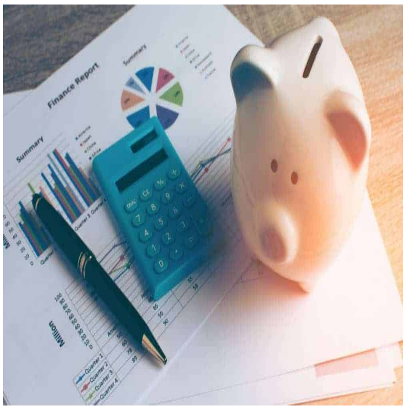

COVID-19 Reveals the Best Canadian Bank Stock to Buy in 2020

Description

Last week, **Laurentian Bank** slashed its dividend by 40%. In yesterday's article, I discussed whether I believe the Big Three TSX bank stocks will cut their dividends or not.

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In this article, I'll cover the rest of the Big Six Canadian bank stocks: **Bank of Montreal** (TSX:BMO)(NYSE:BMO), **CIBC** (TSX:CM)(NYSE:CM), and **National Bank of Canada** (TSX:NA).

Warren Buffett's famous quote fits well here: "Only when the tide goes out do you discover who's been swimming naked."

Dividend history and payout ratio

BMO stock has increased its dividend for eight consecutive years with a five-year dividend**–**growth rate of 5.7%. Its payout ratio (based on the current quarterly dividend and last year's earnings) would be about 45%. In a normal market, that's approximately where its payout ratio would be.

Nine consecutive years — that's CIBC stock's dividend-growth streak. Its five-year dividend-growth rate is better at 7.2%. Its payout ratio based on last year's earnings would be roughly 49%.

National Bank stock's dividend-growth streak is 10 consecutive years. The bank stock's five-year dividend-growth rate is 7.2%. Based on last year's earnings, the bank stock's payout ratio would be roughly 45%.

During the last financial crisis, the banks were able to maintain their dividends, which illustrated the strength of their businesses. As they recovered, they began increasing their dividends again.

Initial COVID-19 impacts on these big TSX banks

COVID-19 is disrupting the economy. The banks' fiscal Q2 results provide a window to the initial impacts of the virus.

BMO stock reported adjusted earnings per share of $1.04, down 55% from the prior year's quarter. As a result, the payout ratio for the quarter was about 102%. The bank's adjusted return on equity dropped from last year's 13.9% to 5.5%.

It increased its provisions for credit losses (PCLs) to $1.1 billion, up from $176 million. The PCL ratio on total loans was 0.94% compared to a low level of 0.16% in the prior year, as the bank set aside more money to cover the increase of bad loans from COVID-19 impacts.

The actual PCL ratio on impaired loans was 0.35% compared to a low level of 0.14% in the previous year. This is still a low percentage that's comparable to **RBC** stock's 0.37%. That said, the ratio is still worth keeping watch on, especially over this highly uncertain pandemic period.

CIBC stock was hit harder than the other Big Six banks. It reported adjusted earnings per share of $0.94, down 68% from the prior year's quarter. This resulted in a payout ratio of about 155% for the quarter. Its adjusted return on equity fell from last year's 15.9% to 4.5%.

Interestingly, of the Big Six Canadian banks, National Bank was the most resilient. The bank stock's diluted earnings per share was $1.01 for the quarter, down only 33% from the prior year's quarter. So, its payout ratio was 70% for the quarter. Its return on equity fell from last year's 17.8% to 10.7%.

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The Foolish takeaway

The big Canadian banks have rallied superbly from their lows due to COVID-19 fears. Specifically, BMO, CIBC, and National Bank stocks appreciated about 24%, 32%, and 55%, respectively.

Of the Big Six Canadian banks, National Bank's dividend appears to be the safest, while CIBC's seems to be the most risky.

We are probably not out of the woods yet with COVID-19. Gatherings and reopening of businesses can lead to subsequent waves. If we get a meaningful drop in the bank stocks, National Bank should be at the top of your list for consideration.

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