Why a Hot Housing Market Could Create an Opportunity to Buy This Stock

Description

The Canadian housing market has been a hot topic as home prices continue to rise at unsustainable rates in the Toronto and Vancouver area. Since the real estate market is cyclical, the home prices will return to the mean eventually. How large will the market correction be? Will it put us back to the 2008 financial crisis?

One thing investors should keep in mind is that the hot housing markets are confined to the Toronto and Vancouver area; they aren't widespread across Canada. Therefore, I don't think we will be in the same situation we were 2008, unless the madness spreads to other major cities. However, I believe it could cause a market correction in the near future.

I can't tell you when a correction will come, but I do know it will be a great test for investors' risk tolerance. The stock market has had a great run as of late, and investors have been rewarded. However, if the markets take a turn, investors may act on emotion, which can lead to poor investing decisions. Therefore, it will be critical for Foolish investors to maintain a long-term view and look for discounts throughout the stock market.

Sectors such as the banking industry would be directly impacted if the housing bubble bursts; companies within the industry could a see a drop in their stock prices. However, **Bank of Nova Scotia** (TSX:BNS)(NYSE:BNS) is one bank with reduced exposure to the Canadian housing market, and if Canadian bank stock prices collectively drop, that could provide a great entry point for the stock.

If the housing bubble bursts, it should have minimal impact on Bank of Nova Scotia's overall earnings. The company has an impressive global reach with 49% of the company's business line earnings being derived from 54 countries outside Canada. Therefore, if the Canadian economy takes a hit, the bank can rely on international revenue sources to mitigate the damage and continue to provide investors with a steady dividend yield of 3.93%.

In addition, in order for Canadian banks to expand their operations, they need to penetrate emerging markets. Bank of Nova Scotia has made this a priority with over over 18% of its income now coming from Latin America. Therefore, if the stock price drops, that creates a great opportunity for investors to obtain a bank with growth potential at a discount.

Foolish bottom line

Bank of Nova Scotia and the other Canadian banks usually trade at a premium due to their strong earnings and the oligopoly structure in Canada. Therefore, the best time to acquire them at a discount is if the economy takes a hit. These banks have weathered every financial storm and continue to provide steady returns to investors. Therefore, if the housing bubble bursts and Bank of Nova Scotia's stock price drops, I highly recommend being greedy when others are fearful.

Fool on!

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