Canada Goose Holdings Inc. Stock Down +16% After Posting Strong Earnings

Description

Canada Goose Holdings Inc. (TSX:GOOS)(NYSE:GOOS) traded as low as 16.68% from its previous close in early trading yesterday after the fast-growing premium apparel designer posted an emphatic quarterly earnings and a revenue beat before market open.

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The company generated revenues of $265.83 million during the last quarter ended December 31, 2017, which were 27.2% better than comparative figures during the same period last year, beating consensus analyst estimates for the quarter by 10.45%.

Quarterly earnings per share at $0.58 were 20.83% better than analyst predictions, while net profit and operating margins continued to grow quarter over quarter.

Gross margins continued to improve from 57.5% in the comparable quarter in 2016 to 63.6% last quarter, as the company continues to reap the benefits of its strategically managed migration from a predominantly wholesale distribution model towards a high-margin direct-to-consumer model through the setting up of several retail stores last year and the launch of seven online stores across three continents during the period.

Why then is the stock down double-digit percentages after a good quarter?

Slower-than-anticipated top-line growth

The revenue growth rate has slowed for Canada Goose. Second-quarter sales were up 34% from a comparable quarter in 2016, while fiscal 2017 revenues were 39% better than fiscal 2016 levels. Therefore, a 27.2% revenue growth last quarter was a bit softer than previous performance, especially considering the extreme cold winter temperatures during the past quarter, which could have tipped the company's revenue scales.

Overpriced?

The stock has been priced to perfection. Canada Goose's trailing P/E ratio had ballooned beyond 120 times earnings per share, which was too high for any retail stock whose niche can be easily invaded by competitors and could suffer heavily should consumer disposable incomes be eroded by higher inflation and increasing interest rates across its target markets.

Profit taking

Most noteworthy, Canada Goose's stock had recently survived and resisted the broader market sell-off where broad market valuations slightly corrected. Investors were more than ready for profit taking after a sustained run on the stock.

The company is also a highly seasonal stock where sales peak during winter seasons. The most recent quarterly revenues were heavily buoyed by an extremely cold winter spell in North America. We may not see that stellar performance in the next two quarters or year.

Possible cannibalization

Canada Goose's sales through the wholesale model declined 2% from $137 million in the comparable quarter in 2016 to $134.2 million during last quarter.

The company explained that this was a result of $18 million in accelerated customer orders delivered during the first half of the year, which were originally meant to be delivered during last quarter but this may not be an encouraging development for a growth stock where investors look forward to accelerating revenue growth from all segments.

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There are new fears that the company's newly deployed retail model may significantly cannibalize wholesale sales and also result in souring relations with traditional wholesale distribution partners, probably leading to slower-than-desired brand awareness and revenue growth.

Investor takeaway

The current plunge in Canada Goose's stock after posting a strong market-beating quarter could be very alarming, but the stock was overdue for a correction after a strong 50% price growth since the last quarterly report that had gone beyond reasonable valuation metrics for a retail stock.

Higher expectations were built in to the stock, and some pundits may have been disappointed by a slower growth rate in the top line. However, there is no reason for a panic sale for long-term shareholders, as there is strong room for a stable recovery over the coming quarters as fundamentals catch up.

It is encouraging to see revenue from the new direct retail distribution model growing 82.78% to $131.6 million from the $72 million realized during the comparable quarter in 2016. Canada Goose is transforming itself into a high-margin designer and retailer of premium-branded apparel through a roll out of new company-operated retail stores and additional e-commerce while exponentially growing its operating cash flow.

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