



## TFSA Investors: Avoid This 1 Stock

### Description

As a Canadian, you would likely have set foot in a **Loblaw** ([TSX:L](#)) owned store at some point in your life. It is the company that owns Shoppers Drug Mart, Real Canadian Superstore, No Frills, Real Canadian Superstore, and Fortinos, just to name a few.

Despite Loblaw owning over 1,000 stores across Canada, there are many flaws to the company that make it unattractive as an investment, especially with [better grocery stocks on the market](#). This includes stagnating revenues and high debt.

### Stagnating revenues

Loblaw has hit a wall when it comes to growing its business. In fact, this has become such a serious issue that in the past three fiscal years, its revenues have ranged from \$46.385 billion to \$46.702 billion, which means its revenues have essentially stagnated.

This means that the company has to rely on acquisitions to grow its revenues. While this may sound enticing, acquisitions are extremely costly and don't always go as planned.

Acquisitions are costly, as companies usually take on massive amounts of debt to finance the acquisition. This exposes the company to leverage risks, which is problematic during years of tight cash flow, as it is put in a position where it could default on its loan payments.

From an interest payment perspective, acquisitions are expensive; a \$1 billion loan at a 1% interest rate results in \$10 million of interest payments per year.

There is a word in the business world called *synergy*. It is used to describe how companies fare after a merger or acquisition. A company with poor synergy has failed to combine the corporate cultures of the company it acquired and itself, which leads to a failed merger or acquisition.

A company with good synergy has succeeded in combining the corporate cultures, and it able to use its merger or acquisition to grow the business.

## High debt

As I mentioned above, acquisitions are costly and usually lead to high debt. In 2014, Loblaw acquired Shoppers Drug Mart for \$12.4 billion. In the same year, it reported total debt and capital lease obligations of \$12.2 billion, which was likely due to money used to finance the acquisition.

As of fiscal 2018, Loblaw had \$8 billion in total debt and capital lease obligations. There are many downsides to having high debt, which include low working capital and high interest payments.

Working capital is calculated by taking current assets minus current liabilities. It is a measure of whether the company has a surplus or deficit of assets.

Assets are used by companies to generate revenues, and a working capital surplus allows the company to use assets for the purposes of generating revenue as opposed to securing liabilities. Loblaw has working capital of \$2.9 billion, which is acceptable, but given revenues of \$47 billion, it should be much higher.

Interest payments for fiscal 2018 are \$260 million, which are attributed to the high levels of debt Loblaw has

## Bottom line

Despite many investors being bullish about Loblaw, I disagree with their assessment of the company. Even though Loblaw has over 1,000 stores across Canada under multiple brands, the company is restricted to an acquisition-centric growth model and has high debt.

An acquisition-centric growth model is very costly due to the leverage risks the company is exposed to in addition to the high-interest payments. Further to this, the company has \$8 billion in total debt and capital lease obligations. In 2018 alone, this has resulted in interest payments of \$260 million, which has been increasing since fiscal 2014.

There are [much better companies](#) in the market that give investors a decent return.

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