Which Bank Is Most Exposed to Wealth Management Reform?

Description

For many decades, Canadian investors have gotten a raw deal from their banks. Whether the investor is buying mutual funds, using a financial advisor, or buying individual stocks, the banks have found a way to make outsized profits from these products and services. As a result, most investors have been better off as bank shareholders than bank clients.

To start, bank mutual funds are generally a bad deal for investors. Most of the largest funds just try to track their respective index, and charge a high fee to do so. Financial advisors usually charge a commission for making trades, which creates an incentive to buy and sell stocks too often. And investors who prefer to pick their own stocks have historically been overcharged for making trades.

But that is slowly starting to change. One of the biggest catalysts has been the growth of index funds, which come with much lower fees than their mutual fund counterparts. For example, **TD Bank** offers index funds (called “e-series”) that charge only 0.33% per year.

But which banks are the most exposed to the changing tides? Which ones make the most outsized profits from the status quo? And should bank investors be worried?

CIBC: The most to lose?

It’s a very imperfect science to figure out which bank would be hurt the most by these changes. But that bank appears to be **CIBC** (TSX:CM)(NYSE:CM). While the other banks are aggressively pursuing foreign markets, CIBC has been going back to basics, focusing on Canada. Wealth management, which currently comprises just over 10% of net income, has been cited as a key area for growth.

RBC: The most insulated

Canada's largest bank, **Royal Bank** (TSX:RY)(NYSE:RY) is actually one of the largest wealth managers in the world. But two thirds of RBC's wealth management revenue comes from outside of Canada. The bank also has very large capital markets and retail and commercial banking businesses – like CIBC, barely 10% of RBC's net income comes from wealth management. So it is probably theleast exposed out of all the banks.

Foolish bottom line

It is still far too early to highlight wealth management as one of the banks' biggest risks. There have been many calls for reform before, and after all this time, the status quo reigns supreme. Meanwhile the wealth management businesses at the various banks have been doing just fine – for example, CIBC's wealth management division increased both its net income and return on equity from 2012 to 2013.

But whenever a business overcharges for its services, investors must always remain wary. Because when a company makes outsized profit margins that it may not deserve, those margins can often go in the wrong direction.

CATEGORY

1. Investing

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2. NYSE:RY (Royal Bank of Canada)
3. TSX:CM (Canadian Imperial Bank of Commerce)
4. TSX:RY (Royal Bank of Canada)

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