Get Emerging Markets Exposure and a 5% Yield With Bank of Nova Scotia (TSX:BNS)

Description

Canada's banks have been taking a pounding with a renewed round of short-selling by U.S. hedge funds weighing on their market performance. Fears of a housing slowdown, financially stretched households, a large quantity of low-quality mortgages, weaker economic growth, and the normalization of the credit cycle has seen short-sellers target the Big Five banks. While there are headwinds ahead for the major banks, the outlook is not as poor as those short-sellers believe. One Big Five bank that is well positioned to dodge the fallout from those headwinds is **Bank of Nova Scotia** (TSX:BNS)(NYSE:BNS).

Solid emerging markets exposure

Unlike its peers, the bank elected to focus on expanding its international operational footprint by investing in building its businesses in Mexico, Colombia, Peru, and Chile. This strategy is not only paying considerable dividends for Scotiabank but also mitigates many of the headwinds facing Canada's banks.

While first-quarter 2019 net income declined by 4% year over year to $2.2 billion because of a flat performance from Scotiabank's Canadian banking business and poor results for global banking, Scotiabank's International division was firing on all cylinders. Net interest income soared by 22% year over year to just over $2 billion, and reported net income shot up by a very impressive 23% to $893 million to be responsible for 40% of Scotiabank's consolidated net income of $2.2 billion.

It was strong deposit and loan growth in Latin America, notably the Pacific Alliance nations of Mexico, Colombia, Peru, and Chile, that was responsible for this notable increase in net income forScotiabank's international business. Loans in the Pacific Alliance, even after including the impact ofScotiabank's latest acquisitions in Chile and Colombia, surged by a whopping 44% year over year,while overall loan growth for the division was a healthy 29%. This impressive performance can beattributed to the economies of Colombia, Chile, and Peru returning to growth after falling into deepslumps from 2015 through to 2017, primarily because of weaker oil and metals prices.

For 2018, Colombia's gross domestic product (GDP) expanded by 2.7% year over year, while for Peru and Chile GDP grew by an impressive 4%. Those figures are significantly greater than the 1.8% reported for Canada. The IMF anticipates that strong economic growth will continue during 2019 and into 2020. This year alone Colombia's GDP is forecast to increase by 3.5%, and if oil continues to rally, it could be even greater, whereas for Peru and Chile it will expand by 3.9% and 3.4%, respectively.

That bodes well for stronger loan and deposit growth for Scotiabank's operations in the region because there is a direct correlation between economic growth and greater demand for credit as well as other financial services. This will help to offset the impact of lower growth in Canada, where the IMF has forecast that GDP will expand by a mere 1.5%.

Those robust growth prospects in Latin America are enhanced by the fact that many countries in the region, including Colombia, are underbanked and have young briskly growing populations coupled with a rapidly expanding middle class, leading to significantly greater demand for credit and wealth management products.

Why buy Scotiabank?

Management's focus on simplifying and de-risking Scotiabank's operations across the board will unlock further efficiencies, reduce costs, and enhance its growth profile, leading to improved profitability as well as earnings. For these reasons and the fact that Scotiabank has trailed behind its peers, gaining a paltry 7% since the start of 2019, there is considerable upside ahead for investors. While they wait for the bank's stock to appreciate, they will be rewarded by its steadily growing dividend, which has a juicy yield of almost 5% and, with a payout ratio of around 50%, appears quite sustainable.

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