3 Things Investors Can Learn From Sears Canada Inc. Bankruptcy

Description

The TSX will delist **Sears Canada Inc.** (TSX:SCC) shares on July 28. Currently suspended from trading by the index, the last shares exchanged at 62 cents. The bankruptcy proceedings likely make them worthless.

An online boycott on **Twitter** is making the rounds — #BoycottSearsCanada — protesting the department store's failure to pay severance to long-time employees, some with as many as 40 years of service to the company, while paying $9.2 million in retention bonuses to key staff responsible for closing the 59 stores affected by its bankruptcy plan.

We should be calling for change

It's understandable that we as Canadians are upset about the shoddy treatment of long-time Sears employees, including Mike Myers' brother Peter, who was let go after 36 years with the company and missed out on approximately 24 months of severance.

That's a hard pill to swallow, and while the laws should be changed to protect employees in these situations, if the remaining employees have any hope of keeping their jobs, a boycott of Sears Canada is the last thing that they need as a show of support.

Rather than trying to send a message to the executives of Sears Canada and its board, we should be writing our MPs, MPPs, and anyone else that can change the bankruptcy rules in this country to put employees on the same level as secured creditors. It's that simple.

But enough about politics. Here are five things investors can learn from Sears Canada's demise as a publicly traded company.

1. Do not invest in money-losing businesses

In fiscal 2011, Sears Canada announced a $50.9 million operating loss, its first in years, if ever. That should have set off an alarm in your head that things weren't perfect at the department store. The next year, when it announced an even bigger operating loss of $82.9 million, you should have been out, especially if you're averse to risk.

You know what they say about a business with strong earnings and little or no debt? It's not going to go out of business anytime soon.

2. Avoid investments run by private equity

Although Sears Canada was no longer directly owned by its U.S. parent, Eddie Lampert, **Sears Holdings Corp.'s** (NASDAQ:SHLD) CEO, owns 45% of the Canadian operation through his hedge fund, ESL Investments, which also owns 48% of the parent as well as a significant amount of debt.

Regardless of what happens to Sears Canada and Sears Holdings, he'll likely still do well when all is said and done, and both companies are dead and buried.

I have seen hundreds of examples of companies bought by private equity firms who suck every last dime out of them and then leave their rotting carcasses by the side of the road, moving on to the next road kill.

Rare exceptions like **Dollarama Inc.** do exist, where private equity hasn't killed the goose that laid the golden egg, but they are rare.

3. Don't fight the trend

The demise of the department store didn't just happen. Other chains, like **Macy's Inc.,** have seen their businesses slowly erode in recent years as consumer shopping preferences changed, whether it be shopping online through **Amazon.com, Inc.** or in brick-and-mortar specialty stores like Sephora.

The moment the departments started using heavy discounting to lure customers into their stores, investors should have realized the jig was up. When macro trends like this develop, whether they're good or bad, you're best to follow them.

Bottom line

While it's sad that so many people are losing their jobs, the cold, hard, underlying economic reality surrounding Sears Canada is that it went bankrupt because Canadians weren't shopping there on a regular basis, which made its cost structure unsustainable over the long run.

Yes, feel sorry for the Peter Myers of the world, but understand that investing, at least in public companies, is about profits and losses, not job creation.

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