



## 1 Top Bank Stock Yielding +4% That Belongs in Every TFSA

### Description

Canada's big banks continue to attract the attention of short sellers with the five most shorted stocks on the TSX being filled by the Canada's largest banks. This considerable interest in shorting the major banks has been ongoing for almost a decade despite them being among the best and most reliable large-cap growth stocks since the end of the global financial crisis. While many of the concerns that have sparked this negative interest could derail the growth prospects of the more domestically focused Canadian banks, it has created an attractive opportunity to acquire **Bank of Nova Scotia** ([TSX:BNS](#))([NYSE:BNS](#)).

### Weak results

Scotiabank has lost 7% over the last year after reporting some disappointing fiscal first quarter 2019 results. Net income declined by 4% year over year to \$2.2 billion because of a sharp decline in non-interest income, rising expenses and a marked increase in provisions for credit losses. The decrease in income from non-lending activities can be attributed to lower trading revenues and advisory fees due to a decline in business for Scotiabank's Global Banking and Markets Division.

Meanwhile, lending loss provisions rose by a worrying 26% year over year to \$688 million because of a sharp uptick in defaults, problematic retail and commercial loans. These events appear to lend credence to the theories espoused by short sellers that focus on weaker than expected economy, cooling housing markets and heavily leveraged households triggering a nasty uptick in credit losses.

Short sellers believe those factors, when coupled with the domestic banks' considerable exposure to Canadian residential mortgages, which make up 36% of Scotiabank's loan book, will have a nasty impact on balance sheet quality and earnings, causing their stock to crash.

While there are certainly headwinds ahead for Scotiabank and the other big five, they are not as severe as those short sellers believe.

## Low risk of a housing collapse

Many short sellers are U.S. hedge funds, which are convinced that Canada's [housing market](#) resembles that which existed in the U.S. in the run-up to the 2006 housing collapse. This demonstrates a fundamental misunderstanding of the domestic housing and banking markets. Unlike in the lead-up to the U.S. housing meltdown, tougher [prudential regulations](#) mean that subprime loans make up a very small proportion of total mortgages. There is also substantially lower risk of contagion because Canada's banks have not bundled up their mortgages as income-producing derivatives and sold them to other financial institutions as occurred with U.S. subprime loans.

Even if there is a marked uptick in loan defaults, the banks are backstopped by mortgage insurance, which will cover the cost of payments until borrowers can meet their financial obligations or the loan can be restructured. This substantially reduces the need for banks to repossess properties and place them on the market at fire sale prices to recoup their losses at a time when the housing market is in distress, which caused prices to cascade ever lower at a rapid rate.

Scotiabank is better positioned than the other major banks to weather any impending headwinds, as it has significantly invested in expanding its international footprint through acquisitions in Latin America. This sees its international business focused on the nations of Mexico, Colombia, Peru and Chile, which form an economic block known as the Pacific Alliance.

It was the bank's operations in those countries that will act as a growth motor, offsetting any slowdown in its Canadian retail banking business.

Scotiabank's international business was responsible for generating 40% of its first quarter 2019 net income, which was underpinned by a 44% increase in loans for its Pacific Alliance operations, triggering a healthy 31% increase in revenue. This notable performance will continue with Colombia, Chile and Peru all expected to experience annual GDP growth of over 3% from 2019 through to 2023.

## Why buy Scotiabank?

Such strong growth combined with a superior net interest margin because of higher headline interest rates in those countries and steadily falling costs will offset the softness anticipated in Canada's saturated mortgage market.

While investors wait for this to boost Scotiabank's stock, they will be rewarded by its sustainable dividend yielding a tasty 5%. Long-term investors, especially those holding the stock in a TFSA, can access the power of compounding by reinvesting those payments through Scotiabank's dividend reinvestment plan.

If investors had reinvested the dividends received from Scotiabank over the last ten years, they would have earned a total return of 213% compared to 193% if they weren't reinvested. This highlights the magic of compounding, a powerful tool for building wealth over the long-term, particularly in a TFSA.

### CATEGORY

1. Bank Stocks

2. Dividend Stocks
3. Investing

## **TICKERS GLOBAL**

1. NYSE:BNS (The Bank of Nova Scotia)
2. TSX:BNS (Bank Of Nova Scotia)

## **PARTNER-FEEDS**

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