Equitable Group Inc. Isn't Home Capital Group Inc., But it Remains Risky

Description

Equitable Group Inc. (TSX:EQB) stock has been hit hard of late, given the various scandals and current run on the deposits of rival alternative lender **Home Capital Group Inc.** (TSX:HCG) over the past few weeks.

I'm going to take a look at whether or not this sell-off has been overblown, if the company will indeed bounce back to the $70 level it saw before the Home Capital crisis emerged, and if more downside still exists with this alternative lender moving forward.

What does Equitable Group do?

Equitable Group operates in the same non-prime alternative mortgage lending space as Home Capital, originating mortgages for immigrants, those with poor or repaired credit, and those who are essentially unable to get a mortgage at a traditional Canadian bank.

While the "Big Five" Canadian banks typically lend out at five-year terms of interest rates of less than 3%, both Home Capital and Equitable Group have actual realized interest rates hovering between 4.5% and 5%, meaning these lenders typically earn much higher returns with the same amount of capital than traditional banks, albeit with higher credit risk.

Can you really compare Equitable Group with Home Capital?

The issues Home Capital has experienced of late have not revolved around the issue of credit quality; it's more a confidence issue with its ability to continue as a going concern, given the recent significant withdrawals made from the lender's high interest savings accounts (HISA) and guaranteed investment certificate (GIC) deposits. Equitable Group, however, has not seen a significant run on its deposits, and it has been able to secure liquidity from large Canadian banking institutions at much more favourable terms to defend itself against a similar run should one materialize at some point in the future.

Equitable Group has repeatedly stated that the strength of its lending oversight policies are second to none, and the credit quality of its loans are much more solid than other lenders in the alternativelending space.

While this may be true, I remain skeptical of the Canadian alternative lending space in general and therefore of Equitable Group specifically, as the overheated Canadian markets (specifically Canada's largest cities, including Toronto and Vancouver), in my mind, pose a significant risk to the higher-risk, higher-return portfolios of lenders such as Home Capital and Equitable Group.

Bottom line

As I have written about previously, Equitable Group has been on the list of my top three short plays for this year. While I may not necessarily have this company has a "strong short" at this point in time, I would encourage investors to remain vigilant with respect to the Canadian housing market, and monitor such exposure closely.

Stay Foolish, my friends.

CATEGORY

1. Investing

TICKERS GLOBAL

1. TSX:EQB (EQB)
2. TSX:HCG (Home Capital Group)

PARTNER-FEEDS

1. Msn
2. Newscred
3. Yahoo CA

Category

1. Investing

Date
2025/08/24
Date Created
2017/05/30
Author
chrismacdonald