It’s Time to Go Defensive as Recession Risks Mount

Description

Many hoped 2022 to be another blockbuster year with a post-pandemic rally. However, some grave challenges have been unearthed, and recession rhetoric has gained ground.

Although equities have been quite volatile of late, the indices, including the **S&P 500** and the **TSX Composite Index**, do not look that pessimistic. So far in 2022, the prior has lost 7%, while the latter has gained 4%.

Recession risks increase

There have been an increasing number of experts that have inclined towards a potential economic downturn soon. One of the most celebrated activist investors, Carl Icahn recently told *CNBC* that an economic downturn could be on the horizon. He said, “I think there very well could be a recession or even worse.”

If the economy takes an ugly turn from here, the global financial markets could significantly hit. Notably, the Russia-Ukraine war intensified the rising inflation situation, which has been at a multi-decade high this year.

Russian oil remains at the epicentre

Russian crude oil contributes almost 10% to global energy supplies. The talks of banning Russian oil could substantially disturb the demand-supply equation, fueling crude oil prices even higher. Oil prices have again breached US$120-per-barrel levels this week.

Such high levels could remarkably dent economic activities and consumer confidence. So, weeding out Russian oil altogether from the energy markets could have all the more adverse repercussions on the global economy.

Last week, the probability of a recession in the next 12 months jumped to 33% from 10% in early

February. That may imply a two-thirds likelihood of stable economic growth. However, what's notable here is the impact the Russia-Ukraine war is having on the global economy and on the recession outlook.

Interestingly, investors do not seem to buy the recession remarks. The potential earnings growth driven by the full re-openings and growth stocks trading at a relative discount against their peaks could be some of the reasons behind being bullish.

However, it would be prudent to take a step back and zoom out a little. If the bull rally continues, increasing exposure to defensive stocks might forgo a few percentage points return. However, they could prove to be an effective hedge in case the markets take an unpleasant turn.

So, what could be some smart picks in this market?

TC Energy

Canadian energy pipeline giant **TC Energy** (TSX:TRP)(TSX:TRP) looks attractive in this market. Even if the recession hits, its earnings growth will likely remain relatively resilient, mainly driven by its stable business model. It earns predictable cash flows from long-term, fixed-fee contracts that are not directly dominated by volatile oil and gas prices.

TRP stock yields 5% at the moment, which is higher than TSX stocks at large. So, when investors compromise on growth, they will be compensated with stable passive income to some extent.

Canadian Utilities

Utility stocks are classic defensives because of their slow stock price movements and dividends. **Canadian Utilities** (TSX:CU) is one such solid safe haven that will likely stay resilient in an economic downturn. It yields a handsome 5%, and it has increased dividends in the last five decades.

Utilities grow steadily, as demand for electricity and gas do not fluctuate with the economic outlook. In addition, CU derives most of its earnings from regulated operations, enabling stable earnings and facilitating secure dividends.

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