



Canadian Western Bank Shares Have Fallen. Is This an Opportunity or a Value Trap?

Description

Banks are an essential part of the economy. Most importantly, they loan money to businesses and families. Businesses lend money to expand their operations or to repay their previous debt at a lower interest. Families would most likely get a loan to buy a home.

Without banks, some businesses would have cash flow problems, in which case, the business would have to halt its operations, which would then have an escalating effect on its suppliers, partners, and customers.

The most compelling opportunity in Canadian banks

When we think of banks, we first think of the Big Five banks. However, the one that has been hit hard lately is **Canadian Western Bank** ([TSX:CWB](#)).

It has been almost a year since Canadian Western hit its 52-week high of \$42. It is now sitting under \$26. Due to low oil prices Canadian Western's price has fallen more than 38% because its main business is in the west. It is presently the most compelling opportunity for investors in the Canadian banks, with a price-to-earnings ratio (P/E) under 10.

The stock is priced at a discount of 35%, assuming it will get back to the \$40 level. However, that won't be any time soon. It wouldn't be until oil prices recover that Canadian Bank will recover.

Earnings staying strong

So far, Canadian Western hasn't shown any deterioration in its earnings. For the first half of the year, its earnings per share (EPS) grew 4%. Since dividends are paid out from earnings, the EPS is the most important metric for income investors to monitor.

Love for dividends

Who doesn't love dividends? You get a regular paycheck for putting your money to work. I love

receiving dividends, and Canadian Western loves paying them, and increasing them, too.

Canadian Western has been paying an increasing dividend for 23 years. That's a longer streak than the Big Five banks, which froze their dividends during the financial crisis. Recently in June, amid low oil prices, Canadian Western continued to grow its dividends. It was an annualized increase of 10%, three times the pace of inflation.

Laurentian Bank of Canada is Canadian Western's closest peer. When compared with Laurentian Bank, Canadian Western's interest coverage is higher and has a lower debt-to-equity ratio.

Canadian Western's dividend is also safer because it has a lower payout ratio of 29% compared with Laurentian's 47%. So, even if Canadian Western's EPS does deteriorate a bit, it will still be able to pay its 3.5% yield.

Should Foolish investors buy today?

As I mentioned before, Canadian Western is cheap today at under \$26. It is priced so cheaply because it is anticipated that some of its loans won't be paid back because of low oil prices, and almost half of its loans are in Alberta and Saskatchewan.

The shares have been holding at the \$25 level since February, but if it breaks through, we might see some downward action for a while. However, long-term investors shouldn't worry. They can add shares in Canadian Western to their portfolios because it is cheap now, and they can add more on the dip.

I would not allocate more than 5% of my portfolio to Canadian Western Bank on purchases, and I won't buy in one lump sum, but I will dollar-cost average into the position.

CATEGORY

1. Bank Stocks
2. Dividend Stocks
3. Investing

TICKERS GLOBAL

1. TSX:CWB (Canadian Western Bank)

Category

1. Bank Stocks
2. Dividend Stocks
3. Investing

Date

2025/08/24

Date Created

2015/07/16

Author

kayng

default watermark