Value Stocks Inspired by Peter Lynch

Description

Retail investors would do well to follow in the footsteps of Peter Lynch. An investing legend, Lynch had a knack for identifying value stocks. At the helm of Magellan Funds for 13 years, he averaged a 29.2% annual return, more than doubling the market. While at the helm, his fund was the best-performing mutual fund in the world.

How did he do it? Analyzing a company's price-to-earnings to growth (PEG) ratio is at the centre of his philosophy. In fact, he made the metric famous. The concept is a simple one: the higher the growth rate, the more an investor should be willing to pay.

A PEG ratio below one is a sign of good value, whereas one below 0.5 is considered to be of deep value. It is an indication that the company's stock price is not keeping up with expected growth rates.

The current bear market is resetting valuations, and investors now have plenty of value stocks to choose from.

A top value stock

One of the hottest stocks in 2019, **goeasy** (TSX:GSY) has taken a beating in 2020. As interest rates crater, and the economy comes to a standstill, alternative lenders find themselves in a challenging lending environment.

Year to date, the company's stock price is down 50.55%, and it is trading at a 58% discount from its 52-week high of $80.15 per share. As of writing, it is now trading at a ridiculously cheap 6.38 times earnings.

Although estimates have since come down, goeasy is still expected to grow earnings by approximately 20% over the next few years. The company sports a PEG ratio of only 0.28, making it a deep value stock and one of the cheapest on the TSX Index.

Bears will point to concerns with respect to non-prime lending. History has shown that these concerns are unfounded. In fact, market research during the financial crisis and the oil bear market in 2015 shows that non-prime defaults only ticked up marginally.

Furthermore, most non-prime customers have loan insurance in the event they lose employment. This is particularly relevant in such times. goeasy is also well capitalized, with enough liquidity to support loan growth through 2021. Now is the time to start building a position in this value stock.

A cheap retail giant

The PEG ratio is not only relevant to high-growth stocks. The ratio can be modified to analyze low-growth stocks. By adding the dividend yield to the expected growth rate, the same principles can be applied.

Canadian Tire (TSX:CTC.A) is expected to grow earnings by approximately 5% over the next few years. This is reflective of current downwards revisions and falls within the low-growth category. Canadian Tire's share price is down by approximately 35% this year.

As a result, the yield has spiked (5% as of writing), and it is now trading at a cheap 6.45 times earnings. This gives the company a PEG ratio of 0.64 and qualifies it as a value stock. In fact, it is one of the cheapest stocks in the retail segment.

High-quality companies like Canadian Tire aren't this cheap too often. It has the brand power to come out on top once the economy rebounds. In the meantime, it is one value stock that investors should consider averaging into.

Why average in? Because trying to time the market is a fool's game. Don't take my word for it, Peter Lynch said it best himself: "Far more money has been lost by investors preparing for corrections or trying to anticipate corrections than has been lost in the corrections themselves."

CATEGORY

1. Bank Stocks
2. Dividend Stocks
3. Investing

TICKERS GLOBAL

1. TSX:CTC.A (Canadian Tire Corporation, Limited)
2. TSX:GSY (goeasy Ltd.)

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