What Will it Take for These Beaten-Down Stocks to Shoot Higher?

Description

The following stocks have one thing in common: their share prices have declined significantly from their 52-week highs.

Why are their shares depressed? And what will it take for them to head higher?

Empire Company Limited (TSX:EMP.A) has more than 1,500 food-retailing stores and 350 retail fuel locations across all 10 Canadian provinces. It operates under the banners of Sobeys, Safeway, IGA, Foodland, FreshCo, Thrifty Foods, and Lawton's Drug Stores.

Food-retailing businesses have historically been defensive stocks. If so, then why has Empire's share price declined more than 36% from its high in 2015? In fact, at under $19 per share, Empire stock is trading at its 2012 levels.

It turns out its share price has been following the deterioration of company fundamentals. Specifically, in the last 12 months, Empire posted a net income loss of $2.17 billion, which was primarily due to the write-down of certain store assets in the Sobeys West operating segment.

In the most recent quarter, Empire faced challenges in the West business unit and soft sales trends in most of the store network.

What will it take for Empire shares to head higher?

If the company overcomes the operational challenges it has faced in the last year, earnings should start to recover at some point. Some things that management is doing include optimizing the execution of the store level offerings and reducing costs.

The takeaway

Although Empire stock has declined for more than a year, it's not priced at a bargain because of its declining earnings. Before its shares can go higher, it'll first need to show some sign of recovery.

In fiscal 2016, Empire's earnings per share declined 20%. If it can show a slower rate of earnings decline in subsequent quarters, the shares should start bottoming.

stock up arrow market

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Goldcorp Inc. (TSX:G)(NYSE:GG) is a large gold miner with operations in politically stable, low-risk jurisdictions in the Americas.

Goldcorp's all-in sustaining costs of producing gold are expected to be US$850-925 per ounce, which is below the price of gold, which has stayed above US$1,050 per ounce for the year and is about US$1,160 currently.

Goldcorp has one of the strongest balance sheets in the sector. It has an S&P credit rating of BBB+ and a debt-to-cap ratio of 16%. Compare that to **Barrick Gold Corp.'s** S&P credit rating of BBB- and debt-to-cap of 45%.

Goldcorp shares have declined 33% from its 52-week high, but they have appreciated nearly 9% year-to-date. The company had positive free cash flow last year and is expected to generate positive free cash flow again this year.

What will it take for Goldcorp shares to go higher?

Historically, gold prices have an inverse relationship with the U.S. dollar. Since the U.S. dollar is expected to remain strong from continued economic strength in the country, it's expected that gold prices won't head higher in the near term.

Additionally, there's a general negative sentiment around precious metals stocks. Goldcorp stock has been stuck in a declining trend since 2012. However, the shares might have bottomed at the start of the year.

If gold prices head higher, or if Goldcorp continues to improve its operations, the company should result in higher free cash flows, which should lead to a higher share price.

The takeaway

Goldcorp is a well-run gold producer with a strong balance sheet. If you want to gain exposure to the precious metals sector with ample upside potential, the large-cap company is a logical choice. Some analysts believe Goldcorp is worth $28, but it might take a few years for it to get there.

Bottom line

Turnaround investments can take longer than expected before things work out. They also carry higher risk than companies that are doing well. So, don’t bet the farm on turnaround candidates. Instead, limit a small percentage of your portfolio to them for potential outsized gains.

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1. Dividend Stocks
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1. TSX:EMP.A (Empire Company Limited)

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