Are the Canadian Banks Still Investable Amid Macro Headwinds?

Description

The Canadian banks have been dealt a tough hand over the past few years with the Canadian credit downturn amid what appears to be a falling interest rate environment. The global economy is grinding to a halt over the impact of the coronavirus (COVID-19), and with more interest rate cuts potentially in the cards, it's the big banks that could stand to have even more salt rubbed in their wounds, as net interest margins (NIMs) are pressured further.

It's tough to garner any meaningful earnings growth when loans are falling in conjunction with margins. Add provisions for credit losses and potentially sizeable restructuring costs into the equation, and you've got what seems like the perfect formula for meagre year-ahead returns with Canada's big banks.

A clue from Uncle Warren?

Warren Buffett trimmed his bank exposure in the latest quarter, and while that's no indication that you should follow his lead by selling your bank holdings, it is only prudent to weigh the new set of risks you'll bear with the banks as they navigate what's likely to be another turbulent year.

The banks are going to enter the second half of the hurricane in 2020, with a similar theme as last year (thinning NIMs, sluggish loan growth, rising provisions, and expenses). That said, not all banks are built the same. Some, like **Royal Bank of Canada**, which is currently hovering close to all-time highs, are better prepared than its peers and can rise in spite of the challenges.

It's tempting to shun the broader basket of Canadian bank stocks given the mounting macro headwinds and all those muted analyst expectations. However, if you consider yourself a long-term investor, it still makes sense to be an owner of some of the more resilient banks if you can get in at the right price.

Consider **National Bank of Canada** (TSX:NA), Canada's sixth-largest bank, which put its Big Five brothers to shame last year; it posted meaningful growth numbers across the board, as though the bank hadn't gotten the memo that the banks were caught in the middle of a credit downturn.

When it comes to the banks, National Bank was a heavy underdog with its small size and lack of geographical diversification relative to its peers. Many Canadians believe that larger, more geographically-diversified banks are a “safer” bet, often counting National Bank out of the race with references to the nation’s big banks as the Big Five, rather than the Big Six.

As we witnessed last year, bigger isn’t necessarily better, especially if you’re talking about loan books made when credit is easy. National Bank maintained prudence throughout the years, and now that the tides have gone out, investors are noticing that the bank is one of few swimmers that didn’t forget its trunks on the shore.

“National Bank has quietly fallen under the shadows of its peers when credit was easy. Now that the tables have turned, I believe it will be National Bank that will finally have a chance to make up ground over its peers.” I said in a prior piece. “As of mid-February, National Bank is looking like the best bank for your buck.”

Foolish takeaway

Investors are noticing the prudence of National Bank CEO Louis Vachon and company, and they’re not going to forget which bank killed it amid mounting macro headwinds while some of its peers crumbled like paper bags. As such, I see National Bank as one of few banks that one can buy and not lose sleep over as industry challenges prevail through the early 2020s.

So, are the Canadian banks investable through 2020?

They can be if you go for the banks that proved themselves last year, because more of the same should be expected as we inch closer to year end.

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