What to Expect From Earnings of Home Capital Group Inc.

Description

Home Capital Group Inc. (TSX:HCG) is going to report earnings soon, and shares will probably move substantially in one direction or another. Although many investors, including Warren Buffett, have high expectations for the company, there are still many naysayers who expect bad things. These are the short sellers.

Since Home Capital Group has been through a minor fiasco, which involved clear wrongdoing, the company has successfully raised money and avoided a run on deposits, which sent shares to almost $5. At a current price of $14, investors could see close to 50% upside if the share price were to return closer to its tangible book value.

The main challenges faced by the company was the run on deposits and the chance that GIC holders would not be able to retrieve their money from the company. The short-term availability of money is known as liquidity; this challenge was resolved with the raising of new capital and the temporary suspension of lending for new mortgages. The long-term value for shareholders, which is known as solvency, is the total coverage of assets and liabilities of the company. In this case, the company has traded at a substantial discount for several months, as the price of the asset sales (which have raised capital) has not been publicly released.

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As is typically the case, uncertainty has led to a higher amount of risk being priced in to shares of the company.

When considering shares of competitor **First National Financial Corp.** (TSX:FN), which recently reported quarterly earnings and saw shares (which carry a low beta of 0.73) rise from $23 to more than $29 on earnings, it became clear that those investing in the alternative mortgage market have a lot of potential upside. In the case of Home Capital Group, the negative momentum seems to have run out, as shares have been moving sideways around the $14 mark for several months.

Given that the 10-day and 50-day simple moving averages (SMAs) have been crossing over each other for months, and the 200-day SMA is starting to approach the current share price, there is no question that shares are primed to move on earnings.

Investors need to be looking for one of a few catalysts in the earnings report. The first catalyst could be the amount of tangible book value on a per-share basis. Barring any large write down, the floor price for shares in this company will eventually move closer to the $21 mark.

After that, the company could announce the redeployment of capital by reintroducing the dividend or by buying back shares. Either would be a sign of financial health for the company, which also ties into the amount of lending that the company is currently undertaking. Essentially, the availability of capital is the key issue, which investors will need to have addressed in the earnings report.

CATEGORY

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