Home Capital Group Inc. Is up 25% Over the Last 3 Months: Time to Sell?

Description

Following a brief period of consolidation, shares in **Home Capital Group Inc.** (TSX:HCG) have taken off recently — up as much as 25% over the past three months.

Shares now trade north of $17 per share on the Toronto Stock Exchange; meanwhile, the world famous “Oracle of Omaha” Warren Buffett is surely contented in having made more than 70% on his 20% stake in the company initiated back in April, not to mention interest earned on the line of credit he provided to the company to shore up its liquidity issues.

Yet every investment needs to be sold eventually to realize a profit, and, for some at least, now might be the right time to take advantage of the opportunity.

Gains of 25% over such a short period of time are relatively rare, even for volatile, or risky, companies like Home Capital Group.

While that doesn’t mean that the next move is necessarily down, it does raise the chances that some investors will be looking to capitalize on the recent share price appreciation, which could send shares lower, if only for the near term.

In 2018, we will see the sixth case of restrictive regulations applied to the Canadian mortgage lending market in an ongoing effort to quell the creation of a dangerous housing bubble.

Notable among the changes are rules that will prohibit borrowers from circumventing capital requirements on mortgages that are guaranteed by a family member, and additional stress testing — even on mortgages that do not qualify for mortgage insurance.

The former will have more of a direct impact on Home Capital Group than other lenders owing to the nature of the company’s customer base — a clientele that is already on the margins of being able to finance a home purchase and often needs assistance in qualifying for a loan.

Yet the latter could have a more significant impact on the health of the overall housing market. It’s expected that over 100,000 mortgage applicants next year will be affected by the oncoming legislation.

Essentially, the new rule will force borrowers to qualify for a mortgage that is 200 basis points, or 2%, higher than rates present in the market at the time of their application.

So, for example, if a would-be borrower were applying for a 5% fixed-rate loan, they would need to be able to show the bank or mortgage lender that they could responsibly make payments on a loan of 7% per year.

Obviously, this makes it more difficult to qualify for a loan, particularly for first-time buyers, who will likely need to delay their purchase until they have saved more money for a down payment, or make concessions on the value of the home they can afford to buy.

Bottom line

It appears the market has already taken note of the forthcoming changes, even while shares in Home Capital Group have risen.

In Toronto, which is the company’s primary market, home prices have declined for six straight months now with the average selling price down more than $170,000 over that period.

While Warren Buffett may be willing — and can afford — to wait, short-term investors may want to use the recent run-up to lock in profits and move on to the next best thing.

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