Bank Stocks: Is This 1 Stock a Buy?

Description

Scotiabank (TSX:BNS)(NYSE:BNS) is a chartered Schedule 1 bank under *The Bank Act* (Canada). It is a global financial services provider that offers a range of products and services including personal, commercial, corporate and investment banking.

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The company reports a market capitalization of $88.08 billion with a 52-week low of $67.17 and a 52-week high of $76.75.

Intrinsic price

Based on my calculations, using a comparable company analysis (CCA) model, I determined that Scotiabank has an intrinsic value of $66.53 per share.

At the current share price of $72.39 at writing, I believe Scotiabank is slightly overvalued. Investors looking to add a bank stock to their TFSA and RRSP should not buy Scotiabank at current prices. Interested investors should add the stock to their watch list and wait for an opportunity to buy shares at less than intrinsic price.

Scotiabank has an enterprise value of $83.8 billion, which represents the theoretical price a buyer would pay for all of Scotiabank's outstanding shares plus its debt.

Financial highlights

For the fiscal year ended October 31, 2019, the company reports a strong balance sheet with retained earnings of $44.4 billion, up from $41.4 billion in 2018.

This is a good sign for investors, as it suggests the company has more years of cumulative net income than net loss, which is reinvested into the company.

Given shareholders' equity of $63.6 billion, goodwill and intangibles of $17.5 billion, the company reports a tangible net worth (equity minus intangibles and goodwill) of $46.2 billion, which is good.

Total revenues are up materially to $31 billion, from $28.8 billion in 2018 (+7.9%) which is offset by an increase in expenses for pre-tax income of $11.3 billion. Scotiabank ended the year with net income of $8.8 billion, up slightly from $8.7 billion in 2018 (+1%).

From a cash flow perspective, management takes a proactive approach to debt management, as indicated by repayments of debentures amounting to $1.8 billion in 2019, $233 million in 2018 and $1.5 billion in 2017. This is offset by proceeds from the issuance of debentures of $3.25 billion in 2019.

The company has a normal course issuer bid (NCIB) in place whereby Scotiabank has repurchased and cancelled $1.1 billion of shares in 2019, $632 million in 2018 and $1 billion in 2017.

Scotiabank's provision for credit losses increased to $3 billion in 2019, up from $2.6 billion in 2018 (+16%), roughly in line with the increase from 2017 to 2018 (+16%), which suggests that Scotiabank's global diversification is providing a cushion to a potentially tumultuous domestic market.

The company is a dividend paying entity with a current yield of 4.97% achieved with quarterly payments of $0.90 per share.

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Foolish takeaway

Investors looking to buy shares of a bank should avoid Scotiabank for now. Despite the company's positive retained earnings, continued profitability and proactive debt management, the company's is trading at $72.39, which is above its intrinsic value of $66.53.

The premium at which the shares are currently trading is attributed to an EV/Revenue ratio that has consistently been above the median for banks in the past two fiscal years.

Using the comparable company analysis (CCA), Scotiabank's EV/Revenue ratio is at 3.3x for fiscal 2018 and 3.4 times earnings for fiscal 2017 compared to the median values of 2.9 times and 3.1 times, respectively.

Thus, RRSP and TFSA investors should avoid Scotiabank for now until its share price dips below the intrinsic value.

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Date
2025/08/15
Date Created
2020/01/21
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