How to Benefit From the Rally in the Best Canadian Dividend Stocks

Description

Canadian banks are the best dividend stocks available for income investors.

The top five financial institutions in Canada benefit from their strong local franchises and a growing global presence. These banks not only dominate the local banking market, but they also maintain a leading presence in the U.S. and other jurisdictions.

Toronto-Dominion Bank (TSX:TD)(NYSE:TD), for example, has become the eighth-biggest U.S. retail bank by assets through its aggressive acquisitions and investments to expand its branch network.

Bank of Nova Scotia (TSX:BNS)(NYSE:BNS) has established a strong presence in Latin America. The lender is benefiting from its aggressive growth strategy in the Pacific Alliance, a Latin American trade bloc comprising Mexico, Peru, Chile, and Colombia.

For long-term income investors, it makes a perfect sense to hold a couple of top banks in their portfolios to earn stable dividend income and capital gains.

And the timing is favourable, as the banking stocks in Canada are emerging just fine from short-selling pressure.

Shorting Canadian banking stocks was a popular trade early this year, as many hedge funds predicted a U.S.-style collapse of the domestic real estate after its decade-long boom and its contagion impact on banks that are heavily exposed to the housing market through their mortgage portfolios.

But after realizing that the Canadian market is different from the U.S., these hedge funds started to unwind their short positions, producing a powerful rally in the banking stocks for the past three months.

Rally in bank stocks continues

During the past three months, Canadian banks have largely been the main contributor in the S&P/TSX Composite Index gains. The shares of Big Five banks have gained in the range of 5-14%, led by TD and Bank of Nova Scotia.

This relief rally started after investors realized that a worst-case scenario in the Canadian housing market crashes would not play out following the government intervention which deflated the housing bubble.

Now that the economy is showing signs of strength, and the Bank of Canada has started raising interest rates, these lenders are well positioned to provide growth and stable dividend income.

Which banking stocks offer better value?

A simple formula that works for income investors willing to take a long position in the Canadian banking stocks is to buy the ones that are lagging behind. In this case, **Canadian Imperial Bank of Commerce** (TSX:CM)(NYSE:CM) and **Bank of Montreal** (TSX:BMO)(NYSE:BMO) are two lenders which offer the best value and have more room to grow after recent gains.

These lenders distribute 40-50% of their income in dividends and have solid track records of growing these payouts.

If you are thinking of adding Canadian banking stocks in your portfolio, keep these two names in your shopping list.

CATEGORY

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TICKERS GLOBAL

1. NYSE:BMO (Bank of Montreal)
2. NYSE:BNS (The Bank of Nova Scotia)
3. NYSE:CM (Canadian Imperial Bank of Commerce)
4. NYSE:TD (The Toronto-Dominion Bank)
5. TSX:BMO (Bank Of Montreal)
6. TSX:BNS (Bank Of Nova Scotia)
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