10 Stocks to Look at if the Market Crashes

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We've all seen the headlines. If you believe the financial media, we're in a bubble and it's about to pop. 2014 is going to be 2008, 2001, and 1929 all over again.

I'm not quite so pessimistic, but it's hard to ignore the fact that the risk in this market is increasing. I wrote back in January that I thought valuations in the market were stretched, and I expect major corrections in certain stocks though not so much for the whole market.

Now that we know the Fed is more likely to tighten than loosen, everyone concedes that it is only a matter of time before certain stocks fall back to earth. The question is not if but when. Still, a tough question.

Typically, bubbles continue and continue until something serious comes along to pop them. I remember back in 1999 - 2000 how everyone knew the market was in a bubble, but they were afraid to miss the upside so they stayed in. And, eventually, got crushed.

The current geopolitical uncertainty adds to the risk in the market. It might not be the straw that breaks the bubble's back, but it certainly raises the risk profile of some already highly overpriced stocks.

With every passing day, success in this market depends more and more on being diligent in your stock, ETF or mutual fund investments. Momentum and technical strategies are crowded and ineffective. Investing is getting harder, not easier. There is no substitute for proper diligence on the true earnings and valuation of securities. Investing based on other criteria is not investing, it is speculating.

So, my advice is do your homework and arm yourself with diligence. And when opportunity presents itself, dive in.

Benjamin Roth, a lawyer during the Great Depression, kept a diary that includes many wonderful nuggets of wisdom on the market. In particular, he wrote in 1931 that "It is generally believed that good stocks and bonds can now be bought at very attractive prices," and then in 1937 that "The greatest chance in a lifetime to build a fortune has gone and will probably not come again soon."

For the long-term investor, a market crash represents an incredible money making opportunity. As long as you have some cash on the sidelines, high-quality companies can often be bought at prices well below where they'd normally trade.

Figure 1 examines 10 stocks that aren't quite screaming buys but could be incredible opportunities if a crash shaves 25% or more off their valuations. All these companies earn a top-quintile return on invested capital (ROIC) and have a price to economic book value that earns my second-best, Attractive, rating.

Figure 1: Stocks to Buy in a Crash

Company	Ticker	ROIC	PEBV
The Gap	GPS	16%	1.2
Sanderson Farms	SAFM	16%	1.2
Becton Dickinson	BDX	15%	1.3
TJX Companies	TJX	20%	1.3
Allegiant Travel	ALGT	25%	1.4
Scripps Networks Interactive	SNI	22%	1.5
Hershey Company	HSY	22%	1.5
Tupperware	TUP	22%	1.5
AmerisourceBergen	ABC	15%	1.6
National Health Investors	NHI	27%	1.6

Sources: New Constructs, LLC and company filings.

All these companies are high quality, value-creating businesses that I would love to own. In fact, I've previously recommended two of them, Gap (GPS) and Scripps Networks Interactive (SNI). Both GPS and SNI have outperformed the broader market and now are just too expensive for me to be a buyer any longer. If the price dropped sharply in a market crash, however, I'd definitely look at re-entering those positions.

The Hershey Company (HSY) is a great example of a company I'd like to own a piece of at a cheaper price. Hershey has steadily increased its ROIC from 15% in 2007 to 22% last year. HSY's consistently solid free cash flow, along with its $750 million in excess cash, give it plenty of resources to either invest in its business or return cash to shareholders.

However, at its current price of ~$92/share, HSY has a PEBV of 1.5, which means that roughly a third of the market's valuation of the stock relies on future cash flow growth. I'd rather not invest in a stock with that much growth already baked into its price.

If the market were to crash and HSY were to fall 30-40%, it would be trading in the low sixties, right at economic book value. Essentially, the stock would be priced for zero growth. HSY bottomed near a PEBV of 1.0 in 2008, and has returned nearly 200% since that time.

A similar story applies to the other stocks in Figure 1. These are some great companies, but too expensive to be good stocks. If the market crashes, keep an eye on these stocks as potential investments when the price is right.

Sam McBride contributed to this report.
Disclosure: David Trainer and Sam McBride receive no compensation to write about any specific stock, sector or theme.

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