



## Long-Term Investors: A Top Contrarian Pick to Buy in September

### Description

The retail sector has been pretty beaten up the last few years as competition heats up and retailers try to insulate themselves from the switch to online shopping.

Many companies in the industry have had their share prices severely impacted, as the market looks for any weakness these businesses may face in the future.

Often times, shrewd investors can find opportunities among the sell-offs and find companies that may have been treated a little too harshly by the market.

These contrarian picks will be doing something right with strong characteristics that suggest it can survive the shifting landscape in retail shopping.

One top contrarian play that's been flying [under the radar](#) is **Sleep Country Canada Holdings Inc (TSX:ZZZ)**

Sleep Country's stock has come down roughly 35% in the last 12 months.

It's in a prime position, as it's one of the largest mattress retailers in Canada, with roughly 30% of the market share in Canada. The company has 265 stores and 19 distribution centres, across nine provinces.

Sleep Country is a decent contrarian pick because its business won't be impacted as much as the market thinks. The main worry for investors of retail stocks is the risk the company faces to losing business online.

Mattresses aren't necessarily something people will be in a rush to buy online for the simple reason that the products are very large, and most people want to try a mattress out before purchasing.

Furthermore, Sleep Country bought an online mattress retailer Endy, in 2018, and has been pushing its digital position to offer a more omni-channel approach to its customers.

The acquisition of Endy is important for the future of the business, but also shows that management is being prudent. Endy will be a big part of Sleep Country's future, as it has already revolutionized the industry. It was founded just four years prior to its acquisition of \$90 million.

The acquisition of Endy isn't the company's only growth plan, however.

In addition to growth through acquisition, the company has been working to revamp its existing stores to grow the company organically. As at the end of February 2019, more than 60% of its existing stores have been upgraded.

It's also been opening a number of new stores each year. The company targets at least eight new stores a year, but has a trailing five-year average of 13 new stores each year.

The new stores have really been the key driver of growth, although same-store sales have contributed a bit too.

Since 2013 sales are up 76%, and earnings before interest, taxes, depreciation and amortization (EBITDA) was up an impressive 169%.

The increase in revenue and EBITDA can be directly attributed to the growth strategies the company has been working on.

Another positive about Sleep Country's business is the low maintenance costs. This allows it to have much lower total capital expenditures and thereby enabling it to have much more free cash flow to return to shareholders. Currently, maintenance and capital expenditures account for less than 5% of sales.

In the last 12 months, Sleep Country has done \$623 million in sales and operating EBITDA of \$105.8 million, providing an operating EBITDA margin of 17%, which is in line with its three-year average.

On the \$105.8 million in operating EBITDA, the company expects roughly \$50 million in free cash flow available for dividends, of which approximately \$27 million will be paid out in dividends, implying a payout ratio of just 54%. The dividend currently yields 3.7%, which is pretty respectable.

The net debt is roughly ~\$140 million, implying a net debt to operating EBITDA of 1.33 times earnings for the last 12 months –a pretty reasonable debt level that should be manageable going forward.

If Sleep Country can continue to grow its revenue and keep its EBITDA margins intact, shareholders will be rewarded nicely. A low payout ratio and strong margins imply continued dividend increases, as long as the company can continue to grow.

## **CATEGORY**

1. Dividend Stocks
2. Investing

## **TICKERS GLOBAL**

1. TSX:ZZZ (Sleep Country Canada)

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