As the Consumer Weakens, Stay Away From These 3 Stocks

Description

Canadian household debt has crept up again in the second quarter, as the debt to disposable income ratio hit 169.1%.

This was up from the prior quarter, but down from a year ago.

But overall, the trend is that it is headed lower, which is what we would expect given the cooling housing market and rising interest rates.

So what is the takeaway for investors?

I think that investors have to pay attention to this, as it relates to some of the favourite stocks out there, such as **Dollarama Inc**. (TSX:DOL), **Canada Goose Holdings Inc**. (TSX:GOOS)(NYSE:GOOS), and **Roots Corporation** (TSX:ROOT), many of which have been trading at exorbitant multiples.

And these danger signs are already appearing in the results, so this risk cannot no longer be ignored.

With Dollarama's second-quarter fiscal 2019 sales falling short of expectations, Dollarama stock was pummeled that day, falling almost 20%.

Year-to-date the stock is down 18%.

We are now seeing same-store sales continuing to slow and gross margins continuing to increase, and we can expect that these trends will continue into fiscal 2019.

Dollarama stock is now trading at 25 times this year's EPS expectation, down from the 29 times P/E multiple it was trading at a few weeks ago, but still high.

Earnings are expected to increase in the mid-teens range, and although margins are coming in strong, the reductions in sales momentum is concerning.

Roots stock is trading more than 30% below its IPO price once again as the stock continues its volatile ride.

I do not view valuation as attractive on Roots stock, although it is quite low at less than 10 times earnings.

As the challenges remain, and with second-quarter results that have come in below expectations. As same-store sales increased a very modest 1.1%, the future is unclear.

With slowing consumer spending, the company will have added difficulties with its expansion to the U.S., which has proven to be a very risky move even in the best of times.

Canada Goose stock is trading 16% below highs that were hit earlier this year, and while this is a sharp drop, the stock is still trading at sky high valuations that are not sustainable in my view, especially considering a weakening consumer spending environment and the company's increased investments in China.

Canada Goose has been very successful in establishing its premium outerwear brand, with consumers paying upward of $800 for their Canada Goose jackets. Going forward, however, the key risks remain.

The company has been globally expanding, but 39% of its revenue still comes from Canada, and as such, it is still vulnerable to a weakening in Canadians' purchasing power.

The company has numerous other risks associated with it, including its concentration risk given that 98% of its sales are in outerwear, as well as potential problems that may arise given PETA's vocal opposition to Canada Goose using goose, duck feathers and coyote fur in its apparel.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:GOOS (Canada Goose)
2. TSX:DOL (Dollarama Inc.)
3. TSX:GOOS (Canada Goose)
4. TSX:ROOT (Roots Corporation)

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