Buy Dollarama (TSX:DOL) Now or You’ll Probably Kick Yourself Later

Description

Dollarama (TSX:DOL) pulled the curtain on its Q2 fiscal 2021 results on Wednesday morning, and the results were nothing short of solid, even though shares of the name pulled back by the slightest of margins on a big up day of value stocks. The Canadian discount retailer crushed analyst estimates, as consumers bought more stuff in fewer trips, a phenomenon that’s become the new norm amid the COVID-19 pandemic.

Dollarama clocks in another beat for the books, but investors were unimpressed

While Dollarama started the day up, shares retreated, likely because management didn’t provide forward-looking guidance for the rest of fiscal 2021.

These days, investors not only want a beat, but also a beat alongside some guidance amid this highly-unpredictable economic environment. The “beat and guide” combo seems to be the formula for a big pop. Still, with unprecedented uncertainties as a result of this pandemic, I think the stock is a buy because even if management were to provide guidance, it would have likely been imprecise, given the COVID-19 impact.

Net earnings came in at $142.5 million (or $0.46 per share, beating the $0.41 per share consensus). The beat was thanks in part to increased sales and slightly higher gross margins in the quarter, which offset expenses relating to COVID-19 (cleaning, personal protective equipment, and all the sort).

Although a worsening of the COVID-19 pandemic could cause Dollarama stores, which are viewed as essential businesses during lockdowns, to operate under reduced hours and that does not bode well for top-line growth over the medium-term. It’s hard to tell whether there will be a second shutdown-inducing wave of COVID-19 cases across Canada. However, there is a very good reason that management was reluctant to provide fiscal 2021 guidance: nobody knows the next step of this pandemic.

While investors weren't fans of management's lack of guidance, Dollarama is capable of delivering an upside surprise somewhere down the line, given it's not setting a bar for itself.

For the duration of this pandemic, Dollarama will remain relatively resilient, but it will feel an impact. Once this pandemic ends, a recession could provide lift to Dollarama shares, as belt-tightening Canadians head to the local Dollarama to take advantage of its unmatched value proposition.

In times of economic hardship, defensive firms tend to fair better than average, and I suspect the company could be a great way to play a potentially severe coronavirus recession.

What about valuation?

At the time of writing, Dollarama stock trades at 4.3 times sales, 19.8 times cash flow, and 17.6 times EV/EBITDA, all of which are lower than DOL stock's five-year historical average multiples of 4.4, 25.6, and 19.7, respectively.

The lack of a sustained post-earnings rally is an opportunity for longer-term investors to back up the truck on a name that could help keep your portfolio above water come the next market-wide pullback. Shares have a 0.78 beta and are more likely to zig while the markets zag on any news relating to COVID-19.

Dollarama will keep rolling with the punches and is a prudent bet for any investor seeking defensive growth at a reasonable price.

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