Should You Buy Canadian Imperial Bank of Commerce or National Bank of Canada?

Description

There are few industries more profitable and secure than Canadian banking. Competition is low, barriers to entry are high, and as a result returns can be through the roof.

And when looking at Canada's big six banks, two in particular place special emphasis on the domestic market: **Canadian Imperial Bank of Commerce** (TSX: CM)(NYSE: CM) and **National Bank of Canada** (TSX: NA). Are either of these companies right for your portfolio? Below we take a closer look.

The case for CIBC

Throughout its history, CIBC has often been the bank most likely to make a big mistake; it has been dubbed the Canadian bank "most likely to run into a sharp object". For that reason, the bank has dedicated itself to getting back to basics. And that means plain old Canadian banking, which accounted for nearly two-thirds of net income last year. In fact, when counting other lines of business, Canada accounted for 83% of net income in FY2013.

This has led to worries about a lack of growth prospects, and these concerns are not unfounded. The bank has emphasized wealth management as a source of growth, but this will likely require acquisitions, which can be very expensive.

But there is good news: CIBC's share price. Because CIBC has such a meagre growth outlook (and perhaps because of its infamous history), the shares trade at only 12.7 times earnings, below the Canadian bank average. Consequently, the bank also has a very nice dividend yield of 3.8%. So ironically, CIBC is arguably the safest of Canada's big banks, which certainly is a break from history.

The case for National Bank

If you thought 12.7 times earnings sounded cheap, how does 11.9 times earnings sound? Not bad, right? Better yet, National Bank earned 97% of its net income from the cozy Canadian market last year. And since it is much smaller than CIBC, arguably there is more room for growth. Is there a catch?

Well, there are certainly some things to watch out for. For one, last year National earned 63% of its total revenue from Quebec. Secondly, National has the lowest capital ratio of any of the big six banks (although still very good by international standards). Finally, National earned more than a third of income through its Financial Markets segment, which is of course a very volatile and opaque business. This share is easily the highest of any big Canadian bank.

That being said, National has performed very well recently, and its shares have outperformed each of the other banks over the last five years. So it does deserve some credit.

The verdict

If you're looking for a safe pick, or you're looking to bet on the Canadian economy in general, CIBC is definitely the way to go. But if you're looking for something with greater potential, and are willing to take some risk, National Bank is the better option.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:CM (Canadian Imperial Bank of Commerce)
2. TSX:CM (Canadian Imperial Bank of Commerce)
3. TSX:NA (National Bank of Canada)

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Date
2025/09/14
Date Created
2014/09/03
Author
bensinclair