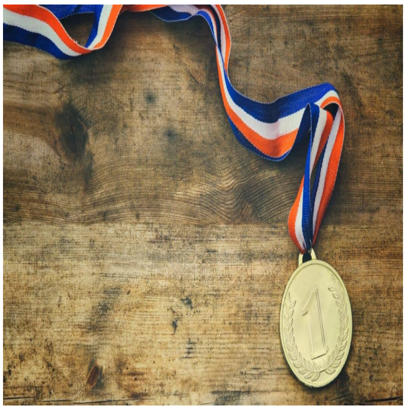

Why This Alternative Lending Company Will Be a Top Performer on the TSX This Year

Description

The non-prime credit segment is a vital part of the Canadian economy. Not only is it important that individuals with low credit scores still have access to capital; it can also be a lucrative business based on the large interest rates associated with high-risk borrowers. These large interest rates present the opportunity for companies to make a lot of money if they are able to manage defaults.

The non-prime credit segment in Canada is a considerable size. Research shows that almost a quarter of Canadians with credit scores are considered non-prime, or have credit scores below 700. That's more than seven million non-prime borrowers that need access to capital. One company that has been expanding rapidly in this segment is **goeasy** (TSX:GSY).

goeasy is a leasing and alternative-lending company. It started in 1990 as Easyhome, a leasing company that would allow customers to lease furnishings and large appliances for their home. While the company still operates Easyhome, only about a quarter of revenue comes from it. Easyfinancial, which was established in 2006, is the non-prime credit lender and accounts for about 75% of the business goeasy does, and this continues to grow.

When dealing with non-prime credit, it is paramount for companies to manage the number of defaults, or charge-off rate. In goeasy's case, charge-off rates have been rising very slightly in recent quarters; however, it is still well within managements range of 11.5-13.5%. Throughout the last decade, goeasy has done an incredible job of steadily decreasing these rates but, more importantly, keeping these rates consistent.

Although neither the company, nor investors want charge-off rates to rise, currently in a worst-case scenario, the company could sustain an 84% jump in charge-off rates, bringing the number from 13% to 23.4%, before the company would start to lose money. This is a very large margin of safety for investors; it would take a catastrophic macroeconomic event for this to happen.

The company looks fairly valued, especially considering the large cash flow it yields. Return on equity has also been growing consistently and now sits above 20%. The net-debt-to-capital ratio, which sits around 66%, shows the company is well capitalized and is far better than many of its peers. The board and management also own 27% of the company, which is a positive sign, as shareholders share the same incentives as the management team.

The main reason for an investment in goeasy is the rapid growth it has been achieving. Since 2001, revenue has grown at a compounded annual growth rate (CAGR) of 12.7% Net income has also been growing well, too. In that same period, the net income CAGR was 29%, while EPS had a CAGR of 22.7%. On top of all of that, the company has reported 70 consecutive quarters of positive EPS.

With huge cash flow yields and solid risk management, goeasy is an exceptional pick for investors. The company continues to meet the targets it sets for itself and continues to set high growth guidance for the next three years. While the growth targets are ambitious, given the track record of management and the company, there's no reason it shouldn't be able to deliver.

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