Are Canadian Bank Stocks a Buy?

Description

The **TSX Index** is up 30% from the March 23 low. Canadian bank stocks have participated in the rally, but pundits have mixed feelings about whether investors are too optimistic.

Recession — or depression?

Seven million Canadians applied for the Canada Emergency Response Benefit (CERB) in recent weeks. According to the OECD report for February 2020, there are roughly 24.5 million Canadians aged 15-64, which is the group considered to be in the working-age range.

Based on the CERB claims number, nearly 30% of Canadians who can work say they are now earning less than $1,000 per month.

Thousands of businesses closed due to lockdowns. As the provinces put plans in place to begin reopening the economy, the government hopes aid measures will result in a quick rebound in rehiring. Wage subsidies, emergency loans, and rent relief are all in the works.

Part of the challenge involves getting businesses back on their feet in a timely manner. Consumers, however, must feel comfortable and actually have cash to spend.

Will we see a "V" recovery or a "U" recovery? This is the major question. Top business leaders and economists have a wide range of opinions. An investor's belief regarding the eventual speed of the recovery has a large impact on whether or not bank stocks should be on the buy list.

Are Canadian bank stocks attractive today?

Optimistic projections suggest a strong economic rebound could begin by the end of 2020. The International Monetary Fund (IMF) expects global growth to rebound significantly in 2021.

The Canadian banks entered the crisis in solid shape. The Big Five all have strong capital positions and should benefit from government programs designed to mitigate the economic damage. CMHC is buying up to $150 billion in mortgage, giving the banks added capital to continue lending.

The banks maintained their distributions during the Great Recession. In the event we see a strong economic recovery in 2021, the dividend payouts should be safe. At the time of writing, dividend yields from the largest Canadian banks range from 5% at **Royal Bank of Canada** to 7% at **CIBC**.

Risks

The magnitude of the economic crisis is as yet unknown. One economist, David Rosenberg, recently told *BNN* that he sees the impact being 10 times that of 2008-2009. If high unemployment continues for the next few years, the banks are going to feel some pain.

Short-term deferrals on loan and mortgage payments simply buy time. People need to return to work and businesses must survive to avoid an extended downturn. The banks have the means to ride out the storm, but they could face larger defaults than currently expected if the crisis drags into the second half of next year.

The bottom line

I wouldn't back up the truck today given the near-term uncertainty, as we could still retest the March low. However, investors with a buy-and-hold strategy might want to start nibbling on their favourite Canadian bank stocks at these levels.

The Canadian banks should prove to be long-term winning bets. In the meantime, you get paid well to ride out the turbulence while waiting for the government stimulus measures to drive new economic expansion.

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