If You Don’t Buy Dollarama Inc., You’ll Be Kicking Yourself Later

Description

There are very few true growth stocks in Canada.

There are a myriad of reasons why. Our economy is mature, so companies can’t just ride GDP growth any longer. Various pockets of the country are really struggling. And we tend to focus more on large-cap stocks, even though major growth tends to be behind a company once it enters the TSX 60 index.

Investors have reacted in a pretty predictable way. Large-cap, true growth stocks tend to attract huge premiums simply because there aren’t many of them. P/E ratios stretch up to the sky as investors become comfortable paying for growth they anticipate will happen.

The big issue for investors is trying to figure out whether the growth is sustainable or whether it’ll lose steam. If growth continues, so will a stock’s march higher. If it doesn’t, look out below.

That’s the conundrum facing **Dollarama Inc**. (TSX:DOL) investors. The stock has been one of the best performers on the TSX since its 2009 IPO, rising more than 700% in the six-and-a-half years since.

Will the stock continue its historic rise? Let’s take a closer look.

A buying opportunity

For the first time in its history as a publicly traded company, Dollarama shares are significantly below their 52-week high. Shares peaked at the $93 level back in October, only to decline with the rest of the market sell-off. Shares are currently hovering around the $80 mark.

Underlying results still look really good. In the company’s most recent quarter, total sales increased 13% compared with the same period last year. Same-store sales, a key metric in the world of retailers, were up 6.4%. Gross margin increased to 40%, and EBITDA margins increased to 23.3%.

In total, earnings were up 41.8% from $0.55 to $0.78 per share. Over the last 12 months, earnings came in at $2.77 per share, a terrific result considering that the low Canadian dollar made it more expensive for the company to import inventory from places such as China.

This next year should be even better. Dollarama is expected to earn $3.22 per share in the company's fiscal 2017. That's only a 16% increase in earnings, even though the most recent quarter saw a jump of 42%. It's easy to see why investors think analysts might not be giving Dollarama the credit it deserves.

If we believe the numbers that analysts predict for this year, shares of Dollarama are trading at nearly 25 times forward earnings. That is expensive, even in a world where interest rates are just above zero. But Dollarama shares have traded at a high multiple for the company's whole existence as a publicly traded company.

In the company's fiscal 2015, it earned $2.21 per share, yet it was trading at $70 shortly after those results were released. That's 31.7 times trailing earnings. If Dollarama hits analyst predictions for earnings of $3.22 per share and trades at the same valuation, shares would be worth $102 in April 2017.

Expansion potential

Dollarama has a great deal of opportunity to expand at home or abroad.

Let's start inside Canada. There are approximately 1,000 stores here at home. The company opens some 75 new stores a year, and there is little indication of it slowing down. Analysts estimate that the company could open anywhere from 500 to 1,000 additional stores and still stay under saturation levels seen in the U.S., depending on what competitors do.

Internationally, the company has an interesting opportunity in Central America that has flown under the radar. It struck a deal back in 2013 to provide inventory and operational assistance to Dollar City, a chain of approximately 15 stores in El Salvador.

These days, Dollar City has expanded to 25 stores, and most analysts agree it's only a matter of time until Dollarama exercises its option to buy the chain. The dollar store concept is just beginning to catch on in the region, which means lots of potential growth once the company really turns its focus down south.

With strong Canadian growth anticipated and further potential in Central America, it's easy to see how Dollarama could continue to be a growth story for years to come. It's not too late for investors to get in on this ride.

CATEGORY

1. Investing

TICKERS GLOBAL

1. TSX:DOL (Dollarama Inc.)

Category

1. Investing

Date
2025/09/11
Date Created
2016/03/22
Author
nelsonpsmith