Worried About Stocks? 3 Easy Ways to Protect Your Dollars

Description

As the TSX Composite Index continues to flirt with all-time highs, certain investors are starting to get nervous. It happens every time. It's a very reasonable thing to do. Those of us who invested heavily during late 2015 and early 2016's downturn are now sitting on some hefty gains. Perhaps it's time to take our profits and move on to other investments, preferably those without a direct correlation to the stock market.

There's just one problem: opportunity costs are incredibly important. Say you take your money out of stocks today and invest it in a GIC yielding 1.5%. Let's also say stocks go up an additional 20% from here before falling 15%. If this takes two years to play out, the person investing in a GIC is 3% richer. The person who held on to their stocks the whole time is still up 2%. The person who got out of stocks is barely better off.

And that's assuming stocks crash. What if they don't?

Still, there are plenty of solutions to this problem short of selling all your stocks and sitting in cash. Here are three ways you can protect your capital.

Selectively sell winners

In a world where many stocks sell at inflated price-to-earnings multiples, it's hard to sell something that's expensive. After all, you'll just have to put that money to work in something else that's overvalued.

Still, there are certain stocks that have really shot past any reasonable valuations. Those companies are great sell candidates today.

One example is **Dollarama Inc.** (TSX:DOL), the fast-growing discount retailer. The company has consistently posted terrific revenue and net income growth, fueled by increasing same-store sales, higher price points (you can now buy $4 items at your local Dollarama), and new store openings.

There's just one problem: shares trade at 29 times trailing earnings. That's expensive, even in this market. If I held Dollarama shares, I would take a serious look at reducing my exposure.

Get boring

If a stock like Dollarama is more volatile than the market as a whole, the solution is simple. Get out of risky stocks and switch to something more boring.

Canadian Utilities Limited (TSX:CU) is the perfect example of a boring stock that can still make you rich. It has 87,000 km of electric power lines, 63,000 km of pipelines, and 15 power plants with 3,587 MW of capacity. It also has seven manufacturing plants that produce temporary structures.

Canadian Utilities is a dividend-growth machine. It has raised its dividend for 45 consecutive years, culminating with a 10% hike earlier this year. Shares currently pay 3.7%.

The company has a beta of 0.17, according to Google Finance. That means shares are just 17% as volatile as the market itself, making it the perfect company to hold if you're nervous.

Embrace preferred shares

Many investors will start to up their fixed-income exposure as stocks go ever higher. But it's hard to find a corporate bond paying more than 3%.

Preferred shares are a nice alternative. Yes, they are a little more exposed to interest rates than the average bond — because a preferred share is essentially a perpetual bond — but investors are compensated for that risk with extra yield. Besides, when stocks tank, interest rates usually aren't going up.

Most preferred shares issued by solid Canadian companies yield about 5% today, making them a great income option. Canada's five major banks are among the country's most active preferred share issuers. It's hard to go wrong with backing like that.

And if an investor holds a preferred share yielding 5% in a non-registered account, it qualifies for the dividend tax credit. A 5% yield on a dividend is the equivalent of 6% or 7% on a bond, depending on your tax situation.

The bottom line

Stocks are expensive. That much is obvious.

This market rally could continue indefinitely, or it could fizzle out. Nobody knows for sure. That's the fun of investing.

Investors who are a little nervous about things can sell overpriced stocks — like Dollarama — and switch into more boring names like Canadian Utilities. Or they can embrace preferred shares. If stocks do tank, you'll be very happy you made these moves today.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. TSX:CU (Canadian Utilities Limited)
2. TSX:DOL (Dollarama Inc.)

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Date
2025/08/26
Date Created
2017/03/16
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