Man’s Best Friend: A Retail Stock That Weathers Recession

Description

Most economists expect a recession by next year. Canadian consumers are already pulling back spending. Meanwhile, corporations have either stalled hiring or launched layoffs. The stock market has plunged in anticipation of this economic weakness.

Investors now need to seek out sectors of the economy that are relatively immune to this headwind. Pet care could be one such recession-resistant niche. Here’s a closer look at why this niche is outperforming other retail sectors and the rest of the economy.

Pet care

If you have a pet, you probably know that pet care isn’t a discretionary expense. Pet food, toys, bedding, and hygiene items need to be replaced on a regular basis, regardless of the economic cycle. That makes the industry relatively recession resistant.

The pet care market continued to grow throughout the 2008 Global Financial Crisis. This year, it seems to be doing the same. **Pet Valu Holdings** (TSX:PET), Canada’s largest pet care retailer, has outperformed the market this year. The stock is up by more than 12% year to date. In contrast, the TSX index is down by about 5%.

As one of Canada’s largest pet food and pet supplies retailers, Pet Valu is uniquely positioned for this upcoming recession. With over 700 corporate-owned and franchised outlets, Pet Value recorded solid sales growth, even at the height of the pandemic. Over the past three years, sales have increased from $529 million to $776 million as of the end of last year.

In the second quarter of this year, sales were up 35% to $312 million. The company is on course to generate between $912 million and $928 million in sales this year. Analysts expect sales to hit the $1 billion mark next year, signaling a forward price-to-sales multiple of 2.6. That’s not bad for a company that’s expanding at double-digit percentages.

Pet Valu valuation

While the stock is trading with a price-to-earnings multiple of 21, it appears to be trading at a discount based on recent growth. Pet Valu's earnings per share is expected to rise to $1.66 next year, translating to a price-to-earnings multiple of about 22.

This is still cheap for a profitable company that is generating solid sales growth amid inflationary pressures and recession concerns. It's also generating free cash flows, allowing it to pay a tiny 0.64% dividend yield. Pet Value is a highly underrated and undervalued stock at current valuation levels.

Bottom line

A recession could be due if it isn't already here. Investors need to seek shelter in sectors that have proven to be resilient during such crises. I believe pet care retailers like Pet Valu could be ideal targets for investors in the near term. The company has seen tremendous sales growth, despite the pullback in the rest of the economy. Keep an eye on this undervalued niche.

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Date
2025/08/15

Date Created
2022/11/30
Author
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