3 Takeaways from Dollarama's (TSX:DOL) Q1 Earnings

Description

Dollarama (TSX:DOL) released its first-quarter results for fiscal 2020 last week. While the company fell short of meeting its analyst expectations for earnings, the results had a lot of positives that helped the stock jump.

Here are three things that stood out to me from the company's latest earnings report.

Its days of being a high-growth stock look to be long gone

The company saw a strong improvement in its top line this quarter with sales up 9.5% year over year. Same-store sales numbers were up 5.8%, and while that's good for retail, it's a downward trend that we've seen from Dollarama over the past few quarters and a key reason that its share price has struggled as badly as it has.

In the earnings release, CEO Neil Rossy said that the company would be "revising upward our full-year assumption for comparable store sales to the range of 3% to 4%." Those are some uninspiring numbers for a stock that used to be one of the best growth stocks on the TSX. While there's still a lot of room for Dollarama to expand around the country, organic growth might be limited in future quarters.

Dollarama is still a good stock that's showing positive growth, but its numbers make the share price look a bit expensive today. If investors are paying more than 25 times earnings, they should expect a lot of growth from a company. And single-digit growth likely won't cut it for many investors, given the more attractive opportunities that are available on the markets today.

More store openings still planned

During Q1, Dollarama opened 11 net new stores, and it is on track to open between 60 and 70 stores by the end of the fiscal year. It's a similar increase that we've seen in the past as the company continues to expand into new markets. As of May 5, the company had 1,236 stores that were opened, which is 66 more than the 1,170 it had a year ago.

New store openings are a good way for the company to continue growing its sales, and it could help improve its same-store growth as well. However, the danger is that it will add costs and run the risk of not being as successful in new markets and potentially cannibalizing sales from existing locations.

Margins have decreased from last year

Dollarama is seeing less of its sales trickle through to its net income, as the company reported a profit margin of 12.5% this quarter compared to 13.4% a year ago. While it's a modest decline, there could be headwinds that see that percentage fall even further. Tariffs, higher interest rates, and wages are all examples of how the retailer might see costs rise higher from the previous year.

Not only are operating costs rising, but the company's gross margin has also seen a decline, dropping from 43.8% to 42.1%. With an already slim increase in net income this quarter (1.9%), further erosion of margins could make the company's prospects of growing its bottom line even more difficult in future quarters.

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