1.3%.

Loblaw is also feeling the pinch of the consumer, which we saw in its third-quarter results, as profit declined a whopping 29% due to reduced margins. Loblaw’s acquisition of Shoppers Drugmart is expected to strengthen the competitive position of both companies in the marketplace.

The good news for Shoppers is the market share increases it is seeing. On the conference call, management said that the cosmetic business, for example, gained 50 basis points of market share and the food business saw a 30 basis point increase in market share.

Foolish bottom line

The marketplace remains challenging for Shoppers Drugmart, but it appears that Shoppers is very well

positioned within the space. During the quarter, the company acquired five independent pharmacies, and they continue to generate good cash flow. Pharmacy sales account for 44.8% of total sales, and over-the-counter and health products account for 17% of total sales, so we have approx. 57% of sales that are relatively economically insensitive.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:TGT (Target Corporation)
2. TSX:L (Loblaw Companies Limited)
3. TSX:TLRY (Aphria)

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