Should Royal Bank of Canada and Toronto-Dominion Bank Remain Part of Your Dividend Portfolio?

Description

A year ago today, Canadian banks were seen as must-own dividend stocks. Fast forward to today and there are numerous concerns for banks. One is the slumping oil market, which is dragging down our economy. Real estate prices remain high, and any pullback could hurt banks' profits. Making matters worse, household debt in Canada remains at record levels, and low interest rates are cutting into the banks' margins.

So, the banks aren't as popular as they were a year ago, and for good reason. That said, should they still be part of your dividend portfolio? Below we take a look, using **Royal Bank of Canada** (TSX:RY)(NYSE:RY) and **Toronto-Dominion Bank** (TSX:TD)(NYSE:TD) as examples.

History is on their sides

On the surface, both of these stocks seem quite risky. After all, banks were collapsing left and right during the financial crisis, and that was less than 10 years ago. But RBC and TD didn't even cut their dividends. In fact, the two banks have paid dividends reliably for decades. RBC has paid a dividend every quarter since 1870, just a few years after Confederation.

TD has a similar track record. Back in 1970, its dividend totaled just $0.0036 per share (after adjusting for stock splits). Since then, the bank has raised its payout more than 60 times and has never cut it once. Now the dividend equals $0.51.

Think about all that has happened in that time. There have been recessions, real estate crashes (which burned RBC in the early 1990s), a tech bubble burst (which burned TD in the early 2000s), the East Asian crisis, and some very high-profile bankruptcies in Canada. When looking back, today's operating environment doesn't seem so serious.

A very fair deal today

Today RBC and TD yield 3.9% and 3.7%, respectively. At first, these may not seem like big yields. But in today's low interest rate environment, they're not bad, especially compared to bonds.

Even better, these two banks pay out less than half their earnings to shareholders. So, even if the bottom line takes a hit, you shouldn't have to worry about a dividend cut. Instead, you should look forward to many more years of dividend increases.

So, are they worth it?

To answer this question, let's take a look at the alternatives. The **S&P/TSX 60** contains 16 companies that yield more than 4%. Of these, four are banks (i.e. the rest of the big six). Of the remaining 12 companies, only two pay out less than 80% of earnings to shareholders. This leaves very little room for dividend growth.

In fact, some of these dividends may be cut soon, such as those from energy companies. So, if you're a dividend investor and want to avoid the banks, there simply aren't that many alternatives.

CATEGORY

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