Loblaw Companies Ltd. Is Down 15% in 3 Months: Should You Buy?

Description

Loblaw Companies Ltd. (TSX:L) has seen a significant drop in its share price in the past three months. I'm going to have a look to see if it is a good time to invest in one of Canada's strongest brands.

Why has the share price declined so much?

The company released its earnings in July, but the stock had already started to decline well before then. One of the bigger stories in mid-June, around the time the stock started its descent, was a video showing employees from one of Loblaw's suppliers abusing chickens, which raised animal welfare issues and concerns. Later in the week, the stock lost over 3% of its share price.

Towards the end of July, the company also released its Q2 earnings, which saw Loblaw post revenue growth of over 3%. The company also saw its bottom line more than double from the previous year. This should have been good news for the company, except that Loblaw also cautioned investors that the planned minimum wage hikes in Alberta and Ontario would inflate its labour costs by approximately $190 million in the following year. Note that this was before B.C. had announced it too would be raising its minimum wage, although that increase is not likely to happen until after 2021.

Will minimum wage hikes make Loblaw a bad investment?

The concern of rising labour costs is likely the key driver that has pushed the company's share price down, and that momentum has kept it from recovering. However, these are industry conditions that Loblaw cannot control, and it is not likely to even be the most impacted company in the industry either.

A company like **Dollarama Inc.** (TSX:DOL) which is even more focused on low prices will see a greater impact given that its employees are more likely to make minimum wage. Any increase in cost will hurt the bottom line, as the company will either absorb the expenses or increase prices, which could drive consumers away.

Ultimately, Loblaw's bottom line might suffer, but, in all likelihood, the minimum wage hike will just result in higher prices, and consumers will end up paying for the increased wages. As a news story, it sounds bad, but it may also be a political move on the part of Loblaw to put pressure on governments to think twice about wage increases, while also giving the company an excuse to justify future price increases.

Should you buy the stock today?

With **Empire Company Limited** (TSX:EMP.A) trading at a multiple of 33 times its earnings, and Dollarama trading at 36 times, Loblaw's price-to-earnings multiple of 21 looks like a bargain. The company also trades at only two times its book value. In the long term, Loblaw has a much brighter future and is less likely to be impacted by the adverse industry conditions than some of the other retailers I have mentioned here. However, with the stock dropping over 5% in value in the past month, I would wait for some stability or even a recovery in the price before buying the shares, but Loblaw is definitely a strong investment going forward.

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