1 Way This Iconic Brand’s Stock Could Rebound

Description

It’s been a little over 13 months since **Roots** (TSX:ROOT) went public at $12 a share, down from the original plan of between $14 and $16.

ROOT stock closed at $10 on its first day of trading, October 25, 2017. The $6 drop from the high end of its range should have been a warning of things to come for investors. Now trading in the low $3s, IPO investors who are still holding have got to be furious about this turn of events.

We’re in the final stages of the 2018 holiday shopping season. For the sake of shareholders, Roots has one way to ensure its stock makes a comeback in 2019.

Dreadful numbers

In the fourth quarter of fiscal 2017, Roots had same-store sales growth of 15.1%, a direct-to-consumer sales increase of 17.6%, and a 22.9% increase in its earnings per share.

It was a strong quarter to finish off a solid year that benefited tremendously from the Canada 150 celebrations.

That was the good news. The bad news is that it made subsequent quarters in fiscal 2018 look dreadful by comparison.

For example, in Q2 2018, Roots reported a 1.1% same-store sales increase, not a great result, but horrific against the backdrop of a 16.3% increase a year earlier in Q2 2017.

Unfortunately, the company’s third-quarter results were much worse than the second quarter, with same-store sales declining by 13.4% — a 23.4 percentage point swing from a year earlier.

“We faced significant headwinds due to three main factors: a weaker brand voice in the absence of a large marketing campaign, unseasonably warm fall weather that persisted through approximately two-thirds of the quarter, and lapping one-time Canada 150-related sales recorded in Q3 2017,” stated CEO Jim Gabel in the earnings release.

The first point boggles the mind. The company should have known there would be a letdown in fiscal 2018 and budgeted accordingly. That’s a rookie mistake for sure.

The second point has become retail industry’s go-to when business sucks. Weather does play a factor, but good companies find a way around it or, at the least, a way to minimize the damage.

Finally, the third point is a reasonable explanation for some of the decline, but surely not the entire 23-point collapse.

Few, if any, catalysts

The company revised its guidance for the fourth quarter on December 5.

It now expects $375 million in sales at the high end of its guidance in fiscal 2018, down 75 million from its previous estimate. It also said there would be a slowdown in the pace of its U.S. expansion (a good thing) from as many as 14 store openings south of the border in fiscal 2019 to as few as five. Also, it will also reduce the number of store locations that get renovations in 2019 (a bad thing).

At this point, it’s almost 100% certain this year’s holiday numbers will be a disaster. Any piece of positive news could be a catalyst to move it into the $4s, but that’s unlikely.

Prem Watsa to the rescue

The CEO of **Fairfax Financial** has quietly been accumulating a retail empire over the last few years — the most recent purchase of Toys “R” Us Canada is the latest example how the veteran investor isn’t afraid to make contrarian bets when the price is right.

Well, Roots’s market cap is now around $137 million, a far cry from the $500 million valuation it got from its IPO coming out party.

Is the iconic beaver worth saving?

Roots shareholders had better hope so.

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