



The Best Long-Short Strategy of the Year!

Description

Two companies I have followed closely for some time, **Home Capital Group Inc.** ([TSX:HCG](#)) and **Air Canada** ([TSX:AC](#))(TSX:AC.B), have certainly diverged as far as their share prices are concerned. Of course, calling Home Capital the [short of the year](#) on a number of occasions (starting at the end of January), and Air Canada as one of the Canadian companies with [significant upside](#) for 2017 may have been easy to do in hindsight; however, going forward, the jury remains out on how these companies will continue to perform, with other analysts and contributors suggesting [opposite strategies](#).

Taking the time to look at how a long-short strategy (long Air Canada, short Home Capital) has worked out so far for investors who've listened, we can see from the numbers that investors who've followed such a strategy since the beginning of 2017 would have seen growth of more than 70% for the Air Canada position and more than 55% on the Home Capital position.

An average 62.5% return for such a play isn't too shabby, but that's all history. What investors want to know is this: Where are these companies headed from here?

How will these companies perform for the remainder of 2017?

I expect Air Canada to continue to outperform its peers, including **WestJet Airlines Ltd.** (TSX:WJA). I recommend investors take a look at isolating Air Canada and the airline's potential for outsized returns compared to its largest competitor in the Canadian market by undertaking a long-short strategy to take advantage of the value gap that exists between the two Canadian airlines.

While the significant value gap that exists between Canada's two largest airlines (a price-to-earnings ratio of 11.7 for WestJet compared to only 7.7 for Air Canada) may not completely close, the current divergence of the two airlines from a valuation standpoint does not make fundamental sense, and I expect that, over the medium term, these valuation multiples will come more in line with investor expectations, creating a situation where an investor can grab much of the value that is currently being left on the table by the market.

In the case of Home Capital, I would recommend a long-short strategy, but this time I would recommend investors go long the "Big Five" Canadian banks and short a consortium of alternative lenders to take advantage of the mispriced risk profile many of these alternative lenders display, which I believe has not yet been fully priced in to the share prices of Home Capital and its peers.

Bottom line

Investors need to think critically about how a company will perform relative to its peers and the overall industry it operates in before undertaking a long-short strategy. I suggest investors maintain the aforementioned Air Canada and Home Capital long-short strategies through the remainder of 2017, as a significant value gap remains in both cases, and reassess as market changes take place.

Stay Foolish, my friends.

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Author

chrismacdonald

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