Why Lowe’s Companies, Inc. Buying Rona Inc. Is Good Business

Description

Lowe’s Companies, Inc. (NYSE:LOW), showed the market last week that persistence has a way of paying off, and when it comes to making an acquisition, it is all about timing.

The home improvement giant approached **Rona Inc.** (TSX:RON) with a $3.2 billion offer that was approved. The deal, which is the second attempt by Lowe’s to acquire Rona in recent years, represents in price nearly double of what Rona’s stock was worth last week when the deal was announced.

Lowe’s tried purchasing Rona back in 2012 and was unsuccessful. Back then the Canadian dollar was trading nearly at par with the U.S. dollar and was worth approximately $1.76 billion, or a 37% premium over what Rona’s stock was trading at the time.

Nonetheless, that offer was rejected, both from within Rona’s management, which cited that a sale wasn’t in the best interest of the company, and from the Quebec government, which at the time labeled Rona as a strategic asset and that ownership should remain in Canada.

Let’s take a look at what this acquisition means for Lowe’s and the company’s operations in Canada.

A larger geographic footprint

Lowe’s has experienced slow, steady growth in Canada since crossing into the market in 2007. The company currently has a total of only 42 stores, mostly in Ontario. Lowe’s has taken a very conservative and cautious approach to expansion in the Canadian market, and with good reason as the examples of both **Sears Canada** and **Target Canada** can allude to.

Lowe’s currently has no store locations in Quebec. Rona on the other hand, has a majority of the 236 corporate and 260 dealer-owned stores operating in Quebec.

Apart from Lowe’s own footprint in the country, the completion of this deal will mean that Lowe’s will unseat **Home Depot** as the largest home improvement store chain in the country.

Increased revenue is possible

Lowe’s stated that the company had identified several ways in which it could increase profitability in Canada, citing a $1 billion increase in revenue that could be realized through the addition of new products that are noticeably absent in Rona stores (such as appliances) and through implementing savings by sharing suppliers.

Rona is different from other home improvement stores in that it offers store sizes and configurations that are vastly different from one another, serving the needs of that particular local market. This is one aspect of the company that has proved successful for Rona, as a greater penetration into smaller markets was possible where the bigger store formats that Lowe’s is accustomed to would not be feasible. It will be interesting to see how or if Lowe’s decides to change this model.

The deal, which still has to pass through the competition bureau, is expected to close in the second half of the year. Lowe’s expects the revenue from the Canadian stores to represent nearly 7% of total annual revenue.

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