



Revealed: This Little-Known Bank Stock Is Poised to Crush the Competition

Description

Most Canadian investors focus on the largest banks, the dominant banking cartel I like to call the Big Five.

We've all heard of these five big banks. They're the ones with a branch on every corner. These companies spend billions on advertising, getting their brand out there via television advertising or sponsoring events. And most importantly — at least for investors — is that these large financial institutions are so dominant, most Canadians end up using their services, almost by default.

But one little-known competitor is killing it lately, dominating a part of the market that larger banks have ignored. This focus is leading to some stellar results. Let's take a closer look.

Alternative lending

Equitable Group ([TSX:EQB](#)) has barely tried to compete with Canada's largest banks.

Instead, the company focuses on niche parts of the banking business — areas its larger competition has chosen to ignore.

This has traditionally been the so-called sub-prime mortgage market, offering financing to the millions of Canadians who might not qualify for financing at their local bank branch. Equitable offers mortgages for self-employed folks, recent immigrants without a typical credit profile, and other types of borrowers that don't meet the traditional definition of a good credit risk.

More recently, there's been one factor that has boosted Equitable's bottom line. The larger Canadian banks have tightened up their lending standards, which means thousands of good borrowers — along with a few bad ones — fall through the cracks. Equitable is picking up some of this business, which is proving good for the bottom line.

We can see how good it is in the company's recently released second-quarter earnings. Equitable saw a 22% increase in residential loans outstanding in its most recent quarter when compared to the same

period last year. Commercial loans also grew nicely. This translated into a 31% year-over-year growth in quarterly earnings, with the bottom line increasing from \$2.43 to \$3.18 per share.

These results are particularly impressive when compared to other banks. One of the reasons why large Canadian bank shares have been somewhat weak over the last few months is that investors are expecting 2019 to be a tepid year. Earnings are expected to be flat versus last year's results.

In other words, Equitable is killing it compared to its competition. No wonder the stock is up more than 40% over the last six months.

A cheap valuation

Despite posting those stellar numbers, Equitable Group shares are still a [fantastic bargain](#) compared to its peers.

Analysts ratcheted up their earnings expectations for 2019, telling investors they expect Equitable to earn \$12.09 per share. They also predict earnings will continue to grow in 2020, surpassing \$13 per share. Considering the growth potential Equitable has, I'd argue 2020's estimates are a little low.

Equitable shares trade at less than eight times forward earnings expectations. The larger banks, meanwhile, all trade at 10-12 times forward earnings expectations. Large bank shares get this premium valuation, despite telling investors to expect little growth over the next 12-18 months.

Equitable shares are even cheap on a price-to-book value perspective. Thanks to this recent run-up, the company's shares finally surpassed book value in a meaningful way. The stock currently trades at 1.2 times book value. Larger banks, meanwhile, trade in a range from 1.5 times book value to sometimes as high as two times book value.

Equitable shares would be 25% higher if the stock traded at 1.5 times book value.

The bottom line

Equitable Group still has tons of [growth potential](#). Despite this potential, shares still trade at a substantial discount to its peers. Look for this discount to slowly go away over time while shares slowly grind higher.

I wouldn't be surprised if Equitable outperforms many of Canada's largest bank stocks over the next one to five years.

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