



Why the Market Has Cooled on Home Capital Group Inc. and What to Expect Going Forward

Description

Shares in **Home Capital Group Inc.** ([TSX:HCG](#)) are virtually unchanged since late July following the company's second-quarter earnings report.

This likely comes as welcome news for shareholders in the company, who have been on a heart-palpitating roller-coaster ride with the alternative mortgage lender since the start of the year.

Shares plummeted from \$28 in March all the way to \$6 fewer than two months later, only to be rescued by the Oracle of Omaha himself, Warren Buffett, who acquired a 20% stake in the company for \$10 a share in June of this year.

While the stability that Buffett brought to the company initially sent shares skyward to \$21, the stock has quieted since then, giving back much those gains and closing trading on October 24 at \$13.38 — a 33% premium to the price paid by the owner of **Berkshire Hathaway Inc.**

The recent quiet period owes mostly to the fact that investors are seeking more clarity on what the new company will look like following the liquidity crisis that nearly brought the alternative lender to its knees this spring.

A leadership shake-up at the top

Following this year's seemingly existential crisis, Home Capital and its board of directors have replaced much of the senior leadership team that got the company into hot water with the OSC, which resulted in a \$11 million settlement and ultimately led to a bank run on the company's deposit base.

Yousry Bissada will lead the new company, as its new CEO and brings with him a long track record of experience in Canada's mortgage marketplace. New CFO Brad Kotush comes to the company following 10 years as CFO of Canadian investment bank **Canaccord Genuity**.

It will naturally take time for Home Capital's new leadership to impart a cultural change on the company, but in the meantime, investors will want to see a rationalization of the company's rates on its

deposit base and an emphasis on more stringent underwriting standards.

On the company's third-quarter conference call, which has yet to be announced as of this writing, much of the focus will likely be on these two key areas of opportunity for the company.

Gaining clarity on Home Capital's retained book of business

Home Capital was forced to sell a significant portion of its book this summer to shore up its balance sheet. On the company's second-quarter conference call, Bissada announced that several more asset sales were completed in July following the end of the second quarter.

As no details have been announced publicly, investors will be anticipating third-quarter earnings to learn exactly how much of the company's \$18 billion loan book has been retained, and what value the company got for its asset sales that closed since the start of July.

Investors may want to follow Buffett's lead

Despite the uncertainty around the extensive shake-up at the top and what kind of effect it will ultimately have the company's culture and operations, in addition to the extent of any unannounced asset sales in the third quarter, investors should be able to take solace in the fact that Buffett is on record as being perfectly contented with his investment in the Toronto-based mortgage lender, with no plans to sell anytime soon.

Over the summer, when he was asked about his stake in Home Capital, Buffett reassured investors that he had no intention of quickly exiting the investment should there be an unexpected adverse development.

Buffett's 20% stake in the alternative lender not only provides a liquidity backstop should there be a need, but it should also say something about the value offered by Home Capital shares as an investment today.

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Date

2025/07/27

Date Created

2017/10/31

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