



This Bank Stock Could Be the Best Bargain on the TSX

Description

Laurentian Bank ([TSX:LB](#)) has had a torrid time over the past several months. The problems started late last year when it was revealed that Laurentian Bank sold mortgages that did not meet [eligibility and documentation criteria](#) to an unnamed third party. A subsequent review also identified ineligible mortgages that were sold to the Canadian Mortgage and Housing Corporation (CMHC) securitization programs.

To correct the damage, Laurentian Bank has had to repurchase the offending mortgages from the third party and the CMHC for a combined total of \$518 million.

Laurentian Bank's problems were compounded by its third-quarter financial results, which were below analysts' expectations. For the quarter, net income was flat, return on common shareholders' equity declined from 11.8% to 9.2%, and diluted earnings per share (EPS) declined by 17% compared to the corresponding period last year. The poor financial performance was largely due to increases in non-interest expenses including acquisition costs and salaries.

These factors have had a negative impact on Laurentian Bank's stock price, which has fallen by more than 29% since last December to its lowest level in more than five years.

Is it time to jump in and pick up this stock at a discount? Here are three reasons why I think you should take the plunge and buy this stock.

Laurentian Bank's mortgage problems have been rectified

Laurentian Bank recently completed a comprehensive review of its mortgages and the results were independently verified. Management is confident that the problems related to the incorrect mortgage sales have been resolved and that no additional repurchases will be required.

It appears that both the third-party purchaser and the CMHC are satisfied with Laurentian Bank's response. The CMHC's securitization programs remain available to Laurentian Bank and have been utilized throughout this year.

Laurentian Bank has stated that the repurchases will not have a material impact on its business, operations, capital, liquidity or funding. In fact, it's likely that Laurentian Bank will emerge stronger given that its mortgage problems have led to improved quality controls and loan underwriting procedures.

The long-term trends are positive

Laurentian Bank's revenue and its adjusted EPS have increased steadily over the last 10 full financial years with solid compound annual growth rates of 4.7% and 4.8%, respectively. Additionally, its three-year total shareholders return of 11.46% is higher than the average return of the Big Six banks.

Although non-interest expenses increased in the third quarter of this year, Laurentian Bank's operations have generally become more efficient over the years. Its efficiency ratio (defined as non-interest expenses/revenue) in 2017 was 69.2% versus 80.6% in 2015. It is likely that Laurentian Bank will continue to focus on efficiency, which will help to drive profits in the long run.

Laurentian Bank's dividend yield is almost 6%

With the recent fall in share price, Laurentian Bank's dividend yield has increased to 5.9%. This yield is significantly higher than those currently on offer from the Big Six banks.

Laurentian Bank's dividend policy has typically been friendly to shareholders; the dividend per share has increased every year for the last 10 years at an impressive compound annual growth rate of 7.3%. Current dividends should be very safe since the payout ratio is quite low at only 44%.

Investor takeaway

Laurentian Bank currently has a P/E ratio of eight and a price-to-book ratio of 0.8. These ratios are much lower than the corresponding industry averages and suggest that the stock is likely close to its price floor. Given Laurentian Bank's solid fundamentals, the stock seems like a bargain.

At its current price, Laurentian Bank's stock is a good buy for long-term [value investors](#) who can hold the stock for years and enjoy a great dividend yield while they wait for a price rebound.

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kvassall

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