The True Cost of Owning Bank Stocks

Description

A relative of mine worked in the healthcare profession for more than 50 years and managed to amass a small fortune. He's now retired. I can remember my well-to-do relative cornering me at a family function to tell me how you can never go wrong with bank stocks.

"They pay a healthy quarterly dividend come rain or shine that just keeps growing year after year. Combine that with a decent amount of capital appreciation," he said, "and you just can't do any better."

I'm paraphrasing, of course, but I can assure you this is a conversation that's taken place in thousands of living rooms, bars, and anywhere else people meet to talk about how things are going in their lives. Banks are a part of our lives.

The problem, as I see it, is that no one ever thinks about the true cost of owning bank stocks.

Like a horse with blinders on, we simply refuse to see the soft underbelly of an industry that's hell bent on taking your hard-earned dollars in an unsuspecting manner, so you continue to use their products and services while also investing in their businesses.

In a way, it's the ultimate Ponzi scheme. Some might go as far as to say that banks are trying to suck and blow at the same time. If this offends you because you are a banker or are friends with a banker, I apologize. The thing is, every investment comes with a string attached. It just so happens that banks have a very long one.

If you'd invested $10,000 a decade ago in the **iShares S&P/TSX Capped Financials Index ETF** (TSX:XFN), you would have $18,249 as of June 15, an annualized total return of 6.2%. That's not bad compared to what you would have received from five-year GICs over the same period. In your best years (2006-2007), you might have gotten a whopping 3.3% for your troubles.

The banks, I can hear my relative reminding me, would have covered that GIC payout with just the annual dividend, leaving investors with the capital appreciation as gravy. Sounds like a pretty good deal. Except, consider how much of that dividend is paid from the ever-increasing fees Canadians are handing over to banks on an annual basis. It's a big chunk.

Recently, Duff Conacher, co-founder of Democracy Watch, an Ottawa-based non-profit dedicated to making governments and corporations more accountable, discussed with *CBC* the concerns his group has with bank fees. "There needs to be an independent audit of every division of the banks to determine whether there's gouging," Conacher said. "And if there's gouging, it should be publicized."

Gouging. Of course, there's gouging.

The banks argue that increased competition and the cost of implementing online banking are the biggest reasons fees are moving higher. But should that be *your* problem? Competition is part of business. If you can't stand the heat, get out of the kitchen. As for online banking, it was either implement it or die. Again, not my problem.

A quick look at the 2015 **Royal Bank of Canada** (TSX:RY)(NYSE:RY) annual report reveals 36 instances of the word "fees" in the 209-page document. In the income statement, fees are mentioned four times to the tune of $7.8 billion, and that doesn't include the many ancillary charges covered under commissions, etc.

Care to guess how much Royal Bank paid out in dividends in 2015? $4.6 billion.

If you bank with Royal Bank and own its stock, it's important that you're mindful of the fact that your relationship with the bank and the fees paid to maintain that relationship more than covered the dividends you got back from your investment in Royal Bank stock in 2015. I'm not picking on Royal Bank. Go through every annual report of the Big Six and you'll see the same thing.

Now, one might consider this a cashback situation where the fees you pay are lower because of the dividends you receive, and if that's the case, so be it. But just remember—the true cost of owning bank stocks is a lot greater than most Canadians realize.

CATEGORY

1. Bank Stocks

TICKERS GLOBAL

1. NYSE:RY (Royal Bank of Canada)
2. TSX:RY (Royal Bank of Canada)
3. TSX:XFN (iShares S&P/TSX Capped Financials Index ETF)

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Author
washworth