# Peering Into Canadian Tire's Balance Sheet Prowess

## Description

**Canadian Tire Corporation** (TSX: CTC) is one of the more diversified consumer cyclical stocks on the Toronto Stock Exchange. Like other consumer conglomerates, it's not likely to grow at a blistering pace any time in the near future. However, since the mid-2011 acquisition of the Forzani Group, owner of popular sports chain Sport Chek, the company has exhibited a faster growth rate than previous years, increasing revenues by 12.7% and 10.0% in 2011 and 2012, respectively. In addition to this momentum, Canadian Tire has employed its resources in a constructive strategy that should benefit shareholder returns for years to come.



**Begin with the balance sheet**
One of the virtues of having predictable margins and cash flow is that over the years, Canadian Tire has built up a very attractive balance sheet. Current assets outpace current liabilities by a ratio of 1.75 to 1.0. Overall, the company's assets outnumber its liabilities by $4.8 billion.

Since Canadian Tire is consistently profitable, it can keep methodically adding to its balance sheet surplus year after year. The company distributes its returns to shareholders sparingly. The current dividend yield is 1.47%, and the company's plan to repurchase $100 million of shares over the next year won't dent its bank account — last year, Canadian Tire generated $743 million in operating cash flow. So if Canadian Tire has been adding to its resources for some time, just how are these assets being employed?

**How to reap substantial, recurring profits**
For 20% of the people reading this article, the answer to the question is likely in your wallet. Canadian Tire's Financial Services segment processes consumer loans, and the segment is a powerful lever that enhances the organization's earnings and cash flow.

The company's best-known consumer loan product is the Canadian Tire Options Mastercard, which it claims is held by one out of five Canadians. At the end of its last fiscal year, Canadian Tire had $4.2 billion of loan receivables on its books. This amount, lent out to consumers, is the balance sheet asset that drives a good portion of Canadian Tire's profits. In the last few years, the company has also added some long-term debt in order to grow the receivables portfolio. The attention to this revenue stream has paid off handsomely: the company derived $981.9 million of revenue from the Financial Services segment last year, and generated $276.9 million in profits from this revenue.

Financial Service's profit accounted for almost 41% of the overall organization's pre-tax net income. Just to demonstrate how efficient this segment is for Canadian Tire, it took the company $10.4 billion of retail sales — more than ten times the amount of Financial Services revenue — to generate the other 59% of system-wide profits.

**Insulation from competition**
While Canadian Tire is working on retail strategies to deal with the coming onslaught of American competition from the likes of **Target** (NYSE: TGT), consider this — American encroachment on the Canadian retail frontier actually benefits Canadian Tire indirectly. After all, the Financial Services segment carries a net profit margin of a whopping 28%. Target and **Wal-Mart** (NYSE: WMT) may be opening up a slew of shopping options, but there are 4 million Canadians walking around with Canadian Tire-branded Mastercards. Canadian Tire is willing to cede a small portion of retail sales to the competition — as long as consumers continue to swipe its credit cards at the American checkout registers.

**Three U.S. stocks to consider …**
Speaking of Target and Wal-Mart, while Canada has yielded its fair share of great companies, unsuspecting Canadian investors could get ambushed by a glaring weakness in their portfolios. One basic investing principle holds the key to a rock-solid portfolio … and it starts with our neighbors to the south, America.

The Motley Fool has put together a Special FREE Report, "3 U.S. Stocks Every Canadian Should Own." The funny thing is, these stocks might as well be Canadian … because you use them every day. Just click here to receive a copy at no charge!



*Asit Sharma does not own shares of any companies mentioned.*

**CATEGORY**

1. Investing

**TICKERS GLOBAL**

1. NYSE:TGT (Target Corporation)
2. TSX:CTC.A (Canadian Tire Corporation, Limited)

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asharma