Attention Growth Investors: This Might Be the Best Bank on the TSX

Description

One of my favourite, little-known growth stocks, **VersaBank** (TSX:VB) reported earnings this morning. The good news is that the bank's growth story is still intact. In 2018, the company bucked the industry downtrend and gained 13.56%. Year to date, it has returned 8.6% and is on pace for another year of double-digit growth.

First-quarter earnings

It was a good start to the year for VersaBank. Net income of $4.9 million grew 24% year over year, and the company's core cash earnings per share grew by 14% to $0.32. Net interest margin was another bright spot, as it grew by 13 basis points to 3% in the first quarter.

Return on common equity grew by 136 basis points to 8.86%, which was in line with the fourth quarter of last year. Its e-commerce business continues to gain traction, as lending assets grew 3.54% to $921 million from last quarter and 10.55% from a year ago. Finally, the company's book value grew to $9.39, up 8.6% from the end of the first quarter of 2018.

Although it was a solid quarter, the company's commercial banking segment underperformed. The portfolio dropped by 8.1% over the first quarter of 2017. The company took a more cautious approach to lending as it adopted IFRS 9, which fundamentally altered its methodology. Furthermore, the company's gross impaired loans jumped to 1.22%, up from 0.04% last quarter. The increase is a result of the bank starting the recovery process on one "well-secured real estate loan."

The company also announced that one of its more exciting products, VersaVault, has completed beta-testing. As such, the company is now looking at commercializing the product. Although the crypto-craze has subsided, there are many uses for VersaVault outside of digital currency. Anything digital, from intellectual property to pictures, can be stored within the VersaVault.

Company valuation

VersaBank has remained chronically undervalued for the better part of the past two years. This is due in large part to the relative obscurity of the company. With only one analyst covering the company on a regular basis, it's not well known in the retail investing community. This doesn't make it a bad stock. In fact, the opposite is true. VersaBank has delivered double-digit returns since its split from PWC Bank, and given its growth profile, there is no reason to expect any different in 2019.

Including the first quarter of 2019, VersaBank is trading at a cheap 9.65 times earnings. Assuming the company grows at a 10% clip, which is well below historical averages, it would have a P/E-to-growth ratio under one. This is a clear sign that the company's share price is not keeping up with expected growth rates.

Likewise, it is trading a $1.52 below book value and its price-to-book ratio dropped to 0.83.

Foolish takeaway

An investment in VersaBank carries more risk but can also lead to outsized returns. Investors who are interested in looking outside the box and can handle volatility would do well to look at VersaBank.

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