Investors: This Unheralded Banking Stock Is Up 788% With More Room to Grow

Description

Let's talk a little about the Canadian banking industry.

As you may already know, the sector is dominated by the so-called Big Five, a handful of banks that command an 80% market share. These fine institutions have gobbled up their competition over the years, and have then used their size to sit comfortably atop the market.

There's just one problem: Canada's top banks aren't exactly growth machines. Profits from domestic operations grow at about 5% per year, especially now, as it's become tougher for home buyers to qualify for mortgages over the last couple of years. International growth is a little better, which helps the overall bottom line.

Compare that to some of Canada's smaller banks and there's no comparison. These smaller institutions offer much better growth potential. They're also easier to analyze, and offer potential upside from being acquired by one of the aforementioned bigger banks.

Let's take a closer look at **Canadian Western Bank** (TSX:CWB), one of these smaller Canadian banks. This stock is no slouch; it has delivered a 788% return — including reinvested dividends — over the last two decades.

The skinny

Canadian Western Bank has 42 branches located in Western Canada, primarily in Alberta and British Columbia with approximately $30 billion in assets and is Canada's tenth-largest bank.

Shares have been somewhat beaten up lately because of a few different factors. The biggest one is Alberta's economy. The energy-dependent province just can't catch a break. Oil prices continue to languish below $60 per barrel, and energy producers are frustrated at the lack of new pipelines transporting Alberta's oil to other markets. Naturally, this translates into lackluster economic numbers.

There's little doubt that this weakness has impacted Canadian Western Bank. And there's always the risk of the Vancouver real estate market suddenly imploding, which wouldn't be a good thing.

Underlying numbers look pretty good, even if Alberta's economy continues to be in the dumps. The company grew revenue by 7% in its most recent quarter, seeing saw profits increase 2%. While that doesn't seem like much, most other Canadian banks saw a decline in profits during the same period. Canadian Western Bank's loan loss provisions are a mere 0.23%, which is lower than the peer average as well.

Just imagine how well it could do if Alberta was humming again, which makes it a natural place to invest if you think Alberta will recover.

The bank is a diverse operator that isn't just about regular mortgages. It specializes in loaning to businesses, including commercial mortgages, franchise financing, and equipment financing and leasing. It also has a small oil and gas lending arm, but that's less than 1% of total loans outstanding.

It has also done a nice job of expanding outside of Alberta and B.C., with 45% of loans now made to folks outside of these two provinces. Growth in Ontario has been the most striking, with nearly 30% of all loans now made to borrowers inside the province.

An underrated dividend

Canadian Western Bank has one of the better dividends in the banking sector, which is saying a lot. After all, Canada's top banks are known for their dividend growth.

Shares currently yield 3.7%, which isn't quite as high as the average yield of the big five. But Canadian Western Bank wins when it comes to its conservative payout ratio. The Big Five target a payout ratio of approximately 50% of earnings. CWB's target payout ratio is just 30% of earnings. The company hasn't quite gotten there yet, but it's pretty close. It paid out just 36% of earnings back to shareholders as dividends thus far in 2019.

If anything, you could argue that Canadian Western Bank's dividend is more secure than the average payout in the sector, and it has hiked its payout each year since 2011.

The bottom line

Despite having to deal with two big oil crashes and going up against tough competition, Canadian Western Bank stock is up 788% over the last 20 years, assuming dividends were reinvested the whole time. That's enough to turn a $10,000 investment made back in June 1999 into something worth $88,734 today.

With ample growth opportunities going forward, I like the company's chances to continue those excellent returns for another couple decades.

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