The Strengthening Loonie Boosts Canadian Tire Corporation Limited and Other Canadian Retailers

Description

The Canadian/U.S. dollar exchange rate is bumping off the US$0.80 level in recent trading sessions after trading at lows of US$0.68 in January of this year. It's a pretty significant and not entirely expected move that's taken the market by surprise.

And with this type of move, there are companies that will benefit, such as Canadian retailers with the bulk of their products being sourced in U.S. dollars. **Canadian Tire Corporation Limited** (TSX:CTC.A), which hit a 52-week high this week and has a three-month return of 29.6%, is one such company.

With a significant portion of its products being purchased in U.S. dollars, profitability had been negatively impacted when the dollar was weakening. However, the company has been working on improving productivity and efficiencies and has offset this.

So even with the weak Canadian dollar, the company posted stellar 2015 results with same-store sales growth of 3.2% at Canadian Tire, 4.4% at FGL Sports, and pretty much flat growth at Mark's. Diluted EPS increased 13.5% for the year and 8.4% on a normalized basis. In the retail segment, gross margins for the year and the fourth quarter increased to 30% and 31.9% respectively, from 28.9% and 30.5% in the prior year. If the Canadian dollar continues to strengthen, we should expect to see a positive impact on margins.

Dollarama Inc. (TSX:DOL) also benefits from the stronger dollar as most of its products are sourced in China and priced in U.S. dollars. The stock appears to be reacting to the strength in the Canadian dollar as well and has a three-month return of 25%.

Recall that with the weakening Canadian dollar last year, the company felt the need to pass on some of the increased expenses to customers by increasing the pricing on some of its items. The problem with this is that as prices rise, it moves the retailer into the same space as other discount chains and leaves it competing squarely against retailers like **Wal-Mart**, for example. I think this changes the competitive environment for the company and the value proposition.

So the strengthening Canadian dollar is good news for Dollarama. In fiscal 2016, same-store sales increased 7.3% and gross margin increased to 39% versus 36.9% in the prior year. Dollarama continues to surpass expectations, and while it is still trading at lofty valuations, the stock should nevertheless continue to get a boost in a strengthening Canadian dollar environment.

In summary, here we have two solid companies that are producing stellar results that will get a nice boost should the Canadian dollar stabilize and continue to strengthen. Consider both stocks for your portfolio.

CATEGORY

1. Investing

POST TAG

1. Editor's Choice

TICKERS GLOBAL

1. TSX:CTC.A (Canadian Tire Corporation, Limited)
2. TSX:DOL (Dollarama Inc.)

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