If I’d Invested in Dollarama Stock at the Start of 2022, Here’s What I’d Have Now

Description

Most stocks have lost value this year. **Dollarama** stock (TSX:DOL) isn’t one of them. The discount retailer has added 28.3% to its market value since January 2022. That’s significantly higher than the rate of inflation. It’s also higher than the **S&P/TSX Composite Index**’s performance of -13.7% over the same period.

If I had invested just $1,000 in Dollarama stock at the start of 2022, I’d have $1,283 today.

Here’s why the retailer is thriving despite harsh economic conditions and what could come next.

Why is Dollarama stock outperforming?

Canada’s largest discount retailer has 1,421 outlets across the country. Traditionally, most of these outlets were stocked with products priced under $2. However, this year the chain has raised the ceiling up to $5. That gives it more room to sustain its profit margins as inflation drives its costs higher.

Meanwhile, inflation is also pushing more customers to Dollarama stores. Canadian families have turned to discount retailers as their household budget is squeezed. This phenomenon has pushed up revenue.

Dollarama’s recent earnings reports clearly reflect these trends. Revenue was up 18.2% year over year while the net profit margin was up to 15.9%. Earnings per share have been consistently rising above 30% in recent quarters. That’s why the stock price is up by a similar amount.

What comes next?

At the moment, inflation is still historically high at 7%. The Bank of Canada expects inflation to gradually subside to 3% by the end of 2023 and 2% by the end of 2024. However, to achieve this the central bank needs to keep raising interest rates and cool the economy.

All considered, Canadians should be prepared for more price pressure in the months ahead and less purchasing power or a recession next year. These factors should keep demand for Dollarama's discounted goods high for the foreseeable future.

Dollarama valuation

Dollarama's stock price is up, but its underlying fundamentals are improving at a faster pace. In recent quarters, earnings per share growth were between 32% to 37%. At that pace, the company could double its earnings power by the end of 2024.

Dollarama stock is trading at a forward price-to-earnings ratio of 21. If the company can sustain its current pace of growth, its price-to-earnings-growth ratio should be well under 1. Put simply, the stock is undervalued.

Bottom line

2022 has been a tough year for most investors and consumers, but some sectors of the economy are thriving. Discount retailers like Dollarama offer families a reprieve from the ongoing wave of inflation. That's why the company's revenues and profits are surging higher.

If I'd invested a small amount in this stock at the start of 2022, I could have outpaced most other stocks and even the rate of inflation. Investors looking for a safe haven to park their cash for the next year should add this stock to their list.

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