These Are the 3 Riskiest Names in Canadian Banking

Description

As an old curmudgeon who still believes that excess debt is not a good thing, I have to admit that I have had my head handed to me. I have long thought that at some point in time, our love affair with credit would end badly, putting enormous pressure on people, countries, and businesses who have large amounts of debt on their ever-deteriorating books. Even though the perpetual motion machine of leverage continues to steam ahead, I can't shake the feeling that it will end badly.

So, if you are a bit of a Chicken Little like me who wants to keep the sky from falling on your head, you have to avoid stocks that are benefitting from the insane run-up in debt. In Canada, there are a number of stocks that could be annihilated should the economy take a dire turn for the worse.

Due to these conditions, it is quite likely that **Home Capital Group** (TSX:HCG), **Equitable Group** (TSX:EQ), and **goeasy** (TSX:GSY) are some of the riskiest names in Canada today.

It's been a great year

The stocks have been performing handsomely, so why worry? Home Capital shares are rising above $30 once again. Its mortgage originations are up almost 17% as of Q3 2019. EQ Bank has had an astounding run this year, with its shares going parabolic, up about 70%. Its earnings per share were up 16.2% year over year on and it increased its dividend by 25% over the previous year's payout.

GSY had similarly great results, with earnings per share up by 54% in Q2 2019 year over year. Its revenues increased by 20%, leading this company to have a similarly massive capital gain of 62% in the last year. I will grant you that these are fantastic returns, but these returns should make you wary.

The danger is real

The fragility in these stocks lies in the fact that Canadians are tapped out. They have borrowed, spent, and leveraged themselves into a corner, and there is a very real possibility that they might soon be trapped. This isn't far fetched. In fact, we had a taste of this a couple of years ago, and there wasn't even a recession.

Back in 2017, Home Capital stock showed what could happen to the sector in the event of a housing collapse or loss of faith in the banking sector. In the case of Home Capital, there wasn't even a real decrease in housing prices that made the stock fall.

There was only the possibility of problems, which led to a run on the bank that nearly leveled the company, driving shares down to single digits. The dividend was cut entirely to preserve capital and has not yet been reinstated.

Equitable was driven down as well, hitting a low of just under $40 before beginning to rebound. The sell-off was vicious, people pulled their money, and the banking shares collapsed. Imagine what would happen if there really was an economic downturn.

While goeasy was not a part of the downturn, it is likely that this stock will be similarly affected. The company makes loans to high-risk individuals, loaning out cash in the range of $500 to $15,000 for rates of around 29.99%. This might be a decent business while people can pay their loans, but what if jobs are lost and suddenly they can't?

The bottom line

These companies have run their businesses well. They have fed Canada's love affair with debt, and shareholders have been greatly rewarded. But the stocks are going parabolic just as the country is running like lemmings towards a debt collapse.

I will say this: if the wheel of perpetual debt keeps turning, all three companies will be fine. They will make a tonne of money as people continue to accumulate debt to infinity. But we have already seen what happens to the stocks when there is panic. A recession, debt collapse, or housing crisis will most likely affect these exposed stocks greatly.

As I frequently like to state, get your money back from these stocks as soon as possible. A combination of capital gains and dividends should pretty much do it for many. Be careful with these stocks, though, and limit your exposure, because their shares might be hit hard.

CATEGORY

1. Bank Stocks
2. Dividend Stocks
3. Investing

TICKERS GLOBAL

1. TSX:EQB (EQB)
2. TSX:GSY (goeasy Ltd.)
3. TSX:HCG (Home Capital Group)

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1. Business Insider
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