



Why Canadian Imperial Bank of Commerce Is a Risky Investment

Description

With the Canadian financial services market at the point of over-saturation, there are fewer domestic opportunities for growth in the sector, forcing the Canada's major banks to look elsewhere.

One bank that remains focused on the Canadian domestic market as its major growth lever is **Canadian Imperial Bank of Commerce** ([TSX: CM](#))([NYSE: CM](#)). The bank's over-reliance on the domestic banking market is causing considerable concern among analysts and shareholders.

Fewer growth opportunities

Once seen as a key strength of the bank, particularly after a number of disastrous forays into the U.S., it now leaves the bank dependent upon and vulnerable to any negative developments in the Canadian economy.

While its strategy of focusing on domestic lending, in particular residential mortgages, as a means of growing its bottom line stabilized earnings, a series of setbacks has left the bank particularly vulnerable.

Not only do these things prevent the bank from taking advantage of growth opportunities in other markets including the U.S. and Latin America, but they also leave its earnings and balance sheet vulnerable to a correction in the housing market.

This lack of international exposure is in stark contrast to the **Bank of Montreal** ([TSX: BMO](#))([NYSE: BMO](#)) and **Toronto Dominion Bank** ([TSX: TD](#))([NYSE: TD](#)), which have made successful forays into the U.S.

This is also in contrast to **Bank of Nova Scotia** ([TSX: BNS](#))([NYSE: BNS](#)), which has built a successful presence in a number of emerging economies across the globe, most notably in Colombia and Peru.

Another vulnerability arising from this over-reliance on the domestic market and lack of international exposure is the impact of any slowdown of the domestic economy, especially with Canadians now carrying record levels of personal debt.

This reliance on the domestic market leaves CIBC overexposed to the Canadian consumer and the Canadian housing market. Just over 91% of its total loans under management are located in Canada, while the majority of its deposits also originate in Canada.

While I certainly don't subscribe to the view that Canada will suffer from a subprime-style meltdown in the housing market, there are signs it is overheated and that a correction or slowdown is long overdue.

Furthermore, as Canada's fifth-largest lender it lacks the scale and market presence of the largest lender, **Royal Bank of Canada** ([TSX: RY](#))([NYSE: RY](#)), to maximize growth opportunities. This also prevents it from leveraging from that size to generate further economies of scale and cost savings.

The remaining offshore operations are costing the bank dearly

Even more concerning is that the bank still has a strong presence in the Caribbean; this presence is costing the bank dearly, with the region's economy remaining stagnant because of sluggish business activity and high unemployment.

For the second quarter of 2014, CIBC took an impairment charge of \$543 million against its Caribbean banking business, and I don't expect the performance of that business to improve for the foreseeable future.

The economic outlook for the Caribbean region is poor and this component of CIBC's business, while accounting for less than 5% of its loans under management, accounts for over 50% of its impaired loans. This shows there is considerable pain yet to come with further potential writedowns against its Caribbean banking business.

In comparison to its peers, which have credible offshore operations and/or a significantly greater share of the domestic mortgage market, CIBC appears unappealing and will more than likely see its bottom line shrink further.

CATEGORY

1. Investing

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1. NYSE:CM (Canadian Imperial Bank of Commerce)
2. TSX:BMO (Bank Of Montreal)
3. TSX:BNS (Bank Of Nova Scotia)
4. TSX:CM (Canadian Imperial Bank of Commerce)
5. TSX:RY (Royal Bank of Canada)
6. TSX:TD (The Toronto-Dominion Bank)

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Date

2025/09/14

Date Created

2014/06/05

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