Was Warren Buffett Right to Bail on Canada’s Housing Market?

Description

It’s been almost two years ago now since world-famous billionaire investor Warren Buffett made headlines across the country when he announced his intention to bail out **Home Capital Group** (TSX:HCG), ultimately saving the firm from what then seemed like almost certain insolvency.

While others at the time were questioning whether Home Capital would make it through the end of the year, Buffett, through his holding company **Berkshire Hathaway**, offered to step in and provide the then-embattled mortgage lender with a $2 billion emergency line of credit in addition to an equity stake in the firm, then valued at as much as US$400 million.

That additional element, the ownership piece, and Berkshire’s willingness to align its interests directly alongside those of the company’s existing shareholders ultimately served to restore investor confidence in the company.

After all, if Buffett was willing to be an owner, why wouldn’t anyone else want to be?

Between May and June of 2017, HCG stock would go on to rally from its intraday low just pennies north of $5 per share to new highs of more than $20 per share.

Since then the stock has worked to find support trading often between the mid-to-high teens, as the company’s leadership team under the direction of new CEO Yousry Bissada, works diligently to regain its footing and to restore its credibility as a trusted alternative lending institution.

Ironically, one of the most volatile periods to hit HCG stock since the Berkshire bailout came late last year in December, when Buffett announced that BRK was planning to “substantially exit” its position in Home Capital.

As part of the original rescue deal, Buffett had negotiated an option whereby he would be entitled to increase his ownership stake from the original 19.9% up to 38.4%.

But when it came to a vote in September of later that year, HCG shareholders voted against granting Buffett the additional stake because of the dilutive impact it would have had on their existing ownership positions.

Foolish bottom line

Despite that the Buffett-Home Capital marriage only ended up lasting a grand total of less than two years, it would still be difficult to argue both parties aren't better off today for having been party to it.

Buffett and BRK, of course, walked away with their line of credit paid back in full in addition to a tidy return on Berkshire's short-lived equity stake in the company.

Meanwhile, Home Capital has enjoyed the benefit of having its investor confidence restored while continuing to make progress, even in the time since Buffett's departure, including year-over-year growth in mortgage loan originations, deposits, and net income during the first quarter.

Yet even despite its progress, HCG shares continue to trade below their reported tangible book value, making this an interesting investment idea should the Canadian housing market continue to display strength.

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