


## Is Dollarama Inc the Top Canadian Retail Stock to Buy Today?

### Description

**Dollarama Inc.** ([TSX: DOL](#)), the leading dollar store operator in Canada with more than 900 locations across the country, has watched its stock rise steadily in 2014, but it has widely underperformed the overall market.

This underperformance has not been a result of weak earnings, as the company has released three very strong earnings reports during the year, including the two most recent quarters in which earnings per share rose more than 25%. This type of situation usually signals a buying opportunity, so let's take a look at the most recent earnings release and check on the stock's valuation to determine if it represents a long-term investment opportunity today.

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Source: *YCharts*

### Strong results cause little movement in the stock

On September 11, Dollarama released its second-quarter report for fiscal 2015. It showed significant growth from the year ago period, but was mixed compared to expectations. Here's a breakdown.

Metric	Reported	Expected	Year-Ago
Earnings Per Share	\$1.03	\$1.03	\$0.82
Revenue	\$572.60 million	\$578.86 million	\$511.32 million

Source: *Dollarama and Markets.FT.com*

Earnings per share increased 25.6% and revenue increased 12% year-over-year, driven by comparable-store sales rising a very impressive 4.2%. Larry Rossy, Dollarama's Chairman and CEO, stated that the success of the company is attributable to its focus on organic growth in the Canadian market and improved operational effectiveness and efficiency.

Dollarama's gross profit increased 10.3% to \$206.57 million and operating profit increased 17.6% to \$99.24 million during the quarter, and in relation, its gross margin contracted 50 basis points to 36.1% and its operating margin expanded 80 basis points to 17.3%.

The contraction of the company's gross margin is a direct result of the cost of sales increasing 12.3% and the expansion of the operating margin can be attributed to selling, general, and administrative expenses increasing just 7% from the year-ago period. The margins are currently within management's expectations for the year, but investors would prefer both to show improvement in the second half.

Net cash provided by operations totaled \$106.9 million for the quarter and \$14.9 million was spent on capital expenditures, resulting in a healthy \$92 million of free cash flow. Dollarama used this free cash,

credit, and its \$37.39 million of cash and cash equivalents to pay approximately \$10.86 million in dividends and repurchase approximately \$132.34 million worth of its common stock.

In the report, the company also announced that it would be maintaining its quarterly dividend of \$0.16 per share and it will be paid out on November 4 to shareholders of record at the close of business on October 2, giving it a yield of about 0.68% at current levels.

Lastly, in terms of expansion, 18 new stores were opened during the quarter, bringing Dollarama's total count to 917. The company has opened 43 stores to date in fiscal 2015, putting it on pace to reach its goal of 70-80 new stores for the year.

Overall, it was a fantastic quarter for Dollarama, but its stock reacted by rising just 0.63% on the day of the announcement and it has since fallen back below these levels. It may have seemed as if a spike higher was imminent, but since this did not happen, let's find out if the valuation of the company's shares was too rich to support a rally.

### **Are Dollarama's shares undervalued, fairly valued, or overvalued today?**

As of today, Dollarama's stock trades just a few points below its 52-week high of \$96.67 reached back in June of this year, has a healthy dividend yield of 0.68%, and trades at 24.3 times trailing-12-months earnings. According to YCharts, Dollarama's five-year average price-to-earnings multiple is 22 and its multiple has been in the range of 23.5 to 26.5 over the course of 2014, allowing me to draw the conclusion that shares are fairly valued today.

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*Source: YCharts*

Even though I feel the shares are fairly valued, as long-term investors, we care much more about where the stock is going than where it is today. Dollarama trades at 21.5 times fiscal 2015's estimated earnings per share of \$4.33 and just 18.5 times fiscal 2016's estimated earnings per share of \$5.06; if shares continue to trade at a multiple of 22, this could place shares upwards of \$111 by the conclusion of fiscal 2016, representing significant upside from today's levels.

Investors should not invest based solely on earnings forecasts or share price projections, but Dollarama is a proven performer in the Canadian retail market and its track record adds supports.

**Is Dollarama a buy?**

I believe Dollarama represents a great long-term buying opportunity today. The company has continued to show significant earnings and revenue growth, and I think it will continue to do so, allowing its stock to rise to fresh all-time highs over the next several months. Foolish investors seeking an investment in the Canadian retail market should take a closer look and consider initiating positions immediately.

## CATEGORY

1. Investing

## TICKERS GLOBAL

1. TSX:DOL (Dollarama Inc.)

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1. Investing

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