Better Turnaround Stock: Valeant Pharmaceuticals Intl Inc. vs. Home Capital Group Inc.

Description

Every once in a while, we are presented with possible turnaround stocks of a lifetime.

Turnaround stocks are certainly not the easiest things to spot, although, in hindsight, it may appear clear. Let's look at two stocks that have big potential for appreciation if, in fact, a turnaround is in progress.

Home Capital Group Inc. (TSX:HCG)

First let's take a look at Home Capital.

Home Capital recently released fourth-quarter and year-end 2017 results that were ahead of expectations. If we exclude one-time items, EPS came in at more than $0.45 compared to consensus estimates of $0.37 and pretty much flat compared to the same quarter last year.

Mortgage loan growth was a dismal -15%, and credit trends weakened somewhat compared to last year, as the environment has become much tougher these days.

The stock has more than doubled since lows that were hit back in April 2017, but since then they have pretty much been hovering in the $14-17 range.

So, will the stock recover from accusations of mortgage fraud that sent the company into a liquidity crisis, as shaken confidence, a run on deposits, and questions about Canada's housing market had investors running?

With a capital ratio of over 23%, which is much improved from the 17% seen in the second quarter, and rising net interest margins, we can feel somewhat confident in expecting increasing profitability.

However, the backdrop that Home Capital must contend with is becoming more challenging, as more stringent stress tests are resulting in lower originations. And while these new rules may bring more customers to higher-risk lenders like Home Capital, overall, the mortgage market is in a rough spot.

Valeant Pharmaceuticals Intl Inc. (TSX:VRX)(NYSE:VRX) also recently released its fourth-quarter and year-end results and 2018 guidance, which was disappointing.

Make no mistake, earnings are still dropping. The stock has been taken down from levels of over $300 per share to under $20 currently — a massive slide that left many shocked and angry investors in much financial pain.

But what's next?

Well, the company's new CEO definitely has a big task ahead of him, with 2018 as the year to set things up for the future.

The core strategy is a sound one, with a focus on reducing patent risk and benefiting from the secular trend of rising demand for healthcare and healthcare-related products as our population continues to age.

And after a few quarters of meeting or beating expectations and room to beat 2018 expectations, patient investors might be rewarded a few years down the line.

A reduced R&D risk profile, the clearing of legal issues, and a strengthening of the balance sheet would go a long way.

But continued high debt levels, accelerated product launches, and spending will put the pressure on results. However, it's short-term pain for long-term gain.

Bottom line

Clearly, both of these names have risks associated with them, but both have much potential as well.

The macro environment for Valeant is more attractive than that for Home Capital, but the company-specific risk is slanted the opposite way.

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Date
2025/07/28
Date Created
2018/03/05
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