What Is Wrong With Canada Goose (TSX:GOOS) Stock?

Description

Canada Goose Holdings Inc (TSX:GOOS)(NYSE:GOOS) used to be the top-performing stock in Canada. In 2017, the stock was priced at just $20. By late 2018, it surpassed $90 per share.

This year has completely destroyed that narrative, with the stock price sinking lower and lower, hitting $40 per share this week. What's going on? Is this a broken story or a chance for smart investors to profit?

Sales are still rising

Canada Goose stock may be slowing down, but sales continue to increase at a rapid pace. Last year, revenue was up by at least 28% across every geography. Some geographies grew sales by more than 50%.

This financial performance shouldn't have been a surprise. In 2017, sales were just $404 million, increasing to $591 million in 2018. Last year, sales surpassed $830 million. This strong momentum won't stop anytime soon.

Profitability is also on the rise. EPS rose from $0.43 in 2017 to $0.84 in 2018, rising again to $1.36 in 2019. Higher sales were obviously a factor, but margins also contributed.

In 2017, EBIT margins were 18.5%, already near the top of the industry. In 2019, management was able to increase margins even further to 24.9%.

Over the next several years, management expects sales to increase by at least 20% per year, with EPS growing by at least 25% annually. In 2022, the company anticipates earning a minimum of $2.66 per share, which means the stock trades at 15.4 times 2022 earnings. That's a bargain valuation for a company growing this quickly.

What's wrong?

Canada Goose appears to be running on all cylinders. What's the problem?

Above all, the stock market is an expectations game. While past history is telling, value will largely come from future performance. In 2018, when shares were trading above $90, the stock had a valuation above 100 times earnings. The market was simply pricing in too much.

When management released its long-term guidance, calling for 20% annual sales growth and 25% annual EPS growth, the market realized that it had *over-estimated* future performance. The company was still growing like a weed, but built-in expectations needed to be revised.

Shares reset to the $60 to $70 per share range, but over the coming months, the stock slipped further, recently dipping below $40. Now what's wrong?

Around one-third of sales currently come from Asia, the largest luxury market in the world. Less than one-quarter of sales stem from China.

Canada Goose has only begun investing in the region, which posted 61% sales growth last year. Long term, this opportunity could double or triple the size of the company.

With slowing growth and health concerns, including the deadly coronavirus, the market has been reassessing potential growth. Management is still confident long term, but the ultimate impact on consumer spending is still unclear. What was supposed to be a record year could turn well out to be a dud.

How to invest

There's no doubt that Canada Goose stock is cheap right now. Apart from China concerns, the stock market seems to have corrected too far. Shares were over-priced in 2018, but following a weak 2019, the stock looks like a bargain.

But what to make of Asian growth? Chinese consumer spending will undoubtedly take a huge hit. Despite slowing GDP, however, luxury spending is still expected to rise considerably this decade. The downturn could be an excellent opportunity to turn short-term pain into long-term gain.

It's not very often that you can snag a company trading this quickly for less than 25 times forward earnings. As long as you can withstand volatility in 2020, however, patient investors should be heavily rewarded.

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