Is Home Capital Group Inc.'s Stock About to Take Off?

Description

Home Capital Group Inc. (TSX:HCG) has quietly been soaring more than 17% in the past month and has gotten a big boost from its recent Q3 earnings that saw the non-bank lender return to profitability after a difficult Q2. The last time the share price was above $16 was back in July after the stock got a boost from a certain high-profile investment.

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The stock looks to finally be picking up steam again after being stuck in a range of $13-14 in the past few months. Let's take a closer look at the stock to assess if it is a good buy today.

Plenty of risk remains

The company has made a good effort to reduce its expenses and change the management — all in the name of trying to turn the ship around and getting back customers — but it might not be enough. Mortgage originations are down significantly from a year ago, and if the company only had its damaged reputation to worry about, then it likely would be fine, but that isn't the case.

Tighter mortgage rules and higher interest rates are a recipe for fewer mortgages, and that will only compound the challenge that Home Capital is already facing in getting its mortgages back to previous levels. If the company is able to do so, it will likely have to provide more aggressive rates, which will erode Home Capital's profitability.

The stock could be a good value investment

An awful Q2 is weighing down the company's earnings per share, which, without the quarter, would have trailing per-share earnings of $2.56 rather than $0.35. That is the difference between the company trading at six times its earnings and trading at a multiple of 45.

The share price also trades at a price-to-book multiple of just 0.72, and investors can get it at a good discount, even at $16 a share. The big question is if the company can build on its recent results and gain the trust back of its customers and investors.

What the technical indicators are saying

Last week, Home Capital finished trading at a Relative Strength Index of over 70 and was as high as 84 to start the week. This suggests to me that the recent results might have had a bit more enthusiasm than what was warranted, and we could see more of a correction on the way.

The share price's 50-day moving average was $14.23 last week and keeps getting closer to the 200-day moving average of $16.21 — a difference of barely $2. If the 200-day mark falls under the 50-day mark, that is a very bearish indicator, and we could see some negative activity if and when that happens.

Investors shouldn't be swayed by recent momentum

We've seen Home Capital get a boost in share price before, only for the stock to eventually return back down in price. Fundamentally, Home Capital would be a good buy if not for adverse market conditions.

The company has done a good job of cleaning up its image, and in the short term, it could be a great buy given how undervalued it still is, but over the long term, there are too many negatives in the industry that would keep me away from not only Home Capital, but any lending company.

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