Dollarama Inc. Announces a 3-for-1 Stock Split, a 9% Dividend Increase, and Booming Sales

Description

In a retail world where we are seeing companies 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 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.** has changed the playing field drastically.

But Dollarama just keeps going strong, with a fine-tuned strategy and business model that capitalizes on a consumer that is demanding lower price points for everyday items. Dollarama does this to perfection, with merchandising skills that have brought down costs and driven up efficiency.

The latest quarter saw more margin increases, a 5.5% same-store-sales growth rate, and a continued expansion of its store base in the last year, with 65 new stores added (+6%).

EBITDA margins continue to expand, coming in at 27.1% in the quarter compared to 26.5% last year, which is far above its peer group, and EPS increased 17% to $1.45.

The company's strong free cash flow generation and return on invested capital came through again in fiscal 2018. Operating cash flow was $611 million compared to $509 million last year, and free cash flow was $498 million.

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

But at what point are we overpaying? And how long can it keep up this growth rate?

I have been admittedly skeptical about the company due to a couple of factors — mostly the stock's valuation. Trading at 34 times fiscal 2018 earnings, this is no cheap stock.

I was also skeptical because of the fact that the company has had to institute price increases in order 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 393% but is only marginally higher year to date.

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, as a value investor, I still view the risk/reward proposition on the shares as unattractive, so I will remain on the sidelines.

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