Is There Still Too Much Risk in Air Canada (TSX:AC) and Dollarama Inc. (TSX:DOL) Shares?

Description

The consumer has been a big driver of economic growth in recent years. And with record low interest rates of 0.5% from 2015 until the end of 2017, and the strong housing market, this is no surprise.

But times are changing. Interest rates have risen steadily since 2017 from 0.5% to the current 1.5%. Economic growth is strong and inflation is creeping up, and this supports further rate hikes. And while this is still low compared to history, make no mistake, rates are going higher and consumers will feel it, as they are drowning in debt. In fact, economists are warning that household debt is a major risk to Canada's economy in light of this reality.

So, in this context, here are two stocks that I would avoid.

Dollarama (TSX:DOL)

Although Dollarama stock had been an investor darling for a long period of time, the stock has lost its shine amid slowing same-store sales growth and a downward re-valuation.

With its second-quarter fiscal 2019 sales falling short of expectations, Dollarama stock got pummeled, falling almost 20% on the day of the report. It is now down 24% year to date, as earnings expectations have come down, reflecting a slowing environment.

At the end of the day, Dollarama stock had been very richly valued, as investors had come to expect strong increases in sales, and last quarter's 2.6% increase in same-store sales is not one that would warrant such rich valuations.

At a time of a weakening consumer, rising interest rates, and a consumer at risk, a retailer is not the best stock to be invested in, especially one that still trades at 24.5 times earnings.

Air Canada (TSX:AC)(TSX:AC.B)

While the five-year chart on Air Canada stock looks very impressive, showing a return of more than

370%, the last year has been less impressive, with the stock falling 11% amid plenty of volatility.

This is despite that fact that the airliner continues to do the right things in its quest to transform itself into a profitable business through the cycles, with a focus on return on invested capital.

So, what caused Air Canada's stock price weakness?

Well, here we have a double whammy.

Of course, I think investors are concerned about the consumer as interest rates continue to rise, but also fuel prices are rising dramatically, putting additional pressure on Air Canada stock.

With oil trading above $70, this is problematic for Air Canada, as we can see in the fact that jet fuel price increased 31% versus last year.

And although ticket pricing has been offsetting increases in fuel prices, as the airliner has been able to raise fares without seeing a hit to traffic, an unfavourable dynamic is setting up here.

So, in summary, I would stay away from these two stocks that are very dependent on discretionary consumer spending, which is at risk in the next few years as interest rates rise.

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