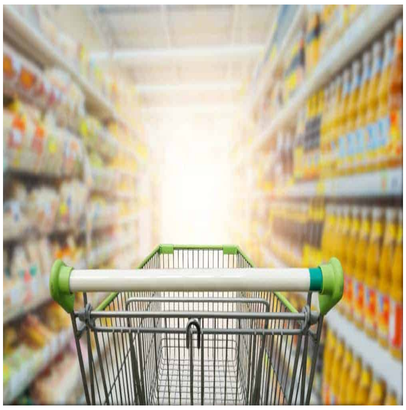

Opportunity: Supermarket Stocks Are an Interesting Niche

Description

How often do you buy groceries? I've long been an advocate of the view that some of the best investments to make are in our daily lives, fulfilling some form of need that we take for granted.

In case you haven't realized it, your local supermarket might be one such investment opportunity worthy of consideration. Both **Loblaw Companies** (TSX:L) and **Metro** (TSX:MRU) are the two largest supermarket chains in the country, and today we'll look at which of the two is the better investment.

The case for Loblaw

The first thing working in favour of Loblaw is its sheer size. Loblaw has an established presence in several provinces with a dizzying array of brands and store banners that are among the most popular in Canada. While brand loyalty is big, Loblaw has recently reminded us that loyalty itself is also huge, with the company's PC insider loyalty program, the $99 annual perks program that provides a host of perks, and discounts proving incredibly popular with customers.

In terms of results, Loblaw's first-quarter results showed a 3.1% increase in revenue over the same period last year, with retail sales also showing a notable 2.9% increase in the quarter over the same quarter last year. Furthermore, operating income and adjusted EBITDA saw handsome gains in the quarter of 19.9% and 41.9%, respectively.

Finally, from a dividend standpoint, Loblaw offers a quarterly distribution that works out to a 1.80% yield. While that may not be the most appetizing yield on the market, it is consistent, and Loblaw has provided a series of decent hikes to the dividend over the past few years and has been repurchasing shares.

The case for Metro

Metro is smaller than Loblaw, both in terms of overall size as well as coverage area. Metro is predominately known for its presence in Quebec and Ontario, but that is not a reason to be dismissive of the company. In fact, the recent quarterly results provided several promising points for investors to consider.

In the most recent quarter, Metro reported sales of $3701.6 million, reflecting a whopping 27.7% improvement over the same period last year, which was primarily attributed to the addition of sales from the Jean Coutu pharmacy. Without the addition of Jean Coutu, Metro realized a still respectable 4% year-over-year gain.

The Jean Coutu acquisition was completed last year, but Metro continues to see synergies of $50 million on an annualized basis from the transaction.

Net earnings for the quarter came in at $121.5 million for the quarter, reflecting a gain of 13.7% over the prior period, while on an adjusted basis earnings came in up 43.5% over the same quarter last year to $155.1 million, or $0.47 per diluted share.

As a dividend investment, Metro currently provides a quarterly payout, which works out to a 1.65% yield. Potential investors should note that while that yield is lower than Loblaw's, Metro has maintained a string of annual hikes to its dividend, with a higher growth rate than Loblaw, meaning that at some point in the future Metro could match, if not surpass Loblaw's dividend.

The better investment?

Both grocers make interesting investments, but at the moment my preference is toward Loblaw, which I can put down to loyalty, branding, and size.

First, Loblaw's loyalty program is, in a word, incredible. Not only is the company gathering oodles of data on its customers' shopping preferences, but it is also going out of its way to make its customers loyal to the Loblaw brand, and that loyalty translates into repeat visits and, by extension, higher revenues.

Second, there's the branding aspect. People go out of their way to purchase the brands that Loblaw offers, which is something that Metro has not yet attained. In an ultra-competitive area of the market, that could be the deciding factor in reaching some level of growth.

Finally, there's the sheer size of Loblaw. Metro's dominance extends just over Quebec and in small pockets of Ontario, whereas Loblaw has an established foothold in several provinces across the country. This not only makes Loblaw the more diversified option but also the one with more growth potential.

CATEGORY

1. Investing

TICKERS GLOBAL

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2. TSX:MRU (Metro Inc.)

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