



The Best Grocery Stock to Own in 2018

Description

What a year it's been for **Empire Company Limited** ([TSX:EMP.A](#)) CEO Michael Medline, who took the top job at the beleaguered grocery store chain on January 12, 2017, less than two weeks into the new year.

I doubt he's had much time for vacation over the past 11 months, as he's worked to make Sobeys a more efficient business from coast to coast.

Investors bought into the company's plan, pushing Empire stock up 69% in 2017 through December 12, comfortably outperforming its grocery store peers.

So, can Medline keep the streak alive in 2018? I think he's got a shot, but first, let's consider where all of the participants stand as we close out 2017.

Empire Company's shrinking office staff

It's never easy laying off staff, so it must have been doubly hard for Medline when the company announced November 24 that 800 office jobs were being eliminated through the creation of a national operations structure that reduces employee overlap from the previous regional structure.

A month before Christmas, it's not a great message to send to employees, but it's a decision that had to be made. If Sobeys ever wants to be an efficient grocery store chain from coast to coast, it's got to tighten its back office.

Fool contributor Joey Frenette [wrote](#) in September that he thought investors should wait for a better entry point to buy Empire stock sometime over the next 12 months. At the time, its stock was up 54% year to date; since then, it's gained another 9%, cooling off ever so slightly.

Where to next?

Around the same time as Frenette's article in September, I [wrote](#) that I thought Empire Company was a \$20 stock, but to get to \$30, it needed to improve operating margins and gain market share from both **Loblaw Companies Ltd.**

([TSX:L](#)) and **Metro, Inc.** ([TSX:MRU](#)).

On the former, it's making headway. In the second quarter ended November 4, 2017, its adjusted operating income was 2.3% of revenue — 100 basis points higher than a year earlier.

These will continue to rise with the reduction in office staff, although the headwinds it faces in 2018 — higher food costs, higher minimum wage in Ontario, and more significant competition through **Amazon.com's** purchase of Whole Foods — will reduce the immediate effect the transformation will have on its overall profitability.

Will Empire stock gain another 70% in 2018? I doubt it for the simple reason that it's never traded higher than \$31.

As for market share, it plans to convert up to 25% of its Sobeys and Safeway stores to its discount FreshCo banner over the next five years — a move that it sees delivering all sorts of new customers.

That's a project in its infancy. Investors shouldn't expect possible market share gains until late next year and into 2019.

What about Loblaw and Metro?

To speed this article along, I'm going to reach out to Fool contributor Stephanie Bedard-Chateauneuf, who just happens to have recently [discussed](#) which of the two grocery stores were performing better.

I used to think that Metro was a better operator than Loblaw, but Galen Weston, Jr., is doing a good job preparing the grocery store operations for the headwinds I mentioned above. As a result, its operating margins have been growing the last year, getting closer to the 7.3% operating margin Metro generated in fiscal 2017.

My Foolish colleague believes both are good long-term investments, but Loblaw is better prepared for the changes expected in 2018.

I don't necessarily disagree.

However, now that Metro has sold most of its **Alimentation Couche Tard Inc.** holdings and is focused on integrating Jean Coutu, a move similar to Loblaw with Shoppers Drug Mart, I feel Metro has an opportunity to surprise investors in 2018.

Which is the best grocery stock to own in 2018?

Although I like what Medline is doing at Empire Company, I'm going to go with Metro. It has always been operationally sharp, and I see it doing a good job integrating Jean Coutu into the fold.

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Date

2025/09/30

Date Created

2017/12/16

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