Capitalize on the Correction With This Growth Stock

Description

Canada Goose Holdings Inc (TSX:GOOS)(NYSE:GOOS) stock was incredibly profitable for shareholders. Between 2017 and 2018, shares roughly quadrupled. Sales and earnings were rising at breakneck speeds. The market assigned the stock a lofty valuation of 150 times earnings.

Notice that all of this story has been in the *past* tense. In 2019, the company continued to grow, but investors assigned the stock a lower valuation multiple, resulting in a quick correction. Then the coronavirus hit.

Today, Canada Goose stock trades at $30 per share, the same price it traded at in 2017. On nearly every metric, this stock is too cheap to ignore. There are risks, but if you can understand them, this could be a great way to profit.

Understand the opportunity

Canada Goose went from market darling to the bargain bin in the span of a single year. What makes such a high-flying stock turn such a sharp corner?

To understand what happened, you have to understand what investors thought *would* happen. When the company was growing quickly in 2017 and 2018, investors had their eye on the biggest prize of all: China.

As the largest luxury market in the world, China could allow Canada Goose to triple in size in just a handful of years. Better yet, the company had only begun to invest there, so growth was still in the early stages.

While early stage growth is lucrative, it can take time to build traction. In 2019, management revealed that its multi-year growth forecast called for 20% annual sales growth and 25% annual EPS growth. While that’s impressive, it’s lower than what the market was expecting. The stock corrected lower on the news.

Then, of course, the coronavirus hit. Chinese economic activity has fallen off a cliff, with consumers opting to stay inside and reduce movement. Suddenly, Canada Goose's international growth plans were put on pause, potentially delayed by a matter of years.

American and Canadian consumers, meanwhile, which constitute a majority of the company's current sales, are expected to reduce their demand for high-priced luxury items, which will directly impact Canada Goose's $1,000 jackets.

Today, GOOS stock trades at 25 times earnings — a 90% reduction in valuation in just 24 months. For risk-tolerant investors, this could be a great chance to profit.

Weigh the risks

Keep in mind that Canada Goose still has a stellar reputation with buyers. The company is hurting from macroeconomic impacts, not changes in consumer preferences. Around 90% of customers say that they'll turn to Canada Goose again for their next winter jacket purchase.

If global conditions were normalized, the stock might be doing quite well. We don't know for sure how long the coronavirus pandemic will persist or what the ultimate global impact will be, but Canada Goose will survive and return to a path of international expansion. How quickly conditions will normalize will directly impact your opportunity to capitalize.

For the full trailing 12 months, Canada Goose is estimated to have earned $1.38 per share. If the company can hit management's growth targets, the company should earn $2.70 after three years, which means that shares trade at just 11 times 2023.

That's a steal, especially if the global economy turns around post-virus and growth picks up even further. In this scenario, annual returns should exceed 25% for several years.

But what if the virus pandemic continues? Or worse, what if the global economy dips into a multi-year recession?

High-multiple stocks usually bear the brunt during a market downturn. Yet here's the thing: Canada Goose's valuation has already compressed tremendously. At current levels, it's no longer being priced as a growth stock. In fact, it's roughly in line with the market.

In a prolonged recession, expect GOOS stock to suffer alongside the rest of the market, but no more. When the economy reverses, you'll have locked in a value price for a high-growth stock. That will lead to long-term gains, but it'll take some patience to see the investment thesis through.

As markets dip, there are a ton of new bargains to invest in. Even if GOOS shares don't fit your investing style, keep looking, as once-in-a-decade deals are starting to spring up.

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