Who Should Alimentation Couche-Tard Inc. (TSX:ATD.B) Buy Next?

Description

Ever since **Alimentation Couche-Tard Inc.** (TSX:ATD.B) announced its fourth-quarter earnings July 9, its stock has been on a nice upward trajectory, rising 12% through July 17.

It's nice to see because Couche-Tard stock's hovered around $60 since August 2015 with little or no movement.

Investors are getting restless. They want to see another big acquisition — the company's modus operandi — despite the fact that it's only been slightly over a year since it closed its US$4.4 billion purchase of CST Brands.

Live by the acquisition, die by it

In April, I compared Couche-Tard with **Dollarama Inc.**, a classic growth versus value study. I concluded that Couche-Tard was the better buy given that it was trading at 12 times cash flow or less than half Dollarama's valuation.

Unfortunately, while Dollarama's biggest concern is rising costs and wages, Couche-Tard's biggest issue is finding convenience-store operators to buy that aren't charging an arm and a leg regarding a sale price.

It's almost as if the sellers see Couche-Tard coming and tack on an extra zero, making it difficult to pull the trigger.

"We remain active in Asia to find the right management team, the right network for new growth platform in that part of the world," CEO Brian Hannasch said during its Q4 2018 conference call. "We, at the same time, remain committed to be disciplined in our buying, and we remain committed to have a balance sheet ready for the right opportunity when it arises."

It has two problems

First, it needs to reduce its debt a bit more before it makes a multi-billion acquisition. At the end of the fourth quarter, it had US$666 million in cash plus US$1.1 billion available on its revolving credit facility.

While that's enough financial clout to make a reasonable-sized acquisition, it probably needs to lower its net debt from 2.46 times EBITDA by another 28% to 1.77 times EBITDA before it can pull the trigger on an acquisition similar in size to the CST Brands deal.

Hannasch says it's close to where it wants to be regarding debt levels; by comparison, Couche-Tard had a leverage ratio of 1.09 times EBITDA before completing the CST deal.

The second problem and likelier the trickier of the two is finding a deal that both moves the needle and doesn't cost too much.

Down in the U.S., consolidation is happening like gangbusters, but people are asking nosebleed prices. Couche-Tard paid 10.4 times EBITDA for CST, 7.0 times EBITDA if you include the synergies acquired.

I think that's as much of a multiple as it's willing to pay, which means it might be waiting awhile.

In the meantime

If Couche-Tard does pull the trigger on a big acquisition, I would like to see it acquire OXXO, Mexico's largest convenience store operator with 16,500 stores, about 7,000 more than Couche-Tard has in the Americas, which includes Canada, the U.S., and Latin America.

If you think Couche-Tard opens a lot of stores, OXXO opens a new store every seven hours. Its annual revenues make it the third-largest retailer in Mexico. Perhaps even more interesting is the fact OXXO's parent is expanding its reach into drugstores; it currently has 1,100 open in Mexico and is expanding rapidly.

It wouldn't come cheap. In fact, it would be its biggest ever, but if it wants to get its stock unstuck, this would certainly do it.

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