



# Stock Pitch

July 18, 2019

Dollarama Inc.

Ticker: DOL

Current Price: \$49.02 CAD

Target Price: \$57.39 CAD

## Summary

To determine the future performance of Dollarama this stock pitch will analyze the company as a whole, from its stock price to its management team. Additionally, this stock pitch will analyze the discount store industry and the potential Dollarama's business model(s) can bring. Furthermore, three theses have been developed to encapsulate findings relevant to Dollarama. The theses are followed by a list of risks and catalysts as well as a financial analysis of Dollarama's fiscal health.

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Eric Mogilner | Michael Himelson | Macy Bass | Shervin Ghaffari | Prakshi Prajapati

## Investa Insights

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# Company Overview



- Dollarama is the largest Canadian-based company operating in the discount retail store industry, offering its customers a variety of products.
- The firm is an established player in the field with over 27 years of experience.
- Dollarama's products retail at a price between \$1 - \$4. Recently, they began selling their products online in bulk.



## Executive Team



Niel Rossy  
CEO



Johanne Choinière  
COO



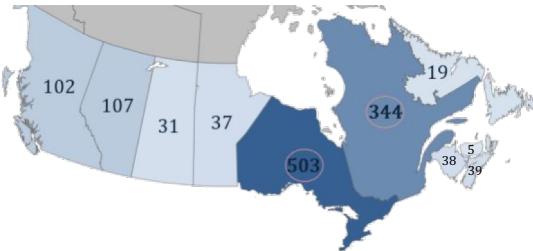
Michael Ross  
CFO

## Stock Summary

Market Cap (B)	\$15.60	PE Ratio(TTM)	28.99
EV (B)	\$18.86	EV / EBITDA	20.04
52 Week High	\$52.49	EPS	1.54
52 Week Low	\$30.12	Beta (6M)	1.269

## Store Locations

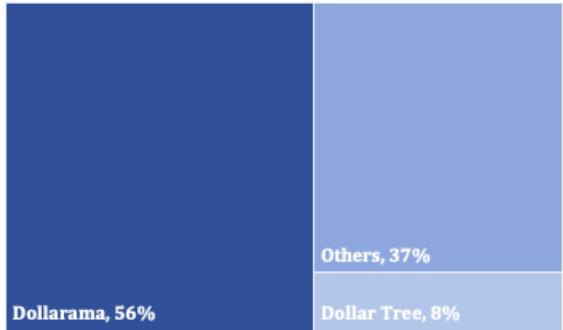
As of June 2019, there were 1225 locations across Canada with a high concentration in Ontario and Quebec.



# Industry Overview



## Canadian Market Composition



Dollarama dominates the Canadian market with a market share of 56%

## Key External Drivers

The industry is generally countercyclical. To sustain revenue growth in periods of economic expansion, dollar stores have improved quality of stock and invested in in-store aesthetics to retain middle-income consumers.



Industry has grown at a 6% CAGR from 2008-2018 and has been one of the fastest growing industries in the retail sector.

## Industry Changes



### Disposable Income

Increases in disposable income represent new opportunities due to an expanded consumer base.



### Unemployment Rate

Increases to the national unemployment rate have historically increased dollar store revenue due to frugal consumers.



### Leisure Time

Dollar stores typically cater to on-the-go consumers. A decrease in leisure time represents a busier lifestyle thus increasing dollar store revenue.

## Key Success Factors

### Controlling Stock Volumes



In this industry it is crucial that adequate stock control measures are in place to lead operational success. It is important that stock is consistently monitored, especially for products that are in high demand.



### Competitive Pricing Policy

Since price is a high driver in this industry, it is important that competitors maintain a competitive edge through price differentiation to attract consumers.



### Economies Of Scale

To maintain adequate profit margins, companies must order large volumes of products to receive discounts, thus, securing a low cost of goods sold.



### Offering a Variety of Products

To remain competitive, companies must provide a vast range of products to meet changing consumer demands.

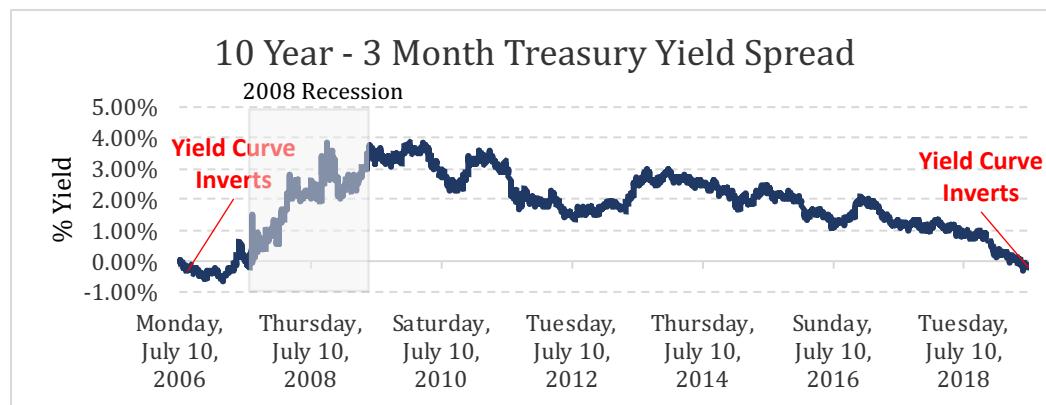
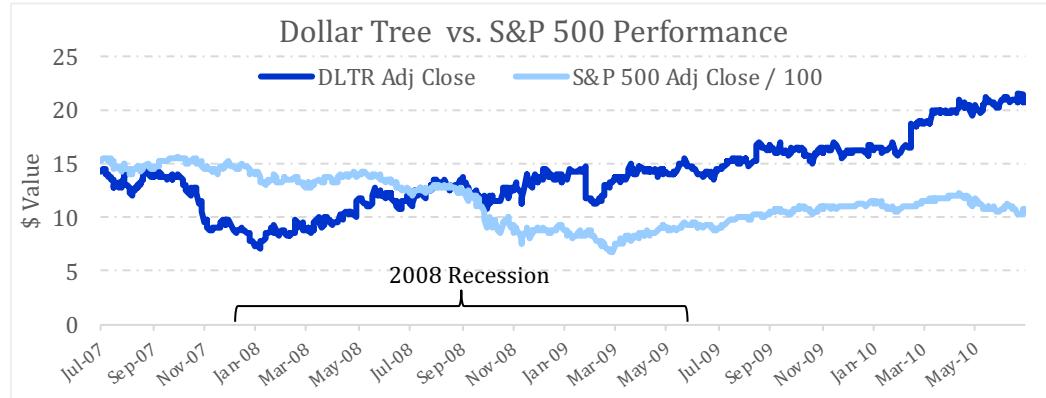
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# Investment Thesis I: "Sin Stocks" like Dollarama do well during a Recession



## Recession 2019/2020

- Current Economic Situation: Longest expansion of all time; the longer this run continues, the greater the chance the economy enters a recession.
- Stock Market: 2016 has felt an injection of higher earnings due to the Trump administration's corporate tax decrease from 35% to 21% - this boom cannot be attributed to exceptional market growth or performance.
- Past Trend: Inversion of the yield curve is a prominent indicator of an incoming recession. The last 7 recessions in the markets have come on the heels of these inversions. Most recently, the yield curve inverted in March of 2019.
- U.S. Student Debt: Total outstanding student loan debt is over \$1 trillion in the U.S., exceeding credit card debt.
- Due to the fact wherever the U.S. economy goes the Canadian economy follows, a recession from the United States' will surely result in a Canadian recession as well.


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# Investment Thesis II:

*Management's ability to transform and innovate*



## Dollar City Acquisition

Since Dollarama's acquisition of Dollar City, Dollar City store locations and average sales per store has increased YoY. Not only does this give Dollarama a dominant presence in the Latin American market, but it also indicates the ability of management to expand and adapt in new markets.

**Future Vision:** Penetrate new markets through identification of attractive trends and synergies

## Dollar City Store Count 2017-2019



## Average Sales/Store (2017-2018)



## Digital Expansion

Dollarama recently launched an online store that allows consumers to purchase products in large quantities and have them delivered across the country.

**Future Vision:** Company hopes to develop the website to be user friendly and increase consumer convenience.

## Price Stability

Dollarama maintains an average sale price of \$1 to \$4 per product. This is formed by their well-maintained relationships with suppliers since 1993, allowing them to offer differentiated products at a low cost. Direct relations enable the company to be involved in various parts of the process like product design. This strategy allows the price to remain stable during economic fluctuations.

**Future Vision:** Develop sourcing practices with Dollar City.

## Stock Management

Technology driven initiatives have helped the company be in a superior stock position to aid their warehousing capacity, increase logistic efficiency, and maintain a rational cost structure.

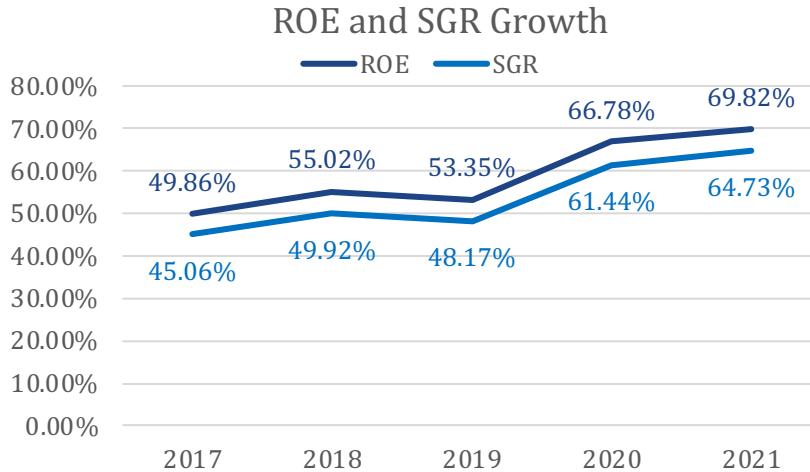
**Future Vision:** Developing mobile scanning technology, Mobile Cash Registers, and Cameras in high shrink stores.

# Investment Thesis III: High ROE and SGR Points to Continued Growth



## DuPont Analysis

	2017	2018	2019	2020	2021	Company	Equity Multiplier
Profit Margin	15.09%	15.68%	15.76%	19.32%	20.54%	Dollar Tree	2.39
Asset Turnover	1.59x	1.69x	1.63x	1.66x	1.64x	Dollar General	2.06
Equity Multiplier	2.08	2.08	2.08	2.08	2.08	Five Below	1.55
ROE	49.86%	55.02%	53.35%	66.78%	69.82%	Family Dollar	2.32
						AVERAGE	2.08



- Adjusted ROE calculated using DuPont Analysis shows exceedingly high returns on equity.
- High ROE points to a competitive advantage that will drive the long-term compounding process to result in superior long-term results for investors.
- Consistently high SGR implies strong inventory management as well as sales maximization.
- The company can continue to grow upwards of 40% without increasing leverage or issuing more equity which would be dilutive to shareholders.

## Price of Growth

1.6X

- Trading on a 1.6x G/PE multiple
- Price per unit of growth is very low
- Undervalued relative to growth
- Attractive time to buy

## Catalysts



### ACQUISITION OF DOLLARCITY

With Latin American economic growth now exceeding Asia's, Dollar City has and will continue to beat growth expectations. Dollarama is expected to add about \$0.03 to EPS for the remainder of fiscal 2020, and about \$0.06 in 2021 through this immediately accretive purchase.



### SLOWING INFLATION

Dollarama's profit margins will experience a boost due to slowing cost inflation, especially on materials imported from China. Furthermore, slowing inflation is a symptom of a slowing economy; as economic growth weakens, demand for Dollarama's inferior goods will increase as consumers seek out less expensive substitutes.



## Risks

### TARIFF TROUBLE

Tariffs from the South have dampened Dollarama's profitability in the past – the stock fell more than 6% when the CEO acknowledged this. The unpredictable nature in which they have been announced makes them an even greater threat.



### SUBSTANTIAL DEBT

While utilizing leverage to fuel growth has its advantages, a greater degree of risk follows. Should Dollarama fail to capitalize on investments funded with debt, they bear the loss/ lack of a gain on these investments as well as costs associated with the debt. This would have a considerable impact given their sizeable amount of long-term debt.

## DCF Unlevered Cash Flow Summary

(CAD\$ millions)	Historical				Forecast			
	2017A	2018A	2019A	2020E	2021E	2022E	2023E	2024E
<b>Revenue</b>	2,963	3,266	3,548	3,758	3,997	4,254	4,543	4,878
COGS	(1,801)	(1,965)	(2,155)	(2,230)	(2,306)	(2,382)	(2,459)	(2,535)
Operating expenses, excl. D&A	(458)	(474)	(509)	(526)	(552)	(579)	(613)	(649)
<b>EBITDA</b>	704	827	884	1,001	1,139	1,293	1,471	1,695
D&A	(58)	(71)	(79)	(81)	(87)	(92)	(99)	(106)
<b>EBIT</b>	646	756	805	920	1,052	1,201	1,373	1,589
Income tax expense	(166)	(196)	(207)	(248)	(284)	(324)	(371)	(429)
<b>EBIAT</b>	480	560	598	672	768	877	1,002	1,160
Add: D&A	58	71	79	119	92	92	99	106
Less: CapEx	(166)	(131)	(180)	(184)	(196)	(208)	(222)	(239)
Less: Change in Net Working Capital	(4)	26	(131)	-	-	-	-	-
<b>Unlevered Free Cash Flows</b>	369	526	366	607	664	761	878	1,027

## DCF Valuation Results

	Forecast				
	2020E	2021E	2022E	2023E	2024E
EBIAT	672	768	877	1,002	1,160
Add: Depreciation & Amortization	119	92	92	99	106
Less: CapEx	(184)	(196)	(208)	(222)	(239)
Less: Change in Net Working Capital	-	-	-	-	-
<b>Unlevered Free Cash Flows</b>	607	664	761	878	1,027
<i>Discount Period</i>	1.0	2.0	3.0	4.0	5.0
WACC	6.3%	6.3%	6.3%	6.3%	6.3%
<i>Discount Factor</i>	0.94	0.88	0.83	0.78	0.74
<b>PV of Unlevered Free Cash Flows</b>	571	588	633	688	757

## DCF Valuation Results

Gordon Growth Method	
PV of Forecast Period	3,236
% of Enterprise Value	15.3%
<u>Terminal Value</u>	
Terminal Year UFCF	1,027
Perpetuity Growth Rate	2.0%
Terminal Value	24,356
PV of Terminal Value	17,945
% of Enterprise Value	84.7%
<b>Enterprise Value</b>	<b>21,181</b>
Less: Net Debt	(2,129)
<b>Equity Value</b>	<b>19,052</b>
Fully Diluted Shares Outstanding	332
<b>Implied Share Price</b>	<b>\$57.39</b>
Current Share Price	\$49.02
<b>Implied Margin of Safety</b>	<b>17.1%</b>

Terminal Multiple Method	
Cumulative PV of Free Cash Flow	3,236
% of Enterprise Value	15.2%
<u>Terminal Value</u>	
Terminal Year EBITDA	1,695
EBITDA Multiple	14.5x
Terminal Value	24,571
PV of Terminal Value	18,103
% of Enterprise Value	84.8%
<b>Enterprise Value</b>	<b>21,340</b>
Less: Net Debt	(2,129)
<b>Equity Value</b>	<b>19,211</b>
Fully Diluted Shares Outstanding	332
<b>Implied Share Price</b>	<b>\$57.86</b>
Current Share Price	\$49.02
<b>Implied Margin of Safety</b>	<b>18.0%</b>

## Sensitivity Analysis

Terminal Growth	WACC				
	5.3%	5.8%	6.3%	6.8%	7.3%
1.50%	53.96	52.72	51.52	50.35	49.21
1.75%	56.87	55.56	54.29	53.06	51.86
<b>2.00%</b>	<b>60.11</b>	<b>58.73</b>	<b>57.39</b>	<b>56.08</b>	<b>54.81</b>
2.25%	63.76	62.29	60.86	59.48	58.13
2.50%	67.88	66.32	64.80	63.32	61.88

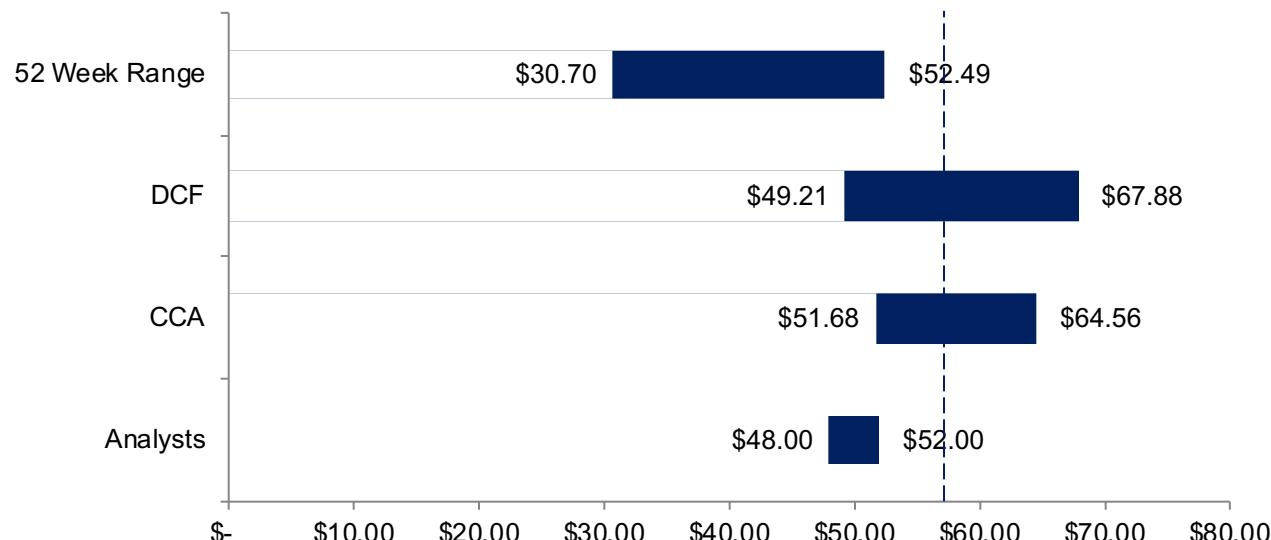
Exit Multiple	WACC				
	5.3%	5.8%	6.3%	6.8%	7.3%
13.5x	56.67	55.37	54.10	52.87	51.68
14.0x	58.64	57.29	55.98	54.71	53.47
<b>14.5x</b>	<b>60.61</b>	<b>59.22</b>	<b>57.86</b>	<b>56.55</b>	<b>55.27</b>
15.0x	62.58	61.14	59.74	58.38	57.06
15.5x	64.56	63.07	61.62	60.22	58.85

Terminal Growth	WACC				
	5.3%	5.8%	6.3%	6.8%	7.3%
1.50%	37.6%	19.4%	51.9%	-6.5%	-16.1%
1.75%	47.1%	26.7%	10.8%	-2.0%	-12.4%
<b>2.00%</b>	<b>58.0%</b>	<b>34.9%</b>	<b>17.1%</b>	<b>3.0%</b>	<b>-8.4%</b>
2.25%	70.8%	44.2%	24.2%	8.6%	-4.0%
2.50%	85.8%	54.9%	32.2%	14.7%	1.0%

Exit Multiple	WACC				
	5.3%	5.8%	6.3%	6.8%	7.3%
13.5x	16.0%	13.1%	10.4%	7.7%	5.1%
14.0x	20.0%	17.1%	14.2%	11.4%	8.7%
<b>14.5x</b>	<b>24.0%</b>	<b>21.0%</b>	<b>18.0%</b>	<b>15.2%</b>	<b>12.4%</b>
15.0x	28.0%	24.9%	21.9%	18.9%	16.0%
15.5x	32.1%	28.8%	25.7%	22.7%	19.7%

## Comparable Companies Analysis

Company Name	Ticker Symbol	Market Data			Financial Data			Valuation					Management		
		Market Cap (\$ Thousands)	Price (\$ / Share)	EV (\$ Thousands)	Sales (\$ Thousands)	EBITDA (\$ Thousands)	EBIT (\$ Thousands)	EV / Sales	EV / EBITDA FY1	EV / EBITDA FY2	EBITDA Margin		ROA	ROE	ROIC
Dollarama	DOL	\$15,642.63	\$49.70	\$18,912.75	\$3,266.09	\$826.11	\$755.56	6.16x	24.35x	17.02x	15.36x	25.97%	20.14%	23.95%	
Dollar Tree	DLTR	\$34,773.03	\$146.39	\$47,673.13	\$30,426.99	\$1,522.52	-\$1,342.49	1.57x	31.32x	15.16x	13.69x	17.06%	7.22%	19.37%	-8.74%
Dollar General	DG	\$47,321.67	\$183.22	\$61,550.50	\$34,451.99	\$5,107.66	\$2,821.23	1.80x	12.13x	17.10x	15.88x	14.88%	9.61%	25.35%	12.71%
Average								3.18x	22.60x	16.43x	14.98x	19.30%			
Median								1.80x	24.35x	17.02x	15.36x	17.06%			



Final Recommendation: BUY

1. Bloomberg
2. Financial Post
3. CBC
4. CapIQ
5. IBIS World
6. Morning Star
7. The Wall Street Journal
8. Thomson Reuters
9. Market Screener
10. Dollarama Financial Statements



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