Dollarama (TSX:DOL) Stock Is a Defensive Growth Stock Priced Like a Value Stock

Description

Dollarama (TSX:DOL) shares are plunging, with shares pulling back 25% from 2019 highs and 34% from 2018 all-time highs.

As you may remember, I was one of Dollarama's most prominent critics back when everything was all fine and dandy for the market darling, which had run above and beyond a multiple that I thought was reasonable. I called the peak at Dollarama, and those who took my advice avoided a nasty plunge that was easily avoidable for those willing to take a deep dive into the financials.

In a nutshell, Dollarama was facing severe headwinds that threatened to turn the growth darling into a stalwart. Any time such a transition happens, the stock corrects violently, as the multiple looks to contract amid a resetting of investor expectations. You can pull on the margin lever and to affect sales, but the only way to gain command of a 30 times trailing earnings multiple is to get margins and sales sustainably in the green.

Dollarama's valuation now makes sense

After falling into a bear market for the second time in two years, I finally think the valuation is right to pick up shares. The negative momentum makes Dollarama stock a falling knife, and you're going to take a beating by going against the grain here. Still, for those with a long-term horizon, I'd recommend nibbling on the way down to the stock's level of support at around $33.

While many of the headwinds I originally outlined in prior warnings to investors are still present, I am still a believer that any stock can be a buy if the price is right. And at just 16.3 times next year's expected earnings, I think one stands to pay three quarters to get a loonie with Dollarama after its recent spill.

Indeed, the stock is priced as a stalwart, when in actuality, there's still a chance that the company can return to the growth track. It's not going to be an easy task to regain its status as a growth darling, given the domestic discount retail market is saturated and facing stiff competition. With an outlet in the Latin America, through Dollar City, though, I see a scenario where Dollarama can slowly but surely regain the growth multiple it once commanded.

There are challenges that come with expanding into foreign markets. The stakes are higher, and the penalty for mistakes is more severe, but at today's valuation, I see Dollarama as a stalwart that's already priced such that its Latin American expedition will mean nothing over the long run. Dollar City won't move the needle for Dollarama anytime soon, but over time, I see Dollarama's toe-dip in its new growth outlet turning into a huge splash.

Dollarama begs for patience, and with the ability to hold its own during times of recession, I see the name as a unique way to play both defence and growth. Let's not be so quick to discount management's success in the domestic market. While there's no guarantee that the magnitude of success will be replicated in new growth markets, I like the chances given today's ridiculously low price of admission.

Foolish takeaway

Even if Dollarama were to remain a low-growth stalwart, I still think 16 times forward earnings is too cheap given the premium defensive characteristics that will allow the stock to buoy your portfolio come the next market meltdown.

Sure, there's baggage with the name, but I think it's more than baked into the stock at $38.

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Date
2025/08/10

Date Created
2020/02/26
Author
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