Could Rate Hikes Deal More Damage to These Housing Stocks?

Description

North American markets have been rattled as the prospect of interest rate hikes loom large this week. The Bank of Canada (BoC) and the United States Federal Reserve are set to meet this week. Inflation has surged in both countries, putting increasing pressure on central banks. Today, I want to look at two Canadian housing stocks that have been hit hard by volatility over the last week. Let's jump in.

Two housing stocks that have plunged over the last week

Home Capital Group (TSX:HCG) is a Toronto-based alternative lender that provides mortgage lending, securitization of residential mortgage products, as well as consumer lending and credit card products. Shares of this housing stock have plunged 9.1% over the last week as of mid-morning trading on January 24. This has pushed the stock into negative territory for 2022.

Investors can expect to see the company's final batch of 2021 results on February 17, 2022. Its shares last had a very favourable price-to-earnings (P/E) ratio of 7.7.

Equitable Group (TSX:EQB) is another top alternative lending company. Its stock has dropped 8.1% week over week. However, shares of Equitable Group are still up 28% in the year-over-year period.

In Q3 2021, the company saw assets under management (AUM) increase 13% year over year to $40.2 billion. Meanwhile, EQ Bank deposits increased 60% to $6.9 billion. Earnings in the year-to-date period rose 39% to $212 million. The company is also set to unveil its fourth-quarter 2021 earnings on February 17. Equitable Group stock last had an attractive P/E ratio of 8.5.

Mortgage lenders and the broader Canada housing industry anxiously await the BoC's decision this week.

Will interest rates hikes hurt the Canadian housing market?

Back in November 2021, I'd discussed whether interest rates hikes would torpedo the red-hot Canadian housing market

. **Bank of Montreal** economist Robert Kavcic recently warned that higher rates would likely lead to a decline in Canada housing prices by the end of 2022. However, BMO does not expect an extreme chill in the market.

Canadians have been able to gorge on fixed mortgage rates that have fallen into negative territory in real terms, factoring in inflation. Indeed, even a few marginal hikes will put the squeeze on a Canadian population that has seen its household debt balloon in recent years.

Bottom line: Should you bail on housing stocks right now?

The interest rate story might not be all bad for Home Capital and Equitable Group. Higher rates will put pressure on consumers, but this could also spur a move to alternatives. Home Capital and Equitable Group both offer loans meant to lure consumers away from larger lenders like the Big Six banks. A higher rate environment could afford these institutions more wiggle room to compete. Better yet, profit margins at these institutions will also receive a boost due to higher rates.

Investors should monitor the drop in both housing stocks as we move into late January. Both stocks boast very favourable P/E ratios at the time of this writing. A steep correction could present a fantastic buying opportunity.

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