



## This Fallen Growth Stock Is Attractively Valued and Poised to Soar

### Description

The last year has been a wild ride for investors in Canada's largest alternative mortgage lender **Home Capital Group Inc.** ([TSX:HCG](#)). After it found itself engulfed in a mortgage origination scandal, securities commission investigation, and class-action lawsuit, the lender suffered a massive run on its deposits, which almost caused it to collapse.

Since being bailed out by legendary investor Warren Buffett, it has been able to stabilize its balance sheet and boost liquidity, allowing it to remain as a going concern. While the worst is well and truly over, Home Capital's stock price has failed to recover, leaving it attractively valued.

### Now what?

At the height of the liquidity crisis, Home Capital plummeted to under \$6 per share, as investors feared the company would fail. Since then, it has more than doubled to almost \$14 per share, but it is still well off the lofty heights of \$50 per share reached in mid-2014.

The relatively flat performance of its stock in recent weeks can be attributed to worries that Home Capital will find it tough to rebuild its business and grow its mortgage book at a decent clip. Those fears have also been compounded by shareholders voting resoundingly against Warren Buffett's planned acquisition of an additional 24 million shares at a steep discount to the market price back in late September. What was increasingly clear at the time was that Home Capital did not require the [additional investment](#), and if it had been approved, the dilutive effect on existing shareholders would have been tremendous.

While there are certainly risks for investors, what is becoming increasingly clear is that Home Capital has put the worst behind it, and it is meaningfully positioned to benefit from the forecast explosion in demand for alternative mortgages.

In fact, the rejection of Buffett's planned share purchase and the failure of the market to recognize that the degree of risk is not as high as believed leaves Home Capital attractively valued.

You see, not only has the lender significantly reduced the risks it is facing by settling the securities

commission investigation and class-action lawsuit, it has also been able to significantly boost its liquidity. Deposit inflows have returned to pre-crisis levels, and it has aggregate liquidity, including available credit facilities of close to \$4 billion.

Furthermore, credit quality remains high, as shown by its second quarter 2017 non-performing loan ratio of a mere 0.23%, and the lender finished that quarter well capitalized, as indicated by its tier one capital ratio of 17%.

For these reasons, Home Capital is well positioned to take full advantage of the expected growth in non-traditional or alternative mortgages created by ever tighter mortgage regulation.

More importantly, Home Capital appears attractively valued. It finished the second quarter with a book value of \$21.63 per share, and after removing goodwill and other intangibles, that falls around \$20 per share, which is a massive 44% higher than its market price. Such a significant disconnect between Home Capital's net tangible asset value and its market price highlights that there is an opportunity for investors.

Once it becomes clear that the lender has been able to recommence originating what are essentially highly profitable mortgages in volumes commensurate to those being underwritten prior to the crisis, its value will soar.

### **So what?**

One-time high-flying growth stock Home Capital is an appealing investment. Not only has it survived the worst crisis in its history, but it is now poised to recommence growing at a solid rate, which means that because of an overbaked perception of risk, it appears undervalued.

## **CATEGORY**

1. Investing

## **TICKERS GLOBAL**

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1. Investing

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