3 Big Bank Dividend Yields to Fuel Your Portfolio

Description

The growing strength of Canada's financial services industry, and especially the top five banks, has proven to be a boon for investors. Not only have the majority of Canada's large banks regularly increased their dividends in recent years on the back of growing and record profits, but they are also well positioned to continue doing so.

Such solid dividend growth, coupled with yields in excess of 3% and the eligibility of their dividends for concessionary tax treatment, makes them a cornerstone investment for any long-term, income-focused portfolio. Let's take a closer look at the three biggest bank dividend yields in the **S&P TSX 60** and see why they should form a core part of every income-focused portfolio.

The sixth-largest Canadian commercial bank pays a tasty dividend yield

One of the best dividend yields paid by Canadian banks isn't found among the top five banks but is instead paid by the sixth-largest domestic commercial bank: **National Bank of Canada** (TSX: NA). This bank pays a dividend yield of 4.1%, and this yield is sustainable when its conservative payout ratio of 37% is considered.

National Bank has established a history of prudent risk management. This, when taken into account with its dominant market share in Quebec and low valuation ratios, including a price of only 11 times earnings, indicates a compelling investment opportunity. The bank also continues to perform strongly, with a fiscal second quarter of 2014 efficiency ratio of 59% and a return on equity of 17%, which with a reported margin of over 2% makes it likely that the bank will continue to hike its dividend over the long term.

The domestic focus of this top five bank continues to pay dividends

It was only a few years back when **Canadian Imperial Bank of Commerce** (TSX: CM)(NYSE: CM) was in the doghouse with investors for its failed and costly foray into the U.S. This venture saw it write down $6.8 billion for investing in a range of toxic debt derivative products that precipitated the global financial crisis and earned the bank a reputation as a "cowboy outfit".

However, significant hard work, a more robust and conservative approach towards risk, and a single-minded focus on its domestic commercial banking operations have seen it become one of the strongest-rated Canadian banks.

While the bank's focus on its domestic operations continues to see it go from strength to strength, with the majority of its net income derived from Canadian retail banking, it is still weighed down by its Caribbean operations. This is a continual risk for the bank and investors alike, with a stagnant regional economy seeing non-performing loans and bad debts rise.

This saw the bank write down $543 million from the value of its Caribbean assets for the fiscal second quarter (calendar first quarter) of 2014. Given the state of the regional economy and growing non-performing loans, further pain is expected for shareholders.

Despite this writedown, CIBC hiked its quarterly dividend by $0.02 per share, or 3%, to $0.96, making it the second-highest-yielding bank in the S&P TSX 60, with a dividend yield of 4% and a very sustainable payout ratio of 45%.

It is also one of the best-capitalized banks in Canada with a Tier 1 capital ratio of 10%. When coupled with an efficiency ratio of 57% and an adjusted return on equity in excess of 20%, this highlights the profitability of its operations despite the issues in the Caribbean, and the likelihood of further dividend hikes.

A conservative offshore growth strategy makes this top five bank an appealing investment

The **Bank of Montreal** (TSX: BMO)(NYSE: BMO) has a dividend yield of 3.9%, which is the second-highest of the top five banks, and when coupled with a conservative payout ratio of 48%, is clearly sustainable. The bank also continues to report stronger net income, with its fiscal second quarter (calendar first quarter) of 2014 net income spiking a healthy 12% compared to the same quarter in 2013.

Much of this can be attributed to the strength of its domestic commercial banking operations, but the bank, like **Toronto Dominion Bank** (TSX: TD)(NYSE: TD), has focused on growing its U.S. retail banking operations. These operations have not performed as strongly as expected despite solid loan and deposit growth due to lower-than-expected margins, but as the U.S. economy continues to improve, the profitability of these operations will also improve.

These things highlight the importance of this growth strategy to the bank and underscore the likelihood of future dividend hikes.

Canada's largest banks continue to be dividend-generating cash machines for investors. It is easy to see why two of the six largest banks have dividend yields of over 4% and are among the top 10 highest dividend yields in the S&P TSX 60. This makes them a core investment for any income-focused share portfolio.

CATEGORY

1. Investing

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5. TSX:NA (National Bank of Canada)
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Author
mattdsmith