Dollarama Inc.: A Perfect Buy-and-Hold-Forever RRSP Stock

Description

Millions of Canadian investors will collectively put billions of dollars to work this month as financially responsible folks everywhere rush to get their RRSP contributions in by the February 29th deadline.

For many investors, the sheer number of choices can be overwhelming. And with stocks down considerably over the last year, many are anxious. They don't want a repeat of 2015's lacklustre results. The combination of these two factors can lead to a frustrating outcome: indecision.

Many investors will just stick their cash in a mutual fund, which is not a great idea. Because of their high fees and the behaviour of fund managers (who often sell when they should be buying, and vice versa), mutual funds are almost guaranteed to underperform the market.

Instead, investors should find great stocks, buy them on dips, and forget about them for a decade or three. It might seem counterintuitive, but buying the best companies and doing nothing is one of the easiest ways to get rich. Warren Buffett wouldn't continue to recommend it if it didn't work.

The only thing left for an investor to do is to pick the companies they want to own. Here's the case for making **Dollarama Inc.** (TSX:DOL) a key holding in any portfolio.

Temporary weakness

From the company's IPO in 2009 until the latter part of 2015, Dollarama was on what seemed to be an unstoppable run. Split-adjusted shares soared from the $9 IPO price to $93, an increase of more than 900%.

The last few months have seen the stock go down significantly for the first time. From the peak, shares are down some 25%, closing at $71.60 on Friday.

Most of this weakness seems to be a reflection of the overall market. A year ago Dollarama posted quarterly results showing that it earned $73 million on revenue of $588 billion, good enough for $0.55 per share. In its most recent quarter, revenue increased to $665 million and profit came in at $100 million, which works out to $0.78 per share.

The growth is there; we're seeing it in the results. The market is just pessimistic about most stocks–Dollarama included. That should change as overall sentiment improves.

Great strategy

The weakening of the Canadian dollar has been a big deal for Dollarama. The company sources most of its products from China, a country which pegs its currency against the U.S. dollar. Thus, costs have gone up.

In response, Dollarama did what every other retailer does–it increased prices. It introduced $2 and $3 price points on certain items and customers didn't even blink. In fact, most customers were excited about the new products stores brought in at those prices.

Investors are missing what could be a great long-term trend for Dollarama. At some point the Canadian dollar will strengthen again. This will improve the company's margins, which are already among the highest in the whole retail sector.

Growth potential

According to analyst reports, Canada can handle many more dollar stores than we have now, at least based on trends currently happening in the U.S. market. This bodes well for the company's long-term expansion plans, which includes a planned 500+ stores. That's a big deal for a company with approximately 1,000 stores now.

Canada isn't the only market with opportunity. Dollarama struck a deal with Dollar City, a chain of approximately 15 dollar stores in El Salvador. Dollarama receives fees for managing the smaller company's logistics and helps supply it with products. Included in the arrangement is an option to buy the Central American chain at some point in the future.

There's also great potential for Dollarama to grow its dividend. Shares currently yield an anemic 0.5% on a $0.09 per share quarterly dividend. Over the last year the company earned $2.77 per share, a payout ratio of just 13%. Dollarama is growing fast enough today for it to increase the dividend handsomely each year without increasing the payout ratio. That bodes well for upcoming dividend increases.

Dollarama is a terrific buy-and-hold-forever stock. It's a natural choice for a long-term investor's RRSP.

CATEGORY

1. Dividend Stocks
2. Investing

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1. Editor's Choice

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