Target's Canadian Expansion: 14 Months in, Still a Disaster

Description

The other day, I went shopping for new jeans. Because I'm cheap and have zero fashion sense, I walked around the mall a little bit frustrated with the prices charged by some of the specialty stores. I just wanted a pair of comfy jeans that wouldn't fall apart in six months.

And then, I spotted **Target** (NYSE: TGT). It seemed perfect.

I couldn't find any jeans that were inexpensive enough for me, but I still spent a little time walking around the store. Like many of you, I had heard about empty shelves and a poor product mix. I heard about higher prices than the company's U.S. stores and how the Canadian stores were largely empty.

I came away from my shopping trip largely unimpressed. Prices were mostly the same or higher than Target's competitors. While Target has filled some of the empty shelves, it's still pretty easy to find spots that are just faced forward so they appear full. The store wasn't busy, but neither was the mall in general, since it was during the middle of the day on a weekday.

In Target's defense, there were still plenty of things this particular store was doing right. The store was sparkling clean, and merchandise was presented well. There were plenty of staff around. Areas like clothes, shoes, and electronics hardly had any empty shelves. The company has also stated that customer surveys indicate that it's making improvement in a lot of these key areas.

But while Target gets its act together in the Canadian market, it's costing the parent company a bunch of money. Since opening more than 100 locations in Canada starting in March of last year, the U.S. parent has recorded losses from operations of more than $1 billion.

Once you combine weak Canadian results with Target's now infamous data breach, it creates a bearish situation for the stock. And to add insult to injury, Target decided to part ways with its CEO, Gregg Steinhafel, who had been with the company for more than 35 years.

Steinhafel's departure creates doubts that Target is even going to continue in Canada. A new CEO could come in and clean house, getting rid of all the mistakes of the previous regime. This seems unlikely considering the company's investment, but we could certainly see store openings slow until results start to get significantly better.

Target still has ambitious plans for Canada. It continues to forecast $6 billion in nationwide sales and 80 cents per share worth of earnings by 2017 for its Canadian operations. At this point, these projections seem pretty ambitious.

It's obvious Target underestimated its Canadian competitors. Both **Loblaw** (TSX: L) and **Empire Company** (TSX: EMP.A) responded to Target's entry into the market by bulking up, acquiring Shopper's Drug Mart and Safeway, respectively. By getting larger, these competitors can put pressure on suppliers to cut product costs.

Wal-Mart (NYSE: WMT) continues to expand in Canada, converting regular stores into larger Superstores. But still, even it is suffering from stagnant same-store sales. Competition is just that intense in Canada.

As the new entrant in the country, Target has to overcome all these competitors on its way to gaining market share. If you combine that with its operational weakness, Target has some significant issues to overcome on its way to good results in Canada.

Investors looking for exposure to Canadian retail would be better off to look at other companies. Target is struggling with operational issues, strong competition from existing chains, and has the added weight of the data breach scandal. There's even the risk that the company might put the brakes on its Canadian expansion. Target has a lot of work to do before it can be a truly dominant Canadian retailer.

CATEGORY

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1. NYSE:TGT (Target Corporation)
2. NYSE:WMT (Wal-Mart Stores Inc.)
3. TSX:EMP.A (Empire Company Limited)
4. TSX:L (Loblaw Companies Limited)

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