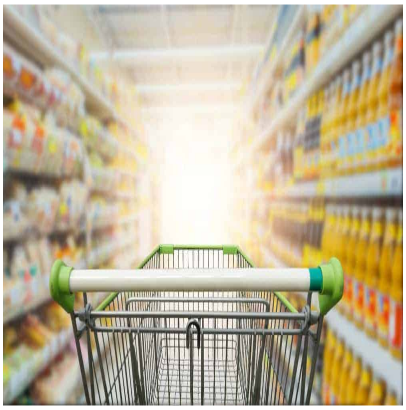

2 Beaten-Up Retailers That Could Rise in a Fed Pause

Description

The concept of a "Fed pause" has been giving a bit of hope to these beaten-down stock markets of late. The hope is that the U.S. Federal Reserve will pause before committing to any further rate hikes by the year's end. Some folks even think the recent slew of economic data is comforting enough to allow the Fed to take on a more dovish tilt before the year ends.

Indeed, the Fed remains committed to fighting inflation. Many members of the Fed remain in full-on hawk mode, while others are beginning to show some concern for the health of the economy and market stability going into the new year. The slew of rate hikes has caused the U.S. dollar to be incredibly strong. Anything less than a dovish surprise could cause the greenback to continue ascending, posing a new threat to the stability of global financial markets.

Undoubtedly, the Fed wants to eliminate inflation, not jobs. However, their hawkish stance leaves them with a pretty high tolerance for pain. In any case, new investors should not seek to predict what central banks will do from here. Any shift could have massive bullish or bearish consequences on markets.

For long-term investors, the beaten-up discretionary retailers seem like attractive bets here and now, regardless of when the Fed turns dovish. If you're in it for the next 10 years, it doesn't really matter if the Fed pauses on its rate hikes earlier next year, later next year, or in 2024. In due time, inflation will normalize, and so too will the economy's growth prospects. When things do return to normal, it's the hard-hit discretionary companies that could lead the charge.

Now, given the propensity of such economically sensitive firms to fall faster than broader markets in the face of recessions, it's wise to be an incremental buyer over time, rather than loading up at any one time or price.

At this juncture, **Canadian Tire** (TSX:CTC.A) and **Leon's Furniture** (TSX:LNF) seem oversold and subject to considerable upside should the Fed decide to pause sooner rather than later.

Canadian Tire

Canadian Tire is a big-box retailer that we're all very much familiar with. There's a Canadian Tire location in close proximity to the average consumer. It's this strong physical presence that makes the retailer a go-to for various big-ticket purchases. Digital retail may be unstoppable, but Canadian Tire has shown that there's no substitute for a strong omnichannel presence.

There's more to the Canadian Tire story than retail, though. The firm's budding financial services business contributed nearly 33% of profits this year. Canadian Tire Bank's heavy credit card business has been making a considerable amount from consumer loans.

As recession risk rises, Canadian Tire's retail business could be weighed down by soured consumer debt balances. Shares of CTC.A have already felt the pinch, down more than 28% from its all-time highs just north of $200 per share. At 8.5 times trailing price-to-earnings, I view CTC.A as a dividend bargain. The 4.3% dividend yield is built to last. Once the Fed pauses, I think recession fears could fade, and the stock could be back in rally mode.

Leon's Furniture

Leon's Furniture is another discretionary retailer that could be in for huge upside once recession fears are replaced with post-recession recovery projections. Indeed, furnishings are among the first to see slashed demand once times get tough. However, when the tides turn, Leon's is one name that could be quick to rebound.

The stock trades at 6.5 times trailing P/E, even lower than CTC.A. With a 3.7% yield and overblown negativity, count me as a fan of the $1.15 billion Canadian furniture giant.

CATEGORY

1. Investing

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2. TSX:LNF (Leon's Furniture Limited)

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