



Should You Buy Canadian Western Bank?

Description

Canadian Western Bank ([TSX:CWB](#)) has been battered in the last year and a half due to its large loan exposure of 41% to Alberta. However, I believe the market should give some credit to the regional bank's strong management team for leading the bank to many years of growth.

Record of outperformance

From 2000 to 2015, Canadian Western Bank's earnings per share (EPS) grew 324% from \$0.62 to \$2.63 at an average annual rate of 10.1%. In the same period, **Royal Bank of Canada's** ([TSX:RY](#))([NYSE:RY](#)) EPS grew 264% at an average annual rate of 9%. Perhaps it's not a fair comparison to compare Canada's largest bank with a much smaller regional bank.

Laurentian Bank of Canada ([TSX:LB](#)) is a fairer comparison because its market cap is closer to Canadian Western Bank's. Laurentian Bank's EPS grew 97% at an average annual rate of 4.6% over the same 15-year period.

From the above comparisons, Canadian Western Bank seems to outperform over the long term. However, in the short term it has underperformed. As oil prices have slid, the bank posted EPS decline of 5% in the 2015 fiscal year that ended in October, while Laurentian Bank posted EPS growth of 6%.

Improvements

Canadian Western Bank understands that it's risky to have a large exposure to Alberta. In March it completed its acquisition of Maxium Financial, which provides loans, equipment leases, and structured financial solutions primarily in Ontario. Although this acquisition contributes negatively to the adjusted EPS this year, it can contribute up to 10% of the bank's net income within five years.

Other than divesting away from Alberta, in the first quarter the bank also focused its efforts away from Alberta. As a result, the bank experienced strong loan growth of 12%, of which two-thirds came from the more economically stable provinces of British Columbia and Ontario.

Dividend

Even when Canadian Western Bank faces hardships, it continues to reward shareholders with a growing dividend. In fact, it remains the third top dividend-growth company in Canada as it has increased its dividend for 24 consecutive years.

It last increased its quarterly dividend in the fourth quarter of 2015 to 23 cents per share, which is 9.5% higher than a year ago. The bank targets a payout ratio of around 30%, while its current payout ratio is 34%.

Conclusion

There's reason Canadian Western Bank's shares are depressed. It experienced 0% EPS growth in the first quarter. However, its medium-term target is to grow its EPS by 7-12%; the median of 9.5% aligns with the average growth rate it has achieved in the past 15 years.

If its earnings-growth target materializes, the bank can trade in the higher multiple range of 13-15. This implies the bank can rise to \$34-39 from \$26 for a 30-50% gain, while it pays a 3.6% dividend yield to shareholders.

If you have an investment horizon of at least three to five years, Canadian Western Bank is a good value dividend investment to consider as it expands outside Alberta and as oil prices stabilize.

CATEGORY

1. Bank Stocks
2. Dividend Stocks
3. Investing

TICKERS GLOBAL

1. NYSE:RY (Royal Bank of Canada)
2. TSX:CWB (Canadian Western Bank)
3. TSX:LB (Laurentian Bank of Canada)
4. TSX:RY (Royal Bank of Canada)

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