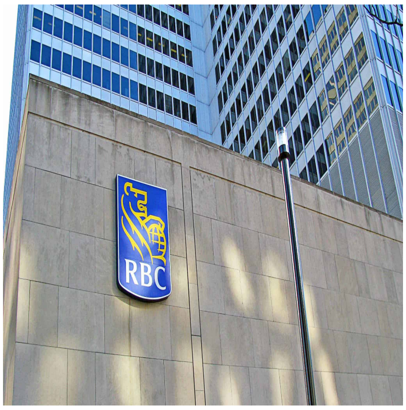

Royal Bank of Canada: Is Further Growth on the Horizon?

Description

There are few things discussed as much as the possibility that there is a housing bubble brewing in Canada, just waiting to burst. Although it's been a decade since the Financial Crisis, investors still remember what happened to banks — in particular, when the market imploded.

But if you're an investor in **Royal Bank of Canada** (TSX:RY)(NYSE:RY), I wouldn't start running for the doors simply because of fear of a housing crisis. I think the concerns are overblown. It's true that the housing market is hot, but I don't see an implosion on the horizon. Rather, I expect to see the housing market slowly cool down — a soft-landing of sorts.

In the meantime, though, the company is executing flawlessly. In Q4, the personal and commercial banking unit delivered a $359 million increase in earnings. Factor in the sale of Moneris, which it earned $212 million on, and earnings were up 11%. Wealth management saw a 25% increase in earnings. And finally, capital markets saw an 11% increase in earnings.

In total, net income came in at $2.837 billion, up 12% from Q4 2016. Its diluted earnings per share of $1.88 were up 14%. And finally, its return on equity (an important factor when analyzing banking stocks) was up 110 basis points.

The reality is, the bank did an incredible job generating strong returns on the quarter.

I am bullish looking forward, because the bank is increasing interest rates following the central bank's recent hikes. By increasing the spread between what it pays savers and what it charges borrowers, Royal Bank of Canada is in a strong position to continue generating stronger returns on equity and earnings.

It's not all bullish sentiment, though. The government has released new mortgage rules for banks. Effectively, the rules stipulate that the bank cannot lend to anyone who wouldn't be able to pay back the mortgage if interest rates increased by 2%. This rule effectively limits who the bank can lend to, which is frustrating because the clients could otherwise be perfect candidates. Alternative lenders are likely to benefit from these rules.

Nevertheless, I would still consider buying shares of the bank for two reasons. First, they trade at a reasonable multiple of earnings compared to some other more speculative growth stocks on the market. That means there could be even more upside but, just as likely, a limitation in the potential downside.

The second reason is because Royal Bank of Canada is a really solid dividend stock. When the bank announced strong Q3 earnings, it also increased the dividend by $0.04, or 5%, to $0.91. With where the price of the stock is now, investors can benefit from a 3.43% yield on investment.

One possible trade here could be to wait for a pullback until the yield is trading closer to 4%. That would increase your overall cash flow and, if you reinvest the dividends, compound your growth. But trying to time the market is always tricky, and it might be better to get the stock now versus waiting for it to appreciate another 5%.

Royal Bank of Canada is a solid investment. I believe you should be looking at it. I also think there are other incredible opportunities available if concerns about the housing market are bothering you.

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