

Dollarama Inc. Shares Keep Rising: Should You Buy or Sell?

Description

In a retail world where companies are filing for bankruptcy and struggling to generate revenue growth, let alone profitability, **Dollarama Inc.** ([TSX:DOL](#)) stands out all the more, given its impressive run of same-store sales growth and profitability.

[The Canadian retail landscape](#) today has seen the once untouchable Sears Canada fail, and Toys “R” Us, with 85 stores in Canada, file for bankruptcy protection, so it can “restructure its outstanding debt” and get back on a path toward long-term growth, as **Amazon.com, Inc.** ([NASDAQ:AMZN](#)) and the online world have changed the playing field drastically.

Exceptional track record

One thing is certain: Dollarama is a force to be reckoned with. It has an exceptional track record of growth and profitability.

And yes, Dollarama deserves a premium multiple due to its superior performance on a number of metrics.

It has had a 60% increase in revenue since 2013 (for a cumulative average growth rate of 12.3% per year) and an industry-leading 22.6% operating margin, which compares to an operating margin of 2.45% at **Indigo Books and Music Inc.** ([TSX:IDG](#)), 13.8% at **Sleep Country Canada Holdings Inc.** ([TSX:ZZZ](#)), and operating losses over at **Hudson’s Bay Co.** (TSX:HBC), and up until its bankruptcy, Sears Canada.

But at what point are we overpaying?

The stock trades at 32 times this year’s expected EPS, 28 times next year’s EPS, and 24.4 times fiscal 2020’s EPS. Let’s remember, this is a retailer, which is a cyclical and sometimes highly volatile sector.

EPS growth rates going forward, based on consensus expectations, are 19.6%, 16%, and 14.7% for fiscal 2018, 2019, and 2020, respectively, so they are declining, yet the stock still trades at over 30 times.

Same-store sales growth still okay

Same-store sales growth in the latest quarter was 6.1%. This compares to Sleep Country’s same-store sales growth of 7.5% and Indigo’s growth of 5%. Online sales growth at Amazon and in Indigo’s online segment is the 20% range.

In conclusion

I have been [skeptical about Dollarama](#) due to a couple of factors, but mostly due to the stock's valuation. Trading at 34 times trailing earnings, this is no cheap stock.

I've also been skeptical because of the fact that the company has had to institute price increases to protect its profitability, so I concluded that this trend would prove to be bad for its competitive positioning.

But I have clearly been wrong. Investors are willing to pay up for strong performance, and consumers just can't seem to get enough of Dollarama.

The stock has a five-year return of 350% and is still going strong with a year-to-date return of 45%.

So, Dollarama is clearly in the sweet spot, thriving in this retail environment where consumers are looking for inexpensive choices, and benefiting from its ability to keep costs down as it sources its products from China, thereby offering value for the consumers, while still generating strong returns for the company.

But at the end of the day, I still view the risk/reward proposition on the shares as unattractive, so I will remain on the sidelines.

CATEGORY

1. Investing

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1. NASDAQ:AMZN (Amazon.com Inc.)
2. TSX:DOL (Dollarama Inc.)
3. TSX:IDG (Indigo Books & Music)
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