



## Should You Buy Canadian Bank Stocks for Dividends?

### Description

I've never had much doubt about the safety of Canadian bank dividends. In fact, I still hold them in high regard and own a few of them outright. Unfortunately, an event occurred last week which stoked my fears about them in a way that I have never felt before.

As fellow Fool contributor Joey Frenette recently reported, **Laurentian Bank** [cut its dividend by 40%](#), the first bank to do so in decades. An event such as this puts into question the sacrosanct dividends of all the banks. Are they as safe as we think?

### A similar situation

Adding further doubt to my mind is the station I recently faced with my pipeline stocks. I owned many pipelines in the past. One of these pipelines, **Inter Pipeline Ltd**, was a former dividend growth stock. In the depths of the oil collapse, Inter Pipeline cut its dividend. Later, other major dividend companies worldwide began doing the same.

Of course, not all pipelines are equal. Many retain their dividends and have the cash flows to continue to grow them. While Inter Pipeline did shake my confidence, further research comforted me by reinforcing my belief that their dividends remained safer. Inter Pipeline had a weaker balance sheet going into the crisis, so it was more vulnerable.

### The banks and their dividends

It's quite likely that the crisis we are about to face may indeed be very severe. There is no way to know how hard economic stress will hit the banks. At the moment we are simply speculating. Laurentian's decision to cut simply makes all dividends seem less secure.

The truth is, though, that Laurentian suffered from a similar situation to Inter Pipeline going into the crisis. It is a Canada-focused lender with a much less diversified business than the larger Canadian banks. It was more vulnerable prior to the crisis.

If you are looking for a bank that is more likely to weather the crisis with its payout intact, you might want to look at **Toronto-Dominion Bank** ([TSX:TD](#))([NYSE:TD](#)). It is a much larger bank with high-quality assets. It also has a diverse business model with trading, investing, underwriting, and lending to drive earnings.

It seems pretty dire at the moment, with profits effectively cut in half. Reported earnings dropped by 52% to \$0.80 in Q2 2020 from \$1.70 in Q2 2019. The earnings collapse foreshadows the potential damage that the pandemic induced shutdown may have on these banks. The drop is due to provisions for loan losses which the bank estimates will hit later this year.

## The bright side

The lower [stock price for TD Bank](#) indicates the skepticism of the market at the moment. There is the possibility, though, that the virus impact won't be as severe as everyone suspects. Defaults may not rise to the levels people are predicting, and the economy might move along just fine. If that happens, earnings will rise, and the stock price will follow.

As far as the dividend is concerned, it's unlikely that TD will follow in the footsteps of Laurentian. It is a much stronger company with a far more diversified asset base and business strategy. The dividend still sits at a historically high 5.19% yield at the moment, which represents a good entry point for new investors or people looking to add to their positions.

As far as dividend increases, it's hard to say at the moment. Let's face it, the outlook for the economy is grim. Things might be bad for a while, so it may be prudent for TD to pause increases. Fortunately, the bank already increased the dividend by 7% this year, giving it a year of leeway to decide.

## The bottom line

This time is certainly worse than we have experienced in the recent past. Up until now, dividends were quite safe. The global pandemic has hammered the global economy, hitting weaker companies, forcing them to cut their dividends. The dividend cuts in turn have created uncertainty that was not there before.

Owning a strong bank like TD will pay off in the long run. If you choose to own one, you should stick to the highest quality name in the group.

### CATEGORY

1. Bank Stocks
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