Why Canadian Imperial Bank of Commerce Will Surprise Analysts in 2018

Description

I don't know what it is — maybe its the bank's red and gold colour scheme — but **Canadian Imperial Bank of Commerce** (TSX:CM)(NYSE:CM) just can't capture the favour of analysts.

Bank of Nova Scotia (TSX:BNS)(NYSE:BNS) analyst Sumit Malhotra recently upped his 12-month price targets for eight different Canadian banks, including CIBC.

However, of the Big Five, Malhotra gives "sector outperform" ratings to just three of them. **Bank of Montreal** (TSX:BMO)(NYSE:BMO), BNS (his bank), and **Toronto-Dominion Bank** (TSX:TD)(NYSE:TD), with **Royal Bank of Canada** (TSX:RY)(NYSE:RY) and CIBC getting the less desirable "sector perform" rating.

That's the analysts' equivalent of not getting asked to dance at your high school prom.

Forget Toronto and Vancouver

If you read into Malhotra's comments about the banks, I have a hard time understanding why analysts are so afraid of CIBC.

Yes, I know, CIBC has more uninsured mortgages in Toronto and Vancouver than any other bank. But as I said in early November, its delinquency rates in Toronto and Vancouver are lower than those of mortgage clients in the rest of the country.

CIBC isn't worried about its Toronto and Vancouver mortgage markets, and neither am I.

The real concern for all banks should be what's happening outside these two markets. Toronto and Vancouver will always be able to attract affluent customers who can pay their mortgages. Beyond these two cities, the state of the economy plays a huge factor in whether banks win or lose.

The analysts' rationale

Getting back to Malhotra, his recent comments about the banks are telling.

“Canadian bank stocks enter Q4/17 reporting season trading at 12.2 times our 2018 estimate, 11.4 times our 2019 estimate, 1.99 times last reported BVPS [book value per share], and offering an average yield of 3.63%,” the analyst said in a research note to clients. “In other words, though valuation has moved higher over the past year, it certainly has not been the biggest part of the story, as both EPS growth (12% year over year thus far in 2017) and ROE [return on equity] expansion (15.7% year to date) have reflected a very strong fundamental year.”

How has CIBC fared in all of this?

Metric	CIBC	Average
2018 estimate	10.5x	12.2x
2019 estimate	9.8x	11.4x
P/BVPS	1.78x	1.84x
Yield	4.5%	3.9%
EPS growth	8.8%	12.0%
ROE growth	-3.7%	15.7%

What’s it all mean?

If you’re not a fan of CIBC, the first thing you’re going to notice are the bottom two numbers. EPS growth is 27% lower than the average of its peers, and ROE growth receded year over year by 3.7% to 18.4% compared to 19.1% for the same nine months in 2016.

Both are relatively easy to explain.

In 2016, CIBC sold its holding in American Century Investments, which that led to a $443 million gain. Otherwise, its Canadian wealth management division would have seen an increase in its ROE rather than a decrease.

As for the decrease in its U.S. commercial banking and wealth management ROE, that has to do with the addition of PrivateBancorp, which increased the equity of the segment with only 39 days of revenue and income between the June 23 closing date and the end of the third quarter. As the acquisition approaches the one-year anniversary, that number should turn positive.

This time next year, CIBC's overall ROE should be growing once more.

As for EPS growth, it lagged its peers as a result of expenses related to the PrivateBancorp acquisition and other strategic initiatives. It too should meet or exceed its peers in 2018 and beyond.

Looking forward to 2018

Fool contributor Joey Frenette recently suggested that investors should be greedy when others are fearful when it comes to CIBC stock. In his opinion, CIBC's lower valuation is partially a result of the perception that the bank is overexposed to Toronto and Vancouver real estate.

I couldn't agree more. Like Frenette, I see good things happening for CIBC and its share price in 2018.

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