This Cheap Stock Has the Highest Upside in the Banking Industry

Description

Canada's Big Five Banks are the cornerstone of many portfolios. They are reliable dividend stocks, and in several cases have streaks of 100+ years of uninterrupted dividends. Even during the worst financial crisis of our lifetime, Canada's banks continued to pay a dividend. Not only did they still pay a dividend, but not one of them cut dividends.

That's quite the accomplishment, especially when banks worldwide were cutting dividends at a rapid pace. However, as Canada's Big Five gain most of the attention, a number of smaller Canadian banking stocks that fly under the radar. For investors looking outside the box, it presents them with an opportunity to load up on these quality stocks on the cheap.

Case in point: **VersaBank** (TSX:VB). VersaBank is Canada's first fully digital Schedule 1 Chartered Bank. For those who took a chance on this company, they have been well rewarded.

Since splitting from PWC Bank in late 2015, the company has outperformed the majority of Canada's Big Five banks with a 14% return. This is second only to the **Bank of Montreal's** (TSX:BMO)(NYSE:BMO) 28% return over the same period.

As the market started to notice its undervaluation, its outperformance has become even more pronounced. Over the past two years, the company's share price has climbed almost 63%, far outpacing the Big Five.

Why is VersaBank topping its larger peers? It's all about growth. This small cap banking star has been growing at an impressive pace. Since going public, the company has averaged 30%+ earnings growth. Although growth is expected to slow, earnings growth in the mid-to-high teens, is still more than double the average of the Big Five.

Through the first six months of the year, net income is up 19% and core cash earnings experienced 15% growth over the first six months of 2018. This banking small cap has done nothing but deliver since going public.

A rising dividend

As the company found its footing as an independent banking stock, it has only recently begun to raise dividends. However, it is doing so at a rapid pace. Versabank announced its first dividend in November of 2017 and has since raised it twice.

The latest dividend bump came along with second-quarter results. The company raised dividends by 33%, or $0.005 per share for a new quarterly dividend of $0.02 per share. It was the second raise in the past three quarters and the dividend has doubled since November of 2017.

It appears to be setting itself up for bi-annual raises (once in Q2 and again in Q4), the same pattern that the majority of other Canadian banks follow. With a very low yield (0.80%) and a payout ratio (9.6%), I expect another high-percentage raise this coming November.

As a stock that flies under the radar, VersaBank can be acquired on the cheap. It trades at only 8.69 earnings and at a cheap 7.5 times forward earnings. Although it may be more volatile than its larger peers, at only 0.65 times book value it has higher upside than the majority, if not all of Canada's banking stocks.

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1. Bank Stocks
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