John Paulson's Housing Bets Pay Off

JOHN MELLOY , FAST MONEY, FAST MONEY: HALFTIME REPORT, MGIC INVESTMENT CORP, RADIAN GROUP INC, GENWORTH FINANCIAL INC, FIDELITY NATIONAL FINANCIAL INC, THE HARTFORD FINANCIAL SERVICES GROUP INC, WILLIAM LYON HOMES, BUSINESS NEWS

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A schadenfreude-fueled press and jealous peers who keep talking about John Paulson's losses in gold are missing the hedge fund manager's second round of masterful trades involving housing—this time on the bullish side.

The man behind the so-called greatest trade ever acknowledged this much in a recent letter to clients pointing out that gold makes up a minuscule portion of the $20 billion Paulson & Co. has under management.

"The Gold Funds, which represent only 2 percent of our AUM, have received a disproportionate amount of attention over recent months and have detracted attention from the performance and positive developments of our other funds, 98 percent of our assets," wrote a firm managing director in a June 6 letter obtained by CNBC.

Those positive developments include a 27 percent year-to-date return in the Paulson Recovery Fund because of big gains in mortgage insurers, such as MGIC, Radian and Genworth, as well as title insurer Fidelity National Financial.

These big bets in this portfolio suggest a man who believes the country is only in the beginning stages of a housing recovery. And he should know.

Paulson, whose firm has had only had two down years since 1994, netted $15 billion in 2007 in betting against complicated subprime mortgage securities tied to a rising housing market, a move immortalized in the book "The Greatest Trade Ever."

(Read More: Paulson Raised Bet on Mortgage Insurers in First Quarter Filing)

To be sure, Paulson's investments in gold and gold miners are enough to drag down the value of the firm's other funds. Paulson Advantage Funds, which make up a quarter of the firm's assets, are up only 4 to 6 percent this year because of investments in gold stocks. The small gold funds have lost half their value this year.

But that's taking the focus off where Paulson's passion apparently lies: finding ways to benefit from the rise of the very same housing market he so presciently saw falling apart just a few years ago.

The mortgage insurers are a purer, riskier play on housing than a bank since their business benefits only if homeowners can afford to keep making their payments and foreclosures don't overwhelm the market.

"Radian's new business is highly profitable as a result of conservative underwriting standards introduced in late 2008," Paulson wrote to clients after the first quarter. "Mortgage insurance stocks remained depressed through the end of 2012 amid lingering uncertainty as to whether they had sufficient capital to absorb losses on delinquent loans originated before the crisis. However, as house prices began to recover, losses started to decline."

Paulson believes Radian, which closed at $12.73 on Friday, could be worth $20 by 2015.

Genworth is up this year "as the company achieved regulatory approval to restructure its U.S. mortgage insurance business and sold one of two non-core businesses," wrote Paulson. "We believe there remains considerable upside as the company continues to make progress on its announced restructuring and the housing markets continue to recover."

The Recovery fund also owns securities in Hartford Financial and Conseco and private stakes in One West Bank and Extended Stay.

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If you have any doubts as to Paulson's conviction behind a strong housing market, look no further than his creation this year of a second real estate fund, which will buy mostly raw land. This real estate will only see very big gains when housing inventory is reduced to a point where home builders come scrambling back to Paulson to buy that land back.

What's more, Paulson was a big backer in the May initial public offering of William Lyon Homes. Paulson remains heavily invested in the builder focused on California, Arizona and Nevada, whose shares are trading at their $25 IPO price.

For the critics, Paulson is still bullish on gold on the belief that inflation will escalate as the Fed and other global central banks try to unwind their unprecedented balance sheet expansion. The miners are cheap, too, he said.

"When measured in terms of EV/EBITDA, the gold sector is currently trading at 6.8x, which is below the lows reached following the failure of Lehman Brothers," Paulson wrote in his first-quarter letter for the Gold Funds.

But who really cares what he thinks of gold? It garners just 2 percent of Paulson's attention these days. The rest of his time is occupied by finding long-term ways to benefit from a burgeoning housing and economic recovery.

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