This Stock Market Genius Has 3 New Stock Picks

Description

If you don't who Steven Eisman, get acquainted. Investors who followed his advice made *billions* during the financial crisis. He's a major character in Michael Lewis's mega-seller book, *The Big Short*. Steve Carrell played him in the movie adaptation. When Eisman speaks, it pays to listen.

In 2007, he was pitching the extreme dangers of mortgage-backed securities. Today, he's worried about Canadian banks. He's gone as far as to bet his own money that three Canadian banks in particular will fall in price.

Fear the banks

Earlier this year, Eisman shorted a handful of Canadian banks, including **Royal Bank** (TSX:RY)(NYSE:RY), **Laurentian Bank** (TSX:LB), and **Canadian Imperial Bank of Commerce** (TSX:CM)(NYSE:CM).

His thesis is simple: it's the calm before the storm. For decades, Canadian banks have largely been immune from economic pressures. This has led investors to assign a healthy premium to the industry.

Take a look at most research on Canada's bank stocks, and you'll see adjectives like *safe* and *reliable*. In reality, the industry could be woefully underprepared for even a slight dip in conditions.

"Canada has not had a credit cycle in a few decades," Eisman told *Bloomberg*. "I don't think there's a Canadian bank CEO that knows what a credit cycle really looks like." When asked how much downside there is, he simply responded: "They'll go lower. How much lower? We'll see. Twenty percent plus. That's about as much as I'll bet at this point."

His confidence that Canadian bank stocks will fall has been growing. In June, he revealed that he's been adding to his positions. "I would say, when we spoke about two, two-and-a-half months ago, my conviction level on the idea was about a seven out of 10," he told *Bloomberg*. "After looking at the Canadian banks' reporting season, I think I'm more like a nine."

What could go wrong?

There are several factors that could send RBC, Laurentian Bank, and CIBC tumbling. Analysts have been suggesting that Canada's real estate markets are approaching bubble territory, especially in metro areas like Toronto and Vancouver. Consumer debt levels are on the rise, and sluggish energy prices have hit regional economies hard.

Any one of these areas could cause a small correction in Canadian markets.

"At this stage in the credit cycle, what you should be seeing is increasing levels of reserves that increase faster than impaired loans, because essentially what you want to do is build money for a rainy day," Eisman believes. "You did not see that at all in Canadian banks. In fact, what you saw was reserves were basically flat."

How quickly could conditions worsen? "I'm not going to make a prediction on what quarter," he cautioned, but added that he thinks a downturn should happen "within a year." If you're expecting your bank stocks to be a safe haven, think again.

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2. NYSE:RY (Royal Bank of Canada)
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