Retail Stocks Get a Breath of Fresh Air in 2019

Description

In the roller-coaster ride of retail sales, there does not seem to be a dull moment.

Retail sales in Canada rose in February, by 0.8%, after many months of declines, as Canadians loosened their purse strings once again amid a rising stock market and household wealth that has so far really held up better than what was feared.

All of this has had the effect of leaving investors feeling pretty secure, providing that green light to spend a little more freely again.

Interest rates are not rising any time soon, investors can maintain their debtloads, and, although these debt levels are higher than they "should" be, in the short term, consumers can maintain this balancing act.

So, where does that leave us with regard to retail stocks? Should we be loading up on them again?

Dollarama (TSX:DOL)

Dollarama stock has made somewhat of a comeback, up 35% from its 2018 lows as it rallies off all the good news in the market these days.

In its former glory, Dollarama stock commanded a price-to-earnings multiple of 35 times, as sales skyrocketed and margins continued to rise.

These days, the stock is trading at multiples of 24.5 times last year's earnings and just over 22 times this year's earnings estimate, as the stock has fallen 22% from its 2018 highs due to slowing sales growth, earnings growth, and falling gross margins.

The last three quarters saw the company report earnings that were below expectations, and while these misses were not big misses, that's still three consecutive misses.

Earnings growth has come down to levels closer to 10% compared to earnings growth of almost 25% a few years ago.

So, if we consider these lower growth rates, we can see that a 22 times earnings multiple doesn't look that great.

Canada Goose Holdings (TSX:GOOS)(NYSE:GOOS)

Canada Goose reported its third-quarter fiscal 2019 results recently, which highlighted why investors love this stock.

Revenue increased 50% and EPS increased 66%, driven by an increase in sales due to five new stores, the launch of a new e-commerce site, and increasing gross margins.

But on that day of the release, the stock fell by approximately 13%, as investors reacted to lower-than-expected margin improvements; it seems clear that investors' expectations baked into the stock were very high.

And, in fact, the stock has fallen 22% from its 2018 highs in what is a classic case of what happens when a stock is priced for perfection.

Canada Goose stock is now trading at approximately 55 times this year's expected earnings. That's still high, even considering the earnings-growth rates the company has historically achieved.

Final thoughts

In summary, the consumer and retail environment are certainly looking better today than in the recent past.

But although the consumer seems to have found its groove again, and rates are not going up any time soon, consumers remain heavily indebted, with many risks going forward.

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