Why Now Is the Time to Add Bank of Nova Scotia to Your Portfolio

Description

Canada's big banks have been incredibly popular with investors in recent years thanks to a string of record profits and ever-increasing dividends. Nonetheless, growing concerns about an overheated Canadian housing market, the impact of a slowing economy, and banks' exposure to a troubled energy patch have seen them fall into disfavour in recent months.

The **S&P/TSX Composite Banks Index** is down by 8% over the last year, and one of the hardest hit is **Bank of Nova Scotia** (TSX:BNS)(NYSE:BNS), which has seen its share price plunge by 16% because of concerns about its exposure to emerging markets. This, however, has created an opportunity for investors seeking exposure to the Canadian bank with the best long-term growth prospects.

Now what?

Bank of Nova Scotia is currently trading with a price of only 1.4 times its book value and nine times its forecast 2016 earnings. While these may appear attractive, they alone do not justify making an investment in stock. It is the quality of the underlying business coupled with its ability to grow earnings that should be the primary consideration, and here Bank of Nova Scotia delivers for investors.

Not only is it operating in an oligopolistic industry that allows it be a price maker rather than a price taker, but the industry is heavily regulated with steep barriers to entry, which shield it from competition.

Investors need to consider that it is the most international of Canada's banks, and while its exposure to emerging markets, particularly in Latin America, is weighing heavily on its share price at this time, it will be a significant tailwind over the longer term.

Those emerging economies are growing at a faster rate than Canada and, once commodity prices bounce back, they will grow even faster.

Colombia, where Bank of Nova Scotia is the fifth-largest bank, reported GDP growth of over 3% in 2015, and this is despite its dependence on oil exports as a key driver of economic growth.

It is also the third-largest bank in Peru, which was one of the fastest-growing economies in Latin

America up until recently. This rapid pace of economic growth should continue once the prices of commodities and metals, on which Peru is particularly dependent, rebound.

Bank of Nova Scotia also has a significant presence in what is considered to be Latin America’s most developed economy, Chile, which will certainly pay dividends once economic growth in the region recovers.

Despite the economic malaise that has engulfed Latin America, the quality of Bank of Nova Scotia’s balance sheet remains high.

Its exposure to the oil and gas industry amounts to only 3.5% of the total value of its loans under management, while exposure to the mining industry is even lower at 1.5%.

Meanwhile, impaired loans remain at about 0.5% of the value of its loans under management, highlighting the quality of its credit portfolio.

It is also worth noting that 49% of its Canadian residential mortgage portfolio is insured, and that of the uninsured portion, the average loan-to-valuation ratio is 53%. This means that even if Canada’s housing market catastrophically collapses, which many international investors are betting on, the impact on Bank of Nova Scotia will be minimal.

So what?

Bank of Nova Scotia is certainly facing its share of headwinds at this time, but of Canada’s banks, it possesses the best long-term growth prospects thanks to its emerging-market exposure. Let’s not forget that patient investors will continue to be rewarded by that sustainable and juicy 5% dividend yield as they wait for the bank’s earnings to grow.

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1. Editor's Choice

TICKERS GLOBAL

1. NYSE:BNS (The Bank of Nova Scotia)
2. TSX:BNS (Bank Of Nova Scotia)

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