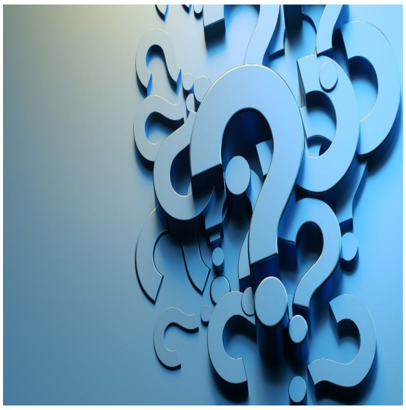

Will This Popular Canadian Stock Boom or Bust?

Description

Okay, let me start with this: I still think **Canadian Tire Corporation** (TSX:CTC.A) is a great long-term bet for investors.

Now that we have that out of the way, I am going to discuss why I see volatility for Canadian Tire's stock on the horizon. Also, I'll discuss what investors ought to look for in terms of timing a purchase.

Balance sheets are everything these days

One thing that is now a blessing and a curse is the increased attention many investors are now paying to the balance sheets of companies. I say this because it is clear to me that there is unwarranted ballooning of valuations across the board during this most recent bull market. I firmly believe this is a direct result of hype and a lack of financial discipline.

Any company with a post office box and a CEO that could show higher than market average growth (on the top line, forget about profitability) was given a gold star and a blank cheque. Companies like Canadian Tire had an excellent bottom line performance. The company certainly performed well during the bull market run.

However, Canadian Tire did not reap the benefit other high-risk asset classes did. This has led to Canadian Tire becoming a stock I have pounded my chest about for some time.

That said, this potentially irrational multiple expansion has allowed for balance sheet deterioration to go unchecked and unnoticed by financial markets. Companies like Canadian Tire have engaged in a series of acquisitions which have significantly added to already relatively, high debt loads.

The future is bright

Canadian Tire's acquisition of Helly Hansen will work out in the long run. However, right now, investors seem to be paying a heck of a lot more attention to the ability of Canadian Tire to make its debt obligations, which means those gold stars are being taken away.

Investors are continuing to move their money to places where earnings may continue to grow in the near term, which mainly includes tech plays.

The fact that Canadian Tire's traditional bricks and mortar retail business model is under pressure is nothing new. This COVID-19 pandemic has brought to the forefront the secular shifts from bricks and mortar retail. The pandemic has accelerated these shifts that were already underway.

That said, as I have written about previously, Canadian Tire's business model is actually uniquely immune to these market forces, for a number of reasons.

Bottom line

Canadian Tire's near-term woes are likely to remain a serious overhang for the stock for a while. I reference the decline in net income of nearly 90% for the company on a year-over year basis as exhibit one.

The company will need to show investors significantly improved results next quarter to regain the full support of investors. Canadian Tire's balance sheet being in focus could require a shift in focus toward debt repayment away from top line growth, which would allow the company to grow more profitably over time.

I would encourage investors to monitor Canadian Tire's stock price over the near-term. They should consider adding a small position and nibbling away on weakness. The company will do fine long term, and I think this is a blip in the radar for a high-quality Canadian company.

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Date
2025/08/15
Date Created
2020/07/09
Author
chrismacdonald