Warning: This Famous Investor Just Called Out Canadian Tire (TSX:CTC.A)

Description

Recently, Steve Eisman, who is famous from his role in *The Big Short,* sounded an alarm over **Canadian Tire** (TSX:CTC.A) and specifically its financial arm and credit card portfolio.

Canadian Tire has quietly built its credit card business the last few years and now it accounts for roughly a third of its business.

Eisman, however, believes this may be an issue, especially if his thoughts on the Canadian credit markets materialize.

default watermark

The threat

It's no secret that debt has been rising for a long time in Canada, led by consumer debt. As this debt continues to grow and reach new record highs almost every quarter, many prominent investors and economists have issued major warnings about how it may turn out.

Eisman has been one of them, and he has been vocal on the Canadian debt markets for years. While in the end, he may not be wrong, till now, he's been early. So far, none of what Eisman has said has panned out, but the situation hasn't gotten any better either.

What is interesting about Eisman's latest comments is that he is one of the first big-name investors to name Canadian Tire as a potential victim.

The worry with increasing consumer debt is that unless there is a considerable increase in income for consumers, at some point, they will have to reduce their consumption to repay the debts from all these years they have overconsumed.

The trouble is, any meaningful reduction in consumption could trigger a recession, especially if spending is reduced enough that the economy's growth turns negative.

Canadian Tire's portfolio

Canadian Tire's credit card portfolio has been growing in recent years. This is part of why Eisman thinks there may be a problem. It makes sense to think that prudent lenders in a credit environment such as Canada's would be originating newer loans and issuing credit cards less often as they managed their risks.

Until now, the banks and Canadian Tire haven't shown any signs of concern in the markets. This leads us to the question of who is right.

Looking at Canadian Tire's credit card portfolio, it had gross average credit card receivables growth of nearly 8% in the second quarter. About half of the increase came from new credit card accounts opened, and the other half came from larger monthly balances carried over.

This increased its normalized earnings before taxes around 12.5% to just under $100 million for the quarter. In the retail segment, the company did about $135 million in income before taxes, and the consolidated company income before taxes was just under $270 million.

This means that the financial arm did roughly 35% of the company's total business in the second quarter.

default watermark

What's also concerning is that a large number of the credit card holders are sub-prime borrowers, who are obviously the most at risk if the economic environment were to soften.

The large portion of business has been a great tailwind for the company to this point, and it has rewarded investors handsomely, but if the credit market does pose a problem for Canadian Tire, it is clearly largely exposed.

Bottom line

Whether or not there is a big event in the Canadian consumer credit markets, consumer debt is still at all-time highs.

Even if investors get lucky and there isn't a massive crash, further growth may not materialize for some time down the line, as the economy corrects to a more sustainable position, but that, of course, would be a best-case scenario.

Investors in any companies that have a loan portfolio should be aware of the risks that exist, especially in the near term as global growth begins to slow.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. TSX:CTC.A (Canadian Tire Corporation, Limited)

PARTNER-FEEDS

1. Business Insider
2. Msn
3. Newscred
4. Sharewise
5. Yahoo CA

Category

1. Dividend Stocks
2. Investing

Date
2025/08/29
Date Created
2019/09/23
Author
danieldacosta

default watermark

default watermark