Should You Buy Bank Stocks Before a Canadian Rate Cut?

Description

Stock market analysts are divided as to whether the Bank of Canada will continue to hold fast to its strategy of static rates. On the “no cut” side, the Canadian dollar is strong against the American counterpart, while our central bank has shown no signs of making a rate cut.

However, the possibility that a surprise cut could come at the end of October isn’t off the cards, while the U.S. Federal Reserve is under pressure to make another swing of the scythe.

Trends are changing south of the border

Bank stocks tend to perform well during periods of monetary easing, with investors enjoying subsequent gains. For instance, when the Fed has cut rates in the past, bank stocks have usually fared well.

However, that wasn’t the case the last time around and might not hold if a further, deeper cut is made, either. So, how might Canadian bank stocks fare if the Bank of Canada follows numerous international lenders and cuts the interest rate?

Investor sentiment is currently fairly bullish on banks. For instance, **TD Bank** (TSX:TD)(NYSE:TD) was up at the start of the week, as investors remain bullish on Canadian banking as well as the overall strength of the American economy, which has stimulated so much of TD Bank’s growth over the past year. A rate cut would likely be viewed positively by Canadian investors as stimulating for the economy.

TD Bank is wonderfully valued at the moment and remains one of the most popular banking stocks on the TSX. Buying it ahead of the rush may be advisable, as a rate cut could very well provide a stimulus to the Big Five and make for narrower dividend yields. Speaking of which, TD Bank’s current yield, just shy of 4%, is one of the best out of the Bay Street bankers.

The TSX will rise with a cut, though there’s no sign of it yet

As such, bank stocks would likely rise should the Bank of Canada, in contrast to their American counterparts after the most recent rate cut south of the border. The American economy faces other stressors, such as the trade war with China, after all, while its central bank has been under considerably greater pressure to make changes to interest rates than ours has been.

For a play on Bay Street bankers with a stronger focus on the Canadian economy, **CIBC** is a solid alternative. Indeed, in the event that further weak manufacturing data emanates from the U.S. or, indeed, a full recession is declared, investors may want to swap out some of those TD Bank shares for ones with less exposure to the economy of our nearest neighbours.

However, it could be a moot point. If the greatest economy of the world goes down the chute, so does everyone else’s.

The bottom line

The end of 2019 is shaping up to be a harsh environment for investors, with several developments coming together to form a conjunction of risks. With Brexit occurring at the end of next month, possibly coinciding with a rate cut from the Bank of Canada, and the potential for stalled talks in the U.S.-China trade war — plus the possibility that a recession is announced between now and then — the safest bank stocks are likely to be popular.

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