Should Investors Prefer These 3 Financials Over the Big 5 Banks?

Description

Many Canadian investors hold banks as the bedrock of their portfolio. It's easy to see why. The banks have a great moat, thousands of collective branches, very little in terms of competition from foreign operators, and business models that have been proven to work through thick and thin. Many of the large banks have paid annual dividends for longer than a century, which is the kind of consistency that many investors crave.

But Canada is filled with plenty of financials that are constantly overshadowed by the five large banks we've all heard of. Let's take a closer look at some of these so-called forgotten financials and see whether they'd be a good fit for your portfolio.

National Bank of Canada

Although it has been around for longer than a century and has a market cap of more than $16 billion, **National Bank of Canada** (TSX:NA) is often overlooked as a potential investment.

But there are some nice advantages to owning it. It consistently trades at a price-to-earnings discount compared with its peers. Currently, the stock trades at just 11.4 times trailing earnings, and at less than 10 times projected 2015 earnings. That's between 10-15% less than its competitors. The stock is also among the cheapest in the sector based on other metrics like price-to-book value.

Two reasons why the stock trades at a discount is because of its Quebec-centric operations, and because it doesn't have any major operations outside of Canada. National could solve both of those problems by finally going out and expanding into the United States. There are dozens of smaller banks in the U.S. that trade at reasonable valuations that could be interested in being acquired by a larger Canadian parent.

Fairfax Financial

The record of Prem Watsa, the man in charge of **Fairfax Financial Holdings Ltd.** (TSX:FFH) is nothing short of extraordinary.

Since Watsa took over in 1985, Fairfax has grown book value by more than 20% annually, a track record comparable with Warren Buffett's. And like Buffett, Watsa uses the float generated by Fairfax's massive insurance holdings to get almost free leverage—cash that's invested in undervalued companies. As results show, he's been pretty successful at it.

Watsa is also famous for taking huge macroeconomic bets. His latest is using derivatives to make a massive wager on both China's economy collapsing and deflation rearing its ugly head. If he's right, he'll earn billions in profits for Fairfax shareholders. These bets may seem a little outlandish, but remember, Watsa did successfully predict the U.S. mortgage meltdown, as well as the tech bubble collapsing.

IGM Financial

IGM Financial Inc. (TSX:IGM) is the parent company of Investors Group, one of Canada's largest wealth managers. The company's more than 5,000 advisors offer clients everything from mutual funds to mortgages to life insurance.

Investors have sent shares lower, bearish on the company because stricter rules on mutual funds fee disclosure is coming in 2016. But the market is missing many of the positives, including the company's more than $150 billion in assets under management, as well as the terrific brand. Even if fees are more accurately disclosed, the vast majority of clients will stick around. They just don't have the skill to invest in self-directed alternatives.

Investors who buy in now are getting a stock that's selling at less than 15 times earnings, and yielding more than 5.2%. That's a pretty solid value for a company that boasts the kind of moat Investors Group offers.

While the big banks get all the attention, Canada is filled with other financials that offer compelling value in today's possibly overextended market. Maybe it's time to expand your portfolio's horizons and add some of these companies to your watch list.

CATEGORY

1. Bank Stocks
2. Investing

TICKERS GLOBAL

1. TSX:FFH (Fairfax Financial Holdings Limited)
2. TSX:IGM (IGM Financial Inc.)
3. TSX:NA (National Bank of Canada)

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