Save Your Money on Canadian Tire Corporation Limited Stock

Description

If you'd bought **Canadian Tire Corporation Limited** (TSX:CTC.A) stock in early August, congratulations; you're sitting on a 48% annualized gain.

In the ninth year of a bull market, buying stocks on the dips has become a bit of a rallying cry for investors.

A classic example of why you should consider buying on the dips came on December 1, when the S&P 500 dropped more than 1.6% on the news that former U.S. National Security Adviser Michael Flynn would testify against his former boss, Donald Trump.

By the end of the day, the index was off just 0.3%, as investors shook off the ramifications of the U.S. president potentially being caught in a lie.

"I would buy any large sell-off, and I will continue to advise that course of action until I see signs of recession, because ultimately that is what will signal the end of this bull market," said Chris Zaccarelli, chief investment officer of Independent Advisor Alliance in a note to clients.

The problem with this theory is that when a dip happens, you don't know whether it's the first leg down of a lengthy correction or just a blip that shakes out the weak hands.

Only buy quality companies

When you're using this strategy, you want to buy stocks that are going to be around in five, 10, or 20 years or more, like Canadian Tire.

I'm no technical analyst, so here's how I consider whether or not to pull the trigger on a stock.

Go back five years and find out how many times a stock has dropped by 10% in a single month of trading. Canadian Tire hasn't seen a 10% dip in a calendar month at any time since December 2012.

Therefore, you've got to broaden your search beyond a 30-day period.

For example, Canadian Tire was trading around $166 at the beginning of May. By the end of July, it was down to $142 — a 17% decline in just three months. The biggest previous decline before this year was 17.8% between November 30, 2015, and January 11, 2016 — a period of just six weeks.

Investors tend to overreact to both good news and bad news with an equal amount of irrational exuberance or fear.

In the case of Canadian Tire, this year's big decline was due to a bad first quarter from its legacy brand, which accounts for the lion's share of its annual revenue. At the time, I'd said I still believed in its stock, but that the company must do a better job with the Canadian Tire brand; in the two quarters since, the company has righted the ship and its stock has rebounded.

The only thing I can think of regarding its decline in late 2015 and early 2016 is the idiom, "Buy on rumours, sell on news."

Fool contributor Joseph Solitro discussed the company's Q3 2015 earnings shortly after it announced them November 11, 2015, and they were impressive. Solitro finished his article by suggesting investors begin building a position in Canadian Tire stock.

It's up 30% since. Good call, Mr. Solitro!

Bottom line on Canadian Tire stock

The headline for this story is meant to be somewhat facetious.

I like Canadian Tire as a long-term buy-and-hold investment, but I believe that this is one of those quality companies where you ought to pay attention when its stock is trading significantly lower over a short period, because even if it keeps dropping for a time after you've bought, the good ones always recover.

Look no further than its performance since the beginning of August for confirmation of this.

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