Why You Should Ignore the Buy Signal for This Top Canadian Bank Stock

Description

On April 1, **Canadian Imperial Bank of Commerce** (TSX:CM)(NYSE:CM) set off a buy signal. At the time, I'd recommended investors pull the trigger and add CIBC at a discount. CIBC stock rebounded nicely into early May, but negative investor sentiment re-emerged ahead of its second-quarter earnings release.

This negative sentiment was not entirely unjustified. Not only had CIBC become a named target of famed short-seller Steve Eisman, but the trouble in its mortgage loan portfolio was a lingering concern. Several top housing markets in Canada have experienced more balanced conditions in 2018 and early 2019, but sales are still down dramatically from the prior year. This increased pressure has motivated real estate industry boosters to lobby for an end to the mortgage stress test, at least for uninsured buyers.

It is unclear whether the federal government will budge on this point. Evan Siddall, the head of the CMHC, recently said that the stress test is needed to "protect the economy." The problems created by a slowdown are nothing compared to the consequences that could emerge from the collapse of a real estate asset bubble. The International Monetary Fund (IMF) has also urged Canada to keep the stress test in place.

CIBC released its second-quarter 2019 results before markets opened on May 22. Adjusted net income attributable to shareholders came in at $2.97 per share, which missed analyst expectations. However, adjusted net income was still up 1% from the prior year. As expected, CIBC's Capital Markets segment enjoyed a significant bounce back compared to a lacklustre first quarter. Net income in this segment climbed 12% year over year to $279 million.

Canadian Personal and Small Business Banking reported net income of $570 million, which was down 2% from the prior year. Higher revenue was offset by higher expenses and provision for credit losses. Net income in U.S. Commercial Banking and Wealth Management increased 18% year over year to $163 million. This was primarily due to higher revenue.

As expected, CIBC reported struggles in its mortgage portfolio. CIBC very recently boasted the strongest mortgage growth out of its peers, but cooling market conditions have changed that. In this quarter, CIBC reported a 0.9% drop in residential mortgage lending. This is especially damaging, as CIBC draws a greater proportion of its earnings from personal banking compared to its peers.

CIBC is facing additional challenges because it has focused on residential real estate lending in large urban markets. It put a focus on the Greater Toronto Area and Greater Vancouver. Both areas have experienced a dramatic decline in sales since the institution of a foreign buyers' tax, new regulations, and the stress test.

CIBC stock is now nearing 52-week lows. The stock has dropped 5.6% week over week as of close on May 23.

Its forward P/E of eight looks good on its value relative to its competitors, but its reliance on the housing market is a growing concern. Shares had an RSI of 26 as of close on May 23, which puts it in technically oversold territory. Investors should ignore the signal for now, but if CIBC's stock falls below triple digits, it will be hard to ignore as a value add.

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