



## Investors: This Retail Stock Is Trading at a Cheap Valuation Multiple

### Description

Shares of **Roots Corp.** ([TSX:ROOT](#)) have burned significant investor wealth. The stock was publicly listed back in October 2017 and has since lost 72% in market value. Roots investors have seen the stock fall by 80% since May 2018.

One of the primary reasons behind the stock's decline is the company's lackluster quarterly performance. Roots has failed to meet analyst earnings expectations in three of the last four quarters, driving the stock significantly lower.

Roots reported earnings of  $-\$0.17$  in the fiscal first quarter of 2019 (ended in April), 13.3% below analyst estimates of  $-\$0.15$ . It missed analyst earnings estimates of  $\$0.16$  by 31.2% in the third quarter of 2018 as the firm reported earnings of  $\$0.11$ .

Roots share lost significant value in the second quarter of 2018, as it reported earnings of  $-\$0.06$ , 200% below estimates of  $-\$0.02$ .

### Has Roots stock bottomed out?

Roots stock is trading  $\$2.67$  per share — its 52-week low. Its forward price to earnings (PE) multiple is low at 5.04. Analysts expect Roots to grow earnings by 4.2% in fiscal 2019 and by 8% in 2020. The stock is undervalued given its earnings growth and forward PE multiple.

Analysts also expect the company to grow sales by 8.2% and 6% in the next two fiscal years. They have estimated sales at  $\$62.08$  million in the second quarter of 2019 with earnings of  $-\$0.10$ . Roots shares will move higher if it manages to beat analyst estimates in the second quarter and beyond.

### What will drive Roots revenue higher?

Roots revenue growth will accelerate in 2019. But what will drive company sales higher? Roots is banking on international stores to drive sales. It has 115 stores in Canada and 8 stores in the U.S.

Comparatively, the firm has opened 115 stores in Taiwan, 39 stores in China and one in Hong Kong.

Roots' management aims to expand this global reach via partnerships in Asia. In the second quarter, it will be opening another store in Hong Kong as well as expanding its online presence in this geography.

In the first quarter, Roots grew sales by 6.5%. Direct to consumer sales were up 5.5% as well. Company CEO Jim Gabel stated, "Our sales growth in the quarter reflects our strength as a seamless omni-channel retailer, the continued success of our renovation and relocation strategy and growth in our partner-operated business in Asia. Increased traffic and higher conversion drove comparable sales growth of 1.5% for the quarter, or 8.3% on a two-year stacked basis."

Gabel added, "In addition, we saw positive consumer response to both new products and our recently launched brand campaign. While we realized short-term pressure on DTC gross margin, it was a result of our meaningful progress in improving our overall inventory position in advance of our move to our new integrated distribution centre in Q2 2019."

## The verdict

Roots stock is trading at an attractive multiple, but the company has a history of disappointing investors and has consistently missed estimates.

While the company is confident about [meeting financial goals](#) in 2019, investors are rightly cautious about the stock. Further, the estimated growth rates and earnings expansion are far from impressive.

Roots will need to expand the top and bottom line at a far higher rate for it to be an attractive investment. Analysts remain optimistic and have a 12-month average target price of \$5.28, indicating an upside potential of 94% from current levels.

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