The Canadian Economy May Be Overheating: How to Invest

Description

While the general mood continues to be bullish, it can't be denied that there are more than a few warnings signs in the economy. Let's go through a few of the reasons why investors need to be cautious at the moment and a few ways to hedge your bets just in case things take a turn for the worst. We'll look at three industries that should continue to fare well and may even get a boost should an economic downturn rear its head.

Almost a year ago, the Bank of Canada warned that the greatest threats to the economy were household debt and home prices. How have things changed since then? The fact is that they haven't, while a situation exists in which inflation seems likely. Let's see how a shrewd investor might shore up their portfolio.

Canadian Tire (TSX:CTC.A)

The combination of patriotism, hardware, and toys is likely to be a big hit if the economy tanks. Expect stocks like Canadian Tire to do well in a recession in much the same way as multi-line retailers did in the U.S. immediately post-2008.

This popular stock is overvalued by not quite 10% of its expected future cash flow value. If shares seem a little pricey at $163 a pop, that's because they are, but not by much: a P/E ratio of 15.9 times earnings isn't too bad, while a PEG of 1.3 times growth is acceptable. A P/B of 2.4 times book is a little high, though.

Canadian Tire is looking at a 12.1% expected annual growth in earnings, which is good for retail at the moment. It offers a dividend yield 2.21% at today's price, which is trending generally upwards, though it did see a sharp fall-off after the summer's Q2 report.

Loblaw (TSX:L)

Discounted by 25% compared to its future cash flow value, this go-to grocery stock is looking like a so-so buy today. Its fundamentals are a little hot — look at a P/E of 19.6 times earnings and P/B of 2.1 times book — but there's nothing too off-putting for this recession-ready stock.

You're looking at a 16.9 % expected contraction in earnings over the next one to three years, though, if you get invested in Loblaw, and its dividend yield is not much to write home about at 1.75%. However, come back in five years, and we'll see what those figures look like then.

Sienna Senior Living (TSX:SIA)

If you're looking for Canadian healthcare stocks that could make you rich, you may want to keep an eye on Sienna Senior Living. It's certainly one of the better valued of such stocks on the TSX, along with competitors such as **Chartwell Retirement Residences**, **Extendicare**, and **Medical Facilities**.

A P/E of 65.4 times earnings is rather worrying, to be honest, and doesn't speak well to this stock's valuation today. A P/B ratio of times book of twice book beats the Canadian healthcare average, but bear in mind that pharma medical aid stocks may be skewing the mean valuation.

However, this stock is looking at a 29.6% expected annual growth in earnings over the next one to three years and pays a dividend yield of 5.24% at today's price of $17.53, which has been trending generally downward this year, though it's picked up since a recent dividend increase.

The bottom line

Trawling through lists of which U.S. stocks have soared during the 2008 financial crisis gives a few ideas for recession-proofing a Canadian portfolio. Stocks in groceries, elderly care, and any store that sells hardware supplies and toys are going to do well if an economic downturn hits our shores. An inflation rate of 3% may be a warning sign to start investing in recession-proof stocks such as Canadian Tire and the two others listed here.

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2. TSX:L (Loblaw Companies Limited)
3. TSX:SIA (Sienna Senior Living Inc.)

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Date
2025/08/20
Date Created
2018/09/05
Author
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