



Is Bank of Nova Scotia a Safe Stock to Buy?

Description

At the end of January, ratings agency **Moody's** downgraded **Bank of Nova Scotia** ([TSX:BNS](#))([NYSE:BNS](#)) to a rating of Aa2. Naturally, this worried investors because it meant Moody's must have seen something that was off.

There are a few reasons why I am not concerned about this recent downgrade. First of all, a rating of Aa2 is still incredibly high. Only **Toronto-Dominion Bank** has a higher rating in Canada; therefore, it's not uncommon for banks to have this rating. Further, only 0.6% of companies that had that rating actually defaulted after 10 years.

But why was it given this rating? The primary reason is because Bank of Nova Scotia has been increasing its exposure to auto loans and credit cards. On the one hand, these sorts of credit bring higher returns. But they also come with increased risk, which is what concerned Moody's. Further, the bank has a significant reliance on short-term funding and a lot of exposure to emerging markets. All told, Moody's viewed Bank of Nova Scotia as just a little bit riskier.

The good news is, this isn't that big of a deal. I actually like the fact that Bank of Nova Scotia is bringing on a little more risk. With interest rates continuing to stay low, this has kept the potential income from mortgages low.

Further, exposure to the emerging markets is a key reason to buy the stock. In Latin America, Bank of Nova Scotia is gaining large amounts of market share that would have otherwise been underbanked. Last year, it bought 51% of **Cencosud SA**, Chile's largest retail bank. In Colombia, it is gaining access to 48.3 million people, and in Mexico it is gaining access to 59.79 million people. For context, Canada only has 35.2 million people in total.

Analysts expect that Chile, Colombia, and Peru will experience earnings growth of anywhere from 10-13% over the next five years. While the risk might be a little higher in these emerging markets, the rewards are much greater than for those banks that stick to Canada only.

Over the long term, I expect many of these Latin American countries to experience tremendous growth. While in the short term, investors might feel some volatility, I fully expect the stock to show growth over

the next few years.

The good news for investors is that Bank of Nova Scotia pays a lucrative 5.27% yield, which comes out to \$0.70 per share per quarter. This was after a 6% increase in 2015. All told, I believe that the dividend is safe and secure with its payout ratio right around 48%. All told, a credit rating downgrade is not the end of the world for this bank. I still view it as a safe, long-term buy for those looking to generate income and growth in share price.

CATEGORY

1. Bank Stocks
2. Investing

TICKERS GLOBAL

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

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Author

jaycodon

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