IPO Alert: Don’t Sleep on This TSX Underdog

Description

Canadian pet supply chain **Pet Valu Holdings** (TSX:PET) had a pretty quiet IPO on the **TSX Index** just a few weeks ago. Undoubtedly, the name gives Canadian investors a domestic way to play the “humanization of pets” trend that may very well be a long-lived secular trend that could pay dividends through the “Roaring ’20s.”

While spending on pets and pet supplies is likely to remain robust over the coming years, it’s worth remembering that brick-and-mortar retail is a tough place to be in, with innovative e-commerce disruptors that are hungry to take share away from the incumbents.

Most notably, e-commerce pet sensation **Chewy** poses a serious threat to the U.S. brick-and-mortar pet retailers. Currently, Chewy isn’t causing disruption in Canada. But this may change in time, especially if the company were to follow in the footsteps of the likes of an **Amazon.com** by getting aggressive on the international growth front.

For now, Pet Valu shareholders can sleep comfortably, as it’s very much a domestic play after shuttering numerous stores located in the U.S. market, many of which experienced considerable pressure due to the impact of COVID-19, which directed traffic to digital pet stores such as Chewy.

With more capital raised from the financial markets, the nearly 50-year-old company can beef up its Canadian presence with more stores whilst chipping away at its debt levels. With over 1.4 million people aboard the loyalty program, I do not doubt that Pet Valu can carve out a growing moat on its home turf.

Is the hot IPO a buy at $26 and change?

Pet Valu had a very successful IPO when it went live on the TSX back in June. Today, shares trade at $26 and change, and analysts appear relatively bullish, with sights set at around the $30 level.

As the company looks to expand its wings across Canada, the longer-term growth trajectory looks very enticing. The company posted $648 million worth of sales last year, with $29 in net income. According to Pet Valu's prospectus, the firm has been growing at around 10% over the past five years — a pretty solid growth rate for the retailer. With more funding and COVID-19 headwinds likely to pass, I wouldn't at all be surprised if Pet Valu can surpass 10% in top-line growth over the next few years.

A competitive retail environment

Indeed, things are looking up for the TSX newcomer on the growth front. But there are major risks. Most notably, the continued rise of e-commerce disruptors could put a growing dent in the firm's bottom line. In a few years down the road, we very well may witness a rise in Chewy plays here in Canada. And let's not forget about the ultimate disruptor in Amazon.com, which offers a wide range of pet supplies.

Moreover, **Canadian Tire** recently made a big push into pet supplies, which could apply pressure to Pet Value, as it continues with its expansion. Yes, it's quite a pivot going from tires to pet food. But that goes to show that the barriers to entry into the pet retail market aren't at all high.

Despite the competitive forces in Canada, I think Pet Valu will continue to do well. The company doesn't just offer pet supplies that can easily be bought online; it offers a wide range of pet services that Canadian Tire and Amazon can't offer. We're talking pet grooming, washes, and all the sort. Such services will drive store traffic, giving Pet Valu the edge in the Canadian pet retail space.

The bottom line on one of Canada's better recent IPOs

So, should you buy Pet Valu? I'd start by nibbling a few shares with the intention of adding on a pullback towards the low-$20 range. There's no question that it's a competitive scene, but I think the Canadian retailer can still do really well.

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