

## 3 Reasons Why Canadian Western Bank Isn't as Risky as Investors Believe

### Description

**Canadian Western Bank** ([TSX:CWB](#)) has suffered badly since the slump in oil began. Not only has its focus on western Canada left it heavily exposed to the economic fallout from the prolonged slump in crude, but there are fears that it's overly exposed to Vancouver's frothy housing market.

Despite these factors and the risks that they pose, it is becoming increasingly clear that the bank's position isn't as bad as some investors believe.

### Now what?

Firstly, Canadian Western's direct exposure to crude is relatively small.

One of the biggest misnomers is that because of its focus on Alberta, Canadian Western was aggressively lending to energy companies in the lead-up to the collapse in crude.

This couldn't be further from the truth.

By the end of the second quarter 2016, its direct exposure to the oil and gas industry amounted to only \$327 million, or 2% of its total loans under management. This is at the lower end of the range for Canadian banks. **Bank of Nova Scotia**, **National Bank of Canada**, and **Canadian Imperial Bank of Commerce** all have greater proportional exposure. It is also the smallest exposure to any single sector in its loan book, in which commercial mortgages and general commercial loans have the greatest value.

Secondly, Canada's frothy housing market poses little risk.

Another misnomer being thrown around by some market pundits is that Canadian Western has considerable exposure to the scorching hot housing market of Vancouver.

However, its total mortgage book is quite small—valued at \$2.8 billion, or just 13% of its total loans under management. Then consider that the total value of mortgages issued in British Columbia amount to only \$74 million—a mere 4% of total loans under management.

Even after assuming that the majority of these mortgages have been issued in Vancouver, which is logical considering it is one of Canada's largest mortgage markets, these relatively small numbers mean that impact of a housing meltdown in Vancouver will be minimal. The fallout would be further minimized by Canadian Western's conservative approach to credit risk; 10% of all mortgages are insured, and those that are uninsured have an average loan-to-valuation ratio of 70%.

Finally, the bank is reducing its dependence on western Canada.

One of the greatest risks facing Canadian Western has been its focus on western Canada, which leaves it exposed to the gyrations of the oil price and the fortunes of the energy patch. This means that its growth opportunities are limited because Alberta is caught in its longest running economic slump

since the 80s.

However, the bank's acquisition of Maxium Financial as well as **GE Capital's** Canadian Franchise Finance business has further diversified its loan book and expanded its footprint in eastern Canada. This not only reduces its dependence on the energy patch, but also enhances Canadian Western's growth prospects and will eventually give its bottom line a healthy bump.

### **So what?**

It is easy to understand why the bank has fallen into disfavour with investors because of its disproportionate exposure to the energy patch and western Canada.

However, the bank's position isn't as risky as many investors believe. It has relatively low direct exposure to energy loans and the frothy housing market of Vancouver. The bank has also taken strides to reduce its dependence on western Canada, which should give its earnings a healthy boost over time.

These factors along with its attractive valuation metrics, including a share price of just over one times its book value, make it an interesting play on a recovery in crude and the health of Canada's economy.

### **CATEGORY**

1. Bank Stocks
2. Investing

### **TICKERS GLOBAL**

1. TSX:CWB (Canadian Western Bank)

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