Bank of Nova Scotia Offers the Best Growth Potential of Canada's Banks

Description

Fears over the health of Canada's economy and that an epic housing bust is on its way have caused investors to shun Canada's banks of late. Many analysts are speculating that the strong growth and relatively easy earnings growth enjoyed by the Big Six in recent years may be drawing to a close with leaner times ahead.

Regardless of these near-term worries, there are signs that over the long term Canada's banks will continue to perform strongly. One that stands out as having the greatest potential to unlock value for investors and deliver solid growth is **Bank of Nova Scotia** (TSX:BNS)(NYSE:BNS).

Now what?

As I am certain many investors are aware, Bank of Nova Scotia is Canada's most international bank and has considerable exposure to a number of emerging markets.

After bolstering its presence in Latin America, particularly Chile, Colombia, Peru, and Mexico, through a series of acquisitions in recent years, the bank now earns almost a third of its net income from its international operations. This means that not only is it less reliant on Canada to generate a considerable portion of its earnings, but it is well positioned to benefit from the higher rates of economic growth that emerging markets typically experience.

You only need to turn to Peru or Colombia, where it is the third- and fifth-largest bank, respectively, to see this. Despite being impacted by the slump in commodities, both economies are still experiencing growth. For 2016, analysts expect that Colombia's GDP will expand by 2.2%, even after allowing for the fallout from the prolonged slump in crude; analysts have forecast that Peru's GDP for the year will grow by an impressive 3.6%.

These growth rates are well in excess of the 1.1% that the Bank of Canada anticipates for Canada.

The recent rebound in metals, especially copper, will bolster economic growth in Chile and Peru, where it is the top export. This will stimulate demand for credit, which will be particularly profitable for Bank of Nova Scotia’s consumer lending portfolio in Chile, where it is the third-largest provider of credit cards.

Such strong economic growth in Latin America is already having a positive effect on its regional loan book. For the third quarter 2016, regional loans grew by an impressive 13%, causing lending revenue to surge by the same amount compared with a year earlier.

Furthermore, Bank of Nova Scotia’s net interest margin in the region is just over double that which it can generate in Canada, highlighting the profitability of its Latin American operations.

Other important growth divers for its Latin American businesses will be the region’s young population, growing wealth, and a rapidly expanding middle class, which will drive greater demand for banking and financial services in countries that are underbanked.

So what?

It is easy to understand the concerns that analysts have for the outlook for Canada’s banks, but what is increasingly clear is that Bank of Nova Scotia’s Latin American strategy will pay considerable dividends.

Over the last year alone, net earnings from the region have grown from a seventh of its total net income to now represent a roughly a fifth. This growth will continue for the reasons discussed, reducing Bank of Nova Scotia’s dependence on Canada and enhancing its bottom line.

While investors wait for this to translate into a healthy bump in its share price, they will be rewarded by the regular dividend which now yields a tasty 4%.

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