Is Dollarama Inc. the Best Retailer in Canada?

Description

Since the company had its IPO back in late 2009, it's been good to own shares of **Dollarama Inc.** (TSX:DOL).

Shares have surged, rising more than 730%, and that's not even including dividends. Same-store sales have done well, the company has continued to expand and open new stores, and management successfully transitioned from only selling items worth a dollar to merchandise up to $2 and $3 in price.

Personally, Dollarama is one of my favourite stores to visit. Often, I'm searching for something disposable that I might only need to use once or twice. I'm not willing to pay top dollar for something I don't really value, so the chain's emphasis on value is enticing. The numbers show I'm obviously not the only one who thinks that way.

But as we all know, investing based on just the past isn't ideal. The future is much harder to predict, but the payoff is potentially very rewarding. Here are the three reasons why I think Dollarama's best days are ahead.

Further expansion potential

Dollarama has come a long way since it was a single store in a Quebec strip mall in the early 1990s.

These days the company boasts a store count of over 900, with plans to push that number to 1,000 as early as next year. Medium-term plans are to boost that number closer to 1,200 by the end of the decade.

According to an analyst report issued last year, that might just be the beginning. Estimates are that Canada can handle another 400-700 additional dollar stores over the medium-term, with potential to support another 1,700 over the next decade or two. That would put Canada at about the same penetration per capita as the United States.

There's also international expansion potential. Currently, Dollarama has a pilot project in place with a 15-store chain in Central America called Dollar City to provide it with merchandise and managerial support. If the company is satisfied with the way things go, it has the option to buy the whole chain outright in 2019.

Terrific results

Dollarama bears keep expecting the company's results to come back down to earth at some point, but the company keeps on delivering.

In the most recent quarter, Dollarama delivered a 13% sales increased, buoyed by same-store sales that were up 6.9% compared with the same quarter in 2014. Gross margins expanded to 36% compared with 35.4% last year. Both EBIDTA and operating income grew more than 22%, and net earnings per share went from $0.39 per share to $0.50 per share.

Analysts have high expectations over the next couple years as well. Earnings are expected to grow to $2.64 per share this year, while hitting $3.10 per share next year. Yes, that puts shares at a very expensive 30.75 times this year's expected earnings, but that's how multiple growth gets in today's market. And if you're a believer in the company's ability to continue to grow, in a couple of years, earnings will be much higher and the price-to-earnings ratio won't look so bad, at least on a cost basis.

Potential recession?

For most businesses, economic weakness is bad news. Customers lose confidence, which leads to them closing their wallets.

For Dollarama, recessions are actually good. Customers seek lower-cost merchandise, desiring to stretch their budget a little further during tough times. And what better place to shop during tough times than a store that doesn't have anything for sale over $3?

What happens during a recession is folks move to cheaper options. Former shoppers of high-end stores will shop at mid-range stores. Mid-range shoppers will filter down to Dollarama. Current Dollarama shoppers can't go much further down, so they stick around.

Dollarama is a great retailer, and there's easily the argument to be made that it is Canada's best retailer. But investors have to be careful of the valuation. If I owned the stock, I'd make sure I kept a trailing stop loss on my shares, just in case it ever posts disappointing numbers and it reacts accordingly.

CATEGORY

1. Investing

TICKERS GLOBAL

1. TSX:DOL (Dollarama Inc.)

Category

1. Investing

Date
2025/07/08

Date Created
2015/08/19
Author
nelsonpsmith