



## Investors: Should You Buy Canada's Cheapest Bank Stock?

### Description

**Laurentian Bank** ([TSX:LB](#)) has long been Canada's cheapest bank stock.

Bears argue the stock is depressed for good reasons. The company consistently posts disappointing results, as it seems like something is always wrong.

Some of the issues plaguing the stock over the last few years include a mortgage scandal, an inability to get unionized workers to agree to branch closures, and seemingly constant disappointing earnings. These issues persisted, despite a strong local economy in Quebec, the company's main operating area.

Management has pledged to solve all these issues, of course. The company has improved mortgage underwriting standards and has closed branches. It has also pledged to get profitability up to a level comparable to its larger competitors, but that hasn't happened yet.

And then COVID-19 hit, and Laurentian Bank did the unthinkable. It [slashed its dividend](#) by 40%. In a world where most Canadian bank stocks are renowned for having stable dividends, the move hit investors hard. Shares sold off on the news and haven't recovered nearly as much as other banks.

Needless to say, Laurentian Bank is dealing with some issues right now. But shares are also incredibly cheap. Does that mean the stock is a buy today? Or should investors avoid it? Let's take a closer look.

### The bull case

The bull case mostly has to do with valuation. Laurentian Bank is Canada's cheapest bank stock by a large margin. There's a lot of upside potential if management can figure things out and shares trade at a similar valuation to peers.

At first glance, Laurentian shares don't look particularly cheap. The stock trades for more than 10 times trailing 12 months earnings, which is actually more expensive than some of its competitors. But trailing earnings are depressed because of COVID-related writedowns on the loan portfolio.

Things look a little different when we look at 2019's earnings, a metric I'd argue reflects Laurentian's true profitability. The sixth-largest Canadian bank earned \$4.29 per share in adjusted earnings last year. That puts shares at approximately seven times earnings, which is a fantastic value.

Shares also trade at a significant discount to book value. Laurentian Bank is a \$30 stock today. Book value, meanwhile, is closer to \$60 per share.

We can also argue the company's dividend cut is a good thing as well. This frees up capital to put towards buying back undervalued shares or simply shoring up the balance sheet. A little financial flexibility is a good thing, especially in a weaker economy.

## The bear case

Many bearish investors argue there are huge reasons why Laurentian Bank is Canada's cheapest bank stock. These issues are why shares will remain cheap for a long time.

Let's start with a key financial metric. Many investors look at a bank's return on equity as a gauge of how efficient it is. Most of Canada's top banks post 12-15% returns on equity. Laurentian Bank posted a return on equity in the 7% range last year. That's not enough to get most investors excited.

The dividend cut was also enough to make many investors bearish. When it cut the dividend, Laurentian admitted to investors that earnings would be depressed for years. It might take several years to bounce back to 2019's earnings, while most other banks look poised to bounce back nicely in 2021.

Laurentian also posted a 75% efficiency ratio in 2019. Its competition, meanwhile, has an average efficiency ratio of approximately 45%. That is a huge gap.

And perhaps the most bearish fact is this: investors have access to other members of the Canadian banking cartel that do just about everything better than Laurentian. Why not just buy one of those companies instead?

## The bottom line on Canada's cheapest bank stock

Laurentian Bank has been hit with a double whammy. COVID-19 has impacted every [financial stock](#), Laurentian included. But the company also has to deal with persistently disappointing financial results.

In other words, Canada's cheapest bank stock is inexpensive for a reason.

But if management can turn this company around, there's serious upside potential from here. That should be enough for investors to take a second look at this stock.

### CATEGORY

1. Bank Stocks
2. Dividend Stocks
3. Investing

## TICKERS GLOBAL

1. TSX:LB (Laurentian Bank of Canada)

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