VersaBank (TSX:VB): A Small Canadian Bank Worth Looking Into

Description

Canadian investors have been pretty happy with their big bank holdings over the years. Companies like **Bank of Nova Scotia** (TSX:BNS)(NYSE:BNS) and **Royal Bank** (TSX:RY)(NYSE:RY) have provided excellent returns with growing dividends over the years. But what about smaller Canadian banks? Would some of these be worth looking at to add to a dividend portfolio?

One Canadian Chartered bank that recently caught my eye is **VersaBank** (TSX:VB). With a market cap of only 145 million, it is much smaller than the big banks, but also much cheaper. While the larger banks are trading at higher valuations, VersaBank trades with a price to earnings ratio of around 8.6 and is currently below book value. The cheapness of the stock is enticing for value-oriented investors.

The bank operates as an online banking alternative with no branches to maintain. The business model is similar to other online banks such as **Equitable Group Inc.**, where the lack of branches frees up capital to offer higher interest rates to depositors. It is also investing in block chain-based savings accounts in hopes of staying ahead of other traditional banks in technological innovation.

The bank is smaller than that of many of its larger competitors, so its gains have been considerable. Over the last year, VersaBank managed to increase net income by 102% and earnings per share increased by 157%. These numbers are quite astounding, even more so since this company is not priced for growth at its modest valuation.

VersaBank also offers investors a dividend, albeit a small one. At the current stock price, the dividend is around 0.43%, not at all as large as the 3-4% yields currently offered by the larger banks. But VersaBank only recently started paying a dividend and the payout ratio is extremely small at just under 4% of earnings. Compare this to the larger banks that often keep their dividends at 50% of earnings and you can speculate there should be decent growth in future payouts.

Although this bank is posting impressive numbers, an investor must look at the risks associated with the investment. VersaBank commercial loans are mostly secured by Ontario real estate, although some are secured by real estate in other parts of the country. The quality of its loans is therefore determined by the health of the Ontario real estate market. If an investor is at all concerned with the

Canadian real estate market, VersaBank may not be a suitable investment for them.

VersaBank is also not nearly as diversified as the larger banks. It is a Canadian bank, serving Canadian customers, so its future rests on the future of the Canadian economy. The economy has been strong and is forecasted to remain so in the near term, so that may not be a concern for many investors. But the size of your investment will directly reflect your faith in the economy's continued strength.

If you choose to invest in VersaBank, you are choosing to invest in the Canadian economy. The bank is currently growing rapidly and has begun to pay a dividend. While I wouldn't recommend selling your holdings of larger banks to buy this one, it might be an interesting idea to accumulate a small number of shares in this bank to complement your holdings of the larger banks. If the Canadian economy continues to be strong, VersaBank should follow along as well.

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