



## Strong Cash Flow Makes This Bank a Must-Own Stock

### Description

I couldn't believe my eyes.

*The Globe and Mail's* Number Cruncher column recently highlighted 15 **TSX** stocks that prioritize cash flow. The name of the stock at the top of the list was **VersaBank** (TSX:VB), Canada's first digital-only bank.

I [recommended](#) VersaBank to Foolish readers in May 2016, suggesting that its share price could easily be higher than \$10 within three to five years. Well, almost three years later, it's trading around \$7.50, up 36% at writing, nearly double the TSX and well on its way to the double digits.

I'd forgotten about the little bank that could until I happened to see the article in mid-April. I'm glad I did because VB stock still appears to be a quality buy. Here's why.

### The criteria for cash flow prioritization

The Globe's article was written by Emily Halverson-Duncan, a chartered financial analyst (CFA) working with Morningstar Research.

Halverson-Duncan set three screening criteria:

First, a stock had to have annual cash flow momentum, meaning that it grew cash flow in its most recent fiscal year. Second, it had to have a positive five-year cash flow growth rate, and finally, it qualified if its cash flow per share was positive over the latest four quarters.

Also, a stock qualified if it had a beta of less than one. Beta is defined as a stock's volatility relative to the **S&P/TSX Composite Index**.

VersaBank, which has a market cap of just \$158 million, had annual cash flow momentum of 149.5%, a five-year cash flow growth rate of 63.3%, and its cash flow per share was positive over the past four quarters.

As I stated in the opening, VersaBank ranked first on the list of 15 stocks. Other names on the list Foolish investors ought to like include **Brookfield Asset Management**, **Alimentation Couche-Tard**, and **Parkland Fuel**.

## VersaBank's other attractive qualities

Fool contributor Victoria Hetherington recently [recommended](#) VersaBank stock along with two other smaller Canadian banks. She suggested that VB is both a value and growth stock boasting a P/E of just 9.2 while also growing its earnings by 30.4% annually over the past five years.

In addition, Hetherington likes its strong balance sheet, and argues the high insider buying in recent months is an indication good things are happening at the bank.

Looking at its Q1 2019 earnings report, all the critical numbers banks use to assess how they're doing were very positive.

Net interest margin, the amount a bank makes on its interest-bearing assets after accounting for the interest it pays to lend out funds, was 3.00% in the first quarter, 13 basis points higher than a year earlier.

The efficiency ratio, defined as a bank's non-interest expenses divided by net income, demonstrates a bank's ability to make money while controlling its overhead and costs. In the first quarter, it was 52%, down from 56% a year earlier. The lower the efficiency ratio, the better.

VersaBank's core cash earnings in the first quarter were \$6.8 million, a 15% increase over the same quarter a year earlier. It finished the first quarter with total assets of \$1.75 billion, \$40 million higher than in Q1 2018. In terms of loans, at the end of the first quarter, it had \$1.6 billion outstanding, 1.3% higher than a year earlier.

To put this all in perspective, the bank's efficiency ratio of 52% in the first quarter, was almost three percentage points lower than the **Canadian Imperial Bank of Commerce's** efficiency ratio in its first quarter.

Maybe that's to be expected when talking about a digital-only bank, but it's still very impressive.

## The bottom line

VersaBank's created VersaVault Inc., a wholly owned subsidiary providing a digital bank vault for cryptocurrency exchanges and funds holding cryptocurrency or blockchain-based assets.

Given the mess surrounding QuadrigaCX, a service that could store the private cryptographic keys needed to access a customer's cryptocurrencies would seem to be something useful worth exploring.

I'm not saying you should buy VB stock because of this, but it sure is a new sideline business that one day could turn into significant revenue.

In the meantime, enjoy VersaBank's steady cash flow.

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