Boxing Day Shopping? Stay Away From These 2 Stocks

Description

Many investors have set their eyes on recovery stocks, in hopes of making big gains once the economy returns to pre-COVID operations. With news of vaccine distributions on the horizon, many recovery stocks started to post impressive gains. However, with new COVID lockdowns being imposed around the country, recovery stocks have begun to suffer once again.

Despite the constant swings, companies like **Air Canada** (TSX:AC) and **RioCan Real Estate Investment Trust** (TSX:REI-UN) continue to attract many investors. One of the most appealing characteristics of these two companies is that they trade at very attractive valuations.

In this article, I will discuss why investors may want to avoid an investment in these two companies for the time being.

Airlines may take a while to soar to previous heights

Air Canada is one of the most well-known airline companies in North America. Within Canada, only WestJet stands as a true competitor. With about 51 million passengers using Air Canada's services to fly to nearly 220 destinations in 2019, it seems like a logical pick for those interested in investing in the travel industry.

However, one of the major issues with airline companies is its low margins. Prior to the pandemic, airline companies were reporting margins of about 10%. This compares to the leaders within the tech industry which often post margins of 80%. That means airline companies are much more susceptible to losses, should their revenue take a hit.

This is exactly what we've seen this year. In Q3 2020, Air Canada reported a net loss of $9 million per day and a projection of $12-14 million in losses per day in Q4.

As I have written previously, one trait that investors should look for in quality companies is a high margin, to protect in cases exactly as I've outlined in this article. However, some may be willing to argue that Air Canada is a bargain, according to its valuation metrics.

Indeed, with a price-to-sales ratio of 0.71, the company appears to be trading at a very attractive bargain. However, Warren Buffett famously sold out of his airline positions this year. This indicates that even he believes the attractive valuations are outweighed by the negatives in this situation.

Retail will continue to struggle

Ever since the outset of the pandemic, retailers have gone through very difficult times. **Brookfield Asset Management** CEO Bruce Flatt believes that not all retailers will be able to make it through this event. According to Flatt, the pandemic will cause consolidations within many industries, and the retail space is no different.

An example he gives is a hypothetical city with eight malls. He believes the top four will survive and come out of the event stronger. The other four? They'll be torn down and turned into something else.

Of course, predictions are tough to get right. However, when someone of Bruce Flatt's calibre makes a prediction like that, it isn't one you would want to ignore. Because of that, I would continue to stay away from the retail space for now.

Like Air Canada, RioCan trades at a very attractive valuation. Its price-to-book is currently 0.69, which falls much under the targeted price-to-book ratio of 3 that value investors look for. The company is also one of the most sought-after dividends on the **TSX**.

As of this writing, RioCan offers a forward dividend yield of 8.28%. However, with all of the uncertainty in the retail space and a stock price that remains nearly 40% down from its pre-COVID levels, RioCan does not appear to be an intelligent investment at the moment.

Foolish takeaway

Investors should stay away from the airline and retail REIT space for the time being. Companies like Air Canada and RioCan REIT are two of the most popular recovery stocks on the TSX.

However, investors are currently pouring into these companies based on pure speculation and a lot of money may still be lost in these plays before things start turning up.

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