



## The Retail Stock Nobody's Talking About

### Description

**Canadian Tire Corporation Limited** ([TSX:CTC.A](#)) stock is on a roll in 2017 and is up 10.7% year to date — 863 basis points better than the S&P/TSX Composite Index.

Hasn't anyone told Canadian Tire investors retail is in a funk?

Well, whoever you are, I'm sure you're invested in Canada's most iconic retailer for exactly that reason — in times of difficulty, it pays to own quality. Canadian Tire is just that.

Recently, I read in a Canadian retail blog about value-priced retailer Old Navy and the fact it was expanding its store footprint in Canada. Currently operating 78 Old Navy stores here, it's planning to open eight in 2017 and another 14, perhaps more, by 2020.

We've already seen the huge growth trajectory that **Dollarama Inc.** ([TSX:DOL](#)) has been on the past few years as retail has skewed high and low, while virtually eliminating the middle. **TJX Companies Inc.** ([NYSE:TJX](#)), a U.S. multi-brand off-price retailer operating Winners, Marshalls, and Home Sense in this country, is also doing brisk business, highlighting Canadian shoppers' desire for good value.

Old Navy clearly wants to take advantage of this trend; given it's the best-performing brand for **Gap Inc.** ([NYSE:GPS](#)), Old Navy's parent company, I wonder if the value-priced division's enthusiasm is rubbing off on its two other brands.

Gap stock has had an incredibly rocky 12 months, twice blowing through \$30 only to retrace its steps into the low \$20s or high teens. Currently trading around \$24, I believe this is the retail stock nobody's talking about but should be; here's why.

In February, Gap reported its strongest quarter in a long time, registering a 2% same-store-sales increase, the first since CEO Art Peck took over two years ago.

"We believe fundamentally, there is a significant market share opportunity [ahead of us]. To read the headlines today, you'll see the words dead, dying, sick. We are none of those. We are healthy and strong and have a plan and clear direction," Peck said during Gap's Q4 2016 conference call. "But we

can all pick our favorite company that's no longer in business and when the lights go off and the windows get boarded over, that is market share that is made available to the rest of the industry. She's not stopping shopping. She's shopping someplace else."

He's so right.

I just wrote about the **Hudson's Bay Co.** (TSX:HBC) M&A [rumours](#), which seem to have it buying everything but the kitchen sink. Former Neiman Marcus executive Steven Dennis made a very interesting observation in *Forbes* magazine; specifically, while Neiman Marcus generates 31% of its revenue from e-commerce, it comes at the expense of its brick-and-mortar stores, what he terms "channel shift."

That's exactly what Peck is talking about.

In the Gap conference call, Peck reminded those listening in that the apparel business is still growing between 2% and 5% annually and will continue to do so for the foreseeable future.

It's one thing if the industry is contracting, but that's just not the case. Gap intends to go after market share both by taking it from retailers who close their doors and creating it through better merchandising and reasonable prices.

That's why Old Navy is expanding in Canada. There's market share to be had.

Globally, Old Navy has close to \$7 billion in annual revenue and has grown sales for five consecutive years. It finished fiscal 2016 with fourth-quarter and December same-store sales growth of 5% and 12%, respectively. The rest of its business, I'll grant you, wasn't nearly as robust, but overall its business is headed in the right direction.

Earnings might not look so hot right now and into the first half of 2017, but come the holidays, things should be doing just fine.

What I see is a business that generated \$1.2 billion in free cash flow in 2016 — 37.7% higher than a year earlier, despite a second consecutive year of declining revenue. Its free cash flow yield is a very attractive 12.5% — four times higher than iconic Canadian Tire.

As Warren Buffett says, "Price is what you pay; value is what you get." Gap provides far more value than Canadian Tire does at current prices.

## CATEGORY

1. Investing

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1. NYSE:GPS (The Gap, Inc.)
2. NYSE:TJX (The TJX Companies, Inc.)
3. TSX:CTC.A (Canadian Tire Corporation, Limited)
4. TSX:DOL (Dollarama Inc.)

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