



Income Investors: Regional Canadian Banks Have Bigger Dividend Yields, But Are They Better Buys?

Description

It's hard to go wrong with any one of Canada's Big Six bank stocks, the largest Canadian banks by market cap. They offer a large upfront dividend yields, above-average dividend growth, and the potential for market-beating capital gains. While most investors may look no further than the Big Six, some of the hungrier income investors out there may look to Canada's smaller regional banks for a little extra yield.

For the income oriented, that extra yield makes all the difference. It's essentially an instant raise, but there's always a catch, usually in the form of a higher degree of risk taken on. As you may know, Canada's Big Six banks are geographically diversified, eliminating the dreaded "single source of failure" that many investors fear may bring about liquidity issues.

Most notably, Canada's frothy housing market is seen as this single source of failure for the banks that are domestically overexposed. Unfortunately, with Canada's regional banks, you're not only domestically overexposed at the national level, but you're taking it a step further by being exposed at the provincial level.

Consider **Laurentian Bank of Canada** ([TSX:LB](#)) and **Canadian Western Bank** ([TSX:CWB](#)), two regional Canadian banks that provide investors with exposure to the Quebec and Western Canadian (B.C. and Alberta) markets, respectively.

While I'm not a fan of the regional banks for the lower amount of diversification they offer investors, I believe that if the valuation is right, such banks can serve as a terrific complement to an already diversified portfolio. As fellow Fool [Chris MacDonald once said](#), "At some price, every company becomes a buy — even those with seemingly nothing going for it."

I've expressed my distaste for Quebec-based bank Laurentian in many prior pieces, but more recently, I [pounded the table on the stock](#) as shares dropped to their lowest levels in recent memory. Just over a month ago, a few days before the markets bottomed, I rung the alarm on the stock, noting that the stock had its highest dividend yield ever and that the stock was unsustainably undervalued and

overdue for an upside correction, despite the “mini mortgage crisis” that was unique to Laurentian.

Indeed, Laurentian was dirt cheap, even considering the baggage that came with the sub-optimal bank. Shares of Laurentian were trading at 7.3 forward earnings, which I thought was an incredible value for those on the hunt for a safe 7% yield.

Unfortunately, the fire-sale on Laurentian didn't last long, and after a 19% rally in a month, the stock now has a 5.9% yield, which is more in line with historical averages. Simply put, if you didn't act at a time of maximum panic, you missed out on an opportunity to lock in a stock that had a market value that was substantially lower than its intrinsic value. While Laurentian is still cheap today (at 8.6 times trailing earnings), the stock is now fairly valued at best and is no longer worthy of pounding the table.

Canadian Western Bank was in a similar predicament just over a month ago, and today, with a weak dividend that pales in comparison to the Big Six, the stock is a major pass in favour of Laurentian or any of the Big Six.

Foolish takeaway

It's easy to shun the regional banks, as they're not one-stop-shop financial holdings that are worthy of a core position in a portfolio. If the price is right, however, income investors may find it worthwhile to keep the regional banks on their radar should their prices ever drop enough to warrant bottom fishing.

At this juncture, I prefer the Big Six over Laurentian or Canadian Western, but if you're keen on the regional banks, I'd go with Laurentian, as the near-6% yield is still pretty enticing from the viewpoint of an income investor.

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