2 Reasons to Avoid Canadian Tire Corporation Limited, and 1 Stock to Buy Instead

Description

The last couple of years have been very kind to shareholders of **Canadian Tire Corporation** (TSX: CTC.A). Since the beginning of last year, the shares are up a whopping 64%.

So is there still room for this stock to run? Well, not necessarily. Below, we show two reasons to avoid the shares of Canadian Tire and one stock you should buy instead.

1. Limited growth opportunities

If you look at Canadian Tire's flagship stores, there are very few opportunities to add new ones. To illustrate, there were 457 such stores back in 2004. Today, there are 491, good enough for a 0.7% annual growth rate. This is understandable — Canadian Tire has been around for 90-plus years, and has pretty much covered the entire country. In fact, over 90% of Canadians already live within 15 minutes from a store. And there is no way the company will expand into the United States, having failed at that twice already.

Making matters worse, competition is always intensifying. While **Target**'s entry into Canada has been a flop, other players, such as **Wal-Mart** and **Amazon**, pose a bigger threat long term.

Tire does have opportunities to grow, but these mainly come from its other banners, such as Mark's and Sportchek. Even with promising results recently, Tire's revenue only increased by 3% last year.

2. Fully priced

At the beginning of last year, there was a perfect opportunity to buy Tire shares. The company's real estate value was not recognized by the market. Neither was its credit card portfolio. And investors were fearful of Target's entry into Canada.

But all of those issues have been flipped on their head, which is why the stock is up so much. And at this point, Tire trades at over 15 times forward earnings (according to Morningstar). That's a high price to pay for a company with limited growth prospects and increasing competition. The company also has a fairly low dividend, still yielding less than 2% despite a couple of recent raises.

1 stock to buy instead: Dollarama

Like Canadian Tire, **Dollarama** (TSX: DOL) has also been very rewarding to investors. Over the past five years, the stock is up nearly 400%. But unlike Canadian Tire, there is still plenty of room for growth.

This was highlighted by a report from Moody's earlier this year, when it said that Canada can still absorb another 1,000 dollar stores before it reaches the same saturation levels as the U.S. That's good news for Dollarama, which still only has about 900 stores. The company has also been able to increase same-store sales by offering products priced up to $3 — unsurprisingly, Canadians are willing to pay more than a dollar if they feel they're getting a good deal.

And according to Morningstar, Dollarama trades at only 15.4 times forward earnings, about the same as Tire. So when deciding between the two stocks, the choice should be clear.

CATEGORY

1. Investing

TICKERS GLOBAL

1. TSX:CTC.A (Canadian Tire Corporation, Limited)
2. TSX:DOL (Dollarama Inc.)

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