

Dollarama Inc.'s Q2: Sales and Debt Levels Continue to Rise

Description

Dollarama Inc. ([TSX:DOL](#)) released its second-quarter results on Thursday, which continued to show strong sales growth for the company with revenues up 11.5% from the prior year, while net earnings are up 24%. Earnings per share of \$1.15 for the quarter are also up from \$0.88 last year.

I will take a closer look at the company's financials to help you assess whether or not the stock is a good buy today

Strong organic growth and expansion has fueled revenues

The company continued to see strong organic growth with comparable store sales increasing 6.1%, which is higher than the 5.7% growth that was achieved a year ago.

Dollarama had a net increase in stores of 17 in Q2, which is also up from a year ago, when the company saw its total stores rise by 13. In one year, the number of Dollarama locations has increased by 7%, or 74 additional stores.

The company's outlook expects a total of 60-70 new stores to be opened in the current fiscal year.

Increase in dollar value of average purchase

The main reason for the sales growth has come from an increase in the average customer purchase, which is 5.9% higher this year compared with a rise of just 4.6% a year ago. The increase in the average purchase could be a result of higher prices for the same items or individuals purchasing a different mix of products. However, the total number of transactions has been flat from a year ago, seeing just a slight increase of 0.2%.

The company continues to repurchase shares and has put equity into the negative

Over 1.3 million shares were repurchased and cancelled by the company at an average share price of \$122.86, which cost the company over \$160 million. With the share price being well above book value, the company continues to drive down its total equity. From over \$100 million a year ago, the company's equity has decreased by almost \$160 million and put it well into the negative.

Debt levels continue to rise

The company has continued to take on more debt with \$1.4 billion in long-term debt this quarter rising 40% from a year ago. With a negative equity, the conventional debt-to-equity ratio will not help us assess the growth, but the debt is currently 78% of the company's total assets, which is up from 56% a year ago.

Total financing costs of \$10 million are up from just \$7 million a year ago for an increase of 40% year over year.

Is Dollarama a good buy?

Dollarama has achieved strong sales and profit growth as it continues to expand and see average purchases rise. However, there are several concerns that would prevent me from investing in the stock.

First, the company's aggressive share repurchases have eroded shareholders' equity and put it into a negative position. The purchases in some quarters have even been higher than the company's cash flow from operations.

Second, debt levels are rising at a high pace, and as interest rates rise, these costs will continue to do so as well and will erode future profitability.

Third, minimum wage increases could also have a significant impact on the company's bottom line.

Lastly, I don't believe the company's business model will survive long term. It's been a long time since Dollarama was truly a dollar store as its prices continue to rise and negate its advantage over big-box retailers.

In the short term, you could make a good return on the share price if hype propels the stock price up, but long term, the concerns outweigh the company's growth prospects.

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