3 Top Retail Stocks for 2017 (and 1 to Avoid)

Description

It hasn't been the greatest year for Canada's top retailers.

Consumer debt continues to be a big problem. The average person in Canada is deeper in debt than ever, owing nearly 170% of their annual disposable income. Yes, low interest rates do help with debt-servicing costs, but there's a limit to how much we can collectively borrow. It appears we're getting pretty close to that limit.

Then there's the overcapacity issue. A number of small- and medium-sized retail chains shut their doors for good in 2016, because there are just too many companies looking for the same dollar. Continued strength from online-only retailers sure didn't help either.

And 2017 should see a continuation of 2016's trends. The strong will keep dominating, while the weak will keep suffering.

Here are three top retail picks for 2017 as well as one chain I'd avoid at all costs.

Canadian Tire

I firmly believe **Canadian Tire Corporation Limited** (TSX:CTC.A) is Canada's top retailer.

It has many things going for it, including a diverse group of banners, strong same-store sales, a solid presence across the country, a financial services division that continues to grow, and valuable real estate that has been flipped into a REIT, creating more shareholder value.

Canadian Tire has traditionally been a growth-by-acquisition story, and it certainly has the balance sheet strength to pull off a deal if management chooses. It has nearly $500 million in cash and just $4.2 billion in debt–a reasonable amount for a company worth almost $11 billion.

Investors are also buying shares today for approximately 16 times earnings with a dividend yield of 1.8%. With one of the lowest payout ratios out there, Canadian Tire is well prepared to grow that distribution too.

Hudson’s Bay

Hudson’s Bay Co (TSX:HBC) is a different story. This stock is all about the real estate.

According to management’s investor presentation at the 2016 annual meeting, Hudson’s Bay is sitting on $36 per share of real estate versus today’s share price of under $14. The company is also actively working towards spinning off that real estate into its own REIT. It’s only a matter of time.

And, as a bonus, investors are getting a retailer that did $632 million in EBITDA over the last 12 months essentially for free. Even without the real estate, HBC trades at less than four times EBITDA versus nearly seven times EBITDA when it IPO’d back in 2012.

North West Company

Let’s shift focus from Canada’s oldest company to its second-oldest. **North West Company Inc.** (TSX:NWC) is a specialty retailer with a strong presence in northern communities. It also has operations in the Caribbean, South Pacific, and Alaska.

North West is often the only retailer in town, giving it the kind of pricing power we don’t often see in a sector flooded with competition. Shares are currently trading at close to a 52-week low, and the yield of 4.8% is well covered by cash flow.

Sears Canada

Poor **Sears Canada Inc.** (TSX:SCC). Shares are down more than 75% over the last year alone as more and more investors start to speculate that the chain’s bankruptcy will happen soon.

Quarterly losses are widening. The company lost more than $90 million in the second quarter alone–a huge blow for a business with a market cap of $225 million. It’s also bleeding cash like crazy. A year ago, book value was $530 million. These days, it’s $390 million.

The company recently announced it would start selling groceries at some of its renovated locations. It’s a desperate move by a company with one foot in the grave.

The bottom line

Canadian Tire, Hudson’s Bay, and North West Company are all good retailers. They are poised to do well in 2017.

Sears Canada is another story. The company may survive 2017, but that’s hardly enough reason to add shares to your portfolio–even if they are incredibly cheap.

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1. Dividend Stocks

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1. Editor's Choice

TICKERS GLOBAL

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2. TSX:NWC (The North West Company Inc.)

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