3 Reasons to Buy This Financial Stock Instead of the Big 5

Description

When building a portfolio of Canadian stocks it is common practice to start with the big five banks. This should come as no surprise as the banks are Canada's largest companies, are generally viewed as safe and pay a nice dividend.

But there is one financial institution that would make a much better staple in your portfolio: **Home Capital Group** (TSX: HCG), which mainly deals with residential mortgages in Canada.

1. Better returns

Everyone knows that Canadian banking is an extremely high-return business. The problem is that Canada's banks are involved in other activities as well. **TD Bank** (TSX: TD)(NYSE: TD) is a prime example. Despite being Canada's second-largest bank, it actually has more branches in the United States. And the U.S. is not nearly as attractive a market; TD's return on equity in the U.S. was only 8.1% last year. As a result, return on equity for TD overall was 15%.

Meanwhile, ROE for Home Capital Group was 23.9% last year and this did not come from taking increased risk. The Common Equity Tier 1 Capital ratio last year came in at nearly 17%, far higher than any of the banks (that number was 9% at TD).

2. Better growth potential

Another problem with Canadian banks is a lack of growth prospects, especially at home. This is a big problem for **Canadian Imperial Bank of Commerce** (TSX: CM)(NYSE: CM). CIBC has decided to retreat from foreign markets and focus on plain old Canadian banking, meaning any substantial growth will likely have to come from (fully priced) acquisitions.

But Home Capital Group isn't nearly as big, and has plenty of room to grow. According to the company, its addressable market (as of late last year) is $260 billion worth of mortgages, meaning Home Capital has about 3% market share.

Its net income growth target is 13%-18% per year, a goal it has been consistently meeting (last year net income grew by 15.6%).

3. Not too expensive

Even though HCG shares have outperformed the Canadian banks over the past 12 months (up 75%), they are still not overly expensive. Take **Royal Bank of Canada** (TSX: RY)(NYSE: RY) for example. Canada's largest company is firing on all cylinders, growing its wealth management and capital markets businesses worldwide as others retreat. But its shares trade at 13.2 times earnings.

Home Capital Group's shares trade at only 12.9 times earnings, even though those earnings are growing faster than RBC's. So for those of you not afraid of Canada's housing market, Home Capital Group makes a much better investment than Canada's largest banks.

CATEGORY

1. Investing

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1. NYSE:RY (Royal Bank of Canada)
2. NYSE:TD (The Toronto-Dominion Bank)
3. TSX:CM (Canadian Imperial Bank of Commerce)
4. TSX:HCG (Home Capital Group)
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Date
2025/09/14
Date Created
2014/07/10
Author
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