The Empire Company Limited Strikes Back

Description

Empire Company Limited (TSX:EMP.A) CEO Michael Medline reported the company's Q3 2018 quarterly results March 14; it was the fifth quarterly announcement since Medline was hired a year ago to turn Sobeys around.

And while the numbers were better than expected — adjusted earnings per share were $0.33, $0.20 higher than a year earlier and $0.08 better than analyst expectations — it's important to remember that Medline still has plenty of work to do.

The competition

Now that **Metro, Inc.** has its own pharmacy chain in **Jean Coutu Group PJC Inc.**, and **Loblaw Companies Ltd.** continues to benefit from Shoppers Drug Mart, Sobeys must work harder than ever to convince consumers that it's got a better grocery store experience.

Personally, since I moved to Halifax from Toronto in early February, I can't believe the difference between the local Sobeys to the Atlantic Superstore owned by Loblaw.

Stepping into the Young Street Atlantic Superstore is like being transported back in time to the 1980s. Talk about a shock to the system. Not too far from the Atlantic Superstore on Windsor Street is a nicely put together Sobeys store.

After my wife and I shopped at both locations for the first time, she turned to me and said, "We're shopping at Sobeys from now on!"

If you live in Halifax, you'd be blind not to notice how superior the Sobeys shopping experience is. Sobeys wants to keep its Nova Scotia stores (its head office is in Stellarton) looking good; I'm not quite sure what Loblaw's strategy is for its Maritime stores. They're drab central.

Anyway, when I lived in Toronto, I either went to Metro (it was close) or Longo's. I never much cared for Sobeys. Call me one of the converted.

To keep the turnaround on the rails, Medline will have to convert more of us.

Out west

Last September, I'd argued that Empire was indeed a $20 stock. To get to $30, however, it needed to pull up its socks when it comes to operating margins, and it needed to take market share from its competitors.

However, what it really needed to do, was fix its western stores while also turning itself from a regional into a national operator. By announcing 800 layoffs across the country in November, Medline and Empire had begun the turnaround.

Project Sunrise had four components: Establishing a national corporate structure, reducing costs, focusing on the customer, and finally, fixing its western stores.

How's it done, so far?

On the matter of turning Sobeys into a national, functionally-led structure, it expects to be completed by the end of April. The total one-time costs to implement this structure are expected to be no more than $240 million. However, the restructuring is expected to produce $500 million in annual savings, more than offsetting the one-time costs.

The cost-reduction initiative for Project Sunrise is still ongoing. Some cost benefits come from the organizational restructuring, but others will come from getting better deals from its suppliers as well as introducing greater efficiencies and productivity into the existing business.

Regarding the customer focus, it's launching an online grocery business in the Greater Toronto Area with plans to move into other urban areas over time. It will be interesting how it makes out against Whole Foods and Grocery Gateway.

The other customer-focused move relates specifically to its western stores. The company is converting up to 25% of its 255 full-service Safeway and Sobeys stores in western Canada to its discount FreshCo banner over the next five years. The premise is that some of its stores are unable to generate enough revenue at the full-service price point.

The bottom line on Empire stock

None of the grocery store chains have done much so far in 2018; the minimum wage hikes in Ontario and Alberta are putting investors in a cautious frame of mind.

In December, I'd said Metro was the best grocery stock to own, and so far it's leading the way.

However, everything I see from Empire Company's Q3 2018 results suggests fiscal 2019 could produce juicier profits and a $30 stock price, perhaps by the end of the year.

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