A Cheap Stock With a 5% Yield and Big Upside Potential

Description

Dividend investors often have to pay a premium to buy stocks with reliable and attractive distributions, but the market sometimes serves up a few deals that can lead to nice capital gains down the road.

Let's take a look at one company that pays a growing dividend and appears oversold right now.

Bank of Nova Scotia

Bank of Nova Scotia (TSX:BNS)(NYSE:BNS) is an interesting player in the Canadian banking sector.

Similar to its larger peers, the bank gets the bulk of its profits from the Canadian operations, but it differs in a way that could see it outperform the others in the long term. The company is betting big on emerging-market growth, with a specific focus on Mexico, Peru, Colombia, and Chile. This might seem like an odd and risky market for an old Canadian bank, but there is method to the perceived madness.

The four countries represent the core of the Pacific Alliance trade bloc that was set up to enable the free movement of goods, capital, and labour among the members. The countries have historically experienced difficult times with bouts of economic and political instability, but recent years have been more stable, and Bank of Nova Scotia sees the growth potential in the roughly 230 million people that are relatively underbanked.

Companies that do business in these countries also need banking services, and Bank of Nova Scotia is positioned well to help businesses with inter-country expansion, as well as provide assistance to international firms.

Bank of Nova Scotia raised its dividend earlier this year and is very profitable. The current payout provides a yield of 5%. The international division already contributes about 30% of total profits, providing a nice hedge against any potential downturn in Canada.

Growth continues through acquisitions in Latin America and Canada. Last year, Bank of Nova Scotia spent billions of dollars on three big deals. One doubled its market share in Chile to about 15%. The other two saw Bank of Nova Scotia beef up its wealth management operations at home.

Risks

Bank of Nova Scotia trades at less than $70 per share today compared to $84 in late 2017. The flurry of deals might be part of the reason for the pullback. Investors might be wondering if the bank has bitten off more than it can chew from an integration perspective, and only time will tell if the new investments deliver the expected returns.

Mexico, Colombia, Chile, and Peru might be more stable politically and economically than they were 20 years ago, but they are still emerging markets with ongoing challenges, which must be considered when evaluating the stock.

Should you buy?

Bank of Nova Scotia trades at 10.3 times earnings. That's pretty cheap for a company that's very profitable and isn't facing an imminent financial crisis at home or in the international operations. The stock offers strong upside potential on an improvement in sentiment, and you get paid well while you wait.

If you have some extra cash on the sidelines, Bank of Nova Scotia might be a good bet today for a buy-and-hold portfolio.

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