Danger: This Incredibly Popular Canadian Stock Could Plunge 40%

Description

I've been urging investors to throw in the towel on **Dollarama** (TSX:DOL) for well over a year now. It's a classic case of a growth stock transforming into a value stock. The last quarter, which saw slower same-store sales growth (SSSG) numbers along with a sharp SSSG guidance downgrade, was evidence of the insidious transformation that's likely far from over.

This isn't a one-off SSSG slowdown. Rather, I think it's the start of a trend that'll probably lead to further losses for investors who've decided that they're going to stick around in the hopes of a turnaround.

In prior pieces, I've emphasized that both increased competition in the discount retail scene and poor decisions made by management would cause the stock to suffer a nasty correction over the near term. I'd noted Miniso as an up-and-coming competitor that Dollarama was unprepared to deal with due to management's reluctance to invest in improving its sub-par in-store experience.

The Canadian discount store scene is about to get crowded

As competition picks up in the Canadian discount retail space, it's no longer just about small up-and-comers like Miniso that Dollarama will need to worry about. **Amazon.com** has a growing selection of low-cost goods that shoppers can "add on" to their original purchases.

Discount stores like Dollarama which were once thought of as Amazon-proof may not be as insulated as many investors may have thought a few years back. Dollarama's moat was its ability to command low prices, but with Amazon breathing down its neck with low-cost "add-on" items, Dollarama's margins will stand to be pressured, and its moat could easily erode because, as we all know, Amazon plays hardball when it comes to price undercutting.

Over the next few years, I wouldn't at all be surprised to see Amazon try to steal lunch away from all the discount retailers. Amazon is going to make it easier for shoppers to bundle their add-on items together, and as its logistics capabilities continue to improve, we're likely going to see Amazon's minimum order fall well below the $35 mark, where it currently stands today.

Who knows? In five years from now, drone deliveries may make it economical for Amazon to deliver low-cost items individually without any additional “add-ons.”

Foolish takeaway

Short-sellers at Spruce Point Capital Management called the company a “broken growth story,” slapped a “strong sell” on the stock, and claimed it could be in for 40% in further downside.

I think they’re right on the money and would encourage investors to cut their losses, as Dollarama could realistically hit the low $20 levels by year end. When you consider the number of headwinds that are still present today, I wouldn’t advise touching shares with a barge pole, even though they may seem like a bargain after the recent flop.

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