Why Hudson's Bay Company Could Win Big From Target's Canadian Closure

Description

Shares of **Target Corporation** (NYSE:TGT) are up this morning as the company announced it was finally going to pull the plug on its troubled Canadian operations.

For investors closely following Canada's retail sector, this news isn't much of a surprise. Target's struggles in Canada are well documented and, frankly, inexcusable. The company struggled with pretty basic things like inventory control, leading to frustrated shoppers who walked up and down the aisles of a store that was mostly empty. It's hard to compete with some of the best retailers in the world when there isn't even enough stock to fill the shelves.

Company execs always just assumed things would get better, but shoppers simply got frustrated and stopped going. I visited a Target store in Calgary just after Christmas which was new, bright, and located in a busy shopping area. The inventory issues had also improved, although not to the point where it was comparable to a **Wal-Mart** store.

And yet, the store was empty.

Management confirmed all this when they took a hard look at the company's operations. According to the press release, Target confirmed that based on what management termed as "realistic expectations," it's Canadian stores wouldn't be in a position to break-even until 2021 at the earliest. Rather than pouring more billions into Canadian operations that have already lost close to $2 billion, the company pulled the plug and filed for bankruptcy protection in Canadian courts.

Now that Target has officially announced it's leaving Canada, how should investors play this? Personally, I think there's an obvious option — **Hudson's Bay Co** (TSX:HBC).

Hudson's Bay has a history with almost all of Target's locations, since it was the company that sold Target the leases in the first place, killing the Zellers chain in the process. If anyone knows the pros and cons of each of those spots, it's Hudson's Bay management.

Plus, Hudson's Bay can easily bring back the Zellers brand. Canadians know it, with most of us having grown up with Zpoints and Zeddy the Bear. The company also competed with Wal-Mart in the

Canadian market for nearly two decades before closing its doors for good in 2012.

Plus, Hudson’s Bay’s current chairman (and ex-CEO) has a history of buying real estate when nobody else wants it. Richard Baker first acquired Hudson’s Bay and Zellers in 2008 for $1.1 billion. By 2013 he had sold the Zellers real estate for $1.8 billion and the company’s flagship location in Toronto for $650 million. That’s not a bad return, plus the company still retained all of its Hudson’s Bay stores and most of its valuable Canadian real estate.

Then, in 2013, Baker did it again. Hudson’s Bay acquired Saks Inc. for $2.9 billion, including $500 million in assumed debt. In November, the company announced that the crown jewel in Saks’s real estate empire — the Saks Building in New York City — was alone worth $4.1 billion.

It’s obvious Baker has the skill to identify undervalued retail real estate.

Hudson’s Bay management has strongly hinted that the company plans to spin off its valuable real estate into a REIT, even going as far as hiring the CFO who was with **Empire Company** when it repackaged its stores as a REIT in 2006. This would likely raise billions, since estimates are the company’s real estate is worth some $7-$8 billion. Even spinning off a quarter of the company’s real estate would likely be enough to to buy Target’s Canadian locations back. I don’t think it’s in a position to really negotiate that hard.

For investors looking to profit from this, Hudson’s Bay Company looks like a pretty good choice. We’ll see if Baker can pull his magic one more time.

CATEGORY

1. Investing

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1. NYSE:TGT (Target Corporation)

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