Yet Another Reason to Avoid the Big 5 Banks

Description

Last fall, the big 5 Canadian banks were widely considered to be must-have investments. After all, they were posting record profits, Canada's economy was performing well, and the country's real estate market was still rolling along.

Since then, a lot has changed. The oil rout has highlighted our concerns about the Canadian economy and real estate market. Banks such as **The Bank of Nova Scotia** (TSX:BNS)(NYSE:BNS) have continued to struggle in the Caribbean. **Toronto-Dominion Bank's** new CEO has warned that times will get tougher.

As a result, all five Canadian banks have seen their shares decline over the past five months, despite a nice rebound since the end of January. So with banks trading at cheaper prices, is now the time to invest?

The prices look very good

At this point, the banks are starting to look very cheap. To illustrate this point, let's take a look at a couple of examples.

Canadian Imperial Bank of Commerce (TSX:CM)(NYSE:CM) is the bank most exposed to the Canadian economy, and as a result its shares have not fared well. Since mid-September, its shares are down by more than 10%, the worst result of any big 5 bank over that time stretch.

As a result, its shares trade at about 12 times earnings, not unreasonable at all for such a solid company. To put this in better perspective, CIBC has the eighth highest dividend yield on the **S&P/TSX 60** despite paying out only about half of earnings to shareholders. All of the top seven pay out a much greater share of their earnings (some have no earnings at all).

Or look at The Bank of Nova Scotia, which also trades at 12 times earnings. And like CIBC, its shares come with a nice dividend, yielding about 4%. But unlike CIBC, the bank is not as exposed to the Canadian market, with a third of net income coming from emerging markets. So at first glance, the company's shares appear underpriced.

Yet another headwind

Canada's banks are trading cheaply for a reason. There are some legitimate concerns about low interest rates, low oil prices, and an overinflated real estate market. And on Tuesday, the banks got some even more bad news.

According to *The Globe and Mail*, smaller lenders such as credit unions are fiercely competing for mortgage business by cutting rates. For example, some online brokerages are offering variable rate mortgages under 2%, and five-year fixed mortgages as low as 2.39%. Both figures are well below the rates you can get from the big banks.

Making matters worse, bank customers are more savvy than ever, especially with all the free information available online. So these small lenders will either eat into the big banks' margins, or market share, or both. This is yet another thing to think about before buying the banks.

CATEGORY

1. Bank Stocks
2. Investing

TICKERS GLOBAL

1. NYSE:BNS (The Bank of Nova Scotia)
2. NYSE:CM (Canadian Imperial Bank of Commerce)
3. TSX:BNS (Bank Of Nova Scotia)
4. TSX:CM (Canadian Imperial Bank of Commerce)

Category

1. Bank Stocks
2. Investing

Date
2025/07/22
Date Created
2015/02/18
Author
bensinclair