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# Company overview

Dollarama's journey from a single store in Matane, Québec, in 1992, founded by Larry Rossy, a third-generation retailer, to becoming a leading Canadian value retailer illustrates its remarkable growth and strategic evolution. Under the leadership of Neil Rossy, a fourth-generation retailer, Dollarama expanded its reach to over 1,500 locations across Canada. Dollarama Inc. has secured its place as a dominant player in the Canadian dollar store market, reflected in its significant market cap of CAD 31.24 billion. Initially offering products for $1.00 or less, Dollarama strategically increased its price points to up to $5.00, broadening its product assortment while maintaining compelling value for customers.

**Current Operations:** Dollarama's expansive product range includes household items, cleaning supplies, office supplies, arts and craft materials, seasonal merchandise, and food, sourced both locally and internationally. The company's sourcing strategy utilizes direct imports from over 25 countries and engages North American vendors for 45% of its products, ensuring a diverse and value-driven selection for consumers in metropolitan areas, mid-sized cities, and small towns across Canada.

**Key milestones in Dollarama's history include:**

1. **Establishment and Early Expansion:**
   * Dollarama started with one store in Quebec and quickly expanded across the province. The success in Quebec encouraged the company to open stores in other provinces.
2. **Growth and Diversification:**
   * Throughout the 2000s, Dollarama significantly increased the number of stores across Canada. By 2004, it had over 335 stores in five provinces and continued to grow at a rapid pace.
3. **Public Offering:**
   * In 2009, Dollarama became a publicly traded company on the Toronto Stock Exchange, which was a significant turning point. The IPO was a success, raising significant capital and providing funds for further expansion.
4. **Product and Price Evolution:**
   * Initially, all items at Dollarama were priced at $1.00. However, in response to inflation and the desire to diversify its product offerings, the company introduced multi-price points up to $4.00 by 2016. This allowed Dollarama to expand its range of products, including higher quality items and seasonal goods.
5. **Expansion of Store Network:**
   * By the late 2010s, Dollarama had over 1,000 stores across Canada. The company aimed to have up to 1,700 stores in Canada, according to market analysis.
6. **Technological Improvements:**
   * Dollarama began investing in technology to improve efficiency and customer experience, including upgraded POS systems and inventory management technologies.
7. **Strategic Acquisitions:**
   * In 2019, Dollarama acquired a 50.1% interest in Dollar City, a Central American and Colombian dollar store chain, marking its first international expansion. This move was part of a strategic alliance to share expertise and expand the dollar store model internationally.

**Macroeconomic Environment:** The company witnessed significant growth, escalating to nearly 350 stores by 2004. This growth attracted Bain Capital, which purchased a majority stake to support Dollarama's expansion. Dollarama's public offering in October 2009 marked a pivotal moment in its financial journey, eventually leading to Bain Capital selling its remaining stake, thus ending its direct financial investment in Dollarama.

**Industrial Competitors:** Dollarama's competitive landscape includes both Canadian and American entities. Notably:

* **Loblaw Companies Ltd**: A major Canadian retailer with operations spanning supermarkets and pharmacies, not a direct competitor in the discount retail segment.
* **Dollar General Corp**: A prominent discount retailer in the U.S., targeting low- and middle-income consumers.
* **Dollar Tree Inc**: Operates across single-price and multi-price point discount retail segments in the U.S.
* **Empire Co Ltd**: Primarily focused on grocery and food retail, posing less direct competition to Dollarama.

**Approximate Market Share:** The below financial metric - share values, reflect the companies' market positioning and investor confidence:

* **Dollarama Inc**: $112 CAD, showcasing its solid standing within the Canadian market.
* **Loblaw Companies Ltd**: $149 CAD, indicating its broader retail dominance.
* **Dollar General Corp**: $146 USD, underscoring its significant presence in the U.S. discount retail market.
* **Dollar Tree Inc**: $126 USD, reflecting its competitive edge in the discount retail sector.
* **Empire Co Ltd**: $32 CAD, highlighting its focus on the grocery and food retail sector.

Dollarama's strategic growth, from its inception to its status as a household name and preferred shopping destination, demonstrates its adaptability and efficiency in the dynamic retail industry. Competing in a sector with entities like Loblaw, Dollar General, Dollar Tree, and Empire Co Ltd, Dollarama has carved out a significant niche, continually adapting its operations and offerings to maintain its competitive edge and market share in the discount retail sector.

Company Position in the Retail Market:

Dollarama presents a financially robust profile with several outstanding metrics, including:

A **Price/Earnings (P/E) ratio of 30.91%**, indicating an optimistic investor outlook, despite it being above the industry standard.

A **Gross profit margin of 44.54%,** highlighting cost-effective management and profitability.

An exceptionally high **Return on Equity (ROE) of 265.3%,** signaling strong profitability and efficient equity use.

Conversely, the high **Debt-to-Equity ratio of 1137.89%** suggests a potential over-reliance on debt. Investors should monitor this alongside the company's strategies for debt management and capital structure optimization.

#### Growth Prospects:

The company has a history of outpacing industry growth, with earnings expanding by 13% annually — higher than the multiline retail sector's 10.9% growth. Analysts forecast Dollarama’s earnings to grow by 8.61% per annum, with EPS predicted to increase by 11.2%, showcasing a bright future for the company's profitability and market share.

#### Investment Recommendations:

While Dollarama's market strength and growth outlook make it an appealing buy, its high leverage and above-average P/E ratio suggest caution. The "Hold" recommendation for existing investors captures the value of the company's past performance, while a "Watchful Buy" is advised for new investors, pending improvement in the company's capital structure or market corrections.

# Financial Health Analysis:

#### Current Financial Status:

Dollarama’s financial health, assessed through key ratios and metrics, indicates a robust liquidity position, reflected in its current ratio of 1.93. However, its quick ratio of 0.58 and cash ratio of 0.46 suggest a considerable amount of current assets are tied up in inventory, which might pose liquidity challenges. A debt-to-equity ratio of 1137.89% points to high leverage, which could impact financial flexibility.

#### Balance Sheet, Income Statement, and Cash Flow Statement Analysis:

An examination of Dollarama’s balance sheet uncovers a heavy reliance on debt financing, despite having adequate shareholder equity. The income statement showcases a strong gross profit margin at 44.54%, indicating efficient cost control relative to sales. The net profit margin and return on equity are exceptionally high, underscoring effective management and profitability. The cash flow statements should be closely analyzed to ensure operational activities provide sufficient cash to support growth and service debt.

#### Recent Financial Events or Results:

Dollarama’s recent financial results have been favorable, with consistent revenue growth. However, investors should be cautious of the high debt levels and consider the potential implications of economic downturns on consumer spending and debt servicing. Continuous growth in the company’s earnings per share (EPS) and diligent management of operational expenses have been instrumental in its financial success.

# Monte Carlo Simulation

The Monte Carlo simulation, which projects the stock price trajectory over 30 trading days, predicts a broad range for Dollarama's stock price, potentially oscillating between CAD $100 and CAD $130. The upward trend in the simulation outputs suggests a likelihood of price appreciation over the long term. However, the considerable range also indicates substantial volatility, implying higher-than-average risk for investors.

# CAPM Analysis:

The Capital Asset Pricing Model (CAPM) analysis presents a contrasting view with a beta of -0.050019968, signifying lower systematic risk compared to the market. This suggests that Dollarama's stock price may not be as susceptible to market swings as other stocks. However, the negative beta also indicates a potential inverse relationship with the market, which warrants careful consideration.

The divergence between the Monte Carlo simulation and CAPM results poses a unique scenario. While CAPM points to a lower market risk, the Monte Carlo simulation reveals a broad range of possible stock price outcomes, indicative of high specific risk. This suggests that Dollarama’s stock price movements could be more influenced by idiosyncratic factors or intrinsic company developments rather than market trends.

# WACC Analysis

#### Investment Insight and Recommendation for Dollarama Inc

**Cost of Capital:** Dollarama's WACC stands at 3.37%, which is substantially low. It indicates efficient capital management and potentially less financial risk for the company and its investors.

Market Valuation vs. Intrinsic Value: Dollarama's market price is $112.05, whereas the calculated intrinsic value is $117.88. This suggests that the stock may be slightly undervalued, offering a margin of safety for investors.

**Investment Potential**: The low WACC combined with the company's market price being lower than the intrinsic value indicates an attractive investment opportunity. However, the intrinsic value surpassing the actual share price also calls for a thorough review of market dynamics and the robustness of the intrinsic value calculation.

#### Brief Recommendation:

Based on the current WACC and the close proximity of market price to intrinsic value, Dollarama appears to be a potentially solid investment. Investors should consider this an opportune time to initiate or increase a position in the company, subject to standard due diligence and risk assessment. However, attention should be given to the company's debt management and market factors that may influence the stock's future performance.

# Recommendations

**Investment Recommendation**: Given Dollarama's strong market position, growth potential, and substantial volatility indicated by the Monte Carlo simulation, a Hold recommendation is advised for current investors. For prospective investors, a Cautious Buy recommendation is warranted, contingent on a thorough assessment of their risk tolerance and investment horizon.

**Growth Prospects and Risks:** Dollarama has demonstrated a consistent growth trajectory and profitability, with a robust gross profit margin. However, its high debt levels and liquidity ratios below the ideal range present financial risks. The potential for stock price volatility highlighted by the Monte Carlo simulation adds to the investment risk.

**Strategic Portfolio Placement:** For investors with a diversified portfolio, Dollarama can offer potential growth and dividends. The company's stock could be a strategic addition for those looking to add a retail segment investment with a history of strong performance and an attractive dividend payout ratio.

**Dividend Analysis:** With a dividend payout ratio of 7.53%, Dollarama retains the majority of its earnings for reinvestment. This is beneficial for future growth but yields a modest dividend income for investors. The company’s dividend policy reflects a commitment to shareholder returns while ensuring sufficient capital to finance ongoing operations and expansion.

# Conclusion

The detailed analysis of Dollarama Inc. reveals a complex but promising investment picture. Dollarama stands strong in the retail market with a history of steady growth, profitability, and efficient use of assets. The company's financial health is robust, with a high gross profit margin and an exceptional return on equity, despite concerns over liquidity and high leverage.

The Monte Carlo simulation suggests potential for future stock price appreciation, albeit with notable volatility. In contrast, the CAPM analysis indicates a lower market risk due to a negative beta value. These findings underline Dollarama’s exposure to company-specific risks rather than market-wide fluctuations.

Considering all factors, the final investment recommendation for Dollarama is a Cautious Buy for investors with a higher risk appetite and a Hold for existing shareholders. This recommendation is based on Dollarama’s solid market position, potential for growth, and financial stability balanced against the risks of high leverage and potential volatility in stock price.