Disnat GPS Report

Dollar General (DG, U$73.62)

Desjardins Online Brokerage

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General Comments

Dollar General is a leader in low-priced retailing, with products that cost between $1 and $10 (mostly under $5).

In this new economy where Amazon and other online retailers are multiplying, retail in physical stores is seeing hard times.

However, not only is Dollar General one of the few companies that will not reduce its number of locations, but rather it will increase them substantially over the next few years.

Dollar General now has about 13,000 stores and plans to increase that number to more than 25,000.

While ambitious, the addition of 1,000 new stores in 2017, compared to 830 in 2016, not only increases the number of stores, but also increases the number of new stores opened year over year!

In addition, the company's strategy, which consists mainly of placing itself in small markets (about 70% of the stores are located in cities with less than 20,000 residents), protects it from larger players which do not find the critical mass necessary to make their business profitable.

This strategy of targeting smaller communities reduces potential competition, as well as allowing Dollar General to lease spaces at a particularly affordable price.

In addition, smaller stores like those of Dollar General allow for a reduction in the number of employees required per square foot.

Lower rental costs, fewer employees per square foot and smaller inventories are all factors that enable the company to enjoy operating costs of $44 per square foot, compared to $78 for Walmart and $56 for Target.

While retail is going through a difficult period, it is clear that the problems faced by some companies in this sector do not seem to affect Dollar General's financial health. On the contrary, the disappearance or reduction of the offer of certain players favors the development of this company.

In a rapidly evolving world in which retailing is increasingly centralized, Dollar General is particularly well positioned to face music!

Other Disnat GPS reports available: Apple, Disney, Nike, Cisco, Microsoft, AT&T and Facebook.

Financial Health

Fiscal Year	2015	2016	2017
Long term debt (in billions of dollars)	2.8	2.8	2.7
Debt/equity ratio	0.46	0.54	0.50

Dollar General's financial health is particularly strong.

The company's debt/equity ratio of 0.50 is less than half that of its main competitor, Dollar Tree.

Not only is debt under control but the fact that the company distributes dividends and regularly redeems its shares shows that this debt is not related to a lack of solvency or liquidity.

On the contrary, its stability confirms that the current level of debt is a choice made by management to optimize its capital structure.

In terms of financial health, the company is an example of good management: its capital structure is optimal, it has not accumulated too much cash which could lead to doubtful investments and its debt is under control.

While its competitor, Dollar Tree, must continue integrating Family Dollar and work to reduce its debt, Dollar General can continue to develop its own network by keeping its finances in order!

Growth

Compound Yield	1 year	3 years	5 years	10 years
Earnings	7.9%	7.9%	8.2%	9.1%
Earnings per share	12%	11%	15%	26%

The growth of Dollar General's revenue and earnings per share over the past five or ten years has been very strong and stable.

The prospect of increasing the number of stores – management believes it can almost double them – and the benefit of better profit margins on private label products should enable the company to post good growth for several years.

In addition, Dollar General's strong competitive position in a relatively safe and resilient niche and its many points of sale could make it a prime target for companies in this sector seeking to expand.

The acquisition of Dollar General could significantly accelerate the development of Amazon, which does not have a large network of physical stores, or Walmart, which might want to enter this lucrative market. At only $20 billion in market capitalization, the cost is very low for companies of this size.

Low priced retail is one of the few sectors that seems to resist online commerce in general and Amazon in particular. This should allow for regular and steady growth for a long time!

Valuation

Key Ratios	DG	DG (5 yr avg)	S&P 500
Price/earnings	16.7	19.3	21.2
Forward price/earnings	16.6	n.a.	19.7
Dividend yield	1.4%	n.a.	2.1%

Dollar General's valuation, and more specifically its undervaluation, is one of the main reasons for our interest in this company.

In terms of future price/earnings and price/earnings ratios, this stock is currently trading at a discount compared to its past five year average. In addition, it is also trading at a high discount compared to the S&P 500.

Currently, the market places a much lower value on a dollar of profit from Dollar General than a dollar of profit from an average S&P 500 company.

We do not agree with the view that more than 250 companies in the S&P 500 have a more promising future than Dollar General.

At Disnat GPS, we believe the market is pricing Dollar General below its fair value. We are therefore very pleased to hold a superior company at a relatively low price!

Governance

Fiscal Year	2013	2014	2015	2016	2017
Earnings per share ($)	2.85	3.17	3.49	3.95	4.43
Dividend ($)	n.a.	n.a.	n.a.	0.88	1.00
Number of shares (millions)	334	324	306	295	282

Dollar General is a growing company that is quietly transforming into a more valuable business.

The company, which introduced a dividend in 2016, is far from being an "aristocrat" – a nickname given to companies that have increased their dividend over the past 25 years – but the first dividend and its increase the following year suggest that the company intends to apply this management philosophy for years to come.

Dollar General regularly buys a portion of its stock. Over the past five years, it has purchased more than 15% of its outstanding shares. The Company maintains a share repurchase program, which it continues to employ when the situation permits. In terms of development, we do not anticipate big acquisitions for now.

Thanks to its growth through the opening of new stores, the dividend yield it offers to its investors and its share buyback program, Dollar General represents everything Disnat GPS is looking for – and has found! – in a company.

Explanatory Notes

Disnat GPS reports contain five separate sections, each followed by comments from the Disnat GPS Portfolio Strategist regarding the following:

1. Company Description

2. Financial Health

3. Growth

4. Valuation

5. Governance

At Disnat GPS, we believe that the topics, ratios and other financial figures presented here are particularly important.

However, for reasons of space, we can not publish all available data. We therefore invite you to read the additional financial information on the Disnat website.

Furthermore, this report is an analysis of the condition of a company today, with a medium to long term view. It is in no way an adequate tracking of daily activities of the stock market in general or of this particular company.

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