Is it Too Late to Buy This High-Growth Dollar Store?

Description

When I compared **Dollarama Inc.** (TSX:DOL) and **Five Below Inc.** (NASDAQ:FIVE) about a week ago, with the conclusion that "Five Below will probably be a better investment for growth … If I had to choose one today, I'd start scaling in to Five Below," little did I know that an investment in Five Below would do so well in such a short time — Dollarama is flat compared to about a week ago, while Five Below is trading roughly 40% higher!

Is Dollarama's share-buyback program good news?

Dollarama will be buying back up to about 5% of its common stock for the next year or so. This is a common way for companies to give back to shareholders.

The thing is that buybacks only generate value to shareholders if the stock is a good value. It's the same concept as retail investors trying to buy a company at a good valuation. The idea is to buy a good company when it's undervalued.

As I mentioned in the article a week ago, I find Dollarama to be pretty fully valued currently. So, if I were a Dollarama shareholder, I'd feel indifferent about the buyback program.

Why Five Below popped about 23% today

Five Below reported a blowout quarter that exceeded its sales and earnings guidance ranges. Here are some key metrics compared to the same period in 2017:

	Q1 fiscal 2017	Q1 fiscal 2018	Change
Net sales	US$232.9 million	US$296.3 million	27.2%
Operating income	US$24.7 million	US$12.8 million	93.3%
Net income	US$21.8 million	US$8.4 million	159.8%
* Diluted earnings per share	US$0.15	US$0.39	160%

** Excluding a US$0.04 benefit due to the accounting for employee share-based payments, the diluted earnings per share would have increased to US$0.35 for a 133% gain.*

Most importantly, management has increased its full-year fiscal 2018 sales and earnings-per-share guidance. For this fiscal year, it expects net sales to be US$1.502 to $1.517 billion, which will be supported by about 125 new store openings and the assumption of a 1-2% increase in comparable sales.

Five Below estimates net income to be US$136.5-139.9 million with diluted earnings per share of US$2.42-2.48.

Is it too late to buy Five Below?

Five Below is trading at about $100 per share, a forward price-to-earnings multiple of about 40, according to management's guidance. So, the stock is trading about a year ahead of earnings. Given that management forecasts sales growth and net income growth of 20% through 2020, this is about as high a multiple any rational investor should be willing to pay for the growth stock.

Five Below's stock doubled its share price in merely a year with the support of double-digit growth. There's no arguing that it is a great business.

However, since it has run up so much in the last year, it's safer for investors to wait for the share price to consolidate first before buying. Moreover, there could be better buying opportunities if the company experiences a sub-par quarter.

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2. TSX:DOL (Dollarama Inc.)

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