Canada’s Bank Stocks Are Oversold: Time to Buy?

Description

It wasn’t a great quarter for Canada’s banks. Only a few managed to meet or beat estimates while the good majority missed expectations. Slowing loan growth, tough capital markets, restructuring and a spike in provision for credit losses are the current headwinds facing Canada’s banks.

Since last week, the industry has been on a downward trend. So much so, that several banks have entered oversold territory.

The 14-day relative strength index (RSI) is among the most popular and widely-used momentum indicators. A 14-day RSI below 30 is a technical sign that the stock is oversold and may be due for a short term bounce.

As of writing there are two Big Banks in oversold territory: the **Royal Bank of Canada** (TSX:RY)(NYSE:RY) and **Toronto-Dominion Bank** (TSX:TD)(NYSE:TD).

I’m not urprised to see either of these stocks on the oversold list. For starters, Royal Bank was my pick as the most disappointing bank from the past quarter.

Although its share price has done quite well (up 14.55% year to date), it missed on both the top and bottom lines. Why is this such a big deal?

It marks the second consecutive quarter in which Canada’s largest bank missed estimates — a disappointment considering it hasn’t missed twice in a row for more than five years.

Royal Bank is largely considered one of the best-in-class and as such, commands a premium. If it continues to disappoint while the others deliver, the premium valuation may not be warranted.

RBC’s current 15-day RSI is approximately 26, putting it firmly in oversold territory. It marks only the second time this year that the company’s 14-day RSI has dropped this low.

The narrative is much of the same for Toronto-Dominion Bank. It has historically commanded a premium thanks to its best-in-class growth rates.

Unfortunately, revenue only grew by 2% and earnings per share missed by a large margin. In fact, adjusted earnings per share dropped by 2.45% in the fourth quarter which was among the worst of its peers. As a result, the company only grew adjusted EPS by 3.4% in 2019.

Given this, it's not surprising that TD Bank's share price has dropped by approximately 5% since it released year-end results. The bank has a 14-day RSI of 27.25 and like Royal Bank, is only the second time this year that it's entered oversold territory.

These Canadian leaders both entered oversold territory in early-to-mid August and it proved to be an excellent entry point. In the months that followed, TD Bank's stock shot up by approximately 8%, while Royal Bank's stock jumped by almost 12%.

Foolish takeaway

Timing time their investments isn't recommended, and this is especially true of Canada's Big Banks, as they have proven to be excellent investments regardless of entry points.

However, when a short-term opportunity presents itself, investors should be prepared to act. Such is the case when Canada's Big Five enter oversold territory.

It's a rare occurrence and thus far, has proved to be an excellent entry point for those looking to top up their positions or start new ones.

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Author
mlitalien